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SBC/AT&T AND VERIZON/MCI MERGERS— REMAKING THE TELECOMMUNICATIONS INDUSTRY

HEARING

BEFORE THE

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TUESDAY, MARCH 15, 2005

UNITED STATES SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Committee met, pursuant to notice, at 2:30 p.m., in room SD–226, Dirksen Senate Office Building, Hon. Arlen Specter, Chairman of the Committee, presiding.

Present: Senators Specter, Hatch, DeWine, Cornyn, Coburn, and Kohl.

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

Chairman SPECTER. The hearing on the telecommunications industry by the Judiciary Committee will now commence, the hour of 2:30 having arrived.

Today, like virtually everyday in the Senate, is complicated because we are taking up the budget, a scheduling turn which was not known when this hearing was set. There are five votes scheduled at three o'clock, so we will proceed as best we can and have to recess during the course of the votes. It is not a very unusual problem for our hearings and we will just do the best we can.

This full Committee hearing was set in order to give all of the members of the Judiciary Committee an opportunity to participate and raise questions about this very, very important subject. Customarily, it is a matter left in the hands of the Subcommittee on Antitrust, and after making an opening statement I will turn the gavel over to Senator DeWine, who is the Chairman of the Subcommittee on Antitrust, and to the ranking member, Senator Kohl. But I did want to begin the session because of the importance of the subject.

There is no doubt that mergers and acquisitions are sweeping America in so many, many industries. The communications mergers are vitally affecting very basic service for almost all American consumers, and the question which we have to answer is whether there will be sufficient competition for consumer protection.

A very lengthy statement which I have will be made a part of the record without being read in order to economize on time and I will make just a few brief introductory comments.

In January, SBC Communications, one of the Baby Bells, announced plans to acquire AT&T. Shortly thereafter, Verizon Communications, a successor to three Baby Bells, announced plans to acquire MCI. Another Baby Bell, Qwest, also is bidding to acquire MCI. SBC, Verizon and Qwest all provide local wire line phone service to primarily residential and small businesses. Verizon and SBC also have become major wireless providers. MCI and AT&T continue to provide long-distance services.

These mergers will reunite local phone service providers and long-distance companies. In the meantime, new competitors—cable companies, wireless providers, voice over Internet providers—have come to compete without distinguishing between local and long-distance service.

There are a number of important questions which the Committee and Subcommittee will want to address. Are the other modes of communication sufficient to put competitive pressure on the merged companies? Second, will the merged companies and other wireless companies be able to use their infrastructure to prevent cable and voice over Internet companies from competing? Even if they have access to the infrastructure, will cable companies, independent wireless and voice over Internet providers be strong enough to keep prices of residential and small businesses low?

There has always been a concern since the founding days of the Republic about the size of corporate America. Justice Brandeis expressed it succinctly in *Liggett* v. *Lee* way back in 1933 when he said, quote, "The general laws which have long embodied severe restrictions upon size and upon the scope of corporate activity were in part an expression for the desire for equality of opportunity." A little later in the opinion he really gets tough, saying, quote, "Such is the Frankenstein monster which has been created by their corporation laws." Going back to Jefferson, the warning was about, quote, "banks and corporations will grow up around the people and will deprive them of their property."

We do not live in the time of Jefferson and we do not even live in the time of Brandeis, but we have to be concerned about the tremendous acquisition of power and be sure that consumers are adequately protected.

Shortly after I was elected to the Senate in 1980, the Antitrust Subcommittee held a hearing and Assistant Attorney General Baxter came in. And as is the way with Senate hearings, soon there was just a witness and a Senator, and I had a fascinating experience, fascinating for me, to be able to question the Assistant Attorney General on Antitrust for about two hours. Nobody else was interested. I think it is a record which was unlistened to and unread.

But that was in the era when AT&T and Ma Bell and all the Baby Bells were dismantled, a decision that gave me a lot of qualms when it happened. And now we are here back with a reconfiguration of a lot of moving parts. So these are big, big issues and we want to take a look at them to see if they make sense for America, for continued growth and opportunity and jobs, and if they adequately protect the American consumer.

Let me yield at this time to my distinguished colleague, Senator DeWine, who is Chairman of the Subcommittee.

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

Senator DEWINE. Mr. Chairman, thank you very much for your good statement and for holding this hearing to examine these mergers. These deals have received really an unusual reception in the press and within the industry, an unusually friendly reception and one that I am not really sure is wholly deserved. In fact, one might normally expect that mergers worth $23 billion, combining four of the country's leading phone companies, would raise great concern among those who follow the industry.

But recent changes in the telecommunications industry have given an air of inevitability to these deals. Market pressures and regulatory changes have significantly limited the options of the long-distance carriers, so that AT&T has already announced that it is exiting the market for residential service, and MCI appears headed in the same direction. Under these circumstances, it is not surprising that many have done a quick analysis and concluded that these deals do not pose any significant antitrust concerns.

However, Mr. Chairman, a quick analysis, whatever the outcome, is really not enough and is not adequate. In fact, I think that certainly there are some antitrust issues that require more thorough examination. Perhaps the most obvious area of concern is the so-called enterprise market, that sector of the market comprised of large businesses with sophisticated telecommunications needs. In this market sector, all four of the merging parties currently compete, and so competition there will be affected by these deals. There are also questions regarding the impact of these deals on the markets for long-haul capacity and the market for Internet backbone. These are all areas that we should explore today.

Even beyond these specific market evaluations, however, is the larger competition issue. Certainly, these mergers represent a loss of competition among the phone companies, but the remaining players will tell us that competition is flourishing via different platforms, specifically that we will have cable companies, wireless companies and companies that provide voice over IP services. In other words, so-called intermodal competition will protect competition in these markets. This, I believe, is the key issue—the broader competition issue that this Committee must examine most thoroughly and must consider as the most obvious candidate for Committee action.

For one thing, we must keep in mind that intermodal competition, by definition, does not always provide the type of direct competition that we are used to seeing. Wire line, wireless, cable—these services are inherently different, much like planes, trains and automobiles, all of which provide a similar service, but in different ways, with different pluses and minuses. Not all will always provide sufficient competitive benefits for all consumers.

Further, in this context, we must discuss today whether or not conditions are required in order to ensure that multiple modes of competition are, in fact, available. For example, voice over IP is a very promising product, but is not in and of itself a separate facilities-based form of competition. Instead, it is a type of service that is only available to a consumer if he or she has broadband access, and currently that access is only available from the phone company or the cable company. In order for voice over IP to be a legitimate competitor to the merged companies, must we require the phone companies to sell DSL separately? These are important questions and we must begin asking them today.

On a final note, Mr. Chairman, as you know, only the four merging companies are represented here today. While we anticipate that this hearing will provide the Committee with a good base of knowledge regarding the deals, we all agree that we cannot responsibly conclude our examination without hearing directly from those who are critical of these deals.

Accordingly, with the consent of the Chairman and the full Committee, on April 19 Senator Kohl and I are planning to hold a follow-up hearing in the Antitrust Subcommittee with a panel of noncompany witnesses who have expressed concerns about these mergers. That hearing, which will be essentially part two of today's hearing, will help us to more fully examine these mergers and explore the competitive impacts.

I thank the Chair.

Chairman SPECTER. Thank you very much, Senator DeWine.

Senator Kohl.

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

Senator KOHL. Thank you, Senator Specter.

We are witnessing the most fundamental reshaping of the telecom industry in decades. In the space of a generation, we have gone from the breakup of Ma Bell to what some fear may be its re-creation, at least on a regional level. The breakup of AT&T two decades ago unleashed an explosion of competition and innovation. The competitive forces freed by the ending of the phone monopoly led directly to the introduction of previously unheard of technologies, ranging from the fax machine, the cellular phone, e-mail, to the Internet itself.

Consumers benefitted from a blossoming of new choices and services. Prices for phone services declined so dramatically that what was once an unusual and expensive event—placing a long-distance telephone call—became routine and almost cost-free. The cost to American business of telecom services dropped considerably, helping spur greater efficiencies and growth throughout the economy.

We are now entering a brave new world of telecom competition. The acquisition of AT&T by one of its Baby Bell progeny, SBC, and the likely of acquisition of MCI by Verizon will create two telecom giants, each dominating many services throughout their regions. Should these mergers be consummated, SBC and Verizon will have a market share of about 90 percent of local residential consumers in their regions, 70 percent in long distance, and about 40 to 50 percent in wireless.

These figures give us pause, but we live in an exciting time in the telecom world where the pace of consolidation is matched by the speed of innovation. AT&T and MCI are both declining companies and have already withdrawn from marketing most services to residential consumers. As a result, with the important exception of the business market, there are few remaining areas where SBC competes with AT&T or Verizon competes with MCI.

In addition, new technologies are emerging—services such as Internet-based telephone service and wireless connections to the Internet which may challenge SBC and Verizon, if given a chance. It is our responsibility to ensure that these emerging new technologies have a real chance to succeed. The possible benefits of new competition will drive growth throughout the economy for decades to come.

We must insist that the promise of tomorrow's technology is not stifled in its infancy by today's consolidation, and we must seek to avoid the creation of a world where consumers are left with only two choices for a bundle of telecom services—the Baby Bell phone company and the cable company.

So we have two concerns with these mergers. First, will this consolidation decrease the choices and increase the cost to consumers and to business customers, both large and small? And, second, how can we ensure that new technologies and new services can get access to the SBC and Verizon networks?

A good place to start would be to require that the Baby Bells offer consumers the choice of buying Internet access without also requiring them to buy phone service. We expect to recommend additional specific pro-competitive merger conditions to the Justice Department and the FCC in the coming weeks. Securing merger conditions such as these will help ensure that the tremendous gains in telecom competition over the last 20 years are not lost in the midst of this industry consolidation.

One more comment. As the Senator from Ohio said, I believe it is essential that our Committee hear from competitors and consumers affected by these mergers. We are disappointed that we will not hear any voices besides those of the merging companies today, but instead we will need to return to this topic in a few weeks so that all voices will be able to be represented.

Thank you again, Mr. Chairman, and we look forward to hearing the testimony today.

[The prepared statement of Senator Kohl appears as a submission for the record.]

Chairman SPECTER. Thank you very much, Senator Kohl. That sets the overall parameters.

Senator Cornyn, would you like to make an opening comment?

STATEMENT OF HON. JOHN CORNYN, A U.S. SENATOR FROM THE STATE OF TEXAS

Senator CORNYN. Thank you, Mr. Chairman. Just briefly, of course, I would like to welcome all the witnesses here today. Mr. Whitacre is a constituent of mine and operates his headquarters out of San Antonio, Texas, my hometown, so I wanted to greet him, and all of you, and thank you for being here today.

We understand that this is going to be the beginning of an awfully long process which is primarily going to reside in the FCC and the Department of Justice. So as I understand it, the purpose of this hearing is to be able to understand from the parties involved generally what the impact of these consolidations are going to be on competition, which we understand benefits consumers by keeping prices low, but also on innovation, and I will have a few questions in that regard. I will reserve the rest for my questions.

Thank you, Mr. Chairman.

Chairman SPECTER. Thank you very much, Senator Cornyn.

Without objection, Senator Leahy's statement will be made a part of the record, and I will now transfer the gavel to Senator DeWine.

Senator DEWINE. [Presiding] Mr. Chairman, thank you very much.

Well, we welcome our panel. Let me briefly introduce our panel. Edward Whitacre is the Chairman of the Board and CEO of SBC Communications. He has led SBC through the acquisitions of Pac Bell, Southern New England Telephone, Comcast and Ameritech. He began his career in 1963 as an engineer with SBC.

Ivan Seidenberg is Chairman of the Board and CEO of Verizon Communications. He previously served as CEO of both Bell Atlantic and NYNEX.

David Dorman is Chairman of the Board and CEO of AT&T. He began his career as the 55th employee of then-fledgling long-distance carrier Sprint, where he rose to become president.

Michael Capellas is the President and CEO of MCI. When he joined MCI in 2002, he had previously served as president of Hewlett-Packard and as Chairman and CEO of Compaq Computers.

We welcome all of you. Mr. Whitacre, you may start. Thank you very much. We are going to go by five-minute rule. Let me just say, gentlemen, that we have votes scheduled at three o'clock. We have five votes scheduled at three o'clock. That means that there will be a halftime at this hearing, so we will have to take a break, but we are going to go as far as we can go.

Mr. Whitacre.

STATEMENT OF EDWARD E. WHITACRE, JR., CHAIRMAN AND CHIEF EXECUTIVE OFFICER, SBC COMMUNICATIONS, INC., SAN ANTONIO, TEXAS

Mr. WHITACRE. Thank you, Senator DeWine. The title of this hearing—"Remaking the Telecommunications Industry"—is appropriate, as demonstrated by the SBC/AT&T merger. Our merger is a positive development for our customers, competition, and for America's leadership in global communications.

We plan to bring together modern networks, innovative, advanced products and services, talent and expertise, and a rich tradition of customer service and reliability. And we are going to ensure that the company which started it all more than a hundred years ago will be part of it for many years to come.

Our merger comes as the U.S. telecommunications industry is trying to get up off the mat. For the first time in a long time, we see some light at the end of the tunnel, but the journey through that tunnel has been pretty hard. Since 2000, telecommunications service providers and equipment manufacturers have lost more than 700,000 jobs. Annual capital investment has declined by more than $70 billion. Companies have lost more than $2 trillion in market capitalization.

Until just recently, SBC was losing 60,000 access lines every week. And in all honesty, adverse regulation has contributed to this downward spiral. So I think the natural result is Wall Street is investing less and less in telecom, telecom is investing less and less in its products and services, and we can see some of the consequences. Today, the U.S. is 11th in the world in broadband deployment. In short, this industry is in turmoil, and that is why we decided to do the SBC/AT&T merger.

The reasons for combining these two companies are clear. First, while SBC has a strong presence in many local markets, we do not have a global network or a national network of our own. We lease one of those networks. AT&T has those assets and they are very good.

Second, the next big thing in communications technology is voice over Internet protocol, or voice over IP. It has already opened the door to a host of new competitors. Dozens upon dozens of cable companies and others are using voice over IP to provide telephone service and they are winning a lot of customers. SBC does not have a consumer voice over IP service, but AT&T does. The combined company will have the resources and incentives to compete with voice over IP in our region, outside our region, and for business customers around the world.

The third reason for our merger is the opportunity it creates for enhanced competition in the large-business customer segment. While we at SBC have made some progress in this market, it has been very slow going for us. AT&T will give us the ability to compete more effectively nationally and globally.

For these reasons, the SBC/AT&T merger will enhance competition and should be viewed positively from an antitrust perspective. For the most part, SBC and AT&T do not compete head to head. This is certainly true in the mass market. Where we do compete in the mid- to large-business space, customers, will still have numerous choices from such diverse providers as systems integrators, equipment manufacturers, and other phone companies such as Verizon and Qwest.

When you assess this market without bias, it is clear that no two companies can control this competitive and crowded space even after these mergers as currently contemplated. The same holds for access to the Internet by rural carriers. Our ability and willingness to connect rural companies to SBC's IP backbone will not change, and we anticipate no change in pricing to these customers.

This merger is a logical step in the evolution of a competitive industry that is light years removed from when the last telecom law was enacted in 1996. Today, there are more wireless subscribers in the U.S. than there are traditional phone lines. Data traffic now exceeds voice traffic by a margin of 11 to 1.

Cable companies will offer phone service to two-thirds of American homes this year, and other competitors using IP-based services continue to grow. On March 9, the Wall Street Journal reported that America Online, AOL, will soon offer voice over IP service to its 22 million U.S. subscribers. In that same day's paper, Cox Communications said in a letter to the editor that in some markets, including Orange County, California, 40 percent of consumers subscribe to Cox digital telephone and 82 percent of their phone customers use Cox for their long-distance service.

None of this was envisioned when the Act was passed, which is why we need the laws to catch up. We need rules to treat new technologies with the lightest touch possible and which allow the competitive marketplace to discipline retail prices. Such reforms would spur much-needed innovation, investment and growth—goals that I hope and believe this Committee shares.

Thank you, Senator.

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

Senator DEWINE. Mr. Whitacre, thank you very much.

Mr. Seidenberg.

STATEMENT OF IVAN SEIDENBERG, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, VERIZON COMMUNICATIONS, INC., NEW YORK, NEW YORK

Mr. SEIDENBERG. Good afternoon, Mr. Chairman and Members of the Committee. Thank you for the opportunity to be part of this discussion on the state of competition in the restructuring communications industry.

As you are aware, Verizon has announced its intention to acquire MCI. This is a response to the dramatically different competitive landscape we have in communications as the industry restructures around new technologies and new markets.

Competing technologies now offer consumers a wide range of choices for voice, data, and increasingly video services. Likewise, large business customers can now choose a much wider range of services from a growing universe of suppliers, including telephone companies, systems integrators, software providers, equipment makers and wireless companies. In fact, earlier this month Microsoft announced a major foray into the enterprise business with a software platform that embeds voice as a free application, much like instant messaging today.

To compete in this dynamic environment, Verizon has sought to differentiate our wireless and wire line services by investing in spectrum, digital capabilities and broadband technologies. Now, by acquiring MCI, we are taking the next natural step by transforming ourselves around the evolving needs of large business customers, a segment in which Verizon has a negligible share today.

MCI and Verizon have complementary assets and capabilities. Verizon has strong local assets and a solid presence among local and regional customers. MCI has strong IP networks and products, and a solid base of national and global customers. Together, we will create a strong, new competitor with the products, network reach and capital capacity required to succeed in this part of the business.

This acquisition does not alter the dynamics that are reshaping the consumer business, nor does it alter the current universal service program or its funding. Long-distance and local as stand-alone businesses are on the way to obsolescence with or without these transactions.

However, is we look at this in terms of the future, it is apparent that customers in all segments of the communications market will benefit. Consumers will benefit because we will have an advanced broadband platform capable of delivering next-generation services in markets across the entire U.S. Businesses will benefit because we will be a strong, stable and secure supplier of advanced communications services. Federal and state government customers will benefit because we will be able to invest in the networks that are critical to their public mission.

National security will benefit because we will continue to strengthen the infrastructure that is a critical component of government communications systems, including those used by the Departments of Defense and Homeland Security. And, of course, the U.S. economy overall will benefit because we will invest in the new technologies so critical to job creation and leadership in the global marketplace.

This transaction is about the future. Verizon and MCI will be a national full-service company with the technology and financial strength to deliver the broadband future and create economic growth in our industry.

Thank you. I look forward to your questions.

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

Senator DEWINE. Mr. Dorman.

STATEMENT OF DAVID DORMAN, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, AT&T CORP., BEDMINSTER, NEW JERSEY

Mr. DORMAN. Mr. Chairman and Members of the Committee, thank you for inviting me to speak with you today about the merger of SBC and AT&T.

There is much to look forward to and nothing to fear from joining together these two companies. Together, we intend to set the global standard for communications for years to come. We will be able to bring advanced IP-based broadband services to market more rapidly and to a wider range of customers than either company could alone, heightening competition for voice, data, wireless and video services.

The rapidly evolving telecom market has changed both companies. SBC today is focused on broadband, video and wireless, while AT&T is now focused on business enterprises, government and wholesale customers. Most of you and your parents and grandparents have known AT&T primarily as your phone company serving residential consumers. That is not the AT&T of today. The AT&T of today is a global networking provider that enables large businesses, state and Federal agencies and other customers to deliver voice, data, video and Internet applications securely and reliably.

The reasons for this transformation are, I think, well known to you. The telecom industry has experienced a very difficult environment. Over-investment by many carriers, tremendous over-supply, a wave of new technologies, an ever-shifting regulatory environment, and even criminal behavior have been experienced.

AT&T's traditional wireline services are being rapidly supplanted by wireless services and Internet-based applications such as voice over IP, and mass market customers are increasingly demanding bundles of services that we are not well positioned to provide. As a result, we determined last year that we would no longer actively compete in the traditional mass market, which includes residential customers and small businesses, and that we would focus virtually all of our attention on large-business, government and wholesale customers.

Last summer, we aggressively and irreversibly implemented our new plan, radically scaling back the operation of our consumer unit and small business units, substantially reducing head count, dismantling marketing and sales functions, retiring support infrastructure and applications, and preserving only those functions necessary to care for our declining number of mass market customers.

The combination with SBC is thus largely a combination of two companies with complementary assets, businesses and skills. Bringing both together should provide a range of benefits. It will create a world leader in advanced communications services as the new company uses its increased efficiencies and expertise in local, broadband, wireless and global networking services to speed the transformation of the legacy networks both at AT&T and SBC to a new integrated IP-based network.

It will reduce our costs and enhance our operations, allowing us to offer better services and better value to all of our customers. It will provide our government customers with more reliable, more resilient and more efficient network capabilities, and it will spur innovation, increasing the pace and breadth of the work of our renowned AT&T Labs, with benefits for all types of customers.

The merger, moreover, will not lessen competition; it will enhance it. The improved ability of the combined company to bring innovative and advanced services will spur others, including cable, wireless and VoIP providers, to enhance their own offers as well. The transaction will lead to greater competition between the Bell companies themselves, and will produce a leading global competitor.

The transaction will not harm competition in any market. In the mass market, SBC is a leading provider of service in its 13-State region, but AT&T is no longer an active mass market competitor in those States. The merger will also not impair competition in the provision of services to business customers, given the large number and diversity of competitors for businesses, the sophistication of those customers and the purchasing power and practices that they employ.

Nor is there any serious argument that the merger will diminish competition in wireless, where AT&T is not currently a provider, international, where SBC has a very limited share, or in Internet backbone services, where many large providers compete. Rather, the merger is a step forward in the evolution of this industry, creating a healthy, competitive and innovative American communications company.

In conclusion, I would like to thank you again for the invitation to speak with you about the very significant consumer and public benefits this merger will produce.

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

Senator DEWINE. Mr. Dorman, thank you very much.

Mr. Capellas.

STATEMENT OF MICHAEL D. CAPELLAS, PRESIDENT AND CHIEF EXECUTIVE OFFICER, MCI, INC., ASHBURN, VIRGINIA

Mr. CAPELLAS. Thank you, Mr. Chairman. My name is Michael Capellas and I am the President and CEO of MCI. Obviously, over the past 5 years, our industry has undergone a series of fundamental changes in technology, in the market, in the regulatory environment, and that technology will continue to accelerate and the incredible potential of the Internet alone guarantees even greater changes in the future.

I have been CEO of MCI for roughly two-and-a-half years. I spent the prior 25 years in the computing industry as a customer of telecommunications services and as a developer who used the power of global networks to fuel innovations in the software industry. I do believe in the power of this technology and in the future of innovation. I have always liked to say there has been a computer on the end of a network for a very, very long time.

Many of the changes in the telecom industry are actually being driven by broader movements in information technology. First of all, there is a movement toward standardization. Basic building blocks such as servers, storage and microprocessors are simply now standard devices that are addresses on a network and can reside anywhere.

Second, the rise of Internet commerce has accelerated the adoption of software standards that enable different systems to talk to each other. At the same time, new tools like Web services allow developers to write applications across different platforms.

Today's communications travel the networks in packets. There is no difference between a voice or a data packet. Whether you are making a phone call or purchasing an MP3 music file, it is all the same. A packet is a packet is a packet.

The Internet-driven standards that allow these systems to talk to each other have redefined network requirements. Formerly, local, long distance and data traveled along separate network paths. Now, there is the need for integrated intelligent paths that can carry voice, data and streamed video without the developer or end user needing to know or care how the path is developed.

And one doesn't need to be a computer scientist to sort of see this in everyday life. A Blackberry is a great example of a device that can instant-message, make a phone call, get news or sports, or stream a video, and this is integrated communications at work.

MCI has been a global provider of communications. We operate one of the industry's most expansive global IP backbone and serve many of the most demanding applications in the world. We serve major financial institutions, complex engineering and manufacturing centers, and provide complex solutions for more than 75 government agencies.

Many of these customers are the early adopters of this new computing infrastructure and are led by some of the best and brightest technologists. These customers have some common requirements—high-end reliability and security, and then global delivery, ease of adapting new technologies and new applications, and low-cost infrastructures.

At the heart of all these requirements is the need to mesh local access with wireless capabilities and the backbone network. Much of today's network architecture was incubated at MCI, in part due to the vision of Internet pioneer Vint Cerf. It is know as the Internet Protocol, or IP. In its simplest terms, IP allows applications, from wireless e-mail to video streaming, to be rolled out without understanding or changing the core network elements underneath it.

New technologies and new delivery methods are reshaping the market. In addition, recent regulatory and legal decisions have made a significant impact, particularly on the consumer segment. The underlying economics have been fundamentally altered. So where is MCI in this perfect storm of IP convergence, market evolution and regulatory change?

Our plan is to leverage our IP network by refocusing on large-business and government customers and deemphasizing our consumer business. It would be virtually impossible to sustain our traditional voice business based on circuit switch technology.

MCI has also entered into an agreement with Verizon to combine our strength. MCI owns a state-of-the-art IP backbone network, but no significant first-mile facilities or wireless. Verizon has extensive first-mile facilities and state-of-the-art broadband. MCI has a large-enterprise and government customer base which has remained loyal because we provide world-class products and service quality. Verizon provides local access to many of those same customers.

Some have asked how this merger will affect competition. In my view, the combined company will benefit both consumers and business users. It will deliver end-to-end network capability and will provide innovation and next-generation applications.

Technology has changed the landscape. Significant competition for consumers will come from alternate technologies the merger will not affect, like cable and wireless. And the same is true for business and Internet service markets. Wireless and other technologies are redefining competition. In addition, we are seeing the increased presence of broad-based technology companies like IBM entering the traditional telco market. This is the natural evolution of changing competition as technologies converge.

In conclusion, Mr. Chairman, technological, marketplace and regulatory changes are driving the forces behind the industry restructuring. Traditional notions of long-distance companies have become obsolete. The merger of MCI and Verizon is a reflection of these fundamental changes. The merger will not have an adverse effect on competition in any line of business. On the contrary, it will strengthen MCI's ability to compete and continue to innovate. Technology will, in fact, move on.

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

Senator DEWINE. Well, we thank you all very much. We have a vote. We are now ten minutes into the vote, so we are going to have to leave. If it is five votes, we are going to be a while, so we will be back.

[The Committee stood in recess from 3:10 p.m. to 4:45 p.m.]

Senator DEWINE. Well, let me call the hearing to order. Thank you all for your patience. We apologize. We had five votes and we are back.

Let me now turn to Senator Kohl for his questions.

Senator KOHL. Thank you, and likewise we apologize for the delay.

For Whitacre and Mr. Seidenberg, we have heard a lot of testimony today about the competition your companies will face in the years ahead from new technologies. One important new way for consumers to make phone calls is through a technology known as VoIP, as you know—voice over Internet protocol. Making phone calls using VoIP requires a high-speed Internet connection—a service many consumers obtain from their telephone company—but neither SBC nor Verizon will sell consumers high-speed Internet service without also requiring that the consumer also buy local phone service. This destroys the incentive of the consumer to purchase VoIP phone service and is therefore a significant obstacle to the deployment of this technology. Would you be willing to commit as a condition of approval of your merger to sell separate Internet service to consumers without also requiring them to buy phone service?

Mr. Seidenberg, you will have the opportunity to respond first, and then you, Mr. Whitacre. The question is would you be willing to commit as a condition of approval of the merger to sell separate Internet service to consumers without also requiring them to buy phone service.

Mr. SEIDENBERG. Senator, I think we have already indicated that on this question we would be providing to the market a service. If I understand the question, in our industry we call it, quote, "naked DSL." So I think in the past we have always provided DSL with a phone number. That is the way we provide service. In the future, we are in the process of working through the mechanics of offering a DSL line without a phone number.

Now, your specific question is would I agree to a condition. At this point in the process, sir, I would prefer not to agree to any conditions, but I think on the point you raise we are going to do exactly what you said.

I would also make one other point. You don't need a broadband line to get voice over IP. There are companies today that put adapters on that do that. So I think voice over IP comes in a lot of flavors, one of which is over a broadband line.

Senator KOHL. So you are saying you wouldn't want to be quoted as agreeing to the merger based on that condition, but you are moving in that direction?

Mr. SEIDENBERG. Yes, that is correct.

Senator KOHL. Mr. Whitacre.

Mr. WHITACRE. Well, we are working the same way. There are companies out now buying loops and they put their own equipment and resell it. So, in essence, what you are suggesting is being done. Now, would SBC do it? Of course, SBC would do it, but SBC is not going to do it under the price of what it costs us to provide it. We have been there and done that with something called UNIP, which was very bad for this industry. We would be willing to do that under the circumstances that it is not underwater and there is a profit to be made for SBC shareholders, too. So the answer is yes.

Senator KOHL. The answer is, yes, you would be willing to condition the merger on that?

Mr. WHITACRE. No, I wouldn't be willing to condition the merger on that. But would we be willing to sell it? Of course, and we are working toward doing just that.

Senator KOHL. All right. Mr. Seidenberg and Mr. Whitacre, on February 17 the Washington Post reported that the FCC was investigating complaints by a company called Vonage that local phone companies were blocking or disrupting access to their VoIP Internet phone service.

Has either of your companies ever intentionally done this? Will you commit as a condition to approval of your merger not to interfere with your customers' Internet connections so as to degrade or block access to competing VoIP phone service?

Mr. SEIDENBERG. Senator, I got this question at the House hearing and checked it out. I know of no case in which we are blocking any traffic from Vonage, and as a normal course of practice, we pass all this Internet traffic through. And just to give you some comfort, we also buy access to AT&T and Ed's network to put our Internet traffic over it. So we would have no reason to block anybody else's traffic, when we are putting our own on other people's network.

Senator KOHL. So you would approve as a condition of the merger?

Mr. SEIDENBERG. Well, I don't like conditions. I guess at this point in the process, we need to see the whole picture. But as a matter of practice, sir, we are not doing anything that would suggest we are blocking anybody's traffic.

Senator KOHL. Mr. Whitacre.

Mr. WHITACRE. SBC would not block any Vonage traffic or anybody else's, and has never done that, would not do that. That is not the way we do business and it is just not going to happen.

Senator KOHL. So you would agree to that as a condition of the merger?

Mr. WHITACRE. Well, you say "condition." We are not going to block anybody's traffic, Senator.

Senator KOHL. Okay, a last question and then we will turn it over to Mr. DeWine.

Mr. Seidenberg and Whitacre, as you know, one important possible alternative for consumers will be wireless connections to the Internet. Using these connections, consumers can access alternative phone providers such as VoIP and avoid the Bell companies' connection to their homes. Cities and municipalities such as Philadelphia have begun to build such wireless networks and plan to offer it to their residents as a municipal service.

In your testimony today, you have spoken at length about the promise of new technologies and how we should not worry about these mergers because the deployment of these technologies will create an abundance of new telecom competition.

Yet, at the same time, we have noticed your companies lobbying State legislatures around the country to stop cities from building these new networks to deploy these very technologies. Pennsylvania recently adopted such a law and other States considering such laws include Illinois, Texas and Florida.

So why have your companies been actively lobbying for such State laws to ban the deployment of municipal wireless? Will you commit to cease your efforts, should your mergers be approved?

Mr. Seidenberg, we will give you the opportunity, of course, which you so much desire, to answer first.

Mr. SEIDENBERG. Actually, I would like to go before Ed just to make sure I get it in before whatever he says. I don't know what he is going to say.

Look, we have squabbled a little bit with a few municipalities and let me tell you why. First of all, we can't stop anybody from putting any technology they put in. But, generally, we find it unfair that municipalities that regulate us, set our taxes, set our franchise fees, participate in running our company in some fashion, also now want to compete with us under a different set of rules. So every time we see that happening, we point it out.

We would also make the point that in all these places where municipalities want to get into this, with all due respect, they don't do a very good job either, which then impacts us because the cities usually come back to us and we need to spend money to fix the things that have occurred. So we are not in the business of stopping anybody from doing it, but where we think the rules are unfair, we are going to point it out.

Senator KOHL. In Pennsylvania, the law was adopted at the behest of your company's lobbying, is that correct?

Mr. SEIDENBERG. I am sorry?

Senator KOHL. In Pennsylvania, the Pennsylvania law was adopted, as I understand it, as—

Mr. SEIDENBERG. But it didn't prohibit the municipality from providing the service.

Senator KOHL. Right.

Mr. SEIDENBERG. It gave us a chance to jaw-bone about it, but it didn't prohibit it from doing it.

Senator KOHL. Mr. Whitacre, where do you come from on this?

Mr. WHITACRE. Mr. Seidenberg answered that as I would. They are the ones that make the laws, the rules, charge franchise fees, et cetera, et cetera, and then to compete against us makes it an unfair competition. From a taxpayer's standpoint, I really don't want my tax dollars to be used by a municipality or a local government to build something in competition where many other businesses already are. But as Ivan said, we can't stop anybody from putting any technology out there.

Senator KOHL. So the lobbying of State legislatures around the country to stop cities from building new networks to deploy these new technologies is not an activity that you all engage in, or you do engage in that?

Mr. WHITACRE. Oh, we have engaged in that.

Senator KOHL. You do engage in that?

Mr. WHITACRE. You bet.

Senator KOHL. Yes.

Mr. WHITACRE. You bet we will. I mean, again, those municipalities, those governing bodies regulate us and at the same time they are competing with us. That makes no sense, so we are certainly going to lobby against that. But can we stop them? No, we can't. They can put one out there if they want.

Senator KOHL. Sure. They can do whatever they wish.

Mr. WHITACRE. Sure.

Senator KOHL. Mr. Seidenberg, were you clear in your response to that?

Mr. SEIDENBERG. I think so. I would like to clarify this. My understanding is this is not a programmable activity on our part. If we see something egregious, we go after it, but this is not something that at every single place in the country we have a policy that argues about it. It is only where we think there is a big duplication of effort and it is unfair. So, yes, we do it, but it is much more episodic.

Senator KOHL. Mike?

Senator DEWINE. Mr. Whitacre and Mr. Seidenberg, the biggest antitrust issue presented by these mergers appears to be in the so called enterprise market. I would like to examine the impact of these deals on small and mid-size businesses, the companies served really most often by AT&T, MCI and their own regional Bell.

It makes sense that you have so far focused on medium and smaller accounts within your region. It also makes sense that, post-merger, you will have a great deal of incentive to pursue the major accounts even if they are out of your home region. But what about pursuing the smaller and mid-sized business accounts out of your region? Doesn't it make more sense to leave those to the other regional Bell which already has a relationship with them and the local facilities to serve them?

Why attempt to compete out of your region, where you would need access to your competitor's network? And if that is the case, aren't we moving from a situation where we have three major competitors—AT&T, MCI and the local Bell—down to only one? Isn't that a clear antitrust problem?

Mr. SEIDENBERG. Does Ed get this one first? Mr. Chairman, do you want me to do this one first?

Senator DEWINE. Well, you know, you went first last time.

Mr. SEIDENBERG. I think he should go first.

Senator DEWINE. Do you think it is his turn?

Mr. SEIDENBERG. I think so.

[Laughter.]

Mr. WHITACRE. You keep talking and I will forget the question.

Doesn't it make more sense? There are many, many competitors in that space that you are talking about. We compete now against Verizon, as an example, against AT&T, against MCI across the country in some medium, some small and some enterprise businesses. There are many other people or other companies in that business, though, that people don't think about everyday. You can think of Cisco, you can think of IBM, you can think of many manufacturers, you can think of Qwest. You can go on and on, so the competition in that space is not three; it is three times maybe, I don't know how many, but it is many, many competitors in that space.

So it is not going down to three. There are many competitors in that space and I think it makes sense on a business case basis—on a case-by-case basis, you would have to decide where you would compete, but certainly we would anticipate doing that.

Senator DEWINE. Mr. Seidenberg.

Mr. SEIDENBERG. Yes, Senator, I would just add this. I think the way we would see it is the market is globalizing. So a small-business customer in Pittsburgh or in Milwaukee or in Nashville want a choice of suppliers, and I think Ed said it. Small-business customers get services from cable companies in the form of modems. They get service from wireless companies.

And with our combination with MCI—MCI has a network that extends into many of these cities, so we would have the capability of being a third or a fourth or a fifth supplier to these accounts. Actually, I think it is just the opposite. With our heft, muscle, brand, our operations focus and the assets that MCI brings to the table, I think we are in a better position to provide more choice for the small and medium customer across the country. So I think we are just following the natural evolution of the market.

Senator DEWINE. Mr. Whitacre, the three I mentioned are the three biggest, though, are they not?

Mr. WHITACRE. You know, Senator, I don't know. We certainly would be up there, but I think we often overlook the impact these other companies have had. I mean, we are not talking small companies. We are talking about companies that have thousands and thousands of customers that are, I guess, below this radar screen.

As far as the enterprise business goes, SBC is a small player, a very small player. Mr. Dorman would have to answer for AT&T, but we are quite small in the enterprise space. In medium and small business, we are stronger in our region, but we certainly have a lot of competition.

Senator DEWINE. Does anybody else want to jump in here?

Mr. SEIDENBERG. If I might—I am sorry, guys, but I just want to address something you said in your opening remarks. If the nature of the question goes to how many telcos will provide these services, then your point is fair that you can look at one, two or three that do that. But the customer's dollar is green and they don't care who they buy these services from.

So the fact is the market now has five, six, seven different places to buy the services they used to buy just from the telco. So as we move into these markets, we are dealing with a very different base of competitive activity in these areas.

Senator DEWINE. Anybody else? Mr. Dorman.

Mr. DORMAN. What we have found that happens on a local basis is smaller companies that compete locally do a very good job of serving small businesses in their home areas. Examples of that are people like McLeod Communications up in the upper Midwest has done a very good job and built a business of almost $1 billion of revenue.

You have Broadwing, XO, Global Crossing, Level 3. Cox Cable just announced that they had just passed 300,000 business customers, and they just started selling to business customers about two-and-a-half years ago. Time Warner Telecom is another cable-affiliated company which has done very well in the medium-business market.

So what we find competing nationally is, yes, we do see the Bell company certainly competing in the region, but typically there are at least five to seven other providers besides MCI and ourselves. We didn't mention Sprint. Sprint is still a $7 billion-plus company in the long-distance and communications space, and more than half of that comes from business customers, about $4.5 billion, in fact.

So my perspective is that there is an abundance of choice for business customers. Certainly, in the context of medium and small customers there is even more. Large customers typically buy more sophisticated things, but even there, there are five to six competing providers. I think Ed mentioned IBM. In almost every one of our large-customer bids these days, we see IBM, EDS, CSC, even Lockheed as systems integrators offering communications and IT services as a bundle. Recently, we lost Bristol Myers Squibb to BT, British Telecom. So there are a number of different competing players across the market.

Senator DEWINE. Mr. Capellas and Mr. Dorman, as part of your efforts to compete with the Bell companies in serving enterprise customers, both of your companies purchase local access facilities that would allow you to provide facilities-based service to many business customers. Now that you are planning to merge with Verizon and SBC, respectively, wouldn't competition be best served by a divestiture of any of those overlapping assets to other CLECs who could use them to compete against the newly-merged entities?

Mr. CAPELLAS. I think first, to put it in perspective, about 52 cents on every dollar we spend has traditionally gone for local access. In fact, we actually have very few facilities which are local. That, in fact, is part of the reason for the merger, but right now we have very, very limited local access capabilities. So while no decision has been made on how we deal with those, it is a very, very small part of our business.

Senator DEWINE. Mr. Dorman.

Mr. DORMAN. In the case of our direct overlap with SBC, we do business in SBC's 13 States, as I recall, in over 100,000 different establishments or buildings. We have facilities overlap with them in something like 2 percent of the cases where we have a fiber into a building that they have service into.

In most mergers, redundant facilities like that end up becoming synergies anyway. So while not committing anything for SBC looking into the future, I think that on a case-by-case basis the major thing I would be concerned about is disrupting customers. If you have a major data network for an American Express and five of the locations happen to be in buildings where you had fiber and SBC didn't and you had to convert them over, I would just simply be wary of the impact on customers. But rejecting that out of hand, I don't think is necessary. In other words, it should be something that we would look at.

Senator DEWINE. Let me move to another ramification of these proposed mergers. Ever since the break-up of AT&T in 1984, we always could count on AT&T and MCI to be on the opposite side of the fence from the Bells on public policy disputes in front of Congress or at the FCC or in the courts. Now, while many of those issues are now resolved, there are many that will no doubt arise in the near future as we consider possibly rewriting the Telecom Act and as we attempt to navigate our way into an era of enhanced services.

Who is going to take the place of AT&T and MCI? As policymakers, who will we look to for an alternative view now if this takes place? And really to get into the crass business and political reality of all of this, what if one or both of the merged entities decides they don't like a decision at the FCC or of the Congress? Really, there is no one else who has the nationwide resources, the political heft or the large constituencies in each State. Who is going to have the resources to fight the merged entities in court or at the FCC? Isn't that a practical problem?

Mr. CAPELLAS. I think like lots of things, you can look at it as an opportunity. If you look at where the innovation and technology has been and the movement particularly in customer requirements, the goal has become how do we take these what should be complementary, seamless technologies and put them together.

If you are a customer and you sort of look at local access, wireless bundling, IP, the software access to reside it, the customer's goal is to actually bring it together to a common goal, and then to set standards across the industry which allow that to happen, to allow these networks to talk to each other.

So maybe the new construct is how do we actually get an industry consortium that drives standards that gains for productivity so all these devices could talk to each other. So as a practical matter, maybe the nature of the beast is no longer in an open warfare, but actually in a set of collaborative sort of efforts and consortia that allow these standards to develop so we can actually take it to the next level.

Senator DEWINE. Herb.

Senator KOHL. Mr. Whitacre and Mr. Seidenberg, many analysts see one of the biggest dangers to competition from these deals is their effect on the business market. AT&T and MCI are today vigorous competitors for the telecom business of large and small enterprises throughout the Nation. The mergers' critics are concerned that once the mergers are completed, the combined SBC/AT&T and Verizon/MCI will prefer to concentrate their marketing efforts on their respective regions and the competition now offered by AT&T int the Verizon region and MCI in the SBC region may well be lost.

Mr. Whitacre and Mr. Seidenberg, after these mergers will SBC and Verizon continue MCI's and AT&T's efforts throughout the Nation, or are the critics correct in fearing that your two companies will engage in a divide-and-conquer strategy and that the enterprise market will lose a strong competitor?

Mr. WHITACRE. Well, Senator, SBC will continue to engage in that kind of competitive activity across the United States. In other words, where AT&T is, we will continue to compete. So the critics are wrong in that case. I think it is a good thing for the Nation. We will be able, from a stronger company, to do more in that arena, not less, and the technology is going to enable that. So from an SBC standpoint, of course, we will be competitive all over the Nation.

Senator DEWINE. Mr. Seidenberg.

Mr. SEIDENBERG. Senator, I agree exactly, and I think the critics misunderstand something. If you take wireless, we have built facilities across the country. We compete everyplace. With respect to enterprise, we didn't have the physical capabilities to go to every city in the country. With a combination with MCI, it gives us access to the top 125, 150 MSOs across the country, and we will use the facilities of MCI to compete aggressively in all those markets. Many of them are not in what you would call our home market.

Senator KOHL. Although we have heard a lot about cable as an alternative provider of phone services, isn't it true that thousands of small businesses—supermarkets, gas stations, dry cleaners—do not have cable service? So what alternatives will these small businesses have after these mergers?

Mr. WHITACRE. Senator, I would like to invite you to San Antonio and take you down a few streets where those kinds of businesses that you are talking about exist. I think the cable companies have a plan; I think they have a business plan to serve those kinds of people. I would like to show you what they done. So, clearly, they are after that kind of customer. They are doing it, and these businesses you talk about are going to have alternatives. They have got many alternatives now; they are going to have even more with cable. It is not just SBC serving those. It is many other companies.

Senator KOHL. What do you think, Mr. Seidenberg?

Mr. SEIDENBERG. I agree with that, sir. It is the same thing. Again, it is a question of how you define the market, and as Michael Capellas said a minute ago, there is a very fine line. If there is any distinction between a computer and a phone network, you can hardly determine it anymore. A packet is a packet.

So if you buy AOL service, you can buy a very cheap line from Ed and then put all of your data over that AOL service and Ed gets no revenue for it. So there is direct competition for the lines. There is substitutable competition for the services. These small-business customers, because of the explosion of technology, have choices today they never had before.

Senator KOHL. Thank you.

Senator DEWINE. I have a statement for the record from Senator Sam Brownback which I would ask unanimous consent to be made part of the record. Without objection, it will be made a part of the record.

Mr. Whitacre, let me ask you a question about the SBC consumer market. First, with regard to the consumer market and SBC's territory, take a State like Texas. My understanding is that in the State of Texas, the consumer long-distance market share held by SBC is about 70 percent. Is that correct?

Mr. WHITACRE. I don't know exactly, Senator, but that is in the ball park.

Senator DEWINE. That is in the ball park?

Mr. WHITACRE. Yes.

Senator DEWINE. How long has SBC been able to offer long-distance service to its customers in Texas? Do you know?

Mr. WHITACRE. I think about 3 years. I would have to check, but it has been several years.

Senator DEWINE. My understanding also is that AT&T holds about 15 to 20 percent of the consumer long-distance market in Texas. Does that sound about right?

Mr. WHITACRE. I don't know, Senator. You would have to ask Mr. Dorman.

Senator DEWINE. Mr. Dorman, is that about right?

Mr. DORMAN. I am not sure. It would be less than 20 percent, would be my expectation.

Senator DEWINE. More than 10?

Mr. DORMAN. Yes.

Senator DEWINE. So if the merger were approved, the combined companies would account for 80, 90 percent of consumer long distance in Texas. Would that be right?

Mr. DORMAN. Well, if you don't count wireless and you don't count cable, if you talk traditional wireline long distance, that fact might be true. But I suspect on the basis of actual usage, if you included all the long distance originated on cell phones, I don't think the number holds up as a percentage.

Senator DEWINE. I want to be fair about this. What do you think the percentage would be if you included those?

Mr. DORMAN. I would bet that wireless originates about as much long distance in Texas as wireline, maybe more.

Senator DEWINE. So you would put it, then, at 45 percent, approximately?

Mr. DORMAN. That would be my guess.

Senator DEWINE. Of that universe?

Mr. DORMAN. Yes.

Senator DEWINE. Let me ask an additional question, Mr. Whitacre. What are SBC's market share goals for consumer long distance in California?

Mr. WHITACRE. I guess broadly put, we want to serve all our customers. We are not the only company operating in California. For example, Verizon is there. There are many competitors there. The cable companies are quite strong and have recently put out that they probably have a bigger share than we do where we traditionally operated.

I think any business person who is truthful would like to have as much share as they can get. As a practical matter, that is a function of a lot of things—price, what you do. But certainly we are trying to serve the consumers we have in California with our long-distance service. That is a goal of ours. We would like for all our customers to have SBC long distance. They do not now.

Senator DEWINE. What about in the Midwest, former Ameritech States?

Mr. WHITACRE. Senator, I can't recall the percentages. As you know, we got in long distance much later, so our percentages would be considerably smaller there. I would just have to get you the correct number, but it would be much smaller.

Senator DEWINE. All right. When you do that, could you also get Missouri, Oklahoma and Kansas?

Mr. WHITACRE. Sure. I would be happy to do that.

Senator DEWINE. Mr. Capellas, there is a great deal of interest in the sale of your company. As we all know, there is still a certain degree of uncertainty as to whether or not Verizon or Qwest will be successful in their efforts to purchase MCI. We certainly don't want you to disclose any corporate secrets or anything you don't feel you can tell us about, but can you tell us what the status is of MCI's deliberations and when we might expect to see a decision?

Mr. CAPELLAS. Well, we do have a signed merger agreement with Verizon, and so that is the first order of business.

Senator DEWINE. Right.

Mr. CAPELLAS. There has been a process undertaken with which, with the consent of Verizon, there could be some additional discussions. That is a time period that ends on Thursday, this coming Thursday, and so at this point there are some deliberations between the teams. But we do have a signed merger agreement and if there is any reason to reevaluate, if the situation warrants, we will, but at this point we have a signed merger agreement.

Senator DEWINE. There was one report—and I may have read it very quickly, but one report that Qwest's offer was a bigger offer. Could you comment on that? That was a published report, and again I may have not read all the fine points and there may be fine points you would like to elaborate on.

Mr. CAPELLAS. Every economic decision, no matter what it is, has a balance of risk and reward and a balance of short term and long term. So the real question here is when we entered into our agreement with Verizon, the thing we were looking for was the ability to compete in a market which was changing—wireless capabilities, access economics, financial strength. And, you know, it is the fiduciary responsibility to take in all the considerations, and so again all those considerations were taken in and our deal with Verizon was really based on long-term ability to go to market.

Senator DEWINE. Do you want to comment on Qwest?

Mr. CAPELLAS. No. I don't think it would—there has been a period open in which some conversations could take place, but I would have nothing to add at this point.

Senator DEWINE. Fair enough.

Mr. Whitacre, let me talk for a minute about jobs, and I will put my hat on as U.S. Senator from Ohio for a moment, if I could. There has been some discussion about job losses for your company overall, and I wonder if you could comment on that and also comment on what impact this might have for the State of Ohio.

Mr. WHITACRE. Well, Senator, for the past several years SBC's workforce has decreased in size. It has decreased because our revenues have been falling, our earnings have been falling. That is part of the problem I addressed in my remarks with this industry. It is an industry that has lost a lot of jobs because of declining revenues.

Specifically, with the AT&T merger, we have said generally about, it looks like, 13,000 jobs would be impacted across both companies. But you have to remember SBC would normally lose by attrition 12,000 a year; that is retirements, et cetera. So I suspect with normal attrition, there is probably not much change.

We are not doing this merger to continue to shrink. This is about changing something in this industry and making these two companies viable and being able to grow again. This is an environment in which you would hope you could increase jobs if it is successful, and you do something exciting for a business that has been in the doldrums for quite some time.

As it impacts Ohio, I can't tell you specifically this early in the talks because I don't know what AT&T has located there. I know what SBC has, and I doubt if our workforce is impacted significantly, if at all, in Ohio.

Senator DEWINE. Let me take advantage of the fact that we have the CEOs of four of the biggest phone companies in the country here to ask a question that may not really have a direct relationship to the merger, but I do have you here and I think it is an important issue.

As we move and see more and more innovation in the telecommunications arena and develop greater broadband capability, I think it is extremely important that we work hard to ensure that the disabled are not left behind. As we make broadband and improve Internet applications, we should be able to come up with better mechanisms to include the disabled in the communications revolution.

Let me ask each one of you if you could address this question, and that is what are you doing and what can we all do as policymakers to take steps toward this specific goal? How can we use all this technology to serve constituencies with different needs and help customized products so that many different people can use them?

Mr. Whitacre?

Mr. WHITACRE. Well, I think the new technology is going to enable us to do that, Senator. I can't speak to all the specific ways, but certainly voice over IP lends itself much more than circuit-switching does to uses of all people of the United States, be it disabled, be it whatever.

I don't know some of the new uses. Perhaps some of the other participants do, but I think it does give us the ability to move things around, change things, switch things, have broadband access, wireless broadband access, which certainly in itself might be a terrific way for the disabled, and that is right around the corner. So I think the era we are moving into lends itself very much to do more in that, and SBC has always been a greater supporter of that.

Senator DEWINE. Mr. Seidenberg.

Mr. SEIDENBERG. Yes, sir, just two points. We have a good record in this area. We have a disabilities center that we have in the East. We opened one in the West, so we serve customers directly out of these centers.

I would make the point that a company of our size and scale has the financial capacity to address these markets. These markets are important to us. People believe that, given our brand and our position, that we should address these markets. We have the financial capability to do so.

For the past 22 years, chasing all these new entrants in the business, I don't ever remember a new company coming into the marketplace and saying we are going to compete in the disabled market. So I think that one of the things that we want to do is to the extent that we can continue to create the financial capacity to address the markets, the disabled market is one we will always keep our eye on.

Senator DEWINE. Mr. Dorman.

Mr. DORMAN. I think the promise of being able to fungibly take text and speech and voice and interact them is an important attribute for various disabilities, the point being if you can type, you can communicate. If you can speak, but not see, you can be able to communicate your words and have them translated into text for other people. So the mixing of media between e-mail and voice is going on right now.

This so-called unified messaging capability, as Ed suggests, comes together with voice over IP very nicely because the interface is typically something as simple as a Web page, where you can listen to your e-mail, you can listen to a voice mail and you can translate. So we are moving that ahead. AT&T actually holds a significant amount of intellectual property on speech processing, which is a very important part of this.

Mr. CAPELLAS. Just to echo Dave's point, we also have a center in California which is for the hearing-impaired which actually will take speech to text and text to speech. So if you have a call that you can't hear, you will send it in, it will be translated and go back.

I think there is tremendous progress being made in the area of linguistics. Particularly for those who have English as a second language, it can be deployed over networks and you see that happening. There is voice activation and all the voice activation that goes with it.

There is a new thing that is being deployed over networks which is called pace-based training for those people who may not have the same skills educationally to be able to actually have educational programs at a different pace, which is actually starting to revolutionize some things in education.

There is another one I think we can all do. When you create an environment of a diverse workforce, you will find that those attitudes actually create environments where people will think of things that are not normal to them. I think just promotion of diversity in your workplace probably does more to let the creativity out than probably anything we can do, because creative people will come up with creative ideas.

Senator DEWINE. Good. Well, I appreciate your statements, all four of you. This is something that this Subcommittee will continue to look at. To state the obvious, the new technology that you all are engaged in and what your business is all about provides just wonderful opportunities for people today that we couldn't have envisioned 10, 15 years ago, maybe even 5 years ago. It presents just tremendous opportunities for people to improve the quality of life, and we would encourage you to continue to make that part of what you do and part of your mission. Mr. Seidenberg, I think, speaks very well of looking at that as part of the mission, being big enough to do it and carry it out, and we appreciate it very much.

Senator Kohl.

Senator KOHL. Well, I think you guys have done a really good job here. It has been informative. I think about the National Press Club, which is an organization here in Washington that has influential and important people like yourselves to speak before the group. After the speech and the questions, which are all quite serious, there is a final question which is serious but somewhat humorous.

I would like to ask all four of you, in the event that this merger goes through, which of you gets the dinner and the gold watch and which of you gets the corner office?

[Laughter.]

Senator KOHL. I appreciate your answer.

[Laughter.]

Senator DEWINE. We appreciate your answers very much. Thank you very much. Well, we appreciate you being here. I think this hearing has given us a good opportunity to examine some of the important antitrust and competition issues raised by these mergers.

As we have discussed, most of the antitrust issues really appear to be in the enterprise market, and I anticipate that the Antitrust Division will examine those and other antitrust issues as it looks at these deals. Further, this hearing has been useful in exploring some of the larger competition issues regarding intermodal competition and whether that is going to be sufficient to protect consumers and competition in the future.

Clearly, this Committee is going to need to consider how we can play a role in making sure that intermodal competition is a part of the competitive landscape in the years ahead. Along those lines, as I mentioned in my opening statement, the Antitrust Subcommittee will hold a follow-up hearing on April 19. We will at that time hear from some of those who have expressed concerns about the mergers. I hope that after hearing from them, we will have a fuller understanding of some of these complicated technical and telecommunications issues, and can decide what steps to take moving forward.

Before I close this hearing today, I would like to thank each of our witnesses for their patience. We were trying their patience and everyone in the audience's patience here today, and the press corps. We thank them. It has been a long day and the hearing certainly did not proceed as smoothly as we would have liked, but all of our witnesses have been very gracious, very professional in their testimony, and really have greatly contributed to this Committee and to this Congress' understanding of the mergers and of the marketplace and how it exists today. So we thank them for their time.

This hearing is adjourned, and we look forward to continuing to explore the issues on April 19. Thank you.

[Whereupon, at 5:27 p.m., the Committee was adjourned.]

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

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

QUESTIONS AND ANSWERS

Michael D. Capellas
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April 19, 2005

The Honorable Arlen Specter
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I appreciate being given the opportunity to testify before the Committee at its hearing on the SBC/AT&T and Verizon/MCI mergers on March 15, 2005. Attached is my response to the written questions you sent me after the hearing on behalf of Sen. Kohl.

If I can be of any further assistance to you or the Committee, please don't hesitate to contact me.

Sincerely,

Michael D. Capellas

RESPONSES TO QUESTIONS FROM SEN. KOHL

SUBMITTED BY

MICHAEL D. CAPELLAS

PRESIDENT & CEO, MCI

1. **AT&T and MCI have been for years the nation's two largest competitors to the Baby Bells for local phone service. Last year, after the FCC rules changed, both AT&T and MCI withdrew from actively marketing local and long distance service to residential consumers. Now AT&T and MCI have agreed to be bought by their main rivals, the Baby Bells. Does this development mean that competition from independent local wire-based phone companies – the so-called "CLECs" – is now over and that the competitive vision of the 1996 Telecom Act has failed?**

The Verizon-MCI merger will not significantly impact competition in the residential market. As your question acknowledges MCI's consumer business is in a continuing and irreversible decline. While MCI is doing its best to manage that decline, our consumer base will inevitably continue to shrink because of the technological, market and regulatory changes that have converged to reshape the telecommunications marketplace.

The competitive vision of the 1996 Telecom Act will continue to drive technological innovation and marketplace competition. CLECs will continue to contribute to this competitive dynamic along with alternative and emerging technologies that this combination will not affect, like cable and wireless. Specifically, competition in mass markets will continue to be robust as a result of the dramatic growth in the provision of voice services by cable firms. Telephony offerings of cable companies grew from 15% of homes nationwide in 2003 to 40% by the end of last year – a figure that is expected to grow to 90% within two years.

2. **AT&T and MCI have been two of the primary forces for phone competition over the last two decades. Before Congress, the FCC and state regulatory bodies, your two companies have been vigorously pressing for the opening of the dominant phone networks controlled by SBC and Verizon. In numerous areas of telecom policy, you have fought the Baby Bells to gain a competitive foothold. However, with these mergers, you will not be continuing this battle.**

Many commentators worry about the consequences of the removal of AT&T and MCI as independent competitors to the Baby Bells. They wonder if the interests of competitors will be adequately represented before regulators and policymakers. How do you respond to these concerns?

MCI's pioneering role in bringing competition to the telecommunications industry shows that an individual company can be a catalyst of change, but MCI is not the only company that can play that role, individually or collectively. Industry competition has given birth to hundreds of companies that compete in all sectors of the business – CLECs, equipment manufacturers, software vendors, Internet service providers (ISPs), VOIP and other IP applications providers, wireless companies, cable companies and many more – as well as each sector's trade associations, ensure that they will be well-represented in proceedings before regulators and policymakers. In addition, residential and business endusers will continue to be very well represented by consumers groups and corporate trade associations, all of whom have a direct stake in preserving and promoting telecom industry competition.

3. **Many analysts predict that we are increasingly moving towards an industry where telecom services are being marketed to consumers in "bundles." The regional Bell phone companies are offering packages to consumers which include local phone services, long distance phone services, wireless phone service, and high speed Internet connections in one package for one flat rate. The only competitor to this bundle of services will come from the consumer's incumbent cable company, leaving the consumer with just two choices. I am concerned because having only two choices for a service does not make for good competition.**

Do we have reason to worry that most consumers will be left with only two choices for their telecom services? How can we be sure that consumers will have a choice of more than just their local phone company and their cable provider for a bundle of telecom services?

The move toward bundled packages of services isn't a matter of predicting the industry's future direction. Consumers have been benefiting from these kinds of packaged offerings for several years and will undoubtedly continue to do so in the future. The question correctly identifies cable companies as significant providers of voice telecommunications services to consumers. In addition to cable firms, of course, wireless providers have assumed a prominent position as providers of voice and data services to consumers. This year, in fact, the number of wireless subscribers will surpass wireline access lines for the first time. In addition, 14 % of American consumers now use wireless providers as their primary means of making calls and 8% have already "cut the cord" and are using wireless as their sole means of communication. That percentage is growing rapidly. Consumers also have the ability to select services from other competitors, such as VOIP providers. VOIP is already available from, or is now being deployed by, a wide range of companies, including national VOIP providers such as Vonage and AOL, traditional wireline carriers, and numerous other national or regional providers.

Consumers have made clear by their choices in the marketplace that they like the convenience and cost savings associated with these kinds of bundles. Going forward, I expect that many companies will continue to compete by trying to improve their bundled offerings – by including additional services and innovative features, by enhancing service quality and security, and by reducing consumers' costs. Clearly, consumers are benefiting now from the direct and aggressive intermodal competition between cable and phone companies, as well as wireless operators. I also expect, however, that new platform technologies will emerge to exert competitive pressure on the marketplace – including new wireless broadband providers, power companies, and ISPs -- as well as VOIP and other IP-applications providers. Emerging competition, both within and between different modalities, promises to ensure a continuing, competitive telecom marketplace.

<u>David Dorman's responses to questions submitted by Senator Kohl</u>

1. AT&T and MCI have been for years the nation's two largest competitors to the Baby Bells for local phone service. Last year, after the FCC rules changed, both AT&T and MCI withdrew from actively marketing local and long distance service to residential consumers. Now AT&T and MCI have agreed to be bought by their main rivals, the Baby Bells. Does this development mean that competition from independent local wire-based phone companies — the so-called "CLECs" — is now over and that the competitive vision of the 1996 Telecom Act has failed?

The 1996 Telecom Act was designed to foster competition, investment, and innovation in telecom markets – and as such was fully supported by AT&T. In AT&T's view, Congress sought to achieve not only intermodal competition, but also intramodal competition by allowing competitive carriers to lease access to the Baby Bells' network facilities.

By these measures, there were significant successes and significant disappointments following the Act. Subscribership to broadband Internet access continues to grow. Cable companies and the Bell companies are now finally entering each other's core markets. And there has been a massive increase in the deployment of intercity fiber networks.

There have been, however, substantial disappointments. Most notably, Congress' goal of creating effective intramodal competition for mass market customers has largely not been achieved. The disappointments do not reflect a failure of the Act. In AT&T's view, the disappointments reflect the failure of the FCC and the courts to remain faithful to the letter and competitive vision of the Act. AT&T made the painful decision to cease marketing traditional mass market services only after it was clear that the FCC would not adopt regulations that were sufficient to provide AT&T with the ability to offer competitive local and long distance services to mass market customers.

That said, however, there is significant and growing competition with the Bells, coming from cable, wireless, and independent VoIP providers. In addition, there remain wireline-based phone companies with facilities and commitment to compete against the Bells, particularly in the business market. Thus, this competition is not "over," though significant challenges do remain. The ability of these wireline carriers to prosper will depend in significant part on industry-wide regulatory decisions, including particularly those concerning access to and pricing of local telephone company facilities.

2. AT&T and MCI have been two of the primary forces for phone competition over the last two decades. Before Congress, the FCC, and state regulatory bodies, your two companies have been vigorously pressing for the opening of the dominant phone networks controlled by SBC and Verizon. In numerous areas of telecom policy, you have fought the Baby Bells to gain a competitive foothold. However, with these mergers, you will not be continuing this battle.

Many commentators worry about the consequences of the removal of AT&T and MCI as independent competitors to the Baby Bells. They wonder if the interests of

competitors will be adequately represented before regulators and policymakers. How do you respond to these concerns?

I believe that the merger will *increase* the diversity of regulatory voices and *enhance* the quality of the advocacy before the FCC. This is because a combined AT&T-SBC will be a unique hybrid carrier that cannot be simply classified as either an "ILEC" or a "CLEC." The combined company will have in-region incumbent local telephone operations, out-of-region competitive telephone operations, and a global network. As such, it will have an incentive to advocate balanced regulatory policies that accommodate these diverse interests.

This new voice before the FCC can only improve the FCC's ability to craft appropriate regulations. At the same time, the merger of AT&T and SBC will not materially diminish the existing voices that are already well-represented in policy debates, including both "pure" ILECs and CLECs. In this regard, while some CLECs have claimed that the FCC cannot make sound decisions in the public interest unless AT&T continues its advocacy in the service of pure CLEC interests, there is no basis for that concern. Foremost, while AT&T often shared interests with other competitors, we did not represent the interests of other carriers. Given our decision to cease marketing traditional wireline services in the mass market, this is significant. Even absent the merger, we no longer would have been significantly pursuing interests beyond those of a global networking company.

In all events, after this merger, the United States will still have many CLECs, each of which will remain free to express its position on any regulatory issue, and trade associations that speak for CLECs in legislative and regulatory forums across the nation. As before, the FCC (and other policymakers) will be more than capable of deciding those CLEC arguments on the merits.

Finally, it is important to note that many of the issues that have divided the industry are receding in importance as a result of intermodal competition and technological change. Perhaps the most important issue now facing the industry is intercarrier compensation and universal service compensation. This issue transcends traditional ILEC-CLEC divisions. Indeed, SBC and AT&T and many other carriers reached a consensus how to address this issue well before AT&T and SBC agreed to this merger.

3. Many analysts predict that we are increasingly moving towards an industry where telecom services are being marketed to consumers in "bundles." The regional Bell phone companies are offering packages to consumers which include local phone service, long distance phone service, wireless phone service, and high speed Internet connections in one package for one flat rate. The only competitor to this bundle of services will come from the consumer's incumbent cable company, leaving the consumer with just two choices. I am concerned because having only two choices for a service does not make for good competition.

Do we have reason to worry that most consumers will be left with only two choices for their telecom services? How can we be sure that consumers will have a choice of more

than just their dominant local phone company and their cable provider for a bundle of telecom services?

At this time, there should not be significant concern that consumers will ultimately be left with only two choices for their communications needs. Technology is evolving at a breathtaking pace in the communications marketplace and holds the promise that, with this evolution, consumers will have more than two providers serving their communications needs. Policymakers can foster this evolution with policies designed to encourage investment in traditional as well as alternate last-mile broadband technologies, like wireless and broadband-over-powerline. Fostering investment in broadband technology will also help ensure that consumers have access to multiple broadband facilities as well as all of the communications applications that broadband enables. And with the advent of VoIP technology, these next generation broadband providers will be able to offer the same bundles of voice and data services as the Bell companies.

One need only consider wireless services to see how technology is enhancing customer choice. For example, wireless carriers are now deploying 3G networks that provide broadband capabilities that are comparable to cable modem and DSL. Thus, wireless carriers will not only be able to offer customers a bundle of "mobile" local and long distance service, but also increasingly mobile high-speed data services.

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April 19, 2005

Senator Arlen Specter
Committee on the Judiciary
United States Senate
224 Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Specter:

I appreciate the opportunity to appear before the U.S. Senate Committee on the Judiciary on March 15th to discuss Verizon's proposed merger with MCI. As requested, I am writing in response to your follow-up questions regarding my testimony.

Before answering the specific questions raised by the Committee, I would like to address a recurring issue they raise – whether Verizon would be willing to commit to various merger conditions. First, as I indicated in my testimony, I do not think conditions are necessary to ensure that customers continue to receive the benefits of competition that has transformed the communications industry in the past few years.

I believe the review process at the Department of Justice and the Federal Communications Commission will show that the combination of Verizon and MCI is strongly in the public interest and will not impair competition in any relevant market. Verizon and MCI have highly complementary network assets and core competencies that will promote immediate efficiencies and long-term innovations that neither company could achieve on its own. To the extent that Verizon and MCI do compete for certain groups of customers today, there is intensifying competition for these customers from a growing number of other significant market participants. Under these circumstances, removal of one of the merging companies would not have any adverse effect on competition, and merger conditions are therefore unnecessary to protect consumers.

In any case, discussions of merger conditions are premature at this point in time. The need for merger conditions is traditionally discussed if at all at the end of this process, after the merging parties have had a chance to evaluate and respond to various concerns regarding any potential lessening of competition. It is too early to jump to any conclusions about the outcome of this process.

1. *At the hearing, you stated that Verizon had never blocked or disrupted any consumer's access to VOIP phone service, and would not do so in the future, but you would not agree to a merger condition on this issue. If Verizon will not block or disrupt access to VOIP, why will you not agree to a merger condition to this effect?*

For reasons described above, I think it is premature to discuss whether Verizon would agree to any potential merger condition, including a condition not to block or disrupt access to VoIP services. I testified that Verizon in fact has not blocked or disrupted any consumer's access to VoIP services and would not intentionally do so in the future, and there is no ground for imposing a merger condition. To the contrary, the fact that Verizon has been providing Internet access services to customers since 1998, and has not received a single complaint that it has restricted access to VoIP demonstrates that such a condition is unnecessary. Verizon itself is a provider of VoIP services and therefore relies on other carriers not to block access.

Verizon faces extensive competition in the provision of Internet access services from cable operators, and new forms of competition are arising from technologies such as Broadband over Powerline, Wi-Max, and 3G mobile wireless networks. To the extent that Verizon tries to restrict the use of its own Internet access service to VoIP or other content or services, consumers will choose these other competitive alternatives, and the threat of that occurring ensures that Verizon will not take steps to restrict the use of its Internet access service in the first instance. Requiring such access as a merger condition would therefore be unnecessary. It also would be counterproductive because subjecting Verizon, but not other competitors, to onerous regulatory conditions tilts the playing field and introduces marketplace distortions.

2. *We hear a lot these days about the new forms of phone technologies such as VOIP, cable telephony, Wi-Fi, and Wi-Max which use high speed wireless Internet services to avoid the entire local phone network to the consumer. But at some point these new technologies for making phone calls must connect to the conventional phone network to complete the call. So the ability to interconnect to the conventional phone network is crucial for these new technologies to compete. Many are concerned with the ability of these competitors to obtain interconnection agreements at commercially reasonable rates with the established Baby Bell phone companies.*

   Will the phone networks that Verizon will control should your merger be completed be open to allowing these new phone technologies to interconnect, and at reasonable rates?

Yes. Under section 251(a) of the Telecommunications Act of 1996, Verizon is required to "interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers." Under section 251(b)(5), Verizon is required to "establish reciprocal compensation arrangements for the transport and termination" of local telecommunications traffic. As a result of these obligations, Verizon is required to provide other local telecommunications carriers access to its local network, regardless of what technology they use to provide local service. Under separate regulations promulgated by the FCC, Verizon also is required to provide information service providers access to its network at just and reasonable rates. The Verizon/MCI transaction does not affect these regulatory obligations in any way. In fact, there is no correlation between the issue described in your question and the transaction, which does not expand Verizon's local footprint or otherwise affect Verizon's incentives or ability to restrict interconnection.

3. *MCI has acquired and developed local phone networks in major cities that serve business customers and compete with facilities owned by Verizon. Should your proposed merger with MCI be completed, will you agree to divest these duplicative facilities to ensure that these facilities are made available to competitors?*

For reasons described above, I do not think it is appropriate at this stage to discuss whether Verizon would agree to any potential merger condition, including a condition to divest any duplicative facilities that MCI currently operates. Nor do I believe such a condition is necessary in order to ensure robust competition for business customers.

As you point out, MCI's local networks are located primarily in "major cities." Although Verizon also has facilities in some of these cities, so do a number of other competitors besides MCI. For example, based on the data that Verizon and MCI have compiled thus far, there are approximately 39 geographic areas where Verizon and MCI have overlapping fiber network facilities. In these 39 areas, there is an average of six providers with fiber facilities in addition to Verizon and MCI. In 92 percent of these areas, at least two or more carriers compete with Verizon and MCI using self-deployed fiber, and there is at least one such competitor in all but one of these areas. (That one area is in Carbondale, Illinois, where MCI's local fiber network overlaps with only a single Verizon wire center.)

Thus, even after this transaction, the areas where MCI's local fiber networks overlap with Verizon's network will still have other competitive fiber networks. These alternative providers include large and small telecommunications companies – including AT&T, Global Crossing, TelCove, and XO/Allegiance – and non-traditional providers, such as affiliates of electric utilities and cable companies. These competing carriers routinely bid against MCI for business customers in the areas where MCI has deployed its own local fiber network.

4. *Although it is no longer actively marketed, MCI's "Neighborhood" service is still one of the nation's largest local phone competitors with about 3 million customers nationally. Should Verizon's bid for MCI be successful, will you commit to continue to offer MCI's competitive local phone service outside the Verizon region?*

For reasons described above, I do not think it is appropriate at this stage to discuss whether Verizon would agree to any potential merger condition, including a condition to continue offering

MCI's Neighborhood service outside the Verizon region. And, once again, I do not believe such a condition is necessary to protect competition for consumers.

As an initial matter, it is important to recognize that, independent of this transaction, MCI made the decision to exit the consumer business. MCI made this decision based on a number of factors, including intense competition from cable, wireless, traditional wireline companies, and new technologies like VoIP and e-mail; restrictions on marketing resulting from Do Not Call legislation; and regulatory changes that affect MCI's ability to provide the Neighborhood service. Although you are correct that MCI still serves roughly 3 million customers nationally with the Neighborhood, that total is rapidly shrinking. And these declines are likely to continue, particularly given that MCI has increased prices for its local customers and has plans to continue to do so in the future.

In addition to the fact that MCI is exiting the consumer market – and that, as a result, there will be little of that business left to continue regardless of the Verizon/MCI transaction – MCI's Neighborhood cannot be considered one of the more important choices for consumers going forward. Rather, it is now clear that, as a result of the introduction and adoption of new technologies that have reshaped the industry, the most significant competition for mass-market customers will come from facilities-based intermodal competitors such as cable and wireless. Customers now view cable and wireless as viable alternatives to wireline telephone service, and that acceptance will only grow going forward. Other services such as VoIP, e-mail, and instant messaging impose still further discipline on the market. This transaction does not affect this intermodal competition. MCI is not providing facilities-based intermodal mass-market competition today, and it has no plans to do so in the future, for reasons that have nothing to do with this transaction. Thus, with or without this transaction, there will continue to be a large number of options for consumers.

5. *Many analysts predict that we are increasingly moving towards an industry where telecom services are being marketed to consumers in "bundles." The regional Bell phone companies are offering packages to consumers which include local phone service, long distance phone service, wireless phone service, and high speed Internet connections in one package for one flat rate. The only competitor to this bundle of services will come from the consumer's incumbent cable company, leaving the consumer with just two choices. I am concerned because having only two choices for a service does not make for good competition.*

   Do we have reason to worry that most consumers will be left with only two choices for their telecom services? How can we be sure that consumers will have a choice of more than just their dominant local phone company and their cable provider for a bundle of telecom services?

No, I do not believe you have reason to worry that most consumers will be left with only their local phone company and their cable operators as their provider for a bundle of telecom services. Before I explain why, however, it is important to emphasize that this transaction does not affect how many options consumers will ultimately have. As I explained in response to Question 4 above, MCI decided to exit the consumer market independent of this transaction. Moreover, even when it was actively serving consumers, MCI provided local service almost exclusively by reselling the service of incumbent local telephone companies, not by deploying its own network facilities. MCI also did not offer wireless services or broadband services to any meaningful degree. Thus, MCI did not at any time offer the bundles of service that you describe, and even the services it did offer were in large part provided using other carrier's networks.

With respect to your question, there are already a number of options that consumers have beyond their cable and local telephone companies. For example, consumers can choose among multiple mobile wireless providers. These providers already offer voice services that compete directly with wireline local and long distance services, and they are rapidly rolling out data services that are comparable to cable and DSL services. Verizon Wireless has already deployed its broadband EvDO service in 30 major markets across the country, and other wireless carriers are now following suit. Consumers also can use their cable connection to obtain voice services not only from their cable company, but from a wide variety of other providers, such as Vonage, Packet8, BroadVoice, and Lingo.

In addition to the choices that are widely available today, there are likely to be an even greater number of competitive alternatives available in the future. Technologies such as Broadband over Powerline and Wi-Max have already been commercially deployed in some areas. Both the FCC and independent analysts believe that these technologies will become more prevalent in the future.

6. *Over the years we've heard a lot of promises from the Baby Bells that they would compete outside of your regions with each other. Yet, these promises never seem to be realized.*

   (a) Other than wireless phones, what can you cite as competition between the Baby Bells other than wireless?

Verizon competes with other Bell companies in a number of respects other than wireless. Of course, such wireless competition should not be downplayed, as wireless now represents approximately a third of the entire telecommunications industry, and is still the fastest growing segment of the industry. Wireless is used by all kinds of customers, from residences to the largest businesses. And it is used for all kinds of services, including local and long distance and increasingly data services. Because the Bell companies are competing in wireless, they are competing for a large share of the entire industry, and for all kinds of customers and services.

In addition to wireless, Verizon and other Bell companies compete in a number of respects. First, they compete for consumer voice and broadband services. For example, Verizon, SBC, Qwest, and BellSouth each offers long-distance service throughout the U.S. in competition with one another. Verizon has launched a consumer voice-over-IP service called VoiceWing, to which anyone in the country can subscribe using a broadband connection. SBC and Qwest similarly have launched consumer VoIP services that they offer out of region. Verizon made a substantial investment in Verizon Avenue which bundles local and long-distance service together with high-speed Internet access, and offers service to high-rise properties, apartment complexes, and condominium communities in major metropolitan markets. Verizon Avenue has competed, for example, with SBC in Chicago; Los Angeles; Dallas; Middletown, CT; and Tulsa.

Second, the Bell companies compete extensively for enterprise customers. Verizon competes for enterprise customers in 28 out-of-franchise areas, 17 of which are in SBC's service area. Verizon operates a frame relay network serving SBC, BellSouth, and Qwest cities including Atlanta, Chicago, Houston, Kansas City, Miami, Phoenix, Salt Lake City, San Francisco, Seattle, and Stamford, Connecticut. Verizon operates an IP/MPLS fiber network with hubs in SBC, BellSouth, and Qwest cities including Atlanta, Chicago, Dallas-Fort Worth, Denver, Los Angeles, and San Francisco. Verizon has deployed 300 miles of optical network facilities in Los Angeles to compete in SBC's franchised territory. Verizon has extended its optical fiber in Dallas by approximately 200 miles to compete in SBC territory. Verizon has extended its optical fiber in Seattle by over 100 miles to compete in Qwest territory. SBC Telecom competes with Verizon for business customers in Albany; Baltimore; Bergen-Passaic, NJ; Boston; Charlotte; Middlesex, NJ; Nassau-Suffolk, NY; New York City; Newark; Norfolk, VA; Philadelphia; Tampa; and Washington, DC. Qwest also competes extensively for enterprise customers outside its region, and has deployed local fiber networks in a number of cities in Verizon's, SBC's, and BellSouth's regions.

Third, the Bell companies compete in the provision of dial-up Internet access. Verizon's dial-up Internet access service is available nationwide. SBC Yahoo! dial-up Internet access service is available in all 50 states, plus the District of Columbia.

Fourth, the Bell companies compete in the provision of directory services outside their traditional local franchise areas. For example, Verizon publishes independent directories in dozens of SBC markets in California, Texas, Michigan, Ohio, and Wisconsin. Both Verizon and SBC also have online yellow pages. Both Verizon's SuperPages and SBC's SMARTpages.com are national in scope.

Fifth, the Bell companies compete in the provision of conference call services. For example, Verizon recently introduced an on-demand conference call service available to businesses anywhere in the country.

Finally, the Bell companies compete in the provision of E911 services. For example, Verizon and SBC have competed outside their franchise areas in the provision of E911 service in several major markets in Texas and California, including Dallas and Los Angeles.

(b) Should the SBC/AT&T and Verizon/MCI mergers be completed, will we see Verizon, SBC, BellSouth and Qwest compete with each other outside in their regions and, if so, in what respect?

As shown above, these companies already are competing extensively today, and there is no reason to believe that either the SBC/AT&T or Verizon/MCI mergers would lessen that competition in any way. Instead, the Verizon/MCI merger is likely to intensify that competition, particularly in the enterprise segment, by enabling Verizon to become a strong competitor for large enterprise customers that typically operate on a national or global scale. Today, Verizon is at most a minor competitor for these customers, and has won very little of these customers' business outside of its region.

(c) We recognize that one area you claim that the Baby Bells compete with each other outside their regions is with respect to wireless phones. But are wireless phones really a substitute for traditional wired phones for most consumers, especially families with children? In the Verizon region, what percentage of consumers go without landline phones and substitute wireless phones?

Wireless carriers compete directly with wireline carriers both for second and third lines and to an increasing extent for primary lines, and even more extensively for local and long-distance calls. Verizon does not have data on the percentage of consumers within its region that have replaced their landline phone with a wireless phone. According to independent sources, as of year-end 2004, wireless displaced approximately 11 million wireline access lines nationwide, and approximately 7-8 percent of wireless users had given up their landline phones; approximately three million additional wireless subscribers are now giving up their wireline phones each year; and at least 14 percent of U.S. consumers now use their wireless phone as their primary phone. Wireless networks are now displacing even larger volumes of telephone calls that previously used the wireline network. According to Merrill Lynch, approximately 29% of voice minutes in the US are now wireless. According to the Yankee Group, 60 percent of long-distance calls in households with cellular phones are now made on wireless phones. As these trends make clear, many consumers now view wireless service as an alternative to wireline service for many purposes.

Insofar as families with children are concerned, I assume your concern is that these families want to ensure that they have a wireline phone for purposes of emergencies at home. But families with children also are major users of wireless phones, and the wireless phone has become an invaluable tool for parents and children to contact each other in the case of an emergency.

7. We have been informed that when one of Verizon's customers who takes both phone service and DSL service wants to switch their telephone provider to a competitor, Verizon won't let that customer take their phone number with them unless they drop Verizon's DSL service. Is this true? If so, why doesn't Verizon allow customers who want to keep your DSL service but switch their phone providers take their numbers with them?

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Verizon originally deployed DSL as a consumer service to be provided as an add-on to voice service provided over the same line. Certain consumers – for example, consumers who wish to abandon wireline telephone service in favor of wireless service – may wish to purchase DSL on a stand-alone basis. To that end, Verizon previously announced that it was developing and planned to offer a product that would enable customers to purchase DSL without underlying voice telephone service.

Because Verizon has not previously had the capability to provide customers with DSL on a stand-alone basis, customers who wished to port their telephone number to another voice service provider have had to disconnect their DSL service in order to do so. However, Verizon has now introduced the capability in certain of the states we serve for customers that have both DSL and voice service on their line to port their telephone number to another voice service provider and retain their DSL service. This is our first step in offering a stand-alone DSL service, and is available initially in the 13 states and the District of Columbia served by the former Bell Atlantic telephone companies. The ability to obtain stand-alone DSL service in additional states and in additional circumstances will follow.

If you have any further questions please contact me.

Sincerely,

Ivan Seidenberg

Responses to Questions from Senator Coburn

1. It is my understanding that SBC uses an Oklahoma company, WilTel Communications, for national fiber network services. How is this merger with AT&T going to impact WilTel?

   A. SBC Communications Inc. ("SBC") and WilTel Communications, LLC ("WilTel") are parties to a Master Alliance Agreement (the "MAA") that was originally entered into on February 8, 1999, between SBC and Williams Communications, Inc., WilTel's predecessor. In connection with the MAA and related agreements between SBC, WilTel and their respective affiliates, WilTel provides SBC certain telecommunications services (including transport services) and SBC provides WilTel certain other telecommunications services. These agreements contemplate the possibility that SBC might acquire a national telecommunications carrier (such as AT&T Corp. ("AT&T")) and prescribe each party's rights and obligations in the event such an acquisition were to occur. SBC is unable to say conclusively how its merger with AT&T will impact WilTel at the present time, but SBC will continue to abide by the terms of the MAA and related agreements.

2. If SBC agrees to honor its contract with WilTel, please explain what that will mean to WilTel.

   A. As previously stated, there is no question that SBC will honor its contracts with WilTel and abide by their terms, but at present SBC is not in a position to opine on what its merger with AT&T will mean to WilTel.

3. It is my understanding that WilTel's network currently provides excellent service to SBC's 20 million long-distance customers and the majority of their data services customers.

   (a) Do you plan to move all that traffic off of WilTel's network and onto AT&T's network?

      A. SBC has not formulated a definitive plan or timetable with respect to its post-merger voice and data traffic, but is evaluating how to provide the highest quality, cost-effective solutions for SBC's customers, now and in the future. As part of this evaluation, SBC is working with WilTel's management in the context of the parties' contractual relationship. In any event, SBC will not execute any plan that would violate any of SBC's contractual obligations to WilTel.

   (b) If so, how soon?

A. See response to Question 3(a).

4. Is there some way you can manage this merger to help WilTel to survive as a competitor?

   A. What SBC can and will do is continue to honor its contractual obligations to WilTel. Beyond that, SBC does not have an opinion on WilTel's future prospects, but is confident, for the reasons provided in the Public Interest Statement filed with the FCC, that SBC's combination with AT&T will enhance competition in the telecommunications industry.

Responses to Questions from Senator Schumer

1. Over the last several years, we have seen fierce competition in the long distance market. In fact, for the past four or five years, long haul prices appear to have dropped 30% to 50% each year. Before the House Energy and Commerce Committee on March 2, 2005, you talked about a similar degree of competition in the local market, referring specifically to Houston, Texas as a highly competitive market with "dozens of CLECs" (Competitive Local Exchange Carriers). Over the last several years, have we seen a drop in residential or commercial dial tone prices in Houston and in many other local markets across the country that corresponds to the growth of competition in the local phone marketplace? If not, why?

   A. Looking at basic dial tone rates in isolation offers little insight into the current state of competitive pricing in the communications industry. These rates have been kept artificially low for decades as part of a long-standing federal and state communications policy of universal service. After the divestiture of the Bell Operating Companies from AT&T in 1984, this policy continued through the use of explicit and implicit subsidies, such as access charges, expressly designed, again, to keep basic residential dial tone rates artificially low, often well below cost. While federal and state reform efforts since the passage of the 1996 Telecommunications Act have rationalized the subsidy structure to a certain extent, there was little or no room to *decrease* already artificially low dial tone rates.

   Notwithstanding the elimination or decrease in these supportive subsidies, dial tone rates generally have remained stable. For example, the residential and business dial tone rates for Houston are approximately $11 and $28, respectively. Neither of these rates has changed *for over 20 years*. And, consumers have enjoyed this price stability even though the cost structure of our circuit-switched network actually has increased over the past decade due to higher labor costs, including health care and benefits, and the need for continuing technological upgrades.

   Aside from the narrow question of subsidized dial tone rates, the communications industry is now characterized by its ever-growing competition and reducing prices. Today, cable companies, wireless providers and IP-service providers are aggressively competing to provide a full complement of communications services to customers in direct competition with SBC's traditional telecommunications services. Texas, for example, reflects these trends. ILEC share of statewide communications connections has decreased from 52% in June 2001 to only 38 % in June 2004, with wireless substitution, CLEC gains, and a growth in broadband accounting for most of the decrease. Indeed, household wireless spending has now eclipsed wireline spending on a national basis. In the wireline segment in SBC Texas' service areas, CLECs now serve approximately 24% of customers. (A copy of SBC's "Trends in Competitive Communications Market in Texas" as of December 31, 2004, is attached for further information on the state of competition.) Moreover, these competitors focus on customers who purchase a broad suite of services, generally bundling basic dial tone service with other services such as voicemail, caller ID, long distance, and other services.

These healthy, competitive trends necessarily mean more choice and lower prices. It is estimated that, between the 4th Quarter 2002 to the 4th Quarter 2004, in SBC's traditional 13-state service territory, local prices declined by 6.7% (or \$2.13 – from \$33.83 down to \$31.70); toll prices declined 133% (or \$1.60 – from \$2.80 down to \$1.20); and long distance prices declined by 26.4 % (or \$2.12 – from \$10.16 down to \$8.04). *See* TNS Consumer Market Share Quarterly Summary Report 4Q04 (March 2005) at 31.

SBC has responded with competitive bundles and packages of its own, providing substantial savings over *a la carte* pricing. SBC companies currently offer All Distance® services, which include the access line, 3 vertical features, voicemail, Linebacker[1] and unlimited domestic long distance calling. In Texas, the packaged price is \$48.95. A customer saves between \$15.93 and \$21.17 by purchasing the All Distance® package as compared to purchasing the same services on an *a la carte* basis. Likewise, business customers benefit from SBC's Custom BizSaver® services, which include the access line, 5 features, and unlimited local calling. The single line package price is \$38.99, saving the customer \$28.76 (42%) over *a la carte* pricing.

In addition, competition has led to significant price decreases for DSL Internet access service. In 1998, a customer paid \$49.95 per month for the service, with a \$400.00 charge for installation and the broadband modem. Today, just by way of one example, customers can sign a 12-month deal for the same service for \$29.95 a month – a savings of 40% – and get the modem for free.

2. You have stated that is no longer a meaningful distinction between local and long distance voice as a result of "all-distance" offerings in the wireline and wireless markets, and also the emergence of new technologies such as VoIP. If that is the case, why haven't the introduction of these new offerings led to a drop in local phone rates?

   A. See response to Question 1.

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[1]Inside wire maintenance service

3. I understand that SBC has announced plans to spend billions of dollars to replace today's local network with a fiber-to-the-node architecture. What steps are you taking to build this next-generation network, and what are your plans for the current local network? What assurances can you give that local phone competitors will have access to your new fiber network for the provision of competitive local phone service?

   A. We are not replacing the local network. Our Project Lightspeed project, like our Project Pronto DSL deployment, will increase the capabilities of our existing networks to bring consumers an array of IP-based voice, Internet access and video offerings. In its initial phase, Project Lightspeed will entail a $4 billion capital initiative to deploy next-generation equipment and 40,000 miles of fiber deep into our customers' neighborhoods. We will use a combination of fiber-to-the-node and fiber-to-the-premises technologies to reach 18 million households across 13 states by the end of 2007.

   These networks, which entail significant risk and investment, should not be subject to traditional competitor-access obligations. As the FCC has recognized, requiring telephone companies to share the fruits of risky investment in new technologies and services – services that do not rely on the legacy network, that are subject to significant intermodal competition, and the demand for which is still unknown – would reduce incentives to make those investments. More to the point, doing so would be in direct contravention of one of the principal stated goals of the 1996 Act, namely to promote the deployment of advanced infrastructure to all Americans. For example, these fiber networks will allow companies like SBC to offer high-quality, feature-rich video services to compete with incumbent cable offerings and other video providers. That kind of innovative, facilities-based competition is good for consumers.

   Nonetheless, in areas where copper facilities already exist, we will continue to maintain those facilities and provide competitors with access to them, as required by the FCC's rules and regulations. While SBC has no current plans to retire any particular copper facilities, the FCC regulates the retirement of such facilities and, among other things, requires that we provide competitors with access to a basic voice channel over our new fiber facilities if and where we retire existing copper. We will, of course, comply fully with all FCC rules.

Responses to Questions from Senator Kohl

1. At the hearing, you stated that SBC had never blocked or disrupted any consumer's access to VOIP phone service, and would not do so in the future, but you would not agree to a merger condition on these issues. If SBC will not block or disrupt access to VOIP, why will you not agree to a merger condition to this effect?

   A. To reaffirm, SBC does not, and would not, block VoIP traffic. SBC is a provider of VoIP services to business customers today, and will be an ever more determined competitor for VoIP customers in the future. AT&T has developed a consumer-oriented VoIP service called CallVantage, a capability that SBC does not currently have; however, due to limited resources and AT&T's decision to focus on serving large business customers, AT&T is not currently directly marketing its CallVantage service. The combined SBC and AT&T, will have the resources and incentive to more aggressively market VoIP services to the consumer and small business segment of the market, both inside and outside of SBC's traditional in-region service territory. Thus, we have a vested interest today, and an increased interest post closing, in ensuring that VoIP traffic can be delivered to its intended destination on the PSTN without being blocked. To the extent there are concerns about VoIP blocking, however, SBC believes the best way to address those concerns is through rules that apply evenhandedly to *all* providers. There are more than one thousand incumbent local exchange carriers in the United States, as well as numerous competitive local exchange carriers, long distance providers, wireless providers, VoIP providers, and other service providers. Thus, it would not be effective to create a separate set of requirements just for SBC without addressing all of the other communications providers in the marketplace. Instead, if a need arises to address VoIP blocking, SBC believes the FCC -- which already has shown its willingness to swiftly tackle concerns about VoIP blocking -- is well equipped to adopt uniform rules for the communications industry.

2. We hear a lot these days about the new forms of phone technologies such as VOIP, cable telephony, Wi-Fi, and Wi-Max which use high speed wireless Internet services to avoid the entire local phone network to the consumer. But at some point these new technologies for making phone calls must connect to the conventional phone network to complete the call. So the ability to interconnect to the conventional phone network is crucial for these new technologies to compete. Many are concerned with the ability of these competitors to obtain interconnection agreements at commercially reasonable rates with the established Baby Bell phone companies.

Will the phone networks that SBC will control should your merger be completed be open to allowing these new phone technologies to interconnect, and at reasonable rates?

A. SBC is always willing to engage in good faith commercial negotiations with any provider that wants to connect with our networks at reasonable rates. In fact, selling connectivity services to other providers is a large part of SBC's business today and we plan to grow that business in the future. Moreover, in addition to providing traditional telephone service over our existing local telephone network, SBC is also heavily engaged in using other technologies to provide communications service to our customers. For example, we are a joint owner of Cingular Wireless, as well as a provider of long distance service, a provider of VoIP services to business customers, and a provider of Wi-Fi hotspots across the country. Just like our competitors who offer these services, SBC needs to be able to ensure that all of our services can obtain connectivity with other providers' networks at reasonable rates throughout the nation. Therefore, it is in the best interests of SBC and our customers to negotiate commercially reasonable rates with providers seeking connectivity to our network, so that those providers will offer SBC commercially reasonable rates when we seek connectivity to their networks.

3. AT&T has acquired and developed local phone networks in major cities that serve business customers and compete with the facilities owned by SBC. Should your proposed merger with AT&T be completed, will you agree to divest these duplicative facilities to ensure that these facilities are made available to competitors?

A. As Mr. Dorman made clear in his testimony before the Senate Judiciary Committee, and as stated in declarations submitted to the FCC, AT&T has irreversibly exited the mass market segment of the telecommunications industry. This includes ceasing all active efforts to market to mass market customers. Thus, there will be no substantial lessening of competition for mass market consumers. Larger business consumers have many choices for local service and they too will not face any anticompetitive effects. Thus, we feel there is no reason for any divestiture of network facilities.

We have not yet made any decision regarding the specifics of integrating the SBC and AT&T networks. We understand that AT&T's local facilities are fully integrated into its network for providing long distance and other services and are used substantially to serve large business customers. One of our goals in the merger is to enhance our ability to serve those customers both inside and outside our traditional local service territory. We would not want to take any actions that would jeopardize or interfere with the service AT&T currently provides to those customers.

4. Although it is no longer actively marketed, AT&T's local phone service is still one of the nation's largest local phone competitors with about 3 million customers nationally. Should SBC merger's with AT&T be completed, will you commit to continue to offer AT&T's competitive local phone service to consumers both within and outside the SBC region?

    A. SBC is spending billions of dollars to acquire AT&T. To maximize the return on that investment, SBC hopes to continue to serve all of AT&T's current customers and to use all of AT&T's assets to compete for the business of all customers in the most efficient way possible.

    Most of AT&T's current local residential and small business customers are currently served using the local networks of SBC and the other incumbent local exchange companies (so called "UNE-P" customers). In order to stimulate the development of facilities-based competition, the FCC has decided to eliminate the requirement that incumbent providers support UNE-P starting in March 2006. At that time, even if this transaction did not take place, AT&T would need to make new arrangements to serve these customers. Therefore, if and when the proposed transaction closes, we will need to determine how we can best compete to provide local services outside SBC's region. For example, even though AT&T's consumer VoIP service has not been as successful in the marketplace as many other VoIP services – and in any event is not being directly marketed by AT&T – we intend to utilize SBC's experience and expertise in marketing services to consumers, and the improved financial capabilities of the combined company, as compared to AT&T on a stand-alone basis, to offer VoIP services to consumers across the country far more effectively than has AT&T.

5. Many analysts predict that we are increasingly moving towards an industry where telecom services are being marketed to consumers in "bundles." The regional Bell phone companies are offering packages to consumers which include local phone service, long distance phone service, wireless phone service, and high speed Internet connections in one package for one flat rate. The only competitor to this bundle of services will come from the consumer's incumbent cable company, leaving the consumer with just two choices. I am concerned because having only two choices for a service does not make for good competition.

    Do we have reason to worry that most consumers will be left with only two choices for their telecom services? How can we be sure that consumers will have a choice of more that just their dominant local phone company and their cable provider for a bundle of telecom services?

    A. We agree that cable companies are, and will increasingly be, very effective competitors in the provision of bundles of communications services. They are not, however, the only competitors we face now or are likely to face in the future. Whether for bundled or *a la carte* services, competition is also coming in the form of IP technology, for voice, data and video services, offered not only by cable companies but also by independent IP-based firms, wireless providers, CLECs, and other traditional telecommunications carriers. New forms of broadband – WiFi, WiMAX, other broadband wireless access, even satellite – make this competition ubiquitous and many-sided. Many firms are and will be able to provide a wide variety of voice, data and video services as these new broadband technologies become more widespread. Some of those firms will own broadband facilities; some will not, but will nonetheless be able to successfully offer consumers various communications services. For example, Vonage has had considerable success selling VoIP services.

In addition, SBC and other wireline carriers are facing increasingly strong competition from wireless providers for voice and data services and, now, for high-speed Internet access. Consumers everywhere have a choice among numerous wireless carriers. Even after the proposed Sprint-Nextel merger, there will be four strong national wireless carriers along with numerous regional and local providers. Not only are wireless companies expanding the capabilities of their networks to provide high-speed Internet services, but they also are partnering with other firms to provide a full package of services competitive with wireline companies.

In addition, there are – and will remain – competitors using traditional local phone networks, including many smaller competitive local phone companies that are quite successful on a regional basis.

6. Over the years we've heard a lot of promises from the Baby Bells that they would compete outside of your regions with each other. Yet, these promises never seem to be realized.

   (a) Other than wireless phones, what can you cite as competition between the Baby Bells other than wireless?

      A. SBC has invested over a billion dollars over the past five years to develop telecom facilities in 30 Metropolitan Statistical Areas outside its region. It has sought and will continue to seek to use these facilities to compete with other RBOCs (as well as other companies) for the full range of consumer telecommunications services in these areas, starting with locations adjacent to its traditional service territory (for example, Las Vegas, outside Dallas, and outside Los Angeles). For over a year, SBC has also actively sought to compete for the voice and data needs of business customers both in and out of its region.

To date, SBC's success in these efforts to make forays into other RBOC and ILEC territories has been mixed: business customers with largely in-region presence have begun to use SBC services outside SBC territory, but few customers with more than half of their locations outside SBC territory have done so. In large part, SBC's success has been limited because competition – not only from the other RBOCs and ILECs but also from a wide range of other service providers – is (and will remain) fierce both in and out of SBC territory. We already see other RBOCs (particularly Verizon and Qwest) competing in SBC territory.

(b) Should the SBC/AT&T and Verizon/MCI mergers be completed, will we see Verizon, SBC BellSouth and Qwest compete with each other outside in their regions and, if so, in what respect?

A. SBC's acquisition of AT&T will significantly build on SBC's existing efforts to develop an out-of-region presence by adding both AT&T's extensive national network and AT&T's local facilities in areas where SBC has none. As such, the acquisition will bring SBC into increased competition with the other RBOCs on a full range of local and long-distance voice and data services for customers of all types. We already see other RBOCs (particularly Qwest and Verizon) competing against us where we are the incumbent local exchange company and we expect all three of the other RBOCs to step up their efforts to compete with SBC in SBC territory, both as an ordinary competitive response (independent of any acquisitions they may make) and using expanded geographic presence through acquisitions of their own.

(c) We recognize that one area you claim that the Baby Bells compete with each other outside their regions is with respect to wireless phones. But are wireless phone really a substitute for traditional wired phones for most consumers, especially families with children? In the SBC region, what percentage of consumers go without landline phones and substitute wireless phones?

A. There is an unmistakable trend towards consumer use of wireless phones in place of their wireline phones. A Standard & Poor's analyst recently estimated the proportion of customers using wireless exclusively at 10-15 percent of the total market. A recent analysis showed that this trend is continuing: Seven percent of SBC local telephone customers said they were likely to switch from wireline to wireless in the next 12 months alone, and another 16 percent said they may switch in that time frame. *See* TNS Consumer Market Share Special Studies Report 4Q04 dated March 2005 ("TNS Study") at 22.

Of equal or greater importance, consumers are migrating minutes of use from wireline to wireless, using their wireless phones more in place of the wireline local and long distance service provided by carriers such as SBC and AT&T. The analysis referenced above showed that 38 percent of SBC's local service households are making 40 percent or more of their calls on wireless phones. *See* TNS Study at 24. This is consistent with a national estimate that, in 2004, in households with wireless phones, wireless calls replaced 60 percent of the wireline long distance calls and 35 percent of local calls. *See* Yankee Group Report, "Divergent Approach to Fixed-Mobil Convergence" (January 2005) at 7.

We cannot ignore these significant trends affecting our wireline business. While not every customer may choose to cut the cord and abandon wireline phones, a significant number can and are doing so.

SUBMISSIONS FOR THE RECORD

U.S. SENATOR SAM BROWNBACK

Senate Judiciary Committee

Hearing on "SBC/ATT and Verizon/MCI Mergers – Remaking the Telecommunications Industry"

March 15, 2005

OPENING STATEMENT

Thank you, Chairman Specter, for calling this very timely and important hearing on two of the many pending mergers taking place in the telecommunications industry. I know the House Energy and Commerce Committee held a very insightful hearing earlier this month, so I am pleased that we, in turn, are taking an in-depth look at these historic changes before us from a Judiciary Committee standpoint.

If lawmakers were told as they wrote the '96 act that within ten years, SBC and AT&T would be merging, I don't think they would have believed it. Today, it makes perfect sense, and it's hard to find someone who does not believe this merger will go through. So much has changed in such a short period of time. It's been amazing to watch how quickly the new communications innovations, such as the Internet and wireless technology, have transformed the telecommunications industry.

I strongly support the SBC-AT&T union. Mergers create a larger, stronger, more financially secure company. This benefits both customers and employees because it takes advantage of economies of scale - in other words, the cost per customer of running two separate companies is much higher than it will be for the combined company. This can foster innovation and improvements in prices and services. And any short term job loss will give way to the creation of even more jobs as companies grow and advance.

The reason these telecom mergers are occurring is because they need to occur. The industry is recovering from a severe slump. Instead of continuing to beat each other up, these companies need to become financial healthy enough to grow and enhance their networks. I think network building is the main thing we are looking for out of these mergers because Internet Protocol and broadband technologies are revolutionizing communications allowing one platform for the offering of voice, video and data services. The convergence of these services is taking competition from an intra-modal race to an inter-modal race in which we will quickly see the combined Bell-Long Distance companies compete against cable, wireless and satellite providers.

It is important to remember that the telecom industry is a very powerful economic engine in this country. Its health affects so many other aspects of our economy as well as our quality of life. Moreover, the ability for individuals and businesses to communicate quickly, efficiently, and inexpensively will greatly determine our ability to compete in the world. The United States still ranks 11^{th} in the world in broadband deployment. We have to change that. We cannot allow ourselves to be left behind. I hope the Department of Justice will keep these things in mind as they review these mergers.

Thank you again, Chairman Specter. I look forward to the testimony of the witnesses.

STATEMENT OF

MICHAEL D. CAPELLAS

PRESIDENT & CHIEF EXECUTIVE OFFICER

MCI, INC.

BEFORE THE

COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

MARCH 15, 2005

Good afternoon. My name is Michael Capellas. I am the President and CEO of MCI. Thank you, Mr. Chairman and Members of the Committee, for giving me the opportunity to testify today about the changing structure of the telecommunications industry. Over the past five years, our industry has undergone a series of fundamental shifts – in technology and in the evolution of the marketplace, as well as in the legal and regulatory environment. The as yet untapped potential of the Internet guarantees even greater change in the future.

The combination of Verizon and MCI is a reflection of the need for both companies to re-position themselves in order to compete effectively to meet customer demands. The purpose and effect of the merger is to make the company a stronger competitor in what is and will remain an intensively competitive market. Residential, business and government customers will be the beneficiaries. Policymakers should encourage this marketplace evolution.

Introduction: A Technologist's Perspective

While I have been CEO of MCI for roughly the past two and a half years, I'd like to start by saying that I bring a different perspective to this discussion, having spent the past 30 years of my career in the computing industry before I arrived at MCI. I was previously CIO for two global Fortune 50 companies and CEO of Compaq and President of HP.

My life's projects include designing and developing systems, from using supercomputers to solve complex human genome problems to utilizing web analytics to better understand consumers and their online buying patterns. Why is this relevant to the telecommunications industry? As I like to say, there has been a computer on both ends of the communications network for a very long time.

I have spent my professional career as a customer of telecommunications services, as a developer who used the power of global networks to fuel innovation and productivity, and I believe in the power and promise of technology.

How is computing leading the structural changes within telecommunications?

First of all, there is a movement within computing towards standardization. Basic computer building blocks such as servers, storage and microprocessors are standard devices that are addresses on a network and can reside anywhere. Second, the rise of Internet commerce accelerated the adoption of software standards that enable different systems to talk to each other. At the same time, new tools like web services are allowing developers to write applications across different platforms.

Today, communications travel over the network in what we call "packets." There is no difference between a voice or data packet over the network. Whether you are making a voice call or purchasing an MP3 music file, it is all the same – a packet is a packet.

The Internet-driven standards that allow systems to talk to each other have redefined network requirements. Formerly, local, long distance and data traveled separate network paths. Now, there's a need for integrated, intelligent paths which can carry voice, data and streamed video without the developer or end-user needing to know or care how the path is developed.

One does not need to be a computer scientist to see this in everyday life. A "Blackberry" is a great example of a simple device that can instant message, make a phone call, get news or sports, or stream a video. It is called integrated communications. In more technical terms, we call it wireless broadband to an IP network. This ability to do integrated communications is becoming commonplace around the world and the path for future technology is clear. The only question is the pace of adoption and we may be behind the curve in this country.

Today, MCI is a leading global communications provider and operates the industry's most expansive global IP backbone. MCI develops the converged communications products and services that are the foundation for some of the most demanding applications in the world. We service major financial institutions, complex engineering and manufacturing centers, and provide complex solutions to more than seventy-five government agencies.

Many of these customers are the early adopters of new computing infrastructures and are led by the best and brightest technologists. These customers have some common requirements:

1. High reliability and security;
2. End-to-end global delivery;
3. Ease of adopting new applications; and
4. Low cost infrastructures.

At the heart of these requirements is the need to mesh local access with wireless capabilities and the core backbone networks. The core technology of the backbone of the future was largely incubated at MCI, in part due to the vision of the legendary Internet pioneer Vint Cerf, a 15-year veteran of MCI. It is known as Internet Protocol – or IP. In its simplest terms, IP allows applications from wireless email to video streaming to be rolled out without understanding or changing the core network elements underneath.

Broadband and Internet Adoption are Driving Technological Change

The momentum is clear: wireless and broadband connecting to IP is the wave of the future. On the broadband side, cable modem service and DSL offerings are being widely deployed. Some companies have started to rollout "next generation" broadband. Public and private entities are starting to deploy wireless "WiFi" networks. Newer and better wireless broadband technologies, such as "WiMax," offer great potential down the road.

Hand-in-hand with broadband is the move to IP. IP technology has led to a convergence of computing and communications, of voice and data, the first manifestation of which is Voice over IP technology ("VoIP"). The introduction of VoIP has lead to the emergence of new and non-traditional providers of voice applications, such as the cable companies and VoIP providers such as Vonage. Peer-to-peer providers, such as Skype, have also started to provide voice applications.

But VoIP is only the tip of the digital iceberg, a precursor to what I call "Everything over IP," or "EoIP." Think of a future where you communicate not just with your voice over a telephone, but with new applications such as video e-mail and the realization of decades-old promise of "picture-phones." In short, IP makes old voice telephony seem as archaic as the telegraph. The rapid convergence of computing and communications has been remarkable.

The Telecommunications Marketplace Has Changed Dramatically

As the technology changes, customer expectations and acceptance of that technology changes. On the market front, we are already seeing a revolution in how we communicate. Wireless service has become a true substitute for traditional landline long distance service. Today, more than half of all long distance calls are made via wireless devices. The traditional distinctions between local and long distance have blurred considerably as providers offer products that give consumers unlimited local and long distance calling.

A growing number of consumers are abandoning traditional wireline companies altogether, in favor of wireless or cable companies or other non-traditional providers. This market trend toward new, non-traditional means of communication becomes more pronounced as each new generation comes on-line. E-mail and "instant messaging" have become significant substitutes for voice traffic. If you have ever watched a teenager do instant messaging, you can assume we are not far from peer-to-peer video as a way of life. Those who grew up on wireless phones and Internet-based access to music, movies and other forms of content will easily move away from traditional phone companies and purchase communications applications from a host of new companies.

Legal and Regulatory Changes are Causing Industry Restructuring

In addition to the technological and marketplace forces I've described, recent legal and regulatory changes have had a significant impact on the industry and, in particular, have hampered the ability of companies like MCI to compete for residential consumers:

- The decision last year by the federal court of appeals in Washington, D.C. in the *Triennial Review Order* case led the Federal Communications Commission (FCC) to issue new rules which dramatically affect the residential market. These rules contribute to the continuing decline in MCI's ability to serve residential customers who demand all-distance service. In particular, the FCC has significantly restricted so-called in<u>tra</u>modal competition by curtailing the ability of competitive carriers to lease unbundled network elements from incumbent carriers to provide local service. These decisions fundamentally alter the underlying economics, forcing MCI and other companies to re-examine whether they can continue to address residential markets.

- Historically, MCI's primary residential sales vehicle has been outbound telemarketing. Federal legislation was enacted in 2003 that established a national Do-Not-Call registry and more than eighty-five million telephone numbers have since been registered. The net result is that MCI's use of the most cost-effective means of contacting potential new customers has been dramatically curtailed. In fact, more than half of all potential customers were removed from the reach of MCI's chief marketing channel.

We are already seeing intermodal competition begin to take place with cable companies investing heavily in their networks. Wireless companies, such as Sprint and Nextel, are moving to provide wireless broadband services. Power utilities are beginning to provide facilities-based broadband in some localities. The use of licensed and unlicensed spectrum to provide new, wireless broadband networks will be an area of great significance in the coming years. Emerging intermodal competition promises a continuing, robustly competitive marketplace.

MCI's Challenge

So where is MCI in this "perfect storm" of IP convergence, market evolution, and regulatory changes?

One of the first things MCI recognized was that, given all of these changes, it would be virtually impossible to sustain its traditional voice business based on circuit-switched technology, especially in the consumer market. As a result, we sought to de-emphasize the importance of our irreversibly declining consumer business and refocus the company on next-generation services for large business and government customers. Although it was the right thing to do, this was a wrenching change, given the fact that MCI played no small part in the creation of residential communications competition in the U.S.

As we transition away from our role in the consumer long distance business, our plan is to build on and leverage the strength of our IP network. In executing that plan, we have moved recently to expand our ability to provide network management and web hosting services, as well as network security applications.

MCI has also entered into an agreement with Verizon to combine our complementary strengths:

- MCI owns a state-of-the-art IP backbone network, but no significant "first mile" facilities or wireless. Verizon has extensive "first mile" facilities and is upgrading those facilities with state-of-the-art broadband technology. Verizon also owns a majority interest in Verizon Wireless.

- MCI has a large enterprise and government customer base that has remained loyal to us because we provide them with world-class products and service quality. Verizon, in contrast, has a much smaller presence in the enterprise markets but is very well-positioned in the consumer market.

The combined company will own a powerful end-to-end network that will permit it to launch a whole suite of innovative next-generation applications that will benefit residential, business and governmental customers.

Some have raised questions about whether the Verizon-MCI merger will significantly impact competition in the residential market. The answer to that question is plainly "No." The facts make incontrovertibly clear that MCI's consumer business is in a continuing and irreversible decline. Our consumer base will inevitably continue to shrink because the technological, market, and regulatory changes I've already described have converged to reshape the telecommunications landscape. Faced with the irreversible decline of our consumer business, MCI is trying only to manage that decline. The more significant competition for consumers will come from alternative technologies that the merger will not affect, like cable and wireless.

Some have also asked whether this combination will significantly reduce competition to provide Internet services. In short, it will not. The combination of the Internet assets of Verizon and MCI does not raise any competitive issues. MCI operates a global Internet transmission network or "backbone" that is comparable in size to those of several other firms that operate such networks, including AT&T, Sprint and Level 3. Verizon, by contrast, manages a much smaller Internet backbone that is located primarily in the northeastern U.S. and does not extend beyond our border. Thus, the combination of the two companies will not materially change the position of the merged company as a provider of Internet services.

Conclusion

Technological, marketplace and regulatory changes are the driving forces behind industry restructuring. Traditional notions of "long distance companies" or "local companies" have become obsolete in this evolving environment. One of the enduring strengths of our antitrust laws is that they recognize that markets are dynamic, not static.

The merger of MCI and Verizon is a reflection of these fundamental changes in the marketplace. The merger will not have an adverse effect on competition in any line of business. Quite the contrary: it will strengthen MCI's ability to compete and to continue to meet our customers' expectations. It is a beginning, an important part of a new and exciting era of competition in an expanding and converging "communications" world.

Thank you very much.

The Testimony of

Mr. David Dorman

Chairman and Chief Executive Officer, AT&T Corp.

Mr. Chairman and Members of the Committee, thank you very much for inviting me to speak with you today regarding the merger of SBC and AT&T, and the enormous benefits that the combination of these companies will bring to consumers and to the nation.

My message to you today is that there is much to look forward to, and nothing to fear, from the joining together of two companies that share an ongoing legacy of innovation, integrity and reliability. Together we intend to set the standard for communications for years to come. Together, we create a national flagship carrier for the 21st century that, from "day one," will be a leader in delivering seamless, secure, and cost-effective new communications solutions to our state and federal government customers, to residential consumers, and to small and large businesses, across the country and around the world.

Together, AT&T and SBC will be able to bring advanced, IP-based broadband services to market more rapidly, more efficiently, and to a wider range of customers than either company could alone, accelerating broadband deployment and heightening competition for voice, data, wireless, and video services. Together, AT&T and SBC can provide the base that will ensure that the United States, in the face of increasing global competition, retains its traditional role of undisputed leader in global communications, and that our national economy obtains all of the benefits that accompany that leadership role. And together AT&T and SBC can ensure that our valued government customers will receive the most advanced, secure, reliable, robust and resilient services and network capabilities.

The merger is fully consistent with the antitrust laws. It will not lessen competition in any line of commerce or create a monopoly—to the contrary, it will promote competition and benefit the public.

WHY AT&T HAS AGREED TO THE MERGER

I speak to you today from a unique perspective. When the 1996 Act was passed, I led Pacific Bell, one of the incumbent Bell companies that today is part of SBC. Today, I lead AT&T, where I have been since December 2000. So I am very familiar with the supremely talented and hard-working people, the best in class networks, and the research and innovation know-how of these two great companies. And as I look at the two companies' assets, I see that they complement one another tremendously – two companies with very different focuses today that, when combined, will create a much better whole. And a key part of understanding why I think this combination is so good – both for consumers and for my shareholders – is the remarkable transformation that AT&T has experienced over the last few years.

Most of you, and your parents and grandparents, have always known AT&T primarily as *your* phone company, a residential consumer-oriented company whose main business for more than a century was providing basic telephone services to the mass market. That is not the AT&T of today. The AT&T of today is a global IP networking provider with a software infrastructure that gives large businesses, state and federal agencies, and other communications providers the flexibility to deliver applications in a secure and reliable way. The reasons for that transformation are, I think, well known to all of you.

AT&T has experienced an environment that has been very difficult for telecommunications companies: fraud and overinvestment, tremendous oversupply and pricing pressures, a wave of technological advances, and a shifting regulatory environment. Our traditional wireline services were being rapidly supplanted by wireless communications and Internet-based applications such as e-mail and instant messaging. Mass market customers were increasingly demanding broad bundles of communications and entertainment services, including services we are not well-positioned to provide. Customers were leaving. Prices were plummeting. Over the last five years, our revenues plunged from $49.6 billion in 1999 to $30.5 billion in 2004. Much of that decline came from our consumer services division.

We knew we had to change, fundamentally and fast. I am proud of the very difficult transformation that we have accomplished. We determined unilaterally that we would no longer actively compete in the traditional mass market, which includes residential customers and small businesses, and that we would turn our attention to delivering powerful networks, applications, and capabilities to business customers worldwide and to our valued government and wholesale customers. It is difficult for many to accept – and it was a painful choice for us to make – but we are no longer a residential consumer and small business company. That is simply not a business that makes sense for AT&T today or going forward. We stopped actively marketing and trying to compete for new mass market customers and quickly, aggressively, painfully and irreversibly implemented our new plan, radically scaling back the operation of our consumer unit— substantially reducing headcount by many thousands, dismantling marketing and sales functions, and retiring support infrastructure and applications. AT&T is far down this path and its mass market phase out is effectively irreversible. I want to assure you, however, that we will, of course, continue to support and provide first class service to our remaining mass market customers as they migrate to other active mass market providers. And I want to point out that by helping larger companies and government to find better ways to meet their needs, AT&T continues to bring great benefits to the marketplace.

The combination with SBC will allow AT&T to continue this process of transforming its business in response to market and service developments. The combination will provide the increased scale and scope that are important to success in transforming our network to implement IP-based technology and in bringing advanced, attractively priced services to market. It will enable us to expand and improve what, in our view, is already the finest global network in the world. It will ensure that AT&T's strengths in the large business customer market can be deployed for the benefit of smaller businesses and residential customers, and that SBC's strengths will enhance our ability to provide new and advanced services to large business customers. The combined company will have the ability and incentive to increase innovation and development of advanced services for the benefit of all customers, in the U.S. and globally.

THE MERGER WILL PROVIDE IMPORTANT PUBLIC BENEFITS

Consumers of all types will benefit from this merger because of what the two companies share and, more importantly, because they have complementary and different strengths.

The two companies share a common past and an ongoing legacy of innovation, integrity, reliability, and customer service.

The two companies also bring together different strengths and product sets, ensuring that the merger will produce a combined company that is more than the sum of its parts. SBC is a provider of voice, data, broadband, and related services to consumers and businesses – especially small businesses – primarily on a local and regional basis in its 13-state region.

AT&T has a different focus. We provide a broad array of voice, data, and IP-based services to customers on our global and national IP-based networks. We provide services to the largest businesses, government agencies, and wholesale customers. AT&T has a presence in more than 50 countries, allowing it to compete for the business of the largest global enterprises. AT&T

Labs has ensured that the company has remained a leader in the invention and development of innovative services and advanced network capabilities.

The combined SBC and AT&T will be a stronger and more innovative U.S.-based global competitor than either company could be alone. The merger will produce a flagship U.S. carrier that will offer the most efficient, highest quality capabilities to government, business, and residential customers nationwide and globally. The combined company will continue to provide U.S. government customers with the most advanced and secure services and network capabilities. 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, as well as the marketing expertise and infrastructure to reach those customers.

Combining the two companies' core strengths will result in more investment in, and faster deployment of, innovative new technologies and network capabilities that will benefit all customers. The combination of AT&T and SBC will enhance competition, resulting in improved services and lower prices for consumers, and will not impede competition in any market.

Let me elaborate on each of these points:

Global Leadership. The transaction will establish a world leader in advanced communications services, which will provide very significant benefits for all American consumers. The nation's economic growth and ever-improving standard of living have resulted, in substantial part, from the United States' position as an undisputed world leader in communications. Recently, that leadership has been questioned, fairly or not, as European and Asian-Pacific carriers and technology companies have grown rapidly and other markets – different from our own for many and varied reasons – have surpassed the U.S. in broadband penetration. Many of these companies now are competing in the U. S. market.

By combining firms that are recognized leaders in both enterprise and mass market services and in the design and engineering of local, broadband, wireless, and global networks, the merger will create an American carrier that will undoubtedly set the global standard for communications service leadership. The companies' complementary strengths ensure that the combined company can rapidly complete the transformation of legacy networks to IP. These same synergies will drive the achievement of end-to-end service quality standards that previously have been unobtainable and will ensure the United States' preeminence in communications.

Service to Government. Federal government departments and agencies, including those with national security responsibilities and requirements, will directly benefit from the service and network improvements that this merger will enable. Today, AT&T provides advanced services to a broad range of government agencies, including those involved in national defense, intelligence, and homeland security. AT&T's customers include the White House, the State Department, the Department of Homeland Security, the Department of Defense, the Department of Justice, and most branches of the armed forces.

AT&T's support of the intelligence and defense communities includes the performance of various classified contracts.

The transaction will enable Government customers to receive the most advanced, improved services and network capabilities. SBC's and AT&T's separate networks will be transformed into a larger and more advanced IP-based network, which will be more reliable, robust, and resilient.

Increased Innovation. This merger will spur innovation and share the fruits with those who would not otherwise benefit. A crucial benefit of this combination for all consumers is greater research, development and innovation – especially for advanced and IP-based services and network capabilities. For customers, this should mean lower costs for existing services, the more rapid development of new services, and the development of services that otherwise would not exist.

The merger will promote and widely distribute the benefits of innovation by enabling the combined entity to take greater advantage of the research and development capabilities of one of AT&T's "crown jewels" – AT&T Labs, which is a direct successor to the Bell Telephone Laboratories. Innovations undertaken by Bell Labs and its successors have launched or proved instrumental to the development of basic innovations that have shaped our daily lives and launched entire industries.

Let me tell you more specifically about the innovation this transaction will foster.

Innovative Mass Market Services. The transaction will increase innovation because the combined company will seek to develop and deploy, for smaller business and residential customers on whom AT&T would not otherwise focus, the storehouse of existing and ongoing innovations produced by AT&T Labs for large enterprise customers. The potential benefits of research and development, however, are not limited to those customers. Breakthroughs that AT&T achieves in research and development aimed at producing new enterprise services, or providing those services more efficiently, often will have relevance to other services that could potentially be offered over the combined company's network facilities, such as mass market services. Let me identify some areas where exciting benefits can be achieved:

- For example, AT&T is a global leader in the development of text-to-speech engines, synthesized voice capabilities, automatic speech recognition, and natural language speech understanding systems. These technologies have the potential to allow real-time translation services and exceptionally efficient customer care and relationship management capabilities. Accelerated deployment of these capabilities into residential and small business offerings holds the potential for significant public benefits, particularly for visually, hearing, and speech-impaired customers.
- Similarly, AT&T Labs is a leader in the development of network security services for business customers. It is developing capabilities to detect unauthorized use of communications services and customer

information. As demand for anti-fraud and security services among mass market and small business customers continues to grow, very significant public interest benefits may be realized by additional innovation the combined company will undertake to meet that demand.

- AT&T Labs continues to develop advanced e-commerce support and enhancement capabilities. Translating these ongoing innovations from large business-focused services to services designed to meet the needs of smaller businesses and residential customers is another source of significant public interest benefits.
- And AT&T Labs is developing an IP environment that can support a broad range of communications services, including video services. AT&T has also developed a number of innovations to make the delivery and use of video services far more effective than is achievable today, with clear benefits for smaller business and residential customers.

Innovative Network Capabilities. In addition, combining the two companies creates scale and brings together complementary strengths that will lower the costs and increase the benefits of pursuing research and development initiatives – and thus increase the pace and breadth of innovation. AT&T's unmatched research and development capabilities will be combined with SBC's financial strength, capacity to capitalize on transformative opportunities, and its local network expertise.

The merger will enable a more rapid transformation of the companies' networks, which meet current needs efficiently, to a unified, IP-based service platform, with numerous advanced capabilities that will benefit customers. Developing these advanced network capabilities lies at the heart of AT&T's and AT&T Labs' core missions and expertise. Through the merger, SBC will bring to the combined entity the scale, greater financial strength, and network capabilities that ensure that the combined entity will have an increased incentive and ability to develop advanced network capabilities and related services and can do so much faster than AT&T would on its own. The resulting advanced networks can provide consumers of all types with the ability to choose, provision, change, and maintain their services with an almost unimaginably greater degree of speed, efficiency, and efficacy. Greater innovation and wider deployment of its benefits will help keep America in the forefront of the global communications industry and benefit our economy.

THE MERGER WILL ENHANCE RATHER THAN IMPEDE COMPETITION

I believe that this transaction will only enhance competition in communications markets.

The important network and service benefits I've described above reflect improvements in competition. The improved ability of the combined company to bring innovative and advanced services to market, for a broader range of customers, will expand customer choice and offer improved alternatives that competitors of all types will be forced to match. This includes cable, VoIP, and wireless competitors in SBC's traditional local service region.

I also believe that the transaction will inevitably lead to greater competition between the Bell companies themselves. The Bells today already compete against one another for wireless services. With this merger, the combined company will be competing for large business customers across the nation and very much in the local service territories of the other Bell companies. They will have to improve their services, both in their incumbent regions and beyond, if they are to remain competitive. And the combined company will continue to develop AT&T's VoIP service, which is designed for residential customers throughout the nation in direct competition with the Bells' local service offerings.

For the reasons I've outlined above, the merger also will produce a more capable global competitor with a broader geographic scope of service and a broader line of more advanced services and network capabilities. This will benefit U.S. companies as they compete overseas and will benefit all communications customers as other global service providers must improve their offerings to compete effectively with the combined company.

Nor will the transaction harm competition in any market, principally because the two companies' businesses are largely complementary. In the mass market, SBC is a leading provider of service in its 13-state region, but AT&T is no longer an active mass market competitor in those states. AT&T's earlier irreversible decision to stop actively marketing to such customers for either local or long distance wireline telephone service means that it is no longer a substantial competitor in mass market services. Removing AT&T as a separate service provider thus could not harm competition in the provision of those services to residential and small business customers. Moreover, competition increasingly is coming to these customers from cable, VoIP, and wireless providers, including powerful new players. AOL just announced, for example, that it will launch an Internet phone service imminently, and Microsoft is embedding voice and communications into its software platform, which will create additional competition for business and residential customers.

The merger will also not impair competition in the provision of services to business customers. The market for services to these customers is exceptionally competitive and will not be impaired by this transaction. Suppliers include interexchange carriers, systems integrators, equipment vendors and value-added service providers, other network providers, foreign carriers, CLECs, cable operators, and other ILECs. With voice service increasingly only one of many business needs on increasingly integrated platforms, diverse companies originally focused on other services such as IBM and EDS are providing vigorous competition for a broad range of services to mid-size and large businesses. Moreover, because large business customers are highly sophisticated, have widely varied needs, and rely on complicated and detailed bidding procedures, providers cannot successfully engage in anticompetitive conduct. Given the number and diversity of competitors offering services and products to businesses and the sophistication of customers and the purchasing practices they employ, the marketplace will undoubtedly continue to be vigorously competitive after the merger is concluded. In these circumstances, the transaction cannot reduce competition for the business of these large customers.

Nor is there any serious argument that the merger will diminish competition in wireless, international or Internet backbone services. SBC has a majority ownership interest in Cingular Wireless, but AT&T long ago divested itself of its interest in AT&T Wireless, its cellular service operation. Combining these companies results in the loss of no significant competitor.

So, too, with international services. AT&T has an extensive global presence, especially for large business customers, but SBC provides only a very limited share of international communications. Provision of these services is, in any event, highly competitive and will remain unaffected by the merger.

And while AT&T is one of the largest providers of Internet backbone services, SBC's network is much smaller. AT&T – but not SBC – is a Tier 1 provider of Internet backbone services. Following the merger, at least five other Tier 1 providers will remain to provide robust competition in that market.

* * * *

In conclusion, I would like to thank you again for the invitation to speak with you about the very significant consumer and public benefits that this merger will produce. This transaction will create an American global communications company for the 21st century – a company capable of delivering advanced services to customers of all types throughout America and around the world. And it will do so by increasing, rather than by posing a threat to, competition.

I would be pleased to answer any questions that you may have.

News from

HERB KOHL

United States Senator
Democrat of Wisconsin

330 Hart Senate Office Building • Washington, D.C. 20510 • (202) 224–5653

FOR IMMEDIATE RELEASE: **March 15, 2005**
Contact: Lynn Becker or Zach Goldberg **Phone: (202) 224-5653**

Statement of U.S. Senator Herb Kohl - Judiciary Committee

Thank you, Mr. Chairman. We are witnessing the most fundamental reshaping of the telecom industry in decades. In the space of a generation, we've gone from the break-up of Ma Bell to what some fear may be its recreation, at least on a regional level.

The break-up of AT&T two decades ago unleashed an explosion of competition and innovation. The competitive forces freed by the ending of the phone monopoly led directly to the introduction of previously unheard-of technologies ranging from the fax machine, the cellular phone, e-mail, to the Internet itself. Consumers benefited from a blossoming of new choices and services. Prices for phone services declined so dramatically that what was once an unusual and expensive event - placing a long distance telephone call - became routine and almost cost free. And the cost to American business of telecom services dropped considerably, helping spur greater efficiencies and growth throughout the economy.

We are now entering a brave new world of telecom competition. The acquisition of AT&T by one of its Baby Bell progeny, SBC, and the likely acquisition of MCI by Verizon, will create two telecom giants, each dominating many services throughout their regions. Should these mergers be consummated, SBC and Verizon will have a market share of about 90 percent of local residential consumers in their regions, 70 percent in long distance, and about 40 to 50 percent in wireless.

These figures give us pause, but we live at an exciting time in the telecom world where the pace of consolidation is matched by the speed of innovation. AT&T and MCI are both declining companies, and have already withdrawn from marketing most services to residential consumers. As a result, with the important exception of the business market, there are few remaining areas where SBC competes with AT&T or Verizon competes with MCI. In addition, new technologies are emerging - services such as Internet-based telephone service and wireless connections to the Internet - which may challenge SBC and Verizon if given a chance.

It is our first responsibility to ensure that these emerging new technologies have a real chance to succeed. The possible benefits of new competition will drive growth throughout the economy for decades to come. We must insist that the promise of tomorrow's technology is not stifled in its infancy by today's consolidation. And we must seek to avoid the creation of a world where consumers are left with only two choices for a bundle of telecom services - the "Baby Bell" phone company and the cable company.

--More--

Telecom Hearing, Page 2

So we have two concerns with these mergers. First, will this consolidation decrease the choices and increase the costs to consumers and to business customers, both large and small? Second, how can we ensure that new technologies and new services can get access to the SBC and Verizon networks? A good place to start would be to require that the Baby Bells offer consumers the choice of buying Internet access without also requiring them to buy phone service. We expect to recommend additional specific pro-competitive merger conditions to the Justice Department and FCC in the coming weeks.

Securing merger conditions such as these will help ensure that the tremendous gains in telecom competition over the last twenty years are not lost in the midst of this industry consolidation.

One more comment - I believe it is essential that our Committee hear from competitors and consumers affected by these mergers. We are disappointed that we will not hear any voices besides those of the merging companies today. Instead, we will need to return to this topic in a few weeks so that all voices are represented.

Thank you again, Mr. Chairman, and we look forward to hearing the testimony today.

# # #

Statement of Senator Patrick Leahy
Ranking Member, Senate Judiciary Committee
"SBC/ATT and Verizon/MCI Mergers –
Remaking the Telecommunications Industry"
March 15, 2005

I am pleased the Committee is convening a hearing today for the telecommunications industry is in the midst of a tumultuous transformation. Our society is catapulting from the days of the party line, operator-mediated calls and expensive long-distance bills to an era of portability of service, intramodal competition among providers, and multi-use devices. This transformation raises many important and difficult questions about how we can best ensure that the benefits of the rapidly changing technologies, the rapid globalization of communication, and the aftermath of the Telecommunications Act of 1996 are all harnessed to bring the highest quality of communications services to all Americans, with the broadest variety of choices at the lowest possible prices. This is no small task, and hearings in the relevant Committees are certainly a useful first step in what will doubtless be a long and involved process. As we all go through that process, I hope we will bear in mind that the much-vaunted competition goals of the 1996 Act were not fully realized, and that we must be particularly careful to avoid the pitfalls of that legislation again.

A great deal of our usefulness rests on our ability to respond to – and engage in – important events that may bear upon the legislative process. Six weeks have passed since the announcement of the SBC-ATT merger, and more than a month has passed since Verizon announced plans to merge with MCI. These are the latest in a string of three multi-billion dollar deals. The Committee and Antitrust Subcommittee will want to follow through after today's hearing to hear other perspectives and create a balanced record. Today, I will ask consent to at least insert in the record testimony from Consumers Union and the Consumers Federation of America.

When I cast one of only five votes against the Telecommunications Act of 1996, I did so in large part due to my belief that the competition anticipated by that bill was an empty promise. Time has borne out the truth of my prediction, and inadequate competition has not been isolated to telephone service. Cable rates have continued to skyrocket well beyond the pace of inflation, and, according to the International Telecommunications Union, the United States is thirteenth in the world in broadband deployment. Many consumers are fed up, and rightly so, they deserve better.

In light of the failure of the 1996 Act to spur effective competition, we should closely scrutinize deals that would put more and more of our telecommunications infrastructure

under the control of fewer companies. At the same time, we must also acknowledge and consider the rapid pace of technological change that has taken place within this industry in the past several years. Telephones, and making telephone calls, used to be pretty straightforward. Some of us still remember phones with dials rather than buttons. And some of us even recall when operators connected callers and when the industry was dominated by a single company: AT&T. Times certainly have changed.
The growing popularity and shrinking size of cellular phones mean that a growing number of consumers do not use wireline telephone service at all. At the same time, Voice over IP can bring us telephone calls in large part by using the infrastructure of the Internet. Cable companies look forward to developing a substantial new revenue stream in providing telecommunications services. In the not-too-distant future, we may find that Broadband over Power Lines allows Internet calling wherever there is electricity. And WiFi access on BPL could make Internet calls a viable possibility for wireless customers. These are just a few of the myriad developments – and many new acronyms – that have entered this arena since the break up of the old Bell System.

While anti-trust enforcement always requires some attempt to predict the future, we in Congress must attempt to draft legislation that not only accommodates technological innovation, but protects and promotes it. This will be particularly important as Congress revisits the Telecommunications Act of 1996.

# # # #

Office of the Ohio Consumers' Counsel *Your Residential Utility Consumer Advocate*

Janine L. Migden-Ostrander
Consumers' Counsel

March 15, 2005

United States Senator Mike DeWine
Chairman-Sub Committee
Antitrust, Business Rights & Competition
Senate Committee on the Judiciary
161 Dirksen Building
Washington, D.C. 20510

Re: Proposed Mergers of SBC with AT&T
and Verizon with MCI

Dear Senator DeWine,

On January 31, 2005 SBC and AT&T announced their intent to merge. Exactly two weeks later, on February 14, 2005, Verizon and MCI announced their proposed merger.[1] These two mergers would combine the largest providers of local exchange service in their territories with the largest non-Regional Bell operating company ("RBOC") providers of long distance service in their territories.[2] AT&T and MCI are also the largest competitors for local exchange service in SBC and Verizon territories.

The Office of the Ohio Consumers' Counsel ("OCC") is in the beginning phase of reviewing these mergers, which will result in an unprecedented consolidation of the telecommunications industry. However, we have identified several public policy issues that concern us. Other issues will undoubtedly emerge as our analysis progresses.

OCC believes that SBC and AT&T ("SBC/ATT") and Verizon and MCI ("Verizon/MCI") should be required to present evidence that there will be no negative impacts on consumers and that the mergers will provide long-term benefits for residential consumers before federal or state regulators approve the proposed mergers. Without evidence that consumers will not be harmed and that consumers will receive benefits from these two mergers, OCC believes that the mergers cannot be in the public interest.

[1] Qwest has until March 17, 2005 to make a counter-offer to acquire MCI. As of the writing of this letter, Qwest has not made such an offer.

[2] A recent Wall Street Journal article provides the long distance market share in the United States in 2003. See "Telecom Mergers Limit Choices of Customers" (February 4, 2005). This article shows that these mergers involve the four largest long distance providers: AT&T has the largest market share at 31.5%, Verizon is second with a 11.5% market share, SBC follows with a 9.6% market share and MCI comes in fourth with a 9.0% market share.

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We believe that the proposed mergers may be anti-competitive. It is only logical to conclude that if a company merges with its largest competitor that competition will be harmed since customers will have fewer companies to choose from. When the current state of the telecommunications market for local exchange service is viewed from a historical perspective, it is obvious that the litigation and roadblocks to competition that SBC and Verizon have pursued since the passage of the Telecommunications Act of 1996 ("the Act") have produced the desired objective: their major competitors are so beaten that it would be easier for them not to continue as separate entities.

Couple the current dismal state of local competition with the RBOCs push to be deregulated in almost every state and consumers -- especially residential consumers -- are justifiably alarmed. If the efforts to both merge and deregulate are successful, consumers will be faced with having to deal with a deregulated monopoly mega-conglomerate. This is not the vibrant competitive marketplace for local exchange service that was promised in the Act.

One of our primary concerns involves the ultimate price impacts of these mergers on residential consumers. As stated above, these mergers will eliminate SBC's and Verizon's two largest competitors for both local service and long distance service.[3]

We suggest that companies will continue to compete for high-end users (i.e., some telephone companies claim that they obtain 80% of their revenues from 20% of their customers). We are concerned about what will happen to the average and low-use customer as a result of these mergers. For example, residential customers may face rate increases and elimination of competitive options for local exchange service.

We are concerned with the availability of broadband service in rural areas. In Ohio, there are some areas that do not have access to broadband service. One result of the proposed mergers should be that broadband is deployed to currently unserved areas. Otherwise, these customers will have no alternatives to the higher monopoly rates of the utilities.

Regarding intermodal competition,[4] OCC does not believe that is a reality today. Cellular and VoIP services are not equal substitutes to the traditional service that residential consumers have come to expect (indeed, to demand). For instance, consumer protections are missing from alternative services. The most critical is that E9-1-1 service is not ubiquitously available with alternative services. Additionally, power outages will most likely mean that telephone service provided via

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[3] This makes these two mergers both quantitatively and qualitatively different from the last round of consolidation in the telecommunications industry, specifically the SBC/Ameritech merger and the Bell Atlantic/GTE merger that created Verizon. None of those companies competed against each other; indeed, the mergers were approved on the condition that the companies compete outside their traditional service territories. To date, that out-of-territory competition has not occurred.

[4] Supporters of intermodal competition assert that there is competition among the various modes of communicating such that, for example, cellular service and Voice over Internet Protocol ("VoIP") are equal substitutes for traditional local exchange service.

cellular[5] and VoIP will not be available. Disruptions in the delivery of cable service may interrupt VoIP-based telephone service.

Another point regarding intermodal competition: If these mergers are consummated, the companies will be merely "competing" with themselves for cellular and VoIP service. SBC is the major partner in Cingular, and Verizon, of course, will continue to operate Verizon Wireless.[6] Instead of launching its own VoIP service, SBC will undoubtedly use AT&T's current VoIP service (marketed as "CallVantage"). Just as in the local exchange service and long distance markets, SBC and Verizon propose to "buy-out" the competition instead of providing genuine competition.

Another issue that should be evaluated involves control of the Internet backbone, including the incentive of the merged companies to deny access to their facilities. Should this occur, opportunities for competition will be further eroded. The enclosed Rogers Report illustrates the impact of the proposed mergers on the control of the fiber Internet backbone facilities in the United States. Others have expressed concern over this issue.[7]

Experience with previous mergers in Ohio (specifically the SBC buy-out of Ameritech in 1999) indicates that service quality may decline soon after the combination is completed. For instance, on April 8, 1999, the Public Utilities Commission of Ohio ("PUCO") approved the SBC/Ameritech Ohio merger. Just four months later, the PUCO opened a proceeding to investigate whether Ameritech Ohio had violated several provisions of Ohio's minimum service quality standards.[8] In 2000 and 2001, the 5-state legacy-Ameritech territory experienced an unprecedented service quality meltdown.[9]

In the end, these mergers should be approved only if conditions or commitments are attached that would provide genuine benefits to consumers. Such conditions and commitments must include strong and effective enforcement provisions in order to ensure that not only the letter but the spirit of

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[5] Most cellular towers need electricity to function and do not have a back-up power source in the event of an electric outage.

[6] According to an FCC table showing the top 25 mobile telephone operators by subscriber (as of year-end 2003), Verizon has the most subscribers (approximately 37 million), Cingular Wireless is second with approximately 24 million customers and AT&T Wireless is third with approximately 22 million subscribers. See Table 4 of the 9th Annual CMRS Competition Report (WT 04-111) dated September 28, 2004 which can be found at http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-04-216A1.pdf. Not reflected in these numbers is the purchase of AT&T Wireless by Cingular in 2004.

[7] Also see a February 16, 2005 article in the Washington Post entitled "Mergers Raise Concerns Over Internet Access."

[8] In the Matter of the Commission-Ordered Investigation of Ameritech Ohio Relative to Its Compliance with Certain Provisions of the Minimum Telephone Service Standards Set Forth in Chapter 4901:1-5, Ohio Administrative Code. Case No. 99-938-TP-COI.

[9] See for example, "[SBC] Chief Visits Chicago to Apologize for Shoddy Service" COMTEX Newswire, October 17, 2000 and AP Financial reporting that regulators from five states grilled executives (including SBC CEO Edward Whitacre) from Ameritech and parent SBC about recurring phone service problems throughout the Midwest (October 16, 2000).

the conditions are met. The stockholders of these corporations must not be the only ones to benefit from this round of industry consolidation.

Thank you for the opportunity to provide OCC's preliminary perspective on these mergers. Please feel free to contact me at 614-466-7239 or OCC's Legislative Director Dennis Stapleton at 614-466-9539.

Sincerely,

Janine L. Migden-Ostrander

Janine L. Migden-Ostrander
Ohio Consumers' Counsel

Ivan Seidenberg
Chairman and Chief Executive Officer -- Verizon
Senate Judiciary Committee
March 15, 2005

Written Testimony

Mr. Chairman and members of the Committee, thank you for the opportunity to be part of this discussion on the state of competition in the restructuring communications industry.

As you are aware, Verizon has announced its intention to acquire MCI to form a strong, stable and secure national communications provider. We recently filed our application for approval with the FCC, we have filed in several of the two dozen or so states where we are required to gain state approvals, and we are actively working with the Department of Justice to provide them with the information they need to complete their review.

In each of these filings, we make the point that I make to you today: that this recent wave of mergers and acquisitions is a response to the dramatically different competitive landscape we face in communications as the industry restructures around new technologies and new markets.

It should be evident to anyone with a cell phone or an e-mail account that the old distinction between local and long distance is obsolete, as is the need for separate companies to provide them. Competing technologies – cable, wireless, satellite, IP, and wireline – now offer consumers a wide range of choices for voice, data and, increasingly, video. And the pace of technological change is accelerating, which makes these markets more dynamic and competitive with each passing day.

What may *not* be as apparent is that the same forces are transforming the large-business marketplace. Traditional voice services make up a smaller and smaller piece of the pie. Instead, these large, technologically sophisticated customers are demanding a much wider range of services, platforms and applications from a growing universe of suppliers – not just "telephone" companies, but systems integrators, software providers, equipment makers and wireless companies. These companies include some of the biggest names in industry, such as Cisco, IBM, EDS and British Telecom.

A case in point is Microsoft, which earlier this month announced a major foray into the large business marketplace with a software platform that embeds voice and communications as a free application in its Microsoft Office product line, much like Instant Messaging is today. Looking ahead, this approach makes companies like Microsoft, Yahoo and other Internet and software companies legitimate competitors in the enterprise market.

Since our formation five years ago, Verizon's overriding imperative has been to build a company capable of competing in this technology- and market-driven environment. For us, this has meant gaining scale in the growth segments of the marketplace, such as wireless and broadband; reinventing our networks around new digital and fiber technologies; and equipping ourselves to compete as other technology companies do, through investment and innovation.

I stress "investment" because it has been Verizon's willingness to put substantial risk capital into our networks that has differentiated our company and provided more value and choice for customers. We have indicated our intention to invest substantially in MCI's infrastructure once this transaction closes. It is this ability and willingness to invest in our future that moves the industry forward and strengthens this country's communications assets.

We have followed this path in the wireless business, where we put together a national network and invested in spectrum, digital capabilities and, now, broadband technologies to expand the market and grow through innovation.

We are following this path in the consumer wireline business, where we are transforming our *telephone* network into a *broadband* network by deploying DSL and fiber-to-the-premises, over which we are providing voice, data and – as we move forward – video services.

Verizon's acquisition of MCI represents the next logical step in this process, as we transform ourselves around the evolving needs of the large-business, or "enterprise" market.

We have always viewed the large-business marketplace as one of the keys to our long-term growth strategy. As in all network-centric businesses, scale is important in this segment, and while we have a solid presence among local and regional customers, we have no significant market share among national and global customers. In fact, a market analysis of the enterprise long-distance voice and data market performed by Sanford Bernstein puts the market share of Verizon, SBC and Bell South *combined* at just 3 percent. A Lehman Brothers analysis, using an expanded definition that includes competitors such as Cisco, IBM, EDS and others, lumps Verizon's share in a slice of a pie chart labeled "the highly fragmented rest."

So we knew we needed to add substantially to our product set and network reach to be able to compete for these customers, and we have been investing in these capabilities steadily over the years.

The MCI acquisition accelerates that effort substantially. I should point out that MCI's and Verizon's assets are complementary, not duplicative. One of MCI's core strengths is its global Internet backbone network. Verizon today has no comparable asset. Therefore, by bringing our companies together, we will create a strong *new* competitor in the enterprise space – one with the advanced products, network reach and capital capacity required to invest in these assets and compete in this technology-intensive and highly competitive market.

I understand that some questioned how this latest phase of restructuring in the communications industry will affect consumers. Let me be very clear. Verizon's acquisition of MCI does not alter the dynamics that are reshaping the consumer market. Nor will it have any impact on the current Universal Service program or its funding.

Long distance and local as stand-alone businesses are on their way to obsolescence, with or without this transaction. Competition from wireless, cable telephony, e-mail, Instant Messaging and VOIP will continue to drive pricing, with or without this transaction. And in any meaningful sense of the word, the consumer marketplace will continue to become *less* concentrated over time – with or without this transaction – as new platforms and providers vie for the broadband household.

My message to this committee, then, is that to view this deal in terms of the communications business of the *past* 20 years is to miss the benefits that will accrue in the *next* 20 years.

Consumers will benefit because MCI's IP network and products, combined with our deployment of fiber directly to homes and business, will be the most advanced broadband platform in the country, capable of delivering next-generation multimedia services in markets across the U.S.

Enterprise customers will benefit because we will create a strong, stable and secure strategic partner for national and global businesses as they prepare for the broadband future.

Federal and state government customers will benefit because they will have a choice of financially stable players that can stay current in technology and invest in the networks that are critical to their public mission.

National security will benefit because we will continue to invest in and strengthen the national and international communications infrastructure that is a critical component of government communications systems, including those used by the Departments of Defense and Homeland Security.

And the U.S. economy will benefit because we are creating a strong, U.S.-based company capable of investing in the new technologies so critical to job creation and leadership in the global marketplace.

This transaction is about the future. Verizon and MCI will be a national, full-service company with the financial strength and technology resources to deliver the broadband, multimedia world of tomorrow to customers and create economic growth for America today.

Thank you. I look forward to your questions.

STATEMENT OF
EDWARD E. WHITACRE, Jr.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER
SBC COMMUNICATIONS INC.

BEFORE THE
JUDICIARY COMMITTEE
UNITED STATES SENATE
ON

SBC/AT&T AND VERIZON/MCI MERGERS:
REMAKING THE TELECOMMUNICATIONS INDUSTRY

March 15, 2005

Thank you, Chairman Specter and good afternoon to you and the Committee.

The title of this hearing, "Remaking the Telecommunications Industry" is appropriate...as demonstrated by the SBC-AT&T merger.

Our merger is a positive development for customers, for competition and for America's leadership in the global communications marketplace.

The combined SBC-AT&T will be a flagship American communications company for the 21^{st} century.

We will bring together outstanding state-of-the-art networks... innovative, advanced products and services... unmatched talent and expertise...and a rich tradition of customer service and reliability.

And we will ensure that the company which started it all more than one hundred years ago...will be part of it all for many years to come.

That's why more than 250 consumer, business and civic groups, as well as unions and elected officials of both parties have already announced their support for the merger.

Our merger comes as the U.S. telecommunications industry is trying to get up off the mat. For the first time in a long while, we can see light at the end of the tunnel.

But the journey through that tunnel has been pretty hard.

Since 2000, telecommunications service providers and equipment manufacturers have lost more than 700,000 jobs. Annual capital investment has declined by more than $70 billion. Companies have lost more than $2 *trillion* in market capitalization.

Until relatively recently, SBC was losing 60,000 access lines each week.

And in all honesty, adverse regulation has contributed to this downward spiral.

So, Wall Street is investing less and less in telecom. Telecom is investing less and less in its products and services. We can see the consequences: today, for example, the U.S. is 11^{th} in the world in broadband deployment.

In short, this industry is in turmoil...and that's why we decided to do the SBC-AT&T merger.

The reasons for combining these two companies are pretty clear...and so are the benefits to customers.

First, while SBC has a strong presence in many local markets, we do not have a national or global network of our own. We lease one.

AT&T has those assets, and they are very good.

Second, the "next big thing" in communications technology is voice over Internet Protocol...or VoIP.

IP is changing how people communicate. And it has already opened the door to a host of new competitors. Dozens upon dozens of cable companies and others are using VoIP to provide telephone service, and they are winning customers.

SBC does not have a consumer VoIP service. And while AT&T has stopped actively marketing consumer services, it does have a VoIP offering. The combined company will have the financial resources and incentives to use it to compete in our region, outside our region and for business customers around the world.

The third reason for our merger is the opportunity it creates for competition in the large business customer segment.

While SBC has made some progress in this market...it is slow going. AT&T will give us the ability to compete more effectively in this highly competitive segment of the market nationally and globally.

For these reasons, the SBC-AT&T merger will enhance competition and should be viewed positively from an antitrust perspective.

For the most part, SBC and AT&T do not compete head-to-head. This is certainly true in the mass market, where competition is already vigorous.

Where we do go up against one another, in the mid- to large-business space, customers will still have numerous competitors from which to choose...including competitors such as systems integrators, equipment manufacturers, other phone companies including Verizon and Qwest and more.

When you assess the market without bias, it is obvious that no two companies can control this highly competitive and very crowded space, even after the mergers as currently contemplated.

The same holds for rural carriers and their access to the Internet. The fact is that rural telephone company access to SBC's IP backbone will not be affected by the merger.

Our ability and willingness to connect with rural companies will not change, and we anticipate no change in pricing to these customers.

For these reasons and more, the SBC-AT&T merger is in the public interest.

This merger is a natural and healthy evolution of a dynamic, competitive industry that is light years removed from when the last federal telecom law was enacted in 1996.

Today there are more wireless subscribers in the U.S. than there are traditional phone lines.

Data traffic now exceeds voice traffic by a margin of eleven-to-one.

Cable companies will offer phone service to two-thirds of American homes this year. And other competitors using IP-based services continue to grow.

On March 9th, the *Wall Street Journal* reported that America Online will soon offer VoIP service to its 22 million U.S. subscribers...with plans to extend it even further.

In that same day's paper, Cox Communications said in a letter to the editor that Cox "had more telephone customers than any other cable company."

The letter went on to say that in markets some markets, including Orange County, California...40 percent of consumers subscribe to Cox Digital Telephone, and 82 percent of their phone customers use Cox for their long-distance service as well.

Very little of this was envisioned when the Act was passed...which is why we need the laws to catch up. Policymakers and those who regulate us have an obligation to keep pace.

We need rules that treat new technologies with the lightest touch possible and which allow the competitive marketplace to discipline retail prices.

Such reform would spur much-needed innovation, investment and growth...goals that I hope and believe this Committee shares.

Thank you.

Merger of

SBC Communications Inc.

and

AT&T Corp.

Description of the Transaction, Public Interest Showing, and Related Demonstrations

[Excerpt]

Filed with the Federal Communications Commission
February 21, 2005

In connection with the proposed transaction, SBC intends to file a registration statement, including a proxy statement of AT&T Corp., and other materials with the Securities and Exchange Commission (the "SEC"). Investors are urged to read the registration statement and other materials when they are available because they contain important information. Investors will be able to obtain free copies of the registration statement and proxy statement, when they become available, as well as other filings containing information about SBC and AT&T Corp., without charge, at the SEC's Internet site (www.sec.gov). These documents may also be obtained for free from SBC's Investor Relations web site (www.sbc.com/investor_relations) or by directing a request to SBC Communications Inc., Stockholder Services, 175 E. Houston, San Antonio, Texas 78258. Free copies of AT&T Corp.'s filings may be accessed and downloaded for free at the AT&T Relations Web Site (www.att.com/ir/sec) or by directing a request to AT&T Corp., Investor Relations, One AT&T Way, Bedminster, New Jersey 07921.

SBC, AT&T Corp. and their respective directors and executive officers and other members of management and employees may be deemed to be participants in the solicitation of proxies from AT&T shareholders in respect of the proposed transaction. Information regarding SBC's directors and executive officers is available in SBC's proxy statement for its 2004 annual meeting of stockholders, dated March 11, 2004, and information regarding AT&T Corp.'s directors and executive officers is available in AT&T Corp.'s proxy statement for its 2004 annual meeting of shareholders, dated March 25, 2004. Additional information regarding the interests of such potential participants will be included in the registration and proxy statement and the other relevant documents filed with the SEC when they become available.

Certain matters discussed in this statement, including the appendices attached, are forward-looking statements that involve risks and uncertainties. Forward-looking statements include, without limitation, the information concerning possible or assumed future revenues and results of operations of SBC and AT&T, projected benefits of the proposed SBC/AT&T merger and possible or assumed developments in the telecommunications industry. Readers are cautioned that the following important factors, in addition to those discussed in this statement and elsewhere in the proxy statement/prospectus to be filed by SBC with the Securities and Exchange Commission, and in the documents incorporated by reference in such proxy statement/prospectus, could affect the future results of SBC and AT&T or the prospects for the merger: (1) the ability to obtain governmental approvals of the merger on the proposed terms and schedule; (2) the failure of AT&T shareholders to approve the merger; (3) the risks that the businesses of SBC and AT&T will not be integrated successfully; (4) the risks that the cost savings and any other synergies from the merger may not be fully realized or may take longer to realize than expected; (5) disruption from the merger making it more difficult to maintain relationships with customers, employees or suppliers; (6) competition and its effect on pricing, costs, spending, third-party relationships and revenues; (7) the risk that Cingular Wireless LLC could fail to achieve, in the amount and within the timeframe expected, the synergies and other benefits expected from its acquisition of AT&T Wireless; (8) final outcomes of various state and federal regulatory proceedings and changes in existing state, federal or foreign laws and regulations and/or enactment of additional regulatory laws and regulations; (9) risks inherent in international operations, including exposure to fluctuations in foreign currency exchange rates and political risk; (10) the impact of new technologies; (11) changes in general economic and market conditions; and (12) changes in the regulatory environment in which SBC and AT&T operate.

The cites to webpages in this document are for information only and are not intended to be active links or to incorporate herein any information on the websites, except the specific information for which the webpages have been cited.

EXECUTIVE SUMMARY

For more than a century, the telecommunications networks and services in this country were the envy of the world. We had the fastest, cheapest, most advanced technology and an infrastructure that reached into just about every home and business in the nation. No other country could boast comparable levels of service and technology.

As a result, our telecom industry has long been a critical engine for domestic economic growth. The telecom sector standing alone accounts for nearly three percent of the U.S. GDP – more than any other high-tech industry. The existing infrastructure reflects literally trillions of dollars in capital investment. At its peak in the year 2000, the sector as a whole was investing about $110 billion per year, and thus accounted for about 10 percent of all annual capital spending in the United States. Through its impact on productivity, moreover, the telecom sector's capital investment boosts economic output across the board. The Bureau of Economic Analysis estimates that each dollar invested in U.S. telecom infrastructure results in nearly three dollars of economic output. That multiplier is likely to get larger as ubiquitous, low-cost broadband service becomes more widely available.

The telecom sector has had a commensurately large impact on employment. In the year 2000, it employed almost 1.2 million workers. Employment in the telecom sector as a whole grew more than twice as fast as the national average between 1998 and 2000, and, by the year 2000, the telecom sector was paying nearly twice the average U.S. salary.

As we all know, that situation has changed dramatically. We are currently in a period of "creative destruction" that is transforming the industry. New technologies have advanced at a rapid pace to compete with and displace traditional telecommunications services.

Cable television operators are expected to offer telephony – either VoIP or circuit-switched – to two-thirds of American homes by the end of 2005. At the same time, wireline traffic is increasingly moving to wireless networks, as the already ubiquitous wireless carriers overtake wireline carriers in terms of total "lines" served. And the proliferation of broadband networks – while offering a host of new, IP-based services to consumers – likewise is draining traffic off wireline networks at an astonishing clip.

These competitive developments – though of obvious benefit to consumers – pose a direct threat to the nation's traditional wireline infrastructure. Over the long term, technological transformations cannot be sustained and expanded without extraordinary further investments of capital. Yet just the opposite is happening today. Since 2000, telecommunications service providers, and the equipment manufacturers that supply them, have lost over 700,000 jobs and over $2 trillion in market capitalization, while annual investment declined by more than $70 billion, and the United States fell to 11th in the world in deployment of advanced broadband networks. The capital markets have recognized the increased business risks inherent in traditional telecommunications firms – resulting in constrained access to capital and increasing costs.

This is the environment in which SBC and AT&T find themselves today. Both have endured dramatic declines in market capital, revenues, and jobs. Yet both have significant strengths and resources that are critical to the future of U.S. telecommunications.

The 1984 divestiture of the Bell System and the ensuing 20 years of regulation have segregated the telecommunications industry along artificial local and long distance faults. Companies on both sides of the divide were long precluded from taking advantage of the enormous efficiencies associated with operating an end-to-end network. But the broadband future of our country critically depends on the ability of companies to assemble these separate networks. The maximum potential of broadband can only be achieved where broadband capabilities are implemented at all levels of the network.

That is why the merger of SBC and AT&T provides such an ideal opportunity at this juncture, when intermodal competitors (wireless and cable in particular) are challenging the traditional networks. The existence of separate local and long distance companies no longer benefits consumers. But neither SBC nor AT&T standing alone has the assets and expertise necessary to assemble a true nationwide end-to-end broadband network. Their union will allow beneficial vertical integration without diminishing vigorous horizontal competition. The merger of these two legacy carriers is the most logical and natural outcome to ensure a strong and vibrant industry.

SBC and AT&T have complementary strengths and product sets, and have focused on sales to different groups of customers. SBC is a financially strong provider of voice, data, broadband, and related services to consumers, businesses – especially small and mid-sized businesses – and wholesale customers, primarily on a local and regional basis in its 13-state region. SBC holds a 60% ownership interest in the largest U.S. wireless company, Cingular Wireless, and is one of the leading providers of residential broadband DSL services. At present, SBC is making a $4 billion investment to implement its initial roll-out of next-generation video and other IP-based voice and data services to 18 million households within three years.

AT&T has a different focus. It provides a broad array of voice, data, and IP-based services to customers on its global and national IP-based networks. It has a presence in more than 50 countries, allowing it to compete for the business of the largest global enterprises. AT&T has been a leader in the development of innovative products through its AT&T Labs.

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. The merger will ensure that AT&T, on which the government heavily depends for national security and other needs, remains a strong American company.

Indeed, the merger will produce a flagship U.S. carrier that will offer the most efficient, highest quality capabilities to government, business, and residential customers nationwide. Combining the two companies' core strengths will result in more investment in, and faster deployment, of innovative new technologies and services, and those services will benefit all customers, not just those now served by the legacy companies.

As described above and as demonstrated further in this application, the merger will produce numerous tangible public interest benefits, and it will enhance, not harm, competition in any sector. In the mass market, AT&T's independent, irreversible decision to stop pursuing such customers for either local or long distance wireline telephony means that it is no longer a substantial competitor in that market, and the elimination of AT&T as an independent corporate entity could not harm mass market competition. Moreover, even before AT&T's decision, the Commission had already concluded in the section 271 process that all local markets in SBC's states are open to competition. Far from harming competition, the merger will *enhance* competition outside of SBC's region and will certainly not *reduce* such competition within that region. The enterprise segment is exceptionally competitive. Suppliers include interexchange carriers, systems integrators, equipment vendors and value-added service providers, other network providers, foreign carriers, CLECs, cable operators, and other ILECs. Moreover, because enterprise customers are highly sophisticated, have widely heterogeneous needs, and rely on complicated and detailed bidding procedures, providers cannot successfully engage in anticompetitive conduct. Finally, as explained in the application, the merger raises no concern about diminished competition in the markets for Internet backbone, wireless, or international services.

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For all of these reasons, this merger will decisively advance the public interest, it will not harm competition, and the transfer applications should be approved expeditiously.