Decision **ALTERNATE PROPOSED DECISION OF COMMISSIONERS PEEVEY AND KENNEDY** (Mailed 10 / 19 / 05)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Joint Application of SBC Communications, Inc. ("SBC") and AT&T Corp. Inc. ("AT&T") for Authorization to Transfer Control of AT&T's Communications of California (U-5002), TCG Los Angeles, Inc. (U-5462), TCG San Diego (U-5389), and TCG San Francisco (U5454) to SBC, Which Will Occur Indirectly as a AT&T's Merger With a Wholly-Owned Subsidiary of SBC, Tau Merger Sub Corporation.	Application 05-02-027 (Filed February 28, 2005)

(Appendix A for List of Appearances, see PD.)

OPINION APPROVING APPLICATION TO TRANSFER CONTROL

TABLE OF CONTENTS

Title **Page**

ATTACHMENT A

OPINION APPROVING APPLICATION TO TRANSFER CONTROL

1. Summary

We hereby approve the application of SBC Communications, Inc. (SBC) and AT&T Corp. (AT&T) (collectively, Applicants) for authority to transfer control of AT&T Communications of California and its related California affiliates from AT&T to SBC subject to the terms and requirements set forth in this order. We have reviewed the proposed merger under the authority of Public Utilities Code § 854 to determine whether it is in the public interest. We have determined that § 854(a) applies to this transaction. Sections 854(b) and (c) do not apply to the transaction and even if it could be argued that those sub-sections apply, it is appropriate to grant an exemption under § 853(b).

The Applicants must meet the conditions adopted herein in order to provide reasonable assurance that the proposed transaction will be in the public interest in accordance with § 854(a). We find that, subject to Applicants' compliance with the adopted conditions, the merger will produce net benefits for consumers and will not adversely affect competition for telecommunications service in California. Conversely, if the Applicants declined to implement the conditions set forth herein, we would conclude that the merger did not comply with § 854 and could not be approved.

2. Procedural Background and Description of Financial Transaction

On February 28, 2005, SBC Communications, Inc. and AT&T Corp. filed a joint application for authorization to transfer control of AT&T Communications of California, TCG Los Angeles, Inc. TCG San Diego, and TCG San Francisco from subsidiaries of AT&T to subsidiaries of the combined organization that will

result from AT&T's planned merger with SBC.[1] The proposed merger would create the largest telecommunications firm in the United States.

Under the proposal, AT&T would merge into a newly formed wholly-owned subsidiary of SBC, created for the specific purpose of this transaction. AT&T will be the surviving entity of the merger for legal purposes. AT&T shareholders will receive 0.77942 shares of SBC stock for each share of AT&T stock they own, as well as a one-time cash dividend from AT&T of $1.30 per AT&T share. SBC shareholders will continue to own SBC stock and otherwise will not be affected by the transaction. Upon completion of the merger, former AT&T shareholders will hold approximately 16% of SBC's outstanding shares.

The application, as originally filed on February 28, 2005, requested Commission authorization of the transaction pursuant to Pub. Util. Code § 854(a) on an expedited basis with no evidentiary hearings. Applicants did not initially include a showing under § 854(b) of the Public Utilities Code, instead claiming that the transaction is exempt from § 854(b).[2] Additionally, although Applicants also believe that § 854(c)[3] should not apply, they supplied information in the application that they asserted met the § 854(c) criteria for approval.

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[1] Unless otherwise noted, subsequent references herein to AT&T California include, by reference these TCG affiliates.

[2] Section 854(b) requires the Commission to find that the proposed change in control provides short-and long-term benefits to customers (§ 854(b)(1), equitably allocate forecasted short-and long-term economic benefits where the Commission has ratemaking authority (§ 854(b)(2), and determine that the change in control does not adversely affect competition (§ 854(b)(3)).

[3] Section 854(c) requires the Commission to apply eight criteria in its evaluation of whether a transaction is in the public interest.

SBC's stated purpose in the acquisition of AT&T is to combine the complimentary strengths of the two companies to enable the merged company to compete more effectively in the telecommunications marketplace. The SBC network is nearly ubiquitous where it is the incumbent but virtually nonexistent outside of its ILEC footprint. On the other hand, AT&T's network was initially constructed as a long distance network, and not limited by a need to serve any end points in a local service area. In contrast to SBC's largely local and regional presence, AT&T operates in more than 50 countries, serving the largest global enterprises with a broad array of voice, data and IP-based services. AT&T focuses on enterprise business and government customers through its national and global network.

By combining their respective strengths, Applicants claim that the merger will enable the combined company to become a stronger competitor, and to serve a wider range of customers across all segments of the telecommunications marketplace beyond just the traditional SBC California territory.

AT&T likewise views the merger as an appropriate response to developments that have challenged its competitive stance in certain markets. Among the most significant changes in this regard has been SBC California's entry into the long-distance market. Once SBC California entered the long distance market, it could successfully bundle long distance with local service offerings. SBC thereby strengthened its competitive position compared with that of AT&T. Since receiving authority to offer long distance service, SBC has accumulated in-region market share faster than any other non-ILEC competitor.[4]

[4] Ex.109, Sumpter Testimony (Pac-West) at 11-12.

AT&T has been less successful in being able to offer bundled service without the vast local exchange network that its competitor, SBC, possesses. To a great extent, AT&T had relied on the unbundled network element platform (UNE-P) in providing mass market local exchange service and the purchase of special access for other applications. With the elimination of UNE-P as a competitive resource, AT&T stopped marketing local service to new customers. AT&T chose to consider new options, leading ultimately to the merger that is the subject of the application before us.

On March 16, 2005, an Assigned Commissioner's Ruling required supplementation of the application to provide information necessary to comply with all Pub. Util. Code §§ 854(b) and (c) requirements. Although the Assigned Commissioner deferred ruling on the applicability of §§ 854(b) and (c), he required the supplemental filing in the interest of ensuring that any potential disagreement over the statute's applicability not be a cause for delay in adjudicating the application.

On March 30, 2005, the Applicants filed a "Joint Supplemental Application of SBC Communications, Inc. and AT&T Corp." in response to the Assigned Commissioner's Ruling, dated March 16, 2005. Protests to the Application were filed on April 14, 2005, by the following parties: California Association of Competitive Telephone Companies ("CALTEL");[5] the Communications Workers of America (CWA)[6], AFL-CIO; the Community Technology Foundation of California; Eschelon Telecom, Inc. and Advanced TelCom, Inc.; Level 3

[5] CALTEL filed its protest on behalf of its member companies.

[6] CWA formally withdrew its protest on June 14, 2005.

Communications, LLC; Navigator Telecommunications, LLC; the Office of Ratepayer Advocates (ORA) and the National Consumer Law Center; Pac-West Telecom, Inc.; Qwest Communications Corporation; the City and County of San Francisco; Telscape Communications, Inc.; The Utility Reform Network (TURN), Utility Consumers' Action Network, Disability Rights Advocates, Consumers Union of U.S., Inc., the Greenlining Institute, and the Latino Issues Forum; US LEC; WilTel Communications, Inc.; and XO Communications Services, Inc.[7]

Intervenors claim that the merger, in the form proposed by Applicants, will not assure net benefits to consumers and will adversely affect competition for telecommunications services in California. Certain intervenors categorically oppose the merger under any conditions, claiming that even with certain mitigating conditions, the merger will still be anticompetitive. They argue that SBC already has a dominant share of the market, and that acquisition of AT&T will only further expand its market power by eliminating its largest competitor. Other intervenors do not oppose the merger, as long as certain conditions are adopted to mitigate perceived adverse impacts. Certain parties express concern that the interests of various underserved communities have not been properly addressed. Parties also argue that the proposed Verizon and MCI merger must be also taken into account, as well, in light of its cumulative effect on reducing competition.

Joint Applicants filed a reply in opposition to the protests on March 30, 2005, asserting that the merger is in the public interest, and that there are no

[7] The following parties subsequently withdrew their protests as follows: WilTel on June 18, 2005; US LEC on June 21, 2005; Eschelon Telecom and Advanced TelCom on

Footnote continued on next page

adverse competitive effects. A prehearing conference was held on April 20, 2005, and the Assigned Commissioner issued a Scoping Memo by Ruling on April 26, 2005, directing that evidentiary hearings would be held. Applicants served opening testimony on May 6, 2005, and intervenors served reply testimony on June 24, 2005. Applicants served rebuttal testimony on July 8, 2005. Twenty-eight witnesses submitted testimony. ORA and TURN presented 11 witnesses. Seven witnesses were presented by parties representing competitors including CALTEL, Cox, Qwest, Level 3, Telscape, and Pac-West. Other parties presenting witnesses were Latino Issues Forum(LIF); Community Technology Federation of California (CTFC); Disability Rights Advocates (DRA), The Greenlining Institute (Greenlining); and City and County of San Francisco.

Evidentiary hearings were held from August 8-12 and 15-17. Opening briefs were filed on September 9 and reply briefs were filed on September 19, 2005. Concurrently with their opening briefs, a proposed settlement on certain issues was filed and served, jointly sponsored by Applicants, Greenlining and LIF.

The Commission also conducted Public Participation Hearings (PPHs) in Oakland, Sacramento, Fresno, Culver City, Anaheim, Riverside, and San Diego. These hearings were well attended, particularly in Oakland and Culver City. Many representatives from community organizations and some individuals attended the hearings, presenting a variety of views concerning the proposed merger. Both during and subsequent to the PPHs, many additional individuals and representatives of community organizations contacted the Commission with written letters and by electronic mail expressing their views on the proposed

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June 24, 2005; and XO on June 24, 2005.

merger. We have reviewed and taken into account, as appropriate, the comments presented by members of the public, both at the PPHs and through subsequent cards, letters, and electronic mailings to the Commission. We wish to express our appreciation to all of the individuals who took the time to attend the PPHs or to otherwise communicate their comments.

3. The Corporate Entities

The primary corporate entities involved in this financial transaction are SBC and AT&T. The financial transaction is one that places AT&T under the control of SBC.

3.1. SBC

SBC is a corporation created and existing under the laws of the state of Delaware headquartered in San Antonio, Texas. SBC is a holding company and does not directly provide any services in California or elsewhere.

SBC, through its subsidiaries, offers a wide range of voice, data, broadband, and related services that it provides to consumers, businesses, and wholesale customers, primarily on a local and regional basis. SBC holds a 60% ownership interest in Cingular Wireless which provides wireless services in California and the United States.

SBC California is a regulated public utility and an incumbent local exchange carrier (ILEC) in California. It is one of various subsidiaries directly or indirectly owned and controlled by SBC. SBC California is not a party to the proposed merger transaction or to this Application.

3.2. AT&T

AT&T is a corporation created and existing under the laws of the state of New York headquartered in Bedminster New Jersey. AT&T is a holding company that directly or indirectly owns and controls various subsidiaries,

including four California certificated public utilities: (1) AT&T California, (2) TCG-LA, (3) TCG-SD, and (4) TCG-SF.

AT&T, through its subsidiaries, is authorized to provide domestic and international telecommunications services throughout the United States. AT&T operates the world's largest communications network and offers a global presence in more than 50 countries, national and global IP-based networks, a portfolio of data and IP services, hosting, security and professional services, technology leadership through its AT&T Labs, skilled networking capabilities, and a highly significant base of government and large business customers.

AT&T California is a wholly owned, first-tier subsidiary of AT&T. AT&T California is a Nondominant Interexchange Carrier (NDIEC) and Competitive Local Exchange Carrier (CLEC). The three TCG entities are also NDIECs and CLECs.

4. Jurisdiction and Scope of Proceeding

4.1. Background

The scope of this proceeding is governed by Pub. Util. Code §§ 851-856.

4.2. §854(a) Applies to this Transaction

Pub. Util. Code § 854(a) specifies that, "No person or corporation, whether or not organized under the laws of this state, shall merge, acquire, or control either directly or indirectly any public utility organized and doing business in this state without first securing authorization to do so from this Commission. The Commission may establish by order or rule the definitions of

what constitute merger, acquisition, or control activities that are subject to this section of the statute."[8]

The March 16, 2005 Assigned Commissioner Ruling directed the Applicants to continue to provide all the information they believed necessary and appropriate to demonstrate compliance with all of the provisions of Pub. Util. Code §§ 854(a), (b) and (c) to ensure that there would be no unnecessary delay in processing of the application. There is no dispute as to the applicability of § 854(a) to this transaction.

4.3. Application of §§ 854 (b) and (c) to this Transaction

The plain language of the statute, its legislative history and prior Commission decisions guide our application of this statute to this transaction, specifically the applicability of §§ 854 (b) and (c).

Pub. Util. Code § 854(b) states:

> Before authorizing the merger, acquisition, or control of any electric , gas, or telephone utility organized and doing business in this state, where any of the utilities that are parties to the proposed transaction has gross annual California revenues exceeding five hundred million dollars ($500,000,000), the commission shall find that the proposal does all of the following:
>
> (1) Provides short-term and long-term economic benefits to ratepayers.
>
> (2) Equitably allocates, where the commission has ratemaking authority, the total short-term and long-term forecasted economic benefits, as determined by the commission, of the proposed merger, acquisition, or control, between shareholders and ratepayers. Ratepayers shall receive not less than 50 percent of those benefits.

[8] § 854(a)

(3) Not adversely affect competition. In making this finding, the commission shall request an advisory opinion from the Attorney General regarding whether competition will be adversely affected and what mitigation measures could be adopted to avoid this result.[9]

4.3.1. It is not reasonable to "pierce the corporate veil" as neither SBC California nor AT&T California is "key to the merger."

In D.97-03-067, the SBC acquisition of Pacific Telesis, the Commission determined that "Although the transaction is technically structured as a merger between SBC and Telesis, the practical result of the proposed transaction…is that it involves Pacific." The Commission found that, since SBC, an out of state corporation, was acquiring California's largest provider of basic local exchange service, it was in the public interest to "pierce the corporate veil" in order to consider the transaction based on "substance rather than form."

The Commission concluded that Pacific was a party to the transaction within the meaning of § 854(b) based on the reasoning that the very large California utility being acquired was "key to the merger." Specifically the Commission reasoned that:

- Pacific represented 90% or more of Telesis' assets.
- The economic benefits to be realized from the transaction were based on the joint and combined operations of Pacific and Southwestern Bell Telephone.

[9] § 854(b)

- One of the principal reasons SBC pursued the transaction was to add the 15.8 million access lines in California to its existing 14.2 million telephone access lines.

Applying the same criterion used in the SBC-Telesis merger to the instant transaction leads to the opposite conclusions:

- SBC California is not the subject of the acquisition in this application.

- SBC California does not account for a majority of the holding company's assets Public information indicates that as of June 30, 2005, approximately one-third of SBC's access lines were located in California. [10]

- The economic benefits to be realized from the transaction are not driven by any savings based on the joint and combined operations of SBC California and AT&T California. Only the indirect control of AT&T California will pass to SBC as a result of AT&T's merger.

- AT&T's California subsidiaries are NDIECs and CLECs. Pacific was the largest ILEC in California at the time of the SBC / Telesis merger.

- The principal reason stated by SBC for pursuing the acquisition of AT&T is the addition of AT&T's global presence in 50 countries, national and global IP-based networks, a portfolio of data and IP services, hosting, security and professional services, technology leadership through AT&T Labs, skilled networking capabilities, and a base of government and large business customers. The number of AT&T access lines in California to be added to SBC's access lines through this transaction is *de minimis*.

Applying the criteria used in the SBC-Telesis merger, it is clear that because SBC California is neither the subject of the acquisition nor "key to the merger," there is no reason to "pierce the corporate veil".

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[10] SBC Investor Relations "Fact Sheet" at http: / / www.sbc.com / gen / investor-relations?pid=1130

4.3.2. Exemption under §853(b) makes consideration of affiliate revenues irrelevant

As the law makes clear, this Commission has broad authority under § 853(b) and § 854(a) to exempt transactions from review under §§ 854(b) and (c) regardless of the $500 million threshold. Pub. Util. Code § 853(b) states:

> "The commission may from time to time by order or rule, and subject to those terms and conditions as may be prescribed therein, exempt any public utility or class of public utility from this article if it finds that the application thereof with respect to the public utility or class of public utility is not necessary in the public interest."[11]

As established by D. 97-052-092, D.97-07-060 and D. 98-05-022, the Commission has consistently exercised its broad authority under § 853(b) to exempt transactions from review under §§ 854(b) and (c) regardless of the presence of gross annual revenues in excess of the $500 million threshold when a very large ILEC is not the subject of an acquisition or when the subject of an acquisition is an NDIEC or CLEC.

In the MCI-BT case (D.97-07-060) the Commission recognized the sweeping authority granted to the Commission by the Legislature in this regard: "…the extent of our broad exemptive powers in § 853(b) is clear on the face of that statute..." The Commission further concluded that "We think this evinces a legislative intent to permit us to use our powers under both §853(b) and § 854(a) to exempt transactions from review under §§ 854(b) and (c), regardless of the presence of gross annual California revenues in excess of $500 million."[12]

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[11] §853(b)

[12] D. 97-07-060 (at *24)

Thus, based on the unambiguous authority granted to the Commission under § 853(b), the Commission has clearly and consistently exercised its authority to exempt transactions involving the acquisition of NDIECs and CLECs, regardless of whether the $500 million revenue threshold has been met.

4.3.3. Prior applications of §854(b) to transactions involved the acquisitions of ILECs, not NDIECs or CLECs

In prior decisions, the Commission has distinguished between the application of § 854(b) to transactions involving the acquisition of California's largest incumbent local exchange carriers (ILECs) and transactions involving competitive carriers (CLECs) or non-dominant inter-exchange carriers (NDIECs), choosing not to apply this section of the Public Utilities Code to the latter. Each of AT&T's California subsidiaries is a CLEC or an NDIEC.

A review of past decisions demonstrates that this Commission has clearly and consistently exercised its authority to exempt transactions not involving the acquisition of a California ILEC from application of § 854(b). In all cases over the past 15 years this Commission has exempted transactions involving the acquisition of NDIECs, CLECs, and other non-ILECs.[13]

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[13] In the past decade, the Commission has authorized scores of transactions involving NDIECs and CLECs, but uniformly has exempted them from the detailed requirements of § 854(b), and, with limited exception, has exempted them from § 854(c). The decisions reaching this result include: *Re Application of Resurgens Communications Group, Inc. to Acquire Control of Comm Sys. Network Servs., Inc., TMC Communications, Inc. and TMC Communications, L.P.*, Decision 91-09-095, 41 Cal. P.U.C. 2d 429, 1991 Cal. PUC LEXIS 607 (Sept. 30, 1991); *Re Joint Application of AT&T Corp., Italy Merger Corp. and Tele-Communications, Inc. for Approval Required for the Change in Control of TCI Telephony Servs. of California, Inc. That Will Occur Indirectly as a Result of the Merger of AT&T Corp. and Tele-Communications, Inc.*, Decision 99-03-019, 85 Cal. P.U.C. 2d 249, 1999 Cal. PUC

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LEXIS 382 (Mar. 4, 1999); *Re Joint Application of AT&T Corp. ("AT&T"), Teleport Communications Group Inc. ("TCG") and TA Merger Corp. for Approval Required for the Change in Control of TCG's California Subsidiaries That Will Occur Indirectly as a Result of the Merger of AT&T and TCG*, Decision 98-05-022, 80 Cal. P.U.C. 2d 273, 1998 Cal. PUC LEXIS 533 (May 7, 1998); *Application of MidAmerican Communications Corp. to Transfer, and of LDDS Communications, Inc., to Acquire, Certain Shares and Control of MidAmerican Communications Corp., and for Permission and Approval For MidAmerican Communications Corp. to Borrow, Guaranty, and Grant a Security Interest in Collateral*, Decision 91-06-061, 40 Cal. P.U.C. 2d 637, 1991 Cal. PUC LEXIS 388 (June 24, 1991); *In re Request of WorldCom, Inc. and Intermedia Communications Inc., for Approval to Transfer Control of Intermedia Communications Inc. and its Wholly-owned Subsidiary to WorldCom, Inc.*, Decision 01-03-079, 2001 Cal. PUC LEXIS 219 (Mar. 27, 2001); *Joint Application of Access One Communications Corp., Formerly Known as CLEC Holding Corp., OmniCall Acquisition Corp., and OmniCall, Inc. for Approval of Transfer of Control*, Decision 00-01-059, 2000 Cal. PUC LEXIS 85 (Jan. 28, 2000); *Application of American Network Exch., Inc. and its Subsidiary, Amnex (California), Inc., to Transfer, and of Nycom Info. Servs., Inc., to Acquire Control of a Certificate by Merging American Network Exch., Inc. into Amnex Acquisition Corp., a Subsidiary of Nycom Info. Servs., Inc.*, Decision 90-03-047, 35 Cal. P.U.C. 2d 664, 1990 Cal. PUC LEXIS 154 (Mar. 19, 1990); *Application of State Communications, Inc., TriVergent Communications, Inc., Gabriel Communications, Inc., and Triangle Acquisition, Inc. for Approval of a Transfer of Control*, Decision 01-02-005, 2001 Cal. PUC LEXIS 139 (Feb. 8, 2001); *Re Joint Application of NetMoves Corp., Certain Shareholders of NetMoves Corp., and Mail.com Inc., for Approval of an Agreement and Plan of Merger and Related Transactions*, Decision 00-12-053, 2000 Cal. PUC LEXIS 1055 (Dec. 21, 2000); *Application for Auth. for AppliedTheory Corp. to Acquire Control of CRL Network Servs., Inc., a California Corp., Pursuant to Article 6 of Chapter 4 of the California Pub. Util. Code*, Decision 00-09-033, 2000 Cal. PUC LEXIS 693 (Sept. 7, 2000); *Re Application for Auth. to Transfer Control of StormTel, Inc., F/K/A Z-Tel, Inc., to CCC Merger Corp.*, Decision 00-09-035, 2000 Cal. PUC LEXIS 695 (Sept. 7, 2000); *Joint Application for Auth. for LDDS Communications, Inc. to Merge with Metromedia Communications Corp. and Resurgens Communications Group, Inc.*, Decision 93-08-039, 50 Cal. P.U.C. 2d 611, 1993 Cal. PUC LEXIS 586 (Aug. 18, 1993); *Joint Application for Auth. for LDDS Communications, Inc. to Acquire Control of Dial-Net, Inc.*, Decision 93-03-029, 48 Cal. P.U.C. 2d 420, 1993 Cal. PUC LEXIS 169 (Mar. 11, 1993); *Joint Application of Evercom Sys., Inc. and H.I.G. Capital Partners III, LP for Approval of Acquisition by*

Footnote continued on next page

H.I.G. Capital Partners III, LP of Indirect Control Over Evercom Sys., Inc., Decision 04-11-010, 2004 Cal. PUC LEXIS 534 (Nov. 10, 2004); *Joint Application of T-NETIX Telecommunications Servs., Inc. and H.I.G. Capital Partners III, LP for Approval of Acquisition by H.I.G. Capital Partners III, LP of Indirect Control Over T-NETIX Telecommunications Servs., Inc.,* Decision 04-11-004, 2004 Cal. PUC LEXIS 505 (Nov. 9, 2004); *Re Application of MCCC ICG Holdings LLC and, ICG Communications, Inc. to Complete a Transfer of Control of ICG Telecom Group, Inc. an Authorized Carrier,* Decision 04-10-005, 2004 Cal. PUC LEXIS 483 (Oct. 7, 2004); *Joint Application for Approval of Agreement and Plan of Merger By and Among World Access, Inc., WorldxChange Communications, Inc. and Communication Telesystems Int'l D/B/A WorldxChange, and Request for Expedited Ex Parte Relief,* Decision 00-10-064, 2000 Cal. PUC LEXIS 752 (Oct. 19, 2000); *Joint Application for Approval of Agreement and Plan of Merger by and Among World Access, Inc. and Star Telecommunications, Inc. d/b/a CEO Telecommunications and for the Change in Control of California Certificated Subsidiaries,* Decision 00-10-013, 2000 Cal. PUC LEXIS 812 (Oct. 5, 2000); *Joint Application and Request for Expedited Ex Parte Treatment of KDD America, Inc. and DDI Corp. for Approval of Transfer of Control,* Decision 03-08-058, 2000 Cal. PUC LEXIS 1134 (Aug. 21, 2003); *Joint Application of Telscape Int'l, Inc., Telscape USA, Inc., MSN Communications, Inc., Pointe Communications Corp., and Pointe Local Exch. Co. for Approval of Transfers of Control and Related Transactions,* Decision 00-09-031, 2000 Cal. PUC LEXIS 681 (Sept. 7, 2000); *Joint Application of Zenex Long Distance, Inc., Prestige Invs., Inc., Shareholders of Prestige Invs., Inc., and Lone Wolf Energy, Inc. for Approval of a Merger and Acquisition of Prestige Invs., Inc.,* Decision 00-07-033, 2000 Cal. PUC LEXIS 586, (July 18, 2000); *Re Time Warner Inc. and AOL Time Warner Inc. for Approval of the Change in Control of Time Warner Connect That Will Occur Indirectly as a Result of the Merger of Time Warner Inc. and America Online, Inc.,* Decision 00-04-045, 2000 Cal. PUC LEXIS 180 (Apr. 13, 2000); *Re Time Warner Inc. and AOL Time Warner Inc. for Approval of the Change in Control of Time Warner Telecom of California, L.P. That Will Occur Indirectly as a Result of the Merger of Time Warner Inc. and America Online, Inc.,* Decision 00-04-044, 2000 Cal. PUC LEXIS 179 (Apr. 13, 2000); *Joint Application Under Pub. Util. Code § 854 for Approval of the Merger of ACN Communications, Inc. and Arrival Communications of California, Inc.,* Decision 00-04-043, 2000 Cal. PUC LEXIS 178 (Apr. 12, 2000); *Application of HTC Communications, LLC for Approval Nunc Pro Tunc to Transfer Control to Pointe Communications Corp. and for Other Related Transactions,* Decision 00-04-014, 2000 Cal. PUC LEXIS 192 (Apr. 6, 2000); *Joint Application of Empire One Telecommunications, Inc. and EOT Acquisition Corp. for Approval of the*

Footnote continued on next page

Transfer of Empire One's Assets and Assignment of Empire One's Certificates of Pub. Convenience and Necessity to EOT, Decision 00-02-029, 2000 Cal. PUC LEXIS 73 (Feb. 8, 2000); *Joint Application for Approval of Acquisition by U.S. TelePacific Holdings Corp. of U.S. TelePacific Corp.*, Decision 99-11-066, 1999 Cal. PUC LEXIS 796 (Nov. 30, 1999); *Joint Application and Request for Expedited Ex Parte Treatment by Econophone Servs., Inc. and Viatel, Inc. for Approval of Agreement and Plan of Merger*, Decision 99-11-035, 1999 Cal. PUC LEXIS 848 (Nov. 4, 1999); *Application of MVX Communications, LLC for Auth. to Transfer Control to MVX.Com Communications, Inc.*, Decision 99-10-044, 1999 Cal. PUC LEXIS 706 (Oct. 19, 1999); *In re Application of Global Crossing Ltd. and Frontier Corp. for Approval to Transfer Control of Frontier Corp.'s California Operating Subsidiaries to Global Crossing Ltd.*, Decision 99-06-099, 1999 Cal. PUC LEXIS 470 (June 30, 1999); *Re Claricom Networks, Inc., Application for Approval of an Indirect Change in Control from Claricom Holdings, Inc. to Sigma Acquisition Corp.*, Decision 99-02-093, 85 Cal. P.U.C. 2d 210, 1999 Cal. PUC LEXIS 69 (Feb. 19, 1999); *Application of Teleglobe Inc. and Excel Communications, Inc. for Approval of Agreement and Plan of Merger*, Decision 98-09-084, 1998 Cal. PUC LEXIS 990 (Sept. 24, 1998); *Application of PWT Acquisition Corp. and Pac-West Telecomm, Inc. for Approval to Transfer Control of Pac-West Telecomm, Inc.*, Decision 98-09-050, 1998 Cal. PUC LEXIS 961 (Sept. 11, 1998); *Application of Qwest Communications Int'l, Inc., LCI Int'l, Inc., LCI Int'l Telecom, Corp., and USLD Communications, Inc. for Approval of a Transfer of Control*, Decision 98-06-001, 1998 Cal. PUC LEXIS 385 (June 1, 1998); *Re Application of WorldCom, Inc. and Brooks Fiber Props., Inc. for Approval of Agreement and Plan of Merger*, Decision 97-11-091, 1997 Cal. PUC LEXIS 1071 (Nov. 21, 1997); *Re Joint Application of SmarTalk TeleServices, Inc. and ConQuest Operator Servs. Corp. for an Order Authorizing the Acquisition by Merger of ConQuest Operator Servs. Corp. Pursuant to Cal. Pub. Util. Code §§ 851-854*, Decision 97-11-046, 76 Cal. P.U.C. 2d 547, 1997 Cal. PUC LEXIS 1055 (Nov. 13, 1997); *Application for Auth. for Avery Communications, Inc., to Acquire Control of Home Owners Long Distance, Inc.*, Decision 96-09-049, 1996 Cal. PUC LEXIS 924 (Sept. 11, 1996); *Joint Application of Continental Telecommunications of California, Inc., Continental Cablevision, Inc. and U S West, Inc. for Auth. to Transfer Control of Continental Telecommunications of California, Inc. from Continental Cablevision, Inc. to U S West, Inc.*, Decision 96-08-015, 67 Cal. P.U.C. 2d 214, 1996 Cal. PUC LEXIS 836 (Aug. 2, 1996); *Application for Auth. to Transfer Control of Western Union Communications, Inc. to First Data Corp.*, Decision 95-10-051, 1995 Cal. PUC LEXIS 907 (Oct. 23, 1995); *Re Donyda, Inc. d/b/a/ Call America of Palm Desert and Call America of San Diego, Transferor, and*

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In D. 98-08-068 the Commission clearly articulated the historic application of § 853(b) authority when acquisition of a large California ILEC is not involved: "As in the BT / MCIC and AT&T / TCG mergers, the acquisition of a heavily-regulated local exchange carrier is not the reason for the instant merger."[14] In the footnote to the above citation, the Commission noted: "While AT&T was once more heavily regulated as a dominant carrier, by the time of the TCG merger we had accorded it nondominant status."[15]

Accordingly, and for the same reasons, we conclude that because all California subsidiaries of AT&T are CLECs or NDIECs, it is not necessary in the public interest to apply § 854(b) to this transaction.

California Acquisition Corp. d/b/a/ Valley Acquisition Corp., Transferee, Application for Consent to Transfer Control of a Resale Common Carrier; Re Application of Inland Call America, Inc., Transferor, and Telecom Acquisition Corp., Transferee, Application for Consent to Transfer Control of a Resale Common Carrier, Decision 95-07-051, 60 Cal. P.U.C. 2d 590, 1995 Cal. PUC LEXIS 601 (July 19, 1995); *Joint Application for Auth. for MfsGaAqCo No. 1 to Merge with RealCom Office Communications, Inc.,* Decision 94-07-078, 55 Cal. P.U.C. 2d 505, 1994 Cal. PUC LEXIS 964 (July 28, 1994); *Joint Application for Auth. for LDDS Communications, Inc. to Acquire Control of Advanced Telecommunications Corp.,* Decision 92-09-097, 45 Cal. P.U.C. 2d 658, 1992 Cal. PUC LEXIS 805 (Sept. 29, 1992); *Re Application of American Network, Inc. and ATE, Inc. for Authorization to Merge Amnet Subsidiary, Inc., a Wholly Owned Subsidiary of American Network, Inc., into ATE, Inc.,* Decision 86-11-011, 22 Cal. P.U.C. 2d 304,1986 Cal. PUC LEXIS 676 (Nov. 5, 1986).

[14] D. 98-08-068 Section VI par. 5

[15] Ibid, footnote n4

4.3.4. Legislative history demonstrates that the Legislature intended to give the Commission flexibility in the application of §854(b) where traditional cost-of-service utilities are not involved in the transaction.

Prior to 1995, Pub. Util. Code § 854(b) required the Commission to review acquisitions, mergers and changes of control in instances where "the acquiring or to be acquired utility has gross annual California revenues exceeding five hundred millions dollars."[16] Both subsections (b) and (c), known as the "Edison Amendments," were added to § 854 in 1989 following a series of proposed mergers in the electric industry.

At the time, the applicability of § 854(b)(1) rested on the assumption that a regulated utility subject to an acquisition or merger operated under a traditional cost-of-service ratemaking scheme and that any savings resulting from a merger that were not anticipated at the time the utility's rates were set would not flow through to ratepayers without regulatory action by the Commission.

The pre-1995 statute was historically interpreted by this Commission to require all transactions, regardless of whether a utility was a party to the transaction, to be analyzed according to the provisions in §§ 854 (b) and (c), unless exempted pursuant to the Commission's authority under § 853(b) or § 854(a), with 100 percent of quantified economic benefits allocated to ratepayers.

In 1995 the Legislature amended §§ 854(b) and (c) to limit the application of § 854(b) to transactions to which a large, traditionally-regulated

[16] § 854(b) as amended by SB 52 in 1989

California utility is a party.[17] These amendments were proposed by the CPUC and enacted by the Legislature in response to the Commission's adoption of the "New Regulatory Framework" ("NRF") in which the Commission moved away from traditional cost-of-service ratemaking for telephone service providers and toward a regulatory framework that recognizes the benefits to consumers of increased competition in the telecommunications industry.

Assembly Bill 119 amended § 854(b) (1) in order to "provide the CPUC with the flexibility needed in the current regulatory environment, where, increasingly, rates are set through a price cap or incentive based mechanism, rather than through traditional command and control method."[18] The Commission's analysis in support of the bill indicates the reason the CPUC sponsored the legislation:

> "This amendment modernizes' sec. 854 in light of changes in the regulatory environment since 1989. It recognizes that, increasingly, large utilities are being regulated under 'price cap' mechanism or a 'performance based' system rather than the 'command and control' system of traditional, 'cost-of-service' regulation. In this new regulatory environment utility cost recovery is not guaranteed to the same extent but innovative, cost-cutting behavior is better rewarded. The idea is to better balance utility risk and reward and to bring lower costs to ratepayers (without decreasing service), by moving toward a 'carrot' approach to regulation and away from a 'stick' approach. Under these so-called 'incentive-based' regulatory systems, ratepayers and shareholders share costs, savings and profits in varying degrees."

[17] Amended Statutes 1995 Chapter 622 Section 1 (AB 119).

[18] Report of Assembly Committee on Utilities and Commerce, April 3, 1995 at 1

The Commission-sponsored amendments to § 854(b): (i) remove the requirement that the Commission find that the proposal provides net benefits to ratepayers, and instead require the Commission to find that the proposal provides short-term and long-term economic benefits to ratepayers; and (ii) equitably allocate the short-term and long-term forecasted economic benefits of the proposed transaction as determined by the Commission between shareholders and ratepayers ***where the Commission has ratemaking authority*** (emphasis added). In those cases where merger benefits are allocated by the Commission through its ratemaking authority, ratepayers must receive not less than 50 percent of the benefits.

The Legislature's intent to provide the Commission with the flexibility to determine which transactions are subject to these requirements and to determine how best to allocate their benefits is clear in the statements that were made at the time the amendments were added: "If rates are not regulated because the industry is competitive, it may not be appropriate to require any sharing of benefits."[19]

We conclude that even if this transaction were not exempt from § 854(b) and § 854(c) pursuant to § 854(f), legislative history confirms that the Commission is well within its discretionary authority under § 853(b), to exempt the transaction from the allocation of economic benefits *vis-à-vis* a traditional ratemaking mechanism contemplated under § 854(b). We also conclude that these amendments were not intended to countermand the statutory obligation that any such transaction be approved only if it is in the public interest.

[19] Senate Committee on Energy, Utilities, and Communications, July 11, 1995 at 3

4.3.5. Exempting this transaction from § 854(b) is in the public interest pursuant to the authority granted in § 853(b) and consistent with Commission precedent.

After passage of the 1996 Telecommunications Act[20] and adoption of the New Regulatory Framework in California[21], the Commission consistently relied on a three-part test for telecommunications mergers and acquisitions to guide the determination as to whether a transaction warranted exemption from § 854(b) pursuant to § 853(b) or § 854(a).

Beginning with the British Telecom-MCI merger in 1997,[22] the Commission applied three principal questions to transactions involving telecommunications companies where the application of § 854(b) was considered:

- Does the transaction involve putting together two traditionally or incentive regulated telephone systems?
- Does the Commission exercise the type of ratemaking authority that would facilitate an allocation of the merger benefits as contemplated under § 854(b)?
- Has the acquired company grown under competitive forces at the sole risk of its shareholders?

In the MCI-BT case the Commission concluded:

> "The instant application does not involve putting together two traditionally regulated telephone systems, nor are contiguous or nearby service territories involved….The acquisition does not involve merging any BT operations into MCIC operations. No consolidation of MCIC subsidiary management with BT management is contemplated….We do

[20] U.S. 47

[21] D.89-10-031

[22] Re MCI Communications Corporation, D. 97-05-092, 72 CPUC 2s 656 at 664-665

> not have traditional ratemaking authority over MCIC's operations. Competitive market forces will distribute any benefits of this merger to ratepayers, therefore, to review this transaction under PU Code § 854(b) would be a futile exercise. MCIC has grown under competitive forces at the sole risk of its shareholders without a captive ratepayer base and guaranteed franchise territory to buffer risk and reward. Review of this particular transaction under §§ 854(b) and (c) will stifle competition and discourage the operation of market forces and is contrary to the main thrust of our telecommunications policy and the Telecommunications Act of 1996."[23]

Asking these three questions of the instant application leads to similar answers.

First, the instant application does not involve putting together two traditionally regulated telephone systems. The subject of the acquisition, AT&T, is an NDIEC and a CLEC that operates primarily in the heavily competitive and rapidly declining long distance market. The Commission did not exercise traditional ratemaking authority over AT&T California post-divestiture which occurred in 1984.

Moreover, SBC California is an ILEC no longer subject to traditional cost-of-service rate regulation. It is subject to regulation under the Commission's New Regulatory Framework, designed for transition to a competitive market, with significant or complete pricing flexibility for all services other than basic local exchange service.

Post-divestiture, neither AT&T nor its California subsidiaries have ever been subject to traditional cost-of-service regulation that would facilitate an

[23] In the matter of the Joint Application of MCI Communications Corporation and British Telecommunications, D. 97-07-060 1997 Cal. PUC LEXIS 557, Finding of Fact 15

allocation of the merger benefits as contemplated under § 854(b). Further, although the Commission last distributed merger benefits via a sur-credit following the acquisition of GTE by Bell Atlantic, five years have passed since that action, and NRF ratemaking and the new regulatory environment do not facilitate an equitable distribution of merger benefits through a traditional ratemaking mechanism as contemplated under § 854(b).

Indeed, as contemplated under NRF and the federal Telecommunications Act, the telecommunications industry has become more competitive since 1996. Attempting to mandate the distribution of economic benefits of a merger or acquisition of this type using traditional rate regulation mechanisms today would be detrimental to the operation of market forces and is contrary to the main thrust of the 1996 Telecommunications Act, state telecommunications policy, and this Commission's stated policies under NRF.

Post-divestiture, AT&T has grown (and shrunk) under competitive market forces at the sole risk of its shareholders without a captive ratepayer base and guaranteed franchise territory to buffer risk and reward.

As a result, even if § 854(b) applied to this transaction, granting an exemption would be consistent with past Commission practice and in the public interest. Thus, subjecting such a transaction to §854(b) "is not necessary in the public interest" pursuant to the authority granted us in PU Code § 853(b), as well as §854(a).

4.3.6. Commission precedent and § 854(c) provide the appropriate guidelines for determining whether this transaction is in the public interest.

Over time, the Commission has used its discretion in different ways in reviewing mergers. In D.97-08-29 the Commission approved a transfer of control

after determining that the transaction "would not be adverse to the public interest."[24] Historically, the Commission has sought more broadly to determine whether a change in control is in the public interest:

> "The Commission is primarily concerned with the question of whether or not the transfer of this property from one ownership to another...will serve the best interests of the public. To determine this, consideration must be given to whether or not the proposed transfer will better service conditions, effect economies in expenditures and efficiencies in operation."[25]

D.97-07-060 notes that over the years, our decisions have identified a number of factors that should be considered in making the determination of whether a transaction is in the public interest.[26] More recently, D.00-06-079 provides an overview of these factors:

> "Antitrust considerations are also relevant to our consideration of the public interest.[27] In transfer applications we require an applicant to demonstrate that the proposed utility operation will be economically and financially feasible.[28] Part of this analysis is a consideration of the price to be paid considering the value to both the seller and buyer.[29] We have also considered efficiencies and operating costs savings that should result from the proposed

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[24] *Ibid.*, Finding of Fact 3, 645.

[25] Union Water Co. of California, 19 CRRC 199, 202 (1920) at 200.

[26] 1997 Cal PUC LEXIS 557 *22-25.

[27] 65 CPUC at 637, n.1.

[28] R. L. Mohr (Advanced Electronics), 69 CPUC 275, 277 (1969). See also, Santa Barbara Cellular, Inc. 32 CPUC2d 478 (1989).

[29] Union Water Co. of California, 19 CRRC 199, 202 (1920).

> merger.[30] Another factor is whether a merger will produce a broader base for financing with more resultant flexibility."[31]
>
> "We have also ascertained whether the new owner is experienced, financially responsible, and adequately equipped to continue the business sought to be acquired.[32] We also look to the technical and managerial competence of the acquiring entity to assure customers of the continuance of the kind and quality of service they have experienced in the past.[33]"[34]

Subsequently, D.00-06-079 assessed the proposed transaction against the seven criteria identified in § 854(c),[35] and included a broad discussion of antitrust and environmental considerations.[36] Thus, even though § 854(c) does not apply to this transaction, it is reasonable to consider these factors in helping us determine if this transaction is in the public interest. Therefore, a review of

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[30] Southern Counties Gas Co. of California, 70 CPUC 836, 837 (1970).

[31] Southern California Gas Co. of California, 74 CPUC 30, 50, modified on other grounds, 74 CPUC 259 (1972).

[32] City Transfer and Storage Co., 46 CRRC 5, 7 (1945).

[33] Communications Industries, Inc. 13 CPUC2d 595, 598 (1993).

[34] D.00-06-079 (2000 Cal PUC LEXIS 645, *17-*20), footnotes included but renumbered into the current sequence.

[35] Public interest factors enumerated under this code section are whether the merger will" (1) maintain or improve the financial condition of the resulting public utility doing business in California; (2) maintain or improve the quality of service to California ratepayers; (3) maintain or improve the quality of management of the resulting utility doing business in California; (4) be fair and reasonable to the affected utility employees; (5) be fair and reasonable to a majority of the utility shareholders; (6) be beneficial on an overall basis to state and local economies and communities in the area served by the resulting public utility; and (7) preserve the jurisdiction of the Commission and our capacity to effectively regulate and audit public utility operations in California."

[36] D.00-06-079 (2000 Cal. PUC LEXIS 645, *17-*38); see also D.01-06-007 (2001 Cal. PUC LEXIS 390 *25-*26) for a similar list of factors.

this transaction in terms of § 854(c), as well as a consideration of environmental and competitive issues, constitutes the appropriate scope of this proceeding.

4.4. Summary of Applicable Law

In summary, we find that §§ 854(b) and (c) do not apply to this transaction.

To determine whether this transaction is in the public interest, the proposed transaction will be assessed against the seven criteria identified in § 854(c), and will include a broad discussion of antitrust and environmental considerations, as has been done in previous cases.

5. Does the Proposed Merger of the Parent Companies and Change in Control "Not Adversely Affect Competition?"

The Commission requested an Advisory Opinion from the Attorney General on the competitive effects of the proposed merger of SBC and AT&T.

The Advisory Opinion was filed at the Commission on July 22, 2005. The Advisory Opinion employs the approach embodied in anti-trust laws, including the Department of Justice and Federal Trade Commission's 1992 Horizontal Merger Guidelines and their April 8, 1997 revisions (the Guidelines).

The Advisory Opinion finds that "the merger may have the effect of raising average rates for DS1 and DS3 service."[37] For all other products, however, it finds "that competitive effects in properly-defined markets for other relevant products – including those for mass market local exchange, mass market long distance, "enterprise," and Internet backbone services – will be minimal."[38]

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[37] Advisory Opinion, p. 1.

[38] Advisory Opinion, p. 1.

Although the Advisory Opinion does not control the Commission's findings concerning the effects of the proposed transaction on competition, the Advisory Opinion is entitled to "great weight."[39] In deference to this Advisory Opinion, we organize our discussion of the competitive effects of this merger following the analysis provided by the Attorney General. In particular, we examine the effect of this merger on 1) mass market local exchange; 2) mass market long distance; 3) enterprise services; 4) special access services; and 5) Internet backbone. In addition to following the structure of the Advisory Opinion, we will begin our examination of the effects of merger with the analysis contained in the Advisory Opinion.

The Advisory Opinion notes that the Guidelines require the calculation of changes that occur in the Herfindahl-Hirschman Index (HHI), a measure of concentration in local markets, because of the proposed transaction. The Advisory Opinion notes that "the relevance of the calculation is, however, highly dependent upon the structure of the industry, how rapidly it is changing, and the theory of competitive effects."[40]

For this transaction, the Advisory Opinion notes that "SBC has a relatively minor presence in the relevant markets for both mass market (facilities-based) long distance and enterprise services, AT&T dominates neither of those highly competitive industries, and entry barriers there are relatively minor. Similarly, AT&T has a nominal share of the relevant market(s) for facilities-based local

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[39] See, e.g., *Moore v Panish* (1982) 32 Cal.3d 535, 544 ("Attorney General opinions are generally accorded great weight"); *Farron v. City and County of San Francisco*, (1989) 216 Cal.App.3d 1071.

[40] Advisory Opinion, pp. 16.

exchange services, and its absence will have inconsequential effects on price and output levels."[41] Thus, the Advisory Opinion concludes, "the applicants' market share in all of the relevant markets need not be precisely determined."[42]

5.1. Mass Market Local Exchange

The Advisory Opinion, following standard anti-trust analysis, finds that there is a relevant market for residential and small business (mass market) local exchange services and begins its analysis with this market.

5.1.1. Advisory Opinion finds merger "will not have adverse effects upon competition in local markets"

The Advisory Opinion concludes that because concentration levels in local exchange markets will be affected only marginally by the incorporation into SBC of AT&T facilities-based services, the merger will not have adverse effects upon competition in those local markets in which AT&T does not offer special access service to private line customers.[43]

The Advisory Opinion elects to follow the analytical framework set out in the *WorldCom/MCI* case by the FCC. In that case, the FCC excluded competitively-supplied inputs and focused on the commercial level at which critical supply constraints could be assessed. Following that precedent, the Advisory Opinion notes that AT&T "resells UNE-P services to a significant

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[41] *Id.*

[42] Advisory Opinion, p. 18

[43] The Advisory Opinion addresses special access markets separately, and is discussed below.

number of California mass market customers,"[44] but notes that AT&T provides UNE-L service through its own local switches to "a relatively small number of customers."[45] The Advisory Opinion further notes that UNE-P services are "readily available" from other CLECs.[46] Therefore, the Advisory Opinion concludes that within the relevant market,[47] the merger "will not have adverse effects upon competition." [48]

5.1.2. Position of Parties

In general, the Applicants support the determinations reached in the Advisory Opinion. Concerning mass market telecommunications services, the Applicants argue that: "the protesting parties have placed form over substance, focusing their criticisms on the size of SBC and AT&T. This narrow reasoning misses the point of reasoned competition analysis."[49]

Applicants further argue that the Attorney General properly analyzed the merger and correctly concluded that, "Despite their size, the two firms generally cater to different customer segments and the extent of overlap between their facilities-based services is relatively limited."[50] Applicants cite the fact that, "this

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[44] Advisory Opinion, p. 19.

[45] *Id.*

[46] *Id.*

[47] The Advisory Opinion deems the relevant market to include "facilities-based UNE-L and cable suppliers, but not resellers at the competitive retail level." *Id.*

[48] Advisory Opinion, p. 18.

[49] Joint Brief of Applicants SBC Communications and AT&T Corp., at 48

[50] Joint Brief of Applicants SBC Communications and AT&T Corp., at 48-49; Advisory Opinion, p. 3

transaction will not remove an active competitor from any market segment, and because of AT&T's position in the market, it does not impose a price constraining force on SBC." [51]

The Applicants also support the Advisory Opinion in its finding that the "the retail services provided by SBC are readily available and that the relevant market is limited to facilities-based long distance services, and that the merger will have minimal effects on concentration levels."[52] The Applicants note that "although AT&T continues to serve its existing customers, it has stopped competing for mass market wireline customers. Thus, AT&T is not an active competitor, does not constitute a price constraining force, and its removal from the mass market will not have an adverse impact on the competitive environment."[53]

The Applicants also argue that intermodal competition further mitigates any competitive concern by ensuring the market will remain competitive. In particular, the Applicants state that "The combined organization will be one entity among many engaged in enhanced competition, which will occur not only because of the *number* of competitors, but also because of the diversity of competitors and their approaches."[54] With intermodal competition, applicants continue: "there is virtually no customer without a wide variety of choices, and this merger will not change those market dynamics."[55]

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[51] Joint Brief of Applicants SBC Communications and AT&T Corp., at 49

[52] Joint Brief of Applicants SBC Communications and AT&T Corp., at 50; Advisory Opinion, p. 19

[53] Joint Brief of Applicants SBC Communications and AT&T Corp., at 51.

[54] Joint Application of SBC Communications Inc. and AT&T Corp., at 26-27.

[55] Id.

TURN argues against acceptance of the Advisory Opinion, claiming that it "very seriously misunderstands the nature and likely result of the proposed SBC / ATT merger"[56] stating that it "suspects that the AG [Attorney General] did not examine and does not understand [TURN's] evidence."[57]

TURN's evidence focuses on the calculation of the HHI. TURN argues that application of the Guidelines framework to the evidence in the proceeding suggests unacceptable increases in the HHI and faults the Advisory Opinion for its failure to conduct such an analysis.[58] This, in TURN's view, indicates that the proposed merger would lead to unacceptable increases in market concentration that would likely increase Applicants' ability to exercise market power in most retail markets in California.[59]

In addition, TURN argues that Applicants' claims concerning intermodal competition are wrong, and that intermodal competition will not offer a viable competitive alternative to basic telephone services. In particular, TURN argues that the Applicants misled the Commission by implying that SBC's wireline losses are significant and that they are attributable to intermodal competition.[60]

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[56] TURN Opening Brief, p. 61.

[57] TURN Opening Brief, p. 62.

[58] TURN Opening Brief, p. 63.

[59] See TURN Opening Brief, p. 41.

[60] TURN, Opening Brief, p. 56.

In summary, TURN argues that the proposed merger will have adverse effects on local telecommunications markets and therefore the proposed merger is not in the public interest.[61]

ORA argues that the transaction will have an adverse impact on mass-market customers.[62] ORA presents an HHI analysis that allegedly shows that the transaction will have serious anti-competitive impacts.[63] ORA further argues that intermodal competition is "speculative." It proposes a series of measures to maintain competitive choices, including requirements that SBC offer DSL line sharing at TELRIC-based UNE rate and that SBC offer "stand-alone" DSL.[64]

Concerning VoIP competition over DSL, ORA supports Qwest's proposal that the merged entity be required to offer "stand-alone DSL on reasonable basis."[65]

Telscape argues for what it calls a very modest condition that, "SBC-CA offer a basic two-wire residential loop product at a reduced wholesale price that will enable facilities-based CLECs to compete on a level playing field with SBC-CA"[66] In particular, Telscape proposes that as a condition of the merger, SBC-CA must offer UNE-L at a price at least 50% below the TELRIC rate.

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[61] TURN, Opening Brief, p. 20.

[62] ORA, Opening Brief, p. 26.

[63] ORA, Opening Brief, p. 25.

[64] ORA, Opening Brief, pp. 54-55.

[65] ORA, Opening Brief, p. 95.

[66] Telescape, Opening Brief, p. 2.

CALTEL argues for mitigation of significant harmful effects that it claims will arise from the merger.[67] In particular, CALTEL recommends adoption of two general conditions:

- The Commission should implement a price cap plan for SBC's wholesale network elements.
- The Commission should require SBC to provide fair interconnection prices, terms and conditions for IP facilities and capabilities.[68]

Level 3 proposes one merger condition concerning mass market issues.[69] Level 3 argues that, "if an ILEC offers DSL service but requires customers of that service also to buy its traditional local phone service or its VoIP service, then those customer are effectively precluded from using competitive VoIP providers, unless they want to pay twice for voice service. Such a practice of tying together the service offerings is anti-competitive and should not be allowed."[70]

Qwest argues that the proposed merger should not be approved unless the Applicants provide "stand-alone" DSL service. In particular, Qwest notes that the Applicants trumpet the virtues and the importance of IP-based telephony as a competitive force that justifies approval of the merger. Qwest argues that,

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[67] CALTEL, Opening Brief, p. 1.

[68] CALTEL, Opening Brief, p. 5. We discuss CALTEL's recommendation concerning special access below.

[69] Level 3, Opening Brief, p. 19. Level 3 proposes several special access competitive conditions and several general mitigating conditions. They will be discussed separately.

[70] Level 3, Opening Brief, p. 20.

"Without standalone DSL, likely the only provider to succeed and put pressure on SBC's wireline business will be SBC itself."[71]

The Community Technology Foundation of California (CTFC) argues that, "Although Applicants repeatedly refer to the $14.95 introductory offer for SBC's DSL service, the evidence is that the $14.95 rate is only good for new customers for one year, and only for those customers who also sign up for SBC local voice service. For those residential customers who rely on SBC DSL, this means that VoIP is not a substitute for wireline telephone service but in addition to wireline telephone service." [72]

5.1.3. Discussion

We find no reasonable basis upon which to reject the Attorney General's Advisory Opinion. Further, we concur with the Attorney General's principal conclusion that the proposed transaction will have little effect in the local exchange market. In particular, we find the Advisory Opinion's focus on facilities-based competition in local markets appropriate and consistent with the approaches commonly used to review transactions such as this. As the Advisory Opinion notes, "AT&T provides 'UNE-L' service through its own local switches to a relatively small number of customers,"[73] thus, the transaction does not adversely affect competition in the local service mass market.

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[71] Qwest, Opening Brief, p. 41.

[72] CTCF, Opening Brief, p. 11-12.

[73] Advisory Opinion, p. 17

In addition, AT&T has elected to exit the local market, and thus it no longer provides price constraining competition to SBC. Speculation that AT&T may return to this market is unconvincing.

Similarly, we agree with the Advisory Opinion that HHI analysis does not provide relevant insight into the dynamics of this market, and is not needed to perform a competitive analysis. Indeed, since the Advisory Opinion finds that the relevant local market is that of facilities-based service providers to mass market customers, and since AT&T provides UNE-L facilities-based services in local mass markets to a "relatively small number of customers,"[74] and has no plans to offer service to local mass market customers, facilities-based or otherwise, in the future, then the acquisition of AT&T will produce no significant increase in the HHI for this market.

As a result, TURN's criticism of the Advisory Opinion is particularly misguided. TURN's calculation of dramatic increases in the HHI arise from its definition of the local market to include "resold" or "UNE-P" services. TURN fails to recognize that the Advisory Opinion clearly links its restriction of the market to "facilities-based local services" to traditional competitive analysis that looks at whether a merged entity can manipulate the supply of the service, as well as to recent precedents used by the FCC in examining telecommunications markets that focus on facilities-based competition (which TURN argues do not apply). In addition, we also note that the FCC's competition policy supports just this type of facilities-based approach to competition, for it has recently eliminated UNE-P as a competitive entry mechanism in the TRRO decision and will phase out all

[74] Advisory Opinion, p. 17.

pricing at UNE-P levels. Thus, in this regulatory environment, it would make little sense to include UNE-P resold service in any analysis of market shares, particularly on a forward going basis.

Rather than acknowledge this fundamental disagreement, TURN simply claims that "the AG advisory opinion does not appear to reflect a balanced review of all of the evidentiary record developed prior to July 22, 2005 in the California and Federal Communications Commission ("FCC") proceedings"[75] and claims that the evidence that it offered "is essentially ignored in the advisory opinion."[76]

Most important, TURN's argument does not diminish the relevancy of the Advisory Opinion's straightforward analysis: If AT&T is providing no significant telecommunications services in a market except through the limited resale of SBC services through UNE-P, which the FCC is in the process of eliminating, then consolidation with SBC should not affect the supply of telecommunications service to the market in any way. Without an increase in the ability to restrict supply of telecommunication services in a market, the merged firm does not have an increase in market power.

Furthermore, we find that intermodal competition will continue to provide a check on future anticompetitive outcomes in the local exchange market, but for this to remain a viable check in a highly dynamic and converging industry, consumers must have unfettered access to competitive VoIP services.

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[75] TURN Opening Brief, p. 105.

[76] TURN Opening Brief, p. 106.

Applicants state that the transaction will "result in increased innovation, lead to more rapid introduction of new services and prompt the development of services that would not otherwise exist."[77] Applicants also state that, "the combined organization will be capable of delivering the advanced network technologies necessary to offer integrated, innovative, high-quality and competitively priced communications and information services to meet the evolving needs of customers worldwide."[78]

Applicants further state that "Competition from CLECs, wireless, and IP-based and broadband services is creating a new era fueling growth in innovative, lower cost services to business and consumers while traditional wireline offering steadily decline."[79] We note that industry consolidation and convergence have fundamentally changed the playing field and the nature of competition for wireline carriers. Applicants draw attention to the fact that "intermodal competition also comes from other sources such as pure-play VoIP services from providers like Vonage, Packet8 and Skype," and that "these pure-play VoIP providers, along with other VoIP offerings, exert competitive pressure on traditional telephone services, and will continue to erode wireline market share."[80]

Therefore, we agree with CTFC, Qwest, ORA and Level 3 that customers' access to competitors' VoIP over SBC's DSL service is crucial to

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[77] Joint Application of SBC Communications Inc. and AT&T Corp., at 2

[78] Joint Application of SBC Communications Inc. and AT&T Corp., at 4

[79] Joint Brief of Applicants SBC Communications and AT&T Corp., at 53-54

[80] Joint Brief of Applicants SBC Communications and AT&T Corp., at 55-56

protect consumer choice and maintain competitive pressure on traditional telephone service as the industry consolidates, technology converges, and intermodal competition increases.

Ensuring access to advanced services, including competitive VoIP providers, over DSL broadband is also critical to this Commission's obligation to promote access to broadband and advance telecommunications services, lower prices, and broader consumer choice pursuant to Public Utilities Code §709. As Level 3 stated: "By tying together DSL service with its voice services, whether traditional local exchange service or VoIP, an ILEC discourages consumers from using VoIP competitors."[81]

Public Utilities Code §709 states that it is the policy of the State of California to assure the continued affordability and widespread availability of high-quality telecommunications services to all Californians; To encourage the development and deployment of new technologies; To assist in bridging the "digital divide" by encouraging expanded access to state-of-the-art technologies for rural, inner-city, low-income, and disabled Californians; To promote lower prices, broader consumer choice, and avoidance of anticompetitive conduct; To remove the barriers to open and competitive markets and promote fair product and price competition in a way that encourages greater efficiency, lower prices, and more consumer choice.

Thus, we believe this Commission has a compelling statutory interest in fostering intermodal competition in the local voice telephony market, as well as fostering access to advanced telecommunications services, such as VoIP. To the

[81] Level 3 , Opening Brief, p. 21.

extent SBC forces consumers to separately purchase its traditional local phone service in order to obtain DSL, such a policy frustrates intermodal competition and access to advanced services, and undermines the benefits to consumers that would occur as a result of this transaction.

Intervenors' recommendation that SBC be precluded from bundling its own VoIP product with its DSL Internet service if it chooses to do so, however, has no reasonable basis. National telecommunications policy is clear that, in order to encourage investment in and development of emerging technologies, such as VoIP, these technologies should remain free from unnecessary regulation. The FCC has also occupied the field of regulation in this area, stating that, due to the inherently interstate nature of IP-telephony, VoIP services are under the exclusive jurisdiction of the FCC. Additionally, integrating and bundling advanced services offers benefits to consumers by reducing costs, fostering innovation and lowering prices.

Therefore, as long as there is no evidence that SBC is using market power to limit consumers' access to competitive VoIP providers or other lawful content using SBC's DSL broadband service, there is no compelling reason to place conditions on SBC's ability to bundle its own VoIP product with other advanced services over DSL.

Therefore we will order that as a condition of approving this transaction, no later than February 28, 2006 SBC shall cease and desist from forcing customers to separately purchase traditional local phone services as a condition of purchasing SBC's DSL service. We will further order that no later than February 28, 2006 SBC shall submit an affidavit evidencing compliance with this condition of the merger.

In summary, consistent with the Attorney General's Advisory Opinion finding that the proposed transaction will not have adverse impacts on competition in local markets, we reject the recommendations of parties to deny the proposed transaction as anticompetitive. Moreover, with the exception of the requirement that SBC cease forcing customers to separately purchase traditional local phone service as a condition of obtaining DSL, which we believe is critical to SBC's own argument that intermodal competition is a significant check on an anti-competitive outcome, we adopt none of the restrictions and / or mitigation measures proposed that concern mass-market services.

5.2. Mass Market Long Distance

The Advisory Opinion then turns to an analysis of the competitive effects on the market for long distance telecommunications services sold to residential and small business customers.

5.2.1. Advisory Opinion finds long distance services "readily available" and that merger will "have minimal effects on concentration."

The Advisory Opinion concludes that the merger will have "minimal effects on concentration levels"[82] on mass market long distance services.

The Advisory Opinion follows the reasoning of the mass market local market analysis, but here the situation is exactly reversed. "AT&T is a facilities-based provider of long distance services, while SBC offers long distance services through resale operations."[83] The Advisory Opinion applies the *WorldCom/MCI* reasoning to this transaction, and finds that the retail services offered by SBC in

[82] Advisory Opinion, p. 18

[83] *Id.*

this market are "readily available." The Advisory Opinion further concludes "that the relevant market is limited to facilities-based long distance services, and that the merger will have minimal effects on concentration levels."[84]

The Advisory Opinion also notes that the "FCC has repeatedly determined that competition among long distance suppliers is both substantial and national in scope."[85] The Advisory Opinion explicitly rejects the claims that "there are California "submarkets" for long distance services."[86]

In addition the Advisory Opinion notes that it appears that SBC "has no in-region or out-of-region long distance facilities of its own."[87] Moreover, "SBC competes at the retail level with many alternative suppliers."[88]

5.2.2. Position of Parties

The Applicants support the analysis of the Advisory Opinion on this matter. Applicants cite page 3 of the Attorney General Opinion that "During the past ten years, elimination of entry barriers has facilitated widespread competition for long distance and other traditional products."[89]

In general, parties to this proceeding did not address the mass market for long distance services separately from that of mass market local exchange services. In an argument related to this issue, TURN argues that "the Applicants

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[84] *Id.*

[85] Advisory Opinion, p. 18

[86] Advisory Opinion, p. 19.

[87] *Id.*

[88] *Id.*

[89] Joint Applicants Opening Brief, p. 49

have plainly failed to demonstrate that the proposed merger will not result in a significant increase in market concentration or harm competition in this market."[90] It is, however, difficult to find an analysis by TURN on point because it objects to the market definitions in the Advisory Opinion and does not specifically address the long distance market. Additionally, "TURN acknowledges that the market for 'all other residential services' is more competitive than the market for primary network access connections."[91]

5.2.3. Discussion

We find no reasonable basis upon which to reject the Attorney General's Advisory Opinion that concludes that the merger will have "minimal effects on concentration levels"[92] on mass market long distance services.

Once again, we find the Advisory Opinion's focus on facilities-based competition in local markets appropriate and consistent with the approaches commonly used to review transactions such as this. As the Advisory Opinion notes, SBC does not have significant long distance facilities (if any) and its provision of long distance service does not affect industry output, and that therefore the transaction does not adversely affect competition in the mass market for long distance services.

In addition, AT&T has also elected to exit this market, and thus it no longer provides price constraining competition to SBC. Speculation that AT&T may return to this market is unconvincing. Moreover, this telecommunications

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[90] TURN, Opening Brief, p. 86.

[91] TURN, Opening Brief, p. 85.

[92] Advisory Opinion, p. 19

market sector has been open to competition for the longest time, and the change in market structure brought about by this merger is not significant.

In summary, we find much evidence in the record supporting the conclusion of the Advisory Opinion that this merger will have "minimal effects" on concentration levels in this market, and no evidence that supports a finding that the merger will have an anticompetitive outcome in this market. We find that by a preponderance of the evidence, the Applicants have show that the merger will have no anti-competitive effects in the mass market for long distance telecommunications services.

5.3. Enterprise Services

Following the FCC, the Advisory Opinion recognizes a separate market for large businesses and government users, which the FCC calls the enterprise market. The Advisory Opinion analyzes this market segment next.

5.3.1. Advisory Opinion finds merger tentatively concludes that "merger will not cause undue increases in concentration levels."

Concerning the market for enterprise services, the Advisory Opinion tentatively concludes that the proposed merger of SBC and AT&T "will not cause undue increases in concentration levels."[93]

The Advisory Opinion broadly defines the relevant product for enterprise customers "to include the full array of highly differentiated advanced

[93] Advisory Opinion, p. 21.

information services that large businesses and government users demand"[94] and finds that the "relevant geographic market is the United States."[95]

The Advisory Opinion notes that the Applicants:

> … have focused on different sectors of this $99 billion market. AT&T is a leading supplier to national customers that require long distance and complex or merged services. SBC is a regional provider of local voice and traditional data services.[96]

The Advisory Opinion concludes that "Although we lack detailed data, it appears that the industry is relatively unconcentrated."[97] The Advisory Opinion provides additional support for its conclusion based on multiple FCC determinations. The Advisory Opinion states that "the FCC found in 1990 that the enhanced services market was 'extremely competitive.'[98] Subsequent entry by the BOCs, cable companies, and other well-financed firms further increased market competitiveness."[99] Based on these considerations, the Advisory Opinion concludes tentatively that "the merger will not cause undue increases in concentration levels."[100]

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[94] Advisory Opinion, p. 20,

[95] *Id.*

[96] Advisory Opinion, p. 21, footnotes omitted.

[97] Advisory Opinion, p. 17.

[98] Advisory Opinion, p. 21, footnote omitted.

[99] *Id.*

[100] *Id.*

The Advisory Opinion also finds that it is unlikely that the merger would "facilitate collusion."[101] The Advisory Opinion finds that:

> "Coordination would, in fact, be difficult because the services offered by industry suppliers are heterogeneous, and customers 'often obtain competitive prices through request for proposals from carriers.'. As in *Baker Hughes*, the 'sophistication' of these large business customers is also 'likely to promote competition.' In any event, this merger is particularly unlikely to enhance the possibility of coordinated conduct because the applicants now operate in entirely different product and geographic sectors of the market.[102]

5.3.2. Position of Parties

In general, the Applicants support the findings of the Advisory Opinion and provide additional arguments in support of their view that the merger will not have anti-competitive effects in the enterprise market.

The Applicants argue that the "SBC's services and those offered by AT&T are complementary, rather than overlapping. SBC and AT&T typically sell different services to enterprises and typically succeed with different types of business customers."[103] They further argue that the market is filled with "not only the traditional set of transport-oriented carriers (IXCs, RBOCs, and CLECs), but also newer entrants with alternative networks originally conceived to carry Internet traffic and cable-based video services; systems integrators combining the ability to provide managed services with expertise in putting together networks optimized to meet customer needs; and telephone and other communications

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[101] *Id.*

[102] Advisory Opinion, p22, footnotes omitted

[103] Joint Applicants Opening Brief, p. 52

equipment vendors and resellers offering products that in many cases are displacing traditional equipment and services."[104]

The Applicants also state that "The effects of intermodal competition extend to all market segments. As Dr. Aron described, intermodal competition is not just occurring in the mass market, but in the business segments as well. For example, businesses have begun to deploy IP-based private branch exchanges (IP-PBX) and IP-Centrex systems. In 2004, Ford, Boeing and Bank of America announced rollouts of IP phone systems, and studies indicate that other businesses are following suit."[105]

ORA argues that the merger will have anti-competitive consequences for enterprise markets. ORA states that "SBC made a 'rational business decision' to acquire AT&T rather than pursuing a 'de novo' strategy. The result of this decision however, is to reduce competition. By withdrawing from facilities-based competition and pursuing an acquisition, SBC has reduced competitive pressure on the market.[106]

TURN states that "it appears that SBC can more than 'hold its own' when competing in the enterprise market absent the proposed merger."[107] Moreover, TURN contends that SBC and AT&T are today competing directly. TURN disputes applicants' claim that they can list lots of other possible competitors claiming that such a list "is meaningless absent hard data that any of

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[104] Joint Applicants Opening Brief, p. 53.

[105] Joint Applicants Opening Brief, p. 56.

[106] ORA, Opening Brief, p. 54.

[107] TURN, Opening Brief, p. 93.

those competitors are able to capture any significant portion of the market now or, more importantly, will be able to do so in the future once the top existing competitors are allowed to merge"[108]

5.3.3. Discussion

We reach the conclusion that the merger will not adversely affect competition in this sector.

The enterprise market has been recognized by the FCC as highly competitive for some time, and evidence in this proceeding demonstrates that it remains unconcentrated. Although the Advisory Opinion stated that additional data would be required to conduct a detailed analysis of post-merger competition in the enterprise market, the Attorney General tentatively concluded that this merger will not adversely affect competition in this sector. We find no reasonable basis upon which to reject the Attorney General's Advisory Opinion, and based upon the array of evidence in the record and multiple FCC findings concerning this market that support the Advisory Opinion's analysis, we conclude that this merger will not produce an anti-competitive outcome.

Although TURN urges us to consider more data, we conclude that the record contains sufficient evidence on which we can base a decision.

In particular, the Applicant's evidence concerning the number and range of firms and intermodal competitors is particularly extensive.[109] Further, the string of FCC decisions, ending with the TRRO decision of this year, all finding that this market is highly competitive makes it implausible that the

[108] TURN, Opening Brief, p. 94

[109] Joint Applicants, Ex. 78, pp. 59-72; Ex 79, pp. 66-73.

consideration of more data would do anything other than confirm the Advisory Opinion's conclusion. Thus, we find that SBC has demonstrated through a preponderance of the evidence that this merger will not have an anti-competitive effect in the enterprise market.

5.4. Special Access Services

The market for special access involves dedicated point-to-point facilities that are primarily high capacity (e.g. DS1 or greater) connections that can be used to connect an end user to an IXC s point of presence, to connect two end user locations, and to connect end users to CLEC, ISP, wireless or other competitive networks. The Advisory Opinion finds that there is a separate relevant market for the various special access services sold by the Applicants.[110]

5.4.1. Advisory Opinion finds "potential entry here should be sufficient … to counteract any potential anticompetitive effects."

The Advisory Opinion states that the "merger may enable SBC to raise the average rates paid for DS1 and DS3 private network services."[111]

The Advisory Opinion starts with a review of recent history of activity by BOCs and CLECS. While BOCs' revenues have increased 16% over an eight-year period, CLECs' revenues have increased 67% oven an eight-year period. The Advisory Opinion notes that "Internal expansion by existing firms and widespread entry by a variety of CLECs have combined to meet the rapidly growing demand for special access services. With CLEC entry, the number of MSAs for which full (Phase 2) pricing flexibility was granted on channel

[110] Advisory Opinion, pps. 14-15.

[111] Advisory Opinion, p. 23

terminations increased from none in early 2000 to 81 by November 2002. Despite this growth, special access prices remained almost constant between 1998 and 2001 on a per circuit basis."[112]

The Advisory Opinion finds that "Markets for special access services appear to be competitive for those customers requiring aggregate bandwidth in excess of two DS3 capacity or employing special access to make connections to long distance lines or MTSOs."[113] The Advisory Opinion continues its analysis by stating that "The merger may increase special access rates for DS1 and DS3 private network users if a substantial percentage of customers have dispersed facilities and alternative suppliers are not available to all customers in the relevant market. Presumably, SBC charges a higher rate at locations where entry barriers could not be overcome by alternative suppliers, and the merger will increase the number of these less competitive locations. Assuming that SBC offers discounted service to multi-location customers who meet certain revenue or circuit-based volume commitments, the elimination of competition at locations where AT&T is now the only alternative supplier may raise the average service rate paid by all customers."[114]

The Advisory Opinion and the FCC use the same relevant geographic market for assessing these effects which for special access is the MSA level. The Advisory Opinion lists that SBC's share of statewide private line DS1 and DS3 wholesale revenues is 63.9% and 54.5% respectively. AT&T's corresponding

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[112] Advisory Opinion, pp. 23-24.

[113] Advisory Opinion, p. 25.

[114] Advisory Opinion, pp. 25-26

shares are 5.5% and 8.6% respectively. These figures support the Advisory Opinion's belief that the merger may enhance SBC's market power.

The Advisory Opinion does go on to say that "Significant entry and widespread expansion by existing suppliers suggests, however, that alternative providers responding to nontransitory price increases could eventually supplant SBC at facilities previously served by AT&T."[115]

In conclusion, the Advisory Opinion recommends that:

> To mitigate any adverse effects, we recommend that the Commission freeze for one year rates paid by current AT&T customers receiving DS1 or DS3 private network service. During that transition period, alternative suppliers can extend their networks to meet demand from existing customers that might otherwise be subject to a rate increase. At the same time, the relatively brief span of the transition period would minimize the distortions and disincentives resulting from the rate freeze.[116]

5.4.2. Position of Parties

Applicants oppose the conditions suggested by Qwest, Level 3 and to a lesser extent the Attorney General. Applicants claim that "Qwest and Level 3's proposed special access conditions related largely to interstate special access services that are beyond the Commission's jurisdiction, and are not designed to address any intrastate anticompetitive effects of the merger. Although the Attorney General's proposed condition is more limited, that condition should also be rejected because, contrary to the Attorney General's conclusion, AT&T does not actively compete with wholesale access providers. As a result, the

[115] Advisory Opinion, p. 26

[116] Advisory Opinion, p. 27

merger will not significantly change the level of competition that exists in the marketplace today."[117]

The Applicants take issue with the proposed conditions from Qwest and Level 3 that generally seek to secure low rates (customers should be able to receive the lowest rates offered by either SBC or AT&T and / or should be able to receive the same rates, terms and conditions that the post-merger SBC obtains from ILECs out-of-region), to provide for anti-discrimination (post-merger SBC should be prohibited from offering rates to AT&T or Verizon / MCI that have better terms than offered to others), and to be given a "fresh look" of its current contracts. The Applicants claim that there are three reasons to reject these proposals. "First, these proposed conditions involve *interstate* special [access] services that are not within the jurisdiction of this Commission. Second, none of the complaints raised by Qwest and Level 3 is specific to California. Thus, they bear no relation to the "adverse consequences" of a change of control under California law. Third, a series of FCC proceedings will address special access services and competitive issues, including pricing, provisioning and discrimination, and market power at the wholesale level. These proceedings encompass the issues raised by Qwest and Level 3, which are general complaints related to special access rather than complaints specifically-related to this merger.[118]

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[117] Joint Applicants Opening Brief, p. 81.

[118] Joint Applicants Opening Brief, p. 82

ORA states that "Despite SBC's. . . overwhelming dominance of the special access market. . . , AT&T has up to now been one of the strongest—if not the strongest—competitor to SBC."[119]

ORA goes on to say that "AT&T's departure from the special access market—and the absorption of its fiber optic "last mile" facilities into the SBC asset base—will serve to further cement SBC's all-but-monopoly control over these essential services and facilities."[120]

ORA endorses the one-year moratorium on rates paid by current DS1 and DS3 private line customers.

Qwest and Level 3 believe that AT&T provides pricing discipline to keep SBC's special access rates in check. Qwest and Level 3 also believe that AT&T affects the competitive balance by reselling special access. A loss of AT&T from the market will remove pricing discipline and a provider of resold service. To mitigate these concerns, Qwest and Level 3 seek the following conditions:

- Require SBC to offer all customers intrastate and interstate special access at the lowest rates currently offered by either SBC or AT&T
- Prohibit SBC from giving AT&T or Verizon / MCI better special access terms and conditions than those offered to others.
- Require SBC to offer competitors in California any services or facilities that the post-merger entity purchases from other ILECs out-of-region at the same rates, terms and conditions the post-merger entity obtains from ILECs out-of-region.

[119] ORA Opening Brief, p. 56

[120] ORA Opening Brief, p. 57

- Require SBC to give its wholesale customers a "fresh look" right to terminate their contracts without incurring termination liability.
- Require a "fresh look" at termination rights, and require public disclosure of all special access contracts between SBC and AT&T and its affiliates and to permit competitors to accept individual terms from these agreements without being required to accept all the terms.

5.4.3. Discussion

We find no reasonable basis upon which to reject the Attorney General's conclusion that the merger may increase special access rates for DS1 and DS3 private network users, but that potential entry should be sufficient to counteract any anti-competitive outcomes.

A review of the Advisory Opinion's analysis of this issue shows that it is meticulous. The Advisory Opinion examined the competitive data at the level of specific buildings in those areas where facilities overlap. In addition to examining the presence of competitors at a very granular level, it also examined the locations of customers and fiber routes, concluding that the ability to construct fiber laterals make potential entry a real competitive threat. The level of granularity conducted by the Attorney General in this analysis is more extensive than any such analysis in a merger proceeding reviewed by this Commission in the past 10 years.

In contrast to the detailed and convincing review and sound analysis conducted by the Attorney General, the intervenors failed to engage this issue and analysis on a substantive level. We find no merit to the arguments of ORA, Level 3 and Qwest concerning special access, and no rational basis for adopting the conditions that they propose. As a result, there is no rational basis to reject the Advisory Opinion's recommendation to have a one-year freeze on rates paid

by current AT&T customers receiving DS1 or DS3 private network service. With this condition, we find that any adverse effect of the merger on special access is sufficiently mitigated.

5.5. Internet Backbone

The Advisory Opinion concludes that a relevant market for Internet backbone services can be defined.[121] Following the sequence in the Advisory Opinion, we next address the effects of this transaction on this market.

5.5.1. Advisory Opinion finds markets "are unconcentrated and will remain so after completion of the merger."

The Advisory Opinion notes that several parties to this proceeding have challenged "the integration of SBC's Internet access services into AT&T's Internet backbone, without alleging specific competitive effects in markets for either of those services."[122] The Advisory Opinion, however, finds that "both of those markets are unconcentrated and will remain so after the completion of the merger."[123]

The Advisory Opinion states that the Internet combines three types of participants: end users, Internet Service providers (ISPs) and Internet backbone providers (IBPs). It notes that SBC is a vertically-integrated ISP that also provides Internet backbone services, while AT&T is a major supplier of Internet

[121] Advisory Opinion, pps. 14-15.

[122] Advisory Opinion, p. 27.

[123] *Id.*

backbone services, and has about 1.2 million customers for its WorldNet and DSL services.[124]

The Advisory Opinion finds that the market for ISP services is "highly unconcentrated"[125] The Advisory Opinion also finds that the "backbone market will remain 'competitive' following the completion of this merger" which is consistent with the FCC's relevant market findings.[126] The Advisory Opinion also notes that the FCC has "exclusive jurisdiction over Internet backbone services."[127]

The Advisory Opinion discusses the contention of intervenors, specifically Pac-West and ORA, that combining SBC with AT&T, a Tier 1 peering provider would raise entry barriers or induce degraded services. The Advisory Opinion finds these scenarios "unlikely".[128] The Advisory Opinion finds even the "hypothesized motivation for the surviving firm to predatorily degrade rivals' ISP service" to be "unclear."[129]

5.5.2. Position of Parties

The Applicants support the conclusion of the Advisory Opinion that the transaction will not adversely affect Internet backbone services. The Applicants state that:

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[124] *Id. Footnotes omitted*

[125] Advisory Opinion, p. 28.

[126] *Id.*

[127] Advisory Opinion, p. 27

[128] Advisory Opinion, pp. 29.

[129] Advisory Opinion, pp. 28-29.

> To begin with, this market segment is even less concentrated today than when the FCC approved the divestiture of MCI's Internet backbone facilities to the merging owners of the two top backbone providers, finding that Internet services were 'competitive, accessible, and devoid of entry barriers.
>
> The merger will not change the number of "Tier 1" Internet providers in the 'highly unconcentrated' Internet backbone market segment. . .[130]

CALTEL and Cox seek a condition against de-peering. They argue that SBC should not be allowed to de-peer other Internet providers with whom SBC exchanges IP traffic presently. They recommend that SBC be required to honor all existing Internet peering arrangements and to offer extensions . . . for an additional five years at existing terms, conditions and prices.

5.5.3. Discussion

We find no reasonable basis upon which to reject the Attorney General's Advisory Opinion that concludes that the Internet backbone and ISP markets are highly unconcentrated and will remain so after the merger. Thus, we conclude that this transaction will not adversely affect the market for Internet Backbone services or Internet Services Providers.

The scenarios painted by Intevenors concerning possible discriminatory treatment and anticompetitive pricing have no basis in fact. Indeed, in light of the Advisory Opinion's clear indication that both the Internet Service Provider market and the Internet backbone market are unconcentrated and will remain so after the merger, we reach the same result as the Advisory Opinion – the proposed merger will not produce anticompetitive outcomes in this area.

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[130] Joint Applicants Opening Brief, pp. 66-67.

6. Do the Proposed Transactions Meet the Public Interest Tests Contained in § 854(c)?

As noted above, we have elected to conduct a review using the § 854(c) to guide our determination of whether this transaction is in the public interest. The § 854(c) criteria cause us to ask whether this transaction:

> Maintains or improves the financial condition of the resulting public utilities doing business in California?
>
> Maintains or improves the quality of service to California ratepayers?
>
> Maintains or improves the quality of management of the resulting utility doing business in California?
>
> Is fair and reasonable to the affected utility employees?
>
> Is fair and reasonable to a majority of the utility shareholders?
>
> Is beneficial on an overall basis to state and local economies and communities in the area served by the resulting public utility? And
>
> Preserves the jurisdiction of the Commission and its capacity to effectively regulate and audit public utility operations in California?[131]

Finally, the Commission must consider the implications for competitive markets of the application as well as any environmental impacts.

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[131] As noted earlier, § 854(c)(8) enables the Commission "Provide mitigation measures to address significant adverse consequences that may result." Since this does not create a standard of review, but provides authority to impose mitigation measures, we will not address this section explicitly here. Instead, we will use the authority to propose any needed mitigation measures in conjunction with our review of criteria 1 through 7. In addition, we will also explicitly address § 854(c)(8) in section 8 (below) in conjunction with our § 854(d) analysis, which gives us the authority to consider "reasonable options" offered by other parties.

6.1. Will the Change of Control Maintain or Improve the Financial Condition of the Resulting Utilities Doing Business in California?

Section 845(c)(1) requires that we determine the effect of the proposed merger on the financial condition of the resulting utilities doing business in California.

6.1.1. Position of Parties

The Joint Applicants assert that the organization created by this merger will enjoy financial health.[132] SBC is an established communications provider with a strong balance sheet, investment grade credit and the financial, technological and managerial resources to invest in AT&T's network and systems.

Applicants state that "[t]ogether, SBC and AT&T will be poised to deliver better, innovative products and services to consumers and business customers, and to accelerate the deployment of advanced, next-generation Internet Protocol ("IP") networks and services than either company can provide on a stand alone basis."[133] Applicants also state that, "AT&T has experienced increasing financial challenges which have resulted in thousands of layoffs and created financial uncertainty for workers and shareholders. The merger creates a stronger combined company able to thrive in the telecommunications markets of the future."[134] They add that the merger will strengthen both AT&T and SBC's financial condition. "AT&T and its affiliates will benefit from SBC's stronger

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[132] Joint Applicants' Opening Brief, p. 21, Exhibit 43

[133] Joint Applicants' Application, p. 2.

[134] Joint Applicants' Opening Brief, p. 16.

balance sheet and better access to capital, while the post-merger company will achieve financial benefits through increased efficiencies, lower costs and increased revenues."[135]

Applicants also state that "before its decision to merger with SBC, AT&T was no longer a price constraining force for the mass market, and consummation of the merger therefore obviously should have no adverse effect on competition in that market. Because AT&T has ceased actively competing in the mass market, the merger will not deprive residential customers of a major player in that segment."[136]

In addition Applicants state that the increased financial strength of the combined company will support additional investments in advanced technologies. "SBC expects higher capital spending totaling approximately $2 billion over the first several years after closing than would likely have been incurred by the two companies absent the merger."[137]

ORA argues that the merger may adversely impact SBC California's financial condition[138] because "[u]nder a holding company structure, a regulated utility may be exploited by its parent and affiliates."[139] ORA raises the concern that SBC California's regulated revenues could be eroded by SBC affiliates'

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[135] Joint Applicants' Reply Brief, p. 54.

[136] Joint Applicants' Application, p. 29-30

[137] Joint Applicants' Application, p. 25.

[138] ORA, Opening Brief, p. 76.

[139] ORA, Opening Brief, p. 77.

unregulated VoIP offerings which contribute substantially to SBC California's intrastate revenues.[140]

ORA argues that the Commission should seek to ensure that a merger that may benefit SBC's holding company does not result in long-term harm to the subsidiaries providing telecommunications services in California. In particular, ORA recommends that the Commission require SBC to mitigate the possible exploitation of SBC California by other SBC affiliates.[141] Specifically, ORA recommends requiring the merged company not to cannibalize SBC California's revenues and abide by the Commission's affiliate transaction and cost allocation rules. ORA also recommends that the Commission should reiterate to SBC that it must fully cooperate in ORA's affiliate transactions audit.[142]

TURN argues that the applicants have failed to show that the proposed merger will maintain or improve the financial condition of the resulting public utility doing business in California.[143]

6.1.2. Discussion: The Merger will maintain or improve the Financial Condition of the resulting public utility

We find that this merger will maintain or improve the financial condition of the resulting public utility. We believe that the Joint Applicants have demonstrated that the merger will strengthen the post-merger company's

[140] ORA, Opening Brief, p. 62, Exhibit 12C

[141] ORA, Opening Brief, p. 94.

[142] *Id.*

[143] TURN, Opening Brief, p. 114.

financial condition, and that the benefits of this increased financial strength will accrue to all of the post-merger company's affiliates.[144]

ORA's claim that the holding company structure will lead to adverse financial consequences for the California utilities owned by SBC is not credible, given that SBC California is already a small part of a large holding company. Despite the fact that this holding company structure has been in place for some time, the Commission has seen no negative consequences for the SBC's California utility as a result. Moreover, ORA has not demonstrated any that any such consequences are even plausible. Thus, ORA's concern that this transaction will have adverse financial consequences for SBC's regulated California subsidiary is not credible and there is no reasonable basis for imposing ORA's recommended "first priority condition" on SBC.

As for TURN's claim that SBC has failed to demonstrate that the merger will produce no adverse financial consequences for SBC California, we disagree. Nothing in the record suggests that SBC California will be weakened in any way by the holding company's acquisition of AT&T. In fact, the evidence in the record leads to the opposite conclusion, that a financially healthier, merged company will expend significantly greater capital in California than the two separated companies would expend absent the merger.

Consequently, we conclude that this transaction will not have an adverse impact on SBC's California utilities and accordingly, the merger meets the standard of § 854(c)(1).

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[144] Joint Applicants Reply Brief, p. 54.

6.2. Will the Merger of the Parent Companies and the Change of Control Maintain or Improve the Quality of Service to California Ratepayers?

Section 854(c)(2) provides calls for the Commission to examine whether the transaction is likely to "maintain or improve the quality of service to public utility ratepayers" in California.

6.2.1. Position of Parties

Applicants state that, service quality will be maintained or improve as a result of the merger.[145]

While they are not able to engage in detailed planning until the transaction closes, they anticipate that the integration of AT&T's national and global IP network with SBC's in-region data network will create efficiencies that improve service quality for the combined company's IP-based services.[146] Increasing the amount of traffic that flows over a single network allows for better management of that traffic. An integrated network is easier to monitor, repair and maintain, all of which allow for better service to the customer. SBC expects that this integration process will allow the combined company to maintain or improve the quality of IP-based services of its California operating subsidiaries, for both mass market and large business customers.[147] Applicants further state that the increased financial strength and the investment that will follow the merger will support future service quality.[148] Finally, SBC cites testimonials

[145] Joint Applicants Application, p. 30.

[146] Joint Applicant's Opening Brief, p. 16.

[147] Joint Applicant's Opening Brief, p. 17

[148] *Id.*

given at the public participation hearings as supporting its view that the stronger company will be able to provide better service quality.[149]

TURN raises the concern that merger-related workforce reductions and system consolidation will increase the risk of harm to service quality in California, particularly in the short run. Service quality may affect some types of customers more than others.[150]

ORA states that, "SBC should be required to improve service quality in those areas that the Commission identified as below the industry standard and at least maintain service quality in the areas in which it exceeds or is statistically indistinguishable from the industry standard."[151]

ORA urges the Commission to adopt service quality standards that, "[w]hen customers suffer service outages that should be compensated significantly more than the pro rata share of their monthly charges" and that "[s]ervice monitoring should be expanded to include a requirement for SBC to track the deployment of new technology by wire center and to provide reports on that deployment, along with statistics about wire center demography."[152] ORA argues therefore that the Commission should hold SBC to its claims concerning service quality standards.

DRA states, "[c]onsumers with disabilities are concerned that the proposed merger will limit the quality and accessibility of the programs and

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[149] Joint Applicants' Opening Brief, p. 24-25.

[150] Murray Reply Testimony, p. 127-128.

[151] ORA Opening Brief, p. 87.

[152] ORA Opening Brief, p. 95.

services provided by the new entity".[153] DRA alleges that a shift in focus to the enterprise market "threatens service quality for people with disabilities."[154]

DRA states the merger is "not in the interests of public utility ratepayers with disabilities."[155] DRA alleges that a shift in focus to the enterprise market "threatens service quality for people with disabilities."[156]

6.2.2. Discussion: Merger Will Maintain or Improve Service Quality

We find that the merger will maintain or improve service quality. On the one hand, current operations and networks are largely complementary, with little overlap, and will continue to be operated as separate units following the merger. As a result, it is unlikely that the merger will have any impact on service quality in the short run. However, as the Applicant's experts testified, network integration over time will result in more efficient traffic handling, system maintenance and repair, all of which will tend to improve service quality.

Furthermore, in our recent NRF proceeding we found that SBC California offers generally good service. The company remains subject to our existing tariffs, general orders and other regulations that set a service quality floor and provide effective remedies when service quality falls below that floor. Nothing in the merger will alter or reduce the California subsidiaries service quality obligations.

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[153] DRA Opening Brief, p. 6.

[154] DRA Opening Brief, p. 9

[155] DRA Opening Brief, p. 2.

[156] DRA Opening Brief, p. 3

SBC has a demonstrated commitment to enabling access for persons with varying forms of disability. Nothing in the merger will reduce SBC's provision of disabled access and we are confident that over time the merger will result in improved service quality for both the general customer base and the disabled community.

Finally, there is no credible basis for ordering investigations into service quality as ORA recommends. The Commission has a comprehensive service quality program in place today, and there is no rational basis for changing it.

6.3. Will the Merger of the Parent Companies and Changes of Control Maintain or Improve the Quality of the Management of the Resulting Utility Doing Business in California?

Section 854(c)(3) calls for an examination of whether the transaction will "maintain or improve the quality of management of the resulting public utility" subsidiaries.

6.3.1. Position of Parties

Applicants state that the overall management of the combined company will be enhanced by combining the separate strengths of the two companies. Both SBC and AT&T have management teams with substantial experience in the telecommunications industry. This will not change as a result of the merger"[157]

ORA has raised issues over potential management practices relating to how resources are allocated between regulated and unregulated operations. We address that issue separately in our discussion of how the merger will affect the financial health of the combined utility and our ability to regulate effectively.

[157] Kahan Opening Testimony, p. 22.

In our review of the record in this proceeding no party directly alleged that the merger would have an adverse impact on the management of the California subsidiaries of the resulting company.

6.3.2. Discussion: Proposed Transaction Will Maintain or Improve Management Quality

We find that the new company will maintain the quality of its management. First, there is no reason to doubt the statements of the applicants that a goal of the transfer is to acquire the expertise of AT&T in the enterprise market. Moreover, the proposed transfer of control will have no immediate impact on the management of the subsidiaries offering telecommunications services within California. Second, we find no evidence in the record that the proposed transaction will have an adverse impact on management. Thus, the Applicants' statements that there will be no diminution of managerial quality stand unrebutted.

In summary, we find that the proposed transaction will maintain or improve the quality of management.

6.3.3. Will the Merger of the Parent Companies and Change of Control Be Fair and Reasonable to the Affected Employees?

Section 854(c)(4) provides for an examination as to whether the transaction will be fair and reasonable to the affected utility employees, including both union and non-union.

6.3.4. Position of Parties

The Applicants state that

(a) The merger of SBC and AT&T will create a much stronger job outlook for the combined organization.[158]

(b) A strong combined SBC and AT&T will be able to deliver the advanced networks and services required by American businesses and create more jobs in the overall economy.[159]

(c) News of the proposed merger was received well by union representatives.[160]

(d) AT&T has reduced its overall workforce from over 100,000 employees to approximately 47,000. Out of AT&T's remaining workforce, less than 5% are California employees.[161]

(e) The merger will result in a strengthened post-merger company which will provide greater opportunities for California workers.[162]

(f) The combined long term employment outlook, both nationally and in California, following the merger is better than if the two companies continued operation independently.[163]

ORA argues that the transaction will have a negative effect on employees and recommends the imposition of a merger condition limiting California job cuts to no more than 5% of total post-merger headcount

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[158] SBC / ATT Joint Application, pg. 33.

[159] *Id.*

[160] *Id.*

[161] SBC / ATT Joint Application, pg. 34.

[162] SBC / ATT Reply Brief, pg. 58.

[163] *Id.*

reductions.[164] ORA foresees the possible loss of several thousand California jobs with the associated burden on the state's economy,[165] and fears that after the merger SBC's California workforce may be re-deployed to SBC carriers in other states. [166]

TURN states that, "the Applicants refuse to provide any information to the Commission regarding how many California jobs they will be eliminating should the merger be approved".[167] TURN argues that Applicants' claim that the merger will create more jobs in the overall economy can only be considered an empty promise.[168]

6.3.5. Discussion: Changes will be Fair to Utility Employees

The changes proposed will be fair to utility employees. First, the transaction will have no direct impact on either SBC's or AT&T's California operations because they are complementary and have zero local and consumer synergies.[169] Moreover, the emergence of a stronger combined company will "allow expansion into new markets, development of new technologies, and improvement of its currently existing services," which in turn will provide

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[164] ORA Opening Brief, p. 95.

[165] ORA Opening Brief, p. 87.

[166] ORA Opening Brief, p. 88.

[167] TURN, Opening Brief, p. 115.

[168] *Id.*

[169] SBC / ATT Joint Reply Brief, p. 11.

overall benefits to the economy, resulting in more jobs and employment opportunities.[170]

ORA's calculation of massive job losses is flawed. In addition, TURN's concern that the new company will eliminate redundant positions is less a criticism of this proposed transaction than of mergers in general. Both fail to acknowledge that much of AT&T's business is in irreversible decline and that without the merger its workforce will continue to shrink. The fact that the employee unions representing SBC and AT&T workers strongly support this transaction for the very reason that "The combination will stop the hemorrhaging of jobs at AT&T"[171] belies intervenors' arguments. Intervenor's testimony fails to demonstrate that this transaction will have any adverse impact on employment.

For these reasons, we find that that the changes resulting from the merger will be fair to employees.

6.3.6. Will the Merger of the Parent Companies and Change of Control Be Fair and Reasonable to a Majority of the Utility Shareholders?

Section 854(c)(5) requires an examination of whether the transaction will be fair and reasonable to the majority of affected utility shareholders.

6.3.7. Positions of Parties

Applicants state that the merger will create an organization that will enjoy enhanced financial health and vigor[172] and increased long-term financial

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[170] SBC / ATT Joint Application, p. 33.

[171] Kahan (JAs) Ex. 44, p. 24.

[172] SBC / ATT Joint Application, p. 33.

stability.[173] The Applicants further state that the Boards of Directors of both SBC and AT&T concluded that the transaction is in the best interest of their respective shareholders.

Although TURN's protest to the merger raised questions concerning whether the offer of Qwest would be better for MCI's shareholders, TURN submitted no testimony or evidence pursuing this part of its protest.

6.3.8. Discussion: Transaction is in the Interest of Shareholders

In the Pacific Bell / SBC merger, the Commission found that the approval of boards of directors, financial advisors and shareholders meets the test of "preponderance of evidence."[174] Further, there is no evidence in the record alleging that the merger conditions, if accepted by a majority of shareholders, will not be "fair and reasonable to a majority of the utility shareholders."

Thus, we find that the proposed transaction is fair and reasonable to shareholders.

6.3.9. Will the Proposed Merger of the Parent Companies and Change of Control Be Beneficial on an Overall Basis to State and Local Economies and the Communities Served by the Resulting Utility?

Section 854(c)(6) calls for the Commission to consider whether the merger will be "beneficial on an overall basis to state and local economies, and the communities in the area served by the resulting utility."

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[173] SBC / ATT Joint Brief, p. 1.

[174] D.97-03-067, 1997 Cal. PUC LEXIS 629.

6.3.10. Position of Parties

The Applicants argue that the transaction will result in overall benefits to the State of California and all of its constituencies. The Applicants state that the transaction will promote competition and result in improved service quality and more competitive prices. The Applicants further note that during the public participation hearings held throughout the state, many customers and community groups expressed this view. Furthermore, the Applicants note that SBC has a strong tradition of community support, community service, and corporate philanthropy, which it states it "continue well into the future."[175] The Applicants state further that an agreement reached with Greenlining ("Greenling Agreement") and LIF further demonstrates the Applicants' commitment to the community. The Applicants note that under the Greenling Agreement, they will:

- Participate in the creation of a statewide Broadband Task Force
- Increase corporate philanthropy over the next 5 years by an additional $47 million above current levels, with a good faith goal of giving 60% of the new incremental dollars in California either to underserved communities or to non-profit organizations whose primary mission is to serve underserved communities, minorities and the poor.
- Make a good faith effort to increase the supplier diversity goal for minority business enterprises from 25% in 2006 to 27% in 2010.
- Continue to provide in-language services to non-English speaking customers.
- Maintain current rates for primary line basic residential service and continue to support the Commission's State and Federal Universal Service Lifeline programs to ensure the availability of affordable service to low income customers, including working to overcome language barriers that impede higher subscription rates.

[175] Joint Applicants Opening Brief, p. 22.

- Extend the California Disability Advisory Group until December 31, 2009 and expand it.

Greenlining supports the Greenling Agreement, and urges that the Greenling Agreement be considered in the Commission's determination of whether the transaction meets the public interest standard of § 854.

LIF also supports the Greenling Agreement and urges the Commission to approve it and the pending merger,[176] arguing that they "promote sound public policy and meet the § 854 benefits tests."[177] To buttress this position, LIF cites demographic evidence that it states "dictates that a significant part of § 854 benefits should be directed at low-income communities"[178] and evidence of the so-called "digital divide" that demonstrates a need for the initiatives contained in the Greenling Agreement.[179] Finally, LIF cites prior Commission decisions as precedents for adoption of the Agreement.[180]

ORA, in contrast, argues that the transaction will have a negative effect on the California economy, primarily because of anticipated job cuts resulting from the consolidation of the two companies.[181] ORA argues that the Greenling Agreement is "procedurally defective"[182] under Rule. 51.1(b) of the

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[176] Latino Issues Forum, Opening Brief, p. 1

[177] Latino Issues Forum, Opening Brief, p. _4

[178] Latino Issues Forum, Opening Brief, p. 5.

[179] Exhibit LIF 1 and Exhibit LIF 2.

[180] Latino Issues Forum, Opening Brief, 16.

[181] ORA, Opening Brief, p. 2.

[182] ORA, Reply Brief, p. 33.

Commission's Rules of Practice and Procedure because it is a settlement and the cited Rule requires settling parties to give other parties notice and an opportunity to comment on any proposed settlement"[183]

TURN argues that the Applicants have failed to meet a reasonable burden of proof that the proposed [merger] will not harm the state and local economies in California. TURN agrees with ORA that the Greenling Agreement requires a noticed conference under Rule 51.1(b) and states that the Commission should defer action on the Agreement.[184]

6.3.11. Discussion: Transaction Will Benefit Californians

We find that the transaction will benefit Californians particularly in light of the Greenling Agreement among SBC, Greenlining and LIF.

Pub. Util. Code § 709 identifies access to advanced telecommunications service as a key public policy objective185. Several parties to the proceeding identified enhanced access to high speed Internet ("broadband") and advanced telecommunications services as a primary benefit to consumers embodied in this transaction. Applicants state that the merger will "result in increased innovation,

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[183] ORA, Reply Brief, p. 33. Rule 51.1(b) says, in relevant part: "Prior to signing any stipulation or settlement, the settling parties shall convene at least one conference with notice and opportunity to participate provided to all parties for the purpose of discussing stipulations and settlements in a given proceeding."

[184] TURN, Reply Brief, p. 47.

[185] California Public Utilities Code §709 says in relevant part: "The Legislature hereby finds and declares that the policies for telecommunications in California are as follows: (c) To encourage the development and deployment of new technologies…(d) To assist in bridging the "digital divide" by encouraging expanded access to state-of-the-art technologies for rural, inner city, low income and disabled Californians."

lead to more rapid introduction of new services and prompt the development of services that would not otherwise exist." 186

Greenlining and LIF and their respective affiliates intervened in the instant Application proceeding primarily for the purpose of ensuring that underserved communities receive benefits as a result of the proposed change of control between SBC and AT&T and to ensure that the merger is not adverse to the public interest.

As described above, on September 6, 2005, Greenlining, LIF and SBC California entered into the Greenling Agreement that includes a five-year commitment by SBC California to continue to be a leader in serving underserved communities with a focus, among other things, on bridging the digital divide. As part of the Greenling Agreement, SBC California commits to more than double its charitable contributions in the categories "SBC Foundation" and "Corporate Contributions" from $6.6 million a year to $15 million a year for two years and increased to $20 million for three years thereafter following the close of SBC's merger with AT&T (for a combined total of increase of $47 million over the five year period). SBC has also agreed to a good faith goal of giving at least 60% of the new incremental dollars in charitable contributions in California over the next 5 years to underserved communities or to nonprofit organizations whose primary mission is to serve underserved communities, minorities and the poor. Specifically, SBC has committed to address issues of "digital divide" in underserved communities.

California Emerging Technology Fund (CETF)

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[186] Joint Application of SBC Communications, Inc. and AT&T Corp., at 2

As part of applicants' commitment to ensure that this transaction is beneficial on an overall basis; to enhance the Broadband Connectivity section of the Greenling Agreement, and to ensure that this transaction is consistent with statutory objectives to make advanced telecommunications services available to underserved communities, we order that applicants commit $9 million per year for 5 years in charitable contributions ($45 million total), to a non-profit corporation, the California Emerging Technology Fund (CETF), to be established by the Commission for the purpose of achieving ubiquitous access to broadband and advanced services in California, particularly in underserved communities, through the use of emerging technologies by 2010. No more than half of Applicant's total commitment of $45 million to the CETF may be counted toward satisfaction of the Greenling Agreement to increase charitable contributions by $47 million over 5 years.

The CETF will be organized under the Nonprofit Public Benefit Corporation Law for charitable and public purposes as a nonprofit public benefit corporation, and not organized for the private gain of any person or entity. The governing board of the CETF will include Commission-selected appointees, appointees selected by the applicants, and appointees jointly selected by the Commission and the applicants.

Funds dedicated to the CETF will be used to attract matching funds in like amounts from other non-profit public benefit corporations, corporate entities or government agencies. It is anticipated that initial funding provided by the applicants in this proceeding ($45 million) will be combined with funds from other sources for a total initial endowment for the CETF of $60 million over 5 years. It is further anticipated that a majority of CETF funds will be matched by

other private, non-profit, or government entities for specific projects to reach a total goal of at least $100 million in funding over 5 years.

The Articles of Incorporation, Bylaws and Charter for the CETF will be established by the governing board. The Charter will specify that the purpose of the CETF is to fund deployment of broadband facilities and advanced services to underserved communities. "Underserved communities" is defined as communities with access to no more than two broadband service providers, including satellite, or broadband adoption rates below a statewide average. Communities with below average broadband adoption rates primarily include: low-income households, ethnic minority communities, disabled citizens, seniors, small businesses and rural or high-cost geographic areas.

The CETF will form advisory groups on deployment of broadband facilities and access to critical advanced services, such as online education and telemedicine, in rural and high-cost areas. The CETF will work with these advisory groups as well as organizations and agencies such as, the California Telemedicine and eHealth Center (CTEC), the Corporation for Education Network Initiatives in California (CENIC), the California Business and Transportation Agency (BTH), the Broadband Institute of California, Greenlining Institute, and other organizations representing underserved, minority or disabled communities, to identify ways in which the CETF can coordinate and fund projects to link primary care health clinics and educational facilities in rural and high-cost areas to high-speed broadband networks, and promote economic development in underserved communities.

It is the intent of this Commission that broadband facilities funded by the CETF will be owned and operated by private corporations, non-governmental organizations (such as universities or health facilities) and / or local governments,

or some public-private partnerships involving a combination of these entities, and not owned and operated by the CETF. Any remuneration for CETF facilities transferred to other entities will be returned to the CETF fund for use in future projects.

In D. 03-12-035, the Commission established a similar fund as part of the PG&E bankruptcy reorganization plan. The California Clean Energy Fund, a non-profit public benefit corporation, was established by the Commission for the purpose of supporting research and investment in clean energy technologies in California.

DSL Expansion

Numerous commenters at the Public Participation Hearings articulated concerns that, absent conditions set by the CPUC, the merger will not benefit underserved communities in California. Commenter Pedro Amorrquin, representing a San Francisco non-profit community program stated that to ensure this transaction is not adverse to the public interest, "SBC must protect the interests of the disadvantaged with low priced Internet access and make the technology available to all communities."187 Commenter Van Lam from Fresno stated that underserved communities "want more dollars after the merger to help reduce the 'digital divide.'"188

In response to these and other concerns expressed at the Public Participation Hearings, and to ensure that this transaction is beneficial on an overall basis and meets the objectives of §709 to assist in bridging the 'digital

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187 Oakland PPH, June 14, 2005.

188 Fresno PPH, June 20, 2005.

divide,' we find that SBC should commit to continue its deployment of DSL in rural and underserved communities until at least 95% of all homes within its current footprint are provided with DSL capability. We order SBC to submit an annual report to this Commission until December 31, 2010 or as soon as this objective is reached, whichever occurs first, on the progress toward meeting this objective.

Low-Income Families, Small and Minority Businesses, Senior and Disabled Citizens

Public commenters also expressed concerns that the combined company will focus its technology investments in affluent areas, and not maintain its commitment to assist low-income communities, small and minority-owned businesses, seniors and the disabled community in the wake of the merger.

Several commenters at the PPH expressed concern that the merger will result in the underserved communities [rural, low income and ethnic], non-profit organizations and the disabled being forgotten.

- "My main concern is that the company will only deploy the newest advanced network to high-end users allowing for added advantages and opportunities to a privileged few. And that underserved rural communities will not be offered the same technological capacities."[189]

- "I am here tonight to speak about the issues facing persons with developmental disabilities and our concerns about the merger of SBC and AT&T and to urge the Commission to

[189] Fresno PPH, June 20, 2005, Tr. P. 408.

ensure that people with developmental disabilities not be left behind as a result of this merger."[190]

- "We want to make sure that any merger should result in an intense investment to underrepresented and underserved communities, particularly low-income and ethnic minority communities."[191]

- "I think it will be good if they make a foundation to fund urban kids in California to be updated with technology and stuff, because I think that decision will be -- help them in the future, because we will all grow into technology and nobody will be left behind."[192]

In response to these concerns, and to ensure that this transaction is beneficial on an overall basis to the communities served, SBC should commit to maintain its current efforts to provide technology training and assistance to underserved communities, and develop specific initiatives to enhance technology training for low-income families, seniors, disabled persons, and small, minority and rural businesses in conjunction with community-based organizations. As a condition of approval for this transaction, we order SBC to file an Advice Letter with the Commission outlining specific initiatives to address these issues no later than 30 days after the close of the merger with AT&T.

In summary, we find that SBC's commitments as described herein, in conjunction with the commitments contained in the Agreement among Greenlining, LIF and SBC California, ensure that this transaction is beneficial on

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[190] Fresno PPH, June 20, 2005, Tr. P. 611.

[191] Sacramento PPH, June 15, 2005, Tr. P. 209.

[192] Anaheim PPH, June 28, 2005, Tr. P. 673.

an overall basis to state and local economies and not adverse to the public interest.

Finally, we find little merit in the procedural and substantive objections of TURN and ORA. First, we do not deem the Greenling Agreement to be a "Settlement" governed by Rule 51. Rule 51(c) defines a "Settlement" as "an agreement…on a mutually accepted outcome to a Commission proceeding." An outcome to the proceeding would be a decision to approve or deny the application.

The Greenling Agreement constitutes little more than a common position by certain parties and their experts that offers an appropriate way to address issues of specific concern to California communities, including those issues known as the "digital divide" issues.

Moreover, as noted above, we have used our oversight to amend and augment the Greenling Agreement to specifically address issues relating to the digital divide and this Commission's obligation pursuant to §709 in the context of the merger. Thus, not only is the Greenling Agreement not a "Settlement" within the meaning of Rule 51, we have not given it the deference reserved for a Settlement. We have treated it for what it is – an agreement among parties and their experts as to the specific benefits that will accrue to underserved communities resulting from this transaction.

6.4. Will the Proposed Merger of the Parent Companies and Change of Control Preserve the Jurisdiction of the Commission and its Capacity to Effectively Regulate and Audit Public Utility Operations in California?

Section 854(c)(7) requires that the Commission consider whether the change of control preserves the jurisdiction of the Commission and its capacity "to effectively regulate and audit public utility operations in the state."[193]

6.4.1. Positions of Parties

Applicants state that because the transaction will not alter the legal status of any presently regulated California subsidiaries of SBC or AT&T, the Commission's ability to regulate those subsidiaries will not be impaired, compromised, or altered in any respect. Applicants state that all regulated subsidiaries of both companies will continue to be subject to all the terms and conditions that the Commission has previously imposed.[194] The merger will thus have no impact on either the Commission's jurisdiction or its ability to effectively regulate the combined company's public utility operations in California.

Several parties raise questions concerning the jurisdiction and capacity of the Commission to continue to regulate the California subsidiaries of SBC and AT&T following the merger. ORA states that "ORA and other parties have presented testimony showing that this transaction will diminish the authority and jurisdiction of the Commission"[195] In addition, ORA argues that the disappearance of AT&T, as a well funded pro-competitive voice, may adversely

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[193] § 854(c)(7)

[194] SBC / AT&T Joint Application, p. 39..

[195] ORA Opening Brief, p. 89.

affect this Commission's proceedings.[196] TURN argues that the Commission should impose various monitoring requirements, claims that the regulatory task of auditing will become more complex following the merger, and proposes that the Applicants fund two $1 million audits post merger.[197] TURN further argues that the merger will complicate discovery processes.[198]

6.4.2. Discussion: Transaction Will not Diminish Jurisdiction of Commission or its Capacity to Regulate and Audit Utility Operations in California.

We find that the transaction will not diminish the jurisdiction of the Commission or its capacity to regulate and audit utility operations in California. First, we note that nothing in this transaction in anyway affects the jurisdictional authority of this Commission.

Second, the allegations by TURN and ORA that the merger will decrease the Commission's regulatory capacity are in error. Monitoring the compliance of the merged company with applicable laws and regulations will certainly require no more Commission resources than monitoring the separate companies and probably will require fewer such resources because fewer separate proceedings will be initiated.

Similarly, concerning audits, TURN and ORA fail to acknowledge that as competition emerges audits play a less central role in the exercise of regulatory

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[196] ORA Opening Brief, p. 90.

[197] TURN Opening Brief, p. 130.

[198] *Id.*

oversight. For example, we note that the complex audit issues discussed in the D.04-02-063 and D.04-09-061, albeit leading to a series of regulatory adjustments, had no impact on the rates that SBC charged. Thus, even as corporate structures have become more complex, the ability of the Commission to exercise regulatory oversight has improved with regulatory structures more attuned to the competitive environment. In particular, the level of audit oversight needed to regulate companies subject to market competition is very different than that needed to review a company which uses regulatory authority to pass all incurred costs on to ratepayers who have no choice of service provider.

7. Does the Proposed Merger of the Parent Companies and Change in Control Create Environmental Issues of Concern?

The applicants state "this transaction involves the merger of a telecommunications holding company with another holding company."[199] The Commission has consistently held in the past that the indirect transfer of ownership of facilities, as is the case with this transaction, does not raise significant environmental concerns.

No party raised any environmental issues concerning the proposed financial transaction.

Pursuant to state law and Commission precedents we find this application raises no environmental issues of concern.

8. Other Issues § 854(c)(8) § 854(d)

Section 854(c)(8) states that the Commission shall "Provide mitigation measures to prevent significant adverse consequences which may result." Unlike the other sub-sections of § 854, § 854(c)(8) does not establish criteria for reviewing

[199] SBC / ATT Joint Applicant, p. 14.

the transaction, other than ordering that we provide mitigation measures to prevent "significant adverse consequences."[200]

Section 854(d) states that:

> When reviewing a merger, acquisition, or control proposal, the commission shall consider reasonable options to the proposal recommended by other parties, including no new merger, acquisition, or control, to determine whether comparable short-term and long-term economic savings can be achieved through other means while avoiding the possible adverse consequences of the proposal.[201]

Consistent with the provision of this section, we will therefore consider whether there are "reasonable options" to the merger, including modifying conditions.

8.1. Position of Parties

The Applicants argue that the "proposed conditions lack any plausible nexus to any adverse effect of the merger, as required by § 854(c)(8). In essence, the protesting parties seek improperly to use this proceeding as an open mike on issues previously litigated and a grab bag of concessions that would advance their individual interests, but bear no direct relationship to the merger or anticompetitive effects."[202]

CALTEL proposes a series of mitigation measures, including: 1) a price cap plan for SBC's wholesale network elements; 2) the imposition of a cap on SBC's intrastate special access rates for five years; and 3) a requirement that SBC

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[200] As noted previously, for §§ 854(c)(1) through (7), we have considered mitigation measures at the same time as we have assessed the transaction against the criteria.

[201] § 854(d)

[202] Joint Applicants, Opening Brief, p. 88.

provide fair interconnection prices, terms and conditions for IP facilities and capabilities. [203]

Cox cites § 854(c)(8) and argues that the Commission "is required to provide mitigation measures."[204] Cox then argues that four conditions are needed: 1) a condition allowing CLECs to opt-in to interconnection agreements that SBC has negotiated and / or interconnection agreement provisions that SBC has arbitrated in California; 2) a condition requiring SBC to transit traffic consistent with TELRIC pricing and free of burdensome and unnecessary restrictions; 3) a condition requiring SBC to offer extensions on existing IP backbone agreements; and 4) a condition requiring AT&T to offer extensions on existing transport agreements.

Level 3 asks for 1) divestiture of overlapping in-region facilities; 2) a series of conditions on special access pricing; 3) require SBC to exchange all VoIP traffic at the local compensation rate; 4) require the merged company to return unused telephone number blocks; and 5) require that Verizon offer "stand-alone" DSL.

ORA proposes an extensive set of requirements tied specifically to the various elements of § 854(b) and § 854(c). An extensive summary is provided on pages 92-96 in ORA's Opening Brief.

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[203] CALTEL, Opening Brief, p. 5.

[204] Cox, Opening Brief, p. 18

PacWest proposes a merger condition to "ensure the availability of non-discriminatory interconnection with the packet-switched network facilities of SBC."[205] The condition is:

> In the absence of a negotiated agreement acceptable to any requesting CLEC, SBC's affiliates certificated as public utilities in California shall consent to participate in arbitration proceedings conducted by this Commission pursuant to Section 252 of the Communications Act, the purpose of which shall be to establish reasonable and non-discriminatory terms and conditions of interconnection between the networks of SBC's certificated affiliates in California and the network of the requesting CLEC. This interconnection shall include all technologies and network architectures deployed by the SBC affiliates in California, including but not limited to all packet-switched network technologies. As a condition of this merger, SBC shall further waive any claims that such interconnection obligation involving all of its deployed network architectures exceeds the scope of permissible arbitration under Section 252.[206]

Qwest proposes six conditions for the merger: 1) require that the merged company divest the AT&T overlapping facilities; 2) require SBC to offer intrastate and interstate special access, private line or its equivalent at the lowest rates offered by either SBC or AT&T; 3) require that SBC will show no favoritism post-merger to new affiliates or Verizon / MCI; 4) require that SBC will offer competitors in California any services or facilities that the post-merger entity purchases from other ILECs out-of-region and at the same rates, terms, and conditions that the post-merger entity obtains from those out-of-region ILECs; 5) require that SBC give wholesale customers a "fresh look" right for customers to

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[205] PacWest, Opening Brief, p. 31.

[206] PacWest, Opening Brief, p. 31, citing PacWest Ex. 109, p. 28.

terminate their contracts without termination liability; and 6) require that SBC offer "stand-alone" DSL.[207]

Telescape asks that the Commission require SBC to sell its UNE-L facilities at a 50 percent discount.[208]

TURN's chief focus is to fight approval of the merger, and proposing conditions is a minor part of TURN's showing. In a 132-page brief, only 9 pages focus on merger conditions.[209] Nevertheless, the litany of conditions is extensive and includes:

1. A five years rate freeze for residential and small business basic exchange rates;
2. A requirement that the 1FR, 1MR, 1MB, and local measured usage and ZUM services be available on a stand-alone basis.
3. A requirement that Applicants agree to prominently list the availability of these services in phone books, on the web, and in bill inserts;
4. A requirement that Applicants offer an intrastate long distance calling without a minimum monthly fee;
5. A requirement that SBC provide a competitive alternative for residential and small business customers in Verizon's service territory no later than 18 months from the consummation of the merger. This alternative must be made available at prices comparable to or less than Verizon's.
6. The submission of quarterly reports on the progress of competitive offerings in Verizon's territories.
7. The imposition of a non-trivial penalty, "e.g., $10 million," each month if SBC fails to meet a "target of providing meaningful competitive alternative within 18 months."

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[207] Qwest, Opening Brief, pp. 33-41.

[208] Telescape, Opening Brief, p. 4.

[209] TURN, Opening Brief, pp. 123-131

8. Make approval conditional upon Applicant's agreement to fund independent third-party monitoring of competitive conditions in California;
9. Require corporate affiliates to cooperate with third-party monitoring;
10. Require Applicants to agree to the service quality monitoring recommendation outlined in TURN's Comments in the Rulemaking on General Order 133-B;
11. Adopt further conditions to require the tracking of the deployment of new technology by wire center, along with statistics about wire center demography;
12. Make Commission approval contingent on Applicants agreement to fund two independent audits of SBC's affiliate transactions;
13. Require Applicants to commit in writing that all corporate affiliates of SBC will make their books and records available for inspection by Commission staff and the third-party auditor
14. Require that Applicants modify their standard non-disclosure and protective agreements so that it allows parties to use material obtained in one Commission docket in any other regulatory proceeding as long as the confidentiality of the information is maintained.

DRA argues that the Commission should adopt merger conditions in six areas: 1) ensure that applicants maintain and improve customer service for customers with disabilities; 2) require that applicants renew their commitment to universal design principles; 3) require improvements in accessibility of all communications; 4) improve polices related to bundled services and basic phone service; 5) ensure that an internal committee for voicing the concerns of the disability community is maintained; 6) establish auditing and reporting requirements.

8.2. Discussion

The intervenors in this proceeding have proposed a litany of conditions that they ask the Commission to apply to this transaction. To the extent possible, we have considered each proposed condition in the context of the adverse

consequences that the intervenors alleged would result from the proposed transaction. As discussed at length in prior sections of this decision, we find no basis upon which to conclude that such adverse consequences which these conditions are designed to mitigate would result from this transaction. Therefore the request for conditions recommended by intervenors has little merit.

There are still other conditions that we have not listed above. The voluminous record in this proceeding makes it clear that the proposed transaction will not produce adverse anticompetitive consequences, and that the merger, when combined with the conditions set forth herein and the agreement reached by the Applicants, Greenlining and LIF, is in the public interest. There is therefore no rational basis for imposing any of the additional conditions on this transaction that are proposed by TURN, ORA, Telescape, CALTEL (with Covad), Cox, PacWest, Level 3 or Qwest. We therefore will not discuss these proposals in any more detail than we have done already, for it is clear that these conditions are neither needed to "prevent serious adverse consequences"[210] nor do they represent "reasonable options."[211]

Concerning the proposals of DRA, we see no need to adopt the mitigation measures that they propose. The acquiring entity, SBC, has a record of providing good service to the disabled community, and ensuring this good service remains a focus of the Commission's regulatory program. Indeed, several of the proposed conditions such as "maintain … customer service" and "renew

[210] § 854(c)(8)

[211] § 854(d)

their commitment" to the disabled are both vague in scope and demonstrative of SBC's current commitments to this community.[212]

9. The Commission Should Approve this Application for a Proposed Merger of the Parent Companies and Change in Control at this Time

In summary, we find that the proposed merger of the parent companies and resulting change of control is in the public interest pursuant to §854(a). In addition, in the course of our § 854(c) examination and our examination of the competitive impacts of this merger, we have reviewed proposals recommended by other parties and find that the transaction as proposed and modified herein best serves the public interest.

10. Comments

The proposed alternate decision of Commissioner Peevey and Commissioner Kennedy, the assigned Commissioner in this matter was provided to parties for comment in accordance with Pub. Util. Code Sec. 311(d) and Rule 77.6 of the Rules of Practice and Procedure.

On _____filed Initial Comments and on _____ filed Reply Comments.

11. Assignment of Proceeding

Michael R. Peevey is the Assigned Commissioner and Thomas R. Pulsifer is the assigned ALJ in this proceeding

Findings of Fact

1. This application was filed pursuant to § 855(a). A supplemental application was filed to provide information on §§ 854 (b) and (c) requirements.

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[212] See DRA's Opening Brief.

2. On February 28, 2005, SBC Communications, Inc. and AT&T Corp. filed a joint application to transfer control of AT&T Communications of California, TCG Los Angeles, Inc., TCG San Diego, and TCG San Francisco from subsidiaries of AT&T to subsidiaries of the combined organization. This transfer will occur indirectly as a result of SBC obtaining direct control of AT&T, neither of which is regulated by the Commission as a public utility, and indirect control of AT&T's certified public utility subsidiaries in California.

3. When the transaction is completed, AT&T will become a subsidiary of SBC. The AT&T Subsidiaries in California will become third-tier subsidiaries of SBC, and the authorizations and licenses currently held by the AT&T Subsidiaries will continue to be held by the respective entities. The transaction does not involve the merger of any assets, operations, lines, plants, franchises, or permits of the AT&T Subsidiaries with the assets, operations, lines, plants, franchises, or permits of any SBC entity.

4. The parties to the merger transaction are SBC Communications, Inc. and AT&T Corp. Neither party is a California utility. The California utilities that are subsidiaries of SBC and AT&T are not parties to the transaction. Those California subsidiaries are not being utilized to effectuate the transaction, nor are they using their respective parents to effectuate the transaction.

5. SBC's California subsidiaries account for approximately one-third of the total number of access lines owned by SBC.

6. Fourteen Public Participation Hearings were held. Two Public Participation Hearings were held in each of the following cities: Oakland, Sacramento, Fresno, Culver City, Anaheim, Riverside, and San Diego to take comments from the public on the proposed merger. These hearings were well

attended and demonstrated broad consumer and community support for the merger.

7. Hearings were held from August 8-12 and 15-17.

8. The number of AT&T's access lines in California is *de minimis*.

9. Neither SBC Communications, Inc. nor AT&T Corp., the parent holding companies, were formed around their respective California utilities as a way to escape regulation.

10. AT&T's California subsidiaries are non-dominant and not traditionally regulated utilities.

11. SBC's California subsidiaries are no longer regulated under traditional cost-of-service rate regulation.

12. The Commission lacks effective ratemaking authority over AT&T and its California subsidiaries.

13. Since divestiture, AT&T has grown and shrunk under competitive conditions without a guaranteed franchise.

14. This transaction will likely produce significant cost savings and other synergies for the combined firm. These transaction-related benefits will be passed through to customers through competition and market forces.

15. On July 22, 2005, the California Attorney General filed an Advisory Opinion on the competitive effects of the proposed merger, in which he found that the proposed merger will not adversely affect competition in any relevant market, other than for DS1 and DS3 private network services.

16. The Attorney General found that the relevant markets at issue in this transaction are the markets for: (1) local exchange services and long distance services for residential and small business customers (part of the mass market); (2) long distance services for residential and small business customers (part of the

mass market); (3) business applications sold to medium- to large-business and government customers (the enterprise market); (4) special access services; and (5) Internet backbone services.

17. HHI analysis does not provide relevant insight into the dynamics of the mass market, and is not needed to perform a competitive analysis.

18. AT&T's mass market business consists of the provision of local and long distance services. AT&T's provision of local service is primarily through resale (UNE-P) rather than AT&T-owned facilities.

19. AT&T's mass market business is in an irreversible decline, due to marketplace developments, recent changes in regulation, and increasing competition in its core long distance business.

20. AT&T currently serves relatively few mass market customers in SBC California's service area.

21. Due to this decline in its mass market business, AT&T is not and would not be a meaningful competitor to SBC California in the mass market absent the transaction.

22. As a non-facilities-based provider, AT&T's provision of mass market services does not affect industry output.

23. Intermodal competition, principally from cable, wireless, and voice over Internet Protocol (VoIP) is intensifying in the mass market in California. Intermodal alternatives have displaced and are continuing to apply competitive price pressure on and continuing to displace a significant amount of traditional wireline service and usage.

24. Mass market consumers' willingness to purchase intermodal alternatives instead of traditional landline service constrains SBC's wireline service rates for many telecommunications services.

25. Wireless service has displaced a significant amount of long distance and local calling from landlines by consumers with wireless phones. In addition to using wireless phones to complete many long distance and local calls, a significant number of consumers are relying solely on wireless service.

26. Intermodal competition will continue to provide a check on future anticompetitive outcomes in the local exchange market, but for this to remain a viable check in a consolidating and converging industry, consumers must have unfettered access to competitive VoIP services.

27. If consumers have unfettered access to competitive VoIP services, then the merger will have no anticompetitive impacts in the mass market for local exchange services.

28. Without unfettered access to competitive VoIP services, the anticipated benefits of this transaction to consumers and the Commission's statutory obligation to promote access to advanced telecommunications services will be frustrated.

29. SBC does not have a long-haul backbone of its own or significant long distance facilities.

30. AT&T has elected to exit the mass market for long distance services.

31. Significant intermodal competition from wireless services is already present in the mass market for long distance services.

32. The merger will have minimal effects on the levels of concentration in this market.

33. The proposed merger will have no anti-competitive effects in the mass market for long distance telecommunication services.

34. The market for enterprise services includes the full array of highly differentiated advanced information services, including voice and data services that large businesses and governmental users demand.

35. The enterprise market is highly competitive and includes IXCs (such as AT&T, MCI and Sprint), global network service providers (such as Deutsche Telekom and BT), system integrators, CLECs and DLECs, cable companies and equipment vendors.

36. The enterprise market has been competitive for some time and is not highly concentrated.

37. SBC and AT&T focus their marketing efforts on different sectors of the enterprise market.

38. AT&T is a leading provider of enterprise services to large national customers. SBC has had difficulty attracting the type of large enterprise customers AT&T serves, particularly those based or with communications needs outside of SBC's traditional service area.

39. The Federal Communications Commission has repeatedly deemed this market competitive.

40. The merger will not produce anticompetitive effects in the enterprise market.

41. The market for special access involves dedicated point-to-point facilities that are primarily high capacity (e.g. DS1 or greater) connections that can be used to connect an end user to an IXC's point of presence, to connect two end user locations, and to connect end users to CLEC, ISP, wireless or other competitive networks.

42. In certain locations, AT&T is the only competitor against SBC providing special access services in SBC California's service areas.

43. The Attorney General finds that the proposed merger may enhance SBC's existing market power over DS1 and DS3 services and that entry barriers in the market for these services are long-lasting. Therefore, the Attorney General recommends a one-year freeze on rates paid by current AT&T customers receiving DS1 or DS3 private network services.

44. The Internet backbone and ISP markets are highly unconcentrated and will remain so after the merger.

45. The Attorney General's Advisory Opinion states that the FCC has exclusive jurisdiction over Internet backbone services. Therefore, Internet-peering is outside of the CPUC's jurisdiction.

46. The merger will maintain or improve the financial condition of the affected California utility subsidiaries.

47. There is no rational basis for imposing new quality control conditions because of the proposed merger.

48. The transaction will maintain or improve the quality of management of the affected California utility subsidiaries.

49. The transaction will be fair and reasonable to affected California utility employees, both union and non-union.

50. The transaction will be fair and reasonable to the majority of all affected shareholders.

51. The transaction will be beneficial on an overall basis to state and local economies, and the communities in the areas served by the resulting public utility. Specifically, the merger will produce cost savings and other synergies that will be passed through to California customers through competition and market forces. The transaction will also result in the combined company's ability to offer a broader range of services, and more advanced services, to California

consumers. The transaction will promote competition in communications in California, resulting in improved quality of service, more competitive prices, and greater technological innovation that will inure to the benefit of customers.

52. The Greenlining Agreement ensures that the transaction will be beneficial to the local communities in California.

53. This transaction will not affect the structure of AT&T's California subsidiaries and the Commission's ability to regulate those subsidiaries will not be diminished. The AT&T subsidiaries will continue to be subject to all the terms and conditions that the Commission has previously required. The transaction will therefore not adversely affect the Commission's jurisdiction, nor its ability effectively to regulate the combined company's public utility operations in California.

54. The transfer of AT&T's California subsidiaries takes place at the holding company level and will not result in any incremental impact on the environment.

55. No mitigation measures other than those imposed on the merger in response to the Attorney General's Advisory Opinion, and the requirement that SBC not force customers to separately purchase traditional voice service as a condition of obtaining DSL are reasonable or in the public interest.

56. The material presented by the Applicants and parties to this proceeding has enabled us to reach findings on all issues discussed in § 854

Conclusions of Law

1. This proceeding is a ratesetting proceeding.

2. The proposed transaction is subject to scrutiny under Pub. Util. Code § 854(a).

3. Pursuant to §854(a), Applicants must demonstrate, by a preponderance of the evidence, that the proposed transaction is, on balance, in the public interest.

4. Neither of the direct parties to this transaction, the parent holding companies SBC Communications Inc. and AT&T Corp., are utilities within the meaning of § 854(b).

5. In D.97-03-067, *In re Pacific Telesis Group*, the Commission looked past the formal structure of the transaction at the holding company level because the utility, Pacific Bell, was essentially the only asset of the holding company, Pacific Telesis Group, and the acquisition of the utility was the fundamental reason for the transaction.

6. D.97-03-067 applies only to the specific facts on which it was decided, and does not stand for the proposition that the Commission will pierce the corporate veil separating the utility from its parent whenever a transaction will have an impact on a large California utility.

7. The facts supporting D.97-03-067 are not present here. AT&T's California subsidiaries represent only a small fraction of AT&T's overall business and the transfer of these subsidiaries is not the fundamental reason for this transaction. Further, neither SBC Communications Inc. nor AT&T Corp. was formed around the utilities as a means to escape regulation. Therefore the reasoning of D.97-03-067 is inapplicable to this transaction.

8. Pursuant to §853 (b) the Commission may exempt a transaction from the requirements of §§ 854 (b) and (c).

9. The Commission has articulated a three-part test for determining whether to grant an exemption from the requirements of §§ 854(b) and (c). An exemption is to be granted where: (1) the transaction does not involve two traditionally regulated telephone systems; (2) the Commission lacks effective ratemaking authority over the transferred entity that the Commission could use to mandate the delivery of benefits under §§ 854(b); and (3) the transferred entity has grown

under competitive forces and is subject to competition without a guaranteed franchise territory.

10. All the exemption criteria are met in this transaction. First, the transaction does not combine two traditionally regulated utilities, and because AT&T's California subsidiaries are non-dominant inter-exchange carriers or competitive local exchange carriers. Second, the Commission lacks effective ratemaking authority over AT&T's California subsidiaries. Third, AT&T has grown under competitive conditions without a guaranteed franchise territory since divestiture.

11. Therefore, even if §§ 854 (b) and (c) applied to this transaction, an exemption from those sections would be appropriate under applicable Commission precedent.

12. Because the benefits of the merger will be passed through to California consumers through competition and market forces, there are no policy grounds for mandated sharing of those benefits.

13. In order to determine whether the transaction is in the public interest pursuant to § 854(a), it is reasonable for the Commission to assess the public interest factors enumerated in § 854(c) and undertakes an analysis of antitrust and environmental considerations.

14. Applicants have demonstrated that all of the criteria enumerated in § 854(c) are satisfied by this transaction.

15. In order to determine if the transaction will have an adverse effect on competition, the sole material question is whether the elimination of AT&T as an independent competitor in any properly defined markets would confer market power on SBC or enhance any market power it currently possesses.

16. The transaction will not cause an adverse effect on competition in the mass market for local exchange telecommunications services.

17. The transaction will not cause an adverse effect on competition in the mass market for long distance telecommunications services.

18. The transaction will not cause an adverse effect on competition in the enterprise market.

19. The transaction will not cause an adverse effect on competition for the provision of special access services, with the adoption of the Attorney General's recommendation for a one-year freeze on rates paid by current AT&T customers receiving DS1 or DS3 private network service.

20. The transaction will not cause an adverse effect on competition in the market for Internet Backbone services.

21. The transaction will not have an adverse effect on competition in any properly defined market and it therefore raises no antitrust concerns.

22. Cross-subsidization is unlikely because SBC California's rates are not set with reference to its costs and because the Commission will continue to enforce affiliate transaction rules.

23. The California Environmental Quality Act (CEQA) requires the Commission to consider the environmental consequences of projects that are subject to the Commission's review and approval.

24. It is reasonable for the Commission to approve this transaction, subject to the conditions proposed herein.

O R D E R

IT IS ORDERED that:

1. The joint application of SBC Communications, Inc. (SBC) and AT&T Corp. (AT&T) for authorization to transfer control of AT&T Communications of California, TCG Los Angeles, Inc., TCG San Diego, and TCG San Francisco to SBC, which will occur indirectly as a result of AT&T's merger with a wholly-

owned subsidiary of SBC, is granted subject to four conditions. Those conditions are:

a) SBC shall, by February 28, 2006, cease forcing customers to purchase separately traditional local phone service as a condition for obtaining DSL (this condition is commonly known as a requirement to provide "naked DSL." We further order that no later than February 28, 2006 , SBC shall submit an affidavit evidencing compliance with this condition of the merger.

b) Applicants shall adopt the agreement that Applicants negotiated with The Greenlining Institute (Greenlining) and Latino Issues Forum (LIF) [213] and as modified in this decision (Greenlining Agreement). Under the key terms of the Greenlining Agreement the Applicants agree to:

- Participate in a statewide Broadband Task Force
- Increase corporate philanthropy over the next 5 years. Philanthropy will increase to $15 million for years one and two. Philanthropy will increase yet again to $20 million for years three, four, and five. The total net increase in philanthropy from current levels is $57 million. SBC commits to direct at least 60% of this additional philanthropy to minorities and underserved communities.
- Make a good faith effort to increase the supplier diversity goal for minority business enterprises from the current 23% to 27% by 2010. To achieve this goal, minority, supplier, diversity spending in California could grow to $40 million in 2006 and to $80 million by 2010.

c) Applicants shall commit $9 million per year for 5 years in charitable contributions ($45 million total), to a non-profit corporation, the California Emerging Technology Fund (CETF), to be established by the Commission for the purpose of achieving ubiquitous access to broadband and advanced services in California, particularly in

[213] This agreement between the Applicants, Greenlining and LIF is referred to as the "Greenling Agreement."

underserved communities, through the use of emerging technologies by 2010. No more than half of Applicant's total commitment to the CETF may be counted toward satisfaction of the Applicants' commitment in the Greenlining Agreement to increase charitable contributions by $57 million over 5 years.

d) Applicants shall freeze for one year rates paid by current AT&T customers receiving DS1 or DS3 private network service. This rate freeze shall begin with the date that control is transferred.

2. Applicants shall file and serve a written notice in this proceeding of their agreement to the transfer of control and merger of their companies consistent with the terms set forth in this order. The agreement shall be evidenced by resolutions of their respective Boards of Directors authenticated by appropriate corporate officers. The authority to transfer control and merge granted herein shall expire 90 days from the effective date of this order if Applicants fail to file authenticated resolutions of their agreement with the terms of this order within 90 days from today. The authority to transfer control and merge granted herein shall expire 365 days from the effective date of this order if Applicants fail to transfer control and merge as authorized herein within 365 days from today.

3. Within 30 days of the issuing date of any decision by another jurisdiction which materially changes the terms of the proposed transaction as it affects any of Applicants' California utility operations, Applicants shall file a copy of that decision with the Commission, with a copy served on the service list in this proceeding and the Director of the Telecommunications Division. The filing shall also include an analysis of the impact of any terms and conditions contained therein as they affect any of Applicants' California utility operations.

4. Applicants shall notify the Commission, with a copy served on the service list in this proceeding and the Director of the Telecommunications Division, of the date the merger is consummated. The notice shall be served within 30 days of merger consummation.

5. In the event that the books and records of Applicants or any affiliates thereof are required for inspection by the Commission or its staff, Applicants shall either produce such records at the Commission's offices, or reimburse the Commission for the reasonable costs incurred in having Commission staff travel to any of Applicants' offices.

6. If Applicants consummate the proposed merger authorized herein, their failure to comply with any element of this order shall constitute a violation of a Commission order, and subject applicants to penalties and sanctions consistent with law

This order is effective today.

Dated _____, at San Francisco, California.