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THE AT&T AND BELLSOUTH MERGER: WHAT DOES IT MEAN FOR CONSUMERS?

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THE AT&T AND BELLSOUTH MERGER: WHAT DOES IT MEAN FOR CONSUMERS?

THURSDAY, JUNE 22, 2006

U.S. SENATE,
SUBCOMMITTEE ON ANTITRUST, COMPETITION POLICY AND CONSUMER RIGHTS, COMMITTEE ON THE JUDICIARY,
Washington, D.C.

The Subcommittee met, pursuant to notice, at 3:05 p.m., in room SD–226, Dirksen Senate Office Building, Hon. Mike DeWine, Chairman of the Subcommittee, presiding.

Present: Senators DeWine, Specter, Kohl, and Leahy.

OPENING STATEMENT OF HON. MIKE DEWINE, A U.S. SENATOR FROM THE STATE OF OHIO

Chairman DEWINE. Good afternoon. We welcome all of you today. Welcome to our panelists to today's hearing to examine the merger between AT&T and BellSouth. This merger is another in a series we have seen recently in the telecommunications market, and it certainly is significant. This deal will create the largest telecom company in the U.S. In fact, with a market capitalization over $150 billion, the combined AT&T–BellSouth would be one of the largest companies in the world. This merger will also bring under one roof the largest cell phone provider in the country.

As we evaluate this deal, we must keep in mind how much the market has changed. In 1984, when the Bell monopoly was broken up, most of us only had landline phones attached to the wall. Cell phones and the Internet were virtually unknown. Today, that type of old-fashioned phone service is just one part of a larger patchwork of data and communications services. In recent years, the cable television companies have started to offer high-speed Internet and telephone services, while the telephone companies are beginning to roll out video services. It is clear that soon data of all types, whether it be Internet traffic, phone calls, or television shows, will be delivered via the Internet by a wide range of different companies.

So what does this merger mean for consumers?

In terms of traditional home-phone consumer service, probably not all that much. AT&T and BellSouth both provide that type of service in their own areas, but do not compete in each other's regions, so nothing in this market will change as a result of the deal.

However, the merger may have an impact on consumers in other ways. A combined AT&T–BellSouth will have a unique portfolio of assets, which raises questions of how it will use those assets. For example, once Cingular comes under the ownership of a single com-

pany, the way in it is run may change. Some have expressed concerns that a Cingular under the ownership of a combined AT&T–BellSouth will have the ability and incentive to manipulate connection fees in a way that will unfairly harm competition. This is an issue that we will explore today.

At the same time, the wireless market is beginning to show promise as a medium that can provide new competition in a range of consumer services. The development of the so-called WiMax service means that cellular companies will be able to provide an alternative to traditional phone and cable companies for video and Internet offerings. However, there is some concern that this merger will consolidate so much wireless spectrum in the hands of AT&T that it may hinder the development of WiMax and diminish its potential as a competitive alternative.

This merger will also have competitive implications for the future of the Internet. AT&T will become an even bigger presence in the so-called Internet backbone market. As telecommunications companies get larger, they are looking for different ways to manage their parts of the network, to get it to function more efficiently. Their potential efforts to do so are part of the escalating tensions surround the debate about net neutrality, which the full Judiciary Committee began to examine in a hearing just last week. I think we need to examine and really understand whether this merger will create incentives to lessen competition—in markets for content as well as the carriage of that content—over networks controlled by bigger, more powerful companies, such as the newly merged AT&T.

The deal will impact business customers as well. Businesses, for example, find that very few companies can currently offer services to fit their complex telecommunications needs, and, in fact, there are some businesses right now that can only be served by either AT&T or BellSouth. For them, this merger means that they will go from a market with two options to a monopoly. This is a market sector that will require close scrutiny.

Today, we will hear from the CEOs of AT&T and BellSouth, as well as the CEO of Cbeyond, a smaller Internet-based telecom company, and an independent analyst. I hope these witnesses can give us an accurate and useful picture of what the competitive landscape will look like after this proposed merger and what it will look like in the next few years, specifically with regard to this section of the business market.

We are also, of course, interested in hearing about the potential competitive benefits of this deal. For example, expanding the customer base of AT&T may well allow it to roll out its video service more quickly, and the greater size and scope of the company may enhance other competitive offerings as well. We look forward to examining these benefits with our witnesses today.

Finally, of course, we need to continue to investigate some of the broader telecommunications issues currently being assessed by industry and policymakers, some of which the full Judiciary Committee examined last week, and many of which are being addressed now in draft bills to rewrite our telecommunications laws. Issues such as net neutrality, which I referred to previously, and regulations regarding common carrier and information services may also be affected by this deal, and so we need to consider the possible

ramifications of the AT&T–BellSouth merger in these areas as well.

So we have a range of important and very interesting topics to cover today. I look forward to hearing from our witnesses on all of them as well.

Let me turn now to Senator Kohl for his opening comments.

STATEMENT OF HON. HERBERT KOHL, A U.S. SENATOR FROM THE STATE OF WISCONSIN

Senator KOHL. I thank you, Mr. Chairman. Today, we return to a topic our Antitrust Subcommittee examined a year ago—continuing consolidation of the telecom industry. The $67 billion merger between AT&T and BellSouth we consider today follows closely on the heels of last year's massive AT&T–SBC and Verizon-MCI mergers. These mergers and the rapid pace of the technological changes in this industry are fundamentally reshaping how Americans communicate in what we pay for these services.

While examining the impact of these deals on competition, we must also carefully consider what this consolidation means for our fundamental civil liberties and our National security. The antitrust laws were written out of a concern with the political effects of undue concentrations of economic power, not only their effects on consumers' pocketbooks. And the disturbing revelations in the last few months of the administration's domestic surveillance demonstrate vividly that this deal—and the overall telecom consolidation wave of which it is but a part—may indeed have a profound effect on our civil liberties. It has been reported in the press that the NSA, allegedly with the cooperation of some of the Nation's largest phone companies, including AT&T, is compiling a massive data base of whom nearly every American calls on the telephone. While, of course, we all recognize that we need to listen to any calls that al Qaeda may try to make into the United States, we must do so in a focused manner without trampling on the privacy rights of millions of innocent Americans.

We must realize that the mergers and acquisitions in the telecom industry make overbroad domestic surveillance considerably easier. As the market consolidates, Government eavesdropping is possible merely with the assent of fewer and fewer large phone companies than before. Today, just a very few telecom giants have an enormous amount of personal information on virtually every American's phone calls. As the market concentrates, the threat to our privacy grows. These considerations should be paramount to all of us who have the responsibility to review these mergers.

We also, of course, must carefully examine the more traditional antitrust laws raised by the AT&T–BellSouth deal. Both companies defend this merger by pointing out that this is a merger of regional phone companies with adjacent territories rather than of direct competitors. Further, they argue, technological changes and innovation are bringing new forms of competition to the market.

But as we watch as a formerly regional player grows into the dominant phone company in nearly half the Nation, we must be careful to examine several key questions. Will competitors be able to interconnect into the millions of consumers served by the AT&T network? Will the new AT&T have the ability to charge exorbitant

rates for special access lines into its network? Will the combined company gain too high a share of wireless spectrum needed for new competitive alternatives? More fundamentally, how can we ensure this consolidation will not decrease the choices and increase the cost to consumers and to business customer, both large and small?

Just as with the AT&T–SBC and the Verizon-MCI mergers, we expect that the Justice Department and the FCC will scrutinize these mergers very carefully to preserve competition. A good place to start would be the imposition of some of the same conditions these agencies imposed on last year's deals on this one. We must be especially careful to ensure that the combined company's broadband Internet services do not interfere with consumers' ability to access all Internet content they wish. Securing merger conditions such as these will help ensure that the tremendous gains in telecom competition over the past 20 years are not lost in the midst of this industry consolidation.

Thank you, Mr. Chairman.

Chairman DEWINE. Senator Specter?

STATEMENT OF HON. ARLEN SPECTER, A U.S. SENATOR FROM THE STATE OF PENNSYLVANIA

Senator SPECTER. Thank you, Mr. Chairman.

At the outset, I congratulate you, Chairman DeWine and Ranking Member Kohl, for your excellent work in this very, very important Subcommittee. Thank you for convening this hearing. There are very important antitrust issues raised here. The current AT&T is primarily composed of the former SBC Communications, a company that was formed through the combination of three Bells: Southwestern Bell, Pacific Telesys, and Ameritech. And now with the acquisition, if approved, of BellSouth, it puts the company one step closer to reconstituting the old Ma Bell monopoly.

I recall being in this room in 1981 or 1982 when Assistant Attorney General Baxter, who headed the Antitrust Division, testified when there was the break-up of Ma Bell. Senator Leahy will remember that. He was here. Senator DeWine and Senator Kohl, respectively, joined the Senate in the election of 1994 and the election of 1988, so they did not have the opportunity to participate in those hearings. But it was quite an event.

I remember it especially because Senator Thurmond left, and I was the only Senator present. I had only been in the Senate a short time, and I thought it was terrific to be able to question the Assistant Attorney General. I spent about an hour at it. Nobody was listening, but it was something that I thought was worth doing.

There is another issue which is very much on my mind, and I could not let the presence of the Chairman and CEO of AT&T and Chairman and CEO of BellSouth come to the Judiciary Committee room without my presence and raising an issue which is very much on my mind and on the minds of many people, and that relates to the question as disclosed by the USA Today report about telephone companies turning over identities of callers and calls, not content but callers and calls.

I am not unaware of the position of the U.S. Government on this matter with respect to public disclosure, and it is a matter where I think there is a substantial public interest and the public ought

to have an opportunity to know. And it may be that the details will come forward in closed session, or it may be that there will be another way of finding out exactly what is going on.

The full Committee had considered the possibility on those subjects of a closed hearing. We considered the possibility of subpoenas, and we have put it on the agenda, but behind the NSA electronic surveillance program, which the President confirmed, and we are in discussions with the administration about the submission of that program to the Foreign Intelligence Surveillance Court, and candidly, that comes ahead of the issue of the disclosures by the telephone companies because content is more important, as I see it, and we are pursuing that on a priority basis. But we will return to this issue by the full Committee.

I have seen a publication in the Chicago Sun Times dated today which reports from San Antonio: "AT&T Inc. is changing its privacy policy for Internet and television customers to specify that account information is a business record the company owns and can be disclosed to government and law enforcement and to protect the company's 'legitimate business interests.' AT&T said the account information, including the customer's name, address, phone number, and e-mail address, as well as information about the customer's service, is owned by AT&T. The company said account information doesn't include usage information, such as how a person uses the Web or what TV programs a person watches."

I am very interested to have this assertion of ownership interest; what its legal basis is, if any; when it was adopted; and what relationship it has, if any, to any prior disclosure to the U.S. Government.

Thank you, Mr. Chairman.

Chairman DEWINE. Well, we—Senator Leahy, I did not see you. Senator Leahy?

STATEMENT OF HON. PATRICK J. LEAHY, A U.S. SENATOR FROM THE STATE OF VERMONT

Senator LEAHY. Mr. Chairman, I want to thank you and Senator Kohl for holding this hearing. I agree with Senator Specter that this is very, very timely.

I was one of only five Senators to vote against the 1996 Telecom Act. I was concerned about the consequences of that bill. I argued that the promise of competition between the long distance and local telephone companies would ultimately prove to be a myth. I argued that the Act would allow the local regional Bells to reunite easily with unregulated local monopoly powers.

Over the last decade, we have seen massive consolidation in the industry. Here we are again. Just 6 months ago, two of the biggest local phone companies acquired two of the biggest long-distance companies.

When the AT&T monopoly was broken up, it was divided into seven Bell Operating Companies. Now, after this merger, there are going to be three. And the proposed merger would establish AT&T as the dominant company in 22 States. It seems it only took a few years to go right back and put us right back where we were before.

I wonder what other consolidations this will bring about. As soon as AT&T and BellSouth announced the merger, one analyst said,

"Clearly, Verizon has to go after Qwest now. Verizon has got to keep AT&T from getting it."

You wonder where it ends. Six years ago, I introduced a bill to limit mergers among the RBOCs. I recalled that at my farmhouse in Middlesex, Vermont, and my house here, I had only one choice for local telephone service. And I know these never-ending mergers are not helping rural America, whether it is Vermont or Ohio or Pennsylvania or Wisconsin, very much.

Old monopolies were simply regrouping and getting bigger. It was true then. It is true now. I do not think telephone companies should be able to gain concentrated control over huge percentages of the telephone access lines of this country through mergers.

As President Reagan was wont to say, "Well, here you go again. Here you go again."

If Congress does not protect competition, then consumers are the ones who are going to suffer by having no choices.

I know at my own home the choices I have are between mediocre and poor service. There is no competition there. Where will a consumer, enraged that her phone company is giving the Government records of her phone calls, call for an alternative?

Now, Chairman Specter talked about the AT&T policy report today which AT&T asserts that private customer records are AT&T property. It was in one of a number of papers, actually, this one, USA Today, "AT&T: New privacy policy not 'knee-jerk.'" Well, no, it is not knee-jerk. It is pretty amazing moving on its own. It would allow AT&T to divulge information to the highest bidder or just give it to the Government. It certainly would not make me feel very safe as a customer. It would worry the hell out of me.

In the video services market, the telcos argue that competition is necessary for innovation and lowering prices for consumers. Of course, when it comes to broadband and voice services, apparently they do not feel as strongly about having to compete.

So the merger is a lot more than just two of the biggest remaining wireline communications companies becoming one behemoth.

It would put Cingular, the Nation's largest wireless provider, in the hands of the largest wireline company. That takes care of any issue about competition between wireless and wireline. You wonder where it is going to end. We were told a few years ago, Boy, if we got competition, we are going to be in great shape.

Well, Cingular is currently operating independently of AT&T and BellSouth. I thought it was a promising competitor for voice services and also the broadband access market. Of course, after this merger, it is only going to be part of the largest phone and broadband provider.

When SBC and AT&T merged, AT&T agreed to a number of important but temporary conditions, including offering voice and Internet services unbundled and providing open access to the Internet. Of course, these conditions only remained for 18 months. It is anyone's guess what happens next.

Now, AT&T has made clear its intentions. Mr. Whitacre has infamously said that he is going to charge online businesses, discriminating among services. There goes the Internet as we have known it, and an Internet which has grown very well because Government has kept its hands off. I guess we should have known if you get

a large enough monopoly, they can step in, but Government was wise enough to stay away.

The Internet, which has opened windows on the world in one-room schoolhouses in Vermont or to children from Africa to Indonesia, is the ultimate marketplace of ideas, where a better idea or a better service wins out because it is better. It is not going to be it will win out if it pays more.

So let's see what AT&T and BellSouth have to say about how this helps consumers. And, of course, I have some other questions. Chairman Specter has alluded to them, but I had my staff warn both companies that I am going to ask about this domestic surveillance and whether they act under the guise of law or just in an arbitrary fashion. And I can see by your expressions you can hardly wait for those questions.

Thank you, Mr. Chairman.

Chairman DEWINE. We thank you all for joining us. Let me ask the first question to all of you. Although the telecommunications industry has continued to consolidate, the number of phone company competitors has just decreased. We are seeing more and more competition from other industries, such as cable and Internet companies providing voice service. But at the same time, the phone companies are beginning to offer video service at the same time. In fact, many different types of providers are beginning to compete in providing a bundle of services. So we have begun to focus on this type of competition, known as intermodal, competition as the best hope for providing consumers with more choices.

But, currently, broadband access is mostly available from cable and phone companies, and there is a widespread desire to see a so-called third pipe as a new way to deliver broadband access. Many in the industry believe that the wireless network is the best bet for providing this pipe, and WiMax service appears to be the technology for turning wireless into a viable broadband alternative.

According to testimony from some of our witnesses today, both AT&T and BellSouth own a substantial amount of spectrum which might be suitable for WiMax service. The concern is that after this merger, AT&T will not have any incentive to develop a WiMax service because it would compete with AT&T's existing broadband service. So many people are worried that AT&T will just warehouse the spectrum to prevent others from using it to compete in a broadband market.

So I have two questions for all of you about this. One, how much spectrum is actually practically useful for WiMax? And of that total, how much do AT&T and BellSouth own? And, two, should we be concerned that AT&T and BellSouth will warehouse the spectrum to keep it from being used?

Mr. Whitacre, why don't we just start with you just because you happen to be to my left. And you need to pull that microphone pretty close to you, sir, and make sure it is on. The light should be on.

Mr. WHITACRE. Is that better? Is that good?

Chairman DEWINE. Yes, sir.

STATEMENT OF EDWARD E. WHITACRE, JR., CHAIRMAN AND CHIEF EXECUTIVE OFFICER, AT&T INC., SAN ANTONIO, TEXAS

Mr. WHITACRE. From an AT&T standpoint, we do not have all that much spectrum, really a de minimis amount when you consider the total. BellSouth does have more, and I will let Mr. Ackerman speak to that.

As far as warehousing spectrum, we use that spectrum. We do not warehouse it. WiMax does work. It is in its infancy, as you pointed out. It has a great future. There will be another way to provide broadband type services. I cannot tell you how far away that is, but I think it is months, not years, because we have it in trial at the laboratories.

But as far as warehousing it, we do not warehouse it. We use that spectrum. That is our intent when we acquire it, and I think Mr. Ackerman has a better handle on what BellSouth has than I.

[The prepared statement of Mr. Whitacre appears as a submission for the record.]

Chairman DEWINE. All right. Mr. Ackerman?

STATEMENT OF DUANE ACKERMAN, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, BELLSOUTH CORPORATION, ATLANTA, GEORGIA

Mr. ACKERMAN. Thank you, Senator.

To address your first question about the percentage of WiMax spectrum available and what percent AT&T and BellSouth will own, as we look at that, it will be somewhere close to approximately 16 percent of the total spectrum available for WiMax. So there is a lot of spectrum still out there.

Having said that, Sprint Nextel has significant coverage. Clearwire has significant coverage. XO has significant coverage. And so there are a number of players and a lot of spectrum that is available for continued competition in this market.

I think that in terms of warehousing versus use, I can only say, you know, some of the use that indeed we have put forward, for example, in Katrina, we used that spectrum to provide broadband services in the Bowl when there was a lack of other facilities due to the damage from the flooding that occurred during Katrina. We have provided services in rural areas that we did not have broadband facilities, so that indeed we could, you know, address that market there, places like Palatka. Certainly Athens is not rural, but we were looking next to a university to see how that would work. There were a number of other rural locations where we have provided that service.

So we are experimenting on delivering this service in rural areas and trying to create a robust market there, and indeed, there is a great deal of spectrum still available.

[The prepared statement of Mr. Ackerman appears as a submission for the record.]

Chairman DEWINE. Mr. Geiger?

STATEMENT OF JAMES F. GEIGER, FOUNDER, PRESIDENT, AND CHIEF EXECUTIVE OFFICER, CBEYOND COMMUNICATIONS

Mr. GEIGER. I think that the pressure that comes to bear in our industry, in the competitive industry, is that there are very few choices. Broadband powerline is maybe an aspiration for the future. Cellular is not a substitute. Cable TV certainly has a network duopoly with the incumbent AT&T and BellSouth.

I think what you find is, as the pressure for people to—for us in the industry to answer how do you intend to have your own network into these customers, we clearly cannot financially. It is not financially feasible to string our own networks. You know, it would be the equivalent of putting in new highways and railroad tracks.

So I think what we look at in our industry is a financially viable way of doing that is wireless, and that spectrum would be very valuable to competitive companies.

[The prepared statement of Mr. Geiger appears as a submission for the record.]

Chairman DEWINE. Mr. Rubin?

STATEMENT OF JONATHAN L. RUBIN, SENIOR RESEARCH FELLOW, AMERICAN ANTITRUST INSTITUTE, WASHINGTON, D.C.

Mr. RUBIN. Thank you, Mr. Chairman. I am not sure what definition you are using for "warehousing," but my understanding is that BellSouth has had quite a bit of spectrum—

Chairman DEWINE. You have to pull your microphone up, and you are going to have to turn it on, sir.

Mr. RUBIN. My mistake. Thank you, Mr. Chairman. I am not sure what your definition of "warehousing" is. I know that BellSouth has had spectrum that is suitable for WiMax in the 2.5 gigahertz frequency range for about 10 years. To have taken 10 years to roll out experimental WiMax in Palatka, Florida, and Athens, Georgia, to me I think that is warehousing.

Whether or not in the future this spectrum is warehoused or not warehoused, either way it is a bad deal for consumers, and the reason is because this is the only hope really, at the moment the immediate hope of intermodal competition, that is to say, to have a separate, independent company providing broadband access. And if the post-merger company is able to control wireline broadband access, wireless broadband access, then there really will be no alternative but the cable-telco duopoly, which is the main problem here.

[The prepared statement of Mr. Rubin appears as a submission for the record.]

Chairman DEWINE. Thank you very much.

Senator Kohl?

Senator KOHL. Mr. Whitacre, many of us are concerned about recent press reports concerning the NSA domestic surveillance program and reports that AT&T and BellSouth have given the NSA records of the phone numbers called by millions of Americans. While, of course, we realize that there is a need to monitor phone calls by al Qaeda into the United States, obviously we want to do so in a way that protects Americans' privacy rights as well.

Mr. Whitacre, has AT&T or its predecessor, SBC, turned over customer phone records in bulk to the NSA without court order, as described by that article in the May 10th USA Today?

Mr. WHITACRE. Thank you, Senator. Privacy of our customers is really utmost to AT&T. It has been for many years. Over the years, we have fired a lot of people for violating privacy.

I will tell you that we follow the law, we don't break the law, and that's the story.

Senator KOHL. Well, on May 11th, BellSouth issued a press release denying that it had any contact at all with the NSA or ever provided NSA with customer data. If AT&T did not supply such information to the NSA, why could you not also make the same statement that BellSouth made?

Mr. WHITACRE. Senator, all I can say is the privacy of our customers is utmost, and we follow the law. That's what we do.

Senator KOHL. Thank you.

Mr. Whitacre or Mr. Ackerman, one important consequence of all this consolidation in the industry is that it has become much easier for the Government to eavesdrop on consumer phone calls. There were once seven regional Bell companies and dozens of long-distance phone companies. After the merger, we will be left with just three regional phone companies—companies that have acquired their main long-distance phone company competitors and that owned the two largest cell phone providers. So now the privacy of consumers is left to the judgment of ever fewer and fewer people.

So what are the implications for citizens' privacy rights of concentration of this sort in our telecom system in so few hands? Do you believe that we should consider this in deciding whether to approve the merger?

Mr. Whitacre, we will start with you, and then we would like to hear from Mr. Ackerman.

Mr. WHITACRE. Well, certainly I can only speak for our company, but privacy, again, is utmost. We carefully guard that privacy. I don't think that would change at all—in fact, I know it wouldn't change with a merger or combining two. And, again, we are going to follow the law. The laws of the country are pretty plain. We know how to act on those. We have for many years. And we would follow the law, and I think it makes no difference.

Senator KOHL. Mr. Ackerman?

Mr. ACKERMAN. Yes, certainly in speaking for BellSouth and even anticipating the merger, you know, these two companies have a very similar history. I think they have a very similar culture. And, indeed, protecting the privacy of customers has been at the top of the list for a long, long time. And so I think as I speak for BellSouth, we are obviously very careful about protecting the privacy of our customer base, and I doubt seriously that there would be any impact as a result of this merger.

Senator KOHL. Mr. Whitacre, the San Francisco Chronicle reported earlier this week that a new privacy policy will go into effect at AT&T tomorrow. The policy states that all confidential customer information is the property of AT&T and customer information can be used to "safeguard others or respond to legal process." This is quite different from the current policy, which states that customer data can be used only "to respond to subpoenas, court orders, or

other legal process, to the extent required and/or permitted by law."

So what has prompted AT&T to change its privacy policy to enable it to share customer data more freely?

Mr. WHITACRE. Senator, that is not correct, but I'd be happy to talk about that. Again, we care very much about our customers' privacy. We updated our privacy policy for our retail customers and our website visitors because of the SBC–AT&T merger, and we needed to put the two policies of the company together.

We also updated the Yahoo! Internet policy, AT&T Yahoo! Internet policy, to include video customers and to reflect the fact that we are offering video, which we have not done before.

The spirit of our policies, privacy policies and practices have not changed. We wanted to make our policies easier to read and easier to understand for our customers and to reflect the changes to our company and our new products. We have accomplished this, and we went outside to an organization called Trustee, and they give our new policies the thumbs up. We hope it is easier for them to read. They are in line with and they go in some cases beyond industry standards. I can't think of a company—media company, communications company—that doesn't have a similar policy. We don't provide personal information to third parties for marketing purposes. We use customer information in order to prioritize or customize or personalize our customers' viewing experience.

And so we are under obligation to assist law enforcement under proper circumstances, but trust with us and the trust our customers have in us come No. 1. We have done nothing but update our policy. There really is no change. We have made it easier to read.

Senator KOHL. Thank you very much.

Thank you, Mr. Chairman.

Chairman DEWINE. Senator Specter?

Senator SPECTER. Mr. Whitacre, you say you do not provide customer data to third parties. Does that include law enforcement?

Mr. WHITACRE. I said except under legal circumstances, Senator.

Senator SPECTER. Well, answer my question. Does that include law enforcement?

Mr. WHITACRE. If it's properly asked of us and it's the proper documentation and it's legal and it's lawful, we will cooperate.

Senator SPECTER. Has AT&T provided customer information to any law enforcement agency?

Mr. WHITACRE. Senator, we protect the privacy of our customers and we follow the law, and that's all I can say about that.

Senator SPECTER. Are you declining to answer my question, Mr. Whitacre?

Mr. WHITACRE. We follow the law, Senator.

Senator SPECTER. Does AT&T provide customer information to any law enforcement agency?

Mr. WHITACRE. We follow the law, Senator.

Senator SPECTER. That is not an answer, Mr. Whitacre. You know that.

Mr. WHITACRE. That's all I'm going to say is we follow the law. It is an answer. I'm telling you we don't violate the law. We follow the law.

Senator SPECTER. No, that is a legal conclusion, Mr. Whitacre, and you may be right or you may be wrong. But I am asking you for a factual matter. Does your company provide information to the Federal Government or any law enforcement, information about customers?

Mr. WHITACRE. If it's legal and we are requested to do so, of course we do.

Senator SPECTER. Have you?

Mr. WHITACRE. Senator, all I'm going to say is we follow the law.

Senator SPECTER. That's not an answer. That's not an answer. It's an evasion.

Mr. WHITACRE. It is an answer.

Senator SPECTER. If you are under instructions by the Federal Government—

Mr. WHITACRE. We follow the law, Senator.

Senator SPECTER. You said that. I don't care to hear it again.

Mr. WHITACRE. I don't care to repeat it again, either, but—

Senator SPECTER. Well, then don't.

Mr. WHITACRE.—we do.

Senator SPECTER. Then don't. If you are under instructions by the Federal Government as a matter of state secrecy not to talk, say so.

Mr. WHITACRE. Senator, we follow the law.

Senator SPECTER. Well, I think that answer is contemptuous of this Committee.

Mr. Ackerman, does your company provide customer information to any law enforcement agency?

Mr. ACKERMAN. Where we are given a subpoena, yes, we do. But in relationship—

Senator SPECTER. Could you speak into the microphone so we can hear you, please?

Mr. ACKERMAN. Yes. In relationship to the story in USA Today, NSA did not ask BellSouth for information. We did not provide bulk calling information to NSA, and we do not have a contract with NSA.

Senator SPECTER. So you provided no information to NSA.

Mr. ACKERMAN. No, sir. We have been unable to determine that we have. We do indeed provide—

Senator SPECTER. You said you have been unable to determine?

Mr. ACKERMAN. Well, that is proving a negative, but that is not—I am not splitting words there. I am simply saying we do not have a contract with NSA, they have not asked, and we have not provided.

Senator SPECTER. OK. That is—

Mr. ACKERMAN. But I do, you know, hasten to say that where we get a legal subpoena from a law enforcement entity and it is court-ordered or any kind of lawful request, we do provide that information.

Senator SPECTER. Mr. Ackerman, I respect that. That is the way the system works. If you get a subpoena or a court order, you provide the information.

Mr. Whitacre, with that precedent in mind, has your company gotten a subpoena or a court order to provide any customer information?

Mr. WHITACRE. Senator, we get court orders or subpoenas all the time to provide that information—

Senator SPECTER. Let me rephrase—

Mr. WHITACRE. If it's legal, we do it.

Senator SPECTER. Have you gotten any court order or subpoena or legal process to provide the information that was disclosed in the USA Today story?

Mr. WHITACRE. I assume you are talking about the story that appeared several weeks ago.

Senator SPECTER. That is a pretty safe assumption.

Mr. WHITACRE. Well, Senator, I am not allowed to answer that. That is classified information. We follow the law.

Senator SPECTER. Well, now you are saying a little more. Has somebody told you you are not allowed to provide that information?

Mr. WHITACRE. Well, Senator, I have talked to a lot of lawyers on this, and, you know, the answer is just the one I have given you, that is, we abide by the law.

Senator SPECTER. You were told you could not provide the information. You have testified to that. And you have testified that you could not provide the information because it is classified.

Mr. WHITACRE. Senator, I was advised to say—and I agree—that we follow the law. We abide by the laws.

Senator SPECTER. Well, you have said a little more.

Mr. WHITACRE. I cannot say any more than that.

Senator SPECTER. Who told you that you could not provide the information because it was classified?

Mr. WHITACRE. I have certainly talked to several attorneys in AT&T, and—

Senator SPECTER. Who are they?

Mr. WHITACRE. Well, the general counsel, for example. But I am not at liberty to talk any more about it other than to inform you that we follow the law.

Senator SPECTER. My red light is about to go on, and I respect the red light, and I respect you, and you and I will talk about this further.

Mr. WHITACRE. Fine. That would be fine with me.

Chairman DEWINE. Senator Leahy?

Senator LEAHY. Thank you, Mr. Chairman. I have enjoyed—not enjoyed, but I have noted Mr. Whitacre's non-answers to Chairman Specter. I still don't know whether NSA got the information or not. Mr. Ackerman says they did not. You do not respond. It would be interesting if they were able to in one and not in the other. It makes you wonder just how important the information is if you could leave such big gaps.

Mr. Whitacre, you have said over and over again that the privacy of your customers is paramount. The Washington Post this morning reported your company has revised its privacy policy to claim—and I was astonished at this—that AT&T owns personal customer records and the company has a right to disclose those records. In addition, the new policy apparently no longer assures customers that AT&T will not access, read, upload, or store data from private files without specific authorization. It seems to allow AT&T to collect Internet navigation and video viewing records.

I am beginning to wonder if anybody who deals with your company, any American who deals with your company, whether they have any privacy at all left. The administration claims the right to eavesdrop on Americans' telephone calls without a warrant. Now the Nation's largest telephone company says that they can control these private telephone and Internet records, and in this report, you are not asking about any kind of a valid order. Your spokeswoman, Tiffany Nels, was quoted as saying, "These changes are principally motivated" by the proposed merger we are examining today. And I know that you were reading very carefully the statement in response—and I agree with him, the non-response—to Chairman Specter. At least you are not exactly taking the Fifth, but you are certainly not responding. If that was done to placate Chairman Specter on the Republican side or me on the Democratic side, it did not.

Mr. Ackerman, let me ask you this: This newly announced AT&T policy, is that the current policy of BellSouth?

Mr. ACKERMAN. Senator, I haven't had an opportunity to see—I read that in the newspaper this morning also. You know, again, I think that the spirit and the actuality of all this is that, you know, our customers are notified in advance. We put on our website when they apply for service the conditions under which we will share their information. And—

Senator LEAHY. Well, let me go into that a little bit. Both Senator Specter and I are former prosecutors. Senator DeWine was. We know that you can get a subpoena for such records. I do not question that. But would that allow you to just go in and—do you interpret your company policy that you can just go in and sell data to somebody that may want it for advertising purposes or anything else?

Mr. ACKERMAN. No, sir. As I was about to say, we do not disclose this information to third parties for marketing purposes or other purposes. We, in fact, do tell them that this information can be shared if we are trying to deal with some legal issue that, in fact, has had a subpoena or a lawful request for that data. And, indeed, we share this information with them.

As far as laying everything down, again, I have not had an opportunity to look at that tit-for-tat, but I think in general, it is probably fairly similar.

Senator LEAHY. Well, Mr. Whitacre, you—am I pronouncing your name correctly?

Mr. WHITACRE. Yes, you are, Senator.

Senator LEAHY. Mr. Whitacre, you said your new privacy policy does not represent a change. Apparently, the press probably did. But does that mean you have always taken the position you had complete control over private customer data?

Mr. WHITACRE. Senator, as Mr. Ackerman just said, we carefully guard that information. The conditions are put out up front to each customer what that concerns. Those are business records. We use those to personalize the services we give. We do not market those or give those lists or any of that information to third parties. We have just simply tried to make the privacy policy more understandable to our customers, and I would dare say that every company

has a privacy policy that is very similar, if different at all, to this one.

Senator LEAHY. Let me ask you specifically about your privacy policy. Your privacy policy, if somebody signed a contract with you, with your company for your service, does that allow you to own the data? I am not talking about a valid court order or valid law enforcement subpoena. Does it allow you to own, under the contract they sign, does it allow you to own their data?

Mr. WHITACRE. Well, it allows us to have information, Senator, to, for example, personalize their service, installation data, repair data if the problem goes in, but that data is held in the strictest of confidence. But it is business records of AT&T.

Senator LEAHY. To personalize their—if they have broadband, would that include being able to tell companies which sites they go on the most?

Mr. WHITACRE. No, sir, we would not do that.

Senator LEAHY. Does it allow it to have people tailor ads for that particular customer?

Mr. WHITACRE. No, sir, we would not do that.

Senator LEAHY. My time is up, but I am disturbed by this testimony. I would also note, Mr. Chairman, we have votes on. I was going to ask Mr. Whitacre about why he opposes network neutrality, but I will submit that for the record.

Chairman DEWINE. All right. Mr. Whitacre, members of the panel, we have a series of three votes. That is probably good news for you all. That means the hearing is going to end in just a moment. I am going to ask one question, and we will then turn it over to Senator Kohl. I am going to leave after I ask my question because I am going to start walking to the vote.

Mr. Whitacre, it is a question for you, if you could take about 2 minutes to answer it, and then that will give Senator Kohl time to ask one question, as well, maybe Senator Leahy.

On several occasions, we have discussed your new video service, which you are beginning to roll out throughout the country. You have said that in certain areas this merger will increase the speed of the rollout. How are you going to—how are you doing with regard to your efforts to provide video service? What are the biggest problems you have encountered? Where are you having the most success? And, specifically, what are AT&T's plans to provide video service in Ohio? And will this merger make service available any more quickly in Ohio? In about 2 minutes, if you can do that.

Mr. WHITACRE. Well, we are doing well in the television services called IPTV. We now have it in operation in San Antonio. We have a schedule. We will cover 18 million of our current AT&T customers in the next 3 years. The BellSouth addition to that will make that number go up. I have not had a chance, nor can I yet tell you how many.

There is a plan for Ohio, I am happy to report. I think you will like the service very much. I can't tell you the specific date, but I can tell you it will be within the next 12 to 14 months.

Chairman DEWINE. Senator Kohl, for about 2 minutes, and then Senator Leahy for 2, and we will be done.

Senator KOHL. Mr. Whitacre, as part of the approval of the SBC–AT&T merger, we recommended and both Justice and the FCC ap-

proved a number of pro-competition merger conditions. These conditions included offering DSL Internet connections to consumers without also requiring them to buy phone service, a requirement that AT&T divest duplicative, overlapping networks, and several others.

Could you commit to us today to follow similar merger conditions as a condition of approval of this merger today? If there are any merger conditions that you believe should not be applied to this deal, could you identify them and explain why?

Mr. WHITACRE. Senator, I don't believe that there should be any conditions applied. The industry has changed drastically. There are many competitors. There used to be one; now there are hundreds. There is wireless, there are CLECs, there are cable companies, there are voice over IP services. I don't believe there should be any restrictions.

In the previous one, we had some on special access where we had duplicative facilities and there was no other way to get in the building, if you would. Certainly we would agree with that this time. Beyond that, I don't think there should be any conditions.

Senator KOHL. Mr. Geiger, do you have any comment on that?

Mr. GEIGER. Well, I think that this combined company is vertically integrated beyond which most people understand. You know, even in an intermodal environment, companies like Sprint and Nextel need to come to these companies for interconnection, for special access services. And I would tell you that as far as network intermodal—real network competition, there are very few. The cable company has real competition in residence but not to business, I am here to tell you—because I look for alternatives. BellSouth & AT&T are my two biggest suppliers, and we constantly are looking for alternatives. There aren't any.

So on a network basis, there isn't much intermodal competition at all.

Chairman DEWINE. Senator Leahy?

Senator LEAHY. Thank you, Mr. Chairman.

Mr. Whitacre, you have been one of the most outspoken opponents of network neutrality. You very openly, and I would say very honestly, express your intention to charge Internet companies for access and for priority in reaching consumers on your network. While I disagree with what you want to do, I admire your candor. If you are going to pick our pockets, you are going to let us know ahead of time.

But last year, as part of the AT&T–SBC transaction, your company made, by the FCC, what they termed certain voluntary commitments. One of them was to comply for 2 years with their policy statements. That arguably permits broadband access providers to charge for better access. I understand you currently are not discriminating against providers.

Why did you make that commitment to the FCC? And what circumstances would allow you to back off from it?

Mr. WHITACRE. Senator, the FCC has put out a set of principles covering the Internet, which I think cover all facets of it. Maybe contrary to popular belief, AT&T is not the Internet. There are many other backbone providers to the Internet, not just AT&T.

I really think it is probably a solution looking for a problem. We have openly stated, as I will again, we will not block, we will not impair anybody's service on the Internet. But, Senator, this Internet is growing, and it is growing at an astounding rate. The facilities that back up the Internet, the backbone, if you will, continually have to be expanded. Somebody has to pay for that. You cannot expect any company, my company or anyone else, to pour in these billions of dollars that are required without some return.

Senator LEAHY. But what you are saying is you could say we will charge more if you get this site than if you get this site. Is that what you are saying?

Mr. WHITACRE. No, Senator. I am saying we would like to offer quality of service, or whatever the customer wants, for a fee. The alternative to that is to raise the fees for the end users if somebody is going to pay for this, and it has to be paid for. I don't think that is a very good solution.

Chairman DEWINE. Mr. Whitacre, I—

Mr. WHITACRE. I think quality of service and those sorts of things would be healthy. Sorry, Senator.

Chairman DEWINE. No. I know you have got to answer, but our time is up, and we have about 4 minutes to walk over there and vote. So we appreciate it. We appreciate all of you coming in.

We will submit questions for the record, and we will give you all a chance to answer some more questions. But we appreciate you coming in. Thank you.

[Whereupon, at 3:55 p.m., the Subcommittee was adjourned.]

[Questions and answers and submissions for the record follow.]

[Additional material is being retained in the Committee files.]

QUESTIONS AND ANSWERS

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July 21, 2006

VIA ELECTRONIC AND U.S. MAIL

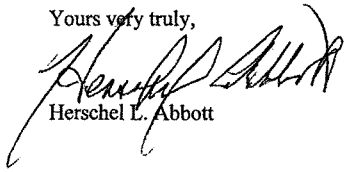
Aaron Calkins
Antitrust Subcommittee
Senate Judiciary Committee
224 Dirksen Senate Office Building
Washington, DC 20510-6425

Dear Mr. Calkins:

In response to Chairman DeWine's July 5, 2006 letter to Duane Ackerman, enclosed please find BellSouth's responses to the written questions from members of the Antitrust, Competition Policy and Consumer Rights Subcommittee of the Senate Committee on the Judiciary.

Please let me know if you have any questions or need any additional information.

Yours very truly,



Herschel L. Abbott

HLA/dlr

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Follow-up questions for the hearing
"The AT&T and BellSouth Merger: What Does It Mean for Consumers?"
Subcommittee on Antitrust, Competition Policy and Consumer Rights

Questions of Senator Mike DeWine

1. For some businesses, AT&T and BellSouth are among the few—if not the only two—providers which offer the type of complex telecom services they need. Although, as the testimony for this hearing has shown, there appears to be some dispute about how many businesses will find themselves in this position. Due to this merger, many of these businesses will be losing a choice, and some may even be left with only one choice, which raises obvious competitive concerns. On the other hand, however, a combined company may be in a better position to invest in new services for business and corporate customers. How do the merged company's claims of an enhanced ability to invest in new services for business customers weigh against the potential loss of competition due to this merger, and how does this merger affect the marketplace?

RESPONSE:

Let there be no mistake – the combination of BellSouth and AT&T will be a major win for business customers. The parties have identified numerous substantial benefits from the merger, including creating a better and more efficient network that will be better able to respond to natural disasters and emergencies, giving BellSouth customers access to the innovations developed by Bell Labs, and providing customers in BellSouth's region the benefit of a seamless integration between BellSouth's local assets and AT&T's out of region assets. The merger also will generate significant financial synergies, such as lower purchasing costs, eliminating redundant assets, and lowering operating costs. In addition, the merger will allow for a more seamless integration of the wireless products offered by Cingular with the wireline products offered by both BellSouth and AT&T. For example, we will be able to use one IP Multimedia Subsystem ("IMS") network instead of the three now being built by Cingular, AT&T and BellSouth.

These benefits are not seriously disputed by the merger's critics. And the specter of lost competition those critics attempt to raise against the merger does not survive

scrutiny. The truth is that in today's telecommunications market, the merger will in no way reduce the vibrant level of competition currently enjoyed by telecom customers.

First, in the business realm, BellSouth and AT&T focus on serving very different types of customer needs. For the most part, BellSouth focuses on mid sized and smaller businesses that are entirely contained in BellSouth's region. It must do this because BellSouth does not have significant assets outside of its own region. As a result, despite efforts to partner with other providers, BellSouth has had extreme difficulty competing to serve the primary requirements of larger enterprise customers, which almost invariably have many locations out of BellSouth's region.

Second, as the FCC already determined in reviewing the SBC/AT&T and Verizon/MCI mergers, there are a significant number of competitors for enterprise customers, including interexchange carriers like Verizon and Sprint; data providers like Global Crossing and Level 3; international carriers such as BT and FT; CLECs and cable providers like Time Warner and Covad; VoIP providers like Vonage and Skype; systems integrators like IBM and EDS, and many others. Indeed, dozens and dozens of customers of AT&T and/or BellSouth filed statements with the FCC attesting to the vibrant state of competition they have experienced in the real-world marketplace.

Third, AT&T operates local fiber networks in only 11 BellSouth metropolitan areas. The vast majority of the buildings connected to AT&T's local fiber network in these areas are either currently served by other carriers or readily could be. In fact, applying competitive screens used by the Department of Justice, there are no more than 32 buildings in the BellSouth region that may raise any competitive issues, and these buildings are located in Miami/Ft. Lauderdale and Atlanta, two of the most competitive areas in the entire nation. Thus, there are few, if any, businesses for which AT&T and BellSouth are the only two providers of the services these businesses may need.

2. Cingular Wireless is now jointly owned by AT&T and BellSouth, and as a result seems to operate somewhat independently of both parent companies; after merger, AT&T will have more direct control over Cingular operations, and we have heard concerns that the merger will increase the incentive to use wholesale rates to disadvantage rivals. How will the merger change the way Cingular is operated, and how do you respond to concerns raised about wholesale rates?

RESPONSE:

The merger will make Cingular a more efficient and nimble competitive force. Today, Cingular is jointly controlled by AT&T and BellSouth. While this arrangement has been extremely successful, there are opportunities to make it even more so, particularly as the convergence between wireless and wireline services continues to grow.

For example, the merger will allow the combined firm to fulfill business customers' demand for one monthly recurring charge for a combined bucket of wireless and wireline minutes of use. The combined firm also will have significantly more flexibility to combine wireless services in existing package discount programs to business customers and offer business customers a single point of contact for all billing and service issues.

The concern raised by some opponents that bringing Cingular under unitary control will result in discrimination against wireless companies is simply misguided. Over the history of the wireless industry, it has been common for wireless companies to be owned by incumbent telephone companies, and few would question that wireless competition has nonetheless thrived. Furthermore, wholesale rates for special access services provided to wireless carriers by the merged company will continue to be regulated by the FCC, either under: (i) pricing flexibility in those areas with significant competition where the FCC has granted authority to operate under pricing flexibility; or (ii) price cap regulation in those areas where competition is not as robust.

The FCC has repeatedly found that issues concerning potential discrimination in the provision of services by incumbent carriers should be determined in specific regulatory proceedings or through industry-wide regulation rather than through merger-review proceedings, and the Subcommittee can be confident that the FCC will continue to investigate such issues as appropriate.

3. In your testimony you describe a number of potential advantages to merging with AT&T, such as increased efficiency at Cingular, improving the network, and achieving cost savings. However, many of these advantages have existed for some time, yet in the past, despite being mentioned as a potential merger partner on numerous occasions, BellSouth has always decided to go it alone. What has changed to make this deal more appealing than such a deal would have been 5 years ago?

RESPONSE:

BellSouth is proud of its track record as an independent company, but many of the opportunities in today's telecommunications marketplace – opportunities to serve the ever-growing requirements of its national and international customers who are located in the Southeastern United States, opportunities to develop a true competitive alternative to cable television, opportunities to develop fully converged wireless/wireline services – can be achieved much more readily, efficiently and effectively by a combined AT&T/BellSouth than would be possible by BellSouth alone. In addition, the wireless business is increasingly a national business. Simply put, the merger offered BellSouth, its customers and its shareholders an unbeatable opportunity to be at the cutting edge of the 21st century communications market.

4. In the past, critics have argued that the old Bell companies avoid competition by staying out of each other's territories. For the most part it is true that we have not seen very much "Bell against Bell" competition, which has been a source of frustration to many consumers and policy-makers as well. But we heard from all of the witnesses at this hearing that this merger will increase investment to integrate the various types of networks, and that we will soon see products being delivered to consumers over the internet, which should change the market dynamic and also the economics of providing those services. Do you think that a combined AT&T/BellSouth would be more likely to enter into Verizon's and Qwest's territories than it has so far?

RESPONSE:

Thanks to the emergence of a myriad of new forms of enterprise competition through wireless, the Internet and other modalities, AT&T, Verizon and Qwest are national competitors already. Similarly, Cingular is a major national player already in robust competition with Verizon Wireless, T-Mobile, Sprint-Nextel, Alltel and others. The added capabilities of BellSouth will make the combined company even better positioned to compete for customers of all sizes across the nation. Thus, as we have already seen with Verizon's increasingly vigorous competition in the BellSouth region after the MCI transaction, we expect the combination of BellSouth and AT&T to enhance the merging companies' incentives and abilities to compete out of region.

5. When the Justice Department looked at the SBC/AT&T merger, and the Verizon/MCI merger, they focused on loss of competition for high-capacity business customers, and to address that problem, they utilized an unusual remedy - - something known as an "indefeasible rights of use." Basically, this is like a long term lease that provides a certain amount of service to these businesses. How has this remedy been working? Do you think it has been effective at maintaining competition in these markets?

RESPONSE:

The remedies imposed by the Antitrust Division in the prior transactions took place outside the territory where BellSouth operates, so AT&T is better situated than BellSouth to answer that question. In the view of BellSouth, however, competition for private line and special access services in the BellSouth territory is presently intense, with the merger doing nothing to change this fact. Consequently, we believe no such remedy should be required in the pending transaction.

Questions of Senator Herb Kohl

More than 99% of consumers who access the internet with a broadband connection today choose between their Bell phone company or their cable provider. So, many argue that the giant phone and cable companies have the capacity to become the gatekeepers for internet content. This has led to proposals to require net neutrality.

Your company argues that legislation to require non-discrimination by internet service providers is unnecessary because no phone company has ever blocked or degraded internet content. However, your company's public statements seem to indicate to the contrary.

Last December, the Washington Post reported that the Chief Technology Officer for BellSouth stated that BellSouth should be allowed to strike deals to give certain web sites priority in reaching computer users. The Post reported that he told industry analysts that BellSouth should have the ability to charge Yahoo to have its search site load faster than Google, for example.

(a) Does this statement show that BellSouth is prepared to cut deals right now that will give preferential treatment to certain web sites and therefore this debate is not premature? Does BellSouth in fact have any such deals in place right now, or plans to do so in the future?

(b) If your answer to part (a) is that BellSouth presently has no such deals, then what would be wrong with enacting a net neutrality principle into law?

RESPONSE:

(a) BellSouth is willing to enter into commercial agreements with Internet service companies seeking to purchase optional network management services from BellSouth, which would enable their customers to enjoy a better Internet experience. For example, BellSouth provides hosting services for Movielink.com by which the content offered by Movielink.com is stored in servers on BellSouth's network. This arrangement allows Movielink.com customers to have a better customer experience when downloading movies because it avoids problems that can occur when content is transmitted between multiple networks (e.g., latency and packet loss).[1] Providing hosting services that enable

[1] This enhanced experience paid for by Movielink.com occurs without degradation of the customer's general internet access service, which BellSouth offers at varying speeds (four

content to be delivered closer to the end-user is a well established commercial business practice on the Internet today. BellSouth also has discussed offering Movielink.com network priority services beyond local hosting, although BellSouth has no agreement with Movelink.com or any other content provider that gives "certain web sites priority in reaching computer users." However, if BellSouth were to enter into such an agreement, BellSouth would not block customer access to or degrade the ease and speed by which customers can access competing websites.

(b) Preliminarily, we wish to point out that the predicate to the question – that customers have limited choices among broadband providers -- is incorrect. According to the FCC's high-speed Internet access subscribership data, vigorous competition exists for broadband subscribers, including vigorous competition between cable and phone companies,[2] with significant increases in penetration[3] and significant reductions in prices.[4] Furthermore, there is increased competition from satellite and fixed wireless

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services ranging from 256 kbps to 6 Mbps). The arrangement is analogous to today's familiar 1-800 services through which some businesses offer customers an improved experience by paying for the call the customer makes to transact business, while not degrading the customer's basic telephone service.

[2] According to the FCC's broadband deployment data, the share of all residential high-speed lines accounted for by cable modems has declined from 70% in June 2000 to 61% in June 2005, while ADSL rose from 24.4% to 37.2%. *See* High-Speed Services for Internet Access: Status as of June 30, 2005, Industry Analysis and Technology Division, Wireline Competition Bureau, Table 3 (April 2006) ("*FCC Broadband Report*").

[3] According to the FCC, between June 2000 and June 2005, residential ADSL subscribers increased from under a million to over 14 million while residential cable subscribers increased from approximately 2 million to over 23 million. *See FCC Broadband Report* at Table 3. Furthermore, the percentage of zip codes reported to have two or more providers rose from 33.7% in December 1999 to 82.9% in December 2004 and 88.8% by June 2005. *FCC Broadband Report* at Table 15.

[4] According to the *Pew Broadband Report*, the average price of residential DSL service has decreased from $38 per month in February 2004 to $32 per month in December 2005. *See Pew Broadband Report* at 6-7.

broadband, with the number of lines almost doubling between December 2004 and June 2005.[5]

Importantly, the FCC's data does not capture significant portions of the broadband market; as the FCC has made clear, its data only include broadband services involving facilities-based, high-speed connections that "terminate at end user locations ...."[6] In other words, the FCC's data do not reflect mobile wireless broadband services including unlicensed services, such as Wi-Fi and WiMax, as well as licensed services, such as the mobile broadband services of wireless carriers including Cingular, Verizon Wireless, and Sprint Nextel, which enable consumers to access the Internet using a cell phone, personal digital assistant, or wireless modem card in a personal computer. Given the substantial number of customers who access the Internet using mobile devices every day, it would be incorrect to read the FCC's data to suggest that customers do not have broadband choices beyond "their Bell phone company or their cable provider."

Turning to the substance of the question, from BellSouth's perspective, "net neutrality" means assuring that broadband consumers have the ability to: (i) access their choice of legal Internet content within the bandwidth limits and quality of service of their service plan; (ii) run applications of their choice, within the bandwidth limits and quality of service of their service plans, as long as they do not harm the provider's network; and (iii) attach any devices at the consumer's premises, so long as they operate within the

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[5] FCC data shows that from December 2004 through June 2005 the number of satellite and wireless broadband lines almost doubled, from 550,000 to almost 1 million. While virtually all of this increase has been for business customers, the FCC and others believe that wireless technologies have wider potential for broadband provision. *See FCC Broadband Report* at Table 1.

[6] *FCC Broadband Report* at 1.

bandwidth limits and quality of service of their service plans and do not harm the provider's network or enable theft of services. With that said, there would be nothing wrong in theory with enacting these "net neutrality" principles into law, assuming stakeholders and policymakers could even agree on what "net neutrality" actually means. These principles are essentially the "Broadband Principles for Consumer Connectivity" developed in September 2003 by the High Tech Broadband Coalition, a group consisting of equipment vendors and others.[7] BellSouth supports these principles and does not oppose legislation that would write them into law. In fact, this is generally the approach to "net neutrality" taken in H.R. 5252, which BellSouth has endorsed.

However, BellSouth opposes the efforts of proponents of a restrictive form of net neutrality who seek to impose an unprecedented requirement that broadband providers not discriminate against Internet application or content providers despite the substantially different network requirements imposed by certain applications such as video streaming, VoIP and on-line video game providers. Imposing such a "nondiscrimination" requirement under the guise of "net neutrality" would be ill-advised for several reasons.

First, restrictive "net neutrality" legislation would mean higher broadband prices for consumers by requiring that they disproportionately shoulder the infrastructure costs incurred by broadband providers in building out their networks. According to one analyst, if broadband providers are precluded from entering into commercial agreements with content owners, the cost of broadband service "would be as much as $80 per

[7] Ex Parte Letter from High Tech Broadband Coalition to Michael K. Powell, FCC Chairman, CC Docket Nos. 02-33, 98-10 & 95-20 and CS Docket No. 02-52 (September 25, 2003); Ex Parte Letter from Robert Blau, BellSouth, to Michael K. Powell, FCC Chairman, CC Docket Nos. 02-33, 98-10 & 95-20 and CS Docket No. 02-52 (September 29, 2003).

month."[8] A preferable solution is to allow market forces to determine when and whether content owners should partner with broadband providers to enable broadband providers to make significant investments needed to carry the content owners' traffic. If this were to occur, the likely outcome would be that prices to consumers would *fall*. Restrictive "net neutrality" provisions thus have the effect of keeping prices to broadband users higher in the future than would otherwise be the case, which would undermine efforts to increase broadband deployment and penetration.

Second, restrictive "net neutrality" regulation in the form of a broad nondiscrimination obligation would harm consumers by reducing innovation in services and investments in increasing broadband capacity and reliability. Most obviously, regulatory obligations can be expected to reduce incentives for new investment, by eliminating the ability of broadband providers to enter into commercial agreements with content owners to build out the network to handle the content providers' ever increasing traffic. Moreover, regulation can inhibit innovation and differentiation, preventing BellSouth and other broadband providers from offering services that are optimized for certain applications, such as video conferencing and home health care.

Third, restrictive "net neutrality" regulation would harm consumers by locking content owners into an historical business model that has diminishing significance in the future. Internet traffic has traditionally been delivered on a "best-efforts" basis that treats all traffic equally. This model worked fairly well when the Internet was used for applications such as e-mail and web browsing that were quite tolerant of delay. However, real-time, interactive services like VoIP, on-line video gaming or video

[8] Craig Moffett, "Net Neutrality – Beware the Law of Unintended Consequences," Bernstein Research Weekly Notes, at 3 (April 7, 2006).

streaming are much less tolerant of packet delay. In BellSouth's view, broadband providers must be in a position to manage their traffic to ensure that services that cannot tolerate delay are treated appropriately, and this may require treating traffic differently, something that restrictive "net neutrality" regulation would prohibit.

Moreover, BellSouth's efforts to deliver such real-time, interactive services is significantly impeded by so-called "bandwidth hogs" who use a disproportionate amount of BellSouth's bandwidth, thus diminishing the experiences of other users. Again, broadband providers must be in a position to manage the traffic on their networks to ensure that a few users are unable to diminish the experience of the balance of its users, and again, restrictive "net neutrality" language may inhibit BellSouth from doing so.

As a recent OECD report on net neutrality cautions, "The introduction of quality of service over the Internet is something that policy makers should encourage and promote. There is likely a wide range of future innovations that will require better quality of service than the current Internet can provide. The ability to designate priority to certain applications will be a boon for consumers and providers as long as there is sufficient competition in the market."[9]

Finally, the "nondiscrimination" obligation that proponents of restrictive "net neutrality" seek to impose would be costly and lead to endless litigation. The nondiscrimination obligation historically imposed upon common carriers, which is set forth in 47 U.S.C. § 202, only applies to customers. As one federal court recently explained, "[t]he bottom line is that the focus of a § 202 inquiry is on discrimination

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[9] Working Party on Telecommunication and Information Services Policies, *Network Neutrality: A Policy Overview*, Organization for Economic Cooperation and Development (April 2006) at 3.

among customers" of the common carrier, not third parties.[10] With respect to telecommunications services provided under section 202, Internet application and content providers are third parties, not customers, and thus have never enjoyed any protections under common carrier regulation. And, of course, the cable provision of broadband services has never been subjected to nondiscrimination requirements.

However, restrictive "net neutrality" language of the sort proposed by Senators Snowe and Dorgan would change all that; in addition to extending nondiscrimination obligations to all broadband network providers (which has never been the law previously), it would expand this obligation to cover not only customers but every Internet application and content provider. Consequently, under this approach, to the extent any website, Internet application, or blog believed its content was not being treated the same as the broadband network provider's content, it could file a complaint against that provider. This would be a trial lawyer's dream but do nothing to help consumers.[11]

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[10] *Z-Tel Communications, Inc. v. SBC Communications Inc.*, 331 F. Supp.2d 513, 556 (E.D. Tex. 2004); *accord* Sixth Memorandum Opinion and Order, *Petition for Forbearance of the Indep. Tel. & Telecomms. Alliance*, 14 FCC Rcd 10840, ¶ 10 (1999) ("section 202 of the Act . . . prohibits unreasonable discrimination among customers and rates that are unjust and unreasonable"); Notice of Proposed Rule Making, *Bundling of Cellular Customer Premises Equip. and Cellular Serv.*, 6 FCC Rcd 1732, ¶ 2 n.2 (1991) ("Section 202(a) of the Act prohibits carriers from discriminating unreasonably among customers in the 'charges, practices, classifications, regulations, facilities, or services' for 'like' communication service.").

[11] This raises another aspect of "nondiscrimination" over which trial lawyers are likely to salivate. Read literally, the language proposed by Senators Snowe and Dorgan would appear to say that a broadband network provider is "discriminating" against content stored on a remote server that does not download as quickly as content stored on a server on the provider's network. Similarly, some enterprising lawyer could argue that a broadband network provider is "discriminating" in favor of its own content by loading such content on servers on its network without doing the same for every other content provider.

In sum, the Internet has been able to flourish and innovate in large part because of the absence of direct government intervention. Imposing restrictions on the types of business models that broadband providers and content providers can utilize would reduce the incentives and ability of broadband providers to invest in their networks, improve or differentiate their services, and lower costs to consumers, making the future of the Internet less promising than its past.

Questions of Senator Patrick Leahy

1. At the hearing, you stated that you had not yet had an opportunity to review AT&T's revised privacy policy. You also stated that you would not interpret BellSouth's policy as permitting the disclosure of subscriber information for commercial purposes or in the absence of lawful process. Now that you have had more time to examine AT&T's revised policy, do you believe it is consistent with your company's policy? If not, how is it different?

RESPONSE:

BellSouth has reviewed AT&T's Privacy Policy dated June 16, 2006, as well as AT&T's Privacy Policy for AT&T Yahoo! And Video Services effective June 23, 2006. In general, AT&T's policy concerning customer privacy is consistent with BellSouth's – both companies are committed to honoring and protecting customer privacy. For example, absent customer consent, BellSouth will not make customer-specific information gathered online available to unaffiliated organizations for commercial purposes unrelated to the business of BellSouth. Based on BellSouth's understanding of AT&T's privacy policy, the same is true for AT&T. Similarly, both BellSouth and AT&T have codes of conduct to which their employees are required to adhere, both of which require compliance with legal requirements and corporate policies related to the privacy of communications and the security and privacy of customer records.

In certain respects, AT&T's publicly available privacy policies appear to be more extensive than BellSouth's. For example, AT&T has adopted additional privacy protections for customers utilizing AT&T's Internet services provided jointly with Yahoo! as well as for AT&T's video services. BellSouth does not have a similar arrangement with Yahoo! and has not made a decision about whether to proceed with a broad-scale commercial roll out of a competing video service (which is another benefit of the merger, since it would allow the combined company to bring a competing video service to BellSouth's customers more quickly than would otherwise occur).

James F. Geiger Responses

Follow-up questions for the hearing
"The AT&T and BellSouth Merger: What Does It Mean for Consumers?"
Subcommittee on Antitrust, Competition Policy and Consumer Rights

Questions of Senator Mike DeWine

1. For some businesses, AT&T and BellSouth are among the few—if not the only two—providers which offer the type of complex telecom services they need. Although, as the testimony for this hearing has shown, there appears to be some dispute about how many businesses will find themselves in this position. Due to this merger, many of these businesses will be losing a choice, and some may even be left with only one choice, which raises obvious competitive concerns. On the other hand, however, a combined company may be in a better position to invest in new services for business and corporate customers. How do the merged company's claims of an enhanced ability to invest in new services for business customers weigh against the potential loss of competition due to this merger, and how does this merger affect the marketplace?

Response: As history has demonstrated, without competitive pressure, the RBOCs will have no incentive to invest and innovate. For example, in the residential market, it wasn't until the cable companies began to offer cable modem service that AT&T and the other RBOCs began to invest in mass market xDSL service offerings and only then did they do so in exchange for and after significant regulatory relief. Without the presence and competitive pressure exerted by competitive local exchange providers, DSL would never have become a commercial reality. In light of this it is fair to say that the combined company actually has less incentive to invest in new services particularly in the business market due to do the elimination of AT&T, its single largest competitor. Additionally, and specific to the small and medium size business market, the elimination of one of the few providers of alternative local transmission providers in the BellSouth region will increase the merged firm's opportunities and incentives to discriminate against competitors in the downstream retail market. This will result in a general weakening of the competitors who remain to serve the business market and ultimately result in less innovation and investment if the merged firm's incentive to discriminate posed by this merger is not adequately addressed.

2. When the Justice Department looked at the SBC/AT&T merger, and the Verizon/MCI merger, they focused on loss of competition for high-capacity business customers, and to address that problem, they utilized an unusual remedy - - something known as an "indefeasible rights of use." Basically, this is like a long term lease that provides a certain amount of service to these businesses. How has this remedy been working? Do you think it has been effective at maintaining competition in these markets?

Response: This "remedy" has not been implemented yet, because it has not yet been determined by the judiciary to be likely to replace the competitive harm lost by the elimination of AT&T and MCI as independent competitors, and therefore in the public interest. The likely efficacy of this controversial remedy is at the heart of an inquiry

currently being conducted by the U.S. District Court for the District of Columbia pursuant to the Antitrust Procedures and Penalties Act ("Tunney Act"), as amended by Congress in 2004. However, according to COMPTEL, the leading association representing competitive carriers, this controversial remedy is unlikely to have any significant remedial effect for several reasons.

First, the merger Complaints acknowledge that competitive harm will be suffered on a geographic scope as large as an MSA, yet the remedy is entirely building specific. Second, the building-specific remedy is generally divorced from the commercial realities associated with the very high demand customers likely to be served by alternative facilities. In other words, customers have demand for telecommunications services, buildings do not. Thus, unless a customer has all of its demand contained within one of the buildings in question, the remedy will only have a coincident correlation to loss of customer choice. Finally, even if a significant portion of a customer's demand does reside in one of the buildings that are the subject of this "remedy," it is important to realize that the fiber leases do not provide any "service" at all as that term is commonly understood. The fiber for which leases are being offered is all "dark" (incapable of carrying traffic without being "lit" through the further investment in equipment by another carrier); the fiber only extends to a building's doorstep (a prospective competitor would have to undertake further expense to negotiate building access and to pull fiber through the building); and, additionally, it is significant to consider that, even with the proposed remedy in place, all customer demand contained in those buildings is presently being served by the merged firms. The "remedy" does not allow any customer out of its existing contract, and is comprised of entirely excess capacity.

The District of Columbia provides a useful example with which to evaluate the likely efficacy of this remedy. It covers 16 buildings in DC. Seven of these buildings are government locations that have multiple other locations, for which no laterals are being offered. For example, excess capacity to the IRS building at 1111 Constitution Avenue is being made available, but no other IRS locations that MCI had capacity to are being made available to competitive carriers. Another building in DC for which fiber laterals are being offered is the Verizon Center; it seems unlikely that another competitive carrier would be likely to lease this excess capacity to somehow become the phone service provider to the Verizon Center. Thus, it seems clear that even in the limited number of buildings for which excess capacity is being made available, it is unlikely that for a substantial number of these buildings, a competitive carrier could actually use this excess capacity to replace the competitive intensity lost by the elimination of AT&T and MCI as independent competitors.

Questions of Senator Herb Kohl

1. What do you believe will be the implications of the AT&T/BellSouth merger for special access rates?

Response: If approved, the proposed merger would have two major consequences for the special access market. First, merger would effectively eliminate the single largest special access competitor in the BellSouth region. AT&T's presence in the BellSouth markets currently serves as a check on special access pricing, and this check on competitive wholesale pricing will be eliminated if this merger is approved. Second, the expanded ILEC footprint of the merged firm will give the company an increased incentive after the merger to unfairly leverage its increased market power by discriminating against purchasers of special access that compete in downstream retail markets. This is because the merged firm will be able to capture a larger portion of the benefits it receives from such discrimination than it would absent the merger. For example, if BellSouth today discriminates against a competitor that offers competitive retail business service in Miami, Dallas, Houston and Los Angeles, BellSouth will only experience the benefits of a weaker competitor in the Miami market. After the merger, however, the merged firm would experience the benefits of a weaker competitor in Miami as well as Dallas, Houston and Los Angeles. The opportunity to capture a larger benefit from discrimination will increase the merged firm's incentive to engage in such discrimination in Miami.

2. As part of their approval of the SBC/AT&T merger, we recommended and both the Justice Department and the FCC approved a number of pro-competition merger conditions. These conditions included offering DSL internet connections to consumers without also requiring them to buy phone service, a requirement that AT&T to divest duplicative overlapping networks, and several others. Do you believe that similar merger conditions should be imposed as a condition of approval of the AT&T/BellSouth merger? Are there additional merger conditions you believe are warranted? If so, describe them and explain why you believe they are necessary.

Response: Yes, however, given the potential threat to competition posed by the instant merger far exceed those of the ABC/AT&T merger, the conditions must be correspondingly more comprehensive than the conditions placed on the SBC/AT&T merger. First, the DOJ should require that the AT&T network in BellSouth territories be divested. Second, the DOJ should require that all unused licensed spectrum that could be used to develop a wireless alternative to the wireline network be divested by AT&T and BellSouth. Third, to address the substantial increase in the merged firm's incentive to unfairly leverage its now increased market power, we have advocated a series of conditions we believe the FCC should also impose to thwart potential anti-competitive behaviors that could result. These conditions include a freeze on access current special access and UNE access rights as well as a cap on existing pricing for five years. The comprehensive list conditions we have proposed to the FCC is attached to this response.

Question of Senator Patrick Leahy

This Committee recently held a hearing on competition in the telecommunications market. You make two interesting observations in your statements – not only is competition currently lacking in the broadband access market, but the spectrum that is best suited for providing wireless competition to the incumbents is being held, but not used, by the incumbents.

The incumbent telephone companies appropriately argue that competition will lead to innovation and lower prices in the video services market. Competition, of course, would also lead to innovation and lower prices in the broadband access market. What policies should this Committee consider to encourage competition and the deployment of new wireless broadband access providers?

Response: The Committee should consider the following policies to encourage competition and the deployment of new wireless broadband providers. First, the merged firm should be required to divest unused wireless spectrum to free up these assets for use by companies to develop an alternative wireless network to compete with the existing wireline network. Second, the merged firm's existing legal duties to provide access to unbundled network elements and interconnection should frozen for an appropriate period of time (e.g., five years). Third, the merged firm should be prohibited from increasing its prices for special access and UNE services. Stability in the merged firm's legal duties and pricing of essential inputs will provide the preconditions necessary for competitors to provide innovative broadband products and applications to the business market, particularly in the small business market – the sector so critical to our nation's economic strength.

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The American
Antitrust Institute

July 24, 2006

Hon. Mike DeWine
Chairman, Antitrust, Competition Policy
and Consumer Rights Subcommittee
United States Senate
Committee on the Judiciary
Washington, D.C. 20510-6275

Re: Answers to follow-up questions for the hearing "The AT&T and BellSouth Merger: What Does It Mean for Consumers?" before the Subcommittee on Antitrust, Competition Policy and Consumer Rights

Questions of Senator Mike DeWine

Question 1.

For some businesses, AT&T and BellSouth are among the few—if not the only two—providers which offer the type of complex telecom services they need. Although, as the testimony for this hearing has shown, there appears to be some dispute about how many businesses will find themselves in this position. Due to this merger, many of these businesses will be losing a choice, and some may even be left with only one choice, which raises obvious competitive concerns. On the other hand, however, a combined company may be in a better position to invest in new services for business and corporate customers. How do the merged company's claims of an enhanced ability to invest in new services for business customers weigh against the potential loss of competition due to this merger, and how does this merger affect the marketplace?

Answer

The proposed AT&T-BellSouth merger touches a large and complex system of markets for telecommunications services. In addition, profound institutional, regulatory and technological changes are now taking place which also impact the competitive assessment of the proposed merger. On balance, it is more likely that competition between AT&T and BellSouth in each firm's respective service region would result in a greater level of aggregate investment and yield greater social benefits than a merger that eliminates any possibility of competition between the two firms. This is because new technologies undermine the need for common ownership of network infrastructure to achieve interoperability and provide next generation services. Claims that the merger is necessary to stimulate additional investment to achieve a greater level of

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service for customers are without merit, for the reasons set forth with more particularity in the answer to Question 3, below.

Question 2.

When the Justice Department looked at the SBC/AT&T merger, and the Verizon/MCI merger, they focused on loss of competition for high-capacity business customers, and to address that problem, they utilized an unusual remedy - - something known as an "indefeasible rights of use." Basically, this is like a long term lease that provides a certain amount of service to these businesses. How has this remedy been working? Do you think it has been effective at maintaining competition in these markets?

Answer

The contracts for the IRUs to be divested in connection with the SBC/AT&T and Verizon/MCI mergers remain executory, pending approval of the mergers by the district court, which is currently in the process of its Tunney Act review. Accordingly, it is as yet impossible to determine the efficacy of this type of remedy.

However, there is no reason to be optimistic that IRUs will fulfill the intended function of a divesture in this context. According to the *Antitrust Division Policy Guide to Merger Remedies*,[1] "divestiture assets must be substantial enough to enable the purchaser to maintain the premerger level of competition,...."[2] The most significant feature of the proposed IRU remedy is the divestiture of dark circuits without an associated revenue flow. The divestiture of un-used circuits on a building-by-building basis is unlikely to maintain premerger levels of competition for several reasons.

First, the existence of an independent operator of circuits in a particular location is unlikely to replace lost competition because the potential customer base for such circuits is already fully serviced. Well-known pricing and discounting strategies by incumbent LECs bind enterprise customers to minimum spend levels or capacity usage, creating a strong disincentive for such customers to switch to rival operators that may own capacity that serves a particular location.

Second, while a particular building may house enterprise customers with a single point-of-presence ("POP"), enterprise customers are more likely to require private line services to multiple POPs. Such customers do not bid on or purchase private line services on a building-by-building basis but instead negotiate for services for all of its POPs on a regional, national, or global basis.

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[1] U.S. Department of Justice, Antitrust Division, October 2004, available at: <http://www.usdoj.gov/atr/public/guidelines/205108.htm>.
[2] *Id.*, at 9-10.

Finally, there is a legitimate question with respect to the criteria applied by the Department of Justice in determining which buildings should be the subject of the IRU remedies. Putting aside the inadequacy of a building-by-building market definition where buyers do not buy and sellers do not sell on such a basis, the remedies proposed in both mergers are limited only to those buildings in which the number of providers is reduced through merger from two to one and where the probability of entry is determined to be low. Thus, the proposed remedies do not regard a reduction in competitors from three to two to involve a substantial lessening of competition. Moreover, the same conditions that indicate a low probability of competitive entry (*e.g.*, large enterprise tenants or isolated locations) are likely to render the IRU remedy ineffective, as well.

A divestiture of circuits currently in use together with the associated revenue flow (*i.e.*, customers) would be much more effective in replacing lost competition. No explanation for proposing IRUs rather than a more traditional remedy is given by the Department, however, other than the fear of the "disruption" that might follow from a more complete divestiture. Disruption of this type, however, is at best a pretext. Network operators routinely engage in "circuit grooming" which moves customers' circuits transparently and without service interruption.

Question 3.

In the past, critics have argued that the old Bell companies avoid competition by staying out of each other's territories. For the most part it is true that we have not seen very much "Bell against Bell" competition, which has been a source of frustration to many consumers and policy-makers as well. But we heard from all of the witnesses at this hearing that this merger will increase investment to integrate the various types of networks, and that we will soon see products being delivered to consumers over the internet, which should change the market dynamic and also the economics of providing those services. Do you think that a combined AT&T/BellSouth would be more likely to enter into Verizon's and Qwest's territories than it has so far?

Answer

The proposed AT&T/BellSouth merger will *decrease* rather than increase "investment to integrate various types of networks," a proposition the merging parties readily admit. For example, the parties explain that each of the three pre-merger firms (AT&T, BellSouth, and Cingular) "must design and build its own IMS [IP Multimedia Sub-system] network."[3] They explain that "capital is being spent on three systems instead of one."[4] In other words, the firms

[3] Description of Transaction, Public Interest Showing and Related Demonstrations, *Applications for Transfer of Control of Domestic Section 214 Authorizations, Applications for Transfers of Control of International Section 214 Applications, Applications for Transfer of Control of Station Licenses and Operating Authorizations* (filed March 31, 2006) WC Docket No. 06-74, at 13.

[4] *Id.*

without the merger must engage in a level of capital investment that will not be necessary after the proposed merger takes place.

This is a strange justification for the transaction, indeed. An "IMS network" is an IP-based architecture with a logical layer that allows for the convergence and interoperability of wireless and wireline and IP and legacy network infrastructure. It permits the end-user to initiate a session that signals the user's presence on a particular network to all other networks—no matter by whom operated—and to switch freely between them. The entire purpose of the development of the IMS architecture is to promote network interoperability and convergence and to allow smooth and invisible transitions between modalities and proprietary operations. Multiple IMS networks are designed to achieve a level of technological agnosticism that renders the common ownership of dissimilar network infrastructure entirely unnecessary for interoperability. To aver that the proposed merger will achieve efficiencies by requiring only one rather than three separate IMS networks to be built flatly ignores one of the principle advantages and purposes of the IMS architecture in the first place.

Moreover, competition necessarily implies a healthy degree of duplication, the elimination of which acts to the detriment rather than the benefit of the consumer. In the present context there is no reason to believe that IMS implementations adopted by three pre-merger entities will not be able to freely interoperate while at the same time there is no reason to believe that these implementations will be identical. Innovation—both the product and process varieties—results from rival implementations, a clear benefit that will be lost as a result of the proposed merger.

Similarly, the parties claim that the combined company will be a "more attractive partner for content providers."[5] There is little or no support for this statement. The loss of two additional bidders for content will tend to homogenize program offerings as a whole and should be expected to result in less investment in content variety and less locally or regionally responsive programming rather than more.

The failure of the incumbent local exchange carriers (LECs) to compete *inter se* is well known and is the subject of a private antitrust class-action pending in the Southern District of New York.[6] The allocation of territories among competitors is, of course, unlawful *per se* under the antitrust laws. In the case of the incumbent LECs, moreover, such coordination and forbearance from competition would be contrary to the clear policy behind the Telecommunications Act of 1996.

The Verizon/MCI and SBC/AT&T mergers followed closely by the proposed absorption of BellSouth by new-AT&T will create three geographically separate, vertically integrated incumbent local exchange carriers (LECs) (Verizon, Qwest, and the "new" AT&T), an industrial

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[5] *Id.* at 25.

[6] See Twombly v. Bell Atlantic Corp., 425 F.3d 99 (2nd Cir., 2005), *cert. granted* Bell Atlantic Corp. v. Twombly, 126 S.Ct. 2965, 74 U.S.L.W. 3713 (June 26, 2006).

structure that will eliminate any remnant of an incentive for these firms to engage in out-of-region competition by substantially increasing the ease and therefore the likelihood of collusion and continued market allocation, tacit or otherwise. The proposed AT&T/BellSouth merger will render inter-Bell competition less likely than would be the case were BellSouth to continue as an independent network operator.

Question 4.

You expressed concern that this merger takes the nation down a path to a duopoly in the telecom industry, and argue that it is a "giant step." Do you think that it will increase the likelihood of future telecom deals, and if so, why? What merger can we expect to see next?

Answer

The principal concern is the emergence of local cable-telco duopolies as the best-case scenario for mass-market internet access in most communities. This outcome is likely even in the absence of any further consolidation in the industry.

The AT&T/BellSouth transaction represents a "giant step" because it removes a significant potential competitive source of mass market internet access and it all but eliminates any hope of inter-Bell competition for the reasons given in the answer to the preceding question.

In addition, the BellSouth/AT&T transaction represents more than a substantial combination of service territories but also a significant cross-platform consolidation of wireless and wireline technologies. In the absence of the proposed merger, an independent BellSouth and an independently managed Cingular would have significantly greater incentives to invest in and market "stand-alone" wireless broadband access as a competitive alternative to digital subscriber line (DSL) services. By contrast, indications are that wireless assets controlled by the post-merger firm will be bundled with wireline services as "back-up" access or as an additional feature offered with wireline-based subscriptions, nullifying any competitive discipline that could be gained by the presence of wireless access modes in the future.[7]

In short, the AT&T/BellSouth transaction is poised to limit broadband access to one of two types of providers for any given community, the local LEC and the local cable operator. Moreover, for those communities without LEC- or cable-based service, the result is a monopoly provider. Of course, in communities without either, broadband access is simply unavailable.

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[7] See, *e.g.*, "BellSouth Introduces Wireless Broadband Product Enhancements," BellSouth News Release, Las Vegas, March 21, 2006, available at: <http://bellsouth.mediaroom.com/index.php?s =press_releases&item=2834> (announcing wireless broadband to permit BellSouth wireline business customers to "back up their existing wireline Internet service").

The parties' argue that a combined AT&T-BellSouth will serve to "check the incumbent cable provider's market power with respect to video programming,"[8] This "countervailing market power" justification is fallacious in general and here it is almost self-evident that a combined AT&T-BellSouth-Cingular program provider in a given locality offers less competitive discipline for an incumbent cable operator than would two or three competitors providing a greater number of alternatives. There is no sound economic justification for the establishment of a duopoly based on the perception that cable operators possess market power, or that only a unitary provider can effectively compete against them.

Question 5.

You mention in your testimony that recent legislative proposals would place broadband service under the exclusive jurisdiction of the FCC. This may have an impact on regulatory decision making, since the legal standards applied by the FTC and the FCC are different; for example, when the FTC evaluates a merger it looks to see if that merger "substantially lessens competition," whereas the FCC evaluates whether that merger is "in the public interest," which is a broader and less defined standard. What are the practical differences you have seen between the FTC and the FCC with respect to preserving competition in content industries, such as video and the Internet, and what differences would you expect to see in telecommunications?

Answer

In light of the on-going transition to a market-based regulatory paradigm, antitrust principles should play a more prominent role in media and telecommunications, not a lesser one. Accordingly, to the extent that conferring exclusive jurisdiction over competition policy in media and telecommunications on the FCC will result in the application of the FCC's "public interest" standard rather than the more competition-specific standards of the Clayton Act, such a change would be seriously ill-advised.

With respect to merger policy, many scholars believe that the present system of sharing responsibility for merger review between a competition authority (FTC or DOJ) and the FCC is dysfunctional.[9] If the present procedure for review cannot be improved significantly, placing the responsibility for merger oversight within the exclusive jurisdiction of a single agency would be one suitable solution.

Proposals that would create exclusive jurisdiction for competition policy in the media and telecommunications industries at the FCC with instructions to apply traditional antitrust standards raise a closer question. In order for such a proposal to make sense, the grant of

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[8]Description of Transaction, Public Interest Showing and Related Demonstrations, Federal Communications Commission, *Applications for Transfer of Control of Domestic Section 214 Authorizations, Applications for Transfers of Control of International Section 214 Applications, Applications for Transfer of Control of Station Licenses and Operating Authorizations*, WC Docket No. 06-74 (filed March 31, 2006), at 27.

[9] See, *e.g.*, Phil Weiser, "Rethinking Merger Remedies: Toward a Harmonization of Regulatory Oversight with Antitrust Merger Review," available at: <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=893072>.

jurisdiction must be accompanied by sufficient appropriations to allow the FCC to establish a competent staff of professional competition attorneys and economists. On the other hand, the FTC already has the competence to discharge such an antitrust function, and enjoys a greater degree of independence as a result of its cross-industrial responsibilities.

Questions of Senator Herb Kohl

Question 1.

Do you share the concerns expressed by critics of the AT&T/BellSouth merger that it will lead to unreasonably high special access rates?

Answer

By all indications, pricing in the special access market nationwide is already unreasonable. Unfortunately, the degree to which AT&T presently constrains BellSouth's special access pricing, a function of the extent to which AT&T offers competitive special access facilities in the BellSouth region, cannot be determined without the benefit of the additional data that has been requested by the FCC but is not yet available. In any event, it is unlikely that the pricing problem in the special access markets will subside without decisive regulatory action in the "pricing flexibility" proceeding presently pending at the FCC.[10] However, the prospect of such action appears unlikely.

Question 2.

As part of their approval of the SBC/AT&T merger, we recommended and both the Justice Department and the FCC approved a number of pro-competition merger conditions. These conditions included offering DSL internet connections to consumers without also requiring them to buy phone service, a requirement that AT&T to divest duplicative overlapping networks, and several others. Do you believe that similar merger conditions should be imposed as a condition of approval of the AT&T/BellSouth merger? Are there additional merger conditions you believe are warranted? If so, describe them and explain why you believe they are necessary.

Answer

While divestiture of overlapping assets may be in principle a sound approach to restoring competition lost through a merger, the implementation of such a remedy through the use of IRUs without also divesting the revenue flow associated with the divested circuits and in the narrow circumstances in which they were imposed in the SBC/AT&T merger is not likely to be effective, for the reasons given in the answer to Question 2 of Senator DeWine, above. With

[10] See Federal Communications Commission, *Special Access Rates for Price Cap Local Exchange Carriers,* WC Docket No. 05-25.

respect to the condition that the post-merger firm offer "naked DSL," the implementation of this condition by the new AT&T has made a mockery of the condition. The *San Francisco Chronicle* reports that AT&T is offering naked DSL at $44.99/month, compared to about $46 for a bundle that includes both DSL and local phone service, a savings to consumers of about $1/month.[11] As a result, these same conditions in connection with the AT&T/BellSouth merger are unlikely to be effective in improving the options facing end-users or remedying the loss of competition resulting from the transaction unless they are linked to some enforcement mechanism to ensure they are meaningfully implemented.

While it is always difficult for an outsider to comment with any real degree of certainty about such a large transaction without the benefit of the resources and information at the disposal of the reviewing competition and regulatory authorities, some general comments nonetheless may be offered.

Conditions designed to remedy the anticompetitive effects of the AT&T/BellSouth merger should be tailored to a particular theory of harm expected to occur in an appropriately defined market. This merger is likely at the least to affect markets in the BellSouth service region for a) mass market broadband access, b) private line services for enterprise customers, and c) any other market, such as long-distance voice services, in which the merging firms may compete directly against one another.

With respect to the mass market for broadband access, for the reasons set forth in the answer to Senator Leahy's Question, below, BellSouth should be required to divest its rights to owned or leased frequencies in the 2.5 Ghz band which are suitable for deployment of WiMAX-powered broadband access. Such a divestiture condition should involve a permanent "fee simple" transfer of rights to a qualified independent acquirer willing to commit to deploying WiMAX broadband access using the divested frequencies throughout the BellSouth service region.

While the parties play down the effect on competition in private line services in the BellSouth region because of only limited competition between AT&T and BellSouth in this segment, the lack of competition and the profits now being earned by incumbents in special access are notorious. The reason for this is primarily because the FCC permitted "pricing flexibility" without first insuring the presence of adequate competition. Special access represents a stubborn "bottleneck" which is held in place in part by pricing and discounting strategies by the incumbents which inhibit switching by customers to competitive carriers. "Price caps" of the type imposed in the AT&T/SBC and Verizon/MCI mergers are only a temporary measure that does not address the root cause of the problem.

Accordingly, traditional divestitures to restore competition lost through the merger (*i.e.*, divestitures that transfer not only circuits but also customers to the acquiring firm) should be

[11] See Ryan Kim, "AT&T offers broadband by itself, Unpublicized DSL service won't save subscribers much," San Francisco Chronicle, June 17, 2006, page C-1.

required in any region or municipality in which the merging parties both have a presence. Moreover, the incumbents should be prohibited from imposing minimum spend levels, quantity-forcing "first dollar" discounts, and other non-linear pricing strategies which exert a stranglehold on their existing customer base.

Question 3.

In your written testimony, you state that antitrust law is "inadequate" to address the issue of net neutrality. What do you mean by this statement? Would repealing the FTC telecommunications common carrier exception aid the ability of antitrust enforcement to address this issue?

Answer

The inadequacy referred to in the statement is the result of the manner in which courts have applied the antitrust laws to industries in transition to market-based models of regulation rather than from any failure of the antitrust laws, as such. Broadly speaking, the difficulty arises when courts fail to recognize that judicial precedent applicable to regulatory regimes that have been repudiated or dismantled cannot continue to be applied to deregulated industries without grotesque results. Entities formerly subject to rate of return regulation, for example, have successfully pressed courts to continue to apply outmoded doctrines as defenses to antitrust claims (such as the filed rate doctrine or common carrier exemptions) while simultaneously exercising freedoms that are gained from deregulation. This problem is particularly acute in the telecommunications and electricity sectors.

Even its most vociferous proponents recognize that net neutrality addresses a competition problem in the internet access market and that a sufficiently competitive market would obviate the need for a net neutrality regulation. The net neutrality issue, therefore, arises largely because the antitrust laws as presently applied have been as yet ineffective in promoting and maintaining adequately competitive telecommunications markets, a condition which extrapolates logically to the market for internet access.

Repeal of the FTC's common carrier exception would assist the courts in appropriately applying antitrust principles when confronted with claims arising in the context of industries formerly regulated as common carriers. Because of the pace in which common carrier regulation is being withdrawn from such industries, however, such an amendment should not be necessary as a technical matter. However, it would certainly place an obstacle in the path of defendants that persist on seeking shelter under such an exception despite the fact that they are operating in newly "competitive" markets.

With respect to the relative merits of FCC or FTC jurisdiction over competition enforcement in the telecommunications industry, please refer to the answer to Question 5 of Senator DeWine, above.

Question of Senator Patrick Leahy

This Committee recently held a hearing on competition in the telecommunications market. You make two interesting observations in your statements – not only is competition currently lacking in the broadband access market, but the spectrum that is best suited for providing wireless competition to the incumbents is being held, but not used, by the incumbents.

The incumbent telephone companies appropriately argue that competition will lead to innovation and lower prices in the video services market. Competition, of course, would also lead to innovation and lower prices in the broadband access market. What policies should this Committee consider to encourage competition and the deployment of new wireless broadband access providers?

Answer

The importance of the broadband access market to American consumers and business end-users cannot be overstated. Technical migration from legacy network platforms to internet protocol- (IP-) based platforms implies that in the near future IP connectivity will provide the underlying mode of access to all telecommunications and media services (with the exception, perhaps, of over-the-air digital broadcasting). As a direct result, IP-based connectivity will soon dwarf all other forms of access in practical importance and economic significance.

Toleration of a duopolistic structure in which local markets are served by at most two providers of broadband access—an incumbent telco and a cable provider—can only serve to hinder progress in broadband penetration in the U.S. and stultify a market that is central to the nation's productivity. Accordingly, policies that promote additional, independent broadband access providers are vital to national welfare and competitiveness.

As the question recognizes, wireless broadband provided by independent network operators (*i.e.*, services <u>not</u> offered as a bundle with wireline or cellular telephone service or even offered by a telco or cable duopolist as a stand-alone offering) represents one of the most promising avenues for alternative competitive broadband access. Unfortunately, BellSouth has been allowed to amass significant spectrum in their southeast region in the 2.5 Ghz frequency band, ideal for "WiMAX" powered wireless broadband access. The term WiMAX stands for "Worldwide Interoperability for Microwave Access," an IEEE 802.16 air interface standard providing broadband wireless technology that supports fixed, nomadic, portable, and mobile access. WiMAX can provide faster data rates than either DSL or cable modem technology.[12]

The control of this spectrum is unfortunate because it functions as a "blocking position" with respect to the build-out of a national-footprint WiMAX network by others, while at the same time the post-merger company will have little or no incentive to roll-out a WiMAX

[12] See www.wimaxforum.org for further technical information and resources devoted to WiMAX implementations.

platform because it is likely to cannibalize its other broadband services in which sunk investments have already been made.

Specifically, BellSouth owns or controls 28 out of 33 available 2.5 Ghz channels in Atlanta, Georgia, 24 of 33 channels in Jacksonville, Florida, 20 of 33 channels in Louisville, Kentucky, 26 of 33 channels in New Orleans, Louisiana, together with similar capacity in other cities in Florida, such as Orlando, Daytona Beach, Lakeland, and Miami, and in Georgia, such as Rome and Athens.[13]

To be sure, the roll out of a WiMAX broadband access service with a national footprint by a new entrant such as Clearwire would not be technically *impossible* in the absence of divestiture of BellSouth's 2.5 Ghz holdings. The WiMAX Forum standards body and manufacturers of WiMAX equipment may eventually establish standards and offer devices for other frequency bands, in which case a national footprint could be pieced together by, for example, building into devices multiband capability. But such an outcome is likely to require an enormous additional investment and involve a delay that could be as long as several years. These costs, however, dwarf any doubtful benefit of permitting the post-merger company to retain its 2.5 Ghz spectrum, which has remained largely unutilized by BellSouth until recently, despite the company having owned or controlled this spectrum for ten years or more.

Thank you for the opportunity to share my views with the Committee.

Respectfully submitted,

Jonathan Rubin
Senior Research Fellow
American Antitrust Institute

[13] See Clearwire Corporation Petition to Deny or, in the Alternative, to Condition Consent, Exhibit 1.02, Federal Communications Commission, *Applications for Transfer of Control of Domestic Section 214 Authorizations, Applications for Transfers of Control of International Section 214 Applications, Applications for Transfer of Control of Station Licenses and Operating Authorizations*, WC Docket No. 06-74, (filed June 5, 2006).

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July 21, 2006

United States Senate
Committee on the Judiciary
Subcommittee on Antitrust, Competition Policy and Consumer Rights
224 Dirksen Senate Office Building
Washington, D.C. 20510

ATTN: Mr. Aaron Calkins

Re: Response to Written Questions from Committee Members

Enclosed please find AT&T Inc.'s responses to the written questions submitted by committee members on or about June 30, 2006. A copy of these responses will also be sent electronically to the following email address: Aaron_Calkins@judiciary-rep.senate.gov.

Please let us know if the committee requires additional information.

Very truly yours,

Bruce R. Byrd

Enclosure

cc: Timothy P. McKone

Responses to Questions Posed by Senator DeWine:

Q1. For some businesses, AT&T and BellSouth are among the few—if not the only two—providers which offer the type of complex telecom services they need. Although, as the testimony for this hearing has shown, there appears to be some dispute about how many businesses will find themselves in this position. Due to this merger, many of these businesses will be losing a choice, and some may even be left with only one choice, which raises obvious competitive concerns. On the other hand, however, a combined company may be in a better position to invest in new services for business and corporate customers. How do the merged company's claims of an enhanced ability to invest in new services for business customers weigh against the potential loss of competition due to this merger, and how does this merger affect the marketplace?

A. AT&T and BellSouth undertake their merger in the face of a hotly competitive environment for business services. That is, the premise of the question – that there are only a few providers that offer complex telecom services to businesses – is not supported by the facts. In approving last year's merger of SBC and AT&T, the FCC concluded that the merger would not result in anticompetitive effects in the market for enterprise customers because "myriad providers are prepared to make competitive offers" to business customers and such customers are likely to take full advantage of the choices available to them.[1]

The same conclusions are compelled here. The competition between BellSouth and AT&T in BellSouth's region is no more significant than was the competition between pre-merger SBC and AT&T in SBC's region; in fact, BellSouth is even more limited as a competitor for large, national enterprises because of a strategic focus on customers located predominantly within its region and its lack of out-of-region assets. In the BellSouth region, no less than in the SBC region, a broad range of providers, both traditional and non-traditional, compete aggressively for enterprise customers. And in the BellSouth region, no less than in the SBC region, IP-based applications and services are revolutionizing the provision of services, lowering entry barriers and creating opportunities for a host of new competitors, including, but not limited to, cable and VoIP providers, which are emerging as stiff challengers to incumbent providers. Wireless carriers as well are capturing larger shares of the retail business segment. And, of course, in the BellSouth region business

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[1] *In re Applications of SBC Commc'ns Inc. & AT&T Corp.*, Memorandum Opinion and Order, WC Dkt. No. 05-65, FCC 05-183, ¶ 73 (Nov. 17, 2005) ("*SBC/AT&T Merger Order*"). *See also, SBC/AT&T Merger Order* at ¶64 ("[T]here are numerous categories of competitors providing services to enterprise customers. These include interexchange carriers, competitive LECs, cable companies, other incumbent LECs, systems integrators, and equipment vendors."), and ¶74 ("We find that systems integrators and the use of emerging technologies are likely to make this market more competitive, and that this trend is likely to continue in the future.").

customers take full advantage of the numerous choices available to them, making informed decisions based on expert advice in order to obtain the best service at the best price.

Perhaps most persuasive is that customers perceive that they have numerous alternatives and will benefit from the merger, as shown by the dozens of supportive statements from large and small businesses submitted as part of the record in the FCC proceeding.[2]

In short, the merger portends no tradeoff of lost competition in return for enhanced investment – as the question suggests. The market for enterprise customers is experiencing vibrant competition, and the combined company will be a robust, effective player in it.

Q2. Cingular Wireless is now jointly owned by AT&T and BellSouth, and as a result seems to operate somewhat independently of both parent companies; after merger, AT&T will have more direct control over Cingular operations, and we have heard concerns that the merger will increase the incentive to use wholesale rates to disadvantage rivals. How will the merger change the way Cingular is operated, and how do you respond to concerns raised about wholesale rates?

A. Cingular Wireless today is owned and controlled pursuant to a joint-venture agreement between two ILECs – AT&T and BellSouth, and after the merger it will be owned and controlled by a single ILEC – the combined AT&T and BellSouth. Thus, the merger will not cause any fundamental change in Cingular's parentage that would create the incentive to discriminate against rivals. No such discrimination has occurred to date and, with the vigorous competition in both wireline and wireless services that will remain, none should be expected as a result of the merger.

On the other hand, while the Cingular joint venture has been successful by every measure, the merger of AT&T and BellSouth will rationalize its management and enable Cingular to become an even more efficient and innovative competitor. Because of the rapidly changing and fiercely competitive environment in which Cingular operates, the challenges inherent in any joint venture have become increasingly more prominent in the management of Cingular. Among other things, the operating profiles

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2 In the merger proceeding pending at the FCC, AT&T and BellSouth submitted for the record over 140 signed statements from a wide range of retail business customers that provide real-life details about procurement methods, the numerous alternative providers they consider, and the intensity of competition. As the Federal Trade Commission and Department of Justice recognize, "[c]ustomers typically are the best source . . . of critical information" relevant in assessing likely competitive impacts of a proposed merger. U.S. Dep't of Justice and Fed. Trade Comm'n, *Commentary on the Horizontal Merger Guidelines* (Mar. 2006) at 9.

of Cingular's parents have diverged during the five years since its creation. AT&T is a national and international provider of a broad suite of communications services. By contrast, BellSouth has remained a regional wireline carrier. Thus, the merger will harmonize the strategic focus of the various entities and streamline decision-making.

Moreover, unified ownership and management will accelerate key technology and service decisions facing Cingular. In a structure involving three companies, decisions relating to technology choices, utilization of multiple networks and when and where to make certain essential investments become more difficult and, of even greater importance in a rapidly changing market, slower. By combining these businesses, the merger will align incentives and focus in a manner that facilitates a more efficient decision making and investment structure – and a quicker integration of the companies' network capabilities. The result will be a cohesive, efficient IP network over which Cingular will be able nimbly to respond to customer demand and offer unique services that could not be realized as well or as quickly, if at all, without the merger.

Finally, the merger will have no adverse impact on wholesale rates faced by other wireless carriers. ILECs have been vertically integrated with wireless service providers since those services were first offered. And, while AT&T, BellSouth and Verizon today participate in wireless joint ventures, these carriers initially had complete ownership of their wireless affiliates. Likewise, Sprint Nextel until very recently wholly owned both its wireless and ILEC operations. Despite this legacy of ILEC participation in the wireless business, the provision of wireless services is vigorously competitive. The success of Verizon, Cingular and Sprint Nextel outside the footprints served by their ILEC "parents," as well as the success of T-Mobile, Nextel (since acquired by Sprint), and AT&T Wireless (since acquired by Cingular), confirm that ILEC affiliation with wireless providers has no adverse impact on the pricing or availability of wholesale inputs. And, a variety of wholesale carriers that are not affiliated with wireless carriers will continue to offer competition to the ILECs.

Q3. In the past, critics have argued that the old Bell companies avoid competition by staying out of each other's territories. For the most part it is true that we have not seen very much "Bell against Bell" competition, which has been a source of frustration to many consumers and policy-makers as well. But we heard from all of the witnesses at this hearing that this merger will increase investment to integrate the various types of networks, and that we will soon see products being delivered to consumers over the internet, which should change the market dynamic and also the economics of providing those services. Do you think that a combined AT&T/BellSouth would be more likely to enter into Verizon's and Qwest's territories than it has so far?

A. In approving the merger of SBC and AT&T, the FCC flatly rejected claims that the merger would lead the Bell Operating Companies ("BOCs") to avoid head-to-head competition.[3] Of course, it was precisely because SBC sought to expand its capabilities to offer the full range of communications services to residential and business customers – big and small – throughout the country that it merged with AT&T. The companies' complementary assets and capabilities made each entity a more potent and efficient competitor than either could have been standing alone.

Likewise, AT&T's merger with BellSouth will enhance, not diminish, direct competition among the BOCs. The merger will permit integration of BellSouth's, Cingular's and AT&T's now separate IP-based networks into a single IP network capable of carrying local and long distance voice, data and wireless traffic. The merger will make it possible to offer "follow me" converged wireless/wireline services that will provide voice, data and video content to residential, business and government customers seamlessly across wireless and wireline telephones, personal computers, televisions and myriad other devices. The result will be a U.S.-based competitor with an integrated global network offering a comprehensive suite of services and able to compete with the BOCs and all others throughout the country.

Moreover, heightened competition between BOCs is not just a future proposition. Today, AT&T, Verizon Business, and Qwest compete vigorously for retail business customers throughout the U.S. Moreover, there is intense competition between Verizon Wireless and Cingular (each owned by BOCs) to provide mobile wireless services. In addition, prior to its merger with AT&T, SBC invested over $1 billion to compete in 30 MSAs outside of its 13-state local-service region.

Q4. When the Justice Department looked at the SBC/AT&T merger, and the Verizon/MCI merger, they focused on loss of competition for high-capacity business customers, and to address that problem, they utilized an unusual remedy - - something known as an "indefeasible rights of use." Basically, this is like a long term lease that provides a certain amount of service to these businesses. How has this remedy been working? Do you think it has been effective at maintaining competition in these markets?

A. Indefeasible rights of use ("IRUs") are an effective and not uncommon tool that can enhance competition. The DOJ has recognized that IRUs are commonly used in the telecommunications industry and often viewed as

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[3] *SBC/AT&T Merger Order* ¶ 79.

indistinguishable from ownership.[4] In fact, many metropolitan area networks operated by CLECs – including some of those operated by pre-merger AT&T – are constructed largely from IRU fiber rather than owned fiber.[5]

Responses to Questions Posed by Senator Kohl:

Q1. More than 99% of consumers who access the internet with a broadband connection today choose between their Bell phone company or their cable provider. So, many argue that the giant phone and cable companies have the capacity to become the gatekeepers for internet content. This has led to proposals to require net neutrality.

Your company argues that legislation to require non-discrimination by internet service providers is unnecessary because no phone company has ever blocked or degraded internet content. However, your public statements seem to indicate to the contrary. Last year, you told Business Week that you would seek to have internet sites who use your "pipes" "pay for the portion they're using."

(a) Does this statement show that AT&T is prepared to cut deals right now that will give preferential treatment to certain web sites and therefore this debate is not premature? Does AT&T in fact have any such deals in place right now, or plans to do so in the future?

(b) If your answer to part (a) is that AT&T presently has no such deals, then what would be wrong with enacting a net neutrality principle into law?

A. As an initial matter, the predicate of the question – that there is limited consumer choice for broadband services – is faulty. Even two years ago, 63% of all zip codes already had a choice of *more* than two broadband providers, and 81% had *at least* two.[6] Moreover, this static view misses the real picture of the "dynamic broadband market," because there is every reason to expect that intermodal competition will "become increasingly robust."[7] Indeed, the FCC has found that, in addition to cable and telcos, other broadband platforms have begun to proliferate: "Broadband Internet access services are rapidly being developed or provided over technologies *other* than wireline and cable, such as wireless and powerline."[8] These technologies include wireless broadband, including 3G, WiMax, and Wi-

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[4] *See* Plaintiff United States' Response to Public Comments, at 39, United States v. SBC Communications, Inc. et al., (D.D.C) (No. 1:05CV02102).

[5] *Id.* at 39-40.

[6] FCC High-Speed Servs. Report, at 4 and Table 12 (http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/ hspd1204.pdf).

[7] *Broadband 271 Forbearance Order*, 19 FCC Rcd 21496, ¶ 29 (2004).

[8] *FCC CALEA NPRM*, 19 FCC Rcd 15676, ¶ 37 n.82 (2004) (emphasis added).

Fi, which has moved from the chalkboard into consumers' homes;[9] broadband over electric powerlines;[10] and satellite broadband.[11] This rapidly expanding competition forces broadband providers to give all their customers the broadest possible access to the applications and content of their choosing. That is, telco and cable broadband providers would block, degrade or restrict access to Internet content at their own severe competitive peril.

Regarding the two specific questions:

(a) The advanced broadband networks that providers like AT&T are constructing today can enable a new realm of differentiated and value-added services that can benefit consumers and Internet providers alike. In general, Internet traffic is handled today in what is referred to as a "best efforts" fashion. For example, AT&T might provide a customer with a 6Mbps dedicated service over AT&T's facilities, over which the customer can access and download, among a countless array of choices, video clips from, CNN.com. But if CNN.com's equipment is able only to support downloads at 2Mbps, the customer will get no better than that speed from that site.

Over next-generation broadband networks arrangements can be made so that certain traffic or services enjoy assured quality or speed all the way from a content or service provider to the customer's home. An example would be an Internet-video company such as Movielink or Akimbo that, in addition to its standard movie-download service, seeks to sell a faster, premium service to end users and arrange for its video content to receive not just "best efforts" service but rather assured quality over a particular broadband network. The keys to such arrangements, however, are that the Internet company and the network provider would enter into them on a voluntary, arms-length basis, and customers would still otherwise enjoy robust best efforts service. That is, such arrangements would be an adjunct to, not a replacement for, today's Internet experience. Following the example from above, end users would be able to choose between

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[9] To take just a handful of examples, Google is rolling out Wi-Fi; Earthlink offers wireless broadband service in Anaheim and will soon begin providing it in Philadelphia and New Orleans; and municipalities, airports, coffee shops, and other entities offer more and more WiFi connections. *See, e.g.,* http://www.earthlink.net/wifi. One study predicts that, by 2009, "wireless broadband will be growing faster than wire-line[.]" *See* http://www.internetweek.com/ showArticle.jhtml?articleID=26100763.

[10] *See* Notice of Inquiry, *Inquiry Regarding Carrier Current Systems, Including Broadband Over Power Line Systems*, 18 FCC Rcd 8498, 8514 (2003), Separate Statement of Chairman Michael K. Powell ("Broadband over Power Line has the potential to provide consumers with a ubiquitous third broadband pipe to the home.").

[11] Satellite providers already serve several hundred thousand broadband customers. For example, Hughes Network Systems Inc. currently supplies its DirecWay high-speed service to nearly 200,000 customers. Chris Walsh, *Aiming Sky High; Companies Want to Launch Satellite Internet Market into Orbit*, ROCKY MOUNTAIN NEWS, July 26, 2004, at 1B. And new entrant WildBlue offers high-speed access to practically every location in the continental United States. *See* http://www.wildblue.com.

Akimbo's best-efforts Internet movie downloads as they do today (which, too, will travel at ever faster speeds and with greater reliability due to the massive investments that network providers like AT&T are making), or they could purchase premium, assured-quality delivery for an extra cost.

While such arrangements clearly will improve the end user Internet experience and offer Internet content and service providers a wealth of new opportunities to innovate, AT&T does not have any such arrangements with content providers today. AT&T is, however, willing to consider and enter into such commercial deals.

(b) There is no agreement regarding what net neutrality is; therefore, it is impossible to agree in advance that it would be appropriate to enact a net neutrality principle into law. AT&T supports net neutrality principles that refer to the concept of not blocking or degrading an end user's (i) access to the Internet content and services of her choosing, or (ii) ability to attach her chosen devices to, or run her chosen applications on, a broadband service. Indeed, AT&T has agreed to comply with such principles for at least two years as a condition of the SBC/AT&T merger, and has supported both House and Senate legislation that would codify these reasonable and measured concepts.

But, to the extent net neutrality refers to some of the unprecedented proposals advanced by Google, Yahoo!, and others, AT&T cannot support writing net neutrality into law. These zealots seek to apply common carrier regulation to the Internet that would require broadband network providers to treat and prioritize *all* Internet traffic identically, regardless of the type of traffic or the additional burdens a particular application might place on the network, *all at no additional charge to the content provider.* Under this principle, the Internet would devolve to one of two irrational and unsustainable models: (i) no specialized or premium services could be made available because all traffic would have to be treated alike – everything would move to the lowest common denominator; or (ii) broadband providers would have to completely alter the fundamental engineering of the Internet and build networks that are exponentially "fatter" than they are today, resulting in consumer broadband prices likewise increasing exponentially from today's affordable levels. The only winners would be the Internet behemoths like Google, Yahoo! and Amazon.com. Either they would face no competition from broadband providers and other content companies seeking to offer value-added premium services, or their own services would enjoy assured-quality, prioritized treatment over the Internet – at no extra cost.

AT&T cannot support this model. Indeed, such heavy-handed regulation would *suppress* broadband competition — and thereby harm consumers

— by depriving would-be broadband providers of any incentive to risk billions of dollars in the creation of new networks.

Q2. Critics of this merger argue that it will result in special access rates to connect to your networks to become unreasonably expensive. What is your response?

A. These concerns are unfounded. First, competition for special access services has existed since well before the 1996 Act – and is becoming ever more potent and widespread. For twenty years providers have been building out fiber transport and loop networks to serve these markets. Just by way of example: Since 1996, special access competitors have invested nearly $75 billion in new facilities and increased their fiber-route miles by 590%; the number of special access competitors has nearly doubled since 1999; and cable providers today have access to over 20 million businesses and are actively expanding their fiber-to-the-curb infrastructure. This competitive entry is real and irreversible, and is the reason that the FCC consistently has ruled that the free-market, not prescriptive rules, would best achieve the objectives of the Communications Act in this area. Indeed, this perspective on continual special access deregulation has been one of the few constants in FCC policies since the early 1990's, regardless of the political composition of the FCC.

Second, AT&T is not a material player in the special access market in BellSouth's territory, i.e., the merger will not remove a constraining competitor from this segment. AT&T has local fiber connections to only a few hundred of the more than 200,000 commercial buildings with special access level demand in BellSouth's 9-state territory. Other carriers with local facilities are equally or more significant competitors to BellSouth for special access services. After applying the competitive analysis used by the government in prior mergers to eliminate buildings for which there is plainly no competitive concern, *only 32 buildings remain in the entire BellSouth region*. All 32 are in the intensively competitive special access markets of Atlanta and Miami/Ft. Lauderdale. In each of those buildings, other providers could readily provide service. Thus, any competitive impact on potential wholesale special access competition would be *de minimus*.

Q3. You argue that a benefit from this merger will be to strengthen AT&T's plans to offer a video service to compete with cable TV. Essential to a competitive video product is obtaining "must have" programming that consumers expect from cable TV, such as local sports channels. Do you have any concerns regarding your ability to gain access to such programming, especially with respect to programming owned by the cable incumbents? Are there any deficiencies in program access law that should be changed to address this concern?

A. Federal legislation to update and sharpen existing program access laws is essential to ensure that new entrants have a fair opportunity to obtain programming on commercially negotiated terms. Consumers will benefit most when they can access the programs they desire via a multiplicity of distribution channels. While the FCC has significant authority to address many programming abuses and market distortions, Congress should reinforce that authority and amend the existing rules in several respects.

As the FCC and many others have recognized, local sports programming is often an essential component of any competitive video offering — one for which there are no readily available substitutes. Cox, for example, publicly touts its exclusive access to a local sports network that provides Padres baseball and other local sports programming in San Diego. Cable incumbents are increasingly exploiting the "terrestrial loophole" in the Act to restrict competitors' access to this valuable programming. Yet, because the FCC has questioned the scope of authority granted by Congress, the agency has refused to step in and address the "terrestrial loophole" in its enforcement of the statutory program access rules. Congress should clarify expeditiously that the mode of delivery does not affect the obligation to make programming available on fair terms. On the other hand, such legislative refinements should be targeted, and should not enact new forms of price or economic regulation. In short, if new entrants are to have a meaningful chance to compete, they should have a fair opportunity to assemble competitive programming packages.

Responses to Questions Posed by Senator Leahy

Q1. In response to my questions last week about whether AT&T's revised privacy policy would, in your view, permit AT&T to sell certain subscriber information, you responded "No, Sir, we would not do that." Is it the position of AT&T that it is not *permitted*, notwithstanding its privacy policy, to sell subscriber information or give it to the Government in the absence of a valid subpoena or court order?

A. AT&T's commitment to protect the privacy of its customers' information, the procedures and policies in place to do so, and it underlying obligations are unchanged. AT&T does not sell its customers' private account information to third parties. Moreover, we disclose information to government agencies only when their requests are lawfully authorized.

Q2. You stated that you do not believe any conditions are necessary on the AT&T-BellSouth transaction. When SBC and AT&T merged, however, you agreed to conditions, including a network neutrality commitment and a commitment to offer circuit-switched voice and DSL services on an unbundled basis. The AT&T-BellSouth merger would create the Nation's largest wireline company, and it would have control of the Nation's largest wireless company. What were the

factors that led to your voluntary agreement to conditions in the SBC-AT&T merger that do not, in your view, exist here?

A. The SBC/AT&T merger conditions were a function of the specific circumstances of that merger, and the hard-date for their expiration reflects a thoughtful conclusion that the remedies embodied in the conditions will be unnecessary after that date. The specific circumstances of this merger – and the clear competitive benefits that will flow from it – indicate that any conditions would be inappropriate. Beyond that, the SBC/AT&T merger conditions remain in place until late 2007. Thus, new conditions or remedies in the context of the AT&T/BellSouth combination are unnecessary.

Q3. Is there a point at which you would acknowledge a merger of the old AT&T Bell Operating Companies would substantially lessen competition or tend to create a monopoly? In your view, could AT&T merge with Qwest, Verizon or both without lessening competition?

A. It is impossible to evaluate the merits or competitive impacts of a hypothetical combination of AT&T with either Verizon or Qwest. The communications industry is undergoing such rapid and fundamental change – technological advances, the convergence of service and lines of business, growing intermodal competition – that the propriety of any merger can only be evaluated based on the particular circumstances of the deal and the market conditions existing at that time. Moreover, here, there are concrete, identifiable benefits that will flow from the combination of AT&T and BellSouth. If a merger of any of the BOCs were to be proposed in the future it should, like this one, be judged based on the state of competition and the merger's foreseeable benefits to consumers, employees and shareholders.

Q4. On the issue of network neutrality, you stated that AT&T will not block or impair Internet service. You also stated that billions of dollars are required for upgrading infrastructure, and someone has to pay for that. If AT&T ultimately decides to charge content providers for priority service over AT&T's network to its subscribers, would you agree to a requirement that such priority service be offered to all similar content providers on a nondiscriminatory basis? If not, why not?

A. While arguably innocuous in concept, a blanket non-discrimination requirement could lead for the first time to the imposition of an antiquated common carrier regime onto the Internet. Instead, premium or assured-quality content-delivery opportunities should result from voluntary arrangements between network providers and content providers negotiated at arms-length – similar to agreements reached in all sectors of American commerce countless times every day without government intervention or regulation and without the stifling presence of an artificial non-

discrimination principle. And, like other business arrangements, dealings between content providers and broadband providers would be subject to the full panoply of generally applicable antitrust, unfair competition and consumer protection laws. Finally, AT&T would have no incentive to unreasonably and arbitrarily discriminate against Internet service providers – and in the process limit its customer base. The point of making a multi-billion-dollar investment to deploy an advanced broadband network is to allow for greater broadband and Internet usage and activity by all users.

SUBMISSIONS FOR THE RECORD

TESTIMONY OF DUANE ACKERMAN
CHAIRMAN AND CHIEF EXECUTIVE OFFICER
BELLSOUTH CORPORATION

HEARING ON THE "*AT&T AND BELLSOUTH MERGER: WHAT DOES IT MEAN FOR CONSUMERS?*"

BEFORE THE UNITED STATES SENATE
COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON ANTITRUST, COMPETITION POLICY AND CONSUMER RIGHTS

June 22, 2006

Mr. Chairman and members of the Committee, it is a pleasure to have the opportunity to appear before this Committee today to discuss the benefits that the BellSouth-AT&T combination will provide to our customers, shareholders, employees and communities. As you know, BellSouth is a telecommunications provider of voice and data services, primarily in the nine states of Alabama, Georgia, Florida, Kentucky, Louisiana, Mississippi, North Carolina, South Carolina and Tennessee. In addition, BellSouth, together with AT&T, owns Cingular Wireless.

In 1984, at the time of the Bell System divestiture, the principal telecommunications technology was the narrowband, circuit-switched wireline voice network, which was used to offer local service and long distance service. Today, the distinction between local and long distance has effectively been eliminated, and the nation's voice, data and video needs are met by numerous competing wireless and wireline networks.

The rapid pace of change in communications services has resulted in the convergence of previously distinct technologies. For example, voice and video services are now delivered through the Internet Protocol to mobile customers who use wireless

devices to connect to the Internet. These technological advances have facilitated the entry of new and innovative communications companies resulting in a wide variety of choices for consumers and enterprise customers. Companies, both large and small, are making substantial investments in the infrastructure needed to deliver these advanced communication services to American consumers and businesses In sum, business and mass market customers alike want mobility, broadband, and converged services, and they have an increasing array of providers and plans to choose from.

The combination of AT&T and BellSouth, two well-respected companies with complementary strengths, will serve to accelerate the rapid pace of technological change, delivering to residential customers, and both large and small enterprises, new and better services at a lower cost. This will allow for closer integration of each company's wireless, wireline, video and IP products and services over a single global IP network, which is increasingly important as the industry moves forward with convergence of the "three screens" that many consumers rely on most today – televisions, computers and wireless devices.

And all of these benefits come without any loss of competition because AT&T and BellSouth are not actual competitors in the consumer market, and because AT&T is not a significant competitor of BellSouth's in the enterprise market in our nine-state region.

I would like to describe some of the most notable benefits this combination will provide, including:

- first, the simplification of Cingular's management structure that will provide for the faster delivery of improved wireless services to consumers and enterprise customers.

- second, the development of IPTV services that will -- at last -- provide consumers with an alternative to the entrenched cable companies.
- third, enhancing the security and reliability of the combined company's network, thus improving both the combined company's ability to respond to the government's evolving needs, as well as its ability to respond to natural disasters, acts of terrorism and other emergencies.
- fourth, the combination of BellSouth's regional assets with AT&T's national assets that will benefit enterprise customers in the Southeast; and
- fifth, the realization of more than $18 billion in synergies that will enable the combined company to offer better products at lower prices.

These are the very sorts of benefits that the FCC credited in approving the "vertical integration of the largely complementary networks and facilities," of SBC/AT&T.[1] And just as was the case with those mergers, this merger is likely to bring very important benefits to customers in the southeastern United States since it will enable BellSouth to offer the international world-class network facilities of AT&T together with our own extensive southeastern network on a seamless basis.

The first notable benefit is that the merger will streamline and enhance management and operations at Cingular, which is currently operated as a separate company with separate management and largely separate networks. Although Cingular has been successful, it faces increasing challenges due to its tripartite management structure. For example, AT&T, BellSouth and Cingular are at various stages in constructing IP-based networks to enable advanced capabilities. This merger will permit integration of those separate networks into a single IP network to carry local and long distance voice, data and wireless traffic, making it possible to offer "follow me" converged wireless/wireline services that will provide voice, data and video content to

[1] SBC/AT&T Merger Order ¶191.

residential, business and government customers seamlessly across wireless and wireline telephones, personal computers, televisions and myriad other devices.

As to the second benefit, consumers seeking a real alternative to entrenched incumbent cable operators should see faster and more economical deployment of next-generation interactive IP television networks as a result of this merger. Because of the substantial investment costs involved in providing such services solely in our nine-state region, BellSouth had deferred deciding on whether to attempt to provide such services on a broad commercial basis. AT&T, by contrast, has committed to providing a broad array of video programming and other services on an integrated IP platform and already has completed much of the work that will make such services possible. By combining BellSouth's southeastern fiber-rich network with AT&T's investments in IPTV technology and content, the combined company will have the national scale and the resources needed to deploy video services more quickly in the BellSouth region, and at a lower per-subscriber cost than BellSouth could have hoped to achieve on its own. The combined company's IPTV initiative will also spur broadband adoption, and increase the amount and diversity of programming available to the public.

As a third benefit, the merger will enhance the ability of the combined company to prepare for, and respond to, natural disasters, acts of terrorism and other emergencies. The merger will join AT&T's unique disaster recovery capabilities and assets developed to meet the needs of government and enterprise customers that demand extraordinary reliability and responsiveness for their networks with BellSouth's extensive experience in responding to hurricanes and other disasters. The merger will permit joint planning in advance of catastrophes, enabling faster deployment of personnel and equipment in

anticipation of predictable disasters, more rapid restoration of critical communications capabilities, and more effective coordination with the Commission's newly established Public Safety and Homeland Security Bureau, the National Communications System and other key government agencies.

As the White House recently observed in a comprehensive review of the federal response to Hurricane Katrina, disaster preparedness has become a national imperative. The merger will enable the combined company to respond more effectively to disasters that affect the communications infrastructure than could either company standing alone.

Fourth, customers in the southeastern United States and the rest of the country will benefit from the expertise and innovation of AT&T Labs, as well as the combination of AT&T's state-of-the-art national and international networks and advanced services with BellSouth's local exchange and broadband distribution platforms and expertise. The merger would also give business and government customers, including military and national security agencies, a reliable U.S.-based provider of integrated, secure, high-quality and competitively priced services to meet their needs anywhere in the world.

Fifth, the merger will allow for the recognition of synergies that we believe will have a net present value of $18 billion, after accounting for the costs of integration and other implementation costs. Those cost savings will allow a stronger network, enable more research and development, enhance service quality and lower costs for consumers, thereby making the combined company a more effective competitor.

While the merger will bring clear and specifically identifiable public interest benefits, it will not harm competition or consumers in any market. There is little competitive overlap between the two companies and, as the Commission concluded in the

SBC/AT&T Merger Order and subsequent market developments confirm, competition is well established in these markets. Indeed, the merger of AT&T and BellSouth involves no meaningful increase in horizontal concentration in any relevant market.

First, the merger will in no way reduce mass market competition for the same reasons that underlay the Commission's conclusion that the merger of AT&T and SBC would not adversely affect mass market competition. As an initial matter, before its merger with SBC, AT&T Corp. made a unilateral business decision to exit the legacy mass market business, a process that has continued since the merger. In the last three years, two-thirds of the legacy AT&T's mass market customers have found another provider. In the words of the FCC, AT&T "is no longer a significant provider (or potential provider) of local service, long distance service, or bundled local and long distance service."[2]

There is likewise limited horizontal overlap in the provision of enterprise services. In BellSouth's region, AT&T focuses mainly on serving the largest retail business customers, most of whom have significant operational requirements beyond BellSouth's nine-state region. For its part, BellSouth lacks a national network and other assets required to provide integrated nationwide service to this market segment. Moreover, as the Commission recently found in the *SBC/AT&T Merger Order*, the enterprise segment is populated by sophisticated customers and a wide and growing range of competitors that now includes national inter-exchange carriers, international carriers, CLECs, IP/data network providers, cable companies, VoIP providers, equipment vendors and systems

[2] SBC/AT&T Merger Order ¶¶81-107,

integrators.[3] There is no prospect that the merged company could dominate the fiercely competitive enterprise space.

Further, there is no basis for concern about reducing competition for wholesale access services in the BellSouth region. AT&T is a fringe supplier of wholesale access services in the BellSouth region. Its focus is almost entirely on serving retail commercial customers. In fact under the criteria accepted by the DOJ and the FCC in the last two transactions, the only local markets where there are as many as ten office buildings that raise any competitive issues are Atlanta and Miami/Ft. Lauderdale. And even in these two markets, there are only a handful of buildings that are not easily served by competitive carriers.

Finally, the merger is not likely to cause competitive harm in the Internet Backbone market. BellSouth is not a Tier 1 backbone competitor and its backbone assets are almost entirely in-region. Furthermore, as with the SBC/AT&T merger, the presence of numerous other Tier 1 providers, together with the ability of Internet service providers to switch backbone providers, dispel any competitive concerns.

In conclusion, we eagerly look forward to the day when we can join these two great companies together to provide better, more efficient and lower cost services to our customers and communities. Thank you for your attention.

[3] SBC/AT&T Merger Order ¶103.

UNITED STATES SENATOR • OHIO

Mike DeWine

FOR IMMEDIATE RELEASE
JUNE 22, 2006

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DEWINE HEARING STATEMENT [AS PREPARED]: THE AT&T AND BELLSOUTH MERGER: WHAT DOES IT MEAN FOR CONSUMERS?

Good afternoon, I want to welcome all of our panelists to today's hearing to examine the merger between AT&T and BellSouth. This merger is another in a series we have seen recently in the telecommunications market, and it is significant. This deal will create the largest telecom company in the US; in fact, with a market capitalization over $150 billion, the combined AT&T/Bell South would be one of the largest companies in the world. This merger will also bring under one roof the largest cell phone provider in the country.

Big, however, doesn't always mean bad, and as we evaluate this deal we must keep in mind how much the market has changed. In 1984, when the Bell monopoly was broken up, most of us only had land-line phones attached to the wall; cell phones and the internet were virtually unknown. Today that type of old-fashioned phone service is just one part of a larger patchwork of data and communications services. In recent years, the cable television companies have started to offer high-speed internet and telephone services, while the telephone companies are beginning to roll out video services. It is clear that soon, data of all types, whether it be internet traffic, phone calls, or television shows, will be delivered via the internet, by a wide range of different companies.

So, what does this merger mean for consumers?

In terms of traditional home-phone consumer service, probably not all that much – AT&T and BellSouth both provide that type of service in their own areas, but don't compete in each other's regions, so nothing in this market will change as a result of the deal.

However, the merger may have an impact on consumers in other ways. A combined AT&T-BellSouth will have a unique portfolio of assets, which raises questions of how it will use those assets. For example, once Cingular comes under the ownership of a single company, the way in which it is run may change. Some have expressed concerns that a Cingular under the ownership of a combined AT&T-BellSouth will have the ability and incentive to manipulate connection fees in a way that will unfairly harm competition. This is an issue we will explore today.

-more-

At the same time, the wireless market is beginning to show promise as a medium that can provide new competition in a range of consumer services. The development of the so-called "Wi-Max" service means that cellular companies will be able to provide an alternative to traditional phone and cable companies for video and internet offerings. However, there is some concern that this merger will consolidate so much wireless spectrum in the hands of AT&T that it may hinder the development of Wi-Max and diminish its potential as a competitive alternative.

This merger will also have competitive implications for the future of the internet. AT&T will become an even bigger presence in the so-called internet backbone market. As telecommunications companies get larger, they are looking for different ways to manage their parts of the network, to get it to function more efficiently. Their potential efforts to do so are part of the escalating tensions surrounding the debate about net neutrality, which the full Judiciary Committee began to examine in a hearing last week. I think we need to examine and really understand whether this merger will create incentives to lessen competition – in markets for content as well as the carriage of that content – over networks controlled by bigger, more powerful companies, such as the newly merged AT&T.

The deal will impact business customers as well. Businesses, for example, find that very few companies can currently offer services to fit their complex telecommunications needs, and in fact there are some businesses right now that can only be served by either AT&T or BellSouth. For them, this merger means they will go from a market with two options to a monopoly. This is a market sector that will require close scrutiny.

Today, we will hear from the CEOs of AT&T and BellSouth, as well as the CEO of Cbeyond, a smaller internet-based telecom company, and an independent analyst. I hope these witnesses can give us an accurate and useful picture of what the competitive landscape will look like after this proposed merger, and what it will look like in the next few years, specifically with regard to this section of the business market.

We are also, of course, interested in hearing about the potential competitive benefits of this deal. For example, expanding the customer base of AT&T may well allow it to roll-out its video service more quickly, and the greater size and scope of the company may enhance other competitive offerings as well. We look forward to examining these benefits with our witnesses today.

Finally, of course, we need to continue to investigate some of the broader telecommunications issues currently being assessed by industry and policy makers, some of which the full Judiciary Committee examined last week, and many of which are being addressed now in draft bills to re-write our telecom laws. Issues such as net neutrality, which I referred to previously, and regulations regarding common carrier and information services, may also be affected by this deal, and so we need to consider the possible ramifications of the AT&T/BellSouth merger in these areas as well.

So we have a range of important and interesting topics to cover today, and I look forward to hearing from our witnesses on all of them. At this point I'd like to turn to the ranking member of the Antitrust Subcommittee, Senator Kohl.

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Senate Judiciary Committee
Subcommittee on Antitrust, Competition Policy, and Consumer's Rights
June 22, 2006
"The AT&T and BellSouth Merger: What Does It Mean for Consumers?"
Written Testimony of James F. Geiger
Founder, President and CEO
Cbeyond Communications

I. Introduction

Chairman DeWine, Ranking Member Kohl and Members of the Committee, thank you for inviting me to testify today about the harms that consumers would likely experience if the proposed AT&T-BellSouth merger were allowed to take place.

I would like to begin by introducing you to my company, Cbeyond. I think it is important for you to understand who Cbeyond is to be able to understand why companies like mine—companies that focus on America's economic engine, its small business entrepreneurs—think this merger has the potential to quickly (and negatively) reshape the competitive landscape and dramatically reduce customer choice. But you are not going to hear just doom-and-gloom from me because I firmly believe that if this Subcommittee vigilantly uses its oversight of the Department of Justice to ensure that a thorough investigation takes place and that every case that can be brought under Section 7 is—in fact—brought, it is very possible to ensure that the potentially negative impacts of this merger never materialize.

II. About Cbeyond Communications

I am the President and CEO as well as founder of Cbeyond Communications. I have over 22 years of experience in the communications industry, and I serve on the Board of

Directors of COMPTEL, the national trade association representing competitive providers of communications services. Prior to founding Cbeyond, I was Senior Vice President and the Chief Marketing Officer for Intermedia Communications, a founding principle and CEO of FiberNet, a fiber-based metropolitan area network provider and began my telecommunications career with Frontier Communications where I held various sales and marketing management positions. Prior to Frontier, I was an accountant with Price Waterhouse.

Cbeyond was founded in late 1999 with the sole mission to deliver "big business" communications services to small business customers at prices they could afford and that we could deliver profitably. We define the market we serve as small businesses with 5 to 249 employees. Cbeyond correctly anticipated that this entrepreneurial class of customers, like large businesses, would embrace productivity-enhancing applications creating a need for more bandwidth. And we knew that they would seek a simple, integrated package of communications services from one provider with one bill and that it had to be affordable and easy to use.

We also knew that the technological, operational and financial infrastructures of the traditional telecom service providers and the early CLECs were built to solve a different problem (primarily the problem of providing reliable voice services) from a different era than was our focus. Cbeyond invested to create a new innovative network powered by Cisco, using advanced, next-generation IP technology and a software-based architecture that delivers converged voice and data applications over a single pipe-or as we say, "one pipe, one protocol, all services." By providing all services over a single, integrated IP-

based network, we've been able to meet the needs of the underserved small business market while at the same time dramatically reducing what it costs to develop, integrate, and provide our products and services. We pioneered this infrastructure with Cisco and they remain an important technology partner today.

Cbeyond began providing service during 2001 in Atlanta, which is also the location of our corporate headquarters. Since 2001, Cbeyond has opened additional markets in Dallas, Ft. Worth, Denver, Houston, Chicago and most recently in Los Angeles. We currently serve over 22,000 small business customer locations, all of this attained through organic growth. Our strategy is to achieve deep market share penetration in our geographic markets while at the same becoming more operationally efficient and more in tune with the local small business community as we expand our network scope and penetration within a city.

As a result, Cbeyond enjoys a 99% customer retention rate and is one of the nation's fastest-growing providers of broadband services-growing organically over 35% year over year. Moreover, successfully satisfying small business customers has translated into financial success as well. Less than eight months ago, Cbeyond completed its initial public offering ("IPO") raising over $70M with a share price of $12. Today, Cbeyond trades at around $20 per share, or just over $500 million in market capitalization.

III. The Merger Will Enhance AT&T's Ability to Raise Rivals' Costs

The most obvious effect of the merger will be to directly eliminate retail competition between AT&T and BellSouth for many segments of the wireline business market. However, the merger will also significantly increase BellSouth's and AT&T's incentive

and ability to use its expanded market power to discriminate against rivals that depend on BellSouth and AT&T for access to wholesale transmission facilities.

Most "intra-modal" competitors (firms like Cbeyond) and so-called "inter-modal" competitors (like wireless carriers) rely on access to wholesale transmission facilities to move telecommunications traffic between geographically dispersed nodes in their networks. These transmission facilities are provided to an overwhelming degree by the incumbent local exchange carrier (*e.g.*, BellSouth in Atlanta, and AT&T in Chicago or Dallas). As I discuss in more detail below, the Merger will foreclose competition in the wholesale transmission market, and—ultimately—severely undermine the potential for intra-modal and inter-modal competition within both the AT&T and the BellSouth incumbent local exchange carrier regions.

More specifically, this Merger will (1) directly eliminate AT&T as a competitive wholesale provider of local transmission services in the BellSouth territory; (2) increase the ability of the post-merger firm to prevent wholesale competition in the provision of local transmission facilities from the developing in the future; and (3) increase the incentive of the post-merger firm to harm competition while reducing competitors' and regulators' ability to stop the merged firm from harming competition and consumers.

a. The Merger Will Directly Eliminate AT&T As A Wholesale Competitor For Both Last Mile and Transport Facilities.

There can be no doubt that, within the nine state region where BellSouth is the incumbent local exchange carrier, BellSouth enjoys what can only be called an overwhelming level of control over the transmission facilities that are necessary to reach business end user

customers like Cbeyond's. This is demonstrated by our experience in recent years in attempting to find what is known in the industry as "alternative last mile" providers. An order issued by the FCC a few years ago, the Triennial Review Remand Order, had the effect of substantially increasing the prices for many of the transmission facilities that Cbeyond leases from the Bell companies like BellSouth. These are high-capacity data facilities known as T-1s, and we use them as inputs to simultaneously deliver both voice and data services to our customers.

After this FCC order, we began to seek out non-Bell providers of T-1 facilities that—we thought—might be able to provide us with more economical access to our customers. In the most densely populated cities we serve (Atlanta, Dallas, Houston and Denver), we were able to identify seven alternative access companies all of which provided connectivity using fiber optic cables. Of these seven, only five were potentially suitable partners for Cbeyond because the others did not offer data speeds designed for smaller businesses. When we compared Cbeyond's customer lists to the available service locations for the remaining five alternative last mile providers, we discovered that they could potentially provide replacement service for only 600 of our more than 25,000 T-1s (or 2.4%). Further, the companies providing these services tended to have unsophisticated order processing systems that made it difficult if not impossible to install customers with the speed they expected. In short, Cbeyond—despite a diligent search—was unable to find a viable alternative to Bell-company T-1s at a time when the pricing umbrella should have facilitated bringing new competitors into the market.

And Cbeyond is not alone in finding that there is really no such thing as an alternative provider of last mile transmission facilities for business customers. Sprint told the Commerce Committee last week about a similar experiences that it had in attempting to find alternative last mile transmission facilities. Sprint's Robert S. Foosaner explained to the Commerce Committee that there were no markets in the BellSouth region—none—where BellSouth's share of Sprint's total last-mile business was not approaching (or well beyond) 90%.

In light of this information, you may be tempted to assume that the situation can't get worse so the merger should be approved. But this is not the case. While it is certainly true that AT&T is not a competitive option for Cbeyond's last-mile needs because its last-mile facilities generally serve very large enterprise-level business customers, AT&T's presence in the market serves as a real check on what would otherwise be BellSouth's unfettered ability to set prices. The reason for this is quite simple: BellSouth is acutely aware that AT&T, as its most well-capitalized competitor for both last-mile and transport facilities, pays close attention to market opportunities, and will begin to deploy additional facilities if BellSouth raises its prices too high. Accordingly AT&T's mere presence in the market has, until now, served as a check on BellSouth pricing, a check that will be lost if this merger is completed. In short, it is critical that AT&T be preserved as an independent competitor to BellSouth.

The impact of the proposed merger is even more insidious in the market for transmission facilities connecting carrier locations because in this market AT&T is a viable competitor to BellSouth on a huge percentage of routes across the southeast. In fact, eliminating

AT&T's competitive influence on the pricing of these transmission facilities will eliminate what I would conservatively estimate to be 75% of the competitive transmission facilities that remain. This merger—should it be allowed to proceed—will take the only currently viable competitive telecommunications facility market in the BellSouth region and deliver it directly to the dominant provider: BellSouth. If this merger is complete, the final check on BellSouth's ability to price its competitors out of the market will be gone. The Antitrust Division should not allow this to happen.

b. The Merger Enhances the Ability of the Post-Merger Firm to Avoid Future Last-Mile Competition

For most of their existence, the Bell Companies have enjoyed an effective monopoly over last mile transmission facilities needed to reach end user customers, a monopoly that was built with legal protections and no risk because of rate regulation designed to let them get the network built. Since the 1996 Act made this public network much more accessible to competitors, the Bells have become quite adept at preventing the rise of alternative last mile networks by leveraging their pricing power over the current network. Such strategic conduct has been referred to as "reducing rivals' revenue."

The Bell Companies reduce their rivals' revenues by forcing companies like Cbeyond and Sprint-Nextel to purchase local transmission facilities pursuant to volume-term agreements that have the effect of "locking up" the market and preventing competitive providers of wholesale transmission from competing effectively. The net effect of these contracts is that the Cbeyond, Sprint-Nextel and other carriers commit to purchasing transmission services from the Bell Company that they would otherwise choose to purchase from competitors. The competitors accede to these commitment contracts in

order to get any discount at all on the extremely high "off the shelf" prices that the Bell Company charges for the transmission facilities in locations where the Bell Company has a monopoly over transmission facilities..

Another feature of these contracts is that customers must pay high penalties if they fail to meet their volume commitments. This means that even if other competitors could offer a better base rate for part of the customers' transmission facilities needs, customers would still be unable to use these services from competitors because the high penalty imposed by the incumbent when the customers could not meet their volume commitment are far greater than any savings recouped from using transmission facilities provided by Bell Company's competitor in the wholesale market. While customers do not like these contracts, they have little choice but to sign them.

The source of the Bell Company's market power in this area is easy to see: over the range of output covered by the contract (*i.e.*, commitments to buy circuits in multiple states/locations) only the Bell Company can supply all of any wholesale customer's demand. Thus, a merger that further expands the geographic territory in which one firm is dominant—like the AT&T-BellSouth Merger—further enhances the ability of the dominant firm to engage in behavior designed to prevent rivals from achieving the scale necessary to become viable competitors.

c. The Merger Increases the Post-Merger Firm's Incentive to Harm Competition While Reducing Competitors' and Regulators' Ability To Constrain this Conduct

The merger of AT&T's ILEC assets with the BellSouth ILEC assets will expand the size of the post-merger ILEC territory to 22 states. This expanded ILEC will be very difficult

to control. To begin with, the merged firm would have an increased incentive to harm competition. A simple comparison of BellSouth before and after the merger illustrates the point. Today, if BellSouth were to discriminate against Cbeyond in the provision of bottleneck facilities, BellSouth would face a weakened competitor in the one market in which Cbeyond competes with BellSouth -- Atlanta. However, the post-merger BOC would face a weakened competitor in Atlanta, *as well as Dallas, Ft. Worth, Houston, Chicago, and Los Angeles*. By adding the BellSouth region to the merged firm, BellSouth can appropriate a larger portion of the consequences of anticompetitive conduct than would be the case absent the merger. These greater "benefits" from discrimination in turn increase the merged firm's incentive to engage in such conduct in Atlanta.

In addition, by eliminating BellSouth as an independent BOC, the merger would eliminate a benchmark against which to judge the reasonableness of AT&T's conduct. Benchmarking one BOC against another is an important means of policing BOC conduct. We at Cbeyond use this technique whenever possible in interconnection negotiations and in other contexts when dealing with BellSouth and AT&T. In fact, given that neither we nor the regulators have as much information about the BOCs' costs or networks as the BOCs themselves, the ability to compare one BOC's conduct against another is indispensable for detecting unreasonable practices. Unfortunately, by eliminating BellSouth as an independent BOC, the merger would eliminate this mechanism. As a result, competitors and regulators would be left with virtually no ability to constrain the merged firm from acting on its now increased incentive to engage in anticompetitive behavior.

IV. The Merger Will Allow Anti-Competitive Warehousing of Wireless Spectrum

In addition to the threat posed by the proposed AT&T-BellSouth Merger to wireline services, the proposed merger also poses a serious threat to wireless services. This is because the post-merger firm will have a dominant share of a prime block of spectrum that could be used to provide broadband wireless service. The post-merger firm, if allowed to warehouse this spectrum, will do just that.

As Mark Del Bianco, a telecommunications lawyer, pointed out in a recent editorial,[1] BellSouth is the second-largest owner of 2.5GHz spectrum in the United States and controls spectrum in most of the 50 largest telecommunications markets. BellSouth also has substantial 2.3GHz spectrum that it acquired in auctions in 1997. These are precisely the spectrum ranges that are best-suited to the creation of a "wireless last mile" transmission via the emerging technology often referred to as Wi-Max. AT&T also has a large amount of 2.3GHz that it brought into its recent marriage to the former SBC, and it is important to note that—because of the exclusive nature of spectrum ownership—none of AT&T's 2.3GHz spectrum overlaps in any geographic location with any of BellSouth's 2.3GHz spectrum.

With all this spectrum you might think that either AT&T or BellSouth (or maybe both) would have deployed some wireless last mile transmission facilities. But this is not the case. Neither company has yet developed any of the spectrum into a commercial line of business, though BellSouth is "testing" a wireless broadband service in nine smaller markets and has announced plans to use the spectrum as a backup to its wireline services.

[1] Mark Del Bianco, Perspective: Bumps in the Road for AT&T-BellSouth Merger?, April 4, 2006, CNET News, http://news.com.com/Bumps+in+the+road+for+AT38T-BellSouth+merger/2010-1037_3-6057214.html.

In short, the spectrum is—for all intents and purposes—being warehoused.

So what will be the impact of the proposed merger on this situation? The answer to this question is—I think—obvious. BellSouth and AT&T will have no discernable incentive to use their spectrum to compete with wireline services they already provide, and their control of the spectrum will amount to nothing more than a way to stifle the competitors (such as Clearwire) that plan to create an alternative last mile to compete with the Bell monopoly over last mile transmission facilities. Moreover, these are competitors that could be using, and contributing to the growth of, non-Bell alternative transmission networks.

Assuming that AT&T's licenses are spread equally around the U.S. and that BellSouth's licenses are located primarily in the BellSouth service area (as appears to be the case), then the pre-merger situation looks like this: 40% of the BellSouth spectrum and 30+% of the AT&T spectrum is located in-region where the Bells have a huge incentive NOT to deploy. As for the other 60% of the spectrum the combined entity would control, the Bell company record of competing against their out-of-region brethren is nonexistent. They simply don't do it. In short, absent action by the DOJ, this merger is likely to result in the permanent warehousing of a valuable public asset that would otherwise be used to enhance consumer choice and bring innovation to our telecommunications infrastructure.

V. The Committee Must Apply Vigilant Oversight to the DOJ In Order to Avoid the Potential Anticompetitive Consequences of this Merger

The Antitrust Division seemed strangely unwilling to exercise its authority when conducting its last round of investigations of giant telecommunications mergers of the

kind the Committee is looking at here. In the case of the SBC-AT&T merger and the Verizon-MCI merger, the Division's "remedy" required nothing of the parties and did nothing to constrain prices. Astonishingly, it was left to the Federal Communications Commission to craft the only conditions placed on those mergers with any teeth. With the proposed AT&T-BellSouth merger, the Department of Justice is facing a much more dramatic consolidation of network power than occurred with last year's mega-mergers (a designation used then that seems quaint today). We are hopeful that the DOJ will take a harder look at this merger, and we ask that you demand this of them. Telecommunications competition in this country has made great strides over the last ten years, but all that has been gained could be lost if the former Bell monopoly is allowed to reform without effective oversight from the very agencies that the American public rely on to be their watchdogs in this area.

To conclude, the Committee asks, as the central question of this hearing, "what does this merger mean to consumers?" It is my fondest hope, as both an entrepreneur bringing innovative services to other entrepreneurs, and as an American citizen, that the message the Committee delivers loud and clear to AT&T and to the DOJ is that even our largest corporate citizens are subject to our time-tested anti-trust laws and the important public policies that support them. The best way to accomplish this is for the Committee to vigilantly use its oversight authority over the DOJ to ensure that a thorough investigation takes place, and every case that can be brought under Section 7 is, in fact, brought. Thank you for your time, Senators.

Statement
United States Senate Committee on the Judiciary
AT&T and BellSouth Merger: What Does it Mean for Consumers?
June 22, 2006

The Honorable Herbert Kohl
United States Senator , Wisconsin

STATEMENT OF SENATOR HERB KOHL
ANTITRUST SUBCOMMITTEE HEARING ON AT&T/BELLSOUTH MERGER

Thank you, Mr. Chairman. Today we return to a topic our Antitrust Subcommittee examined in detail a year ago – the continuing consolidation of the telecom industry. The $ 67 billion dollar merger between AT&T and Bell South we consider today follows closely on the heels of last year's massive AT&T/SBC and Verizon/MCI mergers. These mergers -- and the rapid pace of the technological changes in this industry -- are fundamentally reshaping how Americans communicate and what we pay for these services.

But while examining the impact of these deals on competition, we must also carefully consider what this consolidation means for our fundamental civil liberties and our national security. The antitrust laws were written out of a concern with the political effects of undue concentrations of economic power, not only their effects on consumers' pocketbooks. And the disturbing revelations of the last few months of the administration's domestic surveillance program demonstrate vividly that this deal -- and the overall telecom consolidation wave of which it is but a part -- may have a profound effect on our civil liberties. It has now been reported in the press that the NSA – allegedly with the cooperation of some of the nation's largest phone companies including AT&T – is compiling a massive database of whom nearly every American calls on the phone. While of course we all recognize that we need to listen to any calls Al Qaeda may try to make into the United States, we must do so in a focused manner, without trampling on the privacy rights of millions of innocent Americans.

We must realize that mergers and acquisitions in the telecom industry makes overbroad domestic surveillance considerably easier. As the market consolidates, government eavesdropping is possible merely with the assent of fewer and fewer large phone companies than before. Today, just a very few telecom giants have an enormous amount of personal information on virtually every American's phone calls. As the market concentrates, the threat to our privacy grows. These considerations should be paramount to all of us who have the responsibility to review these mergers.

We also of course must carefully examine the more traditional antitrust issues raised by the AT&T/Bell South deal. Both companies defend this merger by pointing out that this is a merger of regional phone companies with adjacent territories rather than of direct competitors. Further, they argue, technological changes and innovation are bringing new forms of competition to the market.

But, as we watch as a formerly regional player grows into the dominant phone company in nearly half the nation, we must be careful to examine several key questions. Will competitors to be able to interconnect into the millions of consumers served by the AT&T network? Will the new AT&T have the ability to charge exorbitant rates for "special access" lines into its network? Will the combined company gain too high a share of wireless spectrum needed for new competitive alternatives? More fundamentally, how can we ensure that this consolidation will not decrease the choices and increase the costs to consumers and to business customers, both large and small?

Just as with the ATT/SBC and Verizon/MCI mergers, we expect that the Justice Department and FCC will scrutinize these mergers very carefully to preserve competition. A good place to start would be the imposition of the same conditions these agencies imposed on last year's deals on this one. And we must be especially careful to ensure that the combined company's broadband internet services do not interfere with consumer's ability to access the internet content they wish. Securing merger conditions such as these will help ensure that the tremendous gains in telecom competition over the last twenty years are not lost in the midst of this industry consolidation. Thank you, Mr. Chairman.

Statement
United States Senate Committee on the Judiciary
AT&T and BellSouth Merger: What Does it Mean for Consumers?
June 22, 2006

The Honorable Patrick Leahy
United States Senator , Vermont

Statement Of Senator Patrick Leahy,

Ranking Member, Judiciary Committee

Hearing On

"AT&T and BellSouth Merger:

What Does it Mean for Consumers?"

June 22, 2006

I thank Chairman DeWine and Ranking Member Kohl for holding this timely hearing. I was one of five Senators to vote against the 1996 Telecom Act because of concerns about the consequences of that bill. Back then, I argued that the promise of competition between the long distance and local telephone companies would prove to be a myth. I argued in that the Act would allow the local regional bells to reunite easily with unregulated local monopoly powers.

Over the last decade, we have seen massive consolidation in the industry, and here we are again: Just six months ago, two of the biggest local phone companies acquired two of the biggest long distance companies. Where will it end?

When the AT&T monopoly was broken up, it was divided into 7 Bell Operating Companies. After this merger, there would be 3. And the proposed merger we are examining today would establish AT&T as the dominant carrier in 22 states.

It makes me question whether this merger will spur on other consolidations. As soon as AT&T and BellSouth announced the merger, one analyst said that: "Clearly, Verizon has to go after Quest now. Verizon will have to keep AT&T from getting it."

Where will it end?

Six years ago, I introduced a bill to limit mergers among what were then called the RBOCs – the Regional Bell Operating Companies. I recalled that at my farm in Middlesex and at my house here, I have only one choice for local telephone service. I know one thing for sure -- this unending wave of mergers is not helping rural America get better phone service.

When I introduced this bill I was concerned that the concentration of ownership in the telecommunications industry was proceeding faster than the growth of competition. Old monopolies were simply regrouping and getting bigger and bigger.

It was true then and it's true now -- telephone companies should not be able to gain concentrated control over huge percentages of the telephone access lines of this country through mergers, but rather through robust competition.

As President Reagan used to say, "Well, here you go again."

If Congress – and this Committee in particular – does not act to protect competition, consumers will be the ones who suffer by having no choices.

Where will a consumer, enraged that her phone company has given the government records of her phone calls, turn for an alternative?

I am very concerned about the new AT&T policy reported today, in which AT&T asserts that private customer records are AT&T property, which could allow AT&T to divulge that information to the highest bidder or just give it to the Government. I have not seen the actual text of the new policy, but I will be raising questions today on this matter.

In the video services market, the telecos argue that competition is necessary for innovation and lowering prices for consumers. When it comes to broadband and voice services, apparently they do not feel as strongly about the need to compete.

This merger, of course, is about more than just two of the biggest remaining wireline communications companies becoming one behemoth.

The merger would also put Cingular, the Nation's largest wireless provider, in the hands of the largest wireline company. So much for competition between wireless and wireline companies. Where will it end?

Cingular is currently operating independently of AT&T and BellSouth. It was a promising competitor for voice services and was also a potential player in the broadband access market. Following this proposed merger, it would merely be part of the largest phone and broadband provider.

When SBC and AT&T merged, AT&T agreed to a number of important, but temporary conditions, including offering voice and Internet services unbundled and providing open access to the Internet.

These conditions and commitments only remain in effect for another 18 months. What happens then?

AT&T has made clear its intentions. Mr. Whitacre has infamously said that he's going to charge online businesses, discriminating among services.

This Committee must be vigilant to protect the Internet from anticompetitive behavior.

The Internet has opened windows on the world in one-room schoolhouses in Vermont, and the Internet has opened new doors of knowledge and opportunity to children from Africa to Indonesia. It is the ultimate marketplace of ideas, where a better idea, a better service or a better application can succeed on its merits. The Internet must remain free and open.

I am pleased that the CEOs of AT&T and BellSouth are here today to answer our questions and explain how the merger of their two companies will benefit the public.

We had expected to hold a hearing with executives from AT&T, BellSouth and other companies earlier this month regarding their companies' involvement in the domestic surveillance activities conducted by the NSA without court approval.

I hope we still have that hearing. I will ask some questions on those issues today. I had my staff warn both companies that I intended to ask such questions. This Committee, this Congress and the American people have a right to know if their Government is brazenly ignoring laws passed by Congress, and consumers deserve to know how companies are using their information.

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The American
Antitrust Institute

Testimony of Jonathan L. Rubin
Senior Research Fellow
American Antitrust Institute
On
"AT&T and BellSouth Merger:
What Does it Mean for Consumers?"
Before the
U.S. Senate Committee on the Judiciary
Subcommittee on Antitrust, Competition Policy, and Consumer Rights
June 22, 2006

Good afternoon, Chairman DeWine, Ranking Member Kohl, and members of the Committee:

1. Thank you for the opportunity to comment on behalf of the American Antitrust Institute (AAI) on the proposed and historic AT&T/BellSouth merger. I am Jonathan Rubin, Senior Research Fellow at the American Antitrust Institute.

2. The AAI is an educational, non-profit, research and advocacy organization devoted to the promotion of competitive markets through vigorous enforcement of the antitrust laws in the U.S. and around the world. We are generally centrist, pro-competition, and pro-consumer in orientation, and operate with the assistance of an advisory board composed of many of the leaders of the antitrust community, including academicians and practitioners in the fields of law, economics, and business. The AAI's advisory board does not vote, however, so the AAI's positions should not be attributed to any individual advisory board member. Further information may be found at www.antitrustinstitute.org, which also contains a wealth of resources related to antitrust law and policy.

I. Introduction

3. The initial legal issue in evaluating the lawfulness of a merger or acquisition under Section 7 of the Clayton Act is whether the effect of the acquisition "may be substantially to lessen competition, or tend to create a monopoly." In pre-clearing a merger for compliance with this standard, one ordinarily begins with the current state of the market and then tries to predict, given current conditions, whether the merger as proposed is likely to harm competition. In most cases, the clearing agency and the merging parties engage in negotiations over a remedy designed to eliminate, or at least substantially attenuate, any foreseen or alleged competitive harm.

4. Currently, the merging parties compete in some markets, and where they do, it is irrefutable that this merger will directly suppress such preexisting competition. For example, in the previous round of mergers between SBC and the old-AT&T and Verizon and MCI, the Department of Justice imposed protective conditions intended to prevent the joinder of competitive operations in the retail market for "special access," which serves high capacity business customers. Similarly, to the extent there is preexisting competition for long-distance customers, a remedy may also be required.

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5. However, of over-arching concern to consumers should be that the proposed AT&T/BellSouth transaction takes us one giant step farther in the process of converting the national industry to one dominated by duopolies of multi-platform operators of legacy, broadband, and wireless networks. This prospect threatens to stifle consumer choice and create conditions that inhibit customer switching and deter competitive entry by rivals. Of particular concern in this regard is the local broadband access market.

6. To mitigate the broadband duopoly scenario, some parties have asked the FCC to impose conditions on this transaction that would free-up vital un-used wireless spectrum owned or controlled by BellSouth. This spectrum is particularly well suited to provide wireless broadband access using the WiMax standard. A prohibition on telco or cable cross-ownership of WiMax-platform deployment would ease the barrier to entry faced by new unaffiliated providers of WiMax services and promote the deployment of a third competitive alternative to the telco-cable duopoly.

7. This merger is also occurring in the midst of profound institutional, regulatory and technological changes now taking place. Such changes must be factored into the competitive assessment of the transaction.

II. Broader Issues of Institutional, Legal, and Regulatory Policy Are Implicated

8. On the legal front, numerous statutory and regulatory policy changes have been adopted or are being contemplated that will affect the regime under which the industry will operate. For example, by reclassifying internet communications as non-common carrier services, the FCC moved broadband access services to the jurisdiction of the Federal Trade Commission, which is statutorily prohibited from exercising jurisdiction over common carriers. A bill passed by the House last week, however, appears to be designed to counter this consequence of the FCC's reclassification by placing broadband access services under the exclusive jurisdiction of the FCC. At any rate, such institutional reforms are likely to have a dramatic impact on the competitive effects one can expect from any given transaction.

9. Another area of legal upheaval is manifest by the network neutrality debate, which expressly focuses on the duopoly problem in mass-market broadband access. Many experts, including proponents of network neutrality, recognize that in the presence of sufficient competition and consumer choice a network neutrality rule would not be necessary. Consumers would simply vote with their feet and drop the access providers that violate neutrality.

10. The premise of network neutrality, therefore, is that existing mechanisms of domestic competition policy—antitrust law enforcement and merger review—are inadequate as currently applied to ensure competitive internet-related telecommunications markets.

11. Indeed, antitrust as an effective competition policy instrument in telecommunications has been undermined by the 2004 Supreme Court opinion in *Verizon v. Trinko*. I have heard it said that *Trinko* means that "A network's refusal to interconnect is never an antitrust violation." A contrary view, which in my view is based on just as plausible an interpretation of the case, limits any narrowing of Section 2 doctrine to the particular facts and regulatory regime at issue before the *Trinko* Court.

12. Whatever the status of the dual jurisdiction apparently contemplated by the 1996 Act, the progressive deregulation of the industry and the statutory prohibition against "unfair methods of competition" implies explicit application of the antitrust laws, by whatever agency is assigned the task. Legislative proposals that place competition enforcement responsibilities with the FCC must also provide the agency with clear procedural and substantive standards, explicit instructions to follow antitrust common law in adjudications under those standards, and allocate sufficient resources and personnel to the agency so they may competently perform the requisite competition policy analysis, investigation, and enforcement.

III. The Technological Flux Is Migration and Convergence

13. In addition to these institutional and legal changes, a technological flux is re-writing network operators' business models. The flux consists of a migration-convergence process from legacy networks to internet protocol- (IP-) based next-generation-networks (NGNs). Both kinds of changes dramatically influence the economics of the market and thus the competitive impact of the proposed merger.

14. The overlap between institutional and technological change is not coincidental. The IP-based packet-switched services that provide the infrastructure for NGNs are now classified as non-common carrier. *Migration*, therefore, refers not just to the technological shift from circuit-switched to packet-switched network technology, but also to the redeployment of infrastructure from common carrier use to non-common carrier use. For the purposes of AT&T's fiber project, in other words, the conduits and rights-of-way for physical access to buildings that it will acquire with BellSouth are far more valuable than the twisted pairs of wire that now serve as the network infrastructure.

15. The other motion in the technological flux is *convergence*, which also serves double duty by referring both to wireline-and-wireless convergence and to the convergence of the industry on an open industrial standard, IP Multimedia Subsystem, or IMS.

16. IMS provides a unified architecture that supports a range of IP-based services across both packet-switched and circuit-switched networks. IMS promises to provide end users with a network of network resources operated by many different companies and across which users will be able to move with ease. IMS is designed to enable such network features as subscriber "follow-me presence and availability," "push-to" services (to-talk, to-view, to-video), multi-media calls, people-to-content, people-to-people, and people-to-groups.

17. By using technology developed in the cellular telephone sector, session-initiated protocol, or SIP, the network operator is able to geo-locate and track subscribers, monitor and react to their network usage, and push-and-price customized services, such as application-specific quality-of-service. End-users will be able to initiate multiple sessions at once, enabling multi-media or the transfer of on-going sessions from one device to another. IMS and its features work independently of access modality (fiber, wireline, wireless, cable, WiFi, etc.).

18. The SIP function and other network management tools involving deep-packet inspection allow network operators to obtain much more information about how their networks will be used than is presently available. This level of subscriber awareness enables transaction-level billing

and permits the network operator to micro-market and price-discriminate among its subscribers.

19. NGNs are likely to change the way we interact with the network and the way the networks interact with one another. By vesting greater control over the access mode in the hands of subscribers, value moves from the core of the network to its edges. One way to increase the chances that your network will be providing the necessary access to the subscriber is to acquire more territory, as this merger may be demonstrating.

20. Network interoperability, or "inter-working," is a central feature of IMS. Common ownership, therefore, is no longer necessary for efficient technical compatibility. Indeed, differentiated ownership may even benefit consumers by creating an audit trail and thus increasing the potential for greater transparency in the prices paid for network services as the subscriber moves across multiple access providers.

IV. Three Specific Threats to Competition

21. There are three ways in which the likelihood of substantial merger-specific harm to competition may be high. They occur in: the consumer market for broadband access, the "special access" markets in BellSouth's region, and the markets for video content, particularly high-definition programming, and telecommunications equipment.

A. Consumer Market for Broadband Access

22. As Vint Cerf testified recently, incumbent cable and telephone companies provide 99.5% of all consumer broadband access lines. However, a duopoly presently exists for only 53% of consumers. Another 28% of consumers were served by a monopolist and the remaining 19% had no broadband access at all. Thus, nearly half of all consumers are consigned to monopoly conditions or the absence of any broadband offering at all.

23. As discussed above (¶ 9), the need for a network neutrality provision is premised on a lack of sufficient competition in the consumer market for broadband access. Moreover, even in the best case of a cable-DSL duopoly, it may be costly for the consumer to switch. Switching-deterring strategies are anticompetitive because they interfere with the competitive process and deny the consumer the full benefits of competition.

24. At least one party has petitioned the FCC to deny AT&T/BellSouth's joint application for transfer of control on the specific grounds that it would not be in the public interest because it would inhibit network neutrality by concentrating control over too much of the national market for consumer broadband access. More generally, several consumer groups and parties are asking the FCC to require that BellSouth divest itself of the 2.5 GHz spectrum it owns or controls on the basis of the Commission's inter-modal competition policy alone.

25. WiMax technology allows rivals to economically enter as a third supplier of broadband access, either by itself or in conjunction with a super-local WiFi systems or LANs. Standards bodies are about to certify WiMax equipment for deployment on licensed 2.5 GHz spectrum. AT&T should not be permitted to own or control this alternative mode of broadband access.

26. Divestiture of specific spectrum would be an effective, one-off, clean remedy with a targeted and tangible effect on the market.

B. In-Region Special Access

27. In the recent mergers of Verizon/MCI and SBC/old-AT&T, the Department of Justice found a likely violation of Section 7 in the special access markets for high-capacity business lines. The unusual remedy employed there, the use of "indefeasible rights of use," (IRUs), was designed to separate the access lines from the customers using them. As a result, the IRUs may constitute a less than appealing opportunity for an outside competitor, and the remedy may not be restoring pre-merger competition as intended.

28. There is likely to be a temptation in the present case to apply a similar remedy where overlaps and merger to monopoly occur in the special access markets in the BellSouth region. This temptation should be resisted until there is satisfactory evidence that such a remedy actually restores pre-merger competition.

29. In the special access markets, one would expect to see a first-and-only mover advantage if commercial landlords do not want alternative facilities-based carriers on the premises. In any event, the appropriate policy for this segment of the market may be to return to common carrier regulation. A regulatory proposal pending before the FCC is moving slowly.

C. Buyer Power in Media and Equipment Markets

30. Finally, the loss of a new entrant into the multi-channel video program delivery business, (*i.e.*, BellSouth), may not be competitively neutral in adjacent product or service markets. One such market is the wholesale market for video entertainment content, particularly high-definition programming. Similarly, the merger removes a purchaser from the telecommunications equipment markets.

31. Losing BellSouth as a bidder and consolidating it with AT&T risks creating substantial buyer power in the hands of AT&T. It is worth asking whether any benefits of the merger outweigh the pro-competitive benefits of having both BellSouth and AT&T as separate concerns bidding against one another for programming and equipment in competitively supplied markets.

V. Conclusion

32. The proposed AT&T/BellSouth merger is not an ordinary merger. It is taking place at what seems to be the end of an extraordinary string of consolidations and it is occurring at a time of enormous change in the legal framework and technology in the sector.

33. Nonetheless, the same perceived lack of competition in the consumer broadband access market that animates proponents of network neutrality counsels caution against permitting the accretion of too much market power in that market. It would be anti-competitive for the post-merger AT&T, for example, to be permitted to be able to block through rights to licensed spectrum the roll-out of an independently-owned, competing broadband access platform.

34. Given how far the consolidation of this industry has already been allowed to go, it is likely that the best outcome that consumers can hope for would be the divestiture of BellSouth's 2.5 GHz spectrum followed by the entry of an independent provider of WiMax-powered consumer broadband access.

I thank the Committee for this opportunity, and I ask that my written remarks be made part of the record. I am happy to answer any questions you may have.

STATEMENT OF EDWARD E. WHITACRE, JR.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER
AT&T INC.

UNITED STATES SENATE
COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON ANTITRUST, COMPETITION POLICY
AND CONSUMER RIGHTS

June 22, 2006

Good afternoon. Thank you, Chairman DeWine, Senator Kohl, and other members of the Committee for the invitation to talk with you about our merger with BellSouth.

We firmly believe this merger is not only the right thing for our customers, our employees, and our stockholders, but we also believe it is the best thing for the future of telecommunications in our country.

I am pleased to explain why we believe so strongly in that.

First, the merger will bring together three world-class, but separate networks – AT&T's, BellSouth's and Cingular's.

The combined company will be better able to speed the convergence of these networks into a single, fully integrated network, and embrace the industry's shift to Internet Protocol or IP-based technologies.

We are just now scratching the surface of the potential this converged network offers consumers.

For example, customers will no longer be stuck using multiple devices for their different wireline and wireless networks. Instead, these services will eventually blend seamlessly over an advanced, integrated network.

This kind of innovation could not be done as quickly, effectively or affordably if all three networks remained separate.

Plus, once integrated, these networks will be even more robust, better able to withstand, and respond to and recover from disasters. AT&T's unique disaster recovery capabilities were developed to meet the needs of government and enterprise customers. Those customers demand extraordinary reliability and responsiveness for their networks. Combining that with BellSouth's experience in responding to hurricanes and other disasters makes for an even stronger network.

Another benefit of this merger will be sole ownership of Cingular Wireless, which is now jointly owned by both companies.

That partnership operates very well today, providing great service to millions of American consumers and businesses.

But no partnership, however well run, can operate as smoothly and quickly as a solely-owned enterprise. Streamlining Cingular's ownership, and giving it the best known brand in the industry, will only make it better.

After the merger, our wireless operation will be more agile, more effective, and better able to bring new innovations to market faster.

Another consumer benefit from this merger will be new competition in the video market.

As you know, AT&T is leading the way in deploying groundbreaking new video service using IP technology. It's called IPTV and it will change the way millions of Americans enjoy television.

And it will also change a few things for cable companies, too, because our TV service will be a compelling competitive alternative.

Our first IPTV deployment already is under way in San Antonio. And it didn't take long for cable to notice.

Time Warner immediately offered to reduce by one-third the monthly bill for one of the first customers who signed up for our IPTV service.

We plan to roll out this service in 15 to 20 more markets by the end of this year and expect to reach some 19 million customer locations by the end of 2008.

To do that, we are investing nearly five billion dollars in a new fiber network to provide the additional bandwidth that IPTV requires.

From the AT&T-BellSouth merger perspective, the good news is that BellSouth already has deployed a substantial, fiber-rich broadband network throughout a good deal of its territory.

So, by combining AT&T's IPTV expertise and experience with BellSouth's fiber network, we should see faster and more economical deployment of next-generation IP television service throughout the Southeast. And the consumer will be the winner.

We've already seen what competition has meant for telephone service. Since 2000, the average price of telephone service in this country has dropped by 22 percent.

During that same time period, the average price for basic cable in America increased more than 41 percent.

When faced with competition, however, the cable operators respond – and consumers benefit.

When Verizon rolled out its broadband video service in Keller, Texas, the cable incumbent lowered its prices by 25 percent.

Likewise, the introduction of new video competition in places like California, Virginia, and Florida compelled the incumbent cable operators to lower prices, freeze prices for the first time in years, or offer new features.

Of course, Congress has an important role to play when it comes to accelerating video competition.

In fact, consumers across the nation are closer to that competition than ever before, thanks to the vision of many in Congress who voted earlier this month to allow streamlined national video franchising. You know our position on this issue, so I won't dwell on it.

The House has taken the first big step, and the Senate now has an opportunity to pass legislation that will open the marketplace to substantial competition. Millions of consumers are counting on you to do just that.

A few years ago, Congress decided the full weight of regulation designed for incumbents in the telephone business wasn't the best way to encourage competition in that market.

Clearly, that same logic should apply in the video business as well.

A final benefit of the BellSouth merger that I will mention today will be its impact on business customers.

The combination of AT&T's state-of-the-art national and international networks with BellSouth's local exchange and broadband distribution platforms will be a powerful combination for business customers.

And customers in the southeastern United States will benefit from the expertise and innovation of AT&T Labs in much the same way former SBC customers are doing so today.

You don't have to take my word on this. All you have to do is look no further than what has happened since the merger between SBC and AT&T.

Today, less than six months after that merger was finalized, we are making outstanding progress in rolling out new products and services. Together, we are delivering innovation faster than either company could have done standing alone.

Let me give you a few examples.

We're looking at a new concept from AT&T Labs called Voice Signature, which could offer on-line merchants and shoppers an extra layer of protection when using credit cards online.

Consumers would register the sound of their voices, which would then be used as another form of identification. This could be a powerful tool for fighting credit card fraud and increasing consumer confidence in on-line shopping.

Another example shows how we can take technology previously available only to large customers and share it with a broader consumer market.

We're developing new methods to give consumers the same ability to back up their home PC's that our large business customers use.

Once this service comes to market, consumers will be able to use their broadband lines to provide automatic off-site back-up to their home computers. This will provide a simplicity and security that hasn't been broadly available before now.

Thanks to our merger with AT&T, it will soon become a reality.

We also are using our combined strength to give consumers greater access and more choices for broadband, no matter where they live or work.

AT&T is now offering a satellite-based broadband service in certain rural markets in AT&T's residential service territory – areas that generally are not served by landline broadband service today.

We're also deploying trials of fixed-wireless broadband. Two new trials for this technology are starting in Texas and Nevada. These trials will be used to test ways to use both licensed and unlicensed spectrum to better serve rural parts of the country.

These deployments build on the progress the company has made with existing trials in Alaska, Georgia and New Jersey.

The combination of the new AT&T and BellSouth will create a flagship American communications company, prepared to lead the way for this industry at home and abroad.

We are very excited about the possibilities this merger brings. And we look forward to the day this merger is approved and we can begin work on bringing innovation and choice to even more consumers.

Thank you.

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