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

In the Matter of	)	
	)	
Application Pursuant to Section 214 of	)	
the Communications Act of 1934 and	)	**WC Docket No. 06-74**
Section 63.04 of the Commission's Rules	)	
for Consent to the Transfer of Control of	)	
BellSouth Corporation to AT&T, Inc.	)	

REPLY COMMENTS OF SCANSOURCE, INC.

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SUMMARY

As a major BellSouth enterprise customer and a former AT&T enterprise customer, ScanSource opposes the merger of AT&T and BellSouth because it will eliminate actual and potential competition in the enterprise telecommunications marketplace.

The result will be that enterprise customers will have fewer choices, pay higher prices, and have less robust options to ensure that their business is adequately protected in the event of a disaster or other network outage. Productivity and innovation will suffer. The adverse impact of the merger on enterprise customers ultimately will flow downstream to retail consumers in the form of higher prices for a wide variety of products and services. Indeed, the negative effects of the merger will impact not only purchasers of telecommunications services, but will be felt throughout the broader American economy. The significant harms to the enterprise market and the economy at large are not outweighed by affording residential consumers a third or fourth choice of video services providers.

For these reasons, ScanSource respectfully submits that the Commission must reject the proposed merger of AT&T and BellSouth.

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ScanSource, Inc. ("ScanSource"), through undersigned counsel, hereby replies to the comments filed with the Federal Communications Commission ("FCC" or "Commission") on June 5, 2006 in the above-captioned docket concerning the application for consent to transfer of control filed by AT&T, Inc. ("AT&T") and BellSouth Corporation ("BellSouth").[1] As a large enterprise customer with significant, sophisticated telecommunications needs, ScanSource strongly opposes the proposed merger of AT&T and BellSouth, which will drive up prices for mission critical telecommunications services by further diminishing choices in the enterprise customer space, and by eliminating potential and promised competition between AT&T and BellSouth. While ScanSource generally supports the initial comments filed in this proceeding by Cbeyond Communications *et al.*,[2] ScanSource lends a unique perspective to this proceeding as a major BellSouth enterprise customer and a former AT&T enterprise customer. As provided for

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1 *Commission Seeks Comment on Application for Consent to Transfer of Control Filed by AT&T, Inc. and BellSouth Corporation*, Public Notice, WC Docket No. 06-74, DA 06-904 (rel. April 19, 2006).

2 Comments of Cbeyond Communications, Grande Communications, New Edge Networks, NuVox Communications, Supra Telecom, Talk American, Inc., XO Communications, Inc. and Xspedius Communications ("Comments of Cbeyond *et al.*").

in detail below, ScanSource maintains that the Commission must deny the proposed merger of AT&T and BellSouth.

I. INTRODUCTION

The merger of AT&T, the nation's largest incumbent local exchange carrier ("ILEC"), and BellSouth, the nation's third largest ILEC, will undoubtedly harm American enterprise customers by inhibiting competition for a wide variety of enterprise telecommunications services, including local exchange, long distance, toll-free, Internet and data services, resulting in higher prices both for enterprise customers and retail consumers in the downstream sales channels.

For nearly a decade, the Regional Bell Operating Companies ("RBOCs") have claimed that they need economies of scope and scale in order to better fend off competitive challenges.[3] In support of its application to merge with Ameritech, SBC claimed in 1998, for example, that it faced "unprecedented new challenges in the profitable core of their operations, ***in-region service to business customers***[,]" from [CLECs] and foreign carriers.[4] Rather than "try to hang on in the face of the inroads of new competitors,"[5] SBC and Ameritech concluded that a merger would provide them with the necessary "financial resources, customer base, managerial and employee talent, economies of scale and scope and business commitment to most effectively offer integrated telecommunications services . . . to consumers nationwide and

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3 *Applications of NYNEX Corp. and Bell Atlantic Corp. for Consent to Transfer Control of NYNEX Corp. and Its Subsidiaries*, Memorandum Opinion and Order, 12 FCC Rcd 19,985 (1997) ("*Bell Atlantic-NYNEX Merger Order*").

4 *Application of Ameritech Corporation and SBC Communications Inc. for Authority, Pursuant to Part 24 of the Commission's Rules, to Transfer Control of Licenses Controlled by Ameritech Corporation*, WT Docket No. 98-141, filed July 24, 1998, at Att. 2, p. 49 (emphasis added).

5 *Id.* at 50.

beyond, for the benefit of both their customers and shareholders."[6] The unfortunate reality, however, is that enterprise customers and consumers have little more than a series broken promises from SBC to use its size and scale to provide meaningful out-of-region service. Experience indicates that SBC has not dedicated itself in any significant way to competing out-of-region. Moreover, it appears that SBC chalked-up its merger condition violations and associated monetary penalties as an easily absorbed cost of doing business. Today, SBC, now AT&T, comes before the Commission and consumers making the same disingenuous claims -- that the merger is necessary to better compete by providing a vast array of services to consumers. ScanSource's response to the parties' merger application can be summed up simply by invoking a familiar maxim: fool me once, shame on you; fool me twice, shame on me. In order to preserve and facilitate competition in the enterprise market, the Commission must reject the merger of AT&T and BellSouth.

II. ARGUMENT

The proposed merger of AT&T and BellSouth must be rejected. As demonstrated below, the merger will harm enterprise customers and the American economy be eliminating actual and potential competition in the enterprise telecommunications market.

A. THE PROPOSED MERGER IS HARMFUL TO ENTERPRISE CUSTOMERS AND WILL NEGATIVELY IMPACT THE ECONOMY

ScanSource is a leading value-added distributor of specialty technologies, including automatic data collection, electronic security and point-of-sale products. Headquartered in Greenville, South Carolina, ScanSource has distribution centers in Miami and Memphis, and numerous other U.S. locations, including Atlanta and Phoenix. ScanSource also has offices in Canada, Mexico, France, Belgium and the United Kingdom. As a Fortune 1000

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6 *Id.* at 52.

and NASDAQ-listed company with multiple domestic and international offices, ScanSource has significant and sophisticated telecommunications needs.

Currently, ScanSource is a major enterprise user of BellSouth's local services. ScanSource utilizes BellSouth for all of its local telecommunications needs in Greenville, Memphis, Miami and Atlanta, including T1 circuits, standard 1FB business lines, as well as DSL and ISDN services. When making decisions concerning its telecommunications needs, ScanSource looks not only at a carrier's rates, but also weighs a variety of other factors. ScanSource places a premium on "up-time," and is served in Greenville and Memphis, via "two self-healing" SONET rings, which provide redundant capability and afford ScanSource protection from fiber cuts and equipment failures. Additionally, ScanSource has contracted with Charter Communications to provide service to ScanSource's Greenville headquarters in the event of an outage or disaster.

ScanSource also puts great emphasis on a carrier's customer service account team. For instance, ScanSource chose Verizon Business (*fka* MCI) as its domestic data provider, in spite of the fact that its rates were not the lowest, because it better understood ScanSource's business needs and offered superior account accessibility and accountability. ScanSource also uses Verizon Business for it long distance services, including in-bound 800 service, for the same reasons. ScanSource purchases its Internet-based services from several carriers, including BellSouth, Level 3, Verizon Business, and Charter Communications; each vendor provides a different type of service to ScanSource. Finally, ScanSource's European operations utilize Sprint's IP/VPN services.

By spreading its telecommunications needs among several different carriers, each competing for ScanSource's other business, ScanSource is able to effectively meet its business requirements without sacrificing reliability, customer service, or the bottom line. ScanSource contends that the ability to choose one provider over at least two others is critical to enterprise customers and the consumers that ultimately purchase the enterprises' goods or services. This is precisely why the Commission must reject the merger of AT&T and BellSouth. As provided for in further detail below, the merger will result in one less competitive choice for a variety of enterprise telecommunications services and will eliminate the possibility that AT&T and BellSouth will each compete out-of-region against the other for enterprise customers' local exchange service business and other communications services needs.

1. The Merger Will Eliminate Actual Competition

As Cbeyond *et al.* point out in their initial comments, AT&T and BellSouth claim in their application that they rarely compete against each other for the same types of business customers.[7] The applicants contend that AT&T focuses on serving the largest business customers both nationally and globally, while BellSouth concentrates only on significantly smaller local and regional customers.[8] However, as Time Warner Telecom[9] and Access Point *et al.*[10] note, the applicants' claim is disingenuous, as AT&T and BellSouth actually compete for the *same* customers. ScanSource's experience with both AT&T and BellSouth supports the CLECs' position. Indeed, before ScanSource chose Verizon Business to provide its domestic long distance and toll-free services, ScanSource purchased many of those services from AT&T.

7 Comments of Cbeyond *et al.* at 51-52.

8 *AT&T/BellSouth Merger Application* at 64-67.

9 Petition to Deny of Time Warner Telecom at 16.

10 Comments of Access Point, Inc., CAN Communications Services, Inc., Deltacom, Inc., Florida Digital Network, Inc. d/b/a FDN Communications, Globalcom Communications, Inc., Lightyear Network Solutions, Inc., McLeodUSA Telecommunications Services, Inc., Pac-West Telecomm, Inc., SmartCity Networks, Inc., US LEC Corp. at 10-11 ("Comments of Access Point *et al.*").

BellSouth, too, had competed against AT&T to provide certain services to ScanSource and at one point had succeeded in winning ScanSource's toll-free business from AT&T.[11]

Moreover, BellSouth's Securities and Exchange Commission ("SEC") filings undercut the applicants' unfounded claims. In its 2004 10-K, BellSouth claimed that it entered into an arrangement with Qwest Communications allowing it to offer "complex services...to enterprise business customers not just in our nine state region, but throughout the United States."[12] In its 2005 10-K, BellSouth reported that it entered into an arrangement with Sprint Nextel Corporation to enhance its abilities "to meet the needs of sophisticated purchasers of long distance services."[13] Thus, it is clear that BellSouth currently competes both in-region and out-of-region for sophisticated enterprise customers such as ScanSource.

The elimination of BellSouth as a major competitor in the enterprise marketplace will have several serious anticompetitive consequences. First, there will be fewer competitors able to offer sophisticated enterprise services necessary to meet the needs of customers like ScanSource, thereby removing pricing pressure on AT&T and allowing it to raise prices. In fact, AT&T has recently reported that prices have already begun to "stabilize."[14] Because large enterprise customers typically have significant telecommunications usage, they are particularly sensitive to rate increases. This is true despite the use volume and terms contracts, which only provide certainty and mitigate any rate increases for as long as the term of the contract. Upon the expiration of such contracts, however, enterprise customers are often faced with the

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11 *See* Declaration of K. Todd Graham, attached hereto as ***Exhibit A***.

12 2004 BellSouth 10-K at 5.

13 2005 BellSouth 10-K at 11 of 158.

14 *See Morningstar Report*, Michael Hodel, Senior Analyst, dated April 25, 2006 (with respect to large business and wholesale revenues, noting that AT&T "again reported that prices are stabilizing"); *See also, e.g., Wireline Telecom Playbook*: *What's In Store for 2006?*, UBS Investment Research, January 3, 2006 (AT&T and Verizon rates expected to increase in 2006).

Hobson's choice of renewing the contract and acquiescing to rate increases, or putting the services out for bid and potentially severing its relationship with its existing provider, in which case the company may incur significant costs associated with migrating its telecommunications services.[15] Indeed, most of ScanSource's telecommunications contracts expire in 2008. If the Commission allows the merger to proceed as planned, ScanSource no doubt will be faced with the reality of higher prices across the board upon the expiration of its agreements. Rather than absorb such price increases, enterprise customers will likely pass such costs on to their customers. The ripple effect will be felt throughout the supply chain and will ultimately impact retail consumers.

Second, the merger of AT&T and BellSouth will inhibit large enterprise customers' ability to conduct business in the event of an outage or an emergency. As explained above, network "up-time" is critical to businesses like ScanSource. Large enterprise users require several ***independent, unaffilliated*** carriers from which to choose precisely for the reason that in many cases they need to choose ***two*** providers for each of the telecommunications services they intend to purchase -- one to provide service on a day-to-day basis, and another to act as a back-up. However, the continuing industry consolidation that has radically reshaped the telecommunications industry has stripped large enterprise customers of choices. Viable service provider options are few and will be even fewer, if the proposed merger is allowed to proceed. And, contrary to what AT&T and BellSouth imply in their application, competitive local exchange carriers ("CLECs") do not account for enough activity to off-set removing AT&T from

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15 Such costs may include charges associated with setting up the customers account, installing new equipment at the customer's locations to support the new providers' services, *e.g*., channel banks, integrated access devices, and other CPE.

the business marketplace in the BellSouth region.[16] Further, ScanSource agrees with Cbeyond *et al.* that intermodal providers such as wireless, cable and VoIP providers, do not and will not soon qualify as significant players ***independent*** of BellSouth, their principal supplier of network capabilities.[17] Eliminating an independent BellSouth or AT&T from the enterprise space will create the possibility that enterprises may not be able to serve their customers at the level which either of them expects.

Third, ScanSource is concerned that the merger will result in the establishment of AT&T's customer service policies and practices by the combined company, rather than those of BellSouth. While ScanSource is generally satisfied with quality of service provide by BellSouth's customer account teams, ScanSource's experience with AT&T is that it is a massive and generally unresponsive bureaucracy not far removed from its days as the nation's sole-supplier of telecommunications services. AT&T's account teams are generally unable to get things done without senior management level approvals and are frequently unresponsive to customers problems and requests. While such conduct may seem astounding given ScanSource's then-significant telecommunications spend with AT&T, it is indicative of the fact that there are few real choices for sophisticated enterprise customers like ScanSource -- and AT&T knows it. This merger will only exacerbate such problems.

2. <u>The Merger Will Eliminate Potential Competition</u>

The AT&T-BellSouth merger will also eliminate potential competition for enterprise customers in BellSouth's region. By its own claims, AT&T is the largest nationwide competitor for enterprise customers. And, as demonstrated above, BellSouth has taken steps to

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16 *See* Comments of Cbeyond *et al.* at 51 ("Contrary to what is implied in the Merger Application, competitive LECs do not account for enough competitive activity to counterbalance the proposed removal of AT&T from the business services marketplace in the BellSouth region.").

17 *Id.*

prevent the loss of enterprise customers within its region. Indeed, consistent with BellSouth's statements in its 2004 and 2005 10-K filings with the SEC, BellSouth offered to follow ScanSource out-of-region in an effort to better serve ScanSource's business needs. In a January, 2006 meeting between BellSouth and ScanSource, BellSouth representatives requested to bid on ScanSource's out-of-region business, including local dial tone, ISDN, Internet, and long distance services.[18] AT&T had the potential to compete for all of the services that BellSouth offered to provide to ScanSource, especially in Atlanta and Miami, where AT&T has deployed metro fiber rings and extensive switching facilities.[19] Indeed, as geographically adjacent carriers, AT&T and BellSouth are the most likely potential competitors to one another.[20] In fact, both companies expressed to ScanSource its interest in bidding for the services the other was providing.[21] Less than two months later, however, AT&T and BellSouth announced their plans to merge and absent denial of their application, the two companies will never attempt to compete with each other again.

Besides competing for ScanSource's existing telecommunications business, AT&T and BellSouth also could have independently competed for new products and services that ScanSource plans to purchase in order to enhance its current communications platform. For example, ScanSource is interested in purchasing metro Ethernet services, audio and video conferencing, comprehensive network monitoring capabilities, including network security

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18 *See* Declaration of K. Todd Graham at 2-3, *supra* n.11, attached hereto as ***Exhibit A***.

19 *See In the Matter of Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, BellSouth Reply Comments, filed July 29, 2005, Attachment 2, Exhibit A, "Lit Buildings in BellSouth's Territory," slide entitled "Competitive Intensity in Top 20 MSAs."

20 *Applications of Ameritech Corp. and SBC Communications, Inc., For Consent to Transfer Control of Corporations Holding Commission Licenses and Lines Pursuant to Section 214 and 310(d) of the Communications Act and Parts 5, 22, 24, 25, 63, 90, 95, and 101 of the Commission's Rules*, Memorandum Opinion and Order, 14 FCC Rcd 14,712, ¶85 (1999) ("*SBC-Ameritech Merger Order*").

21 *See* Declaration of K. Todd Graham at 2-3.

testing, and business continuity and disaster recovery planning, among other products and services. Other than AT&T and BellSouth, few carriers offer such a vast and comprehensive array of products and services to large enterprise customers. If the Commission approves the AT&T-BellSouth merger and effectively eliminates BellSouth as an independent entity, ScanSource and other similarly situated enterprise customers may need to reevaluate their communications services plans and forego needed new products and services as a result of likely price increases for such services from an even smaller group of potential providers. The net effect will be that such firms will experience a decrease in productivity that will resonate down the supply chain and throughout the economy.

AT&T's pattern of acquiring its actual and potential competitors rather than competing against them should by now be anything but surprising. In the *SBC-Ameritech Merger Order*, the Commission concluded *inter alia* that "the proposed merger of these RBOCs threatens to harm consumers of telecommunications services by . . . denying them the benefits of future probable competition between the merging firms."[22] In order to mitigate the loss of potential competition between SBC and Ameritech, the Commission required the merged firm to open its markets to others, while at the same time entering markets outside of its region. The conditions required the merged SBC/Ameritech to enter 30 out-of-region markets as a CLEC within 30 months of the merger's closing.[23] It is clear now that SBC never intended to abide by the spirit of those commitments, however. Instead, it seems that SBC simply accounted for the merger condition penalties as a cost of doing business, based on the assumption that the Commission would not dare to attempt unwind the merger as a result of SBC's violation of those conditions. Now, the company that swallowed Pacific Bell, SNET, Ameritech, and AT&T wants

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22 *SBC-Ameritech Merger Order,* 14 FCC Rcd 14,712, ¶3.

23 *Id.* ¶421.

this Commission and consumers to believe that its proposed merger with BellSouth merger is somehow different and is truly necessary in order to stem the intrusion of cable and VoIP providers into AT&T's core telephone business and to better compete against cable companies for the provision of video services. If history teaches us anything about AT&T, it is that the justifications and commitments AT&T puts forth in support of its merger application are simply not credible. Accordingly, the Commission must preserve potential competition in the enterprise market by rejecting the merger.

B. THE HARMS OUTWEIGH ANY BENEFITS OF THE PROPOSED COMBINATION

As demonstrated herein, the merger of AT&T and BellSouth will almost certainly drive up prices for enterprise telecommunications products and services, and both enterprise customers and downstream retail customers and clients will bear the brunt of those price increases. As a result, productivity and, in turn, innovation will suffer. Thus, the negative effects of the merger will impact not only purchasers of telecommunications services, but also will be felt throughout the broader American economy. While it may be true that AT&T and BellSouth face a competitive threat from cable providers, in particular, in the mass market, those threats are almost non-existent in the enterprise market. More to the point, however, the significant harms to the enterprise market and the economy at large are clearly not outweighed by affording residential consumers a third or fourth choice of video services providers, and AT&T and BellSouth do not offer any other rational justification for the merger.

C. CONDITIONS SHOULD BE IMPOSED, IF THE COMMISSION IS DISINCLINED TO DENY THE MERGER APPLICATIONS

ScanSource notes that many commenters opposing the proposed merger have proposed conditions that they contend should apply in the event the Commission is disinclined to deny the merger applications.[24] ScanSource contends that no condition short of mandated price controls and significant price regulation could even begin to serve as a sufficient substitute for the actual and potential competition that will surely be eradicated as a result of this merger. As such, ScanSource agrees with the overwhelming majority of initial comments, including those of Cbeyond *et al.*, and others, that call for the Commission to reject the merger. However, if the Commission is nevertheless disinclined to deny the merger applications, ScanSource requests that the Commission impose, at a minimum, the following conditions:[25]

Special Access Rate Cap – For a period of thirty (30) months after the Merger Closing Date, the merged AT&T/BellSouth entity shall not increase the rates in their tariffs, including contract tariffs for special access and private line services that the merged AT&T/BellSouth entity provides in its 22-state operating territory and that are set forth in such tariffs of March 31, 2006.[26]

Fresh Look – The merged AT&T/BellSouth entity shall permit customers with term or negotiated service arrangements to terminate their agreements and pay no termination liability for a period of twelve (12) months from the Merger Closing Date. The merged AT&T/BellSouth entity also shall provide terminating customers with a six (6) month post-termination transition period to migrate off the AT&T/BellSouth networks during which they will pay no shortfall charges and will continue to pay the discounted rates established by their contracts.[27]

While these proposed conditions cannot rectify fully the harms likely to result from the proposed merger, the adoption of them (and others) could partially ameliorate those harms.

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24 *E.g.,* Comments of Cbeyond *et al.* at 96-110.

25 ScanSource submits that the case and basis for such conditions is adequately set forth in the comments of CLECs opposing the merger. *See, e.g., id.,* at 96-98.

26 A nearly identical remedy was adopted by the Commission as part of the SBC/AT&T merger to provide a period of stability for competitive providers to build market share. *AT&T/SBC Merger Order*, Statement of Commissioner Michael J. Copps, Concurring. This condition and the rationale for it apply equally to this proposed merger. *See also,* Comments of Cbeyond *et al.* at 106-07.

27 Providing competitors with rapid access to small business and enterprise customers is critical to creating vibrant competition needed to ameliorate the harms that would arise should this proposed merger be consummated. It is therefore important to adopt a Fresh Look remedy, permitting small business and enterprise customers to choose a competitive provider without incurring any penalty for doing so. *Id.*

III. CONCLUSION

Consistent with the foregoing, the Commission must deny the merger of AT&T and BellSouth in order to prevent significant harm to the enterprise telecommunications market and the American economy.

Respectfully submitted,

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