December 7, 2006

BY ECFS

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

Re: AT&T Inc. and BellSouth Corporation Applications for Approval of Transfer of Control, WC Docket No. 06-74

Dear Ms. Dortch:

In a series of proceedings, beginning less than a year after the BOCs first were granted pricing flexibility, the Ad Hoc Telecommunications Users Committee ("Ad Hoc") has repeatedly sought dramatic reductions in special access rates based on misleading claims about competition, rates, and returns.[1] AT&T and others have repeatedly responded to these claims with hard facts that refute Ad Hoc's glib rhetoric. We have demonstrated, for example, that the special access market is far more competitive now than it was when pricing flexibility was adopted, resulting in reductions (not increases) in the average prices paid by consumers for DS-1 and DS-3 special access services between 2000 and 2004.[2] Undeterred, Ad Hoc again raises in this proceeding its bogus claims that the BOCs have "raised their prices [for special access services] in areas where the FCC has de-regulated pricing."[3] Only now, Ad Hoc bizarrely and incorrectly asserts that the *GAO Study* confirms its claims, and supports its request that the Commission condition approval of the AT&T/BellSouth merger on the imposition of radical and far-reaching limits on AT&T/BellSouth's special access services.[4] But, far from validating Ad Hoc's claims, that study confirms that special access rates have

[1] *Ex Parte* Letter from Levine Blaszak Block & Boothby LLP (Attorneys for Ad Hoc) to Marlene H. Dortch (FCC), WC Docket No. 06-74, at n.1 (filed Dec. 1, 2006) (Ad Hoc Dec. 1 Letter) (noting that, in January 2002, less than a year after SBC and Verizon first were granted pricing flexibility and four months *before* Qwest received flexibility, Ad Hoc first peddled its claims regarding purported "BOC[] rate increases . . . in pricing flexibility areas"). *See also, e.g.* Comments of Ad Hoc (June 13, 2005) at 18, filed in *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25 (claiming that "all four BOCs have increased prices for DS-1 circuits, DS-3 circuits or both in *every* region for which they have received pricing flexibility," and urging the Commission to turn back the clock to rate of return regulation by requiring the BOCs to reinitialize rates at levels that would produce an 11.25 percent rate of return).

[2] *See* AT&T Comments (June 13, 2005), at 2, 21, filed in *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25.

[3] Ad Hoc December 1 Letter at 1

[4] *Id.* citing *FCC Needs to Improve Its Ability to Monitor and Determine the Extent of Competition in Dedicated Access Services*, Report No. GAO-07-80 (Washington, D.C. Nov. 2006) (*GAO Study*).

declined in all markets, including those in which the BOCs have received Phase II pricing flexibility. GAO's only other conclusion was that the Commission needs more and better data to assess competition for special access services – a conclusion with which AT&T agrees, given the refusal of the CLECs to disclose, and the Commission's reluctance to require, data concerning CLECs' deployment of alternative facilities. GAO specifically declined to draw any conclusion regarding the sufficiency of special access competition and the potential impact of the instant and prior mergers on such competition, and expressly stated that its report did not advocate reregulation of dedicated access services. In light of these clear statements, Ad Hoc's claim that the *GAO Study* supports re-imposition of price controls on BOC special access services – particularly through merger conditions applicable only to one market player – is ludicrous.

1. The GAO Study Does Not Support the Need for Merger Conditions.

As an initial matter, Ad Hoc's claims that the *GAO Study* is "highly relevant to the instant proceeding" and "demonstrate[s] . . . that the merger would not serve the public interest unless the Commission imposes conditions to protect competition and consumers from the BOCs' market power over special access" are utterly baseless. Indeed, GAO expressly warned that its report "does not call for the reregulation of dedicated access prices,"[5] and that GAO made no judgment concerning the sufficiency of competition for special access services or the impact of the instant and prior mergers on such competition.[6] GAO further made clear that its analysis aggregated data from across the country to examine "overall trends in markets under different phases of pricing flexibility," and did not focus on results in specific MSAs or regions.[7] The GAO study thus says nothing about the impact of the AT&T/BellSouth merger on special access competition, which is the only issue relevant to this proceeding. And, as AT&T/BellSouth have shown, and DoJ has found, the merger will have no adverse effect on competition for special access services.

2. The GAO Study Confirms that Special Access Prices Have Been Falling.

More importantly, the *GAO Study* concludes that, since 2001, consumers of special access services have paid less for DS1 and DS3 special access services in all areas, including where the Commission has deregulated prices – a finding that cannot be reconciled with Ad Hoc's longstanding and repeated claims about the lack of competition

[5] *GAO Study* at 15.

[6] *Id.* at 50 ("We are not making a judgment on the legal sufficiency of competition in dedicated access services, including whether recent mergers violate antitrust laws or whether proposed remedies that the Department of Justice (DOJ) identified would be sufficient to eliminate the competitive harm of the mergers.").

[7] *Id.* at 11 (noting that data provided by price cap incumbents was proprietary, and thus was averaged to examine overall trends).

for special access services.[8] To be sure, GAO also found that prices, on average, have not declined as rapidly in markets with pricing flexibility as they have in markets still subject to price caps,[9] but that finding proves nothing and, in any event, is flawed. *First,* the Commission itself acknowledged when it adopted pricing flexibility that rates might not decline (and indeed might increase) where price cap regulation had forced rates below market levels[10] – an observation underscored by the D.C. Circuit's vacatur of the productivity factor that applied to special access rates prior to the grant of pricing flexibility.[11] *Second,* in the years since pricing flexibility was first granted, price cap rates have been driven down, not by an approved productivity factor or any other measure of productivity, but rather by a transitional X-factor negotiated as part of the CALLS plan, as the Commission expressly acknowledged:

> "[T]he X-factor as adopted herein will not be a productivity factor as it has been in past price cap formulas. Instead, the X-factor is now a transitional mechanism . . . to lower rates for a specified period of time for special access."[12]

Third, the proponents of that plan recognized when they negotiated those reductions that price cap regulation – and thus the X-factor reductions – would not apply in areas where a carrier received Phase II pricing flexibility, which influenced the X-factor ultimately agreed upon. Consequently, the fact that price cap ILECs' rack rates and average revenues per unit (ARPU) for DS-1 and DS-3 services may be lower in MSAs subject to price caps than in MSAs with Phase II pricing flexibility reflects nothing more than the terms and foreseeable outcome of a negotiated solution to long-standing disputes regarding access charge reform which was approved by the FCC as part of the CALLS plan. It says *nothing* about competition for special access services, nor does it establish that rates in Phase II MSAs are too high, as Ad Hoc contends. Indeed, after years of mechanical X-factor reductions untethered from any actual productivity gains in price cap areas, it would be surprising if prices in areas with pricing flexibility were not different, and in some cases higher, than prices in areas subject to price caps.

In any event, GAO's analysis of DS-1 and DS-3 prices was narrowly drawn, and, by GAO's own account, did not factor in a variety of pricing plans, value-added services,

---

[8] *GAO Study* Highlights ("Available data suggest that incumbent's list prices and average revenues for dedicated access services have decreased since 2001").

[9] *GAO Study* at 13.

[10] *Pricing Flexibility Order* at 14301 ¶ 155 ("We recognize that the regulatory relief we grant upon a Phase II showing may enable incumbent LECs to increase access rates for some customers. We conclude that this relief nonetheless is warranted upon a Phase II showing . . . because our rules may have required incumbent LECs to price access services below cost in certain areas.").

[11] *USTA v. FCC*, 188 F.3d 521 (D.C. Cir. 1999).

[12] *CALLS Order*, 15 FCC Rcd 12962, 13028 ¶ 160 (2000).

and other options – all of which affect the value of service and consumer welfare.[13] For example, certain special access plans spread discounts across all geographic areas and allocate discounts to certain services without regard to geographic location, which makes it difficult if not impossible to assess accurately special access prices on an MSA basis, as GAO attempts to do. GAO also did not adjust prices for inflation, nor did it take into account dramatic changes in customer demand for high capacity special access services and their substitutes over the past five years. Specifically, enterprise and other business customers that previously relied on high capacity special access service to obtain dedicated, high-speed access to the Internet now have a variety of less-expensive options, including xDSL, cable modem, and a variety of wireless services, which have significantly reduced those customers' costs for high capacity Internet access services, but which are not at all factored into GAO's pricing analysis. Thus, if anything, the GAO's conclusions regarding DS-1 and DS-3 pricing in areas in which price cap ILECs have received Phase II pricing flexibility significantly understate the decreases in price and increases in service quality and reliability, and consumer welfare that have been driven by market forces, rather than regulation, since pricing flexibility was first granted.

3. The GAO Study Does Not Support Ad Hoc's Claims Regarding a Lack of Competition for Special Access Services.

Ad Hoc's reliance on the GAO report to support its claims regarding the dearth of competitive alternatives to ILEC special access services is equally misplaced. As an initial matter, these claims cannot be squared with GAO's findings that special access rates have been *declining,* including in areas where rates have been deregulated. But beyond that, the *GAO Study* fails to support Ad Hoc's claims for multiple other reasons. First, as GAO itself readily admits, the data on which it relied was inaccurate and incomplete.[14] For example, it acknowledged that it failed to obtain from competing firms information on the buildings they serve, despite asking competitors (who are the only parties with complete information on their deployment of alternative facilities) to supply such data.[15] It also acknowledged that the data on which it relied instead (that is, GeoResults data and Telecordia's CLONES database, which is the source for GeoResults data) to identify buildings connected to CLEC fiber is incomplete, and may seriously understate the number of buildings served by CLECs. It noted, for example, that the creation of a CLLI code in CLONES is optional for records such as customer premises equipment (CPE), and CLECs thus are not required to, and often do not, register their

[13] *GAO Study* at 55-56 (noting that GAO's analysis did not consider features and options, such as value-added services geared toward providing added network reliability, and a variety of pricing plans).

[14] *GAO Study* at 21-22, and 47 ("We recognize the limits of available data on the extent and effect of competition in the market for dedicated access services.").

[15] *Id.* at 46-47.

CPE.[16] GAO nevertheless relied on this database because it was "the most comprehensive available."[17]

GAO's reservations about the data available were well-founded. As AT&T has previously explained to the Commission, the fact that a CLEC has listed some buildings in the CLONES database does not mean that it has listed all the buildings connected to its network, and thus that the CLONES data is comprehensive, even for those CLECs that have buildings listed in the database. In fact, AT&T's review of CLONES data discloses that two of the largest CLECs appear to have populated CLONES with CLLI customer equipment (CPE) codes for fewer than half of their lit buildings.[18] And, based on a sample of 800 CLEC lit buildings in the SBC region, AT&T has found that CLECs had registered a CLLI for CPE for less than 70 percent those buildings.

That GAO seriously understates the level of competition is evident from the limited number of buildings in the BellSouth region where AT&T has deployed facilities. For example, GAO claims that there are only 25 buildings in the entire Atlanta MSA with at least a DS3 level of demand and a "lit" competitor. However, in this proceeding BellSouth and AT&T have identified 61 buildings in Atlanta with more than a DS3 of demand that they both serve and in which another CLEC has fiber.[19] Similarly, in the Miami MSA, GAO claims there are only 14 buildings with at least a DS3 level of demand and a "lit" competitor. By contrast, BellSouth and AT&T have identified 66 buildings in Miami with more than a DS3 of demand that they serve and in which a CLEC has fiber.[20] Obviously, there are scores of additional buildings in both Atlanta and Miami that have at least a DS3 of demand and CLEC fiber but that are not served by AT&T, which GAO has overlooked.

In view of the serious shortcomings in the data available to GAO, which GAO itself acknowledged, it is not surprising that GAO explicitly chose not to make any definitive finding concerning the extent of facilities-based special access competition. Indeed, GAO's primary conclusion was that the Commission requires more complete data on special access competition – a conclusion with which AT&T concurs, given the longstanding refusal of CLECs to disclose data on their own market penetration and facilities, even as they call for more regulation of their competitors.

---

[16] *Id.* at 51-52.

[17] *Id*. at 52.

[18] Letter from Christopher M. Heimann, SBC Communications Inc., and Lawrence J. Lafaro, AT&T Corp., to Marlene H. Dortch, FCC at 10, WC Docket No. 05-65 (filed July 15, 2005).

[19] Letter from Gary L. Phillips, AT&T Inc. to Marlene H. Dortsch, Secretary, FCC, September 28, 2006, WC Docket No. 06-74, Exhibit 1.

[20] *Id.*

Second, in quantifying the percentage of commercial buildings with at least a single DS-1's worth of demand addressable by lit CLEC fiber,[21] GAO did not account for differences in the size of those buildings and thus did not purport to measure the share of the overall special access market that CLEC facilities can reach. CLECs obviously and by their own admission deploy fiber, first, to the very largest buildings. Plainly, any analysis that lumps together such disparate buildings as the Sears Tower in Chicago and a gas station using a single DS-1 circuit to communicate with suppliers fails to provide a complete and accurate picture of competition.

Third, GAO sought only to measure the deployment of alternative fiber, and did not attempt to quantify or otherwise consider alternative means by which CLECs can and do provide competing special access services, such as through the use of unbundled network elements and alternative technologies.[22] CLECs can obtain copper loop facilities, to which they can attach their own electronics to provide DS1 services (or xDSL services, which can be used to provide high capacity transmission services), as well as purchase DS1 and DS3 loops and transport in the vast majority of wire centers in MSAs in which price cap ILECs have obtained pricing flexibility. For example, under the Commission's unbundling rules, AT&T is required to provide DS1 loops in all but 4 of 172 wire centers in the Chicago MSA, and is required to provide DS3 loops in all but 8 of those wire centers. And, AT&T is required to provide DS1 transport as an unbundled network element (UNE) on over 98 percent of the possible transport routes in the Chicago MSA, and to provide DS3 transport as an UNE on 95 percent of the transport routes in Chicago. Moreover, advances in technology and other marketplace developments (such as advances in fixed wireless technology and high capacity services offered by cable companies) have obviated the need for CLECs to deploy fiber directly to a building. For example, as the *GAO Study* itself reports, 41.4 percent of commercial buildings in Norfolk, Virginia, now are connected to competitive high capacity transmission facilities deployed by a cable service provider.

The *GAO Study* thus does not, as Ad Hoc contends, demonstrate that special access competition is lacking. To the contrary, if anything, its analysis, incomplete as it is, shows quite the opposite – that competition is resulting in lower rates, even in the absence of government regulation.

* * * * *

The *GAO Study* confirms that special access rates have declined everywhere, including in areas in which the Commission has deregulated special access services,

[21] AT&T questions the relevance of examining buildings with a single DS1-worth of demand to evaluate the extent to which competitors have built alternative fiber to the addressable market because many such buildings likely have no demand for high capacity services, and the vast majority of such buildings are served only by copper facilities. But, either way, as discussed herein, the GAO study gauges only the extent of facilities deployment – not the percentage of special access demand that CLECs already can reach with their own facilities, or to which they readily could extend existing facilities.

[22] *GAO Study* at 20.

which should put to rest once and for all Ad Hoc's claims regarding alleged rate increases by BOCs in pricing flexibility areas and the purported need to re-impose stringent pricing controls. Beyond that, there is nothing in the report that is at all relevant to this proceeding. The *GAO Study* does not address the impact of the merger on special access competition, nor does it present data that would shed light on that issue. Indeed, GAO expressly stated that it made no judgment concerning the sufficiency of competition for special access services or the impact of the instant and prior mergers on such competition. Consequently, the *GAO Study* is relevant, if at all, only to the on-going special access rulemaking proceeding currently before the Commission. As such, the Commission should disregard Ad Hoc's *ex parte* and expeditiously approve the proposed merger without the special access conditions proposed by Ad Hoc in its September 22, 2006 *ex parte*.

Sincerely,

/s/ Gary L. Phillips

AT&T Inc.
1120 Twentieth Street, N.W.
Suite 1000
Washington, D.C. 20036
Tel: (202) 457-3055

/s/ Bennett L. Ross

BellSouth Corporation
1133 Twenty-First Street, N.W.
Suite 900
Washington, D.C. 200036
Tel: (202) 463-4113