BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF CALIFORNIA

In the Matter of the Joint Application of SBC Communications Inc. ("SBC") and AT&T Corp. ("AT&T") for Authorization to Transfer Control of AT&T Communications of California (U-5002), TCG Los Angeles, Inc. (U-5462), TCG San Diego (U-5389), and TCG San Francisco (U-5454) to SBC, Which Will Occur Indirectly as a Result of AT&T's Merger With a Wholly-Owned Subsidiary of SBC, Tau Merger Sub Corporation.	Application 05-02-027 (Filed February 28, 2005)

PROTEST OF THE UTILITY REFORM NETWORK, UTILITY CONSUMERS' ACTION NETWORK, DISABILITY RIGHTS ADVOCATES, CONSUMERS UNION OF U.S., INC, THE GREENLINING INSTITUTE, AND LATINO ISSUES FORUM

***** REDACTED VERSION *****

April 14, 2005

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In accordance with Rule 44 *et seq.* of the Commission's Rules of Practice and Procedure, The Utility Reform Network ("TURN"), the Utility Consumers' Action Network ("UCAN"), the Disability Rights Advocates ("DRA"), Consumers Union of U.S., Inc. ("Consumers Union"), the Greenlining Institute ("Greenlining") and Latino Issues Forum ("LIF") (hereinafter referred to as "Joint Intervenors") [1] hereby protest the above-captioned Application jointly filed by SBC Communications, Inc. (SBC) and AT&T Corporation (AT&T) and request that the matter be set for hearing.

I. INTRODUCTION

At least insofar as California is concerned, this Application proposes to reconstitute the Bell System that existed prior to the divestiture of the Regional Bell Holding Companies ("RBHCs") from AT&T. Divestiture was designed to address the

[1] The proprietary material in this protest has been generated and reviewed solely by TURN because the other parties are not yet signatories to a protective agreement with Applicants.

myriad ways in which the former Bell System hindered the growth of competition in telecommunications, particularly through its exercise of bottleneck monopoly control over the critical "last mile" linking individual customer premises to the public switched network. The Application would reinstate the corporate structure that facilitated these competitive abuses.

Much has changed in the over 20 years since divestiture. However, Joint Intervenors seriously question the Applicants' contention that SBC no longer possesses the bottleneck monopoly control over the last mile that allowed the former Bell System to thwart unaffiliated competitors. As we explain in more detail below, Joint Intervenors are prepared to present facts in an evidentiary hearing to show that SBC retains a substantial ability to exercise market power, despite the emergence of cell phones, cable telephony and Voice over Internet Protocol ("VoIP"), and that SBC's ability to exercise market power would be enhanced by the proposed merger.

This factual dispute is not the only issue on which Joint Intervenors disagree with the Applicants; however, it is one of the most important disputes. The claim that emerging competition is sufficient to limit SBC's ability to exercise market power—even after a merger with AT&T—is the essential premise on which the entire edifice of the Applicants' case rests. If this premise is refuted, the Commission cannot accept the Applicants' claim that the merger does not have an adverse effect on competition and therefore cannot find that approval of the merger would be consistent with Section 854(b) of the Public Utilities Code.

Any increase to SBC's market power creates the potential for significant harm to the residential and small business customers whose interests are represented by Joint

Intervenors. This is especially true given the Commission's increasing reliance on competition, rather than direct regulatory oversight, to ensure that SBC's subsidiaries provide high quality service to all Californians at just and reasonable prices.

These residential and small business customers also have a keen interest in ensuring that they receive at least 50 per cent of the short-term and long-term benefits of the merger, as required by Public Utilities Code Section 854(b)(2). As we discuss in more detail below, Joint Intervenors are prepared to present facts at an evidentiary hearing demonstrating that the Applicants have dramatically understated the portion of the total merger benefits that should be attributed to their California operations. Moreover, the Applicants have failed to provide any assurance that consumers in underserved communities—including low-income and minority consumers, disabled consumers and rural consumers—will receive their fair share of even the meager California-specific benefits the Applicants have identified.

Finally, residential and small business consumers also have a stake in ensuring that the proposed merger is in the public interest, as defined by the full range of criteria identified in Section 854(c) of the Public Utilities Code. As just one example, residential and small business consumers in communities throughout California need high-quality service, including access to advanced telecommunications services made possible by upgrades to the Applicants' existing network infrastructures. Thus far, the Applicants have maintained an ominous silence about the effects of the proposed merger on service quality—and the availability of advanced services—in California. Consumers have reason to be concerned that the merger will lead to massive layoffs that could jeopardize

the merged entity's service quality, thus adversely the millions of Californians who rely on SBC or AT&T as their service provider.

As required by the Administrative Law Judge's Ruling, the remainder of our protest states the facts that serve as our grounds for protest; further identifies the effects of the Application on the interested parties represented by Joint Intervenors; identifies the reasons that Joint Intervenors believe the Application as currently presented is not justified; and identifies facts that Joint Intervenors would present at a hearing in support of our request for denial of the Application as currently presented.[2] Our identification of facts and issues to be presented at an evidentiary hearing is necessarily illustrative rather than exhaustive, in large part because the Applicants have failed to provide all of the information necessary to make even a ***prima facie*** case for approval of this merger and because the Applicants have been less than forthcoming in discovery.

Nonetheless, Joint Intervenors respectfully request that the Commission set this matter for an evidentiary hearing and adopt a schedule that provides sufficient time for interested parties to conduct a full and complete investigation of the issues raised by this Application and to bring those issues before the Commission. The information provided in this protest provides ample justification for the Commission to hold evidentiary hearings in this matter.

[2] Administrative Law Judge's Ruling Regarding Due Date for Protests and Scheduling of Prehearing Conference, April 5, 2005, p. 3.

II. THE COMMISSION CLEARLY HAS JURISDICTION OVER THE PROPOSED TRANSACTION AND SHOULD REQUIRE THAT ALL THE REQUIREMENTS OF SECTION 854 BE MET

A. The proposed transaction is significant with major implications for telecommunications competition

The combination of a dominant incumbent local exchange carrier (ILEC) and the state's largest interexchange carrier (IXC) will likely have major reverberations throughout the remaining telecommunications marketplace. SBC's acquisition of AT&T will eliminate the one competitor that SBC itself most fears—and the one that has been the most active in pursuing a pro-competitive regulatory agenda before this Commission. The combined company will, by the Applicants' own claims, become an even more successful competitor than either of the two stand-alone companies is today. This is highly significant when viewed in the light of the most recent data on competition collected by the Telecommunications Division Staff ("Staff") and reported to the California legislature. The Third Telecommunications Competition Report stated in summary that "ILECs continue to control the local wireline market in California, although CLECs are gaining ground in the local toll market. SBC continues to lead the local and local toll marketplaces, earning more than all CLECs combined."[3] The Staff report also found AT&T to be the largest competitor for residential local exchange service, the third largest competitor for local business exchange service, the largest provider of both residential and business long-distance service, and the third-largest provider of both residential and business local toll service (SBC being the largest provider).[4]

[3] *The Status of Telecommunications Competition in California*, Third Report For 2003, October 31, 2003, p. 5.
[4] *Ibid.*, p. 6.

This picture is confirmed and reinforced by SBC's own internal, more current, analysis of competition within various markets in California. To provide a small (but representative) indication, SBC's most recent market share analysis indicates that SBC controls *****BEGIN PROPRIETARY**

[5]

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[9] **END PROPRIETARY*****

The general picture of SBC as a heavily dominant ILEC, challenged primarily by AT&T, has remained unchanged. Bluntly, this merger is very much about SBC eliminating its existing major competitor based on the argument that other competitors will probably arrive soon. Notably, the Applicants—who are in the best position to know the likely forward-looking effect of the merger on market share in various markets—have

[5] Attachment to SBC response to TURN Data Request 1-3, p. 000340. All Applicant discovery responses cited herein are provide in Exhibit 1.
[6] *Ibid.*
[7] *Ibid.*, p. 000413.
[8] *Ibid.*, p. 000137.
[9] Attachments to SBC response to TURN Data Request 1-3, *e.g.*, pp. 000137, 000142, 000145, 000150, 000160, 000161, 000163, 000233, 000226 and 000227.

provided no quantitative information whatsoever concerning their current or anticipated future shares of any geographic or product market within the state of California. By withholding this information, which is necessary for the Commission to assess how the merger will affect market concentration both throughout the state and in specific markets, the Applicants are attempting to prevent the Commission from having a meaningful understanding of what the true effects of the proposed merger would be.

Knowledge of past market penetration, combined with qualitative information about how this proposed transaction will transform the telecommunications marketplace in California, strongly suggests that the Applicants have good reason to be silent. There is every reason for the Commission to expect SBC's acquisition of AT&T to have an adverse effect on competition within this state.

The proposed merger would essentially reverse the small progress that had been achieved heretofore in delivering residential competition. Indeed, even other CLECs and ILECs will likely face significantly less competitive pressure as AT&T's consumer operations are absorbed into SBC (as SBC does not seem to compete in other ILEC areas in the consumer market). Ironically, the Applicants bill AT&T's supposedly "irreversible" retreat from the consumer market as a justification for the merger. To the contrary, that retreat, along with the retreat of other competitors such as MCI, merely affirms that SBC's monopoly bottleneck held firm and has, in fact, choked-off competition. It is thus doubly important that AT&T, SBC's major in-franchise competitor, has not yet retreated from business markets. To a significant extent, it is the fact that AT&T remains the premier competitive alternative in the business services market that SBC apparently considered a serious enough threat to fuel this merger.

Should the merger be consummated, the combined strength of AT&T and SBC (along with the economic advantages such an entity would enjoy relative to other possible competitors, as discussed below) will very likely result in making SBC's bottleneck control over much or most of the access to business markets in California an equally unbreakable stranglehold.

For example, as Joint Intervenors will explain in detail in Section III.B below, the combined SBC/AT&T will attain an even greater economic advantage relative to other IXCs than exists today for SBC California's own intraLATA toll operations (which Staff found to be the largest such operations in the state) and its affiliate's interLATA toll operations (which have grown dramatically in the relatively short time since SBC received Section 271 authority to provide interLATA services within SBC California's service territory). That added economic disadvantage will not only substantially reduce the prospect of survival for any remaining traditional long-distance companies, it will be a huge "nail in the coffin" for business competition (large and small). Unlike residential customers, businesses (for the most part) do not have any near-term prospect of possible cable competition. Wireless is typically an additional cost for businesses, but is not sweeping handsets off of the nation's office desks.[10] Heretofore, SBC's business competitors have primarily been AT&T, MCI and an assortment of much smaller Competitive Access Providers ("CAPs"). Should AT&T (and, likely, MCI) vanish, it is unlikely that CAPs can provide meaningful competition for the vertically integrated juggernaut of a combined SBC and AT&T, on whom they will depend for interconnection and other services. A SBC/AT&T merger will further limit potential

[10] Instead, each additional wireless phone a business buys for employees when they are not at their desks is yet more gravy for SBC as a dominant major provider of cellular service, through its Cingular joint venture.

competition by eliminating any possibility for CLECs such as Covad to find substantial partners for strategic alliances. Finally, a SBC/AT&T combination in California would slam the door on the possibility of almost any emergent new competitor. The economics of new technologies such as IP telephony critically depend on traffic volumes to create economies.[11] In SBC's local service areas, it is inconceivable that any emerging competitor will be able to match the traffic volumes that SBC/AT&T could almost instantly channel into any new application.

B. Contrary to Applicants' contentions, Sections 854(b) and (c) are applicable

The Applicants present two arguments as to why the Commission should ignore its statutory mandate under Public Utilities Code Section 854(b) and (c):

- The transaction "involves the merger of a telecommunications holding company with another holding company" and "does not directly involve any public utility"[12]; and
- The AT&T subsidiaries involved in this transaction are non-dominant interexchange carriers (NDIECs) and competitive local exchange carriers (CLECs), justifying a Section 853(b) exemption.

As Joint Intervenors will discuss below, these arguments are totally without merit, fly in the face of Commission precedent and should therefore be rejected.

[11] Attachment to SBC response to TURN Data Request 1-8, at 000645-000646.
[12] Joint Application of SBC Communications Inc. and AT&T Corp. (February 28, 2005), (Application), p. 14.

1. Applicants should not be allowed to use the structure of the transaction as a shield to prevent valid Commission investigation pursuant to Section 854(b) and (c)

The Applicants argue that the Legislature's use of different terms in Section 854(b) and (c) ("utilities" vs. "entities") means that subsection (b) "is triggered only in the narrow category of transactions directly involving a utility, whereas subsection (c) applies to a broader category of transactions."[13] Because the transaction will result in the "indirect transfer of control"[14] of AT&T subsidiaries to SBC, the argument continues, "neither party to this transaction is a utility";[15] therefore, the Applicants claim, this "parent-level merger"[16] is not subject to Section 854(b).

This is exactly the same argument made by the Applicants in the SBC and Pacific Telesis Group merger. While the Applicants herein dismiss the SBC/Telesis Merger Decision[17] as an anomaly because the acquisition target consisted of 90% local exchange assets, they conveniently leave out some critical language and reasoning from that decision.

In the SBC/Telesis Merger, the Commission stated that the "plain language of subsection (b) is clear, and applies where a utility of a specified financial size is a party to the proposed transaction."[18] Thus, the Commission was faced with the question of whether Pacific Bell was a party to the transaction. The Commission held "[a]lthough the transaction is technically structured as a merger between SBC and Telesis, the practical result of the proposed transaction, if it is consummated, is that it involves

[13] Application, p. 18.
[14] *Ibid.*
[15] *Ibid.*
[16] *Ibid*., p. 19.
[17] Re Joint Application of Pacific Telesis Group (Telesis) and SBC Communications, Inc. (SBC), D.97-03-067, 71 CPUC 2d 351 (March 31, 1997) (SBC/Telesis Merger).
[18] D.97-03-067, p. 6; 71 CPUC 2d 351, 365.

Pacific."[19] Focusing on substance rather than form, the Commission "pierced the corporate veil" to find that 854(b) was applicable to the transaction.[20]

The Applicants in the instant transaction argue that the reasoning in the SBC/Telesis merger does not apply. They contend that:

> AT&T's certificated public utility subsidiaries in California are a modest component of the much larger transaction involving the global, diversified holding company that SBC is acquiring, and the California intrastate revenue of these subsidiaries is a fraction of AT&T's overall revenues. AT&T's intrastate utility operations are not the heart of this transaction. Thus, the Commission should follow the plain reading of the statute. Section 854(b) simply does not apply.[21]

These arguments fail on many grounds. First, the Applicants attempt to have the Commission focus only on the acquisition target of the transaction, *i.e.*, AT&T. Both Sections 854(b) and 854(c) apply to "any of" the utilities or entities involved in the transaction. Thus, the Commission is not limited to only looking at AT&T. The Commission must also examine the other party to the transaction, *i.e.*, SBC.

Second, while not being specific, Applicants imply that AT&T's gross annual California revenues do not meet the statutory threshold under Sections 854(b) and (c) of five hundred million dollars by arguing that "the California intrastate revenue of these subsidiaries is a fraction of AT&T's overall revenues."[22] However, it is clear from proprietary materials filed with the Application that AT&T's California revenues exceed the threshold.[23] And, it is obvious that SBC's California gross revenues also exceed the statutory threshold of five hundred million dollars.

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[19] *Ibid.*
[20] *Ibid.*
[21] Application, p. 19.
[22] *Ibid.*
[23] *See* Application, Exhibit 15, Filed Under Seal.

Finally, the Applicants take great pains, in arguing how the transaction will benefit all consumers, to assert that "as a combined organization, SBC and AT&T will be able to offer a portfolio of services for any consumer."[24] Over and over again, in the Application and exhibits, the Applicants discuss how the

> … combined SBC and AT&T will be a stronger and more enduring U.S.-based global competitor than either company could be alone, capable of delivering the advanced network technologies necessary to offer integrated, innovative high quality and competitively priced telecommunications services to meet the national and global needs of all classes of customers worldwide. The combined company will have the resources, expertise and incentive to adapt the sophisticated products that AT&T has developed for its enterprise customers to the needs of small and medium businesses and consumers, and the marketing expertise and infrastructure to reach those customers.[25]

Presumably, this portfolio of products and services would be offered to California consumers through SBC California—not the holding company, but the operating company that previously was known as Pacific Bell—and/or, perhaps, AT&T California. It is patently absurd for the Applicants to argue that the transaction has nothing to do with local California utilities for purposes of applying Section 854, while at the same time contending that the merger will be in the public interest because it will enhance the ability of the California utility subsidiaries (SBC California and AT&T California) to offer California consumers a portfolio of services. Applicants cannot have it both ways. Either the transaction involves California utilities, or it does not. By the Applicants' own admission, it does; therefore, the Commission should, as it did in the SBC/Telesis Merger, apply Section 854(b).

[24] Application, p. 7. *See also* Application, p. 25 where Applicants make it clear that the merged companies will be a combined organization.
[25] Application, Exhibit 2, Declaration of James S. Kahan, p. 8.

Joint Intervenors submit that the Commission should treat this merger just like it did the SBC/Telesis Merger and hold that Section 854(b) and (c) both apply. To do otherwise would clearly elevate form over substance and would fly in the face of the Legislature's requirements.

2. The fact that AT&T is a NDIEC and CLEC is absolutely irrelevant to the Commission's determination as to whether to apply Sections 854(b) and (c)

The Applicants argue that whether or not the Commission holds that Section 854(b) applies to this transaction, the Commission should exempt the merger from such review pursuant to Section 853(b). The Applicants base their request for an 853(b) exemption on the contention that AT&T is a NDIEC/CLEC and, as such, should not be subject to Section 854 requirements. Applicants argue that "in the past decade, the Commission has authorized scores of transactions involving NDIECs and CLECs, but uniformly has exempted them from the detailed requirements of Section 854(b)."[26]

In support of this argument, Applicants provide a string cite consisting of 43 cases. However, upon examination, it is clear that these 43 cases are totally inapplicable to the instant transaction and represent a colossal waste of time and resources necessary to track them all down and distinguish them. It is true that these 43 cases did involve non-dominant carriers. In addition, these cases share some other important characteristics, about which the Applicants are notably silent, that distinguish them from the transaction under review: almost all the cases were what the Commission characterized as "non-controversial"; almost all the cases were uncontested (or, to the extent some were contested, they were challenged on grounds totally irrelevant to the

[26] Application, p. 14.

instant proceeding); and almost all the transactions were relatively small from a financial value perspective. In comparison, the proposed merger of SBC and AT&T is highly controversial, is being contested and involves SBC's acquisition of approximately $16 billion in assets (the acquisition price being paid for AT&T). Furthermore, as TURN discusses below, this transaction has significant implications for the competitiveness of the telecommunications industry and for consumers.

Citing the proposed merger of MCI and British Telecom,[27] Applicants make much of the purported "three-part standard" for exemption from the requirements of Sections 854(b) and (c) that the Commission developed in that proceeding. According to the Applicants, the Commission, in the MCI/BT case, applied the following reasoning to exempt the transaction from Sections 854(b) and (c) scrutiny:

(1) the merger did not involve two traditionally regulated telephone systems;

(2) NDIECs and CLECs are not subject to the same Commission rate regulation as ILECs; and

(3) the finding of merger benefits and an allocation of a portion thereof to ratepayers did not fit a transaction where the acquired company had been subject to competitive forces without a guaranteed franchise territory.[28]

Applicants assert that the Commission has applied this "test" to "scores" of similar cases. Applicants then proceed to argue that the proposed merger meets these tests "because this transaction does not involve 'the acquisition of a heavily-regulated local exchange carrier.'"[29] Applicants' reasoning is faulty on a number of grounds and should be rejected by the Commission.

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[27] In the Matter of the Joint Application of MCI Communications Corporation (MCIC) and British Telecommunications plc (BT) for All Approvals Required for the Change in Control of MCIC's California Certificated Subsidiaries That Will Occur Indirectly as a Result of the Merger of MCIC and BT, D.97-05-092, 72 CPUC 2d 656 (May 21, 1997) (MCI/BT).
[28] Application, p. 22.
[29] *Ibid.*, p. 24.

At the outset, it is important to stress that the Commission placed some critical qualifications on the three-part test. First, the Commission was clear that "[i]t is the combination of all of the above factors, not just one factor,"[30] that led the Commission to conclude that an exemption was warranted. Second, the Commission has been clear that consideration of an exemption will be made on a case-by-case basis based on the specific facts of the particular transaction.[31] In addition, the Commission has stressed that the exemption "must be applied selectively as it must be the exception and not the rule."[32] In this case, the three-part test cannot be met.

As discussed above, Section 854 does not focus exclusively on the target of an acquisition. Applicants continually maintain that the Commission should ***only*** look at the entity SBC is acquiring, *i.e.*, AT&T. However, this completely ignores several critical facts: that the acquirer is one of the most significant providers of telecommunications services in California; that by acquiring AT&T, SBC is eliminating its most significant California competitor; and that the transaction will have a significant impact on California consumers. The Applicants actually attempt to justify the proposed merger in similar terms, arguing that it will create a "combined" telecommunications powerhouse. Significantly, in the MCI/BT merger and subsequent similar transactions relied upon so heavily by the Applicants, ***both*** parties to the mergers were non-dominant carriers. Here,

[30] MCI/BT, 72 CPUC 2d 656, 665.
[31] *See* MCI/BT, D.97-05-092, 72 CPUC 2d 656, 663 ("We caution that we limit this §§ 854(b) and (c) exemption to the unique facts and circumstances of this transaction."). *See also*, D.98-05-022 and D.01-03-079. In addition, in the non-consummated proposed merger between WorldCom and Sprint, the ALJ clearly ruled, and was specifically affirmed by the Commission, that the cases allowing exemptions from Sections 854(b) and (c) were clearly not precedential (In re Request of MCI WorldCom, Inc. and Sprint Corporation for Approval to Transfer Control of Sprint Corporation's California Operating Subsidiaries to MCI WorldCom, Inc., A.99-12-012, ALJ Ruling Denying Motion of MCI WorldCom and Sprint for Early Determination of Exemption From Public Utilities Code Sections 854(b) and (c), as affirmed in D.01-02-040, COL 12, Feb 8, 2001).
[32] In re Request of WorldCom, Inc. and Intermedia Communications, Inc., for Approval to Transfer Control of Intermedia Communications, Inc. and its Wholly-owned Subsidiary to WorldCom, Inc., D.01-03-079 (Mar. 27, 2001), p. 3.

SBC, the largest party to the transaction, is not only a ***dominant*** carrier, but is in fact a critical provider of essential services in California. Clearly, the Commission never intended to exempt such a transaction from careful Section 854(b) and (c) scrutiny.

Furthermore, this is not a case where the Commission lacks ratemaking authority over a significant party to the transaction. In all the cases cited by the Applicants, the Commission either lacked the requisite jurisdiction, or had forborne from exercising jurisdiction over ***both*** parties to the transaction. Without such jurisdiction, the Commission reasoned in the "scores" of cases cited by the Applicants, the Commission either could not or should not allocate benefits from the merger to ratepayers pursuant to Section 854(b). Contrary to the Applicants' assertions, the Commission has never limited the application of Sections 854(b) and (c) to those transactions where only the acquired company was not subject to both the Commission's jurisdiction and the active exercise of the Commission's ratemaking authority. In the proposed merger of SBC and AT&T, the Commission clearly has ratemaking authority and jurisdiction over both SBC's and AT&T's California operations and actively exercises that authority over SBC's California operations. Therefore, the Commission can and should allocate a portion of merger benefits to SBC's California ratepayers as mandated by Section 854(b). In addition, SBC California did not grow "under competitive forces at the sole risk of its shareholders without a captive ratepayer base and monopoly franchise to buffer risk and reward."[33] Therefore, SBC does not meet the third prong of the MCI/BT test.

The Applicants also cite a series of decisions where the Commission has modified Commission procedures so that transactions involving NDIECs and CLECs, under

[33] Re Application of WorldCom, Inc. and MCI Communications Corp. for Approval to Transfer Control of MCI Communications Corp. to WorldCom, Inc., D.98-08-068, 81 CPUC 2d 704, 715 (August 32, 1998) (MCI/WorldCom).

prescribed circumstances, could proceed via advice letter rather than application.[34] Applicants suggest that the instant transaction is as "routine" as the transactions the Commission has permitted through advice letter filings. The Applicants are wrong. In fact, in the most recent Commission decision on this point, D.04-10-038, the Commission rejected a request that "to expand the use of advice letter fillings for all §§ 851 through 854 requests of NDIECs and CLECs."[35] More significantly, the Commission specifically addressed the applicability of extending the advice letter process to transactions involving ILECs. The Commission refused to apply the streamlined process to ILECs, stating:

> Even though ILECs may enter into non-controversial transactions, disparities necessarily exist in the regulatory and procedural rules between competitive carriers and ILECs. This is because consumer interests in such transactions involving ILECs utilities require a higher level of scrutiny than in transactions of non-incumbent utilities. This is due to the unique status of ILECs, which continue to exercise market power in at least some of the markets they serve. The procedures and consumer safeguards established by D.94-05-051, modified by D.97-06-096, and the subject of this decision are applicable to nondominant telecommunications utilities, which, by definition, do not exercise market power in any of the markets they serve.[36]

Thus, it is clear that none of the cases cited by the Applicants apply to the proposed merger and the Commission should review the transaction under the requirements of Sections 854(b) and (c).

III. THE COMMISSION SHOULD DENY THE APPLICATION BECAUSE THE APPLICANTS HAVE NOT MET THE BENEFITS SHARING AND COMPETITION REQUIREMENTS OF SECTION 854(B) AND THE PUBLIC INTEREST TEST OF SECTION 854(C)

Proper application of the benefits sharing and competition requirements of Section 854(b) and the public interest test of Section 854(c) would require the

[34] Application, n. 21, p. 20.
[35] Application of California Association of Competitive Telecommunications Carriers for Modification of the Rules By Which Carriers Obtain Commission Authority Pursuant to Sections 851-854 of the Public Utilities Code, D.04-10-038 (Nov. 11,2004), p. 3.
[36] *Ibid.*

Commission to reject the Application as filed. In the following discussion, Joint Intervenors note specific deficiencies in the Applicants' showing and identify some of the facts that we would present at an evidentiary hearing to support our request that the Application either be denied outright or be approved only subject to mitigating conditions that the Applicants themselves have failed to propose.

A. Section 854(b)(2) requires that at least 50% of the merger savings subject to Commission ratemaking authority must be shared with ratepayers. The Applicants have failed to meet this requirement

1. The Applicants have misstated the requirements of Section 854(b)(2).

Applicants contend that if the Commission were to apply the requirements of Sections 854(b)(1) and (2) to the proposed SBC/AT&T merger, the Commission should look to the "qualitative standards applied in the AT&T/ McCaw Merger Decision."[37] The AT&T/McCaw decision[38] is the sole case that the Applicants rely upon for supposed "qualitative standards" to be used in assessing the short-term and long-term benefits of a merger. According to the Applicants, the AT&T/McCaw decision stands for the broad proposition that

> … qualitative short-term and long-term benefits to consumers in transactions involving the acquisition of entities over which the Commission does not exercise traditional ratemaking authority (e.g., non-dominant interexchange carriers("NDIECs") and competitive local exchange carriers ("CLECs")) satisfy the requirements of Section 854(b).[39]

[37] Joint Supplemental Application of SBC Communications, Inc. and AT&T Corp. (March 30, 2005), p. 5 (Joint Supplemental Application).
[38] Re American Telephone and Telegraph Company, et al. for Authorization to Transfer Indirect Control of Airsignal of California, et al. from McCaw Cellular Communications Inc. to the American Telephone and Telegraph Company, D.94-04-042, 54 CPUC 2d 43 (Apr. 6, 1994), p. 5 (AT&T/McCaw).
[39] Joint Supplemental Application, p. 4 (footnote omitted).

Applicants' reliance upon the AT&T/McCaw decision is unwarranted. First, the Applicants assert that the Commission applied a "***qualitative*** benefits analysis"[40] in the AT&T/McCaw case. However, the Applicants fail to mention that the Commission never even uses the word "qualitative" in its decision. What the Commission did say was that the assessment of benefits for the proposed transaction was complicated. In discussing these complications, the Commission stated:

> The assessment of benefits in this case is complicated by the fact that this merger, even more than other recent mergers, is a paper transaction. The specific action we are asked to approve is the change in ownership of McCaw; McCaw's California utilities will remain the property of McCaw. More important, because the merger involves two companies in essentially different lines of business, no consolidation of operations affecting the 15 McCaw California utilities is proposed at this time. In other mergers, consolidation is usually the key to the savings that are cited as the net benefits to ratepayers. Because of the nature of this transaction, *applicants have not quantified (with some exceptions) the benefits they believe the merger produces.*
>
> A second complication is that we do not presently impose cost of service ratemaking on McCaw's California subsidiaries. They operate in fields that are largely competitive, and our regulation of these fields is correspondingly relaxed. The consideration of the appropriate "ratemaking method" must recognize the nature of our regulation of these companies.[41]

In comparison, in the instant case of the proposed merger of SBC and AT&T, the consolidation or, as the Applicants continually state in their filings, "combination" of SBC and AT&T is a critical element of the transaction. And, as Applicants have stated in numerous press releases, they expect the merger to "yield a net present value of more than $15 billion in synergies, net of the cost to achieve them."[42] Thus, unlike the AT&T/McCaw transaction, Applicants already have performed a quantitative assessment

[40] *Ibid*., p. 3 (emphasis in original).
[41] AT&T/McCaw, 54 CPUC2d 43, 50-51 (emphasis added).
[42] "SBC To Acquire AT&T, Creates Premier, Global Provider for New Era of Communications," *SBC Investor Briefing No. 246*, January 31, 2005, pp. 2-3.

of expected benefits, and there is no need or justification for the Commission to apply a "qualitative" standard in evaluating the short-term and long-term benefits.

Furthermore, unlike the AT&T/McCaw merger in which the parties were either outside the Commission's rate-setting jurisdiction (McCaw) or subject to streamlined regulation due to competition (AT&T), at least one of the parties in the instant case is an ILEC subject to full Commission authority. The AT&T/McCaw decision is just another in the Applicants' long list of inapplicable cases involving mergers between non-dominant carriers. That is just not the situation in the proposed transaction where a clearly dominant ILEC is buying a NDIEC/CLEC (notably, the ***largest*** NDIEC/CLEC operating in California).

In addition, in the proposed SBC/AT&T merger, again unlike the AT&T/McCaw case, the Commission would not be "reimpos[ing] cost of service ratemaking … merely to ensure that merger benefits are transferred to ratepayers."[43] The instant case is more analogous to the SBC/Telesis merger in which the Commission applied surcredits to distribute merger benefits to ratepayers even where the Commission was not exercising cost-of-service ratemaking authority.

Finally, it is important to note that the Applicants, just as they did with the NDIEC/CLEC cases discussed above, argue that the AT&T/McCaw decision rests in part on the sole identity of the acquired company. There are no cases where the Commission has specifically held that a transaction, for purposes of Section 854, should only be examined from the perspective of the acquisition target. To look at only one side of the transaction, in the instant case AT&T, and ignore the party doing the acquiring, would make a mockery of Section 854, which specifically requires an "equitable allocation,

[43] AT&T/McCaw, 54 CPUC2d 43, 52.

where the Commission has ratemaking authority, of the ***total*** short-term and long-term benefits … of the proposed merger, acquisition or control,"[44] and should not be countenanced by this Commission.

2. The Applicants' quantification of merger benefits violates the standards of Section 854(b)(2).

The moment one considers the benefits accruing to ***both*** parties to the merger transaction, it becomes clear that the Applicants' supplemental filing dramatically understates the merger benefits that should be subject to sharing with California consumers. In press releases announcing the merger, the Applicants claimed that SBC's acquisition of AT&T would be self-financing, *i.e.*, that the net present value of the merger benefits (net of the cost to achieve them) would be roughly comparable to the $16 billion cost of the acquisition.[45] Yet, the Applicants now claim that California-specific

[44] P.U. Code Section 854(b)(2), emphasis added.
[45] "SBC To Acquire AT&T, Creates Premier, Global Provider for New Era of Communications," *SBC Investor Briefing No. 246*, January 31, 2005, pp. 2-3:

> "SBC and AT&T expect the proposed transaction will yield a net present value of more than $15 billion in synergies, net of the cost to achieve them. The synergies ramp quickly with a net annual run rate of $2 billion or greater beginning in 2008.
>
> "Almost all of the synergies will come from reduced costs over and above expected cost improvements from the companies' ongoing productivity initiatives. Nearly half of the total net synergies are expected to come from network operations and IT, as facilities and operations are consolidated. Approximately 25 percent are expected to come from the combined business services organizations, as sales and support functions are combined. About 10 to 15 percent of the synergies are expected to come from eliminating duplicate corporate functions. Approximately 10 to 15 percent of expected synergies come from revenues, as the combined company migrates service offerings to new customer segments.
>
> "SBC has also taken a conservative approach modeling expected AT&T revenues. AT&T's revenues have declined over recent years as it has transitioned from a voice long distance business to an emphasis on business and data markets, and those declines are expected to continue. At the same time, AT&T's next-generation IP and e-services revenues grew 11 percent in 2004.
>
> "SBC expects the acquisition will slow its revenue growth rate in the near term following closing. New revenue opportunities include expanded wireless sales in the enterprise space and taking AT&T's industry-leading portfolio of enterprise IP-based services down market to small business and residential customers.

merger benefits total only $27 million,[46] less than 2/10 of 1% of the total synergies alleged in their press releases. This claim is implausible on its face, given that California is the largest state in the country and that it is one of only 13 states in which SBC and AT&T both have substantial operations. Logically, one would expect that the proportion of merger savings attributable to the combined California operations would be even larger than California's proportion of either the national population or the national number of telephone lines—certainly not less than 2/10 of 1% of the total savings.

Joint Intervenors' initial review of Applicants' cursory showing concerning merger benefits indicates that the huge discrepancy between the $27 million figure and the nearly $16 billion figure quoted in national press releases arises from two sources: (1) Applicants' decision to determine the California-specific share of nationally projected merger benefits as being equal (in percentage terms) to "AT&T's estimated operating expense for California as a percentage of the combined company operating expense"[47]; and (2) Applicants' decision to consider only the "forecasted net expense synergies for the combined company for each of the first five years post-closing,"[48] which necessarily includes the lion's share of the costs relating to the acquisition but only a small fraction of the total synergies expected as a result of incurring those costs. Moreover, the Applicants made no effort whatsoever to examine the specific sources of projected

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> "SBC expects the transaction will be cash flow positive in 2007 and earnings per share positive in 2008 — both growing in the years thereafter. Positive cash flow from the acquired business is expected to provide additional financial flexibility for SBC over the next several years.
>
> "AT&T currently has approximately $6 billion in net debt and SBC has $26 billion, excluding debt at Cingular Wireless. SBC expects free cash flow after dividends from the combined companies to provide the flexibility to continue to reduce combined debt levels over the next five years while providing excellent cash returns to stockholders."

[46] Joint Supplemental Application, pp. 13-14. Applicants therefore allege that at most $14 million of merger savings would be allocable to California ratepayers. *Ibid.*, p. 14.
[47] *Ibid.*, p. 13.
[48] *Ibid*.

savings, which could well reveal that far more than $27 million in projected savings will come from California-specific sources such as employee reductions in California. As noted above, nothing in Section 854(b) limits the Commission to consideration of only merger benefits associated with the company being acquired. Thus, hearings are necessary to test Applicants' unreasonably low estimate of California-specific merger savings, to consider more reasonable allocators of national merger-related synergies and to determine whether it is fair and reasonable to deduct virtually 100% of merger-related costs from the savings to be shared with California consumers while denying those consumers any share in the billions of dollars of expected savings to be achieved—at virtually no incremental cost—more than five years after the transaction is consummated.

Moreover, in "advance objections" to TURN's data requests, the Applicants are refusing to produce the full national synergy model on which they based their *de minimis* estimate of California-specific merger benefits.[49] Yet, the Applicants themselves acknowledge that:

> [t]he forecasted synergy calculations presented here are based on the same models used to forecast overall synergies. The overall forecast models were used by senior management in evaluating the transaction and were presented to the SBC board of directors for approval of the transaction. The forecasts considered by management and the board were on a national basis. They did not analyze synergies that might accrue in individual states.[50]

Based on this admission, the detailed estimates of national merger operating expense synergies and implementation costs to achieve these synergies that apparently are contained in the national synergy model are highly relevant to an evaluation of the

[49] *Ibid.*, Exhibit 1, lines 6 and 9. *See* Exhibit 1 to this protest for a copy of Applicants' objection. It is currently unclear if Applicants refuse to provide access to the "national synergy model" at all or if they merely intend to limit access to that model to "no copies," view-only access to a printout of the model at SBC's offices. Either tactic rendered an effort to review the model in time for analysis herein practically impossible.

[50] Joint Supplemental Application, p. 13, n. 48.

Applicants' claimed California-specific merger benefits—indeed, they are the crux of any such analysis. The Commission cannot possibly determine that the Applicants correctly have identified the relevant net merger benefits—much less that they have attributed a reasonable share of total merger benefits to California—without access to this information.

The Applicants did not provide this model, or any of the underlying detail, as part of their supplemental merger filing. Thus, for example, the Commission and the parties cannot determine the extent to which merger-related reductions to Applicants' cost of capital are included in the $27 million in alleged California-specific merger benefits. Again, hearings are necessary to develop the record concerning the accuracy and inclusiveness of Applicants' national merger synergies forecast and the reasonableness of Applicants' proposed allocation of those merger synergies to California.

B. The Applicants have failed to demonstrate, as required by Section 854(b)(3), that the proposed transaction will "not adversely affect competition."

1. The Applicants have failed to provide any California-specific showing whatsoever concerning the competitive effects of the proposed transaction and have provided no quantitative information whatsoever concerning market shares in any geographic or product market, however defined

The primary evidence that the Applicants provide concerning the proposed transaction's effect on competition lies in two declarations: (1) the Declaration of Dennis W. Carlton and Hal S. Sider,[51] two outside economists; and (2) the Declaration of Thomas Horton,[52] Chief Financial Office and Vice Chairman of AT&T Corp. Neither of these declarations provides specific detail concerning the competitive effects of the

[51] Application, Exhibit 1 (hereinafter, "Carlton/Sider Decl.").
[52] Supplemental Joint Application, Exhibit 2 (hereinafter, "Horton Decl.").

proposed transaction ***in the state of California***. Moreover, the Carlton and Sider declaration presents what the authors themselves describe as an "initial assessment" based on their general industry knowledge, a review of high-level public data and the Applicants' own representations to the declaration's authors.[53] Drs. Carlton and Sider explicitly indicate that their conclusions are subject to revision after they have had an opportunity to review non-public data that the Applicants supposedly would be providing once a protective order was in place.[54] Joint Intervenors note that the Applicants' Supplemental Joint Filing appears to be devoid of any non-public data concerning the effects of the proposed transaction on competition in California. The utter lack of California-specific data and analysis concerning competitive effects means that the Applicants have failed to meet their burden under Section 854(b)(3).

There can be no question that the Applicants are attempting to side-step the Commission's review of the effect of the proposed transaction on competition in California. The Applicants have provided no information regarding the combined market share of SBC and AT&T for residential lines, business lines, intraLATA toll or interLATA toll within SBC California's service territory. They thus expect the Commission to make its decision in a completely uninformed state regarding the level of concentration that the proposed transaction will cause. To justify this non-information, the Applicants present their economists' claim that such evidence of concentration is not relevant because only forward-looking market shares should be considered and AT&T's market share (at least for residential and small business services) is rapidly declining.[55] Notably, however, Joint Intervenors have not identified even a single piece of data

[53] Carlton/Sider Decl., ¶ 4.
[54] *Ibid*., ¶ 4; *see especially* n. 1.
[55] Carlton/Sider Decl., ¶¶ 46, 50-51.

concerning "forward-looking market shares" in any of the Applicants' filings to date with this Commission. The Applicants have not even attempted to define the relevant markets for analysis.[56]

At this point in time, the Commission has no information from the Applicants on the actual level of competition in California, even for large business, absent AT&T. Even a cursory review of SBC's internal market share assessment as recently as year-end 2004 clearly indicates that AT&T is SBC's major competitor—and often the only competitor that SBC bothers to consider.[57]

A preliminary review of the data obtained from SBC in discovery suggests that a complete analysis will likely reveal the merger to have seriously adverse effects on competition, based on the measures that economists traditionally use to make such an assessment. Quantitative analysis of the competitive effects of mergers typically follows the *Horizontal Merger Guidelines* published by the Department of Justice and Federal Trade Commission. According to these *Guidelines*,

> Market concentration is a function of the number of firms in a market and their respective market shares. As an aid to the interpretation of market data, the Agency will use the Herfindahl-Hirschman Index ("HHI") of market concentration. The HHI is calculated by summing the squares of the individual market shares of all the participants. Unlike the four-firm concentration ratio, the HHI reflects both the distribution of the market shares of the top four firms and the composition of the market outside the top four firms. It also gives proportionately greater weight to

[56] Indeed, even where Applicants have argued in their Application that the merger is necessary to respond to "Marketplace Changes," they retreat when asked to identify the markets to which they intended to refer by stating that they actually did not mean any real or particular market at all. SBC Response to TURN 1-12.

[57] Attachments to SBC response to TURN Data Request 1-3, at *e.g.*, 000137, 000142, 000145, 000150, 000160, 000161, 000163, 000233, 000226 and 000227.

> the market shares of the larger firms, in accord with their relative importance in competitive interactions.[58]

The highest possible HHI occurs in a monopoly market in which a single firm has a 100% market share. The HHI in that case is 10,000 (100^2). For purposes of merger analysis, the Department of Justice and Federal Trade Commission have divided markets into three categories, depending on the post-merger HHI.

> The Agency divides the spectrum of market concentration as measured by the HHI into three regions that can be broadly characterized as unconcentrated (HHI below 1000), moderately concentrated (HHI between 1000 and 1800), and highly concentrated (HHI above 1800). Although the resulting regions provide a useful framework for merger analysis, the numerical divisions suggest greater precision than is possible with the available economic tools and information. Other things being equal, cases falling just above and just below a threshold present comparable competitive issues.[59]

These categories help to put the current California markets into perspective. Any market in which SBC has a market share of 43% or more falls into the "highly concentrated" category, regardless of the market shares of the remaining competitors.[60] There are few, if any, telecommunications markets (however defined) within the boundaries of SBC California's service territory in which it is plausible that SBC California and/or its affiliates (including AT&T, post-merger) will not have a "forward-looking" market share of at least 43% in the near-term. Thus, it is likely that the Commission's analysis of competition effects of the proposed merger would take place

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[58] Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines*, Section 1.5, (citation omitted), available online at http://www.usdoj.gov/atr/public/guidelines/horiz_book/15.html (*Horizontal Merger Guidelines*).

[59] *Ibid.*

[60] At 43%, SBC's market share alone would produce an HHI of 1,849 (43^2). Because the HHI is the sum of the squares of the market shares of all market participants, a market can be highly concentrated even if the largest firm's market share is less than 43%. For example, a market in which five firms each have a market share of 20% would have an HHI of 2,000 ($5*20^2 = 2,000$).

entirely within the confines of the *Horizontal Merger Guidelines* for highly concentrated markets.

The *Guidelines* for assessing competitive impacts of mergers in highly concentrated markets include the following "general standards":

> Post-Merger HHI Above 1800. The Agency regards markets in this region to be highly concentrated. Mergers producing an increase in the HHI of less than 50 points, even in highly concentrated markets post-merger, are unlikely to have adverse competitive consequences and ordinarily require no further analysis. Mergers producing an increase in the HHI of more than 50 points in highly concentrated markets post-merger potentially raise significant competitive concerns, depending on the factors set forth in Sections 2-5 of the Guidelines. Where the post-merger HHI exceeds 1800, it will be presumed that mergers producing an increase in the HHI of more than 100 points are likely to create or enhance market power or facilitate its exercise. The presumption may be overcome by a showing that factors set forth in Sections 2-5 of the Guidelines make it unlikely that the merger will create or enhance market power or facilitate its exercise, in light of market concentration and market shares.[61]

To put these *Guidelines* into perspective, consider the hypothetical highly concentrated market shown in the table below in which the pre-merger SBC has a "forward-looking" market share of 80% and the pre-merger AT&T has a "forward-looking" market share of 3%.

Pre-Merger "Forward-Looking" Market Shares

Firm	Pre- Merger Market Share	Post-Merger Market Share
SBC	80	83
AT&T	3	N/A
Firm 3	8	8
Firm 4	5	5
Firm 5	4	4
HHI	6,514	6,994

[61] *Horizontal Merger Guidelines*, Section 1.51.

In this hypothetical, the post-merger HHI of 6,994 exceeds the pre-merger HHI of 6,514 by 480 (6,994-6,514). Hence, even though AT&T would be the smallest of SBC's competitors in this hypothetical, with a seemingly trivial "forward-looking" market share of 3%, SBC's acquisition of AT&T would result in a change in the HHI that far exceeds the *Horizontal Merger Guidelines*' threshold of 100 for a presumption that the merger is "likely to create or enhance market power or facilitate its exercise."[62] Of course, the *Guidelines* specify that there could be mitigating circumstances that would reverse this conclusion—but that would require a specific analysis of the type that the Applicants have not presented thus far.

Although this example is a hypothetical one, the circumstances presented are by no means atypical of today's California telecommunications markets. Exhibit 2 presents similar, preliminary analyses using data provided by SBC in discovery. The "markets" analyzed rely on categories that SBC itself used in its internal analysis of competition and may not correspond to the product and geographic markets that Joint Intervenors would propose, given an opportunity to conduct a full analysis of the issue. Nonetheless, the data currently available for three such "markets" provide the Commission with a valuable insight into the likely competitive issues that would surface, given a full investigation of the merger application, including hearings.

Specifically, Exhibit 2 shows that the "local residential" market is highly concentrated (post-merger HHI greater than 8,000) and that the nearly 1,200-point increase in market concentration due to the merger substantially exceeds the 100-point threshold in the *Horizontal Merger Guidelines*. Similar results obtain for the "local small business" market (post-merger HHI greater than 7,600; HHI increase greater than 1,100)

[62] *Ibid.*

and the "large business" market (post-merger HHI greater than 5,800; HHI increase roughly 1,000). The degree of post-merger concentration in each of these "markets" and the magnitude of the increase in competition resulting from the combination of SBC and AT&T's pre-merger market shares makes it very likely that even a "forward-looking" analysis in which AT&T's market share was presumed to be much smaller than its current share would produce a quantitative result indicating that the merger is "likely to create or enhance market power or facilitate its exercise."[63]

Therefore, the Commission cannot approve the application without first obtaining (through the hearing process) the highly relevant information needed to determine whether the new entity will have market power in any appropriately defined geographic or product market within California and determining whether the proposed transaction might require mitigation measures, such as the reclassification of some service.

2. The Applicants have failed to prove that AT&T's decision to exit the residential market is irreversible and have failed to consider AT&T's role as a potential re-entrant providing service to residential and small business customers.

The Applicants' claim that the proposed transaction will not adversely affect competition rests in large part on their contention that there is little overlap between the markets currently served by SBC and AT&T in California. This lack of overlap is the alleged result of what they call "AT&T's unilateral and irreversible pre-merger decision in 2004 to cease actively marketing local and long distance service to mass market customers."[64] The declaration of AT&T's chief financial officer and vice chairman, which is the supporting documentation on which the Applicants rely for this claim, never

[63] *Ibid.*
[64] Supplemental Joint Application, p. 8, citing Horton Decl., ¶¶ 2-7.

states that AT&T's decision to cease actively marketing local and long distance service to mass market customers is, in fact, irreversible.

Even if one accepts that AT&T has, for the present, ceased active marketing to residential and small business customers, it does not follow that the proposed transaction has no adverse effect on competition for residential and small business customers. To the contrary, the proposed transaction eliminates AT&T as both an actual and a ***potential*** competitor of SBC for residential and small business customers. AT&T's apparent current strategy of exiting the mass market does not eliminate all of the company's many assets as a potential competitor for residential and small business customers in California. AT&T as a stand-alone company would continue to have the unique benefit of a trusted brand name that many consumers, even today, associated with "The Phone Company"—a brand association and loyalty acquired during decades in which AT&T held the exclusive monopoly franchise to provide local and long-distance services to customers in what is now the SBC California service territory. Moreover, a stand-alone AT&T would retain assets such as AT&T Labs. The Applicants' own evidence indicates that ongoing research initiatives of AT&T Labs have significant potential applications in the residential and small business markets.[65] Also, SBC itself has argued that the switches (together with collocation and transport facilities) that AT&T uses to provide enterprise services must be considered as providing potential facilities-based competition in the mass-market as well. The Federal Communications Commission ("FCC") relied in part on this very argument to reach its conclusion that SBC and other ILECs no longer should

[65] Application, Exhibit 3, Declaration of Hossein Eslambolchi, ¶¶ 7-14. *See, for example*, ¶ 7 ("Breakthroughs that AT&T achieves in R&D aimed at developing new enterprise services, or providing those services more efficiently, often will have relevance to other services that could potentially be offered over AT&T's network facilities, to the mass market and small business.").

be required to offer unbundled switching at prices based on Total Element Long Run Incremental Cost ("TELRIC").[66] It is beyond ironic, therefore, that the Applicants now cite that FCC decision (and AT&T's subsequent decision to cease actively marketing services to residential and small business customers) as evidence that AT&T should not be counted as a competitor of SBC in the residential and small business markets. If SBC now believes that AT&T (and, presumably, other similarly situated switch-based competitors) cannot economically provide service to mass-market customers via those switches, it should join this Commission in seeking a reversal of the FCC's *Triennial Review Remand Order*, which is based in part on SBC's own contentions to the contrary.

3. The Applicants' suggestion that AT&T's strength in the large business market would compensate for SBC's relative weakness is not true in California—it is a smokescreen to hide a substantial concentration of market power

Applicants spend little time discussing (and provide no factual data regarding) how the proposed merger will affect competition in the market for medium and large business in California. Instead, they provide vague, positive statements concerning how SBC's acquisition of AT&T will help SBC compete for large business accounts nationwide. Both companies are (so far) silent regarding how the merger might affect competition for business telecommunications services ***in California***.

AT&T claims *****BEGIN PROPRIETARY**

[67]

[66] FCC, WC Docket No. 04-313, In the Matter of Unbundled Access to Network Elements, and CC Docket No. 01-338, Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, *Order on Remand*, FCC 04-290, rel. Feb. 4, 2005, ¶ 209 (FCC *TRO Remand Order*).
[67] AT&T Response to TURN Data Requests 1-1 to 1-5.

.[68] **END PROPRIETARY*** Thus, the Applicants' claim that merging SBC and AT&T would do anything more than bolster and consolidate SBC's dominance of the business market in California is smoke and mirrors.

4. The Applicants have failed to establish that intermodal competition mitigates the competitive harms that might otherwise result from the proposed transaction

The Applicants also provide superficial claims that wireless and VoIP provide meaningful competition for SBC California's residential and small business services[69] without bothering to supply the Commission with meaningful information regarding how much of those markets they already control—despite the fact that they must have that information readily available.

The Applicants' claims concerning intermodal competition fail to recognize that wireless and cable-based services often serve as complements, rather than substitutes, for SBC's own services to residential and small business customers. For example, although customers do make long-distance calls using their cellular phones that might otherwise have traveled over the circuit-switched network, they tend to buy both basic wireline local exchange service ***and*** wireless service, rather than substituting wireless service for a landline. In fact, in authorizing Cingular Wireless to purchase AT&T Wireless, the FCC stated that there is a "…limited level of wireless-wireline competition at this point in time"[70], and that "a relatively limited number of mass market consumers have chosen to

[68] Attachments to SBC Response to TURN Data Request 1-3, at *e.g.*, 000137, 000142, 000145, 000150, 000160, 000161, 000163, 000233, 000226 and 000227.
[69] Application, pp. 27-28.
[70] In the matter of Applications of AT&T Wireless Services, Inc. and Cingular Wireless Corporation For Consent to Transfer Control of Licenses and Authorizations File Nos. 0001656065, *et al.* WT Docket No. 04-70; and Applications of Subsidiaries of T-Mobile USA, Inc. and Subsidiaries of Cingular Wireless

substitute one service [wireless] for the other [wireline]."[71] The FCC also recently concluded, "Although we recognize that limited intermodal competition exists due to VoIP offerings, we do not believe that it makes sense at this time to view VoIP as a substitute for wireline telephony."[72]

Moreover, the Applicants' evidence concerning intermodal competition is not specific to California. This is significant because the California experience with intermodal competition is not necessarily the same as the national experience. As one example, nationally, digital subscriber line (DSL) services provided over ILEC-owned facilities had to pay catch up with cable modem services, whereas in California, DSL jumped to an early lead.[73]

Also, the Applicants' claims of intermodal competition substituting for wireline services fail to recognize that SBC itself—through its Cingular Wireless joint venture—is the largest provider of wireless services. Hence, any analysis of wireless as a competitive substitute must take into account that many, if not most, consumers who substitute an SBC wireline for a wireless line are merely transferring revenue between departments within SBC.

Perhaps most ironically, the Applicants both claim the acquisition of AT&T's VoIP platform as a major benefit of the merger and simultaneously rely on the supposed

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Corporation For Consent to Assignment and Long-Term *De Facto* Lease of Licenses File Nos. 0001771442, 0001757186, and 0001757204 WT Docket No. 04-254; and Applications of Triton PCS License Company, LLC, AT&T Wireless PCS, LLC, and Lafayette Communications Company, LLC Fo r Consent to Assignment of Licenses File Nos. 0001808915, 0001810164, 0001810683, and 50013CWAA04 WT Docket No. 04-323, Memorandum Opinion and Order, October 26, 2004, ¶ 238 (Cingular/AT&T Order).

[71] *Ibid*., ¶ 239.

[72] FCC *TRO Remand Order*, ¶ 39, n. 118.

[73] *Comments of the People of the State of California and the California Public Utilities Commission* before the Federal Communications Commission in CC Docket No. 01-338 *et al.*, In the Matter of Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers ("Triennial Review Proceeding"), April 5, 2002, pp. 7-8.

inevitability of VoIP as an emerging source of significant intermodal competition in the future. However, AT&T has not retreated from the consumer market as a VoIP competitor. To the contrary, SBC's own analysis indicates that AT&T is *****BEGIN PROPRIETARY END PROPRIETARY***** in this market.[74] The Applicants again make no effort to provide information concerning how the elimination of AT&T as a VoIP competitor in the consumer (or any) market will affect SBC's current or "forward-looking market share." It is possible, if not likely, that the proposed merger will eliminate SBC's biggest potential competitor in the VoIP market. Yet, the Applicants provide no information concerning this aspect of the proposed merger. As the merger itself will have an unknown affect on what VoIP competition emerges in the future, the Commission should disregard the Applicants' claim that VoIP presents a serious competitive alternative today. Moreover, any consideration of VoIP as a competitive alternative in any business market the foreseeable future should be dismissed given *****BEGIN PROPRIETARY** [75] **END PROPRIETARY*****

For all of these reasons, the Commission must hold hearings to determine the extent (if any) to which intermodal competition is sufficient to mitigate the competitive harms of the proposed transaction. Certainly, the Applicants have not provided convincing, California-specific evidence to date.

[74] Attachment to Applicants' Response to TURN Data Request No. 1-3, p. 000192.
[75] *Ibid.*, p. 000215.

5. The Applicants have failed to provide any analysis whatsoever of the profound effects of the proposed transaction on the cost structures of SBC and AT&T as long-distance providers and the effects of those cost changes on long-distance competition

The Applicants' submissions to date contain no analysis whatsoever of acquisition-related cost changes (some of which are California-specific) that make it likely the proposed transaction will, in fact, adversely affect competition, especially for long-distance services. These changes to the combined company's cost structure include the internalization of access charges and the ability of SBC's long-distance operations to use AT&T-owned facilities. Indeed, it appears that the Applicants intend to argue that these very real and likely very substantial effects of the proposed merger are irrelevant to the Commission's evaluation, as they have refused to respond to data requests seeking basic information about the level of services the companies currently obtain from each other in California.[76]

With the exception of SBC California's own intraLATA toll operations, all long-distance providers that originate or terminate calls to a customer premises over a loop that SBC California uses to provide retail local exchange services to that customer must pay access charges for the use of that "last mile" connection. These access charges become a direct economic cost to the long-distance providers and can constitute a significant proportion of the total cost of providing long-distance services. Applicants notably dodged providing any direct reply to repeated questions concerning this issue in their initial conference with analysts.[77]

The competitive significance of the cost associated with access charges depends on whether the long-distance provider is affiliated with SBC. AT&T has asserted

[76] Applicants' Objections to TURN Data Requests 1-46 through 1-54.
[77] Attachment to Applicants' Response to TURN Data Request No 1-8, pp. 000634-000636.

elsewhere that the current access charges include a markup over the direct incremental cost to SBC California of providing access services, and it is likely that markup is significant.[78] SBC California does not have to bear the markup cost at all when it provides intraLATA toll services; instead, it only incurs the direct incremental cost of access. The markup also is largely irrelevant when SBC California provides access services to an SBC affiliate because the markup portion of the access charges simply goes from one corporate pocket (the affiliated long-distance provider) to another (SBC California) without changing total company costs and profits. But, the markup substantially increases the direct economic cost of all unaffiliated long-distance providers and reduces their profits from selling long-distance services. Significantly, as a result of this merger, AT&T will become an affiliate of SBC California. Any markup that AT&T pays to SBC California for access services simply will transfer dollars in an accounting sense between the AT&T portion of the merged entity and SBC California. The total corporate costs and profits of the merged entity, ***i.e., what shows up in its annual report to shareholders,*** will be unaffected by the markup that AT&T pays to SBC California for access services, giving AT&T a significant competitive advantage over other, unaffiliated IXCs. Should SBC's mark-up on access be a significant portion of the cost structure of competitors providing intrastate long distance within California (which is very likely to be the case given that SBC controls the majority of access lines in California), a merger that makes this cost effectively vanish from the cost structure of the former AT&T would place remaining competitors at a serious disadvantage.

[78] *See, for example,* Response Testimony of Richard N. Clarke in R.03-08-018, Phase II (filed March 7, 2005), pp. 3-4. Residual access charge markups are likely to be significant because access rates have historically been set deliberately high in order to provide incumbents such as SBC with support (*i.e.*, subsidy) to support universal service. This Commission is currently considering one step to set access rates closer to cost, but it is only dealing with a fraction of the overall access charge.

SBC's current California interLATA operations also will benefit from the merger because SBC will be able to use AT&T's existing California interLATA facilities, eliminating the need for SBC to lease interLATA facilities throughout much of the state. Thus, the costs incurred by SBC's California interLATA operations will decrease significantly, giving the combined utility another massive economic advantage relative to remaining IXCs. Indeed, SBC apparently values *****BEGIN PROPRIETARY**

.[79]

[80] **END PROPRIETARY***** Such comments merely hint at the true magnitude of the advantage that a merged ILEC and IXC will have over all existing and potential competitors. Eliminating those costs, should they be substantial, will be another advantage that is not available to any company that is not the result of combining a major ILEC and IXC.

As the above discussion illustrates, the change in the combined AT&T/SBC economics relative to the remaining IXCs is profound. If IXCs do not show up to protest, the Commission should take that as a sign that a group of companies on which the Commission has long relied to create a competitive environment has effectively vanished.

[79] Attachment to Applicants' Response to TURN Data Request No 1-8, p. 000747.
[80] *Id.*, pp. 000634-000635.

The reassembly of Ma Bell makes it less likely that the Commission can rely on competition to protect ratepayers (indeed, it may even reverse the conditions that led the Commission to declare AT&T nondominant in the California interLATA market).[81]

C. Section 854(c) has eight criteria that the Commission must consider "inclusive" to find that, "on balance," the transaction is in the public interest. The Applicants have failed to meet this standard.

Pursuant to Section 854(c), the Commission's evaluation of a proposed merger must include consideration of each of eight different criteria. Specifically, the Commission must consider whether the Applicants' merger proposal will:

(1) Maintain or improve the financial condition of the resulting public utility doing business in the state;

(2) Maintain or improve the quality of service to public utility ratepayers in the state;

(3) Maintain or improve the quality of management of the resulting public utility doing business in the state;

(4) Be fair and reasonable to affected public utility employees, including both union and nonunion employees;

(5) Be fair and reasonable to the majority of all affected public utility shareholders;

(6) Be beneficial on an overall basis to state and local economies, and to the communities in the area served by the resulting public utility;

(7) Preserve the jurisdiction of the commission and the capacity of the commission to effectively regulate and audit public utility operations in the state; and

(8) Provide mitigation measures to prevent significant adverse consequences which may result.

[81] In D.97-08-060, the AT&T non-dominance order, market share data reviewed consisted of total share of intrastate MOUs and "transmission capacity," with the Commission finding that "AT&T's competitors now control 80% of the active capacity in the state." AT&T also claimed it was at 49% share of revenues, 55% share of minutes and 66% share of presubscribed lines—showing in part that it was losing high revenue/high call volume customers. The Commission found that it should continue to monitor AT&T's earnings until such time as the ILECs entered the interLATA market. Given the collapse of that safeguard as AT&T will now effectively become the ILEC, a reversal would be appropriate.

Any Commission decision approving such a merger must make a finding that, "on balance" (taking into account the Commission's findings on all eight of these criteria), the transaction is in the public interest.

As Joint Intervenors will explain in detail below, Applicants have failed to make the required showing that the proposed merger transaction would meet the public interest standard of Section 854(c). Hence, the Commission cannot and should not approve the merger as currently proposed.

1. The Applicants' own claims concerning the effect of the merger on the financial condition of the resulting public utility, if true, merely provide evidence that the Applicants have failed to identify and quantify all sharable merger benefits.

To satisfy the first criterion of Section 854(c), the Applicants must show that the effect of the proposed transaction would be to "maintain or improve the financial condition ***of the resulting public utility doing business in the state***."[82] The Applicants in their Joint Supplemental Application argue that the proposed merger would meet this standard because the proposed merger "will likely assure broader and more productive uses of AT&T assets and capabilities"[83] and "the transaction will improve access by lowering costs of capital."[84] Both of these arguments focus on the effect of the proposed transaction on ***AT&T*** and are entirely silent concerning the acquisition's effect on SBC California, which indisputably will be "the resulting public utility doing business in the state" (perhaps alone and perhaps in conjunction with an AT&T California subsidiary). Thus, by virtue of their silence concerning the effects of the merger on SBC California, the Applicants simply have failed to make the required showing under Section 854(c)(1).

[82] P.U. Code Section 854(c)(1), emphasis added.
[83] Joint Supplemental Application, p. 9.
[84] *Ibid.*, p. 10.

Elsewhere, SBC has been more forthcoming about the effects of its acquisition on SBC (and, by inference, its California operating company, SBC California). In its Investor Briefing No. 246 announcing the acquisition of AT&T, SBC claimed that:

> SBC expects the transaction will be cash flow positive in 2007 and earnings per share positive in 2008 — both growing in the years thereafter. Positive cash flow from the acquired business is expected to provide additional financial flexibility for SBC over the next several years.
>
> AT&T currently has approximately $6 billion in net debt and SBC has $26 billion, excluding debt at Cingular Wireless. SBC expects free cash flow after dividends from the combined companies to provide the flexibility to continue to reduce combined debt levels over the next five years while providing excellent cash returns to stockholders.[85]

If this claim is true, then it appears likely there is no basis for failure to meet the first criterion of Sec. 854(c). However, the Applicants have not identified this projected merger benefit as being included in their estimate of California-specific merger savings pursuant to Sec. 854(b)(2). The Applicants cannot have it both ways. If the merger will improve the financial condition of SBC, that is a quantifiable merger benefit that must be shared with ratepayers.

2. The Applicants have failed to demonstrate that the proposed transaction will maintain or improve the quality of service to public utility ratepayers in the state.

The Applicants' public statements concerning the savings that investors will enjoy from this proposed merger suggest that the majority of savings will come from personnel reductions. Another large source of savings will supposedly come from the consolidation of the order processing and network management systems of the two companies. Slashing employees, while at the same time changing over internal infrastructure, is

[85] "SBC To Acquire AT&T, Creates Premier, Global Provider for New Era of Communications," *SBC Investor Briefing No. 246*, January 31, 2005, p 3.

practically a recipe for service quality failures. The Applicants offer no evidence that, after the employee reductions that are necessary to satisfy investors' demands for a merger of this scale, they will be able to maintain existing service quality in California (let alone improve it).

Moreover, given that the merger will significantly increase market concentration, it will reduce the Applicants' incentive to maintain service quality and increase the Applicants' ability to compel consumers to purchase unwanted service bundles, at an exorbitant price, simply to obtain high-quality basic service. These effects will be particularly strong in underserved markets or market segments with no (or few) effective competitive options (*e.g.*, rural and other neighborhoods without cable telephony, the small business market, low-income and minority neighborhoods). In those markets, the Applicants will have every incentive to cut back on maintenance of basic services and divert resources to, for example, building out broadband in affluent areas. The Applicants are notably silent on the issue of whether they will give equal emphasis to building out broadband facilities for underserved communities such as low-income, minority and rural customers. The Commission must therefore hold hearings to determine the effect of the merger on service quality for both basic and advanced services to all consumers in California. The Commission also requires hearings to determine whether merger conditions are necessary to guard against an overall service quality decline, to prevent the merged entity from compelling consumers to purchase unwanted bundles and to ensure that all consumers benefit from network quality improvements, such as the build-out of broadband facilities.

3. The Applicants have failed to demonstrate that the proposed transaction will be fair and reasonable to affected public utility employees, including both union and nonunion employees.

So far, the Applicants have refused to provide any information at all concerning how the merger will affect California employment. SBC asserts that "it is premature to determine" if its current force count in California will change as a result of the merger.[86] AT&T likewise declines to provide any information regarding likely force changes.[87] Given that the billions in projected merger savings are primarily driven by employee reductions, it is implausible that the merger will not affect employment in California. Given that the Applicants have so far refused to provide any information whatsoever regarding how employees in California will be affected by the merger, the Commission cannot possibly conclude that the merger would be fair and reasonable to employees without hearings.

The Commission should hold hearings to examine not only overall changes in employment as a result of the merger, but also to consider how the merger will affect diversity in the workplace, as well as supplier diversity.[88] Will the merger disproportionately disadvantage women and minority employees or older employees? The Applicants' total silence on the question of employment changes makes it impossible to answer such questions.

Applicants are also totally silent on the issue of executive compensation and executive compensation reporting, an issue has direct and indirect effects on various aspects of the merged company. For example, excessive executive compensation can

[86] SBC Response to TURN Data Request 1-20.
[87] AT&T Response to TURN Data Request 1-20.
[88] SBC recently achieved nearly 25% supplier diversity, a goal that Greenlining has contended all utilities can and should reach within five years.

have a detrimental impact on the cost structure of the merged company, the fairness of treatment received by middle-management and other utility employees, and union negotiations.[89] PG&E addressed this problem by adopting the most transparent executive compensation reporting model currently employed by any Fortune 500 company in the nation.[90] However, Applicants are silent as to how they will address this important issue.

The Commission cannot conclude that the merger will be fair and reasonable to public utility employees without knowing which employees will be affected by merger-related layoffs; thus, hearings are essential to determine whether the merger satisfies the requirements of Section 854(c)(4) and whether the Commission must impose conditions on the merger to ensure fair treatment of employees and diverse suppliers. Furthermore, given the importance of these issues, as well as the market concentration that this merger could create, Applicants' CEOs should be available for cross-examination on these and other important public interest issues.

4. The Applicants have failed to demonstrate that the proposed transaction will be beneficial on an overall basis to state and local economies, and to the communities in the area served by the resulting public utility.

As established above, the merger will seriously diminish the competitive alternatives available in California today. Decreased competition is harmful to the state and local economies and to the communities served by the resulting public utility. As

[89] *See* A.02-11-017, Michael Phillips' Testimony at 6:20, 7:9-12 (filed May 1, 2003). At least one Commissioner apparently agrees with this perspective. Commissioner Geoffrey Brown stated that when a utility awards its executives large bonuses, the disclosure of the bonuses could negatively impact union negotiations. For example, SBC recently boosted its top California executives' pay by an average of 19% although the company's philanthropy decreased by seven percent. In response to SBC's announcement of their executives' raises, Commissioner Brown said, "I think that type of disclosure will have some impact on their negotiations with the [union]. I am seeing the union go to bat for the company (in lobbying regulators), but at the same, they are resentful of salaries to executives." "SBC Brass Take Home Big Raises," *San Francisco Chronicle*, April 16, 2004.

[90] *See* R.03-08-019, Joint Petition of the Greenlining Institute and PG&E (filed January 30, 2004).

also established above, the merger will fundamentally change the economic viability of providing interexchange toll service for any remaining competitors (and by extension, given the customer demand for bundles, the viability of competing in the overall telecommunications market). The Applicants have not made a serious effort to present the Commission with the information it needs to evaluate these effects of the proposed merger and have suggested no mitigation measures as required by 854(c)(8).

Moreover, by proposing that half of the economic benefit to California ratepayers from the supposed several billion dollars in merger-generated savings is only a few million dollars, the Applicants suggest both that the merger savings in California are not likely to offset the competitive harms and that the merger savings may be exported to Texas and beyond, rather than staying in California to benefit the state and local economies, as required. Absent Commission action, there can be no certainty that ratepayers will receive half of the relevant merger benefit. The Commission cannot rely on the Applicants' vague promise that "SBC expects" higher capital spending to result from the merger as Applicants refuse to commit that even a dime of the expected additional spending would occur in California.

In addition, if the Commission were to rely entirely on competition to deliver merger benefits to ratepayers, those benefits would flow disproportionately to the customers with the most competitive options. Underserved communities such as low-income, minority, disabled and rural customers could expect to see few, if any, tangible benefits from the merger. Applicants also make no mention of community development funding. Thus, the Commission must hold hearings to ensure that the direct financial and

indirect benefits of the merger flow to ***all*** consumers in all parts of the state, including those in underserved communities.

Finally, the Applicants have been silent concerning the level of corporate philanthropy that the merged entity will provide. This includes total silence on President Michael Peevey's suggested philanthropy model of cash philanthropy equal to 2% of pre-tax earnings, with 80% of that being awarded to underserved communities. The Commission therefore must hold evidentiary hearings to determine whether the communities served by the resulting public utility will be adversely affected by a reduction in corporate philanthropy, contrary to the requirements of Section 854(c)(6).

5. The Applicants have failed to demonstrate that the proposed transaction will preserve the jurisdiction of the commission and the capacity of the commission to effectively regulate and audit public utility operations in the state.

The proposed merger adds to the complexity of SBC's affiliate transactions, which already are difficult to regulate and audit. Given SBC's opposition to further comprehensive audits,[91] this is a serious concern. As discussed below, there are already signs in this proceeding that the Applicants intend to act in a manner that makes efficient regulation more difficult than ever. Further, in addition to eliminating SBC's primary existing competitor in California, the merger will eliminate an important source of information and balance for the Commission itself. For several years, AT&T has been perhaps the most significant, if not the only, competitor in California with the resources to monitor and participate in a broad range of Commission telecommunications proceedings and with the resources to seriously examine the more complex claims (such

[91] *See, for example*, Response of Pacific Bell Telephone Company (U 1001 C) to the Petition of Verizon California Inc. to Modify Decision 02-10-020 (filed March 10, 2005) in R.01-09-001/I.01-09-002.

as cost models) put forth by SBC and Verizon. To maintain a balance of voices in regulatory proceedings absent AT&T may require new regulatory mechanisms.

Finally, we note that the Commission needs much better monitoring if it is ever going to know if whatever merger promises and conditions are eventually made or required are ever actually met. Better monitoring is necessary to avoid a repeat of the SBC/Telesis merger "California Commitments" in which the applicants to that merger made numerous promises such as that the merger would create 1,000 new jobs in California, but delivered no means of ever determining if those promises were fulfilled.

For all of these reasons, approval of the merger would, at a minimum, require mitigation measures thus far not proposed by the merging parties, contrary to the requirements of Section 854(c)(8).

6. The Applicants have failed to provide mitigation measures to prevent significant adverse consequences which may result from the proposed transaction

As discussed above, the Applicants have failed to propose any mitigation measures. Mitigation needed to prevent significant adverse consequences to service quality, competition (and thereby the state and local economies of California), and the Commission's ability to regulate the increasingly complex corporate structure of SBC.

Unlike the SBC/Telesis merger and the Bell Atlantic/GTE merger, this merger is a consolidation of two carriers that both already have a substantial presence in California. Hence, this merger is likely to do more to reshape the California telecommunications landscape than either prior merger. Applicants' theory is not much more sophisticated that the mantra "bigger is better." At some point, however, bigger must become worse—particularly if the Commission's intention is to rely on competition to reduce the need for

regulation. The Commission needs to determine the point at which bigger becomes worse (or at least how to monitor for signs that the point has been reached) before approving this merger.

IV. PROCEDURAL ISSUES

A. Categorization and need for hearings

While Joint Intervenors agree with Applicants that this proceeding should be categorized as ratesetting, we disagree with Applicants that hearings are not necessary. As Joint Intervenors have discussed above, evidentiary hearings are absolutely required in this proceeding so that the Commission can ensure that the mandates of Section 854 are met. We have identified facts that Joint Intervenors would present at a hearing in support of our request for denial of the Application as currently presented. An illustrative, rather than exhaustive, summary of those facts in dispute includes:

- Whether SBC retains substantial ability to exercise market power and whether SBC's ability to exercise market power would be enhanced by the proposed merger;
- Whether the combined SBC/AT&T will have market power in any appropriately defined geographic or product market within California and whether the proposed transaction might require mitigation measures, such as the reclassification of some services;
- Whether intermodal competition is sufficient to mitigate the competitive harms of the proposed transaction;
- Whether Applicants have dramatically understated the portion of the total merger benefits that should be attributed to their California operations;

- What is the appropriate level of California-specific merger savings and the appropriate allocation of those savings;
- Whether the proposed merger will improve the financial condition of SBC;
- Whether the merger will likely harm California in other respects, such as diminishing the level of corporate philanthropy and/or the manner in which advanced services are deployed, that require mitigating conditions;
- Whether the proposed merger will negatively impact service quality for both basic and enhanced services for all California consumers and if so what conditions are necessary to mitigate any harmful effects; and
- Whether the proposed merger will have a negative impact on public utility employees.

B. Proposed schedule

Although the Applicants ask for an extremely accelerated schedule in this docket, their actions so far have already ensured that a quick proceeding will not be possible. First, as discussed extensively above, despite the Assigned Commissioner's explicit direction to submit a filing making a proper showing concerning how the merger supposedly complies with § 854, the Applicants have again made no serious attempt to do so. For example, the Applicants did not provide any factual data concerning how the merger will affect market concentration in California, how it will affect employment in the state or what level of merger-related benefits is specifically attributable to the California operations of SBC and AT&T.

Second, perhaps illustrating the regulatory difficulties that will ensue should the merger be approved, the Applicants have manifested a new and uniquely combative and

restrictive approach to discovery (not that SBC was ever particularly cooperative in the past). Such behavior is particularly revealing in this instance as it is the Applicants that have requested an expedited and extreme schedule. It is as much or more in their interests now than it will be in future cases for them to disseminate information quickly. Indeed, it would seem strongly in the Applicants' best interest to take all reasonable steps to avoid lengthy discovery battles or create conditions that will cause parties to need substantially more time that usual to develop their comments or testimony.

However, that has not been the case. Instead, the Applicants have made it as difficult as possible for parties to begin evaluating the proposed merger's compliance with § 854. Most significantly, the Applicants have refused to provide copies of the model and supporting documentation underlying their estimate of merger savings.[92] The Applicants object to providing the basis for their expected merger savings because "the request is overbroad and requires the production of information that is not relevant or material to the subject matter of this proceeding and not reasonably calculated to lead to the discovery of admissible evidence" and because the "burden on Applicants of attempting to produce the highly proprietary information requested far outweighs any potential relevance it might have."[93]

The basis for the Applicants' estimate of merger savings is, rather obviously, central to evaluation of the proposed merger's compliance with § 854. Such documents were readily provided in response to discovery in both the SBC/Telesis merger and the Bell Atlantic/GTE merger.

[92] SBC Response to TURN Data Request 3-2.
[93] *Ibid*.

The Applicants also refuse to produce copies of the basic existing documentation that was reviewed internally by the Applicants' management concerning the purpose and expected value of the merger. Instead, the Applicants have asserted that those documents merit the highest possible, "no copies" level of protection, which would mean that parties must travel to SBC's offices to look at a paper copy of those documents. That policy would prevent this basic merger information from becoming part of the record in this proceeding and would seriously curtail parties' ability to work with and analyze the data therein. It would also make meaningful review of that material take much longer and be much more costly. Again, comparable documents have been made available to parties in prior proceedings without such restrictions.[94]

Moreover, only after "meet and confer" sessions and correspondence have the Applicants belatedly provided usable, electronic copies of any of the documents that they previously have "provided" in response to TURN's discovery requests. Indeed, the Applicants seem intent on wasting as much time as possible supplying essentially useless material. For example, SBC first supplied the attachments to most of its responses to TURN's First Data Request on a CD with each page of material presented as an individual ".tif" file, *i.e.*, as an individual electronic file per page with a picture of each page—2,850 one-page files that TURN would have to open one at a time.

Subsequently, the Applicants provided a paper version of the same material, but without first formatting the printed spreadsheets so that they make sense. Hence, many

[94] SBC's primary reasons for this new and extreme treatment are apparently its presumption that this merger does not *really* involve California utilities and that the documents are so sensitive that they are also closely held within the Applicant companies. The first point is Applicants' legal opinion and not a basis for restricting discovery. The second is a smoke screen. It is obviously premature and inappropriate to disseminate expected merger consolidations within AT&T or SBC. While it may make sense that this data would be closely held within Applicants' organizations as most personnel do not need to know and should not know that information yet, that information is central to issues in this proceeding and to the Commission's obligation to evaluate the consequences.

pages are random selection of numbers on a page with no context at all. Less that a week before protests were due, the Applicants had still not simply put the underlying spreadsheets on a CD and sent them absent any manipulation, which would have saved all parties considerable time. Such behavior suggests that any schedule must provide for substantial time for parties to file motions and slowly wrest relevant data from the Applicants.

Given this established pattern of resistance to discovery and the significance of this Application to the structure of the telecommunications markets in California, Joint Intervenors propose the following schedule:

Joint Applicants Supplement Application Pursuant to Section 854(b)	March 30, 2005
Protest Due	April 14, 2005
Replies to Protest Due	April 29, 2005
Joint Applicants File Opening Testimony	June 15, 2005
Attorney General Statement on Competition	August 15, 2005
Intervenors Reply Testimony	September 30, 2005
Concurrent Rebuttal testimony	October 28, 2005
Hearings	November 28 – December 9, 2005
Opening Briefs	January 6, 2006
Reply Briefs	February 3, 2006

V. CONCLUSION

For the reasons set forth above, Joint Intervenors respectfully request that the Commission hold evidentiary hearings concerning this Application and that the Commission adopt Joint Intervenors' proposed schedule for this proceeding.

Date: April 14, 2005

Respectfully submitted,

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***** REDACTED *****

Exhibit 1

April 14, 2005

***** REDACTED *****

Exhibit 2

April 14, 2005

Exhibit 2 (Redacted)[1]

Illustrative HHI Calculations

Local Residential Market Concentration
(Source: SBC Response to TURN Data Request 1-3, p. 000340)

Firm	Pre-Merger Market Share	Post-Merger Market Share
SBC		
AT&T		
Others		
HHI	6,906.86	8,087.25
Post-merger increase in HHI		1,180.39

Local Small Business Market Concentration
(Source: SBC Response to TURN Data Request 1-3, p. 000413)

Firm	Pre-Merger Market Share	Post-Merger Market Share
SBC		
AT&T		
Others		
HHI	6,477.31	7,605.88
Post-merger increase in HHI		1,128.56

[1] All of the market share data contained in this Exhibit were identified by SBC as proprietary data, subject to the protective order in this proceeding.

Large Business Market Concentration
(Source: SBC Response to TURN Data Request 1-3, p. 000150)

Firm	Pre-Merger Market Share	Post-Merger Market Share
SBC		
AT&T		
Others		
HHI	4,852	5,818
Post-merger increase in HHI		966