STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

SBC COMMUNICATIONS INC., SBC DELAWARE INC., AMERITECH CORPORATION, ILLINOIS BELL TELEPHONE COMPANY d/b/a AMERITECH ILLINOIS and AMERITECH ILLINOIS METRO, INC.	:	
Joint Application for approval of the reorganization of Illinois Bell Telephone Company d/b/a Ameritech Illinois, and the reorganization of Ameritech Illinois Metro, Inc. in accordance with Section 7-204 of the Public Utilities Act and or all other appropriate relief.	:	**98-0555**

ORDER

September 23, 1999

I. INTRODUCTION AND PROCEDURAL HISTORY ---------- 1

II. PURPOSE AND SCOPE OF REOPENING PROCEEDING. ---------- 5

III. ISSUES OF THE CASE ---------- 7

A. THE STANDARD FOR APPROVAL UNDER SECTION 7-204 AND THE APPLICABILITY OF STATUTES OTHER THAN SECTION 7-204. ---------- 7

B. WHETHER THE PROPOSED REORGANIZATION WILL DIMINISH AMERITECH ILLINOIS' ABILITY TO PROVIDE ADEQUATE, RELIABLE, EFFICIENT, SAFE AND LEAST-COST SERVICE. (SECTION 7-204(B)(1)). ---------- 11

C. WHETHER THE PROPOSED REORGANIZATION WILL RESULT IN THE UNJUSTIFIED SUBSIDIZATION OF NON-UTILITY ACTIVITIES BY THE UTILITY OR ITS CUSTOMERS; AND, WHETHER COSTS AND FACILITIES ARE FAIRLY AND REASONABLY ALLOCATED BETWEEN UTILITY AND NON-UTILITY ACTIVITIES IN SUCH A MANNER THAT THE COMMISSION MAY IDENTIFY THOSE COSTS AND FACILITIES WHICH ARE PROPERLY INCLUDED BY THE UTILITY FOR RATEMAKING PURPOSES. (SECTIONS 7-204(B)(2) & (3)). ---------- 32

D. WHETHER THE PROPOSED REORGANIZATION WILL SIGNIFICANTLY IMPAIR THE UTILITY'S ABILITY TO RAISE NECESSARY CAPITAL ON REASONABLE TERMS OR TO MAINTAIN A REASONABLE CAPITAL STRUCTURE. (SECTION 7-204(B)(4)). ---------- 41

E. WHETHER AMERITECH ILLINOIS WILL REMAIN SUBJECT TO ALL APPLICABLE LAWS, REGULATIONS, RULES, DECISIONS AND POLICIES GOVERNING THE REGULATION OF ILLINOIS PUBLIC UTILITIES. (SECTION 7-204(B)(5)). ---------- 44

F. WHETHER THE PROPOSED REORGANIZATION IS NOT LIKELY TO HAVE A SIGNIFICANT ADVERSE EFFECT ON COMPETITION IN THOSE MARKETS OVER WHICH THE COMMISSION HAS JURISDICTION. (SECTION 7-204(B)(6)). 49

G. WHETHER THE PROPOSED REORGANIZATION IS LIKELY TO RESULT IN ANY ADVERSE RATE IMPACTS ON RETAIL CUSTOMERS. (SECTION 7-204(B)(7)). ---------- 107

H. RULINGS PURSUANT TO SECTION 7-204(C) ---------- 123

I. THE SCOPE OF THE COMMISSION'S AUTHORITY UNDER SECTION 7-204(F) ---------- 147

1. Statutory Contribution ---------- 150

2 Joint Applicants' New Commitments ---------- 151

a. Interconnection ---------- 151
b. Shared Transport, Question 3; Attachment A ---------- 171
c. Operations Support Services ("OSS"): Implementation ---------- 182
d. Operations Support Services: Deployment of Interfaces ---------- 195
e. Unbundled Local Switching ---------- 196
f. Unbundling and Wholesale Services ---------- 200
g. Section 251 ---------- 201
h. Enforcement: Liquidated Damages Provisions ---------- 203
i. Enforcement: Mechanisms ---------- 219
j. Enforcement: Performance Reports ---------- 222

IV. ADDITIONAL COMMITMENTS BY JOINT APPLICANTS ---------- 226

V. PROPOSED FCC CONDITIONS AND THE JULY 9 LETTER ---------- 230

VI. CONDITIONS TO APPROVAL OF THE REORGANIZATION ---------- 239

A. INTRODUCTION ---------- 237
B. CONDITIONS: ---------- 237

1. Headquarters ---------- 239
2. Name ---------- 239
3. Charitable Contributions ---------- 240
4. Development ---------- 240
5. Employment ---------- 240
6. Ameritech Illinois' Employee Commitment ---------- 240
7. Network Infrastructure Investment ---------- 240
8. Consumer Education Fund ---------- 241
9. Community Technology Fund ---------- 241
10. Community Computer Center ---------- 242
11. OSS Reports ---------- 242
12. LRSIC & TELRIC ---------- 242
13. Cellular Notification ---------- 242
14. 9-1-1 Service ---------- 242
15. Access to Books and Records ---------- 242
16. CAM ---------- 243
17. TRI ---------- 243
18. Universal Design ---------- 243
19. "Best Practices" Report ---------- 243
20. ADSL Development ---------- 244
21. National-Local Subsidiary ---------- 244
22. Section 251 ---------- 244
23. OOS>24 ---------- 244
24. Regulatory Staff ---------- 244
25. Enforcement and Compliance Monitoring ---------- 244
26. Recordation of All Savings and Costs ---------- 246
27. Interconnection ---------- 246
28. Shared Transport ---------- 250
29. Additional OSS ---------- 253
30. Performance Measuring, Benchmarks and Liquidation Damages ---------- 255
31. Verification ---------- 260
32. Notice ---------- 260

VII. FINDINGS AND ORDERING PARAGRAPHS ---------- 258

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

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SBC DELAWARE INC.,	:	
AMERITECH CORPORATION,	:	
ILLINOIS BELL TELEPHONE COMPANY	:	
d/b/a AMERITECH ILLINOIS, and	:	
AMERITECH ILLINOIS METRO, INC.	:	
	:	**98-0555**
Joint Application for approval of the	:	
reorganization of Illinois Bell Telephone	:	
Company d/b/a Ameritech Illinois, and the	:	
reorganization of Ameritech Illinois Metro,	:	
Inc. in accordance with Section 7-204 of the	:	
Public Utilities Act and for all other	:	
appropriate relief.	:	

ORDER

By the Commission:

I. Introduction and Procedural History

On July 24, 1998, SBC Communications Inc. ("SBC"), SBC Delaware Inc., Ameritech Corporation ("Ameritech"), Illinois Bell Telephone Company d/b/a Ameritech Illinois ("Ameritech Illinois," "AI," or "Company"), and Ameritech Illinois Metro, Inc. ("AIM") (collectively "Joint Applicants") filed a verified Joint Application seeking this Commission's approval, under Section 7-204 of the Illinois Public Utilities Act ("PUA" or the "Act") of the "reorganization" of Ameritech Illinois and AIM resulting from a proposed business combination of SBC and Ameritech.

SBC is a Delaware corporation with its corporate headquarters located in San Antonio, Texas. SBC is a holding company whose subsidiaries include Southwestern Bell Telephone Company ("SWBT"), Pacific Bell, Nevada Bell, and Southern New England Telephone Company ("SNET"), each of which is an incumbent local exchange carrier ("ILEC"). SBC also has subsidiaries and affiliates that provide wireless telecommunications and related services, including in Illinois under the "Cellular One" brand name. In addition, SBC has investments in telecommunications companies that serve selected markets outside of the United States. SBC's consolidated 1997 adjusted revenues were approximately $25 billion with a net income of $1.5 billion.

Ameritech Corporation is a Delaware corporation with its corporate headquarters located in Chicago, Illinois. Ameritech is a holding company whose subsidiaries include

Ameritech Illinois. Ameritech's other subsidiaries and affiliates include ILECs in four other states, wireless telecommunications and related services providers in Illinois and several other states, and a provider of security monitoring services in most of the United States' largest metropolitan areas. Ameritech also has significant investments in the European telecommunications industry. Ameritech's consolidated 1997 adjusted revenues were approximately $16 billion with a net income of $2.3 billion.

Ameritech Illinois is an Illinois corporation with its headquarters located in Chicago, Illinois. Ameritech Illinois is a certificated local exchange and intraMSA interexchange carrier and currently serves approximately 240 exchanges and approximately 6.6 million access lines throughout Illinois. Ameritech Illinois is both a Bell operating company ("BOC") and an ILEC as those terms are defined in the federal Telecommunications Act of 1996 ("96 Act", "Act", or "TA96").

AIM was a wholly-owned subsidiary of AI at the time that the Joint Application was filed. Subsequent to the filing of the Joint Application, AIM merged with and into AI after obtaining this Commission's approval to do so.

SBC Delaware Inc. is a Delaware corporation and a wholly-owned subsidiary of SBC. SBC Delaware was created solely for the purpose of effectuating an exchange of stock between SBC and Ameritech's shareholders as part of the proposed business combination transaction described below. Upon completion of that transaction, SBC Delaware would cease to exist.

The reorganization of Ameritech Illinois that is the subject of the Joint Application would result from a proposed business combination of SBC and Ameritech ("reorganization" or "merger"). The combination would be accomplished through an exchange of stock between Ameritech's shareholders and SBC, via SBC Delaware. Upon completion of the exchange of stock, SBC Delaware would be merged with and into Ameritech, and Ameritech would become a wholly-owned, first-tier subsidiary of SBC. AI would remain a wholly-owned subsidiary of Ameritech. Because this proposed transaction constitutes a "reorganization" of AI under Section 7-204, Joint Applicants request this Commission's approval of the transaction in accordance with that Section.

Pursuant to notice, prehearing conferences were held before duly-authorized Hearing Examiners of the Commission at its Chicago offices on August 18, October 29, November 24, and December 7, 1998. The following parties petitioned for and were granted leave to intervene by the Hearing Examiners: Covad Communications Company ("Covad"), Sprint Communications Company, L.P. d/b/a Sprint Communications ("Sprint"), AT&T Communications of Illinois, Inc. ("AT&T"), MCI Worldcom, Inc. ("MCIW"), DSSA and Neighborhood Learning Networks ("DSSA"), the Citizens Utility Board ("CUB"), the People of the State of Illinois ("AG"), the People of Cook County ("Cook County" and together with CUB and AG, "GCI"), the City of Chicago ("Chicago"), the American Association of Retired People ("AARP"), the Cable Television and Communications Association of Illinois ("CTCA"), 21st Century Telecom

of Illinois, Inc. (“21st Century”), Nextlink Illinois, Inc. (“Nextlink”), MGC Communications, Inc. (“MGC”), Corecomm, Ltd. (“Corecomm”), the Illinois Public Telecommunications Association (“IPTA”), and the Telecommunications Resellers Association (“TRA”). The Illinois Commerce Commission Staff (“Staff”) also appeared by counsel and actively participated in the docket.

Additional petitions for leave to intervene which were granted by the Hearing Examiners were, as follows: the Community Workshop on Economic Development, Sutherland Community Arts Initiative, and the Veterans Neighborhood Builders Association, Inc.

Evidentiary hearings were held on January 25-29, 1999. The following witnesses testified at the hearings: on behalf of Joint Applicants, James S. Kahan, SBC’s Senior Vice President for Corporate Development; Karen E. Jennings, SBC’s Senior Vice President for Human Resources; Charles H. Smith, President of Pacific Bell Network Services; Christopher J. Viveros, Pacific Bell’s Director-OSS Planning and Regulatory Support; W. Patrick Campbell, Ameritech’s Executive Vice President of Corporate Strategy and Development; David H. Gebhardt, Ameritech Illinois’ Vice President - Regulatory Affairs; Richard R. Galloway, Ameritech’s Director of Network Process Management and Service Results; and two outside economists, Dr. Robert G. Harris and Dr. Richard J. Gilbert.

Staff witnesses were Judith R. Marshall, Rasha Toppozada-Yow, Robert Plaza, Deborah Prather, Cindy Jackson, S. Rick Gasparin, Samuel S. McClerren, Christopher L. Graves, and an outside economist, Dr. Carl E. Hunt. GCI witnesses were Dr. Lee L. Selwyn and Charlotte F. TerKeurst. AARP’s witness was an economist, Dr. Mark N. Cooper. AT&T witnesses were Sarah DeYoung, Bruce Bennett, Kathleen S. Whiteaker, and an outside economist, Joseph Gillan. Sprint witnesses were David E. Stahly and Paul A. Wescott, and an outside economist, Dr. John R. Woodbury. MCIW’s witness was David N. Porter. Nextlink’s witness was Daniel Gonzalez. DSSA’s witness was Don S. Samuelson. IPTA’s witness was Martin S. Segal. At the close of the hearing on January 29, 1999, the record was marked “Heard and Taken.”

Subsequently, upon AT&T’s motion, the Hearing Examiners admitted into the record as late-filed exhibits the direct testimony (and exhibits) and cross-examination transcript (and exhibits) of one of SBC’s witnesses, Mr. Kahan, from the merger proceedings conducted by the Public Utilities Commission of Ohio.

Initial Briefs were filed by Joint Applicants, Staff, CUB, AG, Cook County, AT&T, Sprint, MCI, Nextlink, 21st Century, CTCA, TRA and DSSA. Reply briefs and/or draft orders were filed by Joint Applicants, Staff, CUB, AG, Cook County, AT&T, Sprint, MCIW, Nextlink, 21st Century, CTCA, AARP and DSSA. Motions for oral argument were filed by Joint Applicants and AT&T.

On March 29, 1999, the Hearing Examiners issued their Hearing Examiners’ Proposed Order (“Proposed Order”). Exceptions and/or Replies to Exceptions were

filed by Joint Applicants, Staff, CUB, AG, Cook County, AT&T, Sprint, MCI, Nextlink, 21st Century, CTCA, TRA, and DSSA.

All of the exceptions were carefully considered and the Post Exceptions Proposed Order, which was provided to the parties on April 26, 1999, contained substantial changes.

The Commission, On Its Own Motion, heard oral argument on April 29 and 30, May 3 and 4, 1999. Subsequently, on June 4, 1999, the Chairman of the Commission ("Chairman") sent a letter to the Hearing Examiners to which was appended Attachment "A". This Attachment listed thirteen question which concerned and invited response from the Joint Applicants. As directed by the letter, the Hearing Examiners provided a copy of both the letter and Attachment A to the Joint Applicants and all other parties. On June 7, the Joint Applicants filed a written response to the questions set out in Attachment A.

Thereafter, on June 10, 1999, Joint Applicants submitted an Amended Joint Application together with a Motion to File an Amended Application and a Motion to Reopen the Record for further proceedings. As part of their submission this date, the Joint Applicants included a "Summary of Additional Commitments by Joint Applicants" and a "Response to Commission June 4 List of Issues and Joint Applicants Additional Commitments" marked as Exhibits 5 and 6, respectively.

The Hearing Examiners granted both of the pending motions on June 15, 1999 and the Joint Applicants served their pre-filed Direct Testimony on Reopening this same date. Also on June 15, 1999, the Chairman sent out another letter to the Hearing Examiners which included "Attachment A-1". There were listed in this attachment, a series of subsidiary questions as follow-up to those set out in Attachment A. As directed, the Hearing Examiners' served the June 15 letter and Attachment A on Joint Applicants and all other parties to the cases. In response, on June 18, 1999, the Joint Applicants served all parties with pre-filed Supplement Direct Testimony on Reopening and, in addition, filed a separate document addressing the A-1 questions.

Pursuant to a schedule set by the Hearing Examiners upon due notice and a pre-hearing conference held on June 21, 1999. The Staff and numerous parties served their pre-filed Direct Testimony on Reopening on July 6, 1999. Thereafter, on July 9, 1999, the Joint Applicants served Rebuttal Testimony on Reopening.

On July 1, 1999, the staff of the FCC and Joint Applicants announced a list of conditions and commitments that the FCC staff and Joint Applicants had agreed to and that the FCC staff believed would be sufficient for the FCC to issue the required merger-related approvals. This list of conditions was made an exhibit to Mr. Kahan's Rebuttal Testimony on Reopening. The Chairman then sent another letter to the Hearing Examiners on July 9, 1999 ("July 9 letter"), which included an Attachment A-2 that set out some additional questions to be addressed by Joint Applicants and parties regarding the commitments proposed by Joint Applicants at the FCC ("FCC

Commitments"). Joint Applicants' witnesses responded to these questions in oral testimony at the evidentiary hearings and were the subject of cross-examination. On July 20, 1999 Joint Applicants filed a written response, consistent with the testimony, to Attachment A-2 of the July 9 letter.

Upon proper notice, an evidentiary hearing was held at the Commission's offices in Chicago on July 13, 14, 15, and 1999. The following witnesses presented testimony on reopening: On behalf of the Joint Applicants the witnesses were - James S, Kahan; Christopher Veveros; David H. Gebhardt, William R. Dysart, Terry A. Appenzzeller; Curtis L. Hopfinger and Dr. Richard Gilbert. The Staff's witnesses were - Ms. Marshall, Ms. Jackson, Mr. Gasperin, Mr. McClerren, Mr. Graves, and Dr. Hunt. The witness for GCI was Dr. Selwyn. AT&T witnesses were Steven Turner and Mr. Gillan. MCIW witnesses were Joan Campion and Sherry Lichtenberg. Sprint witnesses were Dr. Woodbury, Mark Smith, and W. Richard Morris. DSSA and Neighborhood Learning Networks's ("DSSA") witnesses were Mr. Samuelson and David Garth Taylor. 21st Century's witness was Kristen Smoot. The Office of Small Business Utility Advocate for the State of Illinois' ("SBUA") witness was Vincent Gilbert. Covad Communications' ("Covad") introduced the testimony of Clay Deanhardt. The witness for Accelerated Connections, Inc. ("ACI") was Jo Gentry. The witness for McLeodUSA Telecommunications Services, Inc. ("McLeodUSA") was David Conn. The witness for Global Com was John Shave. In addition to those parties who had intervened earlier in this proceeding, the Hearing Examiners granted petitions to intervene filed after reopening by Global Com, McLeodUSA, Covad, ACI and Northpoint Communications, Inc. At the conclusion of the hearing, the reopened record was marked "Heard and Taken."

Post-Hearing Briefs were filed by Joint Applicants, Staff, AT&T, MCIW, Sprint, the AG, Cook County, CUB, DSSA, 21st Century, McLeodUSA, Nextlink, Covad, Northpoint, ACI and Global Com, CCTA, MGC, and TRA on July 28, 1999. Draft Orders were filed by Joint Applicants, Staff, AT&T, GCI, Sprint, McLeod, Covad, ACI, and NLN. On August 10, 1999, the Hearing Examiners issued a Proposed Order on Reopening. Briefs on Exceptions were filed by Joint Applicant, Staff, AT&T, MCIW, GCI, DSSA, 21st Century, McLeod USA, Nextlink, Covad and CCTA. A Post Exceptions Proposed Order on Reopening was prepared and served on August 17, 1999.

II. PURPOSE AND SCOPE OF REOPENING PROCEEDING.

In their Joint Application, filed on July 24, 1998, the Joint Applicants set out a description of, and the reasons for, the proposed merger. This verified pleading further detailed the statutory provisions pursuant to which Commission approval was being sought, i.e., Section 7-204 of the Act. Attached to the Joint Application and incorporated therein were a number of exhibits. The last of these, "Exhibit 4", was a copy of a letter from the Chairman and Chief Executive of SBC to the Chairman and Chief Executive Officer of Ameritech wherein SBC made six specific commitments to Ameritech regarding the ongoing operations of Ameritech post-merger. It was alleged

by the Joint Applicants that these particular commitments benefit the State of Illinois, its telecommunications customers and Ameritech employees. In the proceeding that grew out of this application, these commitments were hotly debated and in some instances enlarged.

On June 10, 1999, when the Joint Applicants filed their Amended Joint Application, they included a large number of new commitments in addition to those which evolved from the initial evidentiary and briefing stages. The record was reopened on the Joint Applicant's motion thus allowing the parties (Staff, Joint Applicants and Intervenors) to litigate the issues related to these new commitments. This we refer to as the "Reopening Proceeding."

The Joint Applicants' filing of an Amended Joint Application and a Motion to Reopen the Record was in part, precipitated by the Chairman's June 4 letter and the questions in Attachment A thereto. The Reopening Proceeding was authorized by Section 7-204(d) of the Illinois Public Utilities Act ("PUA"), which provides for an extension, not to exceed three months, of the 11-month time frame for a final decision in cases brought under Section 7-204. The scope of the reopening was defined by the questions set out in Attachments "A", "A-1" and "A-2" to the Commission letters (of June 4, 15, and July 9, respectively) and framed by the provisions of Section 7-204 of the Act. In response to the June 4 letter and Attachment A, Joint Applicants set out a number of voluntary commitments, (beyond those made in the earlier phase of this proceeding), which they would be willing to accept as conditions to approval of the proposed merger.

Joint Applicants do not believe that any of the additional commitments made on reopening are actually necessary for us to approve the proposed merger under Section 7-204. They state that the additional commitments were made in response to the questions raised by the Chairman and other Commissioners, and not because the commitments were necessary under Section 7-204. Joint Applicants also state that they do not believe that any of the proposed commitments they made to the FCC are necessary to approve the merger under Section 7-204, but they also would not oppose certain substantive portions of those commitments being incorporated into our Order provided that the conditions were tailored to Illinois and did not expose Joint Applicants to duplicative charges under both the Illinois Order and the FCC's ultimate Order.

This Order takes account of all the testimony and arguments on brief presented in both the initial phase of this proceeding and on the reopening. In most part, our Order combines the Commissions general discussion of Section 7-204 provisions with the additional analysis derived from responses to the Chairman's questions that structured the reopening. This follows the style and manner of our extensive deliberations. Wherever possible, the Commission's questions and the responses of the parties have been placed under the particular statutory subsections from which they arise. While arguably, the majority of the issues addressed on reopening relate to Section 7-204(6), there were also questions and responses which pertain to Section 7-204(b)(7), 7-204(c) , and Section 7-204(c).

Although recognizing that the evidence is fluid in many respects, we have attempted to be clear and distinct in our discussion of the issues on reopening. To meet this objective, we have set out the questions from the various attachments in bold text. The initial set of questions arise from Attachment A of the Commissions June 4 letter (Question No.____). A subsidiary series of questions were set out in Attachment A-1 to the June 15 letter and are identified as such. (Item No.___). In this latter set of questions, there are references made to "Exhibit 6", which is the document entitled "Response to Commission's June 4 List of Issues and Joint Applicants Additional Commitments" that Joint Applicants attached to their amended application, and describes their additional proposed commitments in this cause. Only Joint Applicants addressed every follow-up item which appears in Attachment A-1. Thus, when discussing the issues raised on reopening, we will first describe Joint Applicants' response to the initial question and all sub-parts or items and then set out the position of each other party which addressed the question.

III. Issues of the Case

Section 7-204 of the PUA provides that the Commission shall not approve the proposed reorganization of a public utility if it finds that the reorganization will adversely affect the utility's -- in this case, Ameritech Illinois' -- ability to perform its duties under the PUA. In approving a proposed reorganization, the Commission must make seven specific findings set out in subsection 7-204(b)(1) through 7-204(b)(7), and also must address the provisions of subsections 7-204(c), relating to allocations of reorganization-related savings and costs, and 7-204(f), relating to imposition of terms, conditions and requirements on the proposed reorganization. Because Staff and the parties raise disputes regarding each of these statutory subsections, we will discuss each of these subsections in turn. First, however, we will address the issue of whether any statutory sections other than Section 7-204 -- in particular Section 7-102 -- also apply to the proposed reorganization.

A. The Standard For Approval Under Section 7-204 And The Applicability Of Statutes Other Than Section 7-204.

All parties agree that the proposed reorganization requires Commission approval under Section 7-204. An issue has been raised, however, as to the possible need for approval under Section 7-102. In addition, some parties have implied that the reorganization must not only satisfy the seven elements of Section 7-204(b), but also a "public convenience" or "public interest" test such as the Commission is directed to apply under other statutory Sections. We discuss the Intervenors' positions first.

Intervenors' Position

MCI, joined by a few other Intervenors, contends that this merger requires Commission approval under Section 7-102 and the "public convenience" standard in Section 7-102(i). In support of this claim, MCI notes that Section 7-102 approval was

required in Docket 95-0551 (CIPSCO/Union Electric merger, Order entered September 10, 1997), even though that transaction was subject to Section 7-204. MCI also refers to Sections 13-601 and 13-504(d), which confirm that Section 7-102 can apply to telecommunications carriers such as Ameritech Illinois. MCI acknowledges that Section 7-204(e) states that "[n]o other Commission approvals shall be required for mergers that are subject to this Section," but believes that Section 13-504(d) (which exempts certain small telephone companies from Section 7-102 and certain other Sections, and therefore implies that Section 7-102 does apply to larger carriers like Ameritech Illinois) takes precedence over Section 7-204(e) because, if Section 13-504(d) were not read to make Section 7-102 applicable to AI, Section 13-504(d) would be rendered meaningless. Finally, MCI notes that Section 7-102 has been applied in cases under Section 7-204 even after the amendments adding Section 7-204(e), citing the AI/AIM merger (Docket 97-0675, Order adopted August 26, 1998) and Gallatin River Communications' purchase of exchanges from Centel (Docket 98-0321, adopted October 21, 1998).

CUB argues that the Commission can and should review the merger under a "public interest" standard as a result of its general supervisory authority and/or Section 7-204(f). CUB bases this claim on the language in that Section allowing the Commission to place conditions on its approval of a merger under Section 7-204 as "necessary to protect the interests of the public utility and its customers," and on Sections 13-102 and 13-103, which set forth the General Assembly's "Findings" and "Policy" regarding regulation of telecommunications companies under Article XIII.

AT&T argues that Section 7-102 presents a broader standard of review in that it requires the Commission to find that "the public will be convenienced" by the proposed transaction. According to AT&T, concluding that Section 7-102 does not apply ignores the effect of Sections 13-101, 13-504(d) and 13-601, which make Section 7-102 applicable to telecommunications carriers providing non-competitive services.

Joint Applicants' Position

The Joint Applicants disagree with both MCI and CUB. Regarding Section 7-102, the Joint Applicants rely on the plain language of Section 7-204(e), which states that "[n]o other Commission approvals shall be required for mergers that are subject to this Section. "This directive, they argue, should end the inquiry. (Joint Applicants' Reply Br. at 10.) In addition, they note that the same bill enacting Section 7-204(e) also added language to Section 7-102. This language makes clear that approval under Section 7-102 is not required for transactions that are "exempted in accordance with any other Section of this Act." (Joint Applicants' Reply Br. at 10.)

Beyond the plain statutory language, the Joint Applicants note that the merger here is between holding companies, not public utilities, and the Illinois courts have held that Section 7-101 (which, like Section 7-102, applies only to transactions involving public utilities) cannot apply to such a transaction. <u>People's Energy Corp. v. Commerce Comm'n</u>, 142 Ill. App. 3d 917, 929-30 (1st Dist. 1986). They contend that the same

analysis should apply here with respect to Section 7-102. (Joint Applicants' Reply Br. at 10-11.)

Regarding MCI's claim that Section 13-504(d) would be rendered meaningless if Section 7-102 did not apply here, the Joint Applicants state that MCI has it precisely backwards. If the Commission were to find, despite the plain language of Section 7-204(e), that other approvals could be required, then it is Section 7-204(e) that would be rendered meaningless. Section 13-504(d), by contrast, is not rendered meaningless in any sense by Section 7-102's inapplicability here, since it still would fulfill its role of exempting small carriers from certain portions of the PUA. (Joint Applicants' Reply Br. at 11-12.)

In response to CUB's claim that the Commission should apply a "public convenience" or "public interest" test, the Joint Applicants state that Section 7-204(b) clearly provides the only standard for approval under Section 7-204. There is no reference to any type of "public convenience" test as in Section 7-102, and the General Assembly twice has declined to include such a test (once when Section 7-204 was enacted in 1986 and again when it was amended in 1997). Moreover, they state that CUB's reliance on Sections 13-102 and 13-103 is improper, since those are prefatory Sections setting out the basic goals of Article XIII, and it is well-established that prefatory Sections of the PUA have no substantive effect. Monarch Gas Co. v. Commerce Comm'n, 261 Ill. App. 3d 94, 98 (5th Dist. 1994); Governor's Office of Consumer Services v. Commerce Comm'n, 220 Ill. App. 3d 68, 75 (3d Dist. 1991). With respect to Section 7-204(f), the Joint Applicants note that that provision deals only with possible conditions on the approval of a merger, not with the test for approval itself. Indeed, they explain, reading Section 7-204(f) to require a "public convenience" test would be to override the more specific requirements of Section 7-204(b) and render that provision meaningless. (Joint Applicants' Reply Br. at 12.)

Staff's Position

Staff takes the position that "the proposed merger does not require Commission approval under Section 7-102, or any other Section of the PUA besides Section 7-204." This is because "[s]ubsection 7-204(e) states that '[n]o other Commission approvals shall be required for mergers that are subject to this Section [7-204]. 220 ILCS 5/7-204(e)." Legal Memorandum of the Staff in Response to Notice of Ruling (January 8, 1999) at 8. Furthermore, Staff argues that if the Commission [did] apply Section 7-102 in this case, the Commission should generally consider the same factors under each standard. Staff opines that the Commission, in requiring fulfillment of the conditions enumerated in Section 7-204(b) could also find that the proposed transaction would convenience the public under Section 7-102. Id. at 14. Staff also argues that Section 7-102 mandates that the Commission employ a flexible, balancing test to determine whether the public would be convenienced whereas Section 7-204 applies a stricter test by requiring that the proposed transaction satisfy each of the conditions enumerated in Section 7-204(b). Id.

Finally, Staff opines that Section 7-204(f) states the applicable standard for the imposition of terms, conditions or requirements as "necessary to protect the interests of the public utility and its customers." Id. At 4. Staff argues that the standard imposes two requirements for any terms, conditions or requirements which the Commission decides to impose pursuant to Section 7-204(f). The two requirements are (1) the Commission must determine that the terms, conditions or requirements are reasonably required; and (2) to protect the interests of the public utility and/or its customers. Id.

Commission Analysis and Conclusion

While Section 7-102 could apply to Ameritech Illinois in some circumstances, it cannot apply in any case under Section 7-204, as the explicit language of both Sections 7-204(e) and 7-102 make clear. Yet, no party has asserted that Section 7-204 does not apply in this instance and such a position would not be tenable.

Generally, the Commission's oversight of mergers and reorganizations under Article VII is to ensure that the public utility will continue to be able to provide utility service as required under the Act for the benefit of its customers. On its face, Section 7-204 does not require a specific "public interest" finding, or a "public convenience" determination such as is articulated in Section 7-102. We note, however, that the General Assembly has been far more precise in its directions to the Commission when Section 7-204 governs a proceeding. Indeed, Section 7-204(b) sets out seven (7) specific findings that the Commission is required to make, the very effect of which is to protect the interests of the utility and its customers. Furthermore, as noted by Staff in its legal memorandum, the language in Section 7-204(f) specifically authorizes the Commission to consider the interest of a public utility and its customers when conditioning its approval of merger applications. It is these comprehensive directives, and no other, that set out the scope of our authority in this proceeding.

B. Whether the Proposed Reorganization Will Diminish Ameritech Illinois' Ability to Provide Adequate, Reliable, Efficient, Safe and Least-Cost Service. (Section 7-204(b)(1)).

Joint Applicants' Position

The Joint Applicants contend that there is no basis to conclude that the reorganization will diminish the Company's ability to provide adequate, reliable, efficient, safe and least-cost service. In fact, they contend the evidence establishes that, if anything, the reorganization will enable AI to improve the quality of service that it provides. (Joint Applicants' Init. Br. at 22; Joint Applicants' Reply Br. at 66.)

First, the Joint Applicants point to SBC's record as a telecommunications provider. They observe that SBC has over 100 years of experience. They claim SBC is recognized by the industry and by disinterested observers as a leader in providing telecommunications service and has very high ratings for the quality of services provided. The Joint Applicants point to SBC's above-average rating on 55 of 56 criteria on which RBOCs are evaluated. They further point to marked improvements in telecommunications service provided in California after SBC merged with PacTel. They emphasize AI will obtain access to SBC's subsidiary, Technology Resources, Inc. ("TRI"), a research and development organization claimed to be unlike anything to which AI presently has access. They explain that TRI will be used to improve access to telecommunications services in Illinois for disabled people through its Universal Design Policy. According to the Joint Applicants, upon SBC's experience in California, the merger also should enable Ameritech to employ DSL more rapidly. Finally, they suggest that other "best practices" developed by each of the Applicants will be available for implementation by the other Applicants, which also should improve the quality of telecommunication services in Illinois. (Joint Applicants' Init. Br. at 22-25.)

Staff's Position

It is Staff's position that Section 7-204(b)(1) addresses the proposed merger's impact on Ameritech Illinois' service quality and cost of providing service. Staff concludes that for several reasons the proposed merger, as filed, fails the requirements set forth in Section 7-204(b)(1). Thus, Staff proposes that several conditions be imposed to address its concerns if the merger is to be approved.

Staff raises several service quality concerns about the proposed reorganization. First, Staff expresses concern that the Ameritech Illinois ability to maintain its 9-1-1 service quality may diminish if a post-merger company imposes organizational changes such as database integration and removal of executive authority from AI's 9-1-1 staff. To alleviate these concerns, Staff seeks to place restrictions on AI if operational and organizational changes occur in the post-merger company. Specifically, Staff recommends that AI be required to obtain Commission approval prior to implementing any operational and organizational changes such as the reduction or removal of any 9-1-1 staff, which are functional in providing 9-1-1 services in Illinois; and that any post-

merger operational changes that are made in the delivery of 9-1-1 services, be transparent to the 9-1-1 systems, as well as to the 9-1-1 subscribers. Staff Ex. 6.0. at 6-7.

Second, Staff expresses a concern that the Joint Applicants' desire to "win" large corporate customers will result in diminished services to residential and small business customers. Staff Ex. 7.00 at 3. Staff contends that AI and SBC provide only rhetoric that the merger will permit the new company to take advantage of the best ideas, practices and processes developed through the years of experiences by Southwestern Bell Telephone Company, Pacific Bell and other subsidiaries. Staff Ex. 7.00, Attachment 1. According to Staff, the Joint Applicants claimed that the proposed merger, including the National-Local Strategy ("NLS"), should create scale and scope economies which will lower the cost of maintaining existing services and introduce new products, services and network enhancements, cause costs to be spread over a larger customer base, and promote competitive prices and improvements in service quality for Illinois customers. Id. Staff asserts that AI and SBC failed, however, to answer how or when residential customers would benefit and gave no commitment that rates would be reduced, or that calling areas would be improved or expanded, or that the new company would be able to provide additional services not offered by the other telecommunications providers in Illinois. To alleviate this concern, the Staff recommends that the proposed merger be conditioned on SBC's commitment to focus equally on all classes of customers, and file annual reports detailing how the merged company has met its commitment to equally serve residential, small and medium business customers.

Third, Staff contends that certain Pacific Bell marketing practices in California after the SBC/PacTel merger demonstrate that SBC will engage in deceptive marketing practices here. It cites several complaint cases pending before the California Public Utility Commission ("CPUC") and requests that the proposed reorganization of AI be conditioned on a prohibition against any such deceptive marketing practices.

Staff also recommends that the reorganization be conditioned on advancements in access to telecommunication services for people with disabilities.

In addition, Staff expresses concern regarding the merger's impact on Ameritech Illinois' ability to meet the out of service more than 24 hours OOS>24 requirements. Staff points to AI's acquisition of Central Illinois Telephone Company's ("Centel") assets and service quality problems associated with the unification of the two networks as an indication that a problem could arise after this merger. It proposes modifying the penalty for failure to meet the OOS>24 performance standard contained in Ameritech Illinois Alternative Regulation Plan.

Staff also expresses concerns about the Company's continued investment in its network infrastructure post-merger. Staff notes that although all of AI's central offices utilize digital technology, SBC still operates over 100 analog central office switches. Staff asserts that all of SBC's commitments regarding continued network investment

post-merger are too vague and only applicable to Ameritech's territory as a whole, not Ameritech Illinois in particular. Staff Initial Br. at 109-110. Further, Staff notes that SBC's commitments regarding continued network investment post-merger are inconsistent with other evidence provided by SBC during the proceeding. Staff Initial Br. at 110. As a result, the Staff seeks conditions that would impose infrastructure investment and reporting requirements on Ameritech Illinois following the merger.

Staff also raises concerns regarding Ameritech Illinois' ability to provide "least cost" service following the merger. Specifically, Staff interprets the term "least cost" to mean offering service at the most efficient cost consistent with the provision of adequate, reliable, efficient and safe service. Staff Ex. 3.01 at 31. In applying the term "least cost service" requirement to this transaction, Staff takes the position that the Commission must determine whether the proposed merger will negatively impact the price-to-cost relationship currently present in Ameritech Illinois' rates. In other words, the Commission must determine whether, for those services priced above cost, the proposed merger will widen the gap between Ameritech Illinois' rates and costs. Staff Ex. 3.00 at 23.

Staff explains that currently, Ameritech Illinois offers non-competitive services via its Alternative Regulation Plan. Staff points out that when the Commission developed Ameritech Illinois' Plan, it (1) performed the rate of return analysis and established the just and reasonable rates going into the Plan, and (2) developed the price cap index applicable to Ameritech Illinois' noncompetitive services in the Plan. However, the Commission did not take this merger into account. Id. at 25. The Joint Applicants agree. SBC-Ameritech Ex. 3.1 at 63. Staff further points to evidence in this proceeding indicating that the proposed merger will reduce Ameritech Illinois' (incremental, shared and common) cost of providing service. (Staff Init. Br. at 113-114. Staff concludes that to the extent merger-related savings (which include both expense savings and revenue enhancements) are experienced by Ameritech Illinois and not flowed through to its customers, the price cap formula will no longer be reflective of Ameritech Illinois' overall costs and the price-to-cost relationship in Ameritech Illinois' current non-competitive rates will expand. As a result, absent the allocation of these merger related savings to Ameritech Illinois' customers, the Commission will not be able to make a finding that the proposed merger will not diminish Ameritech Illinois' ability to offer least cost public utility service.

Staff disagrees with the Joint Applicants' position that a price-to-cost relationship is inconsistent with Ameritech Illinois' Plan, and provides the following arguments.

First, Staff points out that there are a number of aspects of the Plan which confirms that it did not eliminate the relevance of price-to-cost relationships in Ameritech Illinois' rates. For example, in developing the price cap formula, in Docket 92-0448/93-0239, the Commission attempted to provide a proxy for changes to the Company's overall costs based on its understanding of the regulatory, technological and market changes occurring at the time. Specifically, the price cap formula or index, which governs the extent to which Ameritech Illinois must adjust its rates under the Plan,

includes a 4.3% total offset to the economy wide inflation. This offset reflects AI's historical productivity and input price levels, with a 1% Consumer Dividend to ensure that ratepayers benefited from any improvements beyond AI's historical performance due to technological and regulatory change. Order in Docket 92-0448/93-0239 at 34-39 and 165. Staff notes that productivity and input prices relate directly to changes in Ameritech Illinois' costs. Staff Ex. 9.00 at 52. Staff further notes that the price cap formula also includes an exogenous change factor that reflects changes in Ameritech Illinois' costs which are outside its control and are not reflected in economy wide inflation figures. Order in Docket 92-0448/93-0239, Appendix A).

Further, in its Order approving the Plan, the Commission clearly stated that by adopting an alternative regulation form of regulation for Ameritech Illinois, it was in no way abandoning its long-standing commitment to marginal cost-based pricing or abdicating its responsibility to scrutinize the pricing practices of the Company. The Commission also noted that it would suspend proposed price changes where warranted, even if the proposed price changes are in technical compliance with the price regulation formula. Staff Ex. 3.01 at 34 (citing Order in Docket 92-0448/93-0239 at 71).

Moreover, the Plan prohibits Ameritech Illinois from reducing the prices for its non-competitive services below their long run service incremental cost ("LRSIC"). (Staff Reply Br. at 120-121 (citing ICC Order in Docket 92-0448/93-0239, Appendix A)). AI is also prohibited from reducing the rates of non-competitive services that are currently below LRSIC further below those LRSICs. (Id. (citing Order in 96-0172 at 12-13 and Order in 98-0259 at 7)). In addition, the Plan includes provisions that allow it to raise the rates for individual services that exceed the limits set forth in the Plan subject to the notice and filing requirements of Article IX of the Act and not as part of the Plan's rate adjustment mechanisms. (Id. (citing Order in Docket 92-0448/93-0239, Appendix A)). As a result, where changes in cost justify rate increases, these rate increases can take place. (Id. at 121 and Staff Init. Br. at 112).

Second, Staff argued that the Joint Applicants' view of the alternative regulation plan is also inconsistent with a number of Commission Orders in which Ameritech Illinois' cost of service was considered and Ameritech Illinois was not afforded special treatment because of its price cap company status. For example, in its Order in Docket 94-0048, the Commission authorized AI, along with all other incumbent LECs in Illinois, to recover its cost of implementing intraMSA presubscription through the introduction of a new rate element in its access charge structure. (Id. at 122 (citing Order in Docket 94-0048 at 39-40; see also 83 Ill. Adm. Code 773, Section 773.160)).

Further, in its Order developing wholesale rates for Ameritech Illinois' retail services, the Commission specifically addressed its cost of providing wholesale service and concluded that Ameritech Illinois should be compensated for these costs. For example, the Commission concluded that wholesale resellers would be responsible for compensating AI for all fixed start up costs it incurs in setting up the wholesale/resale market. Further, the Commission specified the manner in which Ameritech Illinois

would recover those costs. It was directed to recover its start up costs from wholesale resellers based on their wholesale market share. (Id. at 122 (citing Order in Dockets 95-0458/0531 Consolidated at 29). The Commission also allowed Ameritech Illinois to recover other wholesale related costs from wholesale resellers. These include wholesale advertising, maintenance, administrative and shared costs as well as uncollectible expenses. (Id. (citing Order in Dockets 95-0458/0531 Consolidated at 31-34)). The Commission also took Ameritech Illinois' cost of providing service into account in its Orders establishing rates for the Company's various unbundled network element, interconnection, transport and termination services. (Id. (citing Order in Docket 96-0486)).

Intervenors' Positions

Several of the Intervenors take the position that a favorable Section 7-204(b)(1) finding cannot be made. First, Cook County argues that Ameritech Illinois' ability to continue to provide quality service will be threatened by a resource drain from the NLS, which is SBC's post-merger plan to engage in facilities-based, out-of-region entry into 30 of the 50 largest local exchange telecommunications markets throughout the country, and which contemplates roughly $2.5 billion of investment in such markets over a ten year period. It reiterates the 00S>24 service quality criterion problems as an issue to be addressed and points to other concerns also raised by Staff. It argues that there is little similarity between this merger and the PacTel merger in California, so that SBC and Ameritech cannot use the California service quality results to argue that service quality will improve here.

Second, Cook County claims that in California, the number of competitive service jobs, rather than regulated local exchange service jobs, rose. According to Cook County, the latter declined, which it contends also will happen here in Illinois. This leads Cook County to conclude that Ameritech Illinois' service quality will diminish post-merger. Like Staff, it argues that SBC's purported deceptive sales practices, as evidenced by complaints filed in California, will be imported into Illinois and diminish AI's ability to provide quality service.

CUB, too, claims that the merger will result in a degradation of the Company's service quality. It claims that certain post-merger marketing practices from California will be imported to Illinois as "best practices." It cites seven complaint proceedings brought before the CPUC -- involving optional feature packages, inside wiring plans, blocking for caller ID, lack of change authorization, use of sales quotes, and residential customer service deterioration -- as examples of problems from California that it forecasts will occur in Illinois post-merger. The AG expresses similar concerns about Ameritech Illinois' ability to maintain its service quality after the merger.

Together, the GCI argues the proposed merger raised concerns regarding network investment and modernization. (E.g. Cook County Br. At 9-13). GCI witness TerKeurst testified that it is essential that Ameritech Illinois make needed investment in its network to maintain the quality of basic exchange services and to upgrade the basic network infrastructure throughout its service territory so that all customers have access

to a reasonable array of new products and services. (TerKeurst Direct, GCI Ex. 2.0 at 12. Ms. TerKeurst is concerned that with the expiration of Ameritech Illinois' five-year infrastructure investment commitment contained in the company's Alternative Regulation Plan, Ameritech Illinois may reduce network upgrades and modernization. (Id. at 12-13). She points to the risks of the National Local Strategy, in particular, as a determinant that may constrain the Joint Applicants' ability to make needed investment in Ameritech Illinois' network. (TerKeurst Rebuttal, GCI Ex. 2.1 at 8-9). To ensure the merger does not harm network investment and modernization, she recommends the Commission impose a network investment requirement in order to protect Ameritech Illinois' quality of service to its customers. Specifically, she recommends the Commission require Ameritech Illinois to renew and extend the company's five-year network infrastructure modernization program. (TerKeurst Direct, GCI Ex. 2.0 at 13). Along with recommending renewal and extension of the five-year infrastructure modernization program, she recommends specific reporting requirements to ensure that investments needed to maintain the infrastructure are realized. (Id. at 13-14).

DSSA argues that there is a "digital divide" in the United States between those who are able to take advantage of rapid technological changes and those who are not. According to DSSA, this translates into poor and economically disadvantaged telecommunications customers not getting the best telecommunications service at the least cost. DSSA contends that the merger should not be approved until SBC/Ameritech commits to correct this problem.

Finally, CTCA argues against the merger for failure to meet the requirements of Section 704(b)(1), briefly re-making some of the same points argued by Staff and summarized above.

Commission Analysis and Conclusion

Section 7-204(b)(1) requires the Commission to determine whether the proposed reorganization will diminish Ameritech Illinois' ability to provide adequate, reliable, efficient, safe and least-cost public utility service. Significantly, this subsection focuses on whether the impact of the reorganization will "diminish" Ameritech Illinois' ability to provide certain aspects of service, not on whether the merger will improve or enhance those aspects.

Based on the record evidence, the Commission concludes that the Joint Applicants have met their burden of proof, presenting sufficient evidence for us to determine that the proposed merger will not diminish Ameritech Illinois "ability to provide adequate, reliable, efficient, safe and least-cost" service. Nevertheless, the Commission is concerned about the Joint Applicants' continuing commitment and ability to meet their duties regarding certain aspects of service associated with § 7-204(b)(1). Therefore, in order to protect the interests of Ameritech Illinois and its customers following the proposed reorganization, the Commission finds it necessary to adopt the voluntary commitments put forth by the Joint Applicants in this proceeding and to

impose certain additional conditions on the proposed merger, as described more fully below.

1. Network Infrastructure Investment

The Commission agrees with Staff and GCI that a factual foundation exists in the record to support their concerns regarding a possible reduction in the Joint Applicants' infrastructure investment in Ameritech Illinois' network following the merger. (See Staff Br. at 109-111; Cook County Br. at 9-13; CUB Br. at 61-63). The Commission shares the concerns of Staff and GCI that the significant capital investments the Joint Applicants will need to make in order to successfully implement their National Local Strategy present a credible threat to future network infrastructure investment in Illinois. (See TerKeurst Rebuttal, GCI Ex. 2.1 at 8-9; Toppozada-Yow Direct, Staff Ex. 3.00 at 44-46). The Joint Applicants describe the National Local Strategy as "a truly massive undertaking," requiring "billions of dollars in new spending," and project negative cumulative cash flows and earnings for nearly ten years. (Kahan Rebuttal SBC/Am. Ex. 1.1 at 57). As a consequence, financial pressures, both anticipated and unanticipated, from the National Local Strategy may constrain the Joint Applicants' ability to commit adequate capital to invest in Ameritech Illinois' network infrastructure. (See TerKeurst Rebuttal, GCI Ex. 2.1 at 8-9).

The Joint Applicants themselves acknowledge, in the context of discussing allocation of the cost savings from the merger, that Ameritech likely would be pressured to reduce investment in Illinois to achieve profitability goals in certain instances. (See Harris Rebuttal SBC/Am. Ex 4.1 at 47). The Commission believes that just as the Joint Applicants might be pressured to reduce costs to offset allocations of cost savings to ratepayers, they might be pressured to reduce investment in Ameritech Illinois' network to offset losses in cash flows and earnings due to the National Local Strategy. Thus, the Commission concludes that financial pressures from the National Local Strategy and sharing cost savings from the merger, alone, or in combination, may lead to inadequate investment in Ameritech Illinois' network, particularly in areas not subject to competitive pressures. Moreover, the Commission is concerned that existing SBC facilities in SBC service territories are currently less technologically developed than similar facilities in Illinois. (See Gasparin Direct, Staff Ex. 5.00 at 9-10). This technological imbalance between the companies' facilities may lead to increased investment in SBC service territory at the expense of investment in Ameritech Illinois' service territory.

a. Five-Year Network Investment and Modernization Program

To address these concerns, and pursuant to the Commission's authority under § 7-204(f), the Commission requires Ameritech Illinois to renew and extend its five year network infrastructure modernization program previously pledged by Ameritech Illinois in its Alternative Regulation Plan. (See TerKeurst Direct, GCI Ex. 2.0 at 12-14; Toppozada-Yow Rebuttal, Staff Ex. 3.01 at 46-47 (adopting GCI witness TerKeurst's recommendation). The five year extension of the previous network infrastructure investment commitment shall begin in year 2000, or in the first calendar year after the Joint Applicants have obtained all necessary governmental approvals for the merger, and shall total at least $3 billion, subject to adjustment by the Commission in a subsequent review of Ameritech Illinois' Alternative Regulation Plan. The network investment program the Commission requires here does not mandate a specific amount of investment each year, but rather provides Ameritech Illinois the flexibility to structure and apportion the total network investment over a five-year period. In fulfilling this requirement, Ameritech Illinois shall account for network investment expenditures in the same manner as described in its existing Alternative Regulation Plan.

In sum, given the concerns expressed by Staff and the GCI, which are shared by the Commission, we believe a network investment requirement is necessary to protect the interests of Ameritech Illinois and its customers. We conclude that requiring Ameritech Illinois to implement a five year network infrastructure modernization program will help ensure a modern, high-quality network providing exceptional service to all of Ameritech Illinois' customers, particularly those customers in geographic areas and customer classes that will not immediately benefit from anticipated competition in the local market.

Although the Joint Applicants point to SBC's pledge to "continue to invest capital necessary to support Ameritech's network consistent with it's [sic] past practices," the Commission observes that these commitments apply not just to Illinois, but to Ameritech's five-state service territory. (Kahan Direct SBC/Am. Ex. 1.0 at 16-17 & Attach. 5). As a consequence, SBC's voluntary commitment concerning future investment in *Ameritech's* network makes no specific commitment for investment in *Ameritech Illinois*' network.

In addition, the Commission is not persuaded by the Joint Applicants' suggestion that marketplace incentives provide them with sufficient motivation to ensure that Ameritech Illinois' network investment will be adequate following the merger. The Commission does not find the Joint Applicants' suggestion convincing or specific enough to allay its concerns in the critical area of network investment. Their suggestion assumes robust competition in all areas of Ameritech Illinois' service territory and to all customer classes—an assumption belied by the evidence of record. See Graves Direct Staff Ex. 4.00 at 18; Staff Br. at 10 (noting that Ameritech Illinois controls nearly 97 percent of the access lines in Illinois); Gebhardt Rebuttal SBC/Am. Ex 3.1 Proprietary Schedule 2 (indicating a figure slightly less than the percentage calculated by Staff). Nor does the record evidence suggest robust competition in all areas and to all

customer classes in the near term. Moreover, if, as the Joint Applicants maintain, the need to preserve Ameritech Illinois' customer base and to compete are "compelling incentives" to continued network investment, and that "regulatory impetus is not necessary to assure such infrastructure investment," then Ameritech Illinois should have little difficulty meeting or exceeding the level of network investment required here. (JA Reply Brief, at 74-75; see Kahan Rebuttal, SBC/Am. Ex. 1.1 at 13 (anticipating that SBC will need to make substantial capital investments in Illinois).

b. Annual Report Detailing Reported Investment

In addition to requiring Ameritech Illinois to implement a five-year network infrastructure modernization program, the Commission requires Ameritech Illinois to file an annual report detailing, for each reported investment, which of its products and services benefit from the investment made. The report must also identify the geographic area where each reported investment is made. The primary purpose of this reporting requirement is to allow the Commission to determine whether and how the network investment is made, whether the network investment serves to maintain the quality of Ameritech Illinois' network, and whether the network investments are in the interests of all of Ameritech Illinois' customer classes. The annual report is to be prepared by the Joint Applicants and will be examined and audited by the Commission with the assistance of an independent third party selected by the Commission and paid for by the Joint Applicants. Each report must be certified to be true by the SBC/Ameritech corporate compliance offices employed by the Joint Applicants as specified in Part VI of this Order, and expressly accepted by the Commission. If the Commission rejects a submitted report, the Joint Applicants must provide any necessary information requested by the Commission to satisfy the report's shortcomings. The report must be filed each year for five years; however, the reporting requirement can be eliminated, upon application (or by the Commission on its own motion), if the Joint Applicant's have fulfilled the network infrastructure investment requirement before the end of the five-year period and the Commission finds the reporting requirement no longer necessary to protect the interests of Ameritech Illinois and its customers.

2. Out of Service Greater than 24 Hours ("OOS>24")

The Commission's rules for standards of service applicable to a local exchange carrier's noncompetitive telecommunications services are set forth in 83 Illinois Administrative Code § 730. In particular, the Commission has established a standard for restoring interruptions of service. As a general rule, a local exchange carrier must restore no fewer than 95 percent of service interruptions no later than 24 hours after the time such troubles are reported, except when service interruptions are caused by emergency situations or natural disasters affecting a large number of customers. (Id. § 730.535(a)). The stringent OOS>24 service standard reflects the critical role reliable telephone service plays in our daily lives and the Nation's economy and, unsurprisingly, is of considerable importance to the Commission and telephone subscribers. When telephone service is interrupted, subscribers are often unable to contact family, friends,

police, and emergency personnel, among others. In addition to the inconvenience experienced caused and health and safety implicated by service interruptions, commercial customers may suffer lost sales and revenues as their customers or potential customers are unable to reach them.

In 1994, as part of Ameritech Illinois' Alternative Regulation Plan, the Commission adopted a service quality component and incorporated it in the price index formula. Alternative Regulation Plan Order, at 58. The service quality component consists of eight separate measures for tracking and monitoring the company's service quality. Id. Each measure is accorded equal weight in calculating the service quality component. Id. For each measure, Ameritech Illinois receives an annual score of zero if it meets or exceeds the relevant benchmark and -.25% if it fails to meet the relevant benchmark. Id. A negative service quality component in one year reduces the price cap index in the following year, which in turn reduces the amount rates may be increased for services subject to the Alternative Regulation Plan. In adopting the service quality component, the Commission recognized that "one of the theoretical risks of price regulation is that [Ameritech Illinois] may, while seeking to maximize its income, reduce expenditures in certain areas in such manner as to impact service quality adversely." Id. The Commission further noted that "[t]his is especially true for residential services which are the most inelastic services and are unlikely to be exposed to competitive pressures in the near term." Id. One of the eight service quality measures, relevant here, is the percentage of service interruptions restored within 24 hours. (Id. at Appendix A, at 5; Gebhardt Direct, SBC/Am. Ex. 3.0 at 6).

Staff and several intervenors express concerns regarding the proposed merger's effect on Ameritech Illinois' ability to meet the OOS>24 requirement and recommend adjusting the service quality component in the Alternative Regulation Plan to induce Ameritech Illinois to meet the OOS>24 requirement. (Staff Br. at 101-08; CUB Br. at 67; AG Br. at 46-48). Ameritech Illinois' continual failure to meet the OOS>24 standard has been the subject of great concern for the Commission. From 1995 through 1998, Ameritech Illinois' OOS>24 rate averaged 14 percent per year, nearly three times the permitted level. (McClerren Direct, Staff Ex 8.00 at 11; Ameritech Illinois Annual Rate Filing For Non-Competitive Services Under an Alternative Form of Regulation, ICC Docket 99-0185 (filed Apr. 1, 1999) (reporting an OOS>24 rate of 13.9 percent for 1998)).[1] Ameritech Illinois' failure to meet the mandatory service quality standard has adversely affected literally hundreds of thousands of its customers in the most critical way—by disabling their phone service for an extended, unacceptable period of time.

The Joint Applicants acknowledge that OOS>24 is "a long recognized" problem persisting for many years, but contend that the OOS>24 problem is not a merger problem because the problem relates to past performance and thus predates the proposed merger. (JA Br. at 11, 25; JA Reply Br. at 71-72). In other words, according to the Joint Applicants, since Ameritech Illinois has repeatedly failed to meet the OOS>24 requirement month after month, year after year before the proposed merger,

[1] Pursuant to § 200.640(a) of its Rules of Practice, the Commission takes administrative notice of Ameritech Illinois' Annual Rate Filing in Docket 99-0185.

the problem could not result from the merger and, therefore, is not an appropriate basis of inquiry under § 7-204(b)(1). The Commission rejects this contention. First, to the extent the Joint Applicants suggest that existing substandard service, in and of itself, falls outside the ambit of review under § 7-204(b)(1), the Commission rejects this suggestion. The plain language of § 7-204(b) applies to a public utility's service and does not exclude a company's provision of substandard service from review. Indeed, a reading of § 7-204(b) that excluded substandard service would lead to the bizarre conclusion that a company already providing inferior service could insulate such service from Commission review and likely encourage companies to begin providing inferior service in anticipation of a merger.

Second, and more basic, the Joint Applicants' contention ignores the obvious fact that existing problems can be made worse. For example, Ameritech Illinois has repeatedly failed to meet the OOS>24 standard, averaging about 14 percent OOS>24 over the past four years, and the proposed merger may, in fact, worsen the company's already poor track record as outlined in the previous discussion. Third, and particularly relevant here, the merger may impede Ameritech Illinois' efforts to comply with the OOS>24 standard. Although the Joint Applicants indicate that Ameritech Illinois has taken measures to improve its OOS>24 performance, including a "complete review" of repair performance, "with particular emphasis on OOS>24," the Commission observes that the company nevertheless failed to meet the standard in 1998 and the proposed merger may, in fact, constrain the company's efforts to comply with the standard in the future. (See Galloway Direct, SBC/Am. Ex. 8.0 at 6-7).[2]

The Commission believes that if Ameritech Illinois fails to focus sufficient attention on and devote the necessary resources to meeting the OOS>24 standard the merger may constrain the company's ability to meet the standard or exacerbate what is already an intolerable service problem. As the Commission noted earlier in its discussion of network infrastructure investment, *supra* at Section III.B.1, the Joint Applicants will need to make significant capital investments in order to successfully implement their National Local Strategy. Consequently, financial pressures, both anticipated and unanticipated, from the National Local Strategy may constrain the Joint Applicants' ability to allocate the necessary resources to meet the OOS>24 requirement or prevent further increases in the percentage of customers whose service is not restored within 24 hours.

The Commission is also concerned that the Joint Applicants have announced cost savings in the area of provisioning and maintenance of operations should the reorganization be approved, without identifying, other than in general terms, where

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[2] The Commission also rejects the Joint Applicants request that the OOS>24 issue be addressed in other pending Commission dockets, specifically dockets 98-0252 and 98-0453. (JA Br. on Exceptions, at 11-12). Their request overlooks the Commission's statutory role under § 7-204 and, as the Commission's discussion in this section makes evident, avoids the effect of the merger on the OOS>24 issue. Ameritech has a duty to comply with the Commission's standards of service rules and the company's Alternative Regulation Plan, approved under § 13-506.1 of the Act, and the proposed merger may adversely affect its ability to do so.

these cost savings would be achieved. Although the Joint Applicants indicate generally that the companies will adopt "best practices," to achieve the cost savings, the Commission cannot determine which specific "best practices," if any, will be adopted in Illinois and, consequently, cannot conclude whether those practices are in the interests of Ameritech Illinois and its customers. See *infra*, Section III.B.5. In addition, as the Joint Applicants have acknowledged in discussing sharing costs savings from the merger with ratepayers, Ameritech's service quality might be constrained by reducing costs to achieve profitability goals in certain instances. (See Harris Rebuttal SBC/Am. Ex. 4.1 at 47).

Furthermore, the Commission notes that there is information in the record regarding Ameritech Illinois' acquisition of Central Illinois Telephone Company's assets and the resulting level of service quality experienced by customers in Centel's former exchanges. (See McClerren Direct, Staff Ex. 8.00 at 12-13, 15; McClerren Rebuttal, Staff Ex. 8.01 at 13; Galloway Direct, SBC/Am. Ex. 8.0 at 7-10). The Commission is concerned that the Centel asset purchase, while different from the nature and scope of this transaction, further demonstrates the difficulty Ameritech Illinois has in focusing upon certain facets of service quality when undertaking even a relatively small acquisition. The Commission anticipates that the Joint Applicants' proposed reorganization will require substantially greater resources to manage and integrate all areas of operation than either SBC or Ameritech alone has experienced in past acquisitions.

In view of the foregoing, the Commission finds that Ameritech Illinois' continual failure to satisfy the OOS>24 standard, coupled with financial pressures from the National Local Strategy, announced cost savings from provisioning and maintenance, sharing cost savings with customers, or in combination, may constrain the company's efforts to meet the OOS>24 requirement. (See TerKeurst Rebuttal, GCI Ex. 2.1 at 20-21). Consequently, the Commission concludes that the Joint Applicants must be given further incentive to focus on the OOS>24 problem. Accordingly, to ensure that the Joint Applicants continue Ameritech Illinois' efforts to meet the OOS>24, the Commission finds it necessary to impose a condition pursuant to its authority under Section 7-204(f) on the merger to protect the interests of Ameritech Illinois and its customers.

Ameritech Illinois' repeated failure to meet the OOS>24 service standard, however, suggests that the existing service quality mechanism in the Alternative Regulation Plan does not provide an adequate incentive for the company to comply with the standard. The record indicates that Ameritech Illinois' failure to meet its service quality obligation is caused, at least in part, by its perception that it is more cost effective to reduce rates pursuant to the service quality component of the price index formula than it would be to allocate the necessary resources to satisfy the OOS>24 service standard. For example, Ameritech Illinois witness Gebhardt testified on cross-examination that $30 million was the approximate annual expenditure needed to

comply with the OOS>24 standard.[3] In contrast, under its Alternative Regulation Plan, the company's cost of failing to meet the OOS>24 service quality measure has been an annual rate reduction of approximately $2.5 to $ 4 million. (JA Br. on Exception, at 12; McClerren Rebuttal, Staff Ex. 8.01 at 12 (indicating a rate reduction from $2.5 to $4 million per year); Tr. 1383 (cross examination of GCI witness TerKeurst) (noting that the annual rate reduction has declined from approximately $4 to $2.5 million as noncompetitive services are classified as competitive and removed from the Alternative Regulation Plan)). Therefore, given that the proposed merger places additional pressures on the Joint Applicants' resources as discussed above, and given Ameritech Illinois' treatment of this service quality issue on a cost-benefit basis, the Commission finds that in order to protect the interests of Ameritech Illinois and its customers the Joint Applicants must, as a condition of the merger, be provided with an additional incentive for meeting the OOS>24 standard separate and apart from the service quality component incorporated in the price index formula of Ameritech Illinois' Alternative Regulation Plan.[4]

The Commission finds that imposing a condition that relates to Ameritech Illinois' avoided cost of meeting its service quality obligations should eliminate the company's current cost incentive not to meet the OOS>24 standard. Accordingly, and pursuant to its authority under § 7-204(f), the Commission requires the Joint Applicants to demonstrate to the Commission, within six (6) months[5] after obtaining all necessary regulatory approvals and closing the merger, that Ameritech Illinois is in compliance with the OOS>24 service standard. The Joint Applicants shall demonstrate compliance in the same manner currently used by the Commission and Ameritech Illinois to measure the company's compliance with the OOS>24 service standard. If, after notice and hearing, the Commission determines that the Joint Applicants have not demonstrated that Ameritech Illinois is in compliance with the OOS>24 service standard during the last month of the six month period, the Commission shall assess a $15 million penalty ~~fine~~ ($30 million x 50%), separate and apart from any annual rate reduction resulting from the service quality component of the company's Alternative Regulation Plan.

In subsequent full calendar year periods (including calendar year 2000), the Joint Applicants shall demonstrate compliance in the same manner currently used by the Commission and Ameritech Illinois to measure the company's compliance with the

[3] Mr. Gebhardt testified on cross examination that in order to meet the OOS>24 standard under current productivity levels, the company would need to spend about $30 million (300 additional technicians at an average of $100,000 per year). (Tr. 817).

[4] Although we decline to adopt Staff's and GCI's recommendation in this proceeding, we express no opinion here and leave open the question whether their recommendation should be adopted in docket 98-0252 as part of our five-year review of the Alternative Regulation Plan. Alternative Regulation Plan Order, Appendix A at 10.

[5] The six month period begins to run in the first full calendar month following all necessary approvals and close of the merger. Thus, for example, if the Joint Applicants receive all necessary regulatory approval and close the merger on November 15, 1999, the six month period begins to run on December 1, 1999.

OOS>24 service standard or face a one-time, $30 million assessment, separate and apart from any annual rate reduction resulting from the service quality component of the company's Alternative Regulation Plan.[6] The penalties, if assessed, are to be credited to Ameritech Illinois' customers. Ameritech Illinois shall allocate the credit among customer classes (residential, small business, and large business) based on the percentage of lines OOS>24 in each class. For example, suppose that in the six-month reporting period Ameritech Illinois failed to restore 100,000 out of service lines within 24 hours. Suppose further that of the 100,000 lines, 50,000 were residential lines, 30,000 were small business lines, and 20,000 were large business lines. In calculating the credit, Ameritech Illinois would allocate the amount as follows: $7.5 million ($15 million x 50%) to all residential customers, $4.5 million (15 million x 30%) to all small business customers, and $3 million ($15 million x 20%) to all large business customers. The Commission believes that this approach is a reasonable method of apportioning the credit and does not favor one particular class over another.

The condition the Commission imposes here is designed to ensure that the Joint Applicants focus on the OOS>24 problem and devote the necessary resources to meeting the standard. The Commission has attempted to craft a condition that equates Ameritech Illinois' estimated costs of complying with the OOS>24 standard with the company's costs in avoiding it. The Commission believes that the condition is fair, protects Ameritech Illinois and its customers from risks resulting from the merger, and provides the necessary incentive to comply with the OOS>24 standard. Furthermore, the condition shall last no longer than necessary to secure and ensure compliance and protect Ameritech Illinois and its customers, and shall remain in place for each succeeding year until expressly eliminated by the Commission.

3. National Local Strategy

The Commission finds unpersuasive several intervenors' concerns regarding the possible depletion of Ameritech Illinois' personnel to support the National Local Strategy and the need for conditions or remedies to ameliorate any potential dimunition in the quality of service in Illinois. The GCI, for example, argues that the proposed merger will result in the relocation of Ameritech Illinois' experienced managers and other key personnel outside Illinois to support SBC's National Local Strategy. (Cook County Brief, at 13-16; AG Brief, at 28-30; CUB Br. at 60-61). In turn, the Intervenors contend, this loss of talent will lead to service quality deterioration in Illinois as lesser-qualified personnel are left to run Ameritech Illinois' business. (Cook County Br., at 13-14; AG Brief, at 30; CUB Br. at 60).

As mentioned earlier, to meet the requirements of § 7-204(b)(1), the Joint Applicants need only demonstrate that the proposed merger will not diminish Ameritech Illinois' ability to provide service quality, regardless of the Joint Applicant's ultimate allocation of its human resources, which is an internal company decision. The Joint

[6] The Commission notes that if Ameritech Illinois fails to comply within the six month period and the full calendar year 2000, and the timeframes overlap in year 2000, the $30 million assessment will be pro rated to avoid double counting.

Applicants commit that Ameritech Illinois will continue to be operated, where possible, by its current management team. The record reflects that SBC intends to draw upon the resources of both SBC and Ameritech, as well as new hires, to implement the National Local Strategy. (JA Reply Br. at 76; TerKeurst Direct, GCI Ex. 2.0 at 15-16). The record also reflects that the Joint Applicants anticipate the merger will result in duplication of employment responsibilities between the companies, thus making available experienced SBC and Ameritech Illinois managers to staff the National Local Strategy without any dimunition in Ameritech Illinois' service quality. (Jennings Rebuttal, SBC/Am. Ex. 5.0 at 15-16). The Commission cannot conclude from the evidence of record that using Ameritech Illinois personnel to staff the National Local Strategy will diminish Ameritech Illinois' quality of service.

GCI's general focus on employment levels as a reliable indicator of service quality is misplaced. The argument is premised on the unsupported assumption that decreases in employee levels result in decreases in service quality. But a decrease in employment levels does not lead, necessarily, to a decrease in service quality, and GCI witness TerKeurst admits as much when discussing efficiency savings. (TerKeurst Direct, GCI Ex. 2.0 at 17. In any event, GCI presents no persuasive evidence that a positive correlation between the two exists here.

Furthermore, the intervenors offer no evidence that even if SBC were to redeploy key Ameritech Illinois personnel to pursue the National Local Strategy, the remaining personnel (and new hires) would be less qualified to manage Ameritech Illinois' business effectively, much less cause a dimunition in service quality. While the Commission will continue to monitor Ameritech Illinois' service quality after the merger, the Commission finds that the Joint Applicants will adequately allocate managerial and other key personnel so as not to diminish service quality in Illinois. Accordingly, the Commission finds it unnecessary to impose conditions on the merger which would mandate staffing, hiring, or relocation policies of the new company concerning the National Local Strategy.

4. 9-1-1 Service

Next, the Commission turns to the issue of the proposed merger's impact on the quality of Ameritech Illinois' 9-1-1 system. The integrity and reliability of Illinois' 9-1-1 systems is of paramount concern to this Commission. Quite literally, the safety of all Illinois citizens depends on their ability to access emergency personnel quickly, accurately, and reliably.

The Commission agrees with Staff that the proposed merger raises concerns about Ameritech Illinois' post-merger provision and maintenance of 9-1-1 service that must be addressed. There is credible evidence that the merger may lead to a reduction in the quality of Ameritech Illinois' 9-1-1 service. Staff identified various operational differences between the Joint Applicants' 9-1-1 systems, including differences in billing systems and databases. (Prather Direct, Staff Ex. 6.00 at 3-5). Staff concluded that

integrating or standardizing the different polices, procedures, and systems could adversely affect Ameritech Illinois' 9-1-1 system.(Prather Rebuttal, Staff Ex. 6.01 at 2).

The Joint Applicants did not specifically address these operational differences, much less allay the concerns identified by Staff. Instead, the Joint Applicants stated generally that they will not implement changes in 9-1-1 service that would adversely affect delivery of 9-1-1 service: Significantly, however, they conceded that "no post merger planning between SBC and Ameritech has taken place" regarding delivery of 9-1-1 service in Illinois. (Kahan Rebuttal, SBC/Am. Ex 1.1 at 31). Moreover, the Joint Applicants have indicated that after the merger the new company will review its practices and procedures and adopt, where appropriate, the "best practices," which may lead to operational changes in Ameritech Illinois' 9-1-1 system. (Prather Direct, Staff Ex. 6.00, Attach. 1d).

As a consequence, given Staff's concerns regarding the operational differences between the Joint Applicants' 9-1-1 systems and the lack of substantive information provided by the Joint Applicants regarding post-merger plans for Ameritech Illinois' 9-1-1 system, the Commission concludes that the proposed merger may have an adverse affect on the safety, reliability, and service quality of Ameritech Illinois' 9-1-1 system if the Joint Applicants were to implement changes to the current system.

In order to protect the public interest and ensure the safety, reliability, and quality of Ameritech Illinois' 9-1-1 system, the Commission finds it necessary to impose the following condition on the merger using its authority under § 7-204(f). The Commission requires that the new company obtain Commission approval before implementing operational changes to Ameritech Illinois' current 9-1-1 system attributable to or in connection with the proposed merger, including, but not limited to changes in policies, processes, and procedures associated with 9-1-1 billing systems and databases. In addition, the Commission requires that operational changes be transparent to both the 9-1-1 system and its subscribers.

The Commission, however, will not go so far as to adopt Staff's condition requiring the Joint Applicant's to obtain Commission approval for any proposed reduction or removal of 9-1-1 personnel in Illinois. The Joint Applicants have committed to advising Staff prior to reducing or reassigning Ameritech Illinois' 9-1-1 staff. (E.g., Gebhardt Rebuttal, SBC/Am. Ex. 3.01 at 105; Kahan Surrebuttal, SBC/Am. Ex. 1.2 at 6). The Commission believes this process strikes a reasonable balance and allows Staff to identify and raise any concerns that might warrant further investigation by the Commission. In reviewing Ameritech Illinois' 9-1-1 staffing needs, we fully expect the new company to exercise prudent management practices and refrain from taking action that might compromise the integrity and reliability of the 9-1-1 system in Illinois.

5. "Best Practices"

SBC uses the term "best practices" to refer to "the best ideas and practices developed through years of experience by the telephone and wireless subsidiaries of

four different companies—SBC, Ameritech, Telesis and SNET—in addition to ideas developed though working with numerous foreign carriers." (TerKeurst Direct, GCI Ex. 2.0 at 5 n.1 (citing Merger of SBC Communications Inc. and Ameritech Corporation, Description of the Transaction, Public Interest Showing and Related Demonstrations (FCC Merger Filing), filed with the FCC, July 24, 1998, at 46)). GCI recommends that the Commission require Ameritech Illinois to report details regarding any proposed "best practices" whose adoption by SBC or any of its affiliates would affect the provisioning of intrastate telecommunications service. (TerKeurst Direct, GCI Ex. 2.0 at 34). Specifically, GCI witness TerKeurst recommends that "[a]mong other things, Ameritech Illinois should report how each such 'best practice' would affect costs, revenues, employment, service quality, marketing, competition, and the ability of the Commission to monitor and regulate intrastate telecommunications service." (TerKeurst Direct, GCI Ex. 2.0 at 34; see AG Br. at 46). The Joint Applicants have committed to providing a confidential annual report identifying any proposed best practices whose adoption by SBC or its affiliates would affect the provisioning of intrastate telecommunications in Illinois, for a period of up to three years. (JA Br. at 17; JA Reply Br. App. B at 11). The Commission adopts GCI's recommendation as a condition of the merger.

The Commission concludes that a 5-year reporting period (3 years mandatory, 2 years conditional, as described more fully below), beginning upon final regulatory approval of the merger, is necessary to protect the interests of Ameritech Illinois and its customers. See 5/7-204(f). The record reveals that the Joint Applicants' have given equivocal responses to questions about which "best practices" Ameritech Illinois will adopt after the merger. On one hand, SBC lists a number of "best practices" that will be made available to Ameritech Illinois after the merger. (Kahan Direct, SBC/Am. Ex. 1.0 at 16; Jackson Direct, Staff Ex. 7.00 at 11 & att. 4). On the other hand, however, the Joint Applicants claim that they do not know which SBC practices Ameritech Illinois will adopt. (Jackson Direct, Staff Ex. 7.00 at 8 & Attach. 5.). As a result, the Commission cannot determine which specific practices, if any, will be adopted in Illinois and, therefore, cannot conclude whether those practices are in the interests of Ameritech Illinois and its customers. In addition, the Commission believes that implementation of "best practices" in Illinois will likely extend beyond the Joint Applicants' three-year voluntary commitment. (See AG Reply Br. at 10).

The main purpose of the "best practices" reporting requirement is to assist the Commission in monitoring changes in Ameritech Illinois' practices resulting from the merger and to determine whether any proposed "best practices" are in the interests of Ameritech Illinois and its customers. It will also ensure that any "best practices" adopted in Illinois are consistent with Illinois law and the Commission's rules and orders. Therefore, the Commission finds that a 5-year reporting requirement strikes a reasonable balance between the Commission's need to monitor implementation of any proposed "best practices" and the Joint Applicant's interest in lessening the burden of reporting requirements.

The "best practices" report should be filed in the same manner as other annual reports required in this proceeding, and will be subject to the same review process. The annual report is to be prepared by the Joint Applicants and will be examined and audited by the Commission, with the assistance of an independent third party selected by the Commission and paid for by the Joint Applicants. The report must be filed each year for five years; however, the reporting requirement can be eliminated after three years, upon application (or by the Commission on its own motion), if the Commission finds the reporting requirement no longer necessary to protect the interests of Ameritech Illinois and its customers. Each report must be certified to be true by the SBC/Ameritech corporate compliance office employed by the Joint Applicants as specified in Part VI. of this Order, and expressly accepted by the Commission. If the Commission rejects a submitted report, the Joint Applicants must provide any necessary information requested by the Commission to satisfy the report's shortcomings.

6. Misleading or Deceptive Sales and Marketing Practices

Several parties and Staff express concern about SBC's sales and marketing practices in California. Relying chiefly on several complaints filed against SBC at the California Public Utilities Commission ("CPUC") alleging improper sales and marketing practices, they are concerned that the new company will adopt and implement similar sales and marketing practices in Illinois, which, they contend, will lead to decreased service quality. (Cook County Br., at 20-22; CUB Br., at 54-59; AG Reply Br. at 8-11). In light of its concerns, and should the Commission approve the merger, Staff asks the Commission to prohibit SBC from adopting deceptive marketing practices in Illinois. (Staff Br. at 99). In response to these concerns, Joint Applicants consider the California complaints to be without merit and irrelevant to this proceeding. (Smith Rebuttal, SBC/Am. Ex. 6.0 at 24; JA Reply Br. at 68-71).

The Commission believes Staff's and GCI's concerns regarding potentially misleading or deceptive sales and marketing practices are relevant to the Commission's inquiry in this proceeding. The Joint Applicants have identified SBC's marketing programs and practices, among other things, as "best practices" that will be made available to Ameritech Illinois. (Kahan Direct, SBC/Am. Ex. 1.0 at 16; Jackson Direct, Staff Ex. 7.00 at 11 & Attach. 4). At the same time, however, the Joint Applicants indicate that they "have not yet evaluated the practices of each company for the purposes of identifying 'best practices' and, therefore,…do not know which such practices of SBC Ameritech will adopt." (Jackson Direct, Staff Ex. 7.00 at 8 & Attach. 5.). Given the Joint Applicants' equivocal responses, their stated post-merger plans regarding marketing practices are at best uncertain and, at worst, contradictory. Regardless, SBC's sales and marketing practices in other states, and whether SBC will import such practices to Illinois, are matters clearly relevant to the Commission's inquiry here.

The Commission will not tolerate misleading, deceptive, or otherwise improper sales and marketing practices by telecommunications carriers in Illinois. The

Commission specifically notes that implementation of misleading, deceptive or improper marketing practices in Illinois would diminish Ameritech Illinois' ability to provide reliable service to its customers. In addition, such practices would likely violate Illinois law and Commission rules. Furthermore, if Ameritech Illinois employs marketing practices that mislead, deceive or are otherwise improper, and its conduct is found to violate Illinois law, this Commission will not hesitate to penalize the company to the fullest extent permissible by law.

The allegations of misleading and deceptive sales and marketing practices pending against SBC before the CPUC give this Commission pause, as they represent practices SBC may bring to Ameritech Illinois' service territory. Although the Commission finds the number and character of allegations in the California proceedings somewhat troubling, it is mindful, however, that the allegations are unproven and have not been found to violate California law. In addition, whether or not the allegations are eventually sustained, the Commission is not convinced that SBC would consider the alleged misleading marketing practices to be "best practices" suitable for implementation in Illinois, especially given the substantial opposition from consumer groups in California such practices have engendered. Lest it be misunderstood, the Commission takes allegations of marketing abuses to customers very seriously and stands ready to act, upon complaint or its own motion, to eliminate such practices and prevent future abuses.

That said, however, the Commission finds it unnecessary to adopt conditions specifically prohibiting certain marketing practices by Ameritech Illinois in this proceeding. The Commission believes the IPUA, Commission rules, and other laws are adequate to guard against misleading, deceptive, or otherwise improper sales and marketing practices by telecommunications carriers in Illinois. See, e.g., 220 ILCS 5/9-250 (requiring company practices to be just and reasonable); § 5/13-902 (listing rules for verifying subscriber's carrier change and service additions). Moreover, as mentioned earlier, the Joint Applicants are required to inform the Commission of all proposed "best practices," including sales and marketing practices, the adoption of which affect the provision of telecommunications in Illinois. This requirement will allow the Commission to monitor changes in Ameritech Illinois' marketing practices that result from the merger.

In sum, although the concerns of Staff and GCI regarding SBC's sales and marketing practices in California are relevant to the Commission's inquiry here, we do not find it necessary to prohibit specific marketing practices by Ameritech Illinois. The Commission believes adequate safeguards exist under Illinois law to protect Ameritech Illinois' customers from marketing abuses. In addition, the Commission will monitor all proposed "best practices through the reporting requirement imposed in this proceeding. If marketing abuses nonetheless occur, however, the Commission will not hesitate to take appropriate remedial action.

7. Improvements to Service for Disabled and Economically Disadvantaged Customers

Several parties and Staff request that the Commission condition the merger on improving services to particular customers or improving access to technology for certain groups. Staff recommends the Commission condition approval of the merger on SBC's advancement of service quality to persons with disabilities. (Staff Br. at 99-101; Jackson Rebuttal, Staff Ex. 7.01 at 8-10). Similarly, DSSA requests the Commission condition approval of the merger on SBC's implementing DSSA's plan to address the "digital divide" in Illinois. (DSSA Br. at 2).

The Commission notes, however, that these requests to secure improved services for Ameritech Illinois' disabled and economically disadvantaged customers do not directly relate to any diminishment of Ameritech Illinois' ability to provide adequate, reliable, efficient, safe, and least-cost public utility service.

a. Commitments to Persons with Disabilities.

SBC has committed to using its research and development subsidiary, TRI, to assess the needs of disabled customers and provide them with improved services and functionalities when accessing telecommunications services. (Kahan Surrebuttal, SBC/Am. Ex. 1.2 at 7). In addition, it has committed to implementing in Illinois its Universal Design Policy, a goal of which is to "make new telecommunications products and services accessible to and usable by individuals with disabilities." (Jackson Direct, Staff Ex. 7.00, Attach. 11; Kahan Surrebuttal, SBC/Am. Ex. 1.2 at 7; see generally JA Reply Br. at App. B. (proposed conditions 9 and 10)). The Commission believes SBC's commitments address Staff's concerns and offer substantial benefits to Ameritech Illinois' disabled customers as a result of the merger.

b. Commitments to Improve Access to Advanced Technology.

SBC has committed to establishing a Community Technology Fund and will make $1 million available to the Fund for disbursement by Ameritech Illinois in each of three consecutive 12-month periods following the date the Fund is established, for a total of $3 million. According to SBC, the Fund will be dedicated to uses which help assure that rural and low income communities in Illinois have access to advanced telecommunications technology, including expenditures for computer equipment and associated software, Ameritech tariffed services, Internet access, technical support, and other associated services and equipment in rural and low income communities. (Kahan Direct on Reopening, SBC/Am. Ex. 1.3 at 28-29). SBC also has committed to providing funding of $1.45 million over three years to support a Community Computer Center. (Id. at 29). Further, SBC commits that if ADSL service is offered as a service to residence customers in any Ameritech Illinois central office, then ADSL service will be offered to residence customers in any other Ameritech Illinois central office where ADSL is subsequently deployed. (Id. at 29-30). SBC commits that any deployment of ADSL in Illinois will be done in good faith in a non-discriminatory fashion without excluding any particular area of the Ameritech Illinois service area. (Id.).

In addition to commitments made by SBC, the Commission notes that Illinois elementary and secondary schools, libraries, and rural health care providers may be eligible for universal service support. Specifically, eligible Illinois schools and libraries can receive discounts ranging from 20 percent to 90 percent on telecommunications services, internet access, and internal connections. See 47 C.F.R. §§ 54.500-517 (1998); 83 Ill. Admin. Code 765.10 (adopting the FCC's discount matrix and making available discounts for intrastate services). Furthermore, several telephone assistance programs are available in Illinois to help ensure the availability of affordable telecommunications service to all persons, particularly those with low incomes. The federally-funded Link-Up and Lifeline Connection Assistance ("Lifeline") programs assist eligible subscribers with installation costs for new telephone service and monthly local service charges, respectively.[7] Also, the Universal Telephone Assistance Program, funded by voluntary contributions from Illinois telephone customers, provides supplemental assistance to individuals receiving assistance from Link Up and Lifeline. See generally 83 Ill. Admin. Code Part 757. The Commission strongly encourages eligible entities and individuals to participate in these programs.

8. Least Cost

Section 7-204(b)(1) requires that the Commission determine that the proposed reorganization will not diminish the utility's ability to provide least-cost service. The Commission is able to reach such a finding based on the record evidence. Specifically, the record shows that the proposed merger will result in cost savings to Ameritech Illinois. Consequently, the Company's ability to provide least-cost service is not diminished.

The Commission does not accept the argument by Staff that the proposed reorganization will widen the gap between costs and prices and thereby adversely affect the Company's ability to provide least-cost service following the merger. Staff's interpretation of the statute is overly broad. Moreover, Staff's interpretation does not adequately consider the Commission's intent in enacting Alternative Regulation for Ameritech Illinois. The Commission approved an Alternative Regulation Plan for Ameritech Illinois in 1994 which encouraged the Company to reduce costs and to become more efficient. The Alternative Regulation Plan is currently under review by the Commission as required by the originating Order. The relationship between costs and prices is better treated in the context of the ongoing five year review of the Company's Alternative Regulation Plan.

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[7] Link Up is a federally funded program that assists eligible households by contributing 50 percent, up to a maximum of $30, of the cost of installing local telephone service in principal residences. Lifeline is a federally funded program that helps defray the costs of telephone service, providing $5.25 (through discount of $1.75 and waiver of $3.50 federal subscriber line charge) towards the monthly charge for local telephone service. Earlier this year, the Commission authorized additional assistance under the Lifeline program. Through a combination of state support through the Universal Telephone Assistance Program and federal matching funds, eligible subscribers can now receive a credit of up to $7.50 on their local telephone bill. In re Universal Telephone Assistance Corporation, Petition for Determination of the Amount and Form of Supplemental Assistance to Be Provided by Local Exchange Carriers, Pursuant to 83 Ill. Adm. Code § 757.200, ICC docket No. 98-0884, Order (Apr. 21, 1999).

C. Whether The Proposed Reorganization Will Result In The Unjustified Subsidization Of Non-utility Activities By The Utility Or Its Customers; And, Whether Costs And Facilities Are Fairly And Reasonably Allocated Between Utility And Non-utility Activities In Such A Manner That The Commission May Identify Those Costs And Facilities Which Are Properly Included By The Utility For Ratemaking Purposes. (Sections 7-204(b)(2) & (3)).

Joint Applicants' Position

Joint Applicants contend that the record evidence establishes that the proposed reorganization will not result in any subsidization of non-utility activities by AI or its customers. In support of their position, they assert that regulatory and cost allocation procedures currently in place ensure that the merger will not result in such unjustified subsidization. For instance, the Commission has cost allocation procedures that will prevent such subsidization of non-utility activities by the regulated operations of AI post-merger. Additionally, it has adopted implementation processes that ensure "non-utility activities" are not allocated to its regulated operations. Its long-standing accounting procedures remove unregulated investments and expenses from its regulated operations. Joint Applicants assert that AI's implementation processes are an adequate defense against subsidization because they have been reviewed in numerous past rate cases, attested to annually by outside auditors, and examined regularly by the FCC. They argue that, because AI will continue to follow the same procedures and continue to be subject to these same regulatory constraints after the merger, there will be no subsidization resulting from the merger. (Gebhardt Direct, SBC/Am. Ex. 3.0 at 8-10; Kahan Direct, SBC/Am. Ex. 1.0 at 31-32) (SBC/Am. Init. Br. at 71-74.)

Mr. Gebhardt points out that, because Ameritech Illinois will continue to exist as a legal entity, the principal change resulting from the merger is that certain SBC holding company costs incurred in managing Ameritech will be allocated to AI, largely in substitution for comparable Ameritech holding company costs that are incurred today. Joint Applicants argue that the same allocation methodologies established by the Commission that are used to separate Ameritech utility from non-utility costs today will be applied to the new SBC holding company costs. These costs then will be further allocated using existing procedures to determine AI's regulated intrastate costs. They argue that these procedures provide assurance that the merger will not result in cross-subsidization. (Gebhardt Direct, SBC/Am. Ex. 3.0 at 8-10; Kahan Direct, SBC/Am. Ex. 1.0 at 31-32).

Staff's Position

Staff believes that Ameritech has been following and will continue to follow the Commission's rules regarding common cost allocation and affiliate transactions. (Staff Init. Br. at 199). Staff, however, questions whether current safeguards may be sufficient to guard against cross-subsidization in the future. Staff makes several

recommendations that it believes are necessary to verify charges and allocations, and to protect against cross-subsidization in the future. Staff asserts that the Commission cannot make the requisite finding under Sections 7-204(b)(2) and (3) without imposing its recommended conditions. (Marshall Direct, Staff. Ex. 1.00 at 12-15; Marshall Rebuttal, Staff Ex. 1.01 at 10-16) (Staff Init. Br. at 117-118.)

First, Staff requests that it have access to all books, accounts, records, and personnel of all corporate entities affiliated with both Ameritech and SBC. (Marshall Direct, Staff Ex. 1.00 at 13). Both companies have agreed to provide the access requested, on the terms set forth in Dockets 97-0300 and 97-0321. (Kahan Surrebuttal, SBC/Am. 1.3 at 6.) Staff agrees this is acceptable. (Tr. 1582-83 (Marshall).) Second, Staff recommends that AI revise its cost allocation manuals ("CAMs") (Staff Ex. 1.00 at 15). SBC and Ameritech have committed to provide revised CAMs within 60 days of final regulatory approval of the proposed merger, (Kahan Surrebuttal, SBC/Am. Ex. 1.3 at 6; Gebhardt Surrebuttal, SBC/Am. Ex. 3.3 at 47.), an arrangement Staff states is acceptable. (Tr. 1581 (Marshall).) Third, Staff requests a copy of each affiliate service agreement and any relevant updates to the CAMS before AI provides service under any new or revised affiliate agreement. Joint Applicants have committed to do so. (Gebhardt Surrebuttal, SBC/Am. Ex. 3.2 at 48.) In its initial brief, Staff acknowledges that Sections 7-204(b)(2) and (b)(3) have been met because the Joint Applicants have agreed to Staff's proposed conditions. (Staff Init. Br. at 117-19.)

Intervenors' Positions

CUB contends that the size of the newly merged company and SBC's plans to pursue its Strategy provide evidence that the merger does not meet the requirements of Sections 7-204(b)(2) and (3). In particular, CUB argues that the size of the newly merged company will make the Commission's duty to protect AI ratepayers against subsidization of non-utility activities impossible. CUB states that, even if Staff has access to all the documents Ms. Marshall asserts are needed for the Commission to perform this duty, the volume of such materials would make it impossible to detect cross-subsidies and would require a large number of Staff employees to examine them. (CUB Init. Br. at 63-64.)

CUB also contends that use of the ILEC's core revenues to buttress the Strategy financially, as well as SBC's potential plans to draw on current Ameritech employees for NLS duties, is evidence of a substantial cross-subsidy. In particular, CUB asserts that SBC will flow revenues from its core services to make up the ten-year cumulative loss it expects to sustain with the NLS. CUB also asserts that SBC will raid assets and other resources of its ILECs that have been acquired and funded through revenues from its noncompetitive services. These services, CUB concludes, necessarily would include services included in the definition of universal service, which it alleges is prohibited under Section 254(k) of TA 96. Additionally, CUB argues that using the earnings of the merged company's ILEC operations to finance the Strategy would increase the overall portfolio risk of the new SBC, thereby placing upward pressure on its overall cost of

capital. This, CUB concludes, eventually would translate into higher rates for AI services. (CUB Init. Br. at 64-65.)

Cook County contends that the removal of capital and managerial talent, paid for by Illinois ratepayers, would result in the unjustified illegal subsidization of non-utility activities in violation of the Sections 7-204(b)(2) and (b)(3). It argues that, following the merger, Illinois will represent only 12% of the new SBC's ILEC operations and, therefore, will be required to compete for capital with twelve other SBC ILECs, the NLS operations, SBC's wireless business, and various international ventures. Cook County further argues that SBC will raid Ameritech managerial talent to support its Strategy. It asserts that, because recruitment and training of ILEC management personnel is a costly and time-consuming effort funded by revenues from core monopoly services, permitting SBC to raid these resources for the Strategy constitutes a substantial cross-subsidy. (Selwyn Direct, GCI Ex. 1.0 at 62-63; Selwyn Rebuttal, GCI Ex. 1.1 at 38-41; Cook County Init. Br. at 22-23.)

Similar to CUB, Cook County contends that reliance on ILEC core revenues to buttress the NLS not only violates sections 7-204(b)(2) and (3), but also violates Section 254(k) of TA96, which prohibits telecommunications carriers from using services that are not competitive to subsidize services that are subject to competition. Cook County asserts that SBC plans to flow revenues from its core services to make up for the ten-year cumulative loss it expects to sustain from the Strategy. (Cook County Init. Br. at 23-24.)

Cook County argues that the large commitment of capital and other resources to the NLS would increase the overall portfolio risk of a merged SBC/Ameritech. (Cook County Init. Br. at 22-25.) GCI witnesses acknowledge that this may not be an issue under AI's price cap plan because an increase in its cost of capital would not necessarily increase rates. However, they fear that AI may report poorer financial performance in some kind of attempt to revise the price cap plan. (Selwyn Direct, GCI Ex. 1.0 at 7, 61-67; Selwyn Rebuttal, GCI Ex. 1.1 at 38-41.) In adopting price cap regulation, the Commission expressly linked its review of the Plan to the Company's performance and earnings over the initial five-year period. Therefore, Cook County suggests, the inclusion of the Strategy in the Company's cost of capital could eventually, if not immediately, translate into higher rates for its services. (Cook County Init. Br. at 22-25.)

Cook County adds that, unless conditions are imposed, improper cost allocations would lead to subsidization of non-utility activities and the improper allocations would remain undetected by Staff. (Cook County Init. Br. at 25.)

Sprint contends that the profits associated with the Company's regulated operations, specifically access services, would be used to subsidize the merged entity's non-regulated long distance operations. It argues that SBC/Ameritech would have an enormous advantage in competing for long distance traffic because of the large subsidies currently embedded in access rates. (Sprint Init. Br. at 38-41.) Sprint notes

that SBC specifically studied its ability to subsidize its interexchange operations prior to the proposed merger.

CTCA contends that the Commission cannot find that the proposed merger meets the requirements of Sections 7-204(b)(2) and (3) unless it imposes the conditions proposed by Staff. In support of this position, CTCA raises the same concerns about Section 7-204(b)(2) as initially raised by Staff, including: (1) Staff's ability to verify charges and allocation costs among a larger group of affiliates following the merger, and (2) the difficulties in identifying costs and facilities without more description and details for each Ameritech transaction. With respect to Section 7-204(b)(3), CTCA argues that existing safeguards are not sufficient to satisfy that requirement of the PUA. (CTCA Init. Br. at 21-22.)

Commission Analysis and Conclusion

Section 7-204(b)(2)

Section 7-204(b)(2) requires the Commission to determine that the proposed reorganization will not "result in the unjustified subsidization of non-utility activities by [Ameritech Illinois] or its customers" in Illinois. The term "unjustified subsidization" is not specifically defined in the Act. The General Assembly has, however, addressed aspects of the subsidization issue in sections 13-103 and 13-507 of the Act. In section 13-103, the General Assembly stated the policy of the State of Illinois to require that rates for non-competitive telecommunications services should in no case "include any portion of the cost of providing competitive telecommunications services . . . or the cost of any non-regulated activities." (See 220 ILCS 5/13-103(d)). Likewise, under section 13-507, the General Assembly provided for the disallowance of the subsidy of "competitive services or non-regulated activities by non-competitive services." (See 220 ILCS 5/13-103). In order to meet the requirements of that section the Commission is required to apportion facilities and expenses of carriers such as Ameritech Illinois between non-competitive and competitive services. (Id).

As pointed out by the Court in People ex rel. O'Malley v. Illinois Commerce Commission, 239 Ill. App. 3rd 368, 384 (2nd Dist. 1993), the Act grants the Commission broad, general powers to deal with preventing subsidization of competitive services by non-competitive services but does not set forth any specific steps or procedures for the Commission to follow. Neither does the General Assembly set forth any specific steps for the Commission to follow in protecting Ameritech Illinois and its customers from "unjustified subsidization". However, in view of the General Assembly's statements of policy in section 13-103 and its substantive pronouncements in section 13-507, the Commission believes it is reasonable to conclude that, under section 7-204(b)(2), the Commission's duty under this section is to ensure that the proposed reorganization, in and of itself, will not lead Ameritech Illinois to assign costs from its competitive, non-utility functions to its non-competitive, utility activities in a manner not currently allowed by Illinois law and Commission rules.

Applying the foregoing standard to the record evidence, the Commission finds that the reorganization will not result in the unjustified subsidization of non-utility activities by the utility or its customers. However, given the Joint Applicants' voluntary commitment to comply with the conditions recommended by Staff in this proceeding, this Commission incorporates the conditions agreed upon by Staff and the Joint Applicants as further assurance that the Joint Applicants will, after consummation of the merger, continue to meet the burden necessarily imposed on the Joint Applicants by Section 7-204(b)(2). The specific conditions imposed by the Commission, detailed below, include the requirement of updating Ameritech Illinois' Cost Allocation Manuals (CAMs) in accordance with Commission Code Part 711 and as outlined by Staff in its testimony and Initial Brief. (See Staff Br. at 118, Marshall Direct, Staff Ex. 1.0 at 13-15). The Commission formally adopts these conditions pursuant to its authority under section 7-204(f).

1. Cross-Subsidization

The Joint Applicants maintain that Ameritech Illinois has historically followed, and will continue to follow, the Commission's rules governing common cost allocation and affiliate transactions. (See Kahan Direct, SBC/Ameritech Ex. 1.0 at 32). Staff does not dispute the Joint Applicants' claim regarding Ameritech Illinois' compliance with current Commission cost-allocation rules. (See Staff Br. at 119). Accordingly, the Commission concludes that Ameritech Illinois is currently in compliance with the cost allocation and affiliate transaction rules promulgated by this Commission. Staff and Intervenors do contend, however, that the Joint Applicants' reorganization will lead to unjustified subsidization of non-utility activities, and in some instances, suggest conditions which this Commission should adopt in order to mitigate their concerns. (See Staff Br. at 118, Staff Ex. 1.0 at 13-15, CUB Br. at 63-65).

Staff presented concerns that following the merger Ameritech Illinois' status as a subsidiary of SBC may result in the Commission's inability to detect improper allocations for transactions between Ameritech Illinois and other SBC affiliates located outside of Illinois. (Id.). Staff also argued that following the merger Ameritech Illinois will be part of a much larger group of companies, and therefore the added complexity of the corporate organization may increase the chance for costs to be improperly allocated among affiliates. (Id.). As highlighted below, the Commission disagrees with these concerns. The Commission additionally believes that the concerns raised by the Cable Television and Communications Association (CTCA) regarding improper allocations do not have merit as they relate to the current actions of Ameritech Illinois. (See CTCA Br. at 21-22).

The Commission points to a broad array of state and federal rules and procedures which address the allocation of costs between utility and non-utility affiliate activities. Included among these safeguards are this Commission's cost allocation procedures and Ameritech Illinois' implementation of these procedures. (See, for example, 83 Ill. Admin. Code § 711). The Commission also notes the FCC requirements which include the filing and independent audit of a cost allocation manual

with the FCC, as well as Section 272 of the federal Telecommunications Act of 1996. (See Staff Ex. 1.0 at 12). These safeguards will remain in place after the reorganization, thereby protecting Illinois ratepayers against improper cost allocation. Ameritech Illinois' cost allocation procedures have been reviewed by the Commission in past rate cases, annually attested to by independent auditors, and examined regularly by Commission Staff and the FCC. None of these reviews has undermined the conclusion that the cost allocation procedures currently in use satisfactorily protect consumers. (See, for example, Illinois Bell Telephone Company v. Illinois Commerce Commission, Docket Nos. 92-0448 & 93-0239 (Oct. 11 1994), Gebhardt Direct, SBC Am. Ex. 3.0 at 8). After the merger, this Commission notes that the Joint Applicants and Ameritech Illinois will continue to abide by these same procedures because the Joint Applicants will remain subject to the same regulatory restraints.

Moreover, given the Joint Applicants' voluntary acceptance of certain conditions proposed by Staff, the Commission finds that the adoption of such conditions further ensures the continuing compliance by Ameritech Illinois with the Commission's cost allocation rules. These conditions include the updated CAM procedures which Staff outlined in its testimony on this issue. (See Marshall Direct , Staff Ex. 1.0 at 15, Marshall Rebuttal, Ex. 1.01 at 13-16). The Commission orders the Joint Applicants to update the CAM in the manner proposed by Staff. Updates of the relevant CAM item must occur whenever either the cost allocation methodology or the identification of affiliates or services provided or received by Ameritech Illinois changes. Further, Ameritech Illinois must include in its CAM a brief description of each of Ameritech's affiliates as well as detailed information regarding the transactions which occur with those affiliates. These updates must be completed within sixty days of final state and federal regulatory approval of the reorganization. (See Marshall Rebuttal, Staff Ex. 1.01 at 15-16). Conditions concerning updated CAMs are to be complied with by the Joint Applicants and reviewed and audited by the Commission, with the assistance of an independent third party selected by the Commission and paid for by the Joint Applicants. Further specifics for the conditions recommended by Staff and adopted by the Commission related to section 7-204(b)(2) can be found below.

2. National Local Strategy

The GCI parties argue that the Joint Applicants' National Local Strategy, as described by the Joint Applicants throughout this proceeding, will result in Ameritech Illinois' illegal subsidization of non-utility activities. (See Selwyn Direct, GCI Ex. 1.0 at 60-63, CUB Br. at 59-61). The GCI parties argue that such illegal cross-subsidization could occur in two ways. (Id.). First, they allege that the Joint Applicants may staff the National Local Strategy by reassigning experienced Ameritech Illinois' managerial talent, trained with Illinois ratepayers regulated revenues, to locations outside of Illinois. (Id.). Second, the GCI parties argue that the expenditures associated with the implementation of the National Local Strategy will require funding from revenues generated by the Joint Applicants' utility concerns in order to offset the expected losses of the strategy. (Id.).

The Commission rejects these arguments. The Commission finds that transferring employees from one job to another within the merged company is not cross-subsidization so long as Ameritech Illinois properly accounts for the transfer in accordance with current and future practices outlined by the Commission. The Commission also rejects GCI's contention that using Ameritech Illinois revenues to fund the National Local Strategy will lead to cross-subsidization. This contention has no support in the record. First, the Commission has adopted explicit cost allocation procedures, found in Part 711 of the Administrative Code, which protect ratepayers against such cross-subsidization. These procedures, which have adequately protected ratepayers in the past, will remain in force after the merger and will continue to protect ratepayers in the future. Second, the Joint Applicants have represented that the National Local Strategy will not be cross-subsidized by ratepayer revenues. (See Joint Applicants' Initial Br. at 74). The Commission notes that ratepayer subsidized funding would be detected by the rules currently governing Ameritech Illinois. Therefore, funding the National Local strategy in such a manner as represented by the Joint Applicants in this proceeding would not be an illegal cross-subsidization.

The Commission also finds that the use of Ameritech Illinois' return on capital to support the National Local Strategy as it has been represented in this proceeding, does not constitute illegal cross-subsidization by the Joint Applicants. The record does not support such a conclusion by this Commission, and, in fact, upon close examination, CUB and Cook County have failed to raise an adequate cross-subsidization claim. Instead, CUB and Cook County contend that the Company's use of its return to finance specific ventures is illegal cross-subsidization. This argument goes against basic regulatory and legal principles, which give shareholders the right to earn a return on capital and use it to finance other corporate ventures so long as it does not violate the affiliate rules of this Commission. (See Cook County Br. at 22-24). Therefore, if any Ameritech Illinois funds used to finance the National Local Strategy come from the Company's return on capital, such funding would be legal provided the Joint Applicants comply with all other cross-subsidization and cost allocation rules. Accordingly, the Commission concludes that financing the National Local Strategy with Ameritech Illinois earnings, in the manner represented by the Joint Applicants in this proceeding, is legal under current Illinois law and Commission rules and thus does not constitute cross-subsidization.

3. Impact of Entity's Size Upon Cross-Subsidization

Cook County argues that following the merger Ameritech Illinois will represent 12% of the Joint Applicants operations, which will force Ameritech Illinois to compete for capital with other operating units within the combined company. Cook County claims that this action constitutes cross-subsidization. (See Cook County Br. at 22-24). The Commission finds Cook County failed to relate this contention to section 7-204(b)(2) of the statute. Further, the Commission concludes that even if Cook County had clarified this claim as it relates to network infrastructure investment and service quality under section 7-204(b)(1), the Commission's condition in Section III.B.1. of this Order regarding network infrastructure investment, as well as the Company's continuing

compliance with service quality standards and reporting requirements, adequately addresses the concerns raised by Cook County.

The Commission also rejects CUB's argument that the increased size of the newly merged company will impair this Commission's ability to fulfill its duty to protect Ameritech Illinois' ratepayers against subsidization of non-utility activities. (See CUB Br. at 63-65). The record does not support CUB's contention that the size of the merged organization will hinder Staff's ability to detect cross-subsidies, especially in light of the conditions which the Joint Applicants voluntarily agreed to and the Commission has imposed as a condition to this merger. Staff assured the Commission that so long as Staff can access requested documents of the Joint Applicants, Staff feels confident it can detect any cross-subsidies which may occur between the new merged entity and Ameritech Illinois. (See Staff Br. at 117-119). The Commission agrees with the Joint Applicants that Staff is best able to ascertain whether it has sufficient resources and abilities to detect cross-subsidies. (See Joint Applicants Br. at 61-64).

4. InterLATA Cross-Subsidization

Sprint contends that post merger the Joint Applicants will have both the ability and the incentive to implement price squeezing techniques in the interexchange market by utilizing profits earned from monopoly local services to subsidize Ameritech Illinois' interLATA activities. (See Stahly Rebuttal, Sprint Ex. 1.1 at 4-12, Sprint Br. at 38-41). Sprint claims that such price squeezing techniques would constitute illegal subsidies by Ameritech Illinois. Sprint contends that the substantial artificial cost advantage implicit in the merged entity's pricing of access at many times actual cost, and the ability of Ameritech Illinois to leverage its position in the local market, could lead to an unjustified subsidization of non-utility (interexchange) activities by Ameritech Illinois' utility (local) activities. (Id.).

This Commission generally agrees with Sprint's assertions about the hypothetical opportunity for price squeezing by an incumbent in the local market if local access were priced substantially above cost and all other competitive conditions remained equal. This Commission anticipates substantial discussion of such a critical issue if Ameritech Illinois were to submit an application to provide interLATA service in a 271 proceeding before this Commission. If and when the Joint Applicants submit an application to this Commission for interexchange authority, the Commission will consider these issues raised by Sprint. However, this Commission rejects Sprint's arguments as they relate to the proposed reorganization regarding unjustified illegal subsidization because Ameritech Illinois does not currently provide interexchange service. Therefore, the Commission refrains from deciding this specific issue within the purview of this docket. The Commission further notes that it is currently addressing access charges in its access charge proceeding, Dockets 97-0601/0602/0516 Consolidated.

5. Subsidies for Premier Customers

Finally, DSSA and the Neighborhood Learning Networks (NLN) contend that the principal beneficiaries of this proposed reorganization are corporate and 'premier' residential users. (See DSSA Br. at 18-20). As such, DSSA and NLN claim that these users will benefit from the merger because of increased competition between telecommunications providers for business. (Id.). These parties go on to assert that this competition will ultimately result in lower rates for telecommunications services for these business and 'premier' customers. (Id.). DSSA contends lower rates which businesses and 'premier' users may realize as a result of the merger are subsidies for non-utility uses accruing to an exclusive group of customers. (Id.). Therefore, DSSA and NLN contend that subsidies similar to those experienced by the business and 'premier' residential accounts should be allocated to the disadvantaged populations of Illinois. (Id.).

First, the Commission does not believe that only corporate and 'premier' residential users will benefit from the reorganization. Rather, the record indicates that the Joint Applicants discussed in depth the various service offerings which will be made available to residential customers in Illinois in a similar fashion to services provided to California customers after the merger with Pacific Bell. Joint Applicants also committed to provide advanced services to residential customers through the use of their research affiliate, TRI. (See Kahan Direct, SBC/Ameritech Ex. 1.0 at 21-22, Kahan Rebuttal, SBC/Ameritech Ex. 1.1 at 106 and Kahan Surebuttal, SBC/Ameritech Ex. 1.2 at 7-8, 80-86). The Joint Applicants also committed on reopening to provide residential customers access to ADSL services in central office locations where ADSL service is subsequently deployed by the Joint Applicants. (See Joint Applicants' Response to Commission's June 4 List of Issues and Joint Applicants' Additional Commitments at 40). Therefore, the Commission rejects DSSA's assertions that the merger's primary beneficiaries will be business and 'premier' users. DSSA's argument is premised on the proposition that these corporate clients and "premier" users will benefit through reduced rates resulting from competition for their business and that such lower rates are, in effect, subsidies for private non-utility uses. (See Samuelson Rebuttal, DSSA Ex. at 20-21). This Commission does not define the provision of bundled services as an unjustified subsidization so long as the services are properly allocated among utility and non-utility operations. Therefore, the Commission rejects DSSA's arguments under section 7-204(b)(2) because DSSA's arguments do not demonstrate a potential violation of the cost allocation rules as interpreted by this Commission.

Section 7-204(b)(3)

Section 7-204(b)(3) requires the Commission to determine that the "costs and facilities [of Ameritech Illinois] are fairly and reasonably allocated between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities which are properly included by the utility for ratemaking purposes."

This standard requires Commission analysis of many of the same issues which the Commission considered under section 7-204(b)(2). Consequently, many of the issues related to section 7-204(b)(3) have been properly addressed in the

Commission's analysis and conclusions relative to section 7-204(b)(2) above. The Commission believes that the application of sections 7-204(b)(2) and 7-204(b)(3) to this proposed reorganization implicates many interrelated issues. Consequently, whereupon determining that the Joint Applicants have satisfied the Commission with regard to section 7-204(b)(2), many of the issues related to section 7-204(b)(3) have already been fully addressed by the Commission's decision in its analysis and conclusion regarding section 7-204(b)(2) above. In fact, many of the Intervenors in this proceeding linked their 7-204(b)(2) and 7-204(b)(3) arguments. Therefore, in this section of the Order, the Commission will only address parties' arguments not reached in the Commission's analysis under section 7-204(b)(2) .

Reasonable Allocations for Ratemaking Purposes

Staff raised two issues regarding the reorganization's effects upon the fair and reasonable allocation of costs and facilities. The first issue is Staff's concern that, under some circumstances, Ameritech Illinois may be required to comply with Part 285, which requires a summary of affiliated interest transactions. (See Marshall Direct, Staff Ex. 1.0 at 15-16). Second, Staff raises concerns regarding an investigation in California of SBC's cost allocations among and between its affiliates. (Id.). As stated previously, no party contested the Joint Applicants' assertion that Ameritech Illinois currently complies with the Commission's rules regarding cost allocation and affiliate transactions.

The Commission sees no reason why Ameritech Illinois could not comply with Part 285 if so required and notes Ameritech Illinois' consistent compliance with the Commission's cost allocation procedures. The Commission puts the Joint Applicants on notice however, that illegal cost allocation among affiliates will be penalized to the fullest extent of Illinois law. However, similar to section 7-204(b)(2), the Commission incorporates here, as part of its Order in this reorganization, Staff's proposed conditions granting Staff access to all books, accounts, records, independent audit workpapers, personnel, etc. of the regulated and non-regulated utility affiliates of the Joint Applicants which the Commission and Staff deem necessary. The Commission intends this condition to provide Staff access to the items named above in a manner similar to the terms set forth by the Commission in ICC Dockets 97-0300 (reorganization of Consolidated Communications) and 97-0321 (reorganization of Gallatin River exchanges of Sprint Communications). However, the Commission's authority is not limited by the terms imposed in previous dockets. The Commission additionally requires the Joint Applicants to reimburse the Commission Staff for all reasonably incurred travel expenses if Staff must travel out of Illinois in order to review the Joint Applicants' books and records.

D. Whether The Proposed Reorganization Will Significantly Impair The Utility's Ability To Raise Necessary Capital On Reasonable Terms Or To Maintain A Reasonable Capital Structure. (Section 7-204(b)(4)).

Joint Applicants' Position

Joint Applicants contend that the proposed reorganization will not impair the Company's ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure. (SBC/Am. Init. Br. at 75.) They assert that AI will continue to exist in exactly the same form after the merger. Consequently, because it issues its own debt, AI will have the same access to the debt market that it does today. Traditionally. equity has been issued by Ameritech at the holding company level. Joint Applicants state that this overall structure will continue to exist after the merger except that SBC, instead of Ameritech, will issue stock and infuse equity capital into the regulated companies. Joint Applicants assert that, because of the increased size of the company after the merger, AI actually will have better access to capital markets. The merged company's financial strength will provide the combined organization with significant financial flexibility, including the flexibility to issue both debt and equity where needed on reasonable terms. Additionally, they argue, the combined organization's cash flow and funding capabilities will enable it to raise funds for network investments and new products and service on a more cost efficient basis. (Gebhardt Direct, SBC/Am. Ex. 3.0 at 10-12).

Joint Applicants also contend that there will not be any material change in the Company's capital structure after the merger. They point out that this Commission has reviewed its capital structure on numerous occasions and has concluded that it is reasonable. (Gebhardt Direct, SBC/Am. Ex. 3.0 at 10-12). They assure the Commission that AI will continue to operate in accordance with sound financial, accounting and capital management guidelines, and that SBC will continue to infuse capital into it as required. They claim that SBC's current practice with SWBT and PacTel is a strong indication of its commitment to infuse capital into its operating subsidiaries. (Kahan Direct, SBC/Am. Ex. 1.0 at 34).

In further support of SBC's position, Joint Applicants cite comments made by several investment analysts that have praised the combination of SBC and Ameritech. Joint Applicants argue that the analysts' remarks confirm the judgment of the management of SBC and Ameritech that the combination of these two companies is an outstanding fit and will benefit customers, shareholders and employees. (Kahan Direct, SBC/Am. Ex. 1.0 at 35-37).

Staff and Intervenors' Positions

Staff agrees with Joint Applicants that the proposed reorganization will not impair AI's ability to raise capital or maintain a reasonable capital structure as required under Section 7-204(b)(4). (Plaza Direct, Staff Ex. 2.00 at 3-6; Marshall Direct, Staff Ex. 1.00 at 16-17.) Staff points out that AI has access to the long-term debt markets on reasonable terms because of its Standard & Poor's ("S&P") issuer credit rating of AAA, and has access to the short term debt and equity capital markets on reasonable terms as a result of Ameritech's AA+ S&P issuer credit rating. Additionally, because the merger is taking place at the holding company level and not the utility operating level, Staff asserts that the Company's capital structure is expected to remain unchanged immediately after the merger. Because AI will still access the long-term debt capital

market independently of its parent company, Staff finds it will continue to have access on reasonable terms. However, because AI accesses the short-term debt and equity markets through its parent company, Staff evaluated the financial condition of the new parent company, SBC. It found that SBC's financial ratios, as well as the merged company's forecasted financial ratios, demonstrate a strong financial condition. Therefore, Staff concludes that the proposed reorganization complies with Section 7-204(b)(4). (Staff Init. Br. at 120-21.)

Although the GCI parties did not specifically raise arguments concerning Section 7-204(b)(4) in their initial briefs, they argued in the course of this proceeding that the purchase premium will have a negative effect on AI's cost of capital. The merger agreement provides that SBC will acquire Ameritech as a wholly-owned subsidiary through a tax-free stock-for-stock transaction. Shares of Ameritech common stock will be converted into shares of SBC common stock on the basis of a 1.316 exchange ratio. According to the GCI witnesses, this represents a premium of about $13.2 billion over the market value of Ameritech as of the day preceding the merger announcement and, in terms of Ameritech's $15 billion book value, SBC will be paying a premium of $47 billion. GCI argues that the premium paid for the stock will impact Ameritech Illinois' cost of capital adversely in violation of Section 7-204(b)(4). (Selwyn Direct, GCI Ex. 1.0 at 8-9.)

As previously stated, CUB and Cook County have also argued that the NLS will increase the overall portfolio risk of the merged company. These arguments were previously described in our discussion of Sections 7-204(b)(2) and (b)(3).

CTCA agrees with Staff witness Plaza that the proposed merger will not significantly impair Ameritech Illinois' ability to access the capital markets on reasonable terms, or to maintain a reasonable capital structure.

Commission Analysis and Conclusion

Section 7-204(b)(4)

Section 7-204(b)(4) requires the Commission to determine that the proposed reorganization will not "significantly impair the utility's ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure" before the Commission can approve the proposed reorganization. Therefore, the Commission must examine whether after the reorganization of Ameritech and SBC, Ameritech Illinois' access to the capital markets will be significantly impaired, or whether its ability to maintain an appropriate capital structure will be significantly impaired.

Access to Capital Markets

The Commission agrees with both the Joint Applicants and Staff that the proposed reorganization will not significantly impair Ameritech Illinois' ability to raise necessary capital. The Commission interprets the specific language of "ability to raise necessary capital" in section 7-204(b)(4) to mean that the Commission must be

satisfied that the company will have continued access to both the long- and short-term capital markets on reasonable terms after the proposed reorganization. With regard to the long-term debt capital markets, Ameritech Illinois has adequately demonstrated in this proceeding that it will continue to have access to these markets independently of its parent company after the transaction. (See Kahan Direct, SBC/Ameritech Ex. 1.0 at 33-39). With regard to the short-term debt and equity markets, the analysis performed by Staff in this proceeding offers assurances to this Commission that the Joint Applicants' proposed reorganization does not affect the short-term capital needs of the company either. (See Plaza Direct, Staff Ex. 2.0). The Commission specifically refers to the strong financial condition of the newly merged company and its forecasted financial ratios. (Id.). The improved financial condition of an already strong Ameritech Illinois and its parent company give the Commission great assurance that the utility's ability to raise necessary capital will not be impaired.

Parties to this proceeding also raised the issue of negative impacts upon Ameritech Illinois' cost of capital resulting from the purchase premium paid to Ameritech's equity shareholders by SBC. (See GCI Ex. 1.0 at 8-9, 14). Specifically, parties claimed because the premium was substantially above the market value of Ameritech's publicly-traded stock at the time of the announcement, the value of the premium would detrimentally impact Ameritech Illinois' cost of capital. (Id.). The Commission rejects this argument. The record indicates that the financial strength of the combined companies will exceed the financial strength of either company alone. (See Kahan Direct, SBC/Ameritech Ex. 1.0 at 33-39, Staff Br. at 120). As such, the Joint Applicants' access to capital markets will likely be enhanced, not decreased. Moreover, the record indicates that the ability of the Joint Applicants to maintain a reasonable capital structure will not be not harmed by the merger. (Id.). Similarly, the ability of the Joint Applicants to manage their overall portfolio risk adequately, as GCI has raised, will not be harmed by the National Local Strategy. (See Selwyn Direct, GCI Ex. 1.0 at 60-64, Cook County Br. at 24, Kahan Rebuttal, SBC/Ameritech Ex. 1.1 at 13-16). While the National Local Strategy may have a different risk profile than that of the other utility operations of the Joint Applicants, the Commission finds that the size and financial characteristics of the newly merged entity will allow the utility operations of Ameritech Illinois to continue to maintain an adequate capital structure.

Thus, the Commission finds that the proposed merger will not significantly impair the Company's ability to raise necessary capital on reasonable terms or to maintain an appropriate capital structure. The proposed reorganization meets the requirements of section 7-204(b)(4).

E. Whether Ameritech Illinois will remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois Public Utilities. (Section 7-204(b)(5)).

Joint Applicants' Position

The Joint Applicants take the position that, following the merger, Ameritech Illinois will continue to be subject to the jurisdiction of the Commission and to all of the applicable laws, rules, regulations, decisions, and policies relating to its regulation. They also state that there is nothing about this merger that in any way alters the authority of the Commission to regulate AI just as it has been regulated in the past (Kahan Direct, SBC/Ameritech Ex. 1.0 at 40-42; Gebhardt Direct, SBC/Ameritech Ex. 3.0 at 12) and that no party has disputed that fact. (Joint Applicants' Reply Br. at 80.)

Because the Commission's jurisdiction and authority over AI will not change, and it will remain subject to all applicable Illinois laws, the Joint Applicants conclude that Section 7-204(b)(5) has been satisfied and the Commission's inquiry need go no further. They state that the Commission has followed this very same analytical approach in all prior mergers under Section 7-204(b)(5). (See, e.g., Consolidated Communications/McLeod USA Merger, Docket 97-0300, Order dated September 24, 1997 at 13: "[T]he Commission's jurisdiction will not be impacted by the proposed merger. After the merger, ICTC will continue to be regulated by the Commission in the same manner and to the same extent as it is regulated today." CIPSCO/Union Electric Merger, Docket 95-0551, Order dated September 10, 1997, at 68: "[B]oth CIPS and UE will continue to be regulated as Illinois public utilities after the merger and reorganization"); Iowa-Illinois Gas & Elec./MidAmerican Energy Merger), Docket 94-0439,Order dated May 3, 1995 at 36; GTE/Contel Merger, Docket 90-0337, Order dated December 12, 1990 at 7, 10: "[T]he regulatory status of Contel will remain unchanged after the reorganization.")

Further, although they view the issue as irrelevant to Section 7-204(b)(5), the Joint Applicant's note that the voluntary commitments made by SBC and Ameritech actually will improve the Commission's and its Staff's ability to oversee AI and ensure compliance with all laws, regulations, and orders. For example, they have agreed to: (1) file monthly OSS reports with the Commission; (2) submit revised TELRIC and LRSIC studies within six months of the last regulatory approval of the merger; (3) advise Staff of any changes to 9-1-1 service or staffing; (4) grant Staff access to all books, accounts, records, and personnel of Ameritech Corporation, SBC, and their utility and non-utility parent, sister, and subsidiary companies, as well as the workpapers of independent auditors; (5) file a revised Cost Allocation Manual within six months of the last regulatory approval of the merger; (6) work with Staff to ensure equal treatment of all customer classes; and (7) file an annual report on "best practices" for up to three years after the merger. (Kahan Surrebuttal, SBC/Am. Ex. 1.2 at 4-8; Joint Applicants' Reply Br. at 81.)

Staff's Position

Staff disagrees with the Joint Applicants' assertions and contends that Section 7-204(b)(5) can be satisfied only if the Commission imposes certain conditions, discussed below. It believes that such conditions are necessary to avoid any adverse impact on the Commission's ability to regulate AI after the merger. Staff believes that this ability to regulate could be threatened by AI's recent history of non-compliance with

Commission orders, SBC's documented anti-competitive behavior and non-compliance with legal requirements in other jurisdictions, a reduced ability to use "benchmarks," and SBC's possible desire to standardize regulations in its 13-state region.

In arguing that AI has a recent history of non-compliance with Commission Orders, Staff refers to (1) the Bands B and C case (Docket 95-0584), where the Commission reprimanded AI for missing a deadline to file a new tariff; (2) the Commission's Order on reciprocal compensation payments to Internet Service Providers (Docket 97-0404, 97-0519, and 97-0525 (cons.)), where AI delayed paying reciprocal compensation after the stay of the Commission's Order expired; (3) the Commission's "common transport" requirement in Docket 96-0486 by not offering common transport to competing carriers, (4) the Commission's Order on Infrastructure Maintenance Fees (Docket 97-0632), where AI is technically in non-compliance because the Commission has not yet ruled on its request for an extension of time; and (5) Staff's letter to AI on December 1, 1998 regarding problems Staff has had in verifying costs supporting the Company's tariff filings. (Marshall Direct, Staff Ex. 1.00 at 17; Marshall Rebuttal, Staff Ex. 1.01 at 16-19.) Staff has also noticed a "general decline in Ameritech Illinois' compliance with Commission decisions and policies. Concurrently, Staff has noticed reductions in the number of Ameritech Illinois' regulatory staff which should be a consideration in approving the merger considering that one area SBC/Ameritech expects to receive the benefits of cost reductions is in regulatory expenses (See Synergy Summary, SBC Document Number 004-04993)." Staff believes that the merger "is likely to lead to a further decline in Ameritech Illinois' compliance with applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities." (Staff Initial Br. at 125-26.)

Staff also points to SBC's non-compliance with both state and federal requirements. For example, Staff states that the utility commissions in Texas and California have directed SBC to demonstrate that it is following a number of their Orders and intends to follow future PUC directives as part of SBC subsidiaries' Section 271 proceedings. (Yow Direct, Staff Ex. 3.00, Atts. 1 and 2.) Further, based on the Joint Applicants' position that SBC's corporate headquarters in San Antonio, Texas will dictate general corporate goals, commitments, and policies to AI personnel, Staff is concerned that this will make it more challenging for the Commission to regulate AI. Staff cites to decisions by the Texas PUC, the district court for the Western District of Texas, and the American Arbitration Association that criticize certain anti-competitive SBC practices and find it in violation of various requirements of the federal Act of 1996, to support their position. (Staff Brief at 126-29.)

Staff next points out that the merger will reduce the number of independent RBOCs that state and federal regulators can use for comparison purposes, or "benchmarking." It claims that with the reduction in the number of independent RBOCs from seven to five and now potentially four, it will become more difficult for this Commission to evaluate the Company's quality of service, cost characteristics, rate levels, innovation efforts, competitive efforts as well as technical and economic feasibility issues. (Yow Direct, Staff Ex. 3.00 at 17)."

To the extent the Commission concludes that the proposed merger should be approved, Staff recommends that approval be conditioned on the following: (1) Ameritech Illinois' demonstration of compliance with all current Commission Orders; (2) Ameritech Illinois' and SBC's demonstration of compliance with Sections 251 and 271 of TA96; (3) Ameritech Illinois' maintenance of its existing level of regulatory staffing within Illinois; (4) a requirement that Ameritech Illinois seek Commission approval prior to reducing or moving subject matter expert positions outside the state of Illinois; (5) obtaining Commission approval prior to the reduction or removal of any 9-1-1 staff functional in providing 9-1-1 services in Illinois; and (6) ensuring that any post-merger changes that are made in the delivery of 9-1-1 services be transparent to the 9-1-1 systems and to the 9-1-1 subscribers. Staff Init. Brief at 94 and 134.

Intervenors' Position

The GCI parties were the only Intervenors to address Section 7-204(b)(5) in any meaningful way. They essentially support Staff's position, while adding a few claims about the implications of the Joint Applicants' past conduct for the Commission's ability to regulate AI after the merger. Cook County, for example, alleged that SBC's challenge to the California statute regarding sharing of merger benefits in its merger with PacTel and its challenge to the applicability of Section 7-204(c) here show a resistance to regulatory authority. (Cook County Init. Br. at 26-27.) Cook County makes the same claim regarding SBC's and Ameritech's arguments in various cases regarding the proper interpretation of Section 271 of TA96. (Id. at 27.)

Commission Analysis and Conclusion

Section 7-204(b)(5)

Section 7-204(b)(5) requires the Commission to consider if Ameritech Illinois will "remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities" following the reorganization. The Commission interprets this statutory provision as requiring the Commission to ensure that the proposed reorganization does not inappropriately shelter or otherwise remove a utility's activities from regulatory scrutiny by this Commission (e.g., by somehow shifting regulated functions to an unregulated affiliate).

The Commission finds no reason to deviate from its approach in prior proceedings. All parties to this case concur that Ameritech Illinois will remain subject to the jurisdiction of the Commission and to all laws, regulations, rules, decisions and policies to the same extent after the merger as before the merger. Accordingly, the Commission finds that Ameritech Illinois' regulatory status will remain unchanged by the reorganization.

1. Impact of Transaction Upon Regulatory Status

Staff and other Intervenors raise a number of arguments asserting that SBC's acquisition of Ameritech may frustrate the Commission's ability to adequately regulate Ameritech Illinois' activities as required by Illinois law. (See Staff Brief. at 122-134, CUB Br. at 63-65, Woodbury Rebuttal, Sprint Ex. 2.1 at 18-21). In particular, parties cite the anticipated relocation of the holding company's headquarters to a location outside of Illinois, the Joint Applicants' desire to standardize regulatory procedures across its thirteen state operating region, and a reduction in the number of Regional Bell Operating Companies (RBOCs) by which the Commission may "benchmark" Ameritech Illinois' behavior. (See Staff Br. at 122-134, Woodbury Rebuttal, Sprint Ex. 2.1 at 18-21). The Commission rejects these arguments because they fail to address the Commission's jurisdictional authority as required by a plain language interpretation of section 7-204(b)(5). Alternatively, the arguments put forth by these parties attempt to address the Commission's ability to regulate Ameritech Illinois effectively. The Commission finds that the language of section 7-204(b)(5) relates to the jurisdictional authority of the Commission and not to the Commission's regulatory effectiveness.

The relocation of Ameritech's corporate headquarters does not challenge the Commission's jurisdictional authority over Ameritech Illinois. The Commission retains authority over Ameritech Illinois because the products and services offered by the Company fall under the regulatory jurisdiction of this Commission as determined by the Public Utilities Act. Consequently, this Commission concludes that relocating its corporate headquarters outside of Illinois does not, on its own, cause the Joint Applicants to fail the standards of section 7-204(b)(5).

Similarly, while the Joint Applicants' goals may include the standardization of regulatory policy, internal goals of the Joint Applicants do not change this Commission's authority over Ameritech Illinois. The Commission places the Joint Applicants on notice that any attempt to engage in a pattern of non-compliance with this Commission's policies and decisions will face serious and deliberate Commission action. However, the Commission does not believe that Staff's and other Intervenors' claims in this area are warranted.

Finally, with respect to this proposed reorganization's effects upon the ability of the Commission to benchmark behavior, the Commission recognizes the concerns raised by Staff and others. (See Toppozada-Yow Direct, Staff Ex. 3.0 at 14-20, Staff Br. at 122-134, Sprint Br. at 33-35). Specifically, the Commission notes the FCC's statements from the Bell Atlantic/NYNEX decision which parties cited in this proceeding and in this specific area of concern. (See FCC Memorandum Opinion and Order, *In the Application of NYNEX Corporation Transferor and Bell Atlantic Corporation Transferee, For Consent to Transfer Control of Nynex Corporation and Its Subsidiaries*, August 14, 1997 at 147). However, the Commission observes that the FCC's comments in the matter of benchmarking were specifically targeted to address the FCC's ability to identify and constrain market power through the use of benchmarking RBOCs. In contrast, section 7-204(b)(5) of the Act calls for an evaluation of whether or not Ameritech Illinois remains subject to the Commission's laws, regulations, rules, decisions and policies, not a consideration of the Commission's ability to regulate public

utilities effectively. The Commission must follow the intent of the language as constructed by the General Assembly in this matter, and in doing so defers to the FCC's ultimate regulatory authority to benchmark RBOCs in such a way as to constrain market power on a national level.

2. Non-Compliance

Staff's and other Intervenors' most strenuous argument raised under section 7-204(b)(5) relates to the behavior of the Joint Applicants both here in Illinois and in other states which they claim highlights a pattern of non-compliance with state regulatory commission directives. (See Marshall Rebuttal, Staff Ex. 1.01 at 16-19, Toppozada-Yow Direct, Staff Ex. 3.0 at 14-20, Cook County Br. at 25-27). The evidence, which includes assertions of overly litigious nature on the part of the Joint Applicants, concerns this Commission. (Id.). Utilities subject to the Commission's regulations must demonstrate compliance with Commission Orders and the Public Utilities Act. However, in applying section 7-204(b)(5) to this proposed reorganization, the Commission finds that SBC's past alleged conduct, even if such conduct were to be attempted in Illinois would not amount to a failure by the Joint Applicants to meet the requirements of section 7-204(b)(5). Rather, the Commission finds that other sections of section 7-204 grant the Commission the authority to ensure that public utilities are fully compliant with its directives. In addition, public utilities are subject to the enforcement mechanisms available to parties through the existing judicial appeals process. The Commission addresses the concerns of parties regarding compliance by Ameritech Illinois with past Commission orders in sections 7-204(b)(6) and 7-204(f).

3. National Local Subsidiary

The Commission concludes that the creation of a National Local subsidiary will not affect the Commission's ability to regulate Ameritech Illinois effectively. The Commission must only find that Ameritech Illinois will remain subject to the jurisdiction of the Commission and to all laws, regulations, rules, decisions and policies to the same extent after the merger as before the merger. Accordingly, the Commission finds that Ameritech Illinois' regulatory status will remain unchanged by the reorganization and the creation of a National Local subsidiary. The Commission also references its discussion of the National Local subsidiary further contained within Section III.G. of this Order which contains the Commission's analysis and conclusions of this application for reorganization under section 7-204(b)(7) of the Public Utilities Act.

F. Whether the proposed reorganization is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction. (Section 7-204(b)(6)).

1. Initial Phase

Joint Applicants' Position

According to Joint Applicants, the record establishes that the merger is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction, namely the Illinois intrastate markets for local exchange, intraMSA toll, and interMSA toll. (Joint Applicants' Init. Br. at 31-34).

Joint Applicants first contend that Section 7-204(b)(6) requires the Commission to take the relevant markets as it finds them. The purpose of that Section is not to compel general changes in the overall state of competition, but to ensure that existing competition is not harmed. Id. at 35. Its plain language requires us to address the impact of the merger on "actual" competition, not potential competition. Id. As Mr. Gebhardt made clear in his testimony, any assessment of future competition would be highly speculative, dependent on information not normally available to the Commission, and duplicative of the Department of Justice's ("DOJ") role in reviewing this merger. Id. at 36-37.

Joint Applicants claim that the merger would have no adverse impact on actual competition. Id. at 38. To start with, they stress that the merger would take place at the holding company level and thus would have no direct effect on AI. Its legal and contractual obligations after the merger would be exactly the same as they are now. Moreover, as Dr. Harris testified, the merger would not eliminate any competitors or increase concentration in Illinois because it is "primarily a geographic extension merger." Id. at 38-39.

Joint Applicants and Staff agree that the merger would not impact the Illinois interMSA market. In addition, because SBC does not offer local toll service in any Illinois market, the merger would not impact the Illinois intraMSA toll market. Id. at 39. The same is true with respect to the Illinois local exchange market. Id. at 39-40. According to Mr. Gebhardt, the merger also would not change the market structure in Illinois. Id. at 40. The Commission, and not Ameritech or SBC, sets competitive policy in Illinois. This would not change if the merger were approved. Id.

Staff and Intervenors urge the Commission to consider the effects the merger would have on "potential" competition. Even if we were so inclined, Joint Applicants posit that the merger would not adversely affect potential competition in Illinois. They urge the use of the DOJ Merger Guidelines ("Guidelines") to evaluate mergers in the telecommunications industry, including recent mergers of LECs such as Bell Atlantic/NYNEX and SBC/PacTel. Id. at 42-45. They point out that this Commission has employed the Guidelines in prior merger reviews. Id. at 45.

Joint Applicants contend that, based on the Guidelines, the merger would have no impact on potential competition. Id. at 47. As Dr. Gilbert explained, under the Guidelines, a showing of an adverse effect from a merger or acquisition on potential competition requires all of the following elements: (1) the merger eliminates a firm that had a high probability of entering the market as a new competitor; (2) the merger eliminates a firm that is one of only a few firms that are uniquely situated to enter the industry in the future; and (3) the merger eliminates a firm whose entry would have a substantial deconcentrating effect. Id. at 47-48. Under this test, potential competition

claims relating to out-of-region RBOCs have been uniformly rejected. Id. at 50. The FCC, for example, rejected such claims in the SBC/PacTel and Bell Atlantic/NYNEX mergers. Id. at 50-52.

Joint Applicants argue for the same result in this case. First, SBC is not a likely potential entrant in Illinois. Potential entrance, according to Joint Applicants, has been defined to mean entry in the near future. Id. 49-50; 52. There is no evidence that SBC intends to enter the relevant local markets in Illinois in the near future (id. at 520), and Staff's claim that SBC would enter Illinois "at some point" in the future is irrelevant. Id. at 55. To the contrary, there is sworn and unrebutted evidence that SBC has no such plans. Id. at 52-53. It is important to note that the test is "would" a potential competitor enter Illinois in the "near future," not "could" one do so. Id. at 53. This distinction has been recognized by state commissions and federal courts in analyzing mergers. Id. Thus, claims that SBC has the capacity to compete with Ameritech are irrelevant. Unlike the Guidelines, Staff proposes an approach which is speculative and untested. Id. at 55-56. Moreover, Intervenors' reliance on SBC's wireless service in Illinois to prove that SBC is a potential competitor is inconsistent with sworn testimony. Id. at 56.

Second, SBC is not one of only a few potential competitors of Ameritech Illinois. Id. at 57. The Guidelines require that three or more potential competitors exist after the merger. Id. Even if SBC were viewed as a potential competitor, at least six other firms would also be viewed as competitors, far exceeding the "three or more" standard in the Guidelines. Id. at 57-58. Staff agreed that Bell Atlantic, BellSouth and U S West are potential competitors of Ameritech. In addition, Staff agreed that AT&T, MCI and Sprint are, to one degree or another, potential competitors. Id. at 58.

Third, potential entry by SBC would not have a greater competitive effect than entry by others. Id. at 59. Opponents of the merger have failed to explain how SBC, acting alone, plausibly could have more impact than firms like AT&T, MCI, and Sprint, which have already begun competing with Ameritech Illinois and which have far greater brand name recognition. Id.

Joint Applicants challenge Sprint's position that the merger would harm competition by leading to price discrimination. Id. at 61. This argument was rejected in the SBC/PacTel and Bell Atlantic/NYNEX mergers, because, as the FCC pronounced, "[p]rice discrimination . . . is relatively easy for [the Commission] and others to detect, and is therefore unlikely to occur." SBC/PacTel Order at ¶ 53. They, therefore, urge the Commission to reject this argument here.

Joint Applicants also challenge Sprint's argument that the merger would increase the incentive to discriminate because of the so-called "spillover" effect. This alleged increase in incentive is said to arise because the merger enables the post-merger firm to internalize the spillover benefits that are created outside Illinois from noncompetitive practices undertaken in Illinois. Id. at 62. This argument has been rejected in prior ILEC mergers because any such discrimination is illegal and easy to detect. Id. at 63. Moreover, "spillover" is nothing but an untested and uncertain theory. Id. at 63-67.

Finally, having satisfied Section 7-204(b)(6), Joint Applicants oppose Staff's "conditions" on approval. Id. at 67. They aver that this proceeding is not a "wish list" for issues that are both irrelevant and more properly addressed elsewhere; for example, Staff attempts to resolve the common transport dispute. According to the Joint Applicants, the Commission should reject such efforts because common transport is not in any way linked to the merger, and there is no support for the allegation that the merger would delay its provision. Id. at 67-68. There is also no basis for conditioning approval on Section 271 compliance. Id. at 69. The FCC has recognized that approval of a merger is independent of Section 271 approval (Bell Atlantic/NYNEX Order at ¶ 203), and Joint Applicants urge this Commission to do likewise.

Staff's Position

Staff maintains that any given market's place on the continuum from pure monopoly to perfect competition is determined by the degree of competition which exists within the market. Id. Staff noted that four characteristics establish the degree of competition in any market: (1) the number of buyers and sellers; (2) the standardization of the product; (3) the degree of ease to enter and exit; and (4) the amount of knowledge about the nature and prices of the products. Id.

Staff argues that, according to Section 7-204(b)(6), the Commission has jurisdiction over four markets: (1) local exchange telecommunications service; (2) intraLATA interexchange telecommunications service; (3) interLATA inter-exchange telecommunications service; and (4) cellular telecommunications service. (Staff Init. Br. at 6).

Staff argues that the merger would have an adverse effect on the local exchange telecommunications market in Illinois. Staff advances three bases upon which it opines the proposed merger is likely to have an adverse effect on competition: (1) inhibiting the market's transition to competition, (2) increasing the market's barriers to entry, and (3) eliminating an actual potential competitor from the market. Each of Staff's three positions is premised on the fact that the market currently is not competitive. Staff states that the Guidelines have standards for merger analysis under the Actual Potential Competition doctrine, which is the third basis upon which Staff relies to find that the proposed merger is likely to have an adverse effect on competition. However, Staff points out that the Guidelines do not contain standards for analysis under the other two bases advanced by Staff on this issue.

Staff urges the Commission, when analyzing the proposed merger pursuant to the Actual Potential Competition doctrine, not to apply the Guidelines mechanically because the standards contained in the Guidelines for the number of alternative, similarly situated carriers is too strict to be applied herein. First, Staff explains that th~~ose~~ Guidelines are designed for markets that are substantially less concentrated than the Illinois local exchange market. Id. Staff states that in normal merger analysis, the entry into the market of the number of other firms contained in the guidelines, i.e., three

to six, will have the desired effect of deconcentrating the market. However, the Illinois local exchange market is so substantially concentrated that even if all three remaining RBOCs entered the market and won 15% of the market each, which is a liberal estimate, the market would be deconcentrated only to the point where normal merger analysis begins.

Staff's concern is premised on the local exchange market's current high level of concentration, and anticompetitive characteristics and behavior. Staff contends that the local exchange market in Illinois is a de facto monopoly. Staff explains that de facto monopolies are characterized by one firm which controls a large majority of the market and a number of small or niche providers. Staff notes that 22 carriers besides AI exist in the market; but, despite the presence of these other carriers, Ameritech Illinois controls 96.84% of the market. Staff Init. Brief at 10.

Moreover, of the remaining 3.16% controlled by CLECs, only 0.22% is served by facilities-based carriers. Staff argues that facilities-based carriers add more competition to the market than resellers, because resellers are limited to providing service in the manner that the underlying ILEC provides services and have very little ability, particularly in the long-term, to affect the level of supply or prices. Id. at 11.

Staff noted that a market's concentration level can be measured by the Herfindahl-Hirschman Index ("HHI"). The HHI is the sum of the square of the individual market shares of each firm in an industry. Id. at 10, n. 3. Staff explained that an HHI of 10,000 represents a pure monopoly. Staff's calculation of the HHI of the Illinois local exchange market was above 9,000. Id. at 10.

Staff stated that the Commission's certification and the entry of some CLECs since deregulatory efforts began have failed to have more than a very minor effect on the market's competitive environment. Id. at 57. Id. For competition to be effective, firms must make significant inroads into the market; Otherwise, the dominant firm will simply remain dominant. Id. Accordingly, Staff explained that the Commission needs to determine whether the market is sufficiently deconcentrated. Id. at 59. Staff cited three examples for comparison purposes.

First, Staff cited the case of United States v. Black & Decker Mfg., 430 F. Supp. 729 (1976). Staff noted that in Black & Decker, the relevant market had fluctuating two firm concentration ratios between 54.6% and 48.4%, four firm concentration ratios between 69.5% and 82%, and eight firm concentration ratios between 91.6% and 96.0%. Id. at 56. In the years surrounding the merger, demand increased nearly threefold, prompting a substantial number of firms to enter the market. Id. at 59. While several of the new firms increased sales significantly and two became top ten firms, some of the market's largest firms lost growth and market share. Id. Nonetheless, the court held that the market was not on a trend toward deconcentration.

Second, Staff cited to Mercantile Tx. Corp. v. Board of Governors, 638 F.2d 1255 (5th Cir. 1981). In Mercantile Tx., the two relevant markets had four firm

concentration ratios of 86.1% and 73.8%. Id. at 56. Staff noted that the court found that the market was not sufficiently deconcentrated when only a small amount of evidence of deconcentration existed. Id. at 60.

Third, Staff cited to the example of the slow pace of deconcentration in the long distance market. Id. at 61. Staff stated that in 1984, AT&T had a 90.1% market share, that three years later AT&T's market share had dropped to 78.6%, and that thirteen years later AT&T continues to be the dominant provider with 44.5% of the market share. Id. Even with these significant losses in market share, neither Congress nor the FCC has found that the interexchange market is sufficiently competitive for deregulation. Id.

In comparison, Staff notes that the loss of Ameritech Illinois' market share in the local exchange market since deregulatory efforts began has been significantly less than these three examples. Id. at 59-61. Ameritech Illinois has lost only 3.16% of the market. Id. at 60. Further, the majority of CLEC inroads have been made in the large corporate customer segment, thereby resulting in significantly smaller losses in Ameritech Illinois' market share in other market segments. Id. Accordingly, the lack of a trend towards deconcentration evidences that the market's description as a de facto monopoly is an accurate characterization of the market's competitive structure.

Nonetheless, Staff explained that the most reliable indicator of a market's competitive structure is the existence, or lack thereof, of price competition. Id. at 58. However, Ameritech Illinois recently has been able to move prices away from cost. Staff concludes that competitive forces are not at work restraining Ameritech Illinois' ability to increase price. Therefore, Ameritech Illinois has market power. (Id. at 12.)

Further, Staff stated that AI's market power is protected by significant barriers to entry. Id. at 58. CLECs must incur a variety of sunk costs to enter the market which include advertising costs, equipment and facilities costs, and costs to obtain interconnection, unbundled network elements and collocation. Id. at 12. Also, Staff pointed out that potential entrants usually do not have information about price, cost, traffic patterns and customers' needs and desires. Id. Staff explained that sunk costs and uncertainty increase potential entrants' risk and cost of capital. Id. at 12-13. In addition, Staff stated that consumers often do not have knowledge about services and carriers within the market. Id. at 13.

Staff stated that barriers to entry likely exist because of AI's likely failure to comply with the requirements of Sections 251 and 271 of the Federal Act. Id. Staff explained that these Sections are designed to open AI's control of essential, bottleneck facilities to competitive utilization. Id. At this time, no Ameritech local exchange company has been found to be in compliance with Section 271's requirements. Staff stated that noncompliance causes significant barriers to entry to remain in effect. Id.

Finally, Staff explained that the existence of significant barriers to entry is evidenced by the lack of CLEC penetration during the past three years. Id. at 12. Staff

stated that resale is appropriately viewed as an indication of the level of interest for facilities-based entry. Id. at 11. The resale level in the market is very low, and concluded that the low level of resale evidences the fact that barriers to entry are too high for CLECs to be interested in competitive entry. Id. at 12. Accordingly, after analyzing the market in its entirety, Staff concluded that it is appropriately characterized as a de facto monopoly.

According to Staff, the U. S. Congress, Illinois General Assembly, and this Commission have made clear their intention to open up local exchange markets to competition. Id. at 45-49. The merger, Staff argues, runs counter to this intention because the proposed merger is likely either to allow AI to maintain its market share or to cause its market share ~~it~~ to decrease at an even slower rate. Id. at 49. As the basis for its argument, Staff points out that the proposed merger serves only to provide AI with significant competitive advantages. Id. at 13. First, Staff notes that the combined firm will be the incumbent provider in thirteen states. Id. Staff explains that the company's sheer size will create general efficiencies and economies of scale that are not likely to be available to any other competitor besides, perhaps, a combined Bell Atlantic/GTE. Id. Accordingly, Staff concluded that no company (except possibly Bell Atlantic) would be large enough to compete with SBC/Ameritech. Id. at 49-50.

Second, Staff points out that the proposed merger will enable AI to undertake the NLS. Id. Staff explains that the NLS will make CLECs less effective in competing for large corporate customers; in fact, it is undisputed that the NLS is premised on retaining large corporate customers. Id. Staff cites to the admission by Joint Applicants' economic witness, Dr. Harris, that the proposed merger will "reduce [Ameritech Illinois'] loss of market share" in the large corporate segment." Id. at 13-14 (citing SBC-Ameritech Ex. 4.1 at 11).

Moreover, Staff recognized that the Company's increased ability to retain large corporate customers is likely to reduce competitors' incentive to enter Illinois. Id. at 50. The quest for profits provides competitors with the incentive to enter new markets, and large corporate customers provide carriers with the largest profit potential. Id. The proposed merger will result in competitors having more difficulty attempting to win large corporate customers and, therefore, new carriers will have less of an incentive to enter the local exchange market. Id.

Ultimately, Staff concluded that the proposed merger's inhibition on the transition of the market from monopoly to competition is a significant adverse effect on competition. Moreover, in addition to the result violating subsection 7-204(b)(6), Staff explained that this result is in direct conflict with the goal and stated intent of state and federal lawmakers which govern the Commission's actions. Accordingly, the Commission must reject the proposed merger.

Further, as approval of the merger would be a choice in favor of regulation over competition (again in direct conflict with the intent of state and federal lawmakers), Staff believed it imperative to realize the level of difficulty which would be involved in

regulating Ameritech Illinois post merger. Id. at 50-51. First, Staff explained that companies act in response to incentives to increase profits by protecting their market shares. Id. at 50. Therefore, even though a company that has market power may not make a conscious choice to behave anticompetitively, the company's actions will be controlled by its profit potential. Id. (citing, United States v. Falstaff Brewing Corp., 410 U.S. 526, 548 (J. Marshall, concurring).

Moreover, Staff explained that the Commission's ability to effectively regulate AI would be inhibited by SBC/Ameritech's size and scope. Id. at 50-51. The Commission's ability to regulate Ameritech Illinois will be further complicated by the combined company's increased network of affiliates, both regulated and unregulated. Id. at 50. Staff urged the Commission to reject the proposed merger on the basis that it will inhibit the market's transition from monopoly to competition.

According to Staff, the merger is likely to have a significant adverse effect on competition by increasing the market's barriers to entry or, at the least, creating a situation in which the market's barriers to entry are not likely to decline. Id. at 14-19, 51-53. The proposed merger is likely to increase uncertainties about the adoption of an eventual Operations Service System ("OSS") platform, resale prices, and UNE terms and conditions. Id. at 14, 52. This increased uncertainty increases competitors' risk and cost of capital.

The level of information in the market will decline if SBC would have otherwise entered the market as a direct competitor to Ameritech Illinois. Id. at 15, 51. Staff stated that SBC has extensive experience in providing local exchange services and possesses knowledge about the market that other CLECs and potential CLECs do not possess. Id. at 15. Staff concluded that the loss of SBC as a direct competitor decreases the level of information that CLECs otherwise would possess. Id. By eliminating SBC as a CLEC, the level of disparity in information between AI and CLECs will increase. Id. At 51. Also, Staff recognized that some Illinois consumers have information about SBC because it operates as the ILEC in St. Louis and is affiliated with Cellular One. Id. at 15. Accordingly, Staff determined that the loss of SBC as a CLEC in Illinois means that consumers have less information about competitive carriers. Id.

Staff cited evidence which demonstrates that SBC's past conduct has made it difficult for other state commissions to implement pro-competitive policies. Id. at 14-15. Other jurisdictions have found that SBC has engaged in anti-competitive marketing activities and non-compliance with collocation requirements. Id. at 14, 52. Also, Staff acknowledged that SBC may have satisfied fewer Section 271 checklist requirements than Ameritech Illinois. Id. at 14-15, 52. Staff conveyed that the implementation of SBC's anti-competitive practices in Illinois definitely will increase the market's barriers to entry. Id. at 15.

Staff explained that the proposed merger will increase CLECs' sunk costs, such as marketing and advertising expenses. The proposed merger will result in a stronger AI with an increased ability to retain customers and market share. Accordingly, CLECs

will have to engage in even more advertising and marketing activities to attempt to win customers away from a post-merger Ameritech Illinois. Id. at 51.

Staff opined that the proposed merger will increase barriers to entry because it will expand its scope and reach, thereby increasing its ability and incentive to engage in non-price discrimination. Id. at 15. Staff explained that non-price discrimination could take many forms. Id. For instance, AI could prevent its competitors from providing service by delaying or denying the availability of bottleneck facilities. Id. at 16. Also, the combined entity's increased size and superior resource base will allow it to engage in a variety of activities which may include anticompetitive conduct such as cross-subsidization, selective price-cutting, intensive advertising and marketing campaigns, and strategic pricing. Id. at 18-19.

Staff contends that the proposed merger will likely result in small and large scale forbearance. Staff contends that SBC and Bell Atlantic will attempt to control the western and eastern United States' markets and are likely to forbear from any large scale entry into each other's incumbent territories.

Next, Staff opined that the proposed merger increases AI's ability and incentive to engage in tied contracts, which are arrangements where the sale of one product requires, as a condition of that sale, the purchase of a second product. Id. Staff explained that the ability to spread tied contracts over other affiliates, subsidiaries and jurisdictions decreases the risks of detection. Id. at 18. Accordingly, the combined firm's ability to spread such activity will increase its ability to engage in the activity. Id.

Finally, Staff stated that the proposed merger will increase Ameritech Illinois' ability and incentive to deal exclusively. Id. Exclusive dealing is an agreement or a requirement by a buyer to purchase all, or a certain portion, of some commodity from a particular seller; or a particular firm agrees to sell only the products of a particular manufacturer. SBC could decide to make any service rendered to Ameritech a profit center. (Staff Ex. 9.0 at 65).

As its third argument, Staff applies the well-developed Actual Potential Competition doctrine to the facts of this proceeding. Staff explained that the federal courts have developed precedent for this doctrine under Section 7 of the Clayton Act which requires an analysis of whether "the effect of [an] acquisition may be substantially to lessen competition or tend to create a monopoly." Staff Initial Brief at 55. The elements which the courts have found necessary to satisfy the doctrine are as follows:

1. the market is concentrated;
2. the acquiring firm plans on entering the market through the acquisition of a dominant firm;
3. the acquiring firm would have likely entered the market either through de novo expansion or a toe-hold acquisition absent the merger; and

4. either de novo entry or entry through a toe-hold acquisition by the acquiring firm would have been likely to deconcentrate the market or result in other procompetitive effects.

Id. at 54.

Staff did not object in general to utilizing the Guidelines to analyze the applicability of this doctrine to the proposed merger because the elements which the Guidelines establish generally follow the test established by the federal courts. Id. at 37. One significant difference, according to Staff, is that the Guidelines treat the existence of similarly situated firms as an express element while the federal courts tend to consider the existence of such firms as a factor which mitigates the significance of the effect which the acquiring firm would otherwise likely have on the market. See, Id. at 71.

However, regarding the Guidelines' second element, Staff noted that it indicates that a proposed merger is not likely to have a significant adverse effect on competition when three other similarly situated firms exist, and is presumed not to have such an effect when six other similarly situated firms exist. Id. at 37. Staff emphasized that the Commission should not apply this portion of the DOJ's standards strictly. First, it stated that the Guidelines are discretionary. Id. at 26, n. 14. Second, the Guidelines are usually applied to markets with significantly less concentration than Illinois' local exchange market. Id. at 37. Staff explained that when markets are significantly less concentrated, the interjection of three to six competitors may be sufficient to transition the markets to competition. Id. at 37-38. However, Illinois' local exchange markets would need the interjection of significantly more competitors to transition the market to competition. Staff provided the highly optimistic example of all three remaining RBOCs successfully entering the market and winning 15% of the market each. In that scenario, the market's concentration level would be reduced only to the point where normal merger analysis begins. Id. at 38. Staff opined that this fact, combined with the clear legislative intent to transition the market to competition, established that the Commission should evaluate this element more conservatively. Id.

Staff's analysis revealed that the first prong is satisfied because the market is concentrated. Id. at 55-61. The same evidence and method of analysis which Staff utilized to find that the proposed merger raised competitive concerns because of the market's current anticompetitive structure satisfies this element of the Actual Potential Competition doctrine's test. Staff noted that AI's sole control of 96.84% of the local exchange market clearly meets this prong. Id. Further, Staff noted that complete analysis of the market demonstrates that its concentration ratio is consistent with its competitive structure. Id. at 57-61.

Next, Staff stated that the test's second prong is satisfied because the proposed merger seeks to acquire AI which is the market's dominant firm. Id. at 62.

Applying the third prong, Staff surmised that SBC likely would enter the market either through de novo expansion or a toe-hold acquisition in the absence of the proposed merger. Id. at 62-68. Staff noted that three elements must be met to satisfy this prong of the test. First, one must determine that the acquiring firm has available feasible means for entering the market other than through acquisition. Second, a reasonable probability must exist that the acquiring firm would enter the market in the absence of the acquisition. Third, the acquiring firm must be likely to enter the market within a reasonable period of time. Id. at 62, 64-65.

As to the first of these elements, of Staff stated that no legal barriers prevent SBC from entering the market independently. Further, SBC has admitted that it has the financial resources to enter the market independently. Also, Staff opined that the market's barriers to entry are less significant for SBC.

In terms of the second element, Staff found that a sufficient likelihood exists that SBC would enter the market in the absence of the merger. Id. at 64-67. Staff noted that anticipated profitability from independent entry is more substantial than anticipated profitability from other ventures. Staff stated that revenues from large corporate customers constitute approximately 18% of total AI revenues even though the segment constitutes a small percentage of total customers, and that large corporate customers want one stop shopping. Staff noted that SBC's management, as evidenced by its NLS, believes that serving large corporate customers as a CLEC will be extremely profitable. Chicago is one of the most profitable locations to accomplish this goal because of its size and large business community. Finally, Staff noted that SBC has made a commitment to expand its service beyond regional provision of local exchange services. Accordingly, Staff concluded that the objective evidence establishes a reasonable probability that SBC would enter the market in the absence of the merger. Id. at 65-66.

Further, Staff pointed out that a number of options exist for SBC to enter the market. It could acquire a small, niche provider, enter de novo, or expand through an affiliate. Regardless of the method which SBC utilizes, the objective evidence shows that it will pursue entry into Illinois. Id. In fact, Staff pointed out that SBC had planned entry into Illinois in the past, even obtaining certification from the Commission. Therefore, its current plans to enter through the acquisition of Ameritech actually represent its second method to enter Illinois. Id. at 67.

In terms of the third element, Staff found that SBC would enter the market in a reasonable period of time. Staff explained that the necessary time frame for potential entry is dependent on the market's structure. Id. at 67-68. More specifically, Staff stated that entry must be likely within the period of time that the market will not have sufficiently changed such that the pro-competitive effects that are likely to result from entry are no longer needed. Id. Staff opined that SBC would likely enter the market in the next three to five years. Tr. at 1621, 1716. Given the market's extremely slow rate of deconcentration, Staff found that the market is likely to be characterized as

significantly concentrated for many years into the future, sufficiently covering the three to five years anticipated for SBC's independent entry. Id.

Returning to the last prong, Staff found that independent entry by SBC offers a substantial likelihood of ultimately producing deconcentration or other procompetitive effects. Id. at 68-71. Staff noted that at issue in this prong of the test is the degree of effect on the market the new entrant needs to have in order for the effect to be considered significant. Staff cited to several federal court cases which have held that the new entrant's inroads into the market do not have to deconcentrate the market single-handedly. Id. at 68 (citing Mercantile, 638 F.2d at 1270). Instead, the courts have held that even modest inroads into the market can be significant. Id. at 69 (citing BOC Intern. Ltd. v. FTC, 557 F.2d 24, 27 (2nd Cir. 1977)). In fact, the courts have held that significant procompetitive effect exists merely from a new entrant "shaking things up" or engendering competitive motion. Id.

Staff explained that even modest inroads by SBC into the market would be significant, especially when the extremely high level of market concentration is considered. For example, CLECs provide service through the use of unbundled loops to only .22% of Ameritech Illinois' customers. Staff provided evidence that if SBC could win merely 1% of its cellular customers, or if it could utilize its switches in the Chicago area, the number of customers served by CLECs and the number of CLEC switches would increase significantly. Id. at 70.

Further, Staff opined that SBC could have a significant impact on competition by reselling vertical services, a product area in which it has successfully utilized its marketing abilities in its incumbent states and California. Id. at 23. Finally, of the 13 facilities-based CLECs in Illinois, only three provide service outside of Chicago. If SBC entered Illinois outside of Chicago, its entry would increase the number of providers in down-state Illinois by 25%. At the least, SBC's entry would shake things up and engender competitive motion. As all of its examples are conservative, Staff concluded that SBC's entry would clearly be very significant. Id. at 22-24, 68-70.

Finally, Staff concluded that an insufficient number of similarly situated competitors exist to eliminate the need to require SBC to enter independently. Id. at 71. Staff opined that the large inter-exchange firms such as AT&T, MCI/WorldCom and Sprint already have entered the market but have not shown an ability to deconcentrate the market to a sufficient degree. Id. at 39, 71. Accordingly, Staff explained that it would be erroneous to rely on those firms to deconcentrate the market to a sufficient degree. Id. at 39. But most importantly, Staff stated that it is inappropriate to consider those firms as actual potential competitors because those firms are currently competing in the market. Staff Ex. 9.0 at 11. [The issue of actual potential competition was further addressed on reopening. See the subsequent discussion on page **xx** this section for an elaboration of Staff's position].

Staff believes that sufficient conditions do not exist that would mitigate the harms to competition Staff Reply Brief at 74. As explained in its arguments, the proposed

merger will make it harder for competitive carriers to enter Illinois and successfully compete. Accordingly, if the Commission decides to approve the proposed merger, then Staff opines that the Commission should ascertain that the local exchange market is open to competition to the greatest extent possible. Id. In other words, the Commission should undertake measures to ensure that all barriers to entry which can be eliminated are eliminated. Id.

When Congress enacted TA96, Congress found that significant barriers to entry existed in the local exchange market because of the ILECs' control of the local exchange network. Congress designed Sections 251 and 271 to eliminate some of those entry barriers. Id. At this time, neither SBC nor Ameritech has been found to be fully compliant with those Sections. To the extent that other Ameritech and SBC states are not in compliance, the Commission risks having the management of the combined firm incorporate areas of non-compliance into Illinois. Id.

Accordingly, Staff opines that the Commission should require AI and SBC to demonstrate compliance with Sections 251 and 271 to the Commission. Id. at 72-73. Staff states that such action would not exceed the Commission's jurisdiction because it would not be acting to determine whether the Joint Applicants should receive Section 271 authority to provide in-region interLATA service or to coerce the Joint Applicants to comply with the sections' mandates in other states. Id. at 78. Instead, the Commission merely will be reviewing compliance as a prerequisite to merger consummation in Illinois. Id.

Staff states that the Commission has two methods for reviewing compliance. First, the Commission could begin a collaborative process immediately for a period of two to three months. Staff Initial Brief at 72-73. Then, the Commission could reopen the record to provide information about the process and its results. Id. at 73. Second, the Commission can deny the merger because of its failure to satisfy Section 7-204(b)(6). Id. At the same time, the Commission could institute a collaborative process. Id. Then, the Joint Applicants could seek to have their proposed merger approved based on the results of the process by refilling their petition with the Commission. Id.

Staff also explains that it is necessary to require AI to offer common transport in accordance with the Commission's order in Docket 96-0486/96-0569, cons. Staff points out that AI has failed to offer common transport as required by the Commission and that this failure has had an adverse effect on competition. Staff voiced its concern that a merger would likely produce reorganizations of functions and staff, and ultimately delay the provisioning of the service. Staff also pointed out that SBC provides a version of common transport to competitive carriers and that Ameritech should be directed, as previously ordered in Docket 96-0486/96-0569 Consol, to provide the service. (Staff Init. Br. at 74-77).

Staff concedes that the merger is not likely to have a significant adverse effect on competition for interMSA toll markets in Illinois. Id. at 77-82. Staff, however,

believes that the merger may have an adverse effect on competition for intraMSA toll service. Despite the large number of buyers and sellers of intraMSA in Illinois, AI continues to exert some market power over that market; and SBC's_elimination as a potential competitor in the local exchange market will have an adverse impact on that market which may spill over into the intraMSA toll market and make it more difficult for new companies to enter that market. Id. at 82-90.

Finally, Staff takes the position that the proposed merger may have an adverse impact on competition in the cellular markets in Illinois for two reasons. First, now that SBC and Ameritech have proposed to merge and are in the process of divesting one of their cellular properties, they have the economic incentive to cease acting as mutual competitors during this transition period. Second, the long-term contracts prevalent in the cellular market created a significant uncertainty regarding the impact of the proposed merger on competition in that market. Id. at 90-92. Recognizing the limits on the Commission's jurisdiction over cellular markets, Staff makes no recommendations to address the first issue. However, Staff makes recommendations to address its second concern urging the Commission to condition approval of the merger on certain notice requirements it has specified.

Intervenors' Positions

AT&T's opposition to the proposed merger focuses almost exclusively on Section 7-204(b)(6). It argues that the Commission must assess the likely impact of the merger "on the market-opening process" in reaching an ultimate determination on whether it satisfies the standard of Section 7-204(b)(6). (AT&T Init. Br. at 10). In addition, AT&T claims that the "public convenience" test of Section 7-102 should be used by the Commission. Id. at 10-11.

AT&T first challenges Joint Applicants' position that this merger would have no effect on AI because the merger would take place at the holding company level. AT&T contends that this argument ignores the effect the merger would have on the market-opening process. Id. at 11. A combined Ameritech/SBC, according to AT&T, would have both an enhanced ability to forestall competitive entry and an increased incentive to do so. Id.

AT&T also claims the merger is inherently anti-competitive. According to AT&T, rather than competing for local exchange service with other ILECs, SBC has decided to acquire them and further strengthen its hold on local access service. AT&T suggests that approval of the merger would only increase SBC's incentive to resist competition in Illinois. SBC is paying a premium to acquire Ameritech and, according to AT&T, it would not pay a premium if it planned to open the Illinois markets up to competition. Id. at 14. Indeed, AT&T argues that the merger would permit SBC to capture more of the benefits of its anti-competitive activities.

If the merger were approved, AT&T contends that there would be a "2-RBOC" world, dominated by SBC in the west and Bell Atlantic in the east. Id. at 16. Together,

these RBOCs would control almost 75% of the nation's business access lines. CLECs have made few inroads into the local access market, with little progress there having occurred with business customers. SBC's motivation behind the merger -- to acquire business customers in 30 large cities out-of-region -- is designed, according to AT&T, to preclude the only inroads CLECs have made into local markets. Id. at 17.

AT&T also posits that the merger would harm competition because it would eliminate one of Ameritech's largest and most able future competitors. Id. at 18. AT&T points out, in fact, that SBC is more than a potential competitor of Ameritech -- it is a current competitor. SBC competes with Ameritech for wireless service in Illinois, and is authorized to provide local access service. Based on SBC's geographic proximity and history in Illinois, AT&T believes SBC is a natural competitor of Ameritech. It argues that SBC would enter Illinois even if the merger were rejected. Id. at 20. AT&T believes that acquiring Ameritech is simply an "easier path" into Illinois for SBC than competing with Ameritech. Id.

AT&T also contends that the merger would substantially reduce the benchmarks available to the Commission to judge the incumbent's performance on issues such as TELRIC, Section 271 proceedings, and TA96 arbitrations. Id. at 20-21. Currently, the Commission has several ILECs to use as comparables; if this merger and the Bell Atlantic/GTE merger were approved, there would be only three.

In addition, AT&T challenges Joint Applicants' claim that their NLS would result in increased competition in Illinois because their entry into other ILECs' regions would cause retaliatory entry into Joint Applicants' regions (including Illinois). Initially, it insists that retaliatory entry is a theory held by only SBC, and has no economic or empirical support. Id. at 23. Moreover, AT&T claims that this theory is flawed. For the theory to work, SBC would have to enter and win business in out-of-region markets. AT&T points to SBC's Project North Star projections as evidence of the inherent uncertainty and speculative nature of winning business customers out-of-region. Id. at 24.

AT&T asserts that SBC's NLS is no different than the marketing strategy of many CLECs. It is premised on SBC serving out-of-region customers via UNEs. AT&T believes that SBC would face the same anti-competitive roadblocks from other ILECs that CLECs face. AT&T also argues that the NLS would not increase competition for large business customers because there are several ILECs and CLECs (including AT&T) currently vying for that lucrative business. If it is other ILECs that SBC is hoping to attract as competitors, AT&T claims that this refutes SBC's claims that both it and Ameritech are each too small to compete for national businesses. Id. at 27. The remaining ILECs are not appreciably larger than SBC (except a combined Bell Atlantic/GTE).

AT&T also challenges SBC's claim that it cannot pursue National-Local entry without the merger. First, it points out that SBC has the necessary capital to pursue such entry. Second, it claims that there is no evidence that a company needs to control a large base of Fortune 500 customers -- as SBC contends -- in order to compete on a

national scale. Small CLECs, such as TCG and Brooks Fiber, have entered such markets without a large Fortune 500 base. AT&T also believes that SBC has more than enough employees to pursue National-Local entry. Lastly, AT&T contends that there is no credible evidence that the NLS would dilute the value of SBC's shares.

AT&T posits that Ameritech's St. Louis entry demonstrates the fallacy of retaliatory entry. Prior to the merger, Ameritech allegedly entered the St. Louis local access market. But, rather than retaliate by entering an Ameritech market, SBC did nothing. AT&T also claims that Ameritech planned a full-scale entry into the St. Louis market prior to the merger. AT&T claims that this proves Ameritech and SBC are each currently capable of out-of-region entry.

Further, AT&T argues that SBC's track record does not support its claim that the merger would improve competition in Illinois. Id. at 37. According to AT&T, SBC has used aggressive litigation tactics and exorbitant collocation prices to thwart competition in the Texas and California local exchange markets. AT&T points to the denial of SBC's Section 271 applications as evidence of SBC's anti-competitive behavior.

Finally, AT&T contends that it is not possible to craft “conditions” to protect against the anti-competitive impact of the merger. Id. at 44. It believes that such conditions are ill-suited for competitive issues because they address the symptoms rather than the causes of the underlying problem. The cause, according to AT&T, is the inherent conflict of interest ILECs have in allowing competitors entry into their markets. As an alternative to the conditional approach, AT&T proposes that ownership of the Company's network facilities be completely separated from its retail and other activities as a prerequisite to a merger with SBC. Id. at 44-45. AT&T suggests that the Commission use the 1984 divestiture of AT&T as a guide for this separation.
Id. at 50.

Sprint opposes the merger on many of the same grounds as AT&T. It first urges the Commission not to restrict its competition analysis solely to the application of antitrust law. Rather, it urges the Commission to apply the broad range of public interest factors it claims are set forth in Sections 7-204(b)(6) and (7). (Sprint Init. Br. at 11). The DOJ and FCC, according to Sprint, have recognized that antitrust guidelines should not be applied mechanically to mergers in the telecommunications industry. Id. at 13. Moreover, Sprint alleges that one of the factors in the Guidelines -- the presence of actual competitors -- is unproven here because AT&T, Sprint and MCI are not true competitors of Ameritech in Illinois. Id. at 14-15.

Sprint claims that the merger would have an adverse impact on competition for local exchange service in Illinois because Ameritech would be losing a significant potential competitor (SBC). Id. at 16. SBC views itself as a leader in national and international telephone service. Its national ambitions predate the merger. Thus, SBC is a natural competitor of Ameritech. Sprint also claims that SBC possesses the necessary assets to compete with Ameritech in Illinois. Id. 23-24.

Sprint argues that, based on SBC's geographic proximity to Illinois and well-recognized brand name, SBC is one of a small number of significant potential entrants into the Illinois local exchange market. Id. at 19. It maintains that, prior to the merger, SBC had made clear its plan to enter the Chicago local exchange market. Sprint disputes SBC's claim that it abandoned its plan to enter that market based on its experience in Rochester. Sprint contends that Rochester experiment is not comparable to SBC's Chicago plans. Id. at 22-23.

Sprint argues that AI currently has the ability and incentive to engage in exclusionary behavior in Illinois. AI accounts for 97 percent of all network minutes of use in Illinois. Id. at 27. Sprint points to the denial of Ameritech's Section 271 applications, and disputes over shared transport, ISP reciprocal compensation, and OSS as evidence of the Company's exclusionary behavior. SBC's track record, argues Sprint, is no better. Id. at 28-29. It contends that the merger would serve only to increase AI's incentives to engage in exclusionary behavior because of the "spillover" effect of such conduct. Whenever a CLEC is discriminated against by a particular ILEC, such discrimination weakens its position on a national scale, making it more difficult to compete with all ILECs. Id. at 29-30. Before the merger, Ameritech would not have profited from such spillover, but the same would not be true after the merger. Id. at 31-32. Joint Applicants, according to Sprint, have failed to rebut this spillover argument.

Sprint also contends that the merger would reduce substantially the benchmarks available to the Commission to judge the incumbent's performance on issues such as TELRIC, Section 271 proceedings, and TA96 arbitrations. Id. at 33-34. Currently, the Commission has five ILECs to use as comparables; if this merger and the Bell Atlantic-GTE merger were approved, there would be only three.

In addition, Sprint contends that the merger would have an adverse effect on competition in the interexchange market. Id. at 35. According to Sprint, if the merger were approved and if Ameritech Illinois were awarded Section 271 authorization, it would have an incentive to favor SBC interexchange traffic over that of all other carriers. Id. at 36.

Like AT&T, Sprint challenges the NLS. It claims that SBC has been internally inconsistent and confusing in its attempts to explain this strategy. Id. at 41-42. It contends that SBC's actual strategy is to increase the size of its local monopoly by controlling as many access lines as possible in the United States. The larger SBC becomes, the greater its ability to discriminate against rivals. Id. at 43-44. According to Sprint, "SBC simply wants to acquire Ameritech because it is the least risky way to grow." Id. at 44.

The merger also reduces the number of large markets in which SBC would have to compete. By acquiring Ameritech, SBC gains seven of the top 50 markets without competing. Id. at 45. This would give SBC a tremendous advantage in the interexchange market once it obtains Section 271 authorization. Id. at 46.

Sprint claims that the merger is not necessary for SBC to compete on a national scale. SBC currently has the financial and human resources to compete out-of-region. Id. at 47-51. Sprint claims that SBC declared its intentions to compete nationally before the merger was announced. Id. at 48. Moreover, It argues that there is no credible evidence that SBC's stock price would be negatively affected if it initiated the NLS without Ameritech. Id. at 50. Sprint contends that Ameritech also had the ability to compete out-of-region before the merger. Id. at 51. Sprint points to AI's Managed Local Access ("MLA") plan and its entry into the St. Louis market as evidence of this ability. Id. at 51-55.

Sprint also challenges SBC's retaliatory entry theory. Sprint argues that "[f]ar from encouraging entry by other large ILECs, the merger will magnify the effect of the market power that Ameritech Illinois currently has in the provision of local exchange services." Id. at 55. Sprint claims that the fallacy of retaliatory entry is shown by SBC's failure to retaliate against Ameritech for its MLA plan or its entry into the St. Louis market. Id. at 55-56. Moreover, even if the retaliatory entry theory were sound, Sprint claims that its effect on competition in Illinois would be a wash. Id. at 57.

Sprint asserts that SBC is currently authorized to provide one-stop shopping to its large business customers out-of-region. Id. at 58. Indeed, Sprint argues that SBC would be certain to do so if the merger were denied. Id. 57-58. Sprint also challenges SBC's claims that other efficiencies (e.g., stronger incentive to innovate, transfer of best practices, and scale efficiencies) would result from the merger. Sprint claims there is no evidence to support these allegations. Id. at 61-64.

Without making express reference to Section 7-204(b)(6), MCI argues that the merger would affect adversely competition for local exchange service in Illinois. First, MCI claims that the merger should be rejected because Ameritech and SBC have thwarted local exchange competition in their respective regions. To evidence this, MCI points to the rejection and non-renewal of Ameritech's and SBC's Section 271 applications, as well as disputes which have arisen between Ameritech and various CLECs over shared transport and reciprocal compensation for ISP traffic. (MCI Init. Br. at 9-14).

MCI also questions Joint Applicants' National-Local Strategy. MCI believes this strategy is not designed to enhance national competition, but rather to "raise even higher barriers to local entry and lock up a critical group of local customers -- large business customers." Id. at 14. According to MCI, Joint Applicants intend to use their combined monopolies to exclude competition for lucrative large business customers in the combined region. In so arguing, MCI agrees with AT&T that they are attempting to combine "the advantages of geographic reach with the advantages of incumbency." Id. at 17-18. If the merger were approved, MCI contends that it would be harder for CLECs to compete with them to provide facilities-based local services to customers, particularly national and regional businesses.

In addition, MCI claims that the merger would eliminate a potential local competitor (SBC) from Illinois. It also challenges Joint Applicants' claim that they are each too small to compete on a national scale. They believe that $2 billion of capital expenditures would be necessary to compete out-of-region. MCI argues that Ameritech and SBC each has the resources to make such capital expenditures. MCI points to the billions of dollars SBC and Ameritech have invested in overseas markets as evidence of each company's ability to raise $2 billion. In any event, MCI argues that companies much smaller than a combined Ameritech/SBC compete on a national scale.

Finally, MCI claims that competition by an existing ILEC in another's territory -- via UNEs -- would help eliminate obstructionism by monopolistic ILECs, because an ILEC, as opposed to a CLEC, would be in a better position to challenge the obstructionist behavior of another ILEC.

Nextlink opposes the merger claiming it would affect competition in Illinois adversely by creating an "enormous incumbent monopoly with control over monopoly bottleneck facilities in several key markets" (Nextlink Init. Br. at 4), and by removing potential competitors (SBMS Illinois, Inc. and SBC) from the local exchange and the long distance markets in Illinois. It also claims that SBC has a poor history of competitive behavior, pointing to the denial of SBC's Section 271 applications and its record in California since its acquisition of Pacific Bell. Nextlink contends "that SBC has acted to frustrate and limit competition in California" (id. at 9), and it provides several examples of alleged discrimination it claims to have experienced in California at the hands of SBC.

In addition, Nextlink challenges SBC's retaliatory entry theory. Nextlink contends that the retaliatory entry theory is inapplicable where one incumbent monopoly acquires another. Moreover, it argues that the facts in this proceeding undercut the retaliatory entry theory. Prior to the merger, Ameritech had taken steps to compete in SBC's markets. According to the retaliatory entry theory, this should have caused SBC to take steps to compete in Ameritech's markets. Nextlink argues, however, that instead of competing with Ameritech, SBC chose to acquire it. This action, says Nextlink, undercuts the notion of retaliatory entry.

Finally, Nextlink argues that SBC's NLS is an insufficient basis for approving the merger because: (1) that strategy is infeasible unless and until Joint Applicants obtain in-region long distance authority; (2) SBC's claim that it is not large enough to compete outside its own region is belied by the fact that many small telephone companies are competing on a national scale; and (3) SBC's NLS would do nothing to promote competition in Illinois because, by its very definition, it would be carried out in states other than Illinois.

CTCA concurs with Staff on the following points: (1) the markets over which the Commission has jurisdiction; (2) the definition of a competitive market; and (3) use of the "perfectly competitive" model to determine Joint Applicants' compliance with Section 7-204(b)(6). As a result, CTCA agrees with Staff's recommendation to deny the merger

or, alternatively, to condition the merger on Joint Applicants' full compliance with Sections 251 and 271 of the TA96.

21st Century opposes the merger. It argues that the Commission cannot approve the merger unless it finds that the merger satisfies the "public interest" tests of Sections 214(a) and 310(d) of TA96. It claims that these tests, as interpreted by the FCC in its SBC/SNET Order, require Joint Applicants to show that Ameritech and SBC are not competitors or potential competitors, and that SBC is unlikely to have substantial future competitive significance in Illinois. 21st Century claims that they have failed to make these showings.

21st Century believes the merger would eliminate a significant potential competitor in the local exchange market in Illinois. It maintains that, prior to the merger, SBC was in a position to, and declared its intentions to, compete in Illinois markets with both facilities-based and wireless initiatives, which it asserts is proven by SBC's decision to maintain significant assets in Illinois and by its brand name recognition in Illinois. 21st Century also claims that SBC's intentions were made clear in submissions it made to state commissions in California and Illinois. In short, it claims that, absent the merger, SBC would have become a significant competitor of Ameritech for local exchange service in Illinois. (21st Century Init. Br. at 10-14).

21st Century also argues that, prior to the merger, Ameritech intended to, and to some extent did, compete with SBC for local exchange service in SBC's region. In addition, it challenges SBC's NLS, claiming that SBC is large enough to pursue such a strategy without the merger.

Cook County opposes the merger, claiming it "would lead both to diminished actual and potential competition in Illinois and in the Ameritech region generally by removing SBC as a potential entrant and by fortifying the merged company's ability to protect its entrenched position of market dominance against competitive inroads." (Cook County Init. Br. at 28). First, Cook County claims that, contrary to SBC's position in this proceeding, SBC intended to compete with Ameritech in Illinois prior to the merger. Indeed, considering its geographic proximity and national market entry strategy, SBC was the RBOC most likely to compete with Ameritech.

Second, Cook County agrees with Joint Applicants that the Guidelines provide a useful basis for analyzing competition in this proceeding. But it believes that the final determination must be based on the Commission's own rules and regulations.

Third, Cook County questions the relevance of SBC's experience with wireless service in Rochester. It believes that the Rochester market is too small to serve as a comparable to Chicago. It also claims that Ameritech's wireless experience in St. Louis is inapposite.

Fourth, Cook County urges the Commission to reject the merger because, unlike the Bell Atlantic/NYNEX merger, this proceeding involves the acquisition of an ILEC by

a larger, competitive ILEC. Moreover, it argues that, if the merger takes place, there would be one less ILEC which state commissions could use to make cross-carrier comparisons for such things as technical feasibility and reasonableness.

Fifth, Cook County questions SBC's claim that, without the merger, it would be unable to compete with the likes of AT&T, MCI, etc. Cook County contends that SBC is the third largest RBOC in the United States.

Sixth, Cook County argues that both Ameritech and SBC have successfully staved off local exchange competition in their respective regions and, if the merger were approved, they would combine their monopoly powers further to entrench their hold on local exchange service.

Seventh, Cook County points out that, according to its NLS, SBC anticipates only a 4 percent overall penetration rate in the 30 targeted markets. Therefore, even if the retaliatory entry theory were sound, Cook County claims that AI could expect to lose only 4 percent of its customers, still leaving it with a 96 percent share.

Finally, Cook County urges the Commission to take account of SBC's failure to comply with the Section 271 competitive checklist, demonstrated by the denial of its Section 271 applications in Texas and California.

The AG argues that Section 7-204(b)(6) is concerned with the "likelihood" of adverse competitive effects, and not the actual occurrence of such effects. (AG Init. Br. at 9). The term "likelihood," it argues, requires "an evaluation of what is expected or what is probable -- in short, an assessment of the future." Id.

The AG also claims that, prior to the merger, SBC was the RBOC most likely to compete with Ameritech for local exchange service in Illinois. Indeed, SBC's CLEC affiliate, SBMS Illinois, had obtained authority to operate as a local exchange provider in Illinois prior to the merger. SBC's claim that it had canceled its plans to compete in Illinois because of its experience in Rochester, is, according to the AG, "unconvincing[]." The AG argues that SBC did not make a good faith effort to succeed in Rochester and thus that experience is irrelevant.The AG claims that Ameritech and SBC each currently have the power to compete out-of-region, pointing to the Ameritech's Gateway Project in St. Louis -- prior to its pre-merger cancellation -- as support.

The AG also claims that SBC's retaliatory entry theory is a "dubious promise." Id. at 13. There is no evidence in the record, it claims, that SBC's projected retaliatory entry would be of a price-constraining nature. Absent price-constraining competition, there is no true competition. It asserts that the mere existence of competitors in Illinois does not mean there is competition in Illinois.

According to the AG, SBC's Strategy ignores an important segment of the market -- residential and small business customers. The AG also argues that SBC's Strategy is speculative, and that SBC's own witnesses could not accurately project the

amount of competition that would result from this strategy, particularly with respect to residential and small business service.In addition, the AG argues that if Joint Applicants are correct in their belief that only a company the size of a combined Ameritech/SBC is capable of competing on a national scale, that means that a combined Ameritech/SBC would face little or no competition in Illinois because no other company (except possibly a combined Bell Atlantic/NYNEX/GTE) would have the resources to enter the local exchange market in Illinois. As a result, the AG argues that the merger would reduce -- and not increase -- the number of competitors in the local exchange market. Id. at 18.

Finally, the AG questions the practicality of SBC's Strategy. SBC claims the Strategy is designed to offer "one-stop shopping" of local and long distance service to customers in the Joint Applicants' regions. Id. SBC claims it will commence such strategy immediately following the Commission's approval of the merger. But according to the AG, SBC fails to explain how it will do this, considering that it has not yet obtained authorization to offer in-region long distance service. Id.

CUB asserts that the merger does not satisfy Section 7-204(b)(6) on numerous grounds. First, CUB claims that the merger would remove a potential competitor (SBC) from the Illinois local exchange market. CUB contends that the Joint Applicants' claim that the merger would not result in diminished competition presumes that: (1) prior to the merger announcement, neither company had plans to offer wireline exchange service in the other's region; and (2) SBC would pursue its Strategy only if the merger were approved.

CUB claims that these presumptions are rebutted by SBC testimony that its national ambitions began long before its proposed acquisition of Ameritech. It also believes that SBC's claim that it would not pursue the NLS absent the merger strains credibility because SBC has resources to pursue such a strategy and could not "remain idle while [its] competitors capture the huge traffic volumes generated by a relatively small number of large customers." Tr. at 294-95.

CUB argues that SBC had every intention of entering the Illinois local exchange market prior to the merger. SBMS had obtained authority to offer local exchange service in Illinois, had invested hundreds of millions of dollars in Illinois for the purpose of providing local exchange service, and SBC's wireless affiliate had a substantial customer base in Illinois. Indeed, according to CUB, SBC was, prior to the merger, one of the most likely competitors for local exchange service in Illinois.

CUB does not agree with SBC's claim that it abandoned its plan to enter the Chicago market based on its experience in Rochester. CUB contends that the Rochester experience was not a serious effort at local exchange competition, particularly when it is compared to SBMS's plan to offer local exchange service in the Chicago MSA. In short, CUB does not believe SBC abandoned its plans to compete in Illinois based on an allegedly bad experience in Rochester.

CUB disagrees with Joint Applicants' arguments that AT&T, Sprint and MCI are local exchange competitors in Illinois. Despite these companies' advertising and marketing efforts in Illinois, the true test, according to CUB, is their market share of local exchange service. These companies control less than two percent of the local exchange market.

CUB argues that SBC's Strategy is belied by its prediction of retaliatory entry. According to CUB, SBC argues that unless the merger is approved, SBC would be too small to pursue it. At the same time, SBC claims that, if the merger were approved and SBC implements the NLS, other RBOCs and CLECs would retaliate against SBC in its own region. These positions, according to CUB, are inconsistent.

CUB also claims that Joint Applicants' plan to offer "one-stop shopping" is dependent upon in-region Section 271 authorization from the FCC, something no BOC has ever received. Moreover, CUB states that, if the merger were approved and if a combined Ameritech/SBC obtained Section 271 authorization, it would be in a position to extend its monopoly control of local exchange service to long distance service. In addition, CUB argues that SBC's retaliatory entry theory fails to account for competition in the residential and small business sectors.

CUB disagrees with Joint Applicants interpretation of Section 7-204(b)(6). Joint Applicants' argue that Section 7-204(b)(6) is concerned only with the merger's impact on existing competitors and SBC is not an existing competitor of Ameritech (assuming divestiture of SBC's wireless service in Illinois). CUB, on the other hand, argues that rules of statutory construction require the Commission to consider the merger's impact on future and potential competitors.

CUB also urges the Commission not to defer to the Guidelines, as Joint Applicant's suggest, for determining adverse impact on competition. If the Illinois legislature had intended for the Commission to do so, it would have so provided in Section 7-204(b)(6). Moreover, CUB argues that such deference is unwarranted because, unlike the Commission, the DOJ has little or no experience dealing with local telephone companies.

Further, CUB claims that SBC has a history of anti-competitive behavior. To evidence this, CUB points to the denial of SBC's Section 271 applications in California and Texas.

Finally, CUB contends that the merger is anti-competitive under the test proposed by SBC. According to CUB, the merger would: (1) eliminate a firm (SBC) that would have entered the market as a new competitor; (2) eliminate a firm that is one of only a few firms that are uniquely situated to enter the market in the near future; and (3) eliminate a firm whose entry would have had a substantial deconcentrating effect on a concentrated market.

Additional Evidence/Argument on Reopening

2. Actual Potential Competition

The issue of actual potential competition was further addressed on reopening. Here follows a discussion of the positions set out by various parties and Staff at this stage of the proceeding on the Actual Potential Competitor issue.

An explanation of whether SBC is or is not an "actual potential competitor" in Illinois, as the term has been used throughout this proceeding. (Question 1, Attachment A, June 4, 1999 letter)

Joint Applicants' Position

According to the Joint Applicants, the record on re-opening establishes that SBC is not an "actual potential competitor" for local exchange services in Illinois. Joint Applicants assert that this conclusion is affirmed by the fact that the U.S. Department of Justice ("DOJ") – which also considered whether absent the merger SBC is an actual potential competitor for Illinois local exchange services – has approved this merger without any conditions relating to the provision of local exchange service in Illinois.

Joint Applicants first contend that there is a well-developed and accepted method of analysis for determining whether SBC is an "actual potential competitor" in Illinois and, if so, whether the elimination of that potential competitor is likely to have an adverse effect on competition in Illinois. That analysis is based on the DOJ's Merger Guidelines, and has been followed by the FCC and other state regulators charged with reviewing telecommunications company, including RBOC, mergers. Joint Applicants contend that even Staff's own expert witness has conceded that the Merger Guidelines provide an appropriate framework for analyzing the effects of this merger.

As Joint Applicants' expert witness Dr. Gilbert explained, assessing whether SBC is an "actual potential competitor" such that the elimination of it as a potential entrant will have an adverse competitive effect on Illinois markets, requires finding that all three of the following elements are met: (1) the merger eliminates a firm that had a high probability of entering the market as a new competitor in the near future, (2) the merger eliminates a firm that is one of only a few firms that are similarly situated to enter the industry in the near future, and (3) the merger eliminates a firm whose entry would have a substantial deconcentrating effect. Joint Applicants assert that the record evidence refutes all three of these elements.

On the first prong, Joint Applicants contend that there is no credible record evidence that SBC would likely enter the market for Illinois local exchange services in the "near future," whether the "near future" is defined as within two years (as the Joint Applicants assert is the proper test) or within three to five years (which Staff asserts is the proper timeframe). No witness to the proceeding has been able to produce a current business or strategic plan of SBC to enter the Illinois local exchange services market, even though Staff and Intervenors have had the opportunity to review

thousands of pages of documents from SBC in discovery. An SBC officer with decision-making responsibilities has corroborated SBC's lack of entry plans, submitting sworn and unrebutted testimony that SBC has no plans to enter the Illinois local exchange market in the near future.

According to Joint Applicants, the evidence offered by Staff and Intervenors to demonstrate that SBC was likely to enter the Illinois local exchange market is of five general types, all of which are unpersuasive. The first type of evidence is SBC's current cellular assets in Illinois, which Staff and Intervenors argue make it likely that SBC would enter the Illinois market. Joint Applicants respond that there is no evidence in the record that these assets, such as wireless switches, could be used profitably or at all, to support local exchange operations. In fact, Mr. Kahan presented uncontroverted evidence to the contrary. In addition, the record is replete with evidence that while at one time SBC contemplated a local exchange entry plan based on its wireless operations, including one for Chicago, SBC experienced sufficient difficulties with its trial in Rochester that it abandoned such plans. Joint Applicants point to the rest of the wireless marketplace as confirmation of the credibility of SBC's decision to abandon such entry. No other major cellular or PCS operator anywhere in the nation is successfully providing local exchange services using a wireless operations base.

The second type of evidence relied upon by Staff and Intervenors is SBC's combination of (cellular) assets in Illinois and experience as a local exchange carrier ("LEC"), which is asserted to give SBC a greater interest and better ability to enter the Illinois market. Joint Applicants respond that this combination is not probative of whether SBC will enter Illinois. Sprint, AT&T, and BellSouth all have significant wireless platforms and ILEC experience, and yet are not using wireless operations as a base for offering local exchange services. Thus, there is no basis for concluding that SBC's similar combination of assets would lead it to act differently.

The third type of evidence relied upon by Staff and Intervenors is statements made by SBC in 1996 and 1997 of its interest in entering the Illinois local exchange market. This evidence is unpersuasive according to Joint Applicants because of its stale nature. The statements relied upon date from prior to termination of the Rochester wireless experiment, and as SBC's officers have testified, SBC's business plans have changed. These outdated statements reflect abandoned and superseded business plans, and are therefore irrelevant.

The fourth type of evidence relied upon is the filing by SBC for a certificate to provide service in Illinois as a CLEC. Joint Applicants argue that holding such a certificate is insufficient to make it a significant potential competitor, otherwise there would be no question that there are more than enough potential competitors in Illinois given the large number of certificated CLECs in the state.

The fifth type of evidence cited by Staff and Intervenors is the objective attractiveness of the Chicago market, plus SBC's supposed subjective interest in Illinois generally based on its merger plans and National Local Strategy ("NLS"). Joint

Applicants respond that the first piece of "evidence" only establishes that there are likely to be many potential entrants, not that SBC, in particular, is likely to enter. As for the second piece of "evidence," Joint Applicants contend that SBC's interest in the merger and intent to pursue the NLS in the event the merger is approved says nothing material about what SBC's strategy would be in the event the merger is denied. In fact, there are a number of alternative business strategies SBC could entertain that do not involve entry into the Illinois local exchange market at all.

On the second prong, Joint Applicants contend that SBC is not one of only a few potential competitors in Illinois. Under the Merger Guidelines' potential competition doctrine, three potential competitors, according to Joint Applicants, remaining after a merger is sufficient to eliminate any concern of anticompetitive effect, and six potential entrants eliminates any plausible basis for attacking the merger. Joint Applicants assert that the record evidence establishes that there are well more than a few potential entrants.

Joint Applicants point out that Sprint's expert, Dr. Woodbury testified that if SBC is considered a potential competitor in the market for local exchange services in Illinois, then Bell Atlantic, BellSouth, US West, GTE, AT&T, MCI/WorldCom, and Sprint – a total of seven firms – should be considered potential competitors as well. Staff witness Graves agreed on cross-examination to the inclusion of six of the seven firms on this list. Joint Applicants argue that not only did no witness refute this testimony, this compilation of the potential competitors in Illinois is supported by the FCC's recent decision in the Bell Atlantic/NYNEX merger (finding AT&T, MCI, and Sprint to be among the most significant market participants) and recent marketplace developments in which AT&T, MCI, and Sprint have expended billions of dollars to become more effective local exchange competitors.

Finally, on the third prong, Joint Applicants contend that there is no credible record evidence that SBC's potential entry into Illinois would be competitively significant. A small market share loss to SBC would be insufficient unless it is also shown that this loss would have a significant and lasting competitive effect. Joint Applicants argue that there is no evidence of such a lasting impact on this record. Ameritech Illinois did not consider SBC to be a competitive threat, according to Mr. Gebhardt, even when SBC sought and obtained CLEC certification. In addition, there is no combination of valuable assets unique to SBC that would make its entry competitively significant. Joint Applicant points out that there is no evidence of SBC having a strong brand name in Illinois, or that the Cellular One brand name would support customer confidence in a LEC. In contrast, AT&T, MCIW, and Sprint have been and continue to pursue large scale entry, have national brand names, and have experience as LEC. Moreover, there is no evidence that SBC, if it did enter, would do anything more or different than other carriers who have entered solely to pursue large business customers, a market that is already competitive in Illinois.

Staff's Position

Staff maintains the position that, according to Section 7-204(b)(6), the Commission has jurisdiction over four markets: (1) local exchange telecommunications service; (2) intraLATA interexchange telecommunications service; (3) interLATA interexchange telecommunications service; and to a lesser extent (4) cellular telecommunications service. (Staff Init. Br. at 6).

Staff continued to disagree with the Joint Applicants' position regarding competition and, in doing so applied the well-developed Actual Potential Competition doctrine to the facts of this proceeding. According to Staff, Justice Marshall explained the rationale which underlies the doctrine as follows:

> When a firm enters the market by acquiring a strong company within the market, it merely assumes the position of that company without necessarily increasing competitive pressures. Had such a firm not entered by acquisition, it might at some point have entered de novo. An entry de novo *would* increase competitive pressures within the market, and an entry by acquisition eliminates the possibility that such an increase will take place in the future. Thus, even if a firm at the fringe of the market exerts no present procompetitive effect, its entry by acquisition may end for all time the promise of more effective competition at some future date.

…

> [W]here a powerful firm is engaging in a related line of commerce at the fringe of the relevant market, where it has a strong incentive to enter the market de novo, and where it has the financial capabilities to do so, we have not hesitated to ascribe to it the role of an actual potential entrant. In such cases, we have held that … entry by acquisition [is prohibited] since such an entry eliminates the possibility of future actual competition which would occur if there were an entry de novo.

Id. (citing United States v. Falstaff Brewing Corp., 410 U.S. 526, 561 (1973)(J. Marshall, concurring)(emphasis in original)).

Staff explained that the federal courts have developed precedent for this doctrine under Section 7 of the Clayton Act which requires an analysis of whether "the effect of [an] acquisition may be substantially to lessen competition or tend to create a monopoly." Staff Initial Brief at 55. The elements which the courts have found necessary to satisfy the doctrine under the Clayton Act are as follows:

1. the market is concentrated;
2. the acquiring firm plans on entering the market through the acquisition of a dominant firm;
3. the acquiring firm would have likely entered the market either through de novo expansion or a toe-hold acquisition in the near future in the absent the merger;

4. either de novo entry or entry through a toe-hold acquisition by the acquiring firm would have been likely to deconcentrate the market or result in other procompetitive effects; and
5. an insufficient number of similarly situated alternative entrants exists.

Id. at 54; Staff Brief on Re-Opening at 4.

Staff did not object, in general to the reasonableness of utilizing the DOJ's merger guidelines to analyze the applicability of the actual potential competition this doctrine to the proposed merger because the elements which the guidelines establish generally follow the test established by the federal courts and are based on established economic principles. Id. at 37. Staff noted, however, that the guidelines are designed to guide merger review under the federal antitrust laws and not under Section 7-204(b)(6) of the Act. According to Staff, the Commission has to deviate from the guidelines to undertake the type of review required by the Act, namely a review which encompasses all likely effects on competition, including any which are likely to inhibit the market's transition to competition. Staff Reply Brief at 5-22. In this case, Staff opined that the Commission needs to deviate from the general guidelines to account for the market's unusually high degree of concentration and the goal to transition the market from regulation to competition. Staff Initial Brief at 15; Staff Reply Brief at 24.

Particular to the Actual Potential Competition Doctrine, ("APC Doctrine") the guidelines require the acquiring firm to be one of only a few firms that are uniquely situated to enter the market in the near future. The guidelines indicate that a proposed merger is not likely to have a significant adverse effect on competition when three other similarly situated firms exist, and is presumed not to have such an effect when six other similarly situated firms exist. Staff Initial Brief at 37. Staff claims however, that the Commission should deviate from this portion of the DOJ's standards noting that the DOJ guidelines are usually applied to markets with significantly less concentration than the concentration level in Illinois' local exchange market. Id. at 37. Staff explained that when markets are significantly less concentrated, the interjection of three to six competitors may be sufficient to transition the markets to competition. Id. at 37-38. The Illinois' local exchange markets however, would need the interjection of significantly more competitors to transition the market to competition. Staff provided the highly optimistic example of all three remaining RBOCs successfully entering the market and winning 15% of the market each, stating that, in that scenario, the market's concentration level would only be reduced to the point where normal merger analysis begins. Id. at 38. Staff opined that this fact combined with the clear legislative intent to transition the market to competition shows that the Commission should deviate form the guidelines to evaluate this element of the doctrine more conservatively, i.e., by requiring a larger number of similarly situated alternative entrants. Id.

Turning to the actual application of the APC doctrine, Staff contends that the first prong is satisfied because the market is concentrated. Id. at 55-61. The same evidence and method of analysis which Staff utilized to find that the proposed merger

raised competitive concerns because of the market's current anticompetitive structure satisfies this element of the Actual Potential Competition doctrine's test. The application of the same evidence and method of analysis is imperative because the same rationale which underlies Staff's first two arguments also underlies this argument. As stated by the United States Supreme Court, this prong of the test is necessary because "there would be no need for concern about the prospects of a long-term deconcentration of a market which is in fact genuinely competitive." Marine Bancorp., 418 U.S. at 631.

Staff cited to several federal courts' determinations of the level of concentration which satisfied this prong of the test. Staff Initial Brief at 56. Staff set out the cases and the markets which those courts found satisfied the test, as follows:

1. Marine Bancorp, 418 U.S. at 631: (three firm ratio of 92%);
2. Falstaff, 410 U.S. at 478, 484: (four firm ratio of 61.3%); (eight firm ratio of 81.2%);
3. United States v. Phillips Petroleum Co., 367 F.Supp. 1226, 1253 (C.D. Cali. 1973), aff'd per curiam, 418 U.S. 906 (1974): (two firm ratio of 39%); (four firm ratio of 58%); (seven firm ratio of 81.2%);
4. Mercantile, 638 F.2d at 1267: (four firm ratios of 86.1% & 73.8%);
5. United States v. Black & Decker Mfg., 430 F.Supp. 729, 748-50 (1976) Fluctuating ratios between: (two firm - 54.6% & 48.4%); (four firm - 69.5% & 82%); (eight firm - 91.6% & 96%).

Staff Initial Brief at 56. In comparison, Staff noted that Ameritech Illinois' sole control of approximately 95% of the local exchange market clearly meets this prong of the test. Id. Further, Staff noted that complete analysis of the market demonstrates that the market's concentration ratio is consistent with the market's competitive structure or, in other words, accurately depicts the lack of competition which exists within the market. Id. at 57-61.

Next, Staff stated that the APC doctrine's second prong is satisfied because the proposed plan of merger seeks to acquire Ameritech Illinois which is the market's dominant firm. Id. at 62.

Applying the third prong, Staff opined that SBC would likely enter the market either through de novo expansion or a toe-hold acquisition in the absence of the proposed merger. Id. at 62-68. Staff noted that three elements must be met to satisfy this prong of the test. First, one must determine that the acquiring firm has available feasible means for entering the market other than through acquisition of the market's dominant firm. Second, a reasonable probability must exist that the acquiring firm would enter the market in the absence of the acquisition. Third, the acquiring firm must be likely to enter the market within a reasonable period of time. Id. at 62, 64-65.

In terms of the first element, Staff stated that no legal barriers prevent SBC from independently entering the market. Further, Staff pointed out that SBC has admitted that it has the financial resources to enter the market independently. Also, Staff opined that the market's barriers to entry are less significant for SBC for three reasons. First, SBC has experience as an ILEC and as an CLEC. Such experience provides SBC with knowledge about how to provide local service that other CLECs do not possess. In particular, SBC has derived the necessary technical, operational, financial and marketing skills to be a local exchange provider from SBC's experience as such. SBC's experience would also provide SBC with a greater ability to overcome ILEC resistance. SBC would be able to utilize its own ILEC experience to identify CLEC need and successfully arrange to have those needs met. According to Staff, SBC's knowledge would result in SBC successfully negotiating with ILECs and eliminating expensive and lengthy arbitration and/or litigation in which disagreements might otherwise result, thereby reducing the amount of a time and money SBC would have to spend to enter the market. Moreover, Staff claims that SBC has experience as a CLEC which would assist SBC with attaining these same benefits. Staff notes that in SBC's Rochester trial, one of SBC's primary objectives was to gain CLEC experience - a goal SBC met. Cross Ex. 37; Staff Initial Brief at 62-64; Staff Brief on Re-Opening at 21.

Second, Staff claims that SBC has an established brand name both as an incumbent local exchange provider and as a cellular service provider. Along with its established brand names, SBC has a reputation for providing quality service. Staff provided evidence that this advantage would provide SBC with the leverage to immediately win a significant share of wireline customers from SBC's cellular customer base. Staff Ex. 4.02 at 4-6 (citing SBC internal Marketing Research and Analysis Department surveys). Also, SBC provides ILEC services on Illinois' border in St. Louis and SBC's St. Louis advertising reaches Illinois consumers, thereby creating another source for Illinois consumers to recognize SBC's brand name in Illinois and reducing the advertising costs SBC would have to spend to enter the Illinois market. Staff Initial Brief at 62-64; Staff Brief on Re-Opening at 21. Further Staff argues that SBC has extremely effective marketing capabilities as evidenced by its vertical service sales and its acquisition of a significant number of customers in a short time period in its Rochester trial. These marketing capabilities would enable SBC to spread its brand name reputation to the remainder of the market population. Cross Ex. 37; Staff Reply Brief on Exceptions at 26-27 (citing SBC-Ameritech Ex. 1.1 at 26; SBC-Ameritech Ex. 1.0, att.2 (SBC 1997 Annual Report to Shareholders) at 12; Staff Ex. 4.0 at 37).

Third, Staff maintains that SBC is a large, diversified corporation which would have superior resources and economies of scale upon which to draw to enable successful entry. In particular, SBC has access to significantly larger amounts of capital than most alternative entrants. Staff asserts that the only remaining RBOC which would have a comparable revenue base when SBC's and Ameritech's revenues are combined would be a combined Bell Atlantic/GTE. Further, SBC already has employee and equipment resources in Illinois which far outweigh those of alternative competitors. Id. at 62-64; Staff Brief on Re-Opening at 23; see also, Staff Ex. 4.02, att. 5 (demonstrating

that SBC has clear advantages over alternative competitors in revenue base, employee base, and equipment deployment in Illinois). According to Staff these factors show that SBC has the ability to enter the market.

In terms of the second element, Staff argues that a sufficient likelihood exists that SBC would enter the market in the absence of the merger. Id. at 64-67. Staff explained that the Commission should consider a number of objective factors to determine the likelihood of SBC's entry once feasibility of entry is established. These factors are (1) the acquiring firm has an interest in market expansion; (2) the acquiring firm has an incentive to enter; and (3) the acquiring firm's incentive to enter is generally greater than the firm's incentive to undertake alternative expansion strategies. See, Staff Brief on Re-Opening at 9 n. 7.

According to Staff, the record shows that SBC is interested in market expansion. SBC's attempt to acquire AI is SBC's third acquisition of a large ILEC in the last few years. Staff noted that SBC has (or has established the right to acquire) significant ownership holdings in at least three other firms which provide related product lines, namely Williams Communications, Concentric Network Corporation and OnePoint Communications. Staff agreed that through SBC's current and to be future holdings in Williams and Concentric, SBC is positioned to expand into a national provider of bundled services. Staff explained that SBC has established an extensive fiber network in-region and will utilize William's fiber network out-of-region to provide such services. Concentric adds to the mix by providing access to Concentric's leading edge, Internet based business data service technology. Staff Brief on Re-Opening at 10-13. Further, Staff pointed out that SBC's holdings in OnePoint position SBC to compete in multiple markets as a CLEC, including Chicago. Id at 13-14. Moreover, Staff directed the Commission to numerous statements by SBC to the public and SBC's shareholders that SBC must and will expand operations. SBC's statements to its shareholders have focused on specific expansion strategies, such as becoming a national provider of bundled services and cellular expansion. See, Staff Reply Brief on Exceptions at 21-22 (citing some examples of SBC statements).

Also, Staff established that SBC has the incentive (along with all other carriers) to enter the market. Generally, the incentive is driven by a desire to reap profits. Staff pointed out that anticipated profitability from independent entry is more substantial than anticipated profitability from other ventures. Staff explains that SBC would not only desire to enter Illinois to reap new profits but that SBC would need to enter Illinois to protect significant segments of SBC's current profits.

At the outset, Staff states that the market is extremely profitable, in that Chicago is one of the top three markets in the nation. Ameritech had a net income of $2.3 billion in 1997. Staff Reply Brief at 49. Later, Staff explains that entry would be necessary to target large corporate customers which are the most profitable customers. Staff states that revenues from large corporate customers constitute approximately 18% of total revenues even though the segment constitutes a small percentage of total customers. Staff notes that the market for local services alone in Ameritech territory produced

approximately $7 billion in revenue in 1998, 18% of which is $1.26 billion. Significantly, SBC's profits from serving such customers bundled services would increase multiple times when the profits from data or long distance services are added. Staff Brief on Re-Opening at 16. Staff notes that SBC's management, as evidenced by its National-Local Strategy and numerous statements to shareholders, believes that serving large corporate customers as a CLEC will be extremely profitable. See e.g., Staff Reply Brief on Exceptions at 21-22, 24 (citing SBC's announcement to shareholders that SBC's goal is to provide one stop shopping to large corporate customers). As large corporate customers want one stop shopping, SBC would have to provide one stop shopping to compete for those customers. One stop shopping requires the provisioning of service in all geographic locations where the customers are located. Most large corporations have offices in Chicago. Thus, according to Staff, SBC would have to enter Chicago to target large corporate customers.

Further, Staff established that SBC also reaps approximately 18% of SBC's current revenues from SBC's in-region large corporate customers. As those customers want one stop shopping, SBC would likely lose those customers to other competitors who provide one stop shopping if SBC chose not to pursue such a strategy. Accordingly, Staff argues that SBC would have to enter Illinois as a defensive strategy to protect a significant segment of its current customer base. Staff Reply Brief on Exceptions at 21-24.

In addition to establishing SBC's likelihood of entry because of SBC's incentive to pursue profits from large corporate customers, Staff claims that SBC has already positioned itself to undertake a national, bundled services strategy in the absence of the merger. SBC has the right to acquire up to 10% of Williams' common stock at the time of Williams' initial public offering as well as a right to acquire a seat on William's board of directors when SBC obtains Section 271 approval. Staff Brief on Re-Opening at 14-16 (citing Tr. 1915-1916, 2052-53). Staff explained that Williams Communications ("Williams") owns a national, interstate fiber-optic network which transmits both voice and data traffic. Staff Ex. 4.02 at 11. Williams also has an agreement with Metromedia Fiber Network, Inc. through which Williams has access to intra-city fiber networks in the nation's top cities, including Chicago. Tr. 2052-2053.

Staff explained that SBC's investment in Williams represents a strategic position for SBC to advance into the Illinois market. In fact, Staff stated that the investment demonstrates that SBC is positioning itself to provide bundled services on a national basis, including the Chicago market. Prior to SBC's investment in Williams, SBC had built out a significant data network in its major in-region markets. Staff Ex. 4.02 at 10 (citing SBC Investor Briefing: The Dynamics of Data, No. 204 at 4-5 (Nov. 10, 1998)).

> Staff explained that as SBC's self-built fiber network does not extent out-of-region, SBC's agreement with Williams provides SBC with access to a fiber network in out-of-region markets, including Chicago, and the means to provide bundled services to customers on a national basis. Staff Brief on Re-Opening at 14-15. In fact, Staff noted that Williams has announced

> that its strategic agreement with SBC will result in Williams and SBC marketing integrated offerings across the nation.

ICC Staff Ex. 4.02 at 11-12 (citing Williams Communications Press Release, Williams Communications Forms Unique Alliance with SBC, (Feb. 8, 1999)).

Staff explained that SBC has further enhanced SBC's position to provide bundled services on a national basis by entering into an agreement with Concentric Network Corporation ("Concentric"), a company that provides Internet-based business data services. SBC holds an ownership interest in the form of 4% of Concentric's stock along with an option to increase that ownership interest by another 4.5%. SBC's stock ownership is part of an agreement to integrate Concentric's leading edge, Internet based, business data service technology into SBC's growing portfolio of data capabilities. Staff Brief on Re-Opening at 16 (citing Staff Ex. 4.02 at 12).

This evidence, according to Staff, established that SBC has undertaken the steps to implement a national, bundled services strategy which would necessarily bring it to Illinois. Also, Staff claims, it is shown that SBC has the incentive to undertake such a strategy either with or without the proposed merger. Therefore, Staff opined that a high probability exists that SBC would enter Illinois in pursuit of a national, bundled services strategy in the absence of acquisition.

Finally, Staff explained that entry into Illinois would be necessary for SBC in order to target cellular customers. Wireless customers are typically high-value customers because they purchase large amounts of various telecommunications services. Staff Reply Brief on Exceptions at 25-26 (citing SBC-Ameritech Ex. 1.0, att. 2 (SBC 1997 Annual Report to Shareholders). According to Staff, SBC has an incentive to increase the revenues which SBC derives from its cellular base by expanding the types of services which SBC provides to its cellular customers, and those services would include wireline service. Also, Staff claims, as SBC has a large number of cellular customers and facilities in Illinois, cellular expansion would bring SBC to Illinois. Staff Initial Brief at 19-20.

Further, Staff maintains that SBC will have to provide its cellular customers with wireline service. The cellular market is becoming saturated and bundling wireline with cellular services is a proven method of competing for cellular customers. According to Staff, SBC has the incentive to undertake a cellular expansion strategy as a defensive strategy to secure SBC's cellular customer base. Staff Brief on Re-Opening at 12-13.

In addition, Staff claims that the evidence showed that SBC had actual plans to pursue cellular expansion which it abandoned for acquisition. Staff provided evidence of SBC's internal documents which established a cellular entry plan. Those documents include financial plans, Marketing Research and Analysis Department surveys, and cellular business plans. Those documents establish that cellular expansion would be profitable and very likely successful for SBC. Further, Staff showed that SBC abandoned those plans only when it chose to pursue acquisition instead of competitive

entry. Staff Ex. 4.02 att. 1 (showing that SBC's last public announcement of cellular expansion occurred four days before SBC entered into merger talks with Ameritech). According to Staff, this evidence establishes a very high probability that SBC would pursue cellular expansion in the absence of acquisition.

Staff introduced evidence to show that SBC has positioned itself to enter Illinois through a currently operating CLEC. SBC owns 19.9%, with a warrant to increase ownership by another 10%, of OnePoint Communications ("OnePoint"), which is a CLEC operating within Chicago. Tr. 2015. OnePoint provides bundled services to customers in multi-dwelling units and, as of the first quarter of 1999, had a total of 20,755 subscribers in five markets, including Chicago. Moreover, OnePoint's subscriber growth rate is incredibly high, at 22% per quarter. Staff Ex. 4.02 at 9 (citing SBC Response to Data Request R CLG-001, SBCAMIL 02667). Staff explained that SBC's investment in OnePoint establishes that SBC is interested in Chicago's residential market and that SBC has a toe-hold basis to enter that market. Staff Brief on Re-Opening at 17. Staff explained that the record establishes no reason for SBC to abandon this position in the absence of acquisition.

Staff noted that the only defense which SBC advanced to SBC's ownership interests in Williams, Concentric and OnePoint was the claim that such ownership interests did not provide SBC with control. Staff rebutted SBC's claim merely by referencing the statements of SBC's own expert witness, Dr. Harris, who testified that ownership interests of approximately 10% are "significant" and create "strong alliance[s]" which are substantially greater alliances than mere "joint venture[s]" or "loose strategy alliance[s]." Tr. 1281-1282. Also, Staff pointed out that the public statements in Williams' press release belie SBC's claims and indicate a strong alliance of the type referenced by Dr. Harris, especially when SBC has the right to acquire a seat on William's board of directors. Further, Staff witness Mr. Graves testified that SBC has treated other companies within which SBC holds similar ownership interests as strong alliances, providing those companies with significant direction in the form of marketing, engineering and management training. Staff Ex. 4.02 at 13. Mr. Graves also stated that ownership of the level evidenced is significant and results in company influence merely through company managers fulfilling their fiduciary duty to the company's shareholders. Tr. 2841.

Particular to the evidence of SBC's cellular expansion plans, SBC claimed that cellular expansion is not feasible. Staff noted that this infeasibility argument is belied by SBC's expansion from cellular to wireline in the Rochester Trial as well as SBC's numerous internal documents which develop a cellular expansion strategy and SBC's public announcements promoting cellular expansion. See, Staff Brief on Re-Opening at 10-13. In fact, Staff pointed out that SBC continues to promote cellular expansion to SBC's cellular customers over Cellular One's web site. Id., at 13 n. 13. Finally, Staff explained that SBC's argument conflicts with the consent decree which SBC and Ameritech entered into with the DOJ, wherein the Joint Applicants agreed to sell Ameritech's wireless properties in the St. Louis areas in order to provide a third party the opportunity to compete against the Joint Applicants in St. Louis by expanding from

those cellular properties into wireline service. Proposed Final Judgment, United States v. SBC Communications, Inc., 1:99CV00715 at 4 (D.D.C. filed Mar. 23, 1999); DOJ Press Release of Mar. 23, 1999, at 2.

In terms of SBC's alternative plans of entry in general, Staff noted that the only defense advanced was the statements of SBC's managers that it simply would not follow those plans to enter Chicago in the absence of the merger. However, Staff opined that while managers' subjective statements are relevant, they are inherently unreliable because market forces will govern a firm's future conduct. According to Staff, subjective, self-serving statements should only be considered when there is compelling evidence that a firm will not follow its economic self-interest in the future and the objective evidence is weak and contradictory. In this case, Staff noted that the objective evidence is strong, consistent and compelling, and that no evidence suggests that SBC will not follow its economic self-interest in the future. According to Staff, the Commission must rely on the record's objective evidence to find that SBC would likely have entered the Illinois market in the absence of the proposed merger. Id. at 66 (citing Falstaff, 410 U.S. at 548 (J. Marshall, concurring)).

In terms of the third element, Staff argues that SBC would enter the market in a reasonable period of time. Staff explained that the necessary time frame for potential entry, i.e., a reasonable period of time, is dependent on the market's structure. Id. at 67-68. More specifically, Staff stated that entry must be likely within the period of time that the market is expected to remain concentrated such that the acquiring firm's pro-competitive entry will be needed. Id. Staff opined that SBC would likely enter the market in the next three to five years. Tr. 1621, 1716. Given the market's extremely slow rate of deconcentration, Staff anticipates that the market is likely to be characterized as significantly concentrated for many years into the future, sufficiently covering the three to five years anticipated for SBC's independent entry. Id.

In terms of the doctrine's fourth prong, Staff found that independent entry by SBC offers a substantial likelihood of ultimately producing deconcentration or other procompetitive effects. Id. at 68-71. Staff noted that at issue in this prong is the degree of effect on the market the new entrant needs to have in order for the effect to be considered significant. In addressing this issue, Staff relied on several federal court cases which have held that the new entrant's inroads into the market do not have to single-handedly deconcentrate the market. Id. at 68 (citing Mercantile, 638 F.2d at 1270). Instead, the courts have held that even modest inroads into the market can be significant. Id. at 69 (citing BOC Intern. Ltd. v. FTC, 557 F.2d 24, 27 (2nd Cir. 1977)). In fact, the courts have held that significant procompetitive effect exists merely from a new entrant "shaking things up" or engendering competitive motion. Id.

In this case, Staff explained, even modest inroads by SBC into the market would be significant when the extremely high level of market concentration is considered. In order to provide the Commission with a guide to the degree of entry which constitutes a significant impact, Staff referred the Commission to the DOJ Merger Guidelines. Staff pointed out that pursuant to the guidelines, an impact is significant if entry would lessen

the market's level of concentration, as measured by the Herfindale-Hirschman Index ("HHI"), by at least 100 points, or even by as little as 50 points in the absence of other mitigating factors. Staff provided calculations which evidence that SBC's minimum likely rates of penetration would far exceed the penetration levels which would be necessary to achieve a 50, or even a 100, point reduction in the market's HHI. Staff Reply Brief on Exceptions at 119-127 (citing DOJ Merger Guidelines at Sec. 3.11, 4.133).

In regards to cellular expansion, Staff explained that SBC's cellular expansion trial in Rochester serves as a basis to determine the minimum amount of penetration that SBC would be likely to gain within Illinois following a similar, cellular expansion strategy. Staff revealed through calculations that a similar rate of penetration in the Illinois market would decrease the HHI by well over 100 points within a single year. Indeed, Staff explained that the DOJ Merger Guidelines would still hold entry significant even if SBC merely won merely a fraction of the minimum amount expected based on SBC's Rochester trial because such entry would decrease in the market's HHI by over 50 points.

Staff pointed out that SBC would be likely to gain an even greater rate of penetration in the Illinois market than SBC obtained during the Rochester trial for three reasons: First, Illinois' wholesale discounts are significantly greater than those in Rochester. Second, Ameritech's expected penetration rates through cellular expansion into St. Louis were significantly greater than SBC's Rochester penetration rates. Third, SBC's internal customer surveys reveal that a significant portion of SBC's cellular customers would definitely switch to SBC's bundled cellular/wireline service. Staff Ex. 4.02 at 4-5.

Further, SBC has 10 switches in the Chicago area which it currently utilizes to provide cellular service. The number of competitive switches in the Chicago area would increase by 27% if SBC utilized those switches to provide landline service. Staff opined that such an increase would constitute a significant increase in facilities based competition. Staff Initial Brief at 70 (citing Staff Ex. 4.0 at 14, 18, 36).

In terms of SBC's likely entry through a bundled services strategy, Staff explained that SBC's National-Local Strategy plan serves as a basis to determine the minimum amount of entry that SBC would be likely to gain within Illinois following a similar strategy. SBC's business plans provide SBC's anticipated penetration rates over a ten year period in three different market segments, being the large corporate, medium and small business, and residential customer segments. See, SBCAMIL 009114-009115. Staff stated that the significance of these numbers is unquestionable as they far exceed the 50 to 100 point reduction in the HHI required by the DOJ guidelines.

As another example, Staff noted that CLECs provide service through the use of unbundled loops to less than one percent of AI's customers. Staff provided evidence that if SBC could win merely 1% of its cellular customers, or if it could utilize its switches

in the Chicago area, the number of customers served by CLECs and the number of CLEC switches would significantly increase. Staff Initial Brief at 70.

Further, Staff opined that SBC could have a significant impact on competition by reselling vertical services, an area in which SBC has successfully utilized its marketing abilities in its incumbent states and California. Id. at 23. Staff explained the degree of penetration anticipated from any of SBC's possible entry strategies would likely be larger because of SBC's finely tuned marketing capabilities. In California, Pacific Bell had a mere 1.5% penetration rate prior to SBC's recent acquisition of Pacific Telesis Group. Following SBC's acquisition, however, SBC increased Pacific Bell's penetration rate for vertical services by approximately 5% in one year and anticipates increasing the same penetration rate by another 30% by the year 2000. Further, SBC has a 47% penetration rate in Caller I.D. and a 49% penetration rate in Call Waiting in SBC's original five incumbent states. In Illinois, AIs' custom calling features have wholesale discounts of approximately 50% and provide a large profit potential for resellers of those services. According to Staff, SBC's likely entry penetration rates would increase if SBC pursued the obvious and combined its clearly strong marketing capabilities for vertical services with underlying local exchange service to win even more customers. Staff Reply Brief on Exceptions at 26-27 (citing SBC-Ameritech Ex. 1.1 at 26; SBC-Ameritech Ex. 1.0, att. 2 (SBC 1997 Annual Report to Shareholders) at 12; Staff Ex. 4.0 at 37).

Of the thirteen facilities-based CLECs in Illinois, Staff pointed out that only three provide service outside of Chicago. If SBC were to enter Illinois outside of Chicago, its entry would increase the number of providers in down-state Illinois by 25%. In fact, Staff stated that in some down-state markets, SBC would be the first competitor to enter the market. ICC Staff Ex. 4.02 at 13-14. Also, SBC could use its local exchange switches in Missouri to compete in Ameritech's St. Louis Metro East area, Cairo, Quincy and Peoria. ICC Staff Ex. 4.02 at 8-9.

At the least, Staff argues, SBC's entry would have other procompetitive effects. In particular, SBC's entry would shake things up and engender competitive motion. Staff Ex. 9.01 at 27-28. According to Staff, its examples are conservative in showing that SBC's entry would clearly be very significant. Staff Initial Brief at 22-24, 68-70.

As to the doctrine's last element, Staff argues that an insufficient number of similarly situated competitors exist to eliminate the need to require SBC to enter independently. Id. at 71. Staff explained that the Commission needs to consider two separate questions to address this issue. First, how many entrants are needed to transition the market from concentration to competition. Second, do the identified alternative entrants have comparable incentives and abilities to enter the market as does the acquiring firm. Staff Brief on Re-Opening at 21.

On the first of these questions, Staff opined that the Commission should retain all possible entrants, including SBC, as means of transitioning the Illinois market to competition. Staff rationalized that new entrants in highly concentrated markets are not

likely to have the ability to overcome the dominant firm's market power in order to obtain large market shares. Accordingly, Staff explained that it is only through a combination of a number of entrants that the combined entrants' market share will expand to decrease the incumbent firm's market power. Staff also stated that the higher the degree of market concentration, the greater the number of new entrants that are needed to transition the market. In fact, Staff opined that in highly concentrated markets, all possible entrants to the market must be preserved. Staff noted that the FCC and respected antitrust treatises have reached the same conclusion. Staff Brief on Re-Opening at 21-22 (citing FCC BA/NYNEX Order at para. 65-66, n. 155; 3 Antitrust Law, para. 170d at 134-146). As the Illinois market is very highly concentrated, Staff maintains that the Commission must preserve all possible entrants into the market, including SBC. Id.

In terms of the second question, Staff noted that the question becomes largely irrelevant when the market's conditions necessitate the preservation of all possible market entrants. Nonetheless, Staff did provide the Commission with an analysis of the alternative entrants identified by the Joint Applicants in this proceeding and concluded that only one of the identified alternative entrants, i.e., a combined Bell Atlantic/GTE has comparable incentives and abilities to enter the Illinois market. Staff Brief on Re-Opening at 19-26.

Staff opined that the large inter-exchange firms such as AT&T, MCIW and Sprint have already entered the market but have not shown an ability to deconcentrate the market to a sufficient degree. The market remains a de facto monopoly despite these competitors efforts over the last number of years to expand their shares of the market. Id. at 39, 71. Accordingly, Staff explained that it would be erroneous to rely on those firms to deconcentrate the market to a sufficient degree. Id. at 39. But, more importantly, Staff stated that it is inappropriate to consider those firms as actual potential competitors because those firms are currently competing in the market. Staff Ex. 9.0 at 11.

Staff also responded to the Joint Applicants' argument that AT&T will develop into a significant competitor by providing service over cable. Staff opined that it would be inappropriate for the Commission to rely on AT&T to deconcentrate the market because a cable offering is not a current market product and several problems could arise which could prevent cable from evolving into a truly competitive service. First, even though cable has been tested on a small scale, no cable company has ever rolled out service on a large scale to serve hundreds of thousands or millions of customers. Accordingly, Staff opined that AT&T could run into technical difficulties when attempting to develop a mass market product. Further, even if such technical difficulties were overcome, AT&T will have to upgrade the entire cable network to provide such service and those upgrades will be completed too many years into the future. Second, the type of service offering which AT&T will develop is unknown and may be unsuitable for many customers because of price or the type of service offered. In total, Staff witness Dr. Hunt opined that a 25%-30% probability existed that AT&T would develop a product

which would compete with wireline local exchange service on large scale. Staff Ex. 9.01 at 16-17.

Staff explained that AT&T's offering would be insufficient to bring competition to the market even if AT&T does develop a competitive product. Staff opined that a single competitor is insufficient to develop competition within the market. AT&T would have to win close to 25% of the market's customers to transition the market out of de facto monopoly status. However, even then the market would not be competitive because the market would still be classified as a highly concentrated oligopoly. Dr. Hunt explained that generally the same anticompetitive problems are encountered in highly concentrated oligopolies as in de facto monopolies. Even accepting AT&T as a first tier competitor, Staff maintained its position that a significantly larger number of alternative entrants is needed to transition the market to competition. Staff Brief on Re-Opening at 27-28.

According to Staff, the IXCs' financial information does not indicate that they are able to successfully expand their market share. Staff Initial Brief at 39-40. Staff stated that even though AT&T has a market capitalization of $139 billion which is the closest in comparison to SBC/Ameritech's of $159 billion, market capitalization is based on stock value and fluctuates depending on the vagaries of stock market valuations. Id. at 39. Also, Staff pointed out that AT&T's revenues are earned across the fifty states and the international markets whereas SBC/Ameritech's revenues are concentrated geographically. Accordingly, Staff concluded that AT&T would have difficulty bringing the same financial force to SBC/Ameritech's concentrated markets. Id. at 40.

In terms of MCI, Staff stated that MCIW's market capitalization is around $100 billion, its revenues are $10.7 billion and its profits are a negative $2.8 billion. Id. Staff explained that MCIW's financial numbers are small in comparison to SBC/Ameritech's capitalization of $159 billion, revenues of $43.3 billion and profits of $7.1 billions; and to AT&T's capitalization of $139 billion, revenues of $58.6 billion and profits of $4.6 billion. Accordingly, Staff concluded that MCIW has a financial weakness that prevents it from being considered a similar competitor to SBC. Id.

In regard to the RBOCs, Staff opined that a combined Bell Atlantic/GTE will be the only first tier competitor to a combined SBC/Ameritech. Id. at 38. A combined Bell Atlantic/GTE will be the only firm with sufficient size and presence to gain significant entry into SBC/Ameritech territory. Id. Further, Staff explained that Bell South and US West are likely to be forced into mergers with SBC/Ameritech and Bell Atlantic. Id. Even though a combined Bell Atlantic/GTE may have the ability to compete against SBC/Ameritech, in Staff's view the most likely outcome will be forbearance by the two companies from competing in any large scale competition in each other's markets. Id. at 17.

Staff reiterated that SBC has a greater ability to overcome the market's known barriers to entry than other firms. Accordingly, in the absence of the merger, SBC would be more likely to effectively enter the market than many of the other possible

entrants identified by the Joint Applicants. Thus, Staff concluded that an insufficient number of similarly situated carriers exist such that the Commission can forego the procompetitive effects which SBC's independent entry into Illinois would bring.

Staff concludes that the merger is not likely to have a significant adverse effect on competition for interMSA toll markets in Illinois. Id. at 77-82.

Staff believes that the merger may have an adverse effect on competition for intraMSA toll service because despite the large number of buyers and sellers of intraMSA in Illinois, AI continues to exert some market power over that market; and SBC's elimination as a potential competitor in the local exchange market will have an adverse impact on that market which may spill over into the intraMSA toll market and make it more difficult for new companies to enter that market after the merger. Id. at 82-90.

Finally, Staff takes the position that the proposed merger may have an adverse impact on competition in the cellular markets in Illinois for two reasons. First, now that SBC and Ameritech have proposed to merge and are in the process of divesting one of their cellular properties, they have the economic incentive to cease acting as competitors during this transition period. Second, the long term contracts prevalent in the cellular market create a significant amount of uncertainty regarding the impact of the proposed merger on competition in that market. Id. at 90-92. Recognizing the limits on the Commission's jurisdiction over cellular markets, Staff makes no recommendations to address the first issue. Staff, however, makes recommendations to address its second concern. Specifically, Staff urges the Commission to condition approval of the merger on the following notice requirements.

1. Ameritech should send a notice to their respective cellular customers at least 30 days prior to the divested affiliate.

2. The notice should inform cellular customers of the merger between the SBC and Ameritech, as well as the pending sale of Ameritech Cellular to GTE.

3. Ameritech should provide a copy of its notice to Staff for review and comment at least 15 days prior to the date on which the notice will need to be finalized for mailing to Ameritech's cellular customers. Ameritech should provide their customers with the notice incorporating Staff's comments.

Intervenors' Position

Sprint, the only Intervenor to submit testimony on re-opening on the potential competition question posed by Chairman Mathias, continues to oppose the merger on the ground that the merger would eliminate SBC as an important potential competitor of local exchange services in Illinois. Sprint argues that (1) SBC would likely enter the

Illinois local exchange market to serve consumers, (2) there are not so many other potential entrants that the loss of SBC as a potential entrant would have no effect on the development of competition, and (3) SBC's entry likely would have a significant deconcentrating and procompetitive effect on the supply of local exchange service in Illinois.

In support of its first point, Sprint argues that even absent specific entry plans, SBC should still be considered likely to enter given SBC's ability to enter, based on its experience as an ILEC, its back office billing and support systems, its geographic proximity to Illinois, and its brand name. Sprint also argues that SBC's reasons for pursuing the merger are evidence that SBC might enter the Illinois market absent the merger, either through geographic expansion and entry or acquisition of a smaller out-of-region CLEC. Sprint argues that SBC's past indications of an interest in expanding into Illinois, combined with its current overall business strategy, are evidence of SBC's interest in providing local service in Illinois. Sprint notes that SBC owns almost a 20% equity interest in One Point and there are no technical or network limitations that would prevent SBC from using its One Point investment to provide local exchange services in Chicago. (Tr. R25)

Sprint argues that the absence of current plans does not resolve the issue. Its expert Dr. Woodbury argues that SBC could enter, and if the merger is rejected, SBC could undertake the necessary planning in a relatively short timeframe, such that SBC's entry would not be so far out as to be irrelevant to the Commission's evaluation of the merger. According to Dr. Woodbury, given the rapidly changing marketplace, the continuing development and modification of strategies by ILECs, and the changing regulatory barriers to entry, the absence of current plans is not determinative of future behavior. SBC itself changed its overall strategy and out-of-region entry plans in the short period of time since the Pacific Telesis merger closed. He argues that given SBC's pursuit of an expansion-by-merger strategy, SBC had little reason to develop plans for independent out-of-region entry and, in fact, might consciously avoid making such plans in anticipation of regulatory review, thus the absence of such plans now is not determinative of whether SBC would enter the Illinois local exchange market independently absent the merger.

On the second point, Sprint disagrees with Joint Applicants that there are a sufficient number of other potential entrants. Sprint argues that because of the particular market circumstances in Illinois, it is not enough to have three or even six potential competitors remaining after the merger. Dr. Woodbury argues that where, as here, you are dealing with a virtual monopoly, there must be a sufficient number of significant potential entrants to create some actual competition in the market. The loss of one significant market competitor in a virtual monopoly can adversely affect the development of competition and the attendant proposals for deregulation. In support, Dr. Woodbury points to the statements by the FCC that it will not mechanistically apply the Merger Guidelines rule of three remaining potential entrants is enough in analyzing telecommunications markets. Dr. Woodbury further argues that the authority Joint Applicants cite for the "six is enough" rule, an antitrust treatise, has been revised and

applies a stricter standard where one of the merging firms is a monopolist and the other is a potential entrant into the same market.

Finally, on the third point, Sprint continues to argue that SBC's entry would have a significantly deconcentrating effect. Sprint argues that given AIs' dominant market position, any entry will help to deconcentrate the market and result in more competitive conditions. It argues that, in particular, SBC possesses the characteristics to be a significant competitor in the provision of local exchange service in Illinois, and as a result is likely to account for a significant proportion of the local exchange business captured from AI.

21st Century claims that SBC is a potential competitor in the sense that it is so positioned on the edge of the market that it exerts beneficial influence on competitive conditions in the market. Moreover, 21st Century sees SBC, with its knowledge of local operations, as the type of competitor that would effectively challenge Ameritech and make it easier for the CLECs.

Recognizing that it is difficult to prove a negative, i.e., that SBC is not an actual potential competitor, the GCI contend that direct evidence is not the only means by which to evaluate the question. There are a number of factors relevant to such an inquiry, GCI argue, which can be examined and which show that SBC would have a tremendous advantage in providing facilities-based local telephone service. These factors, as set out by GCI, are SBC's experience gained from providing cellular service in Illinois and the wireline service near St. Louis, its size and financial strength. According to GCI, the Joint Applicants have not addressed these factors. The GCI also point to SBC's desire to become a national and international provider of telecommunications service. With such ambitions, the GCI claim, SBC could not avoid competing for local exchange service in Illinois due to the extensive network of national and multinational corporations located in the Chicago MSA. The attractiveness of the Chicago MSA is, according to GCI, borne out by the number of CLECs who have attempted to offer local exchange services here.

The GCI (AG, Cook County and CUB) argue that SBC is an "actual potential competitor" if it is able to enter the local exchange markets in Illinois absent the merger with sufficient ease. These parties add that entry is easy, pursuant to the DOJ guidelines, if it is "timely, likely and sufficient in its magnitude character and scope."

Joint Applicants' Response

On the key question of whether SBC is an actual potential competitor, the Joint Applicants reiterate that there is no credible evidence in the record – on re-opening or prior to re-opening – that SBC would likely enter the Illinois local exchange market in the absence of the proposed merger. Mr. Kahan, the officer at SBC with the responsibility for planning entry by SBC into various markets, testified again that SBC has no plans or intent to enter the Illinois local exchange market absent the merger. The merger opponents, SBC argues, erroneously continue to cite to old Cellular One

business plans, marketing strategies, and the like. As Mr. Kahan testified, SBC has rejected the use of a cellular entity to provide local exchange service on a wide-scale basis as a business model, and this decision is consistent with and corroborated by, the lack of such plans by other major wireless carriers in the nation.

Joint Applicants note that none of the other "new" evidence cited by the Staff (which related only to the first prong of the three prong actual potential competition test) demonstrates that SBC would likely enter the Illinois market absent the merger. Merger opponents incorrectly cite the merger and the planned NLS as evidence of an intent to enter. As Mr. Kahan reiterated, however, SBC has no plans to implement the NLS absent the merger, and will not implement the NLS without the merger. Further, if the merger is rejected, there are a number of strategies SBC can pursue that are consistent with the motivations for the merger but that do not involve entry by SBC into the Illinois local exchange market.

Joint Applicants contend that merger opponents err in their reliance on SBC's investments in OnePoint, Williams Communications, and Concentric Communications as evidence that SBC has entered or will enter the Illinois local exchange market. As to OnePoint, SBC has only a minority investment (which is in the process of being reduced), has no seats on the board of directors, and has no control over prices, strategies, or business plans. OnePoint is the only one of the three companies currently in the local exchange business at all, and given the fact that the company is focused very narrowly on the niche strategy of providing bundled services to MDUs on a resale basis, it is not a significant vehicle for competition with an incumbent LEC. As to the other two companies, neither of which are even in the local exchange business, SBC has only a minority investment, has no seats on the board of directors, and has no control over prices, strategies, or business plans of either company. With respect to the One Point investment, Mr. Kahan testified that SBC viewed this as a financial investment, not as a vehicle for SBC to become a potential competitor of Ameritech Illinois. In fact, SBC has never used such minority investments to perform such important business functions as providing local exchange service.

Merger opponents also err in arguing that SBC's switches in St. Louis constitute facilities in Illinois that make it likely SBC would enter that market. A company needs more than switches to provide successful telecommunications services, as Mr. Kahan points out. Switches need to be augmented with facilities (or resale or UNEs) none of which SBC has in Illinois. Merger opponents also ignore the fact that while adjacent, eastern Missouri and western Illinois are diverse markets, success in one does not necessarily mean success in the other. Finally, Mr. Kahan points out that many advanced services such as xDSL do not necessarily work beyond a certain number of kilofeet from a central office, so it may not even be technically feasible for SBC's existing switches to provide key services in Illinois.

On the second prong, merger opponents' argument that certain firms should not be considered as potential competitors because they are also actual competitors, is wrong. Under the Merger Guidelines, a static look at the current market share of a

particular firm can either understate or overstate a firm's future competitive significance. The ongoing efforts of firms like AT&T and MCIW, which may be nascent competitors in the Illinois local exchange market, is important to the analysis, as their ability to expand and bring on additional capacity in the very near future makes them not only actual potential entrants, but significant actual potential entrants.

Staff's arguments that, even aside from the potential competition question, the merger should be rejected because it makes a strong Ameritech Illinois stronger and raises barriers to entry are wrong. The merger is likely to enable Ameritech Illinois to offer services that customers desire, and such merit-based competition is procompetitive. Staff has provided no evidence that Ameritech Illinois' ability to retain customers will result from anything other than enhanced competition on the merits. As to Staff's argument that the merger will have several effects that will increase barriers to entry, Staff witness Dr. Hunt, who recites these supposed effects, provides no evidence of how or why the listed effects would follow from the merger.

Joint Applicants assert that Staff's attempts to undermine the significance of the DOJ's decision to approve the merger should fail. The DOJ shares the goal of the ICC of protecting competition. In furtherance of that goal, the DOJ analyzed the competitive impacts of the merger on local exchange market, including the local exchange markets in Ameritech's territory. Dr. Gilbert, the only witness with firsthand experience of the DOJ's processes, believes that the DOJ would have carefully examined all theories of potential anticompetitive effects in any relevant product market – including local exchange services – and in any relevant geographic market – including Illinois – and would have challenged the merger if it had identified a significant anticompetitive effect in an Ameritech local exchange service area. This view is confirmed by the fact that it is not unusual for the DOJ to require parties to a proposed merger to divest certain assets to deal with competitive concerns in local markets, and the fact that in this case the DOJ filed a Complaint which identified an anticompetitive effect in the Illinois and Missouri wireless services markets. The inference that DOJ concluded that SBC is not a potential competitor in Illinois is confirmed by the fact that the DOJ's divestiture order required Ameritech's St. Louis, but not SBC's or Ameritech's Chicago/Central Illinois, wireless assets to be sold to a purchaser capable of providing local exchange and long distance service in its service area. If SBC were viewed as a significant potential competitor in Illinois, the DOJ would have imposed a similar restriction on the Illinois wireless assets to offset the loss of SBC as a potential entrant.

3. Commission Analysis and Conclusion

Section 7-204(b)(6) requires the Commission to determine whether the proposed merger is "not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction." (See 220 ILCS 5/7 204(b)(6)). The scope of the Commission's inquiry centers around the wording of this provision. By its very terms, we see that this provision requires us to make two independent but related determinations: 1) what are the markets over which the Commission has jurisdiction;

and 2) is the proposed merger not likely to have a significant adverse effect on competition within those markets.

The language of §7-204(b)(6) links the meaning of "significant adverse effects on competition" closely to the markets "over which the Commission has jurisdiction." While taking the plain meaning of this phase into account, we note that it may differ when applied to different regulated industries or different proposed mergers. Accordingly, we must establish and apply a reasoned definition for purposes of evaluating the proposed merger at hand between SBC and Ameritech.

The term "significant adverse effect on competition," within the meaning of the statute, is defined, for the purposes of this inquiry, as more than the retention or accumulation of a significant market share by an incumbent utility within a concentrated market. In critical part, the record must also reflect evidence of current or future increases in barriers to entry into the relevant market or evidence that the incumbent utility is likely to implement policies or procedures which would frustrate the efforts of this Commission in effectively implementing its policies or Illinois law. (See generally, State of Illinois ex. rel. Burris v. Panhandle Eastern, 935 F2d (7th Cir. 1991) Within this definition a "significant adverse effect on competition" may also be interpreted to include the elimination of a potential competitor such that competition within the industry is negatively impacted in a material manner contrary to the Act. The policy of the State of Illinois, as embodied in Public Utilities Act, is to aid in the orderly transition of the development of markets for telecommunications services from a regulated to a competitive market. On these premises and the particular circumstances of record, the Commission looks to see whether the record shows that the proposed merger is likely to result in a significant adverse effect on competition.

The Relevant Market

First, we will address the relevant market question. The parties generally agree and the Commission concurs, that its jurisdiction includes at least three markets; A) interLATA interexchange, B) intraLATA interexchange, and C) local exchange telecommunications service. Some disagreement exists in the record with respect to the Commission's jurisdiction over a fourth market, i.e., the wireless market. Staff urges the Commission to consider the effects of the proposed reorganization on each of these four markets. (See Toppozada-Yow Direct Testimony, Staff Ex. 3.0 at 3-4). The Commission agrees with Staff to the extent that it affects intrastate commerce. In addition to these broad markets, parties distinguished between providing service to large business customers and providing service to small business and residential customers. (JA In. Br. on Reopening at 11). Thus, it is reasonable to characterize the large business, small business and residential markets as subsets or products of each of the broader markets described above.

The Commission agrees with Staff that wireless service is not a clear substitute for wireline service. However the record also indicates that aspects of the wireless market may have an impact on the wireline markets and vice versa. (See ICC Staff Ex.

9.0 at 36). Responding to Staff's concern that the long term nature of cellular contracts may create significant uncertainty within the cellular market as these contracts relate to the merger, the Commission is satisfied with Staff's proposal to provide notice to AI's cellular customers prior to divestiture of the cellular affiliate.

The Commission also agrees with Staff and Joint Applicants that the merger, as proposed, will not adversely effect competition within the already highly competitive interLATA interexchange market. (JA In. Br. at 29) Staff however, suggests that the proposed merger may adversely effect competition in the intraMSA toll service market. Despite the large number of buyers and sellers of intraMSA toll service in Illinois, Staff suggests that Ameritech Illinois continues to exert some market power over that market and SBC's elimination as a potential competitor in the local exchange market will have an adverse impact on that market. This potential adverse impact may spill over into the intraMSA toll market and make it more difficult for new companies to enter that market after the merger. (See Staff In. Br. at 82-90). After reviewing the record, the Commission does not find these arguments persuasive. We agree with the Joint Applicants and other parties that the proposed merger would not adversely impact the number of buyers and sellers of intraLATA toll services; the standardization of those services; the ability to enter the intraLATA toll market; or the amount of information available to buyers and sellers. (See Joint Applicants Reply Br. at 40)

Having established the broad markets within the Commission's jurisdiction, the Commission next identifies the specific relevant markets which may be affected by the merger. Generally, relevant markets are determined by the alternative sources of products and services available to consumers, or the "area of effective competition. . . in which the seller operates and to which the purchaser can practicably turn for supplies." (JA Initial Br. at 30). The Commission identifies for the markets impacted by the proposed merger by looking for alternative sources of products and services which are available to customers. In doing so, the Commission identifies the Illinois local exchange market as the relevant market for present purposes.

Having identified the relevant markets, we now consider whether the record supports a conclusion that the proposed reorganization is "not likely" to result in "significant adverse effects on competition" within these identified markets.

Present v. Future Competition

Before we begin consideration of any merger-related effects on competition, the Commission must determine if our analysis relates to present or future competition, and to the extent we regard the latter as proper, we must establish a timeframe for the analysis. We believe that looking at present competition is not enough for purposes of this inquiry. On record, Staff suggests that the Commission adopt a three to five year timeframe. The Joint Applicants claim however, that within the context of the rapidly changing telecommunications industry, the Commission should adopt a timeline of no more than two years and preferably restrict its inquiry to events occurring within the next year. (Joint Applicants' Response to Commission's June 4 List of Issues and Joint

Applicants' additional Commitments at 3 Fn 6.) The Commission agrees with the Joint Applicants position to some degree and gives as its reason the fast and continuing evolution of telecommunications industry. The record well shows that the industry is anything but stagnant. Further, the Commission notes, as an example, that in evaluating the three to five year standard retrospectively, it could not have, with any level of precision forecast the state of the market as it stands today if we had attempted to do so in either 1994 or 1996. Therefore, the Commission will conduct its analysis using a two year timeframe to avoid engaging in any undue speculation. The Commission now must identify a method by which to consider the effects of the proposed merger on competition under the language of §7-204(b)(6).

Framework For The Analysis

Some parties urge the Commission to adopt a method for analyzing this merger on the basis of the U.S. Department of Justice's *Merger Guidelines*. ("Guidelines") The language of the Clayton Act prohibits mergers if "the effect of such acquisition may be substantially to lessen competition or tend to create a monopoly." The FCC and other state regulators, applying statutes similar (although not identical) to Section 7-204(b)(6), consistently rely on the *Merger Guidelines* in reviewing telecommunications mergers, including mergers of RBOCs. (See, e.g., Bell Atlantic/NYNEX Order at ¶37; California SBC/PacTel Order at 41-42.) The *Guidelines*, set out the Department of Justice's standards for evaluating a proposed merger under agency policies and federal law. (See Gilbert, Graves Rebuttal; Staff Ex. 4.01 at 6). While the Commission recognizes the merits of both the Guidelines and similar analytical frameworks, the Commission resists the invitation to apply any of these doctrines in a strict fashion. Instead, the Commission will maintain flexibility in interpreting and in applying elements of the Guidelines and similar analytical frameworks. As urged by Staff, the Commission will also consider whether the merger is likely to inhibit the market's transition to competition, or increase the market's barriers to entry.

Under the Guidelines, mergers are considered anti-competitive when the evidence indicates that the merger may encourage collusion, increase or enhance market power and thereby tent to create a monopoly; or allow prices to be maintained above competitive levels. (U.S. Dep't of Justice, Merger Guidelines §1 (1984)). The Guidelines focus on evaluating mergers through an analysis of: (1) market power, (2) market concentration, and (3) market structure, as well as the ability of the merged firm to operate in an anticompetitive manner as a result of the merger. The Commission notes that the Guidelines primary focus is on identifying those mergers which may tend to create a monopoly. As pointed out by Staff and others, Ameritech Illinois may already constitute a virtual or de facto monopoly under traditional Guideline definitions. Accordingly, the Commission will examine the principles espoused in the Guidelines within the context of the Illinois telecommunications market.

Market Power, Structure and Concentration

The level of current market concentration is crucial under the Guidelines because it serves as a benchmark to measure increases in market power and concentration may indicate the development of a monopoly or other anti-competitive market structure. We will evaluate the concentration of market share within the local exchange market by identifying the market participants. (1992 Horizontal Merger Guidelines 57 Fed. Reg. at 41556 §1.3; See also, BA/NYNEX at par. 58). The record shows that, aside from Ameritech Illinois, more than twenty local exchange carriers provide some form of local exchange service in the Ameritech Illinois' service territory. This number includes CLECs as well as interexchange carriers competing as CLECs. At least thirteen of these competitors are facilities-based, such as AT&T, MCI WorldCom, Sprint, and Frontier, while most of the remaining carriers can be classified as resellers of telecommunications services. Despite the presence of these competitors in the market, predominately in the large business segment of the market, the record demonstrates that Ameritech Illinois retains a significant market share. This high degree of concentration is particularly evident in the residential segment of the local exchange market. We note, however, that even though the evidence demonstrates that the local exchange market is highly concentrated, the proposed merger alone will not have the effect of increasing the market concentration because SBC and Ameritech do not currently compete in the relevant market.

Market Structure and Conduct - Barriers to Entry

The Guidelines do not end after an examination of market concentration, but also guide the Commission in its examination of the effects of the merger on market structure and conduct. We recognize that the local exchange market is in the embryonic stages of transitioning from a highly regulated market driven by regulatory mandates to a competitive market driven by market forces. (Staff Br. at 10,56). The Commission needs to focus its inquiry, thus on the possible increases in barriers to entry resulting from the proposed merger and within the context of Staff's concerns. Based upon the record, the Commission defines "barriers to entry" as anything that allows an incumbent firm to enjoy supranormal profits without the threat of entry. For example, barriers to entry can take the form of a cost of producing that must be borne by those firms entering the market but is not borne by incumbent firms. (See, *generally*, Staff Ex. 4.00 and Staff Ex. 9.0)

The evidence presented on this issue, leads us to recognize that barriers to entry already exist in the current market. The Commission notes though that these bariers to entry are not necessarily the result of anticompetitive activity. Some of these barriers are advertising costs, facilities investment such as switches, OSS systems, central office equipment, non-recurring charges to obtain interconnection, uncertainty about prices of inputs and costs of ordering systems, as well as the failure of AI to provide common transport and comply with TA96. It was argued that the merger may actually result in an increase in these barriers to entry. (See *generally*, Staff Int. Br. beginning at 55). For example, Staff argues that the lack of CLEC penetration into Ameritech Illinois' service territories since deregulatory efforts began in Illinois itself indicates the presence of high barriers to entry and expansion. Specifically, Staff presented

evidence tending to show that CLECs incur a variety of sunk costs including advertising, equipment, facilities and interconnection, unbundled network elements and collocation costs. Further, Staff characterizes Ameritech's recent reclassification of previously non-competitive services as competitive, to be representative of Ameritech Illinois' willingness to use its market power to fortify existing barriers to entry. While the Commission considers Staff's evidence indicating that barriers to entry may exist in the current local exchange market, we question how this evidence of existing barriers to entry serves to demonstrate a significant adverse effect on competition owing to the merger. Our assessment of the evidence shows that the market structure would remain intact and retain the same characteristics demonstrated before the merger. Likewise, the Commission is not convinced by any of the evidence that the merger would increase barriers to entry within the next two years.

It is argued that information concerning the prices of UNEs, the eventual OSS platform, and resale prices will create uncertainty and increase rivals sunk costs by increasing the cost of capital. It is further asserted that alternative carriers will not have the same level of information related to these market inputs as prior to the merger caused by underlying changes in AI cost structures related to the merger. So too, it is contended that uncertainty within a market leads to increased risk for firms entering a market and this represents a barrier to entry. The Commission notes that changes of conduct by firms operating within the market may represent an effect on the relevant market which warrants further observation. At the moment, however, due to the speculative nature of the argument, the Commission does not find that this possible effect rises to the precise level of harm required by the statute.

It is claimed that the arrival of SBC may cause changes in tariff terms and conditions as well as operating procedure making it more difficult for firms to compete in the local exchange market. The merger between Bell Atlantic and NYNEX was used to illustrate a situation in which costs to alternative suppliers increased as regulatory and legal proceedings were initiated to address changes in NYNEX's policy regarding assignments of existing customers. (GCI Ex. 2.0 at 68). Further, concerns are raised that, following the merger, SBC would unilaterally switch AI's OSS to an SBC standard without providing adequate time for CLEC's to accommodate such changes. (Id). The Commission finds that these cost driven and technical matters are of import, but can be worked out suitably.

Additionally, Staff asserts that the merger will increase incumbent's control over "bottleneck" facilities and thereby disadvantage competitors. The Commission disagrees with this argument finding the record unclear concerning an increase of incumbent control over "bottleneck facilities." Certain intervenors also argue that "efficiencies and economies of scale," will result from the merger and create barriers to entry. While the Commission recognizes that economies of scale and efficiencies may result from the merger, the Commission declines to conclude that these are barriers to entry of the type which will have a significant adverse effect on competition. The California Public Utilities Commission ("CPUC") rejected this entrenchment theory and we do likewise. As observedby the CPUC , "[e]ntrenchment has been rejected as an

anti-competitive harm when it is alleged to result from an improved efficiency or technological capabilities of the dominant firm as a result of its integration with the acquiring firm." (See CPUC SBC/PacTel Decision, 97-03-067, 3/31/97 fn 34). This Commission agrees with the California Commission that improved efficiencies or technological capabilities resulting from mergers are not automatically anticompetitive.

It has also been argued that SBC has a reputation for anti-competitive behavior in other states and that the entrance of SBC into Ameritech Illinois service territories will create the possibility for anti-competitive behavior. Although past actions may indicate future behavior, attempts to characterize the Joint Applicants' "reputation" in other states as a substantial evidentiary showing of "significant adverse effects" is rejected. On balance, the Commission also notes the Joint Applicants' different characterization of SBC's reputation as contained in the record. In the final analysis, the Commission is confident that Illinois law and our enforcement authority will effectively protect against any anti-competitive behavior and further put the Joint Applicants on notice that such anti-competitive behavior will not be tolerated.

Market Transition to Competition - Potential Competition Analysis

Staff also urged the Commission's consideration of potential competition in terms of the relevant market's structure, specifically in light of the local exchange market's transition to competition. While many of the issues which trouble the DOJ during their consideration of mergers in unregulated markets are appropriate, the Commission must frame its evaluation differently within the context of the regulated market in which Ameritech operates. The reality is that the concerns in an unregulated environment are an increase in price and the creation of a monopoly with an attendant increase in market power and the abuses of such monopoly power. In this instance, it has been asserted that a virtual monopoly already exists. Therefore, while the Commission is concerned about possible increases in barriers to entry as a result of the merger, the Commission also recognizes that this merger is not in and of itself going to create a monopoly which is a prominent concern under the DOJ Guidelines.

Indeed, it has been argued that the Commission should consider Ameritech Illinois a de facto or virtual monopoly and that this characterization should reduce the amount of credence that the Commission gives to a strict interpretation of the Guidelines. (Staff In. Br. at 38.) Since, evidence in the record demonstrates that SBC and Ameritech Illinois do not directly compete with each other, the merger does not involve two actual competitors and thus, is unlikely to result in direct anti-competitive effects. Because SBC and Ameritech do not currently compete, it is also unlikely that the proposed merger will alter the market structure, market shares or market concentration except to the extent already discussed above. Therefore, the Guidelines do not provide the Commission with an exhaustive inquiry into whether the proposed merger is likely to have a significant adverse effect on competition. In order to complete its analysis, the Commission now turns its focus to another area of discussion.

Possible Elimination of a Potential Competitor

While the Guidelines do not officially adopt certain judicial theories of potential competition such as the "actual potential competitor doctrine", the DOJ and other regulatory entities recognize that mergers which involve potential entrants may adversely effect competition in the relevant markets even where the firms to the merger are not currently competing. Therefore, while not rejecting DOJ's method of analysis, the Commission will look beyond the language of the Guidelines in analyzing SBC's potential entry into the Illinois local exchange market using these analytical theories designed to examine potential competition.

Identifying a potential competitor is a matter of some conjecture and is difficult to establish with absolute precision. Nevertheless, given that Staff and Intervenors, have raised a concern with respect to the "adverse effects" on the market resulting from the possible loss of SBC as a potential competitor the Commission will engage in the inquiry. The Commission will consider whether SBC qualifies as an actual potential competitor based on the argument that the loss of an actual potential competitor may harm competition. We will consider the evidence within the context of the actual potential competitor analysis, as addressed by the parties both in the initial stage of the proceeding and on reopening.

Actual Potential Competitor Doctrine

The Joint Applicants, while maintaining that the actual potential competitor analysis could lead to speculative conclusions, offered the following analytical framework , used by the FCC to evaluate the actual potential competitor theory based on the potential competition standards established by the U.S. Supreme Court as well as those standards relied upon by the Department of Justice. The doctrine of "actual potential competition" as laid out by the FCC contains five basic elements: (1) the market in question ("the target or relevant market") is highly concentrated; (2) few other potential entrants are "equivalent" to the company that proposes to enter the target market by merger (SBC); (3) the company entering the target market by merger would have entered the market but for the proposed merger; (4) that company had other feasible means of entry; and (5) such alternative means of entry offer a substantial likelihood of ultimately producing deconcentration in the target market or other significant pro-competitive effects." *Application of Pacific Telesis Group and SBC Communications Inc. for Consent to Transfer Control of Pacific Telesis Group and its Subsidiaries*, FCC 97-28 (rel. Jan. 31, 1997) ("SBC/PacTel Order") at & 18 (footnotes omitted).

1. Market Concentration

The evidence of record meets the first inquiry as the Commission has previously found in this order that the market is highly concentrated. (See Marine Bancorp., 418 U.S. at 631). ("The potential competition doctrine has meaning only as applied to concentrated markets.")

2. Other Entrants

Second, the Commission considers whether there are few other potential entrants "equivalent" to SBC.

Intervenors and Staff suggest that because SBC is an RBOC that it has "first hand experience" thereby making SBC unique and hence not "equivalent" to other potential entrants. However, the Joint Applicants contend that SBC gained its experience competing in local exchange markets outside of Illinois and thus, if the Commission considers SBC's local exchange experience as unique it should also consider the equivalent experiences of firms such as Bell Atlantic/NYNEX, BellSouth, GTE, and U.S. West. Further, even such firms as AT&T, MCIW and Sprint have local exchange experience as CLECs. Joint Applicants contend that these firms, with similar experiences, could be construed as being in some manner, "equivalent" to SBC. In light of these considerations, while SBC may have experience in the residential and small business local exchange markets outside of Illinois, SBC lacks some unique qualities possessed by firms such as AT&T and MCIW which are actual competitors in the Illinois large business market. The presence and visibility of AT&T and MCIW make them the most likely to rapidly capture market share from Ameritech Illinois in the near future. Additionally, any unique qualities which SBC may possess may be offset by the experiences of other firms, such as AT&T and MCIW, which are already competing in the Illinois large business market. The presence and visibility of these firms make them most likely to rapidly capture market share from Ameritech Illinois in the near future supporting the argument that these firms are in some manner "equivalent" to SBC.

Parties entered testimony identifying which firms should be considered actual and/or potential competitors. During the hearings, witnesses for Sprint, Staff, and AT&T all testified that the list of potential competitors included at least; BellSouth, Bell Atlantic, and U.S. West. (Woodbury Tr. At 1469-1470; Gillan Tr. at 1351-1353; Graves Tr. at 1654-1655, 1661-1664; Hunt Tr. at 1707, 1715). Staff contends that the Commission should not consider AT&T or MCIW on the list of potential competitors as these firms are actual competitors in the Illinois market. (See Hunt RR, Staff Ex. 9.01 at 15-16.) The Commission disagrees with the arguments of these parties because of the distinction between the small business and residential market segments versus the large business market segment. While AT&T and MCIW may represent a significant competitive force in the large business market, the presence of these two firms is much less in the small business and residential customer local exchange markets. (See; JA In. Br. on Reopening at 22). Further, the argument can be made that certain firms cannot be considered potential entrants because of some current market presence, however small, is not persuasive. The key inquiry is future competitive significance; if AT&T or MCIW have the "potential" to expand their respective market shares in the Illinois local exchange market, then for purposes of this analysis they are both actual competitors and actual potential competitors. (See, e.g., *In re Heublein, Inc.*, 96 F.T.C. 385, 590-91 (1980); *In re Champion Spark Plug Co.*, 103 F.T.C. 546, 631 (1984)).

Brand name also contributes to the "equivalency" of potential telecommunications providers. The record contains little evidence that SBC has a

strong brand names in Illinois or inspire an increased amount of confidence among consumers. This lack of evidence contrasts with the strong national and international brand names of potential and actual competitors such as MCIW, AT&T and Sprint who are all well recognized and active in the industry. (*See* Gebhardt Surrebuttal, SBC/AM. Ex. 3.2 at 10; Harris Rebuttal, SBC/AM Ex. 4.1 at 10-11). In such a rapidly changing industry, benefits such as brand name may well balance out any advantages held by SBC thereby increasing the number of firms which we consider "equivalent" potential entrants. Considering the foregoing decisions we conclude that more than a few potential entrants are equivalent to SBC.

3. Entry into the Relevant or Target Market but for the Merger

Third, the Commission considers whether SBC would have entered the market but for the merger. This inquiry goes directly to the Company's incentives to enter the market. Therefore, the Commission examines those factors that indicate that SBC "would" have entered the relevant market as opposed to the evidence in the record which indicates that SBC "could" have entered the market. (See, Mercantile Texas Corp. v. Bd. of Governors of the Fed. Reserve System, 638 F.2d 1255 (5th Cir. 1981)). In other words, it is probable, not possible entry by SBC into the relevant market within a reasonable period of time which concerns the Commission. Evidence entered into the record by Staff and others indicates that SBC may have the incentive to eventually enter the large business market in Chicago. However, evidence of record strongly shows no reasonable probability that, but for the merger, SBC would offer local exchange service in Illinois, particularly to service small business and residential customers, within the next two years. Even the attempt to capture large business customers requires extensive planning, advance marketing strategies, surveys, testing and the like. No such evidence appears on record.

In considering evidence regarding the future effects of the merger we are presented with record evidence containing varying degrees of speculation. (See, Mercantile, 638 F2d 1255.) Parties to this proceeding have expressed some concerns about the forward-looking nature of this evidence. (See e.g. AG, Init. Br. at 21 See generally Joint Applicants Init. Br.). These concerns stem largely from record evidence indicating *possible* outcomes as opposed to *probable* outcomes. (See however, probability analysis in Mercantile Texas Corp., 638 F.2d at 1268-1269). For example, Joint Applicants' attempt to discount many arguments related to barriers to entry and anti-competitive conduct by asserting that these arguments are speculative and lack foundation in fact or evidence. (See JA R. Br. at 25). Therefore, the Commission will carefully consider the evidence as it relates to future competition.

Although the large business market is currently experiencing an increasing amount of competition from firms such as AT&T and Sprint, the residential and small business markets remain highly concentrated. As to these markets, nothing shows it probable much less reasonably probable, that but for the merger SBC would enter to serve small businesses and residential customers.

The Joint Applicants submitted testimony which demonstrates that the best, i.e., most profitable, route for competitive entry is for SBC to serve large, corporate customers on a national basis through its SBC owned facilities. SBC itself stated that its business decision is driven by the fact that large corporate customers contribute approximately 18% of Ameritech's total revenues even though these numbers only constitute about 1% of its customer base, and that those customers want to obtain fully integrated services from one provider on a broad geographic basis. (Kahan Rebuttal Testimony SBC/AI Ex. 1.1 pg. 18). Many parties argue that the National Local Strategy provides direct evidence that SBC "would" enter the relevant market but for the merger. The Commission does not agree for the reasons discussed below. However, the record contains additional evidence which the Commission must consider in addressing whether the SBC would have entered the relevant market but for the merger in the next two years.

Staff argues that SBC would likely have entered the market but for the merger for a number of reasons. Included among these reasons are; 1) SBC has the resources to enter the market; 2) SBC has knowledge of local exchange service; 3) SBC has experience in the local exchange market; and 4) SBC's efficiencies tend to indicate that such entry would be profitable. (*See* Staff In. Br. at 62-66). Staff also references SBC's testimony in the SBC/PACTel merger as objective evidence that SBC "would" enter the market. 21st Century also introduced testimony asserting that SBC was in a position to and declared its intentions to, compete in Illinois markets with both facilities based and wireless initiatives. After reviewing the entire record the Commission concludes that, although SBC may have considered entry into the Chicago market a number of years ago, there is little if any current evidence which indicates that entry into the market, particularly the small business and residential markets, is still being considered by SBC. The Commission's conclusion is further supported by the record evidence discussing the rapidly changing nature of the telecommunications industry. The rapidly changing markets bring into question the validity of two and three year old business plans particularly given rebuttal testimony entered by the Joint Applicants. In this type of environment what a company may have considered two or three years ago may no longer be a prudent business decision. In other words, change breeds change. So too, AT&T and the Attorney General suggest that both Ameritech and SBC are currently capable of out-of-region entry. However, even if correct, such capability only addresses the issue of whether SBC "could" enter the relevant market, not whether SBC "would" enter the relevant market in the next two years. While the Commission acknowledges that some of the evidence may tend to indicate that SBC has the incentive to enter, and "could" enter the local exchange market, we do not believe that these factors support the conclusion that SBC "would" enter the market in the next two years.

In summary, the Commission does not find the evidence supports, with a reasonable probability, that SBC "would" have entered the small business or residential markets in the next two years. It is important to note that the Commission is not rejecting the notion that the evidence shows no *possibility* that SBC could become an entrant under certain sets of circumstances or that SBC might have entered certain

segments of the local telephone market. But after applying the standard of "reasonable probability" the Commission finds that a preponderance of the record evidence does not support a conclusion that SBC would be an actual potential competitor in all segments of the Illinois local exchange markets i.e., the relevant market in the near future. (See also SBC/PacTel Decision of the California Public Utilities Commission, 1996).

4. "Other Feasible Means of Entry"

Fourth, the Commission considers whether SBC has other, feasible means of entry into the local exchange market other than the proposed merger. Entry into a relevant market, other than merger or acquisition, generally occurs either through a toehold or de novo entry. A toehold entry is considered entry into a market, by a firm not currently competing in the market, in combination with another entity already present in the market.By contrast, de novo entry is independent entry into the market. The record evidence presents the Commission with conflicting positions on the issue of whether SBC could or would enter the local exchange market and under what means. Although SBC's executives testified extensively, both in the initial proceeding and during the reopening, that SBC has no plans to enter Illinois local markets in the near future, the record contains other evidence which suggests that SBC may have feasible means of entry into the relevant market other than the merger.

Staff witness Dr. Hunt testified that, "I think it's very *possible* that SBC could enter the market, wanted to enter the market through cellular. . ." (Staff Int. Brief at 23 citing Tr. at 1725-26). Other record evidence counters this claim with repeated testimony from the Joint Applicants that, absent the proposed merger, SBC has no plans to implement its National Local Strategy and no alternative feasible means of entry. Staff and the Attorney General both submitted evidence indicating that SBC could pursue a cellular expansion strategy by using the firm's cellular investments as toeholds for alternative entry into Illinois. As evidence of SBC's intent to employ this strategy, parties submitted evidence that SBC undertook a cellular to local exchange entry trial run in Rochester, New. York. Although the Attorney General found SBC's testimony "unconvincing", the Commission concludes that SBC adequately countered the suggestion that cellular expansion is a feasible alternative means of entry by providing evidence that SBC considered the trial run in Rochester (based on cellular) a failure. SBC testimony also undermined the validity of Staff's argument by pointing out the significant differences between the Illinois local exchange markets and the Rochester markets. In fact, there is no evidence that SBC could use its Illinois cellular switches for local exchange networks. SBC offered unrebutted testimony demonstrating that SBC's cellular switch technology in Chicago cannot be used for local exchange service. (Kahan Surrebuttal, SBC/Am. Ex. 1.2 at 10). In view of this testimony, the Commission concludes that SBC's entry through a cellular toehold is not currently a feasible alternative means of entry in the next two years.

Parties also presented evidence that SBC's financial investment in OnePoint could provide a toehold for alternative entry. Additionally, Staff and CUB argue that SBC's certification to provide local exchange service in Illinois through its CLEC, SBMS,

is evidence that SBC would enter into the market. (See; ICC Staff Ex. 4.00 at 24, 26-27; Ex. 9.0 at 21-23). As for SBC's use of its investment in the multi-dwelling niche provider, OnePoint, as a toehold into the Chicago market, SBC's witness Kahan testified that SBC has no seats on the board of OnePoint and has no control over the prices, strategies or business plans for OnePoint. Staff also presented testimony that SBC currently has financial investments in Williams Communications and Concentric Communications. (Graves Direct, Staff Ex. 4.02 at 11-13). However, the Joint Applicants submitted rebuttal testimony indicating that SBC's investments in these firms were minority investments and were solely financial in nature. (Kahan Direct, SBC/Am Ex. 1.3 at 4) In view of this testimony, the Commission concludes that it is not reasonably probable that SBC would use its minority investment in either OnePoint, its other investments, or its cellular affiliate, as a toehold for alternative entry in the next two years.

Regarding the issue of whether SBC has alternative independent means of entry, the Commission is again faced with conflicting evidence and party positions. SBC's executives and decision making personnel testified that while SBC may have previously considered entering Illinois, SBC's current plans do not include entry into the Illinois local markets within the next two years. (See Kahan Rebuttal, SBC/AI. Ex. 1.1 at 66-69; Kahan Surrebuttal, SBC/Am. Ex. 1.2 at 8-12). The record contains no current business or strategic plans of SBC to enter the Illinois local exchange market which the Joint Applicants argue supports Kahan's sworn testimony. However, given the self-serving nature of this testimony, the Commission will consider other factors, urged by several of the parties, which impact the issue of independent entry as a feasible alternative to entry through merger.

Merger opponents argued that SBC obtained state certifications for local exchange service in Illinois and this demonstrates an alternative means of entry. However, during the rebuttal phase of the proceeding, none of the parties brought forth evidence which adequately disputed SBC's claims about future plans. The mere acquisition of state certifications for local exchange service in Illinois, in and of itself, does not support the argument that independent entry into the market is intended or a reasonable alternative form of entry within the next two years. Moreover, the record contains evidence that SBC might not come into the Illinois market at all since it has a number of attractive options from which to choose including the pursuit of international opportunities. Nothing demonstrates that SBC would prefer entering Illinois over other opportunities for either expansion or investment. Another option would include entering the large business segment of the relevant market only to focus on select large business customers. (Tr. 2660, 2673-74, Woodbury). Even Staff allowed that SBC's entry options were varied and might not include alternative entry into the Illinois market either in the short or in the long term. (Tr. at 2833, 2835 Graves; *also see* Tr. at 2899, Hunt).

The evidence, taken and weighed together fails to rise to the level necessary for the Commission to find, under the actual potential competitor doctrine, that alternative, feasible means of entry, into the broader local exchange market, other than through the proposed merger, are easily available to the Joint Applicants. Although

many parties argued that SBC has alternative means to enter, evidence also exists which shows that SBC might only enter the large business market and choose to serve only large business customers and not serve the less profitable small business and residential segments of the local exchange market. No evidence supports the proposition that SBC would have entered the residential segment of the local exchange market within the requisite time period. Therefore, the Commission concludes that record evidence is insufficient to support the inference and the conclusion that entry by SBC either independently, or through a toehold is a reasonably probable means of entry with a two year period.

5. Deconcentrating Effect of Entry or Other Significant Pro-Competitive Effects

Perhaps the most critical factor for our consideration is whether, if SBC were to enter the relevant market, such entry would have a substantial likelihood of producing a significant deconcentration of the target market or other significant pro-competitive effects. A small addition to existing competition is not enough. (Mercantile 638 F2d 1270). The Commission notes the testimony of the various parties, and our conclusions above, that any alternative entry into the local exchange market within the next two years would be limited in scope and geared to capture large business customers.

Staff and other parties argued that SBC's entry would "shake up" the market and result in a relatively significant deconcentration of the local exchange market. The Commission recognizes that the entry of a large firm into a concentrated market may "shake things up". But we also recognize that SBC's entry based on this premise may have little, if any, lasting impact. (See *Mercantile, at* 1270) Moreover, testimony indicates that the big business strategy does not significantly impact the level of competition within the residential and small business market segments. There is little evidence that SBC's entry into the market would have a greater impact on the Illinois local exchange market, particularly the small business and residential markets, than that of potential entrants such as, AT&T, MCIW, and Sprint. Each of these potential entrants possess significant technical and capital resources, ILEC experience (except for MCIW), customer loyalty and national brand names. SBC, on the other hand has no name recognition or visibility in our markets and experience tells us that it would take substantial time and effort for SBC to accumulate a market share and deconcentrate the market. Thus, entry by SBC into only the large business market would not have a meaningful deconcentrating effect on the broader local exchange market within our timeframe.

The evidence supports some but not all of the elements set out in the APC doctrine. In view of the foregoing discussion, the Commission concludes that SBC should not be considered on actual potential competitor to Ameritech Illinois for local exchange services in Illinois, particularly for mass market customers. The Commssion finds it important to note that the evidence on the issue of SBC's characterization as an actual potential competitor is such that the evidence allows for more than on

reasonable inference and that the interpretations, import, and applications of this doctrine have varied. Furthermore, it is only one part of our analysis and does not constitute a complete answer to the real issue before us.

Summary

On the basis of all the discussion above, the Commission concludes that the evidence in the record does not adequately support a finding that the proposed merger will have an adverse effect on competition in the local exchange markets. Relevant to where the markets stand today, large business, small business and residential, the merger, as proposed, will produce little change. As we stated above, this Commission defines a "significant adverse effect" under the language of §7-204(b)(6) as more than just an increase, or retention of market share by an incumbent firm. We require evidence which tends to indicate an increase in current or future barriers to entry or changes to the relevant market which may frustrate the implementation of Commission policies.

Additionally, the Commission takes into account the effect of proposed mergers on future competition within the relevant markets. We do not consider any single factor or finding listed above as definitive evidence that a proposed merger will or will not likely have a significant adverse effect on competition. Instead, the Commission weighs all of the above considerations within the context of the industry and the current state of competition within the relevant markets before coming to a conclusion. Further, the particulars of any individual case may produce a significantly different outcome when the Commission applies the language of the statute to a set of facts and circumstances.

The Commission concludes that the evidence in the record does not adequately support a finding that the proposed merger will have an adverse impact on potential competition in the local exchange markets in Illinois, particularly the residential and small business markets. The Commission finds, based on our above discussion that the proposed merger is not likely to increase market barriers to entry or to inhibit the transition of the Illinois local exchange market from a regulated market to a competitive market within the next two years. The Commission also finds it unlikely, that SBC's entry into only the large business segment of the market would single-handedly de-concentrate the broader local exchange market in Illinois.

In this instance, the Commission finds that the Joint Applicants have met their burden under the requirements of §7-204(b)(6) and the proposed merger is "not likely to have a significant adverse effect on competition within the markets over which the Commission has jurisdiction." Both the totality of the evidence and the sum of our findings under other subsections of §7-204 lead to this conclusion.

The New Commitments

We recognize that the Joint Applicant application for merger approval was amended to include a large number of additional commitments which relate to the

evolving competitive market in telecommunications. As detailed elsewhere, we have examined and discussed the evidence on each individual commitment and have rendered separate conclusions on each in turn. Section 7-204(f) states that the Commission may "impose such terms, conditions or requirements as, *in its judgment*, are necessary to protect the interests of the public utility and its customers." (See 220 ILCS 5/7-204A) (emphasis added). To the extent that we found any particular commitment of the Joint Applicants unsatisfactory, we exercised our conditioning authority under Section 7-204(f), as necessary, to modify the conditions and/or terms of the proposals in an effort to improve upon the commitments and in order to protect the interests of Ameritech Illinois and its customers. The Commission's modifications therefore take into account the evidentiary testimony put forward by the various Intervenors in response to the Joint Applicants original commitments on reopening and improve upon those commitments.

While we find that the amended application and the commitments contained therein represent substantial pro-competitive benefits for CLECs and end-users in Illinois, the Commission's analysis of the merger's impact on competition renders its conclusion based upon all facts contained in the record. The commitments made by the Joint Applicants and subsequent modifications made by this Commission are designed to provide long term assurances to both the utility and its customers in a rapidly changing industry. However, the Commission's final analysis of whether the Joint Applicants reorganization will have a *significant adverse effect* upon competition does not rely upon the commitments and subsequent modifications of this Commission.

G. Whether The Proposed Reorganization Is Likely To Result In Any Adverse Rate Impacts On Retail Customers. (Section 7-204(b)(7)).

Joint Applicants' Position

Joint Applicants contend that the proposed merger will not result in any adverse rate impacts on retail customers. They state that, because AI will continue to be the regulated carrier in its service territory, it will remain subject to the Plan approved by the Commission in Docket 92-0448. The Plan does not permit AI to raise noncompetitive services rates. To the contrary, the index requires year-by-year decrease in inflation-adjusted prices, assuming continuation of current economic conditions. Accordingly, they argue, the retail rates are no more at risk the day after the merger than they are the day before. (Kahan Rebuttal, SBC/Am. Ex. 1.1 at 96-97; SBC/Am. Init. Br. at 29.)

Joint Applicants further argue that, rather than threaten any increase in retail rates, the merger is intended to protect rates. They opine that the merger will create the economies of scope and scale that will enable AI to continue region-wide network upgrades. They maintain that, through the merger, Ameritech and SBC will be able to unify procurement for both of their operations, thereby expanding the scale of purchases and gaining increases in volume discounts from their suppliers. They argue that AI must be permitted to reduce and spread costs in this manner, especially in light

of its universal service obligations and the growing number of CLECs that focus their competitive energies on larger business customers. (SBC/Am. Init. Br. at 30-31.)

Staff's Position

Staff interprets the term "adverse rate impacts" in Section 7-204(b)(7) to encompass two standards. One, that the proposed merger is not likely to necessitate rate increases to the Company's retail services. Two, that the proposed merger is not likely to have an adverse impact on the price-to-cost relationship of its services. (Staff Init. Br. at 135.)

Regarding the first standard, Staff takes issue with Joint Applicants' position that the merger will reduce any upward pressure on the Company's rates. Staff's concern arises from AI's current involvement in a number of proceedings before this Commission that require an analysis of costs in order to establish rates. In particular, AI has filed a petition seeking leave to rebalance its residential network access rates, and there are two TELRIC investigations before the Commission. Staff argues that, in order for the Commission to make informed decisions in these cases, we need to examine updated cost studies. Consequently, Staff recommends that, if the Commission approves the merger, it should condition its approval on the submission of updated LRSIC, TELRIC, shared and common cost studies within six months after final regulatory approval. Additionally, Staff recommends that the Commission utilize those updated studies in its analysis of the Company's request for rate rebalancing and in the two TELRIC investigations. (Staff Init. Br. at 135-36). It notes that Joint Applicants have agreed to work out priorities for cost studies to be filed following approval, and that this approach is acceptable to Staff. However, Staff remains concerned because the Joint Applicants do not agree that the updated studies should be utilized in the rate rebalancing proceeding. (Staff Init. Br. at 136.)

Staff also disagrees with the Joint Applicants' contention that AI's Plan insulates customers from rate increases. Staff notes that there are a large number of Ameritech Illinois services that do not enjoy any of the Plan's perceived rate protections. These include all new services which are excluded from the Plan for a period of one year. Additionally, all of Ameritech Illinois' interconnection, transport, termination and UNE services have been excluded from the Company's Alternative Regulation Plan. Staff also notes that pursuant to the terms of Ameritech Illinois' Plan, the Company is allowed to file for rate increases that exceed the Plan's limits on 45 days notice. This provides yet another vehicle to reflect Ameritech Illinois' cost increases in its customer rates. (Staff Reply BR. at 107-108). In addition, Staff notes that all of Ameritech Illinois' competitive services are automatically removed from the Plan by virtue of their (re)classification. As a result, they also do not enjoy any of the Plan's perceived rate protections. (Id.) Moreover, Staff notes that the Plan prohibits Ameritech Illinois from reducing the prices for its non-competitive services below their long run service incremental cost ("LRSIC"). Ameritech Illinois is also prohibited from reducing the rates of non-competitive services that are currently below LRSIC further below those LRSICs. (Id. at 108-109) (citing Order in Docket 92-0338/93-0239, Appendix A and Order in 96-

0172 at 12-13 and Order in 98-0259 at 7)). Staff contends that all of these provisions of the Plan provide Ameritech Illinois with avenues to raise rates if needed. (Id.).

Regarding the second standard, Staff concludes that, absent the allocation of merger-related savings to the Company's customers, the merger will impact negatively the price-to-cost relationship of its service. Therefore, Staff recommends that, if the Commission approves the merger, it should condition its approval on the allocation of merger-related savings to AI's customers. (Staff Init. Br. at 136-37). Staff disagrees with the Joint Applicants' position that a price-to-cost relationship is inconsistent with Ameritech Illinois' Plan, and provides a number of arguments to support its position. Staff's arguments are set forth in detail in Staff's Position under Section 7-204(b)(1). Staff's argument and specific proposal for the allocation of savings is set forth in more detail in the Commission's analysis under Sections 7-204(b)(1) and (c).

Intervenors' Positions

CUB contends that, under Section 7-204(b)(7), the Commission must reject the merger if it finds that any kind of adverse rate impact is likely as a result of the merger. CUB makes numerous arguments to support its conclusion that the merger would result in adverse rate impacts.

CUB argues that Joint Applicants' reliance on their Plan as the basis for asserting that the Company's noncompetitive service rates will not be increased post-merger is tenuous. It asserts that this reliance on the existing formula as a means of constraining noncompetitive prices assumes that the productivity factor will remain static and that current economic conditions will persist. In further support of its position, CUB argues that the rate freeze, and possibly the price cap plan, will expire in October of 1999, thereby providing no price protection. (CUB Init. Br. at 9-14.)

CUB maintains that the proposed reorganization will result in adverse rate impacts because Joint Applicants will not commit to extending the residential rate basket freeze post-merger. It asserts that SBC's projections allegedly show an increase in the basic residential access line rate from $16.35 in 1998 to $17.35 in 2008. CUB asserts this is evidence of the merged company's intention to increase prices. (CUB Init. Br. 14-16.)

CUB argues that the premium paid for the acquisition of Ameritech will likely trigger the need for increased retail rates post-merger. CUB asserts that, because SBC is paying $13.2 billion over the pre-announcement market value of Ameritech stock and $47 billion over the net book value of its assets, the merger will place significant upward pressure on prices for non-competitive services. (CUB Init. Br. 16-17.)

CUB also argues that SBC's alleged reliance on Ameritech's noncompetitive service core revenue base to finance the NLS will have an adverse impact on rates. In support of this position, CUB asserts that the Strategy will not generate positive cash

flow for ten years, and SBC will use revenues from in-region noncompetitive service markets to support the NLS. (CUB Init. Br. at 17-18.)

Next, CUB claims that Joint Applicants have a propensity to increase the rates of recently reclassified competitive services. It claims that AI has been awarded significant rate increases upon reclassification of numerous, traditionally noncompetitive service. CUB points out that both SBC and Ameritech declined to ensure that reclassified services will not undergo rate increases. (CUB Init. Br. at 19-26.)

In connection with the above argument, CUB asserts that SBC's reclassification of certain services as competitive in the PacBell service territory, with proposed accompanying price increases, is evidence that proposed rate increases are likely in Illinois post-merger. CUB claims that several rate increase proposals have been made by the reconfigured PacBell. (CUB Init. Br. at 26-28.)

Last, CUB argues, even if rates remain the same as a result of the merger, rates allegedly would no longer be least-cost, in violation of Section 7-204(b)(1). In support of this contention, CUB refers to testimony by Joint Applicants indicating that the costs associated with providing telecommunications services will be reduced as a result of the merger. CUB states that an examination of how the proposed merger will impact cost-to-price relationships is relevant to the analysis of 7-204(b)(7) because "adverse rate impacts" encompasses more that rate increases. CUB asserts that adverse rate impacts can occur when costs fall significantly but there is no concomitant decrease in price. (CUB Init. Br. at 28-31.)

The AG contends that Section 7-204(b)(7) requires the Commission to find that there is no "likelihood" of "any" adverse rate impact on retail customers. It argues that the qualifier "any" creates an absolute standard which requires the Commission to find that there are no adverse impacts whatsoever before approving a merger. In support of this position, the AG cites Illinois Bell Telephone Co. v. Illinois Commerce Comm., 283 Ill. App.3d 188, 669 N.E.2d 919 (2nd Dist. 1996) in which the Court construed the phrase "any incremental risk or increased cost of capital" under Section 9-230.

The AG contends that the proposed merger will result in adverse rate impacts for several reasons. First, it argues that retail services currently subject to the price cap can be reclassified as "competitive" and be increased by a tariff filing. In support of this position, it asserts that Ameritech has used reclassification in the past to increase rates. Second, it argues that competition is not currently a "limiting factor" on rates as suggested by Joint Applicants. It asserts that giving the local exchange monopolist an opportunity to price competitively has only caused the company to increase rates. Third, it contends that the overwhelming driver behind the merger is to protect shareholders from earnings dilution. The AG claims that SBC wants a guaranteed revenue stream from noncompetitive local service markets to finance the NLS without subjecting its shareholders to the risks inherent in the NLS. The AG asserts that, as the NLS loses money and while ratepayers wait for the benefits of the merger to materialize, SBC will satisfy its shareholders' expectations of dividend growth through

rate increases. Fourth, the AG contends that the purchase premium will result in adverse impacts on rates. Fifth, it refers to SBC's requests for rate increases in California as evidence of its future rate policies in Illinois if the merger is approved. Last, the AG is concerned that, although SBC claims that increased competition is a resulting benefit of the merger, it is unwilling to cite reduced prices (the most obvious benefit of competition) as a likely outcome of the proposed merger. (AG Init. Br. at 19-27.)

Cook County also asserts that the proposed reorganization is likely to result in adverse rate impacts. First, it alleges that the purchase premium will require AI to recover $1.7 billion in additional annual intrastate earnings for a period of ten years. This, Cook County asserts, implies a significant overall increase in intrastate revenues. Second, it argues that the need to support the Strategy with core revenue financially from the Company's noncompetitive services will have an adverse impact on retail rates. Third, it contends that, although the current price cap system has resulted in decreased rates, SBC is likely to seek a significant decrease or elimination of the offset factor. Cook County argues that this could lead to substantial rate increases. Fourth, it contends that SBC could obtain rate increases through tariff filings in noncompetitive services as well as through higher rates for services that are reclassified as "competitive." In support of this argument, Cook County states that, since the PacBell merger, SBC has submitted applications and tariff filings to the CPUC seeking increases in certain rates. It suggests that similar requests can be expected in Illinois if the merger is approved. Last, it briefly argues that the Company's impaired ability to raise necessary capital on reasonable terms and to maintain a reasonable capital structure, as well as the reduced level of potential competition AI will confront within the local service market, adversely affects rates. (Cook County Init. Br. at 43-47).

Sprint contends that, because the merger allegedly will increase the incentives and ability of the merged entity to discriminate against competitors in both the local and interexchange markets, it follows that the merger will have an adverse rate impact on retail customers in violation of Section 7-204(b)(7). Sprint asserts that SBC's own financial projections reflect an increase in retail rates over the ten years following the merger. Sprint further asserts that SBC and Ameritech have not provided safeguards to offset the adverse rate impacts associated with the proposed merger. (Sprint Init. Br. at 37-38.)

Nextlink contends that the premium paid to acquire Ameritech, SBC's plan to use Ameritech revenues for out of region competitive ventures, its conduct since the PacBell merger, and the loss of a potential competitor make it impossible for the Commission to find that the proposed reorganization is not likely to result in any adverse rate impacts on retail customers. (Nextlink Init. Br. at 13-16.)

In particular, Nextlink argues that the acquisition is likely to pressure SBC to generate additional revenues from Illinois consumers in all markets in which it does not face price-constraining competition. This pressure, Nextlink asserts, comes from the premium SBC will be paying to acquire Ameritech. Additional pressure to raise rates

allegedly stems from SBC's plan to use revenues from non-competitive services to support out of region competitive ventures. Nextlink also suggests that SBC's conduct in California since the PacBell merger indicates its desire to raise rates. Nextlink points out that SBC has submitted tariff filings seeking rate increases in California and, in its pending price filing, PacBell proposes significant changes to the current regulatory framework which would allow PacBell upward pricing flexibility for services not currently subject to competitive pressure. Lastly, Nextlink argues the elimination of SBC as a potential competitor that could put competitive pressure on Ameritech and CLECs prevents the Commission from concluding that the acquisition is not likely to have any adverse rates impact. (Nextlink Init. Br. at 13-16).

Similar to several other parties, 21st Century contends that the purchase premium, as well as SBC's plan to use Ameritech Illinois revenues and other non-competitive service markets to support out-of-region competitive ventures, will have an adverse effect on rates. 21st Century also has concerns about the rate increases SBC has sought in California since the merger with PacBell. 21st Century agrees with Staff's argument that the acquisition, as proposed by SBC, will result in telecommunications services that are currently priced above cost being priced even more above cost. (21st Cent. Init. Br. at 21-22.)

CTCA contends that, if the Plan deprives customers of the benefits of reorganization synergies, adverse rate impacts will result. CTCA agrees with Staff's contention that, if merger synergies are not accounted for in some manner, Ameritech Illinois' alternative regulation plan can no longer be presumed to produce just and reasonable rates. CTCA alleges that a similar position was adopted by the Connecticut Commission in its order approving the SBC-Southern New England Telephone merger. (CTCA Init. Br. at 31-32.)

Additional Evidence/Arguments on Reopening

The reopening of the record in this proceeding raised the following issue related to the National Local Subsidiary and its potential effect on retail rates.

Question 9; Attachment A "National Local Subsidiary

A clear explanation of the National Local Subsidiary, as used in this docket, and the impact that this subsidiary would have on retail rates. Explain what happens to AI's retail rates should the applicants transfer the top-revenue customers to this subsidiary for telecommunications services. Explain what the revenue impact would be for Ameritech Illinois if the top customers are shifted to the National Local Subsidiary. Explain if the National Local Subsidiary would provide local service for its customers in Illinois. Explain whether the National Local Subsidiary would be certified as a CLEC in Illinois. Explain whether the National Local Subsidiary would be treated as any other CLEC would be treated in its interactions with AI.
(Question No. 9, Attachment A; June 4, 1999 letter).

Joint Applicants' Position

Joint Applicants note, as a threshold matter, that this issue was not the subject of this docket. Joint Applicants state that they did not make it a subject of this docket because the National-Local Subsidiary will not operate directly in Illinois for the foreseeable future.

Joint Applicants explain that they intend to pursue the primary piece of the National-Local Strategy -- entry into out-of-region markets (where neither SBC nor Ameritech is the incumbent LEC) -- through a newly formed subsidiary. However, they believe that the use of a National-Local subsidiary out-of-region will have absolutely no impact on the operations of Ameritech Illinois or on its retail rates.

SBC's Mr. Kahan explained how Ameritech Illinois would participate in the National-Local Strategy. Specifically, Joint Applicants' incumbent LEC operating companies like Ameritech Illinois would cooperate with the National-Local Subsidiary in the same way that incumbent LEC cooperate today with companies like AT&T and MCIW to provision multi-state service contracts. Joint Applicants note that it is relatively common business practice even now for a national carrier like AT&T or MCIW to bid on Requests for Proposals ("RFPs") from and to enter into contracts with national or multinational companies for comprehensive telecommunications service running the gamut from local exchange to interstate, interLATA across the country or around the world. In order to respond to such RFPs and enter into such contracts, those carriers will, in essence, subcontract with LECs like Ameritech Illinois to provide certain local exchange services. Those local exchange services are acquired out of the LEC's tariffs. Moreover, subcontracting for such services does not require certification since, under these circumstances, Ameritech Illinois is the local service provider for state certification authority purposes.

A primary purpose of the proposed merger is to allow Joint Applicants to compete effectively for the high volume, high revenue customers that enter such contracts. Unlike their competitors, however, Joint Applicants (who will ultimately view the economic return on serving these customers on a consolidated basis) do not have an incentive to move such customers off the incumbent network, given their prior and continuing investments in the network. Since these network costs are driven far more by whether the traffic is actually carried on the incumbent network than by who retails the traffic, the customers of the incumbent network will benefit from the existence of the National-Local Subsidiary and its strong incentives to continue to use the incumbent network.

Under the approach to be followed by Joint Applicants, at least initially, the National-Local subsidiary will not require certification in Illinois and the National-Local subsidiary will not itself provide local exchange services in Illinois. Those services will continue to be provided by Ameritech Illinois by authority of Ameritech Illinois' existing certification and under Ameritech Illinois' tariffs. However, all dealings between

Ameritech Illinois and the National-Local Subsidiary will be controlled by federal and state affiliate transaction rules, and will be subject to review by the Commission. Thus, Joint Applicants maintain that there will be no impact on retail rates in Illinois.

Joint Applicants add that if at some time in the future they wish to have the National-Local Subsidiary provide local exchange service in Illinois, they would first have to seek appropriate local exchange certification from this Commission. As indicated above, Joint Applicants do not presently intend to pursue their National Local Strategy in this manner. Nevertheless, to address the apparent concerns in Chairman Mathias' letter and stated by Staff, Joint Applicants are willing to make an additional commitment not to seek local exchange certification for their National-Local Subsidiary in Illinois prior to January 1, 2003, which should be more than enough time for SBC to obtain interLATA approval under Section 271 of TA96 in Illinois.

Joint Applicants further state that even if the National-Local Subsidiary becomes a CLEC in the State of Illinois after January 1, 2003, it could not "transfer the top revenue customers to this Subsidiary for telecommunications services" as posited by the Commission's question. First of all, they argue, that CLEC would have to enter into an interconnection agreement with Ameritech Illinois. Any interconnection terms it received would have to be made available to other CLECs in Illinois pursuant to TA96. Also, any such transaction between the National-Local Subsidiary and Ameritech would continue to be an affiliate transaction covered by applicable federal and state affiliate transaction rules, a limitation that no other CLECs would face. In addition, the National-Local Subsidiary, as an Illinois CLEC, could not receive any preferential terms or treatment from Ameritech Illinois that were not provided to other CLECs on a non-discriminatory basis.

Joint Applicants state that if, under these circumstances, the National-Local Subsidiary competed for the customers of Ameritech Illinois, it would have the same array of options to serve those customers as any other CLEC. However, Joint Applicants have noted their intent and incentive to continue to utilize the Ameritech Illinois network in serving those customers.

Staff's Position

In response, Staff witness Graves testified that the Joint Applicants may wish for their National Local customers to be served through one of its strategic partners such as Williams Communication or Concentric Communications rather than establishing a separate subsidiary. Staff Ex. 4.02, at 24. He further testified that if the Joint Applicants wished to serve National Local customers itself, it would have to utilize a separate subsidiary in incumbent markets because SBC will only be able to provide in-region, inter-LATA telecommunications services (once Section 271 relief is granted by the FCC) through a separate affiliate. See, 47 U.S.C. Sec. 272(a)(1)(A), (2)(B). The Joint Applicants concede this fact. Amended Joint Application, Ex. 6 at 28 n. 24; SBC-Ameritech Ex. 1.3 at 18.

Staff acknowledges the Joint Applicants' change in its commitment for the National Local Subsidiary. However, Staff still has concerns regarding this issue. One such concern is that a combined SBC/Ameritech would be able to exercise considerable market power even through an affiliate. This market power could be utilized to cross subsidize non-utility activity, misallocate costs, and possibly cause adverse rate impact to captive customers. It is far from certain that sufficient competition to restrain SBC/Ameritech's market power will develop by January 1, 2003. In order to guard against SBC/Ameritech utilizing its market power in a non-competitive manner the Commission could either: (1) review the status of competition in 2003 and decide at that point whether of the National Local affiliate can enter as a CLEC in Illinois or (2) restrict the entry National Local affiliate until SBC/Ameritech holds less than a 50% market share of the local market in Illinois.

AT&T's Position

Mr. Gillan testified that a principal reason for the merger is Joint Applicants' National Local Strategy, which would be implemented via the National Local Subsidiary ("NatLoCo"). Mr. Gillan testified that the merger would establish NatLoCo as a company serving nearly 40% of the nation's multi-line business market within its franchise footprint. Understanding how NatLoCo intends to leverage its exchange footprint against rivals is the single most important competitive issue of the merger. Creating a massive footprint of incumbent facilities is the reason for the merger – and is also the reason the merger poses a threat to competition. Mr. Gillan explained that by capturing more of a customer's locations within the footprint of its affiliated ILECs, SBC can then bundle these services together in a package that only an equally large ILEC could match. He testified that the only way to lessen the potential harm to competition from this strategy would be through conditions that: (1) reduce the market power of the combined entity, and (2) prevent the combined entity from leveraging the market power that remains. AT&T Ex. 1.2 (Gillan DOR), at 6-7.

Mr. Gillan framed the fundamental questions as follows: What will be the relationship between Ameritech-Illinois (SBC's ILEC) and NatLoCo (SBC's "CLEC")? Does Ameritech-Illinois intend to treat NatLoCo like any other CLEC? Or, will

Ameritech-Illinois discriminate in favor NatLoCo, thereby enabling SBC to bundle monopoly (i.e., within franchise) services with competitive (i.e., beyond franchise) services into a single package that only another massive ILEC can match? Id. at 21-22.

Mr. Gillan testified that the Joint Applicants apparently envision an arrangement whereby Ameritech-Illinois would offer and provide local service in Illinois, while NatLoCo would have some role in "coordinating" the services of SBC's ILEC affiliates to give the impression of a single provider. In effect, Mr. Gillan explained that Ameritech-Illinois would evidently become the Illinois arm of SBC's National Local Strategy. Moreover, Mr. Gillan noted that NatLoCo would have the appearance of competing in Illinois, without any formal legal standing. Id. at 23, *citing* SBC/Ameritech Exhibit 1.3 (Kahan DOR), at 21 and Direct Testimony of Thomas Reiman at 25, Indiana Utility Regulatory Commission Cause No. 41255.

Mr. Gillan testified that the Joint Applicants indicate that they have no intention to treat NatLoCo like any other CLEC. Mr. Gillan noted that NatLoCo will not operate as a CLEC in Illinois at all – and, therefore, will not have to overcome the barriers that Ameritech throws in the way of legitimate entrants trying to buy network elements and/or interconnection as arm's length competitors. Instead, NatLoCo will work "cooperatively" with Ameritech-Illinois in some vague and undisclosed manner. Mr. Gillan observed that the Joint Applicants' never suggest (and, when pressed, deny) that services/facilities provided by Ameritech-Illinois to NatLoCo would be available to other CLECs in any manner. Id. at 24, *citing* SBC/Ameritech Exhibit 1.3 (Kahan DOR), at 20-21.

Mr. Gillan testified that the Company has made clear that whatever the relationship between Ameritech-Illinois and NatLoCo, it has no obligation to extend similar – much less, nondiscriminatory – treatment to other competitors. Id. at 25, *citing* SBC Ameritech Response to AT&T Request 1-20(b). Moreover, Mr. Gillan noted that general questions concerning the relationship between Ameritech-Illinois and NatLoCo were met with stonewalling by Ameritech. *See* AT&T Ex. 1.2 (Gillan DOR), at 24, Attachment 1.2.2, SBC-Ameritech's response to AT&T 1-19. Mr. Gillan testified that SBC-Ameritech's response to AT&T 1-19 is particularly important because that request essentially sought detailed answers to the same question posed by the Commission – exactly how will Ameritech-Illinois provide service to NatLoCo, and will it treat all CLECs the same? He pointed out that, even at this late date, the Joint Applicants' response to AT&T 1-19 demonstrates that they would rather deflect questions than defend their intention. Id. at 26.

Mr. Gillan testified that, aside from Ameritech-Illinois' intention to provide (some undisclosed mix of) services/facilities/marketing to NatLoCo that it will not make available to other CLECs, there is also the issue as to what NatLoCo will pay Ameritech-Illinois for these services/functions that only it can obtain. With respect to this concern, the Joint Applicants' offer vague, empty responses to pointed questions. For instance, when pressed for details regarding the governing rules on dealings between Ameritech Illinois and the NatLoCo, the Joint Applicants responded weakly

that "presumeably 47 CFR § 32.27 and § 64.901 and any other applicable affiliate rules" would govern. Id. at 26, *citing* SBC Ameritech Response to AT&T 1-20(c). Mr. Gillan was troubled by Joint Applicants response because the Joint Applicants apparently cannot now bring themselves to agree that any specific rule would unambiguously apply. Further, although the Joint Applicants assert that any cost allocation would be subject to review by this Commission, they did not cite a single Illinois rule that would be within the Commission's jurisdiction. Both rules they offer – which don't even apply to the problem at hand – are federal, and not state, rules. Id. at 28.

Mr. Gillan testified that the Joint Applicants did not directly answer the Commission's question as to "whether the National Local Subsidiary would be treated as any other CLEC would be treated in its interactions with Ameritech-Illinois." But, he pointed out, through inference and discovery the answer becomes clear -- Ameritech-Illinois will not treat NatLoCo like other CLECs. Mr. Gillan contended that although SBC tried to soften the harshness of this answer with vague references to "cost allocation and affiliate transaction rules," none of the cited rules would ensure that Ameritech-Illinois would treat NatLoCo like any other CLEC. Id. at 30.

Mr. Gillan asserted that if there is to be a NatLoCo, then it is critical that other CLECs have an opportunity to compete with it on a level playing field. This means that NatLoCo should not be allowed to create national local packages in "cooperative partnership" with its ILEC affiliates. He testified that NatLoCo, like any other CLEC, should be required to overcome the same entry barriers (such as primitive OSS and efforts to limit the availability of UNEs) that its ILEC affiliates impose on every other market participant. Id. at 31.

Mr. Gillan testified that in order to assure that Ameritech Illinois treats NatLoCo like any other CLEC it would be necessary, first, to bar NatLoCo from including, in any national bundle that it offers, any service offered by Ameritech-Illinois. Mr. Gillan asserted that the only way that Ameritech-Illinois can treat NatLoCo like other CLECs is if NatLoCo offers services in Illinois as a separate entity, and subject to rules which recognize the unique problems that arise when a CLEC is a wholly-owned affiliate of an ILEC. He explained that the key problem stems from a single, undisputed fact that must be recognized in every Commission policy that addresses Ameritech-Illinois' relationship to NatLoCo: Because these companies have the same stockholder, the price that NatLoCo pays to Ameritech-Illinois for services/facilities is irrelevant to its economic behavior. All that matters is the cost that Ameritech-Illinois incurs. Mr. Gillan explained that this means that the most important restriction that can govern Ameritech-Illinois' relationship to NatLoCo is that NatLoCo be permitted to buy from Ameritech-Illinois only those services/facilities that are: (1) available to any other CLEC, and (2) are priced at rates based on economic cost. Id. at 32.

Mr. Gillan testified that it is important that the price of any service/facility that Ameritech-Illinois provides to NatLoCo must be cost-based because NatLoCo and Ameritech-Illinois are owned by the same entity. Consequently, the price that NatLoCo

pays Ameritech-Illinois is nothing more than shifting dollars from one entity to another. Mr. Gillan explained that NatLoCo's "cost" for services/facilities purchased from Ameritech-Illinois becomes Ameritech-Illinois' revenues. When costs/revenues are consolidated to determine SBC's earnings, the transaction "nets out" with no effect on corporate profits. Id. at 32-33.

Mr. Gillan pointed out that the Joint Applicants agree that they will compete based on the combined effect on Ameritech-Illinois and NatLoCo, that it will be the consolidated return from a customer that will determine their competitive behavior. He noted that the principal implication is that the Commission must always require that whatever service/facility Ameritech-Illinois provides to NatLoCo, the facility must be priced at its forward-looking economic cost and be available to other CLECs on identical terms and conditions (including ordering and provisioning using the same OSS). Other approaches will simply fail. Id. at 33-34.

Mr. Gillan similarly noted that "allocation" rules that allegedly divide costs between Ameritech-Illinois and NatLoCo provide the illusion of protection without the effect. Moreover, he found this approach is even more troubling because it implies both that the transaction is not cost-based and the service/facility will not be available to other CLECs. Mr. Gillan also asserted that the Commission must prohibit NatLoCo from simply "reselling" Ameritech-Illinois' services because service-resale is inherently discriminatory and favors an affiliate of an ILEC such as NatLoCo. Id. at 34-35.

Mr. Gillan testified that service-resale by an ILEC's affiliate uniquely advantages the affiliate and is inherently discriminatory. He explained that a wholly-owned affiliate like NatLoCo is able to use resale within the franchise of its affiliated ILEC because none of the financial and market constraints that would affect a legitimate entrant apply. Id. at 35.

For instance, Mr. Gillan explained that under service resale, Ameritech-Illinois would continue to receive access revenues for each of NatLoCo's customers. In effect, NatLoCo would be nothing more than an uncompensated marketing agent for Ameritech-Illinois' access service. Mr. Gillan noted that while this relationship would be acceptable to NatLoCo, no independent CLEC could succeed in such a role. Mr. Gillan pointed out that access revenues would figure prominently in the consolidated return enjoyed by NatLoCo and Ameritech-Illinois, but would figure just as prominently as an actual cost for any CLEC that provided both local and long distance service. Id. at 35-36.

Furthermore, Mr. Gillan pointed out that the defining constraint of resale is that the CLEC-reseller can only offer services that are identical to those of the incumbent. This limitation, however, could actually work to NatLoCo's advantage. He explained that far from being concerned with an inability to establish a unique product, NatLoCo would want customers to perceive it as the incumbent – the goal would be to trade Ameritech-Illinois' monopoly legacy and reputation. Because of the inherent limitations

of service resale, virtually every major carrier that has tried to compete using service resale -- at least, every unaffiliated carrier -- has terminated its resale activity. Id. at 36.

Mr. Gillan emphasized that competition would be harmed if SBC were allowed to bundle monopoly and competitive services across its vast post-merger footprint – a footprint that no other carrier comes close to replicating. He explained that whether the harm is achieved by bundling NatLoCo's services with those of Ameritech-Illinois – or by NatLoCo reselling the same Ameritech-Illinois service – the result would be a crowding out of legitimate competitors that have no base of incumbent customers to leverage. Id. at 36.

The GCI Parties' Position

GCI contends that Joint Applicants have not been responsive to the Commission's question because they have failed to specifically address the impact of the National Local Strategy on retail rates. GCI witness Dr. Selwyn argues that the Strategy will have an adverse impact on Illinois retail rates because it will require a national pricing structure, including volume and incentive discounts, and such discounts would be granted by sacrificing revenues in Illinois. Dr. Selwyn asserts that Joint Applicants have already admitted that they will finance the National-Local Strategy with revenues from core local services. GCI contends that Joint Applicants would finance the Strategy and make-up for lost core revenues by either seeking to modify Ameritech Illinois alternative regulation plan (*e.g.*, by eliminating or reducing the X factor), or by declaring services to be competitive and immediately increasing prices, even when there is no actual competition. GCI claims that Ameritech has employed the latter strategy in both Illinois and Indiana in the past.

Joint Applicants' Reply Response

In response to Staff's concerns about the length of the period until the National-Local Subsidiary would seek certification as a CLEC in Illinois, Joint Applicants agree not to seek CLEC entry in Illinois until January 1, 2003, a two-year extension from their initial proposal. Mr. Kahan's rebuttal testimony also provided detail on the operation of the National-Local Subsidiary, which will obtain local services from Ameritech Illinois' tariffs and be subject to all applicable state and federal affiliate-transaction rules. Mr. Kahan added that the operation of the National-Local Subsidiary will have no adverse impact on retail rates in Illinois.

Regarding Staff witness Graves's concerns about the impact on Ameritech Illinois' costs and revenues of moving customers off the Ameritech Illinois network, Joint Applicants explained that customers of the National-Local subsidiary would continue to use Ameritech Illinois' network – unlike customers stripped away by CLECs using their own facilities. Joint Applicants added that because network costs are driven far more by actual usage than by who retails the traffic, Illinois customers will benefit from an arrangement that will help ensure that traffic will be carried on Ameritech Illinois' network.

With regard to AT&T's request that the National-Local Subsidiary be treated as a CLEC, Joint Applicants contend that this will occur when the Subsidiary becomes a certified CLEC, but until that time it will provision service in Illinois through a subcontracting arrangement. Joint Applicants also note that AT&T's proposal is at odds with Staff's desire to delay the Subsidiary's operation as a CLEC, and that they believe the commitment not to seek CLEC certification until January 1, 2003 strikes a balance between these positions. In addition, Joint Applicants argue, AT&T's proposal does not actually treat the National-Local Subsidiary as a CLEC because it would bar the Subsidiary from reselling Ameritech Illinois' service. Joint Applicants could not agree to AT&T's suggestion to take away an entirely lawful means of CLEC entry from the National-Local Subsidiary, and expressed doubt that such a restriction would be legal.

As for AT&T's suggestion that it would be improper for the National-Local Subsidiary to engage in joint marketing with Ameritech Illinois, Joint Applicants point out that even under the interLATA provisions of TA96, Section 272 (47 U.S.C. § 272) allows a Bell operating company ("BOC") to use a separate affiliate to market the incumbent affiliates' local exchange services if the BOC gives other carriers the same opportunity.

Turning to GCI's suggestion that the National-Local Strategy will increase local rates, Joint Applicants deny that any such impact is likely or even possible. They explain that the purpose of the National-Local Strategy is to *keep* large business customers, which will provide revenues for the entire Illinois operation and benefit ratepayers, shareholders, and employees. They also note that the National-Local Subsidiary will purchase services from Ameritech Illinois' tariff, meaning that Dr. Selwyn's alleged concern about revenue-reducing discounts is baseless; any discounts offered in Illinois will be specifically available under an approved tariff. Finally, Joint Applicants reject any claim that they could reclassify services as competitive and increase rates for these services to fund the National-Local Strategy, as that gives no credit to the Commission's enforcement authority and oversight of service classifications. Joint Applicants also refute GCI's claim that there will be less regulatory oversight if the merger is approved, stating that Dr. Selwyn's description of proceedings in Connecticut and SBC's conduct there is entirely incorrect and, in any event, irrelevant to the issues in this case.

Commission Analysis and Conclusion

The Commission finds that the proposed merger is not likely to result in any adverse retail rate impacts. Several parties are concerned that the merged company will raise retail prices in order to cover the purchase premium or to finance the National Local Strategy (the "Strategy") and other competitive ventures. The Intervenors present no credible evidence to substantiate their claim that the premium, or NLS, will place upward pressure on retail rates in Illinois. The premium is not a cash expenditure and, therefore, it will not impact the merged entity's revenues, expenses, or earnings post-merger. As such, the premium is unlikely to have any effect on prices. With respect to

the NLS, as pointed out by Joint Applicants, any money used to fund this Strategy will come from shareholder equity -- not increased rates. Furthermore, after the merger, AI will remain subject to its Plan, which was approved by this Commission in Docket 92-0448. The Plan does not permit AI to raise residential noncompetitive services rates at this time.

The Commission is aware, however, that the rate freeze on the residential basket expires in October 1999 under the Price Cap Order issued in Dockets 92-0448/93-0239. We are also aware that the five year review of the Alt Reg Plan is currently underway. Because there is a rate cap in place and until such time as this Commission votes to allow an increase, we find that imposing a rate cap in this merger review is not necessary. We note that the pending five year Alt Reg review may serve as a more appropriate forum to discuss the need for a rate cap for residential rates.

We also reject Cook County's argument that, after the merger, AI will attempt to decrease or eliminate the X-factor in the Plan in order to raise rates. In addition to finding this argument extremely speculative and unsupported by the record, we find it irrelevant. Even if AI attempted to change the X-factor, it cannot do so unilaterally, as there are protections and processes in place to cover this situation.

Several parties raise concerns about SBC's "propensity" to increase rates. They argue that SBC's conduct in California is evidence of the merged company's intention to raise prices in Illinois. They also assert that previous Illinois rate increases for reclassified services indicate a "propensity" to increase rates. The Commission finds these allegations to be speculative and largely irrelevant to the issue before us. Wwe continue to have full authority to investigate any proposed rate increases for non-competitive services. We also find that the reclassification proceedings in Illinois are irrelevant to the merger. The Plan and the operation of State law provide a mechanism to reclassify services and the Commission has the authority to investigate such reclassifications. This Commission will not reject this merger merely because of the possibility the merged company might at some future time petition to raise prices or reclassify services as competitive..

Lastly, we reject the argument that, even if rates remained the same as a result of the merger, rates would no longer be just and reasonable, in violation of Section 7-204(b)(7). As Joint Applicants point out, this argument is based on inapplicable rate-of-return principles. The purpose of price regulation is to provide AI the opportunity to earn a higher return by becoming more efficient relative to its "traditional" cost basis. Under the Plan, rates were initially set based on a traditional rate of return analysis and then altered annually through application of a price index which attempts to measure productivity, inflation and quality of service. Customers may or may not benefit annually by this approach as prices are tied to some quantities that are under control of the company (i.e., productivity and quality of service) and some that are not (i.e., inflation). Under Illinois Law, if AI found itself financially unable to continue providing service under the Plan it could petition the Commission to have the plan rescinded. Similarly, if the Commission found, upon complaint or on its own motion, the Plan no longer

furthered the goals of alternative regulation (including maintaining just and reasonable rates), it could be rescinded. 220 ILCS 5/13-506.1(e). Furthermore, as noted above, we are in the midst of a five-year review of the Plan. In these three instances, traditional costs measures may be more appropriately argued. Therefore, the Commission will operate under the assumption that rates are just and reasonable, according to the Plan, until such time as the rates are reviewed through an appropriate mechanism. Therefore, we believe that the proposed Staff conditions are appropriate. We are of the opinion and will require however, that within six months from the date of merger approval, the merged company should submit updated LRSIC, TELRIC, and shared and common cost studies. We will use these updated studies in the merged company's request for rate rebalancing, in the TELRIC investigations or other investigations as deemed appropriate.

In their responses to the Commission's questions on reopening the Joint Applicants state that the National Local Subsidiary will have no adverse impact on retail rates. (See Kahan Direct on Reopening, SBC/Ameritech Ex. 1.3 at 18-22). Joint Applicants point to price caps in place under the alternative regulation plan governing Ameritech Illinois' rates which will not allow for prices to be increased. (Id). Joint Applicants also state that under their current business plans for the National Local Subsidiary, all dealings between Ameritech Illinois and the National Local Subsidiary will be controlled by federal and state affiliate transaction rules. (Id.). Joint Applicants claim that the existence of price caps, as well as affiliate transaction rules at the federal level and in Illinois, should assure the Commission that the National Local Subsidiary will not adversely impact rates.

The Commission agrees that price caps under the Alternative Regulation Plan offer assurance that the merger will not adversely impact retail rates until such time as prices are increased with Commission approval. The Commission also agrees that state and federal affiliate transaction rules will govern the interactions between Ameritech Illinois and the National Local Subsidiary under the business plans described by the Joint Applicants. The Commission notes, however, that affiliate transaction rules for telecommunications carriers, Illinois Administrative Code Part 310, were originally issued in 1955 and last revised in 1984. Given that the existing Illinois affiliate transaction rules of this Commission were enacted before TA96 and do not account for such ILEC/CLEC relationships as the National Local Subsidiary, the Commission concludes that these affiliate transaction rules must be updated in order to adequately protect the interests of Illinois consumers after the merger. Therefore the Commission will, as a result of this merger, undertake a proceeding intended to update the relevant Code Parts of the Illinois Administrative Code governing affiliate transactions. Such an update will ensure that the affiliate transaction rules which the Joint Applicants reference in their testimony and briefs will appropriately govern the interactions of Ameritech Illinois and the National Local Subsidiary.

Joint Applicants state that under current business plans the National Local Subsidiary will not seek to provide local exchange services in Illinois. (Id.). However, as a commitment to this Commission in the event that business plans of the National Local Subsidiary are modified to offer local exchange services, the Joint Applicants

state that the National Local Subsidiary will not seek local exchange certification for their National Local Subsidiary until January 1, 2003. We conclude that Joint Applicants' commitment not to seek certification for the National Local Subsidiary as a CLEC in Illinois until 2003 offers further assurances that the creation of the National Local Subsidiary and its operations in Illinois will have no adverse impact on retail rates.

We reject AT&T's request to require the National-Local Subsidiary to operate as a CLEC right away. We also see no danger of the Subsidiary being granted excessive discounts, as it will purchase services directly from Ameritech Illinois' tariffs. Further, the affiliated transaction rules which the Commission will develop will provide adequate protections in those situations not governed by tariffs. GCI's claims regarding the funding of the Subsidiary were raised in the earlier phase of this proceeding and are not persuasive. We retain authority over requests to reclassify services as competitive, and fully intend to exercise that authority to ensure no services are misclassified.

H. Rulings pursuant to Section 7-204(c)

Section 7-204(c) of the Act states as follows:

> The Commission shall not approve a reorganization without ruling on: (i) the allocation of any savings resulting from the proposed reorganization; and (ii) whether the companies should be allowed to recover any costs incurred in accomplishing the proposed reorganization and, if so, the amount of cost eligible for recovery and how the costs will be allocated. 220 ILCS 5/7-204(c).

This particular subsection was added to Section 7-204 on December 16, 1997 by P.A. 90-561; the Electric Service Customer Choice and Rate Relief Law. Although we have approved a few reorganizations since the enactment of Section 7-204(c), the meaning of this statute was not an issue in those cases. Here for the first time we are being called upon to construe subsection (c) and determine: (1) if it is applicable in this proceeding and, if so; (2) how it should be applied.

1. Applicability of Section 7-204(c)

Joint Applicants' Position

The Joint Applicants argue that, as a matter of law and policy, Section 7-204(c) does not apply to companies operating under price regulation as opposed to those operating under rate-of-return regulation. Thus, because Ameritech Illinois operates under the Plan, they contend that Section 7-204(c) does not apply here and we should not allocate any costs or savings in any manner. (Joint Applicants' Reply Br. at 88; Joint Applicants' Init. Br. at 76-80.)

The Joint Applicants' legal argument is based on the history leading to Section 7-204(c) and on Section 7-204(c)(ii)'s reference to recovery of merger "costs." At the outset, they assert that the Commission must consider the historical context for the enactment of Section 7-204(c) and the shortcomings sought to be remedied by that provision. Marriage of Logston, 103 Ill.2d 266, 279 (1984); Arview v. Industrial Comm'n, 415 Ill. 522, 526 (1953). Specifically, they contend that Section 7-204(c) was a reaction to our decisions in the CIPSCO/Union Electric and Iowa-Illinois/MidAmerican Energy merger cases and must be interpreted in light of those decisions. (Joint Applicants' Reply Br. at 88-90.)

In the CIPSCO/Union Electric merger, the merging companies proposed a plan to allocate 65% of net merger savings to ratepayers and 35% to shareholders. (CIPSCO/Union Electric Merger Docket 95-0551, Order dated September 10, 1997 at 20). They sought approval of their plan as part of the merger docket in hopes of "provid[ing] shareholders with assurance of fair treatment of merger costs and savings prior to consummation of the merger." Id. CUB also sought approval of an allocation plan in that proceeding to give 80% of actual net savings to ratepayers and argued that the allocation of net merger savings had to be addressed in that docket because "in order to decide whether the merger is likely to benefit ratepayers, the manner in which savings are to be shared must first be determined." Id. at 16, 21. (Joint Applicants' Init. Br. at 77-78.)

The Commission, however, accepted Staff's and IIEC's argument that the ratemaking treatment of merger-related costs and savings "should not be determined outside the context of a general rate proceeding in which all elements of the utility's cost of service are examined." Id. at 31. In effect, say the Joint Applicants, the Commission concluded that making such a determination outside a rate-of-return ratemaking proceeding would run afoul of the well-established prohibition against "single-issue ratemaking" under Illinois law. (Joint Applicants' Init. Br. at 78.)

The merger of Iowa-Illinois Gas and Electric and MidAmerican Energy, Docket 94-0439, Order entered May 3, 1995 at 10, involved a similar analysis. While CUB argued that the Commission should condition its approval of that merger by requiring the utilities to guarantee future savings to ratepayers the Commission found it "premature" to decide that issue in that docket stating that "[t]he issues raised by CUB are more appropriately addressed in future rate proceedings." Id. (Joint Applicants' Init. Br. at 78.)

The Joint Applicants argue that Section 7-204(c) is a response to these decisions and is intended to carve out a specific exception to the rule against single-issue ratemaking by authorizing the Commission to address the allocation of merger-related costs and savings in the merger proceedings themselves. They further state that the rule against single-issue ratemaking applies only in the rate-of-return context. That rule prohibits the Commission from revising a rate-of-return utility's rates outside a general rate proceeding, because only in a general rate proceeding can the Commission consider all of the utility's costs and expenses and determine its revenue

requirement and return on equity. See Archer-Daniels-Midland Co. v. Commerce Comm'n, 184 Ill. 2d (1998); Citizens Utility Board v. Commerce Comm'n, 166 Ill.2d 111, 136, 651 N.E.2d 1089, 1102 (1995). They aver that concepts such as rate base, revenue requirements, and aggregate cost of service simply do not apply to utilities operating under price regulation. Rather, their prices are set according to an established price-cap index, which functions independently of the utility's cost of service, rate base, revenue requirement, or allowed return on equity. (Gebhardt Rebuttal, SBC/Am. Ex. 3.1 at 61; Gebhardt Surrebuttal, SBC/Am. Ex. 3.2 at 34; Kahan Direct, SBC/Am. Ex. 1.0 at 54; Kahan Rebuttal, SBC/Am. Ex. 1.1 at 101-02.) Consequently, because the intent of Section 7-204(c) was to carve an exception to a doctrine that applies only to rate-of-return utilities, the Joint Applicants conclude that this provision does not and cannot apply to price-cap companies like AI. (Joint Applicants' Init. Br. at 79.)

The Joint Applicants also contend that subsection (ii)'s focus on "recovery" of merger "costs" proves that Section 7-204(c) is intended to apply only to rate-of-return utilities. A rate-of-return utility determines rates based on its costs and expenses of providing service. Under standard rate-of-return principles, the costs of a merger would be recovered in the utility's rates (absent a Commission ruling to the contrary). By contrast, the cost of service is irrelevant to a utility operating under alternative regulation. After initial approval of a price-regulation plan, the utility's prices are capped and adjusted annually according to a price index formula and are wholly independent of the utility's actual costs and expenses. Illinois Bell Tel. Co. v. Commerce Comm'n, 283 Ill. App. 3d 188, 195-97 (2d Dist. 1990); Gebhardt Rebuttal, SBC/Am. Ex. 3.1 at 58-59. As the Commission has stated, "[a] fundamental objective of alternative regulation * * * is to break the traditional link between costs and prices and to substitute market forces as the primary determinant of Illinois Bell's financial success or failure." Order in Docket 96-0172 (AI 1996 Alt. Reg. Plan Filing), adopted June 26, 1996 at 5.

Thus, the Joint Applicants contend that to speak of a price-regulated utility recovering its merger-related "costs" is meaningless, as there is no opportunity for it to do so, and that Section 7-204(c) therefore cannot be read to apply to such utilities. Texaco-Cities Service Pipeline Co. v. McGaw, 182 Ill.2d 262, 270 (1998) (statutes should not be interpreted so as to render any portion meaningless or superfluous); Gebhardt Direct, SBC/Am. Ex. 3.0 at 22.

The Joint Applicants next assert that even if Section 7-204(c) could apply in this case, the Commission could, and should, fulfill its duty under that provision by deciding to review appropriate merger savings at a later date, such as in a review of the Plan after savings actually have been achieved. They contend that all merger-related savings and costs are at this point purely speculative, and that the effect of the merger on rates will and should be determined by the marketplace and other economic forces driving consolidations and expansion in the telecommunications industry. Thus, they conclude that sound regulatory policy requires that there be no arbitrary allocation of estimated merger costs or savings as part of this docket. (Joint Applicants' Init. Br. at 81.)

Under the Plan Ameritech Illinois' rates are strictly limited by a price index. Ameritech Illinois assumes the risk that it cannot recover its costs (including investment in plant). In return, AI can take full advantage of increased efficiencies and new revenues resulting from marketing and other initiatives in the form of higher earnings, and these earnings may well exceed what would otherwise be permitted under rate-of-return regulation. (Gebhardt Rebuttal, SBC/Am. Ex. 3.1 at 59-61; Joint Applicants' Init. Br. at 81-82.)

The Joint Applicants maintain that the Plan makes no distinction based on the source of efficiencies, and that the efficiencies which they hope to achieve from this merger are precisely the sort of behavior which the Plan was designed to encourage. They contend that nothing in the Commission's Order in Docket 92-0448 can be read to limit this incentive structure to only certain circumstances or certain ownership situations. Therefore, they conclude that application of a rate-of-return-based ratemaking provision such as Section 7-204(c) to this merger would defeat the goals the Commission established for AI and itself when embarking on this new method of regulation. (Harris Rebuttal, SBC/Am. Ex. 4.1 at 43-44; Joint Applicants' Init. Br. at 82.)

The Joint Applicants add that the merger will expose AI and SBC to considerable risks, because the savings, while anticipated, are not guaranteed. They state that the financial markets will exact their own retribution if the companies fail. (Harris Direct, SBC/Am. Ex. 4.0 at 14-16, 19; Gebhardt Direct, SBC/Am. Ex. 3.0 at 23.) Thus, they argue, since the Company's consumers will not be bearing any of these risks -- because noncompetitive rates will not be increased if the merger results in more costs than savings -- there is no policy basis for consumers to receive the benefits. (Gebhardt Direct, SBC/Am. Ex. 3.0 at 24; Gebhardt Rebuttal, SBC/Am. Ex. 3.1 at 65-66; Kahan Direct, SBC/Am. Ex. 1.0 at 54-55; Harris Direct, SBC/Am. Ex. 4.0 at 18-19; Harris Rebuttal, SBC/Am. Ex. 4.1 at 43-44; Illinois Public Telecommunications Ass'n v. FCC, 117 F.3d 555, 570 (D.C. Cir. 1997) (under price-cap regulation, shareholders bear "the risk of loss on . . . assets" and therefore "should recoup the benefit of increases in the value of such assets.") (Joint Applicants' Init. Br. at 82-83.)

The Joint Applicants also believe that benefits will accrue directly to AI's consumers without any regulatory intervention. Some benefits will be experienced directly and immediately (e.g., efficiency and service improvements in areas such as repair, maintenance and installation and access to SBC's research and development arm). Over the longer term, the need to respond to competitive pressure and other changes in the industry will result in greater innovation, increased speed to market, and more competitive offerings. Ultimately, they argue, the marketplace can and should determine whether savings are returned to customers in the form of lower rates or in the form of new service offerings, investment in advanced network facilities or otherwise. (Harris Rebuttal, SBC/Am. Ex. 4.1 at 48-49; Joint Applicants' Init. Br. at 83-84.)

In addition, the Joint Applicants state that applying Section 7-204(c) in this case could undermine the economics of the transaction. (Gebhardt Direct. SBC/Am. Ex. 3.0

at 23-24; Harris Direct, SBC/Am. Ex. 4.0 at 14-17.) They also contend that any sharing requirement, if adopted by other state commissions, could end up depriving the companies of 50% of the savings generated by the merger. Such a result, they argue, would discourage beneficial mergers such as this, and cannot constitute sound regulatory or competitive policy. (Gebhardt Rebuttal, SBC/Am. Ex. 3.1 at 72-73.)

Finally, the Joint Applicants point out that their approach is entirely consistent with the regulatory treatment of Ameritech Illinois' competitors engaging in similar acquisitions, such as AT&T and MCI. None of these competitors has been required to flow-through any anticipated savings or revenue enhancements to consumers, even though all of the merging companies expected savings. They argue that AI and SBC should be permitted to achieve the same synergies in the same way, without regulatory involvement. Asymmetrical treatment of competitors could skew the competitive battle significantly in favor of less efficient firms. (Harris Direct, SBC/Am. Ex. 4.0 at 20.) Such a result, they contend, would not be consistent with this Commission's pro-competitive regulatory policies. (Joint Applicants' Init. Br. at 84.)

Staff's Position

Staff asserts that Section 7-204(c) applies to AI. In its present version this statute was enacted subsequent to both Section 13-506.1, which governs alternative regulatory plans for telecommunications carriers, and the Commission's Order in Docket 92-0448, which established AI's Alt. Reg. Plan. Given these facts, Staff concludes, if the legislature had intended to exempt it or any other utility under alternative regulation from Section 7-204(c), it would have done so explicitly.

Staff further contends that, as a policy matter, Section 7-204(c) requires savings to be flowed-through to ratepayers because the Commission did not take this proposed merger — and the ensuing potential productivity gains, cost savings and revenue enhancements — into account when it approved the Plan. Staff states that the Commission formulated the components of the Plan to address the regulatory, technological and market conditions at that time. As a result, the Commission took into account activities it would carry out to make the Company more efficient or profitable under those conditions. Staff claims that in 1995, when the Alt. Reg. Order was entered, a merger was not a foreseeable change in the structure of the telecommunications industry, nor could it be categorized as a technological or regulatory change. As a result, merger-related benefits are not accounted for in the current Plan. But, Staff states, if these merger-related benefits are not accounted for in the Plan in some manner, it can no longer be presumed to produce just and reasonable rates or satisfy the requirements of Section 13-506.1, and would therefore have to be rescinded. (Marshall Rebuttal, Staff Ex. 1.01 at 5-6.)

Staff contends that several state commissions have concluded that merger benefits should be allocated to the ILECs' customers regardless of the existence of Alt. Reg. Plans. For example, in its Order approving the SBC/PacTel merger, the CPUC required Pacific Bell to refund to ratepayers 50% of the short-term and long-term

economic benefits of the merger in the amount of $248 million over five years, despite the fact that Pacific Bell is regulated pursuant to an Alt. Reg. Plan. (Yow Direct, Staff Ex. 3.00, Attachment 5.) Staff also claims that in its Order approving the SBC/SNET merger, the Department of Public Utility Control in Connecticut ("Connecticut PUC") concluded that the merger between SNET and SBC was not foreseen at the time SNET's Alt. Reg. Plan was adopted, and that it significantly altered the basis for that Plan. As a result, the Connecticut PUC decided to reopen SNET's Alt. Reg. Plan to reflect the impact of the merger on its non-competitive rates within the context of a formal review of that Plan in the future. Connecticut PUC Interim Order in Docket 98-02-20, at 48-52 (September 2, 1998). As a result, Staff contends, it is appropriate for the Commission to allocate merger-related synergies to AI's ratepayers even though it is regulated under a price cap plan. (Yow Rebuttal, Staff Ex. 3.01 at 29.)

Staff next argues that competition in Illinois could be adversely affected if merger-related savings are not allocated to AI's customers. This is because the "price-to-cost" spread in its rates could increase, thereby increasing its potential net income. Price regulation, Staff argues, can be effective at preventing cross-subsidy, cost-shifting, price discrimination, and not raising barriers to entry only if it prevents the utility from earning more than a reasonable return, and this merger endangers that premise.

Staff also claims that allowing changes to the Company's price-to-cost ratio would violate the "least-cost" service requirement set forth in Section 7-204(b)(1). Similarly, Staff contends that changes in the price-to-cost ratio would have an adverse impact on AI's retail rates, in violation of Section 7-204(b)(7). Staff says that the only way to avoid these problems is to allocate merger savings to ratepayers.

Finally, Staff contends that equity requires merger savings to be allocated. It claims that if Section 7-204(c) is not applied, AI's end users would be disadvantaged relative to the end users of telecommunications carriers under rate-of-return regulation because, unlike those customers, its customers would not share the benefits of its increased revenues and reduced costs. (Marshall Direct, Staff Ex. 1.00 at 18-19.) Staff also contends that merger savings must be allocated to ratepayers because they bear the risk of the merger leading to reduced service quality. It similarly avers that AI is an important source of the resources that SBC intends to rely upon to launch its NLS. Since AI will provide a significant amount of resources to support the NLS, Staff argues, it is only equitable that Illinois customers benefit from any merger-related revenue increases. (Yow Direct, Staff Ex. 3.00 at 33.)

In response to the Joint Applicants' argument that the reference to "costs" in Section 7-204(c)(ii) means that Section 7-204(c) can apply only to rate-of-return utilities, Staff claims that costs of service are in fact an integral part of the price cap formula because, in developing that formula, the Commission attempted to provide a proxy for changes to the Company's overall costs based on its understanding of its cost conditions at the time. Further, in its Order in the Alt. Reg. proceeding, the Commission reiterated its commitment to cost-based pricing. Moreover, Staff notes that pursuant to AI's Plan, it is not allowed to reduce the rates for services below, or further below, its

incremental costs. Staff argues that, to be consistent with the continued importance of costs in an Alt. Reg. Environment, AI must flow-through merger-related synergies to its ratepayers. (Staff Init. Br. at 119-122 and Staff Reply Br. at 107-109.)

Responding to the argument that applying Section 7-204(c) here would undermine the risk/reward regulatory trade-off of the Plan, Staff claims that because the proposed merger was not contemplated by either the Commission or AI at the time the Plan was adopted, it assumed no increased risk associated with this merger and there was no "regulatory bargain" with regard to this issue. (Marshall Rebuttal, Staff Ex. 1.01 at 8-9.) Further, in response to the Joint Applicants' reference to the Illinois Public Telecommunications Association v. FCC court case, Staff notes that this court case is irrelevant to this proceeding because the Joint Applicants fail to address the many differences between the Illinois and federal price cap mechanisms. For example, when the court case referenced by the Joint Applicants was being argued (May 13, 1997), the FCC had in place three different price cap formulae. Each contained a different X (or productivity offset) factor and two of the formulae included earnings sharing obligations. (Staff Reply Brief at 123 (citing FCC Order No. 97-157 at ¶ 10)). None of these formulae resembles Ameritech Illinois' price cap formula in Illinois. Staff notes that the FCC ultimately replaced the three formulae with a single formula containing a 6.5% productivity offset (compared to the 4.5% productivity offset in Illinois) and no earnings sharing requirement. (Id. at 123-124 (citing FCC Order No. 97-157 at ¶¶ 8 and 149)). However, there is no record evidence to support a finding that the latter formula contains similar provisions to Ameritech Illinois' price cap formula in Illinois. For example, there is no evidence to indicate that the federal price cap mechanism, similar to the Illinois price cap mechanism, allows an incumbent LEC to offer, tariff and price services outside the price cap mechanism. For these reasons, Staff concluded that the Joint Applicants' position should be rejected. (Id. at 124).

With respect to the argument that applying Section 7-204(c) may make the proposed merger less attractive to investors and shareholders, Staff argues that the Company's share of merger-related expense savings will be small and that giving it to Illinois ratepayers cannot affect the overall economics of the merger. Staff claimed that it was unable to quantify Ameritech Illinois' share of merger-related revenue enhancements because neither the magnitude of these revenue enhancements, nor Ameritech Illinois' share of these revenue enhancements was provided by the Joint Applicants. (ICC Staff Ex. 3.00 at 35). Staff contends that there has been no evidence that the sharing of merger-related benefits with California ratepayers has had a negative impact on the merger. (Yow Rebuttal, Staff Ex. 3.01 at 36.)

As for the Joint Applicants' argument that application of Section 7-204(c) likely would place pressure on other state commissions to allocate a portion of merger-related synergies to ratepayers in their states, Staff believes that such considerations are irrelevant to what the Illinois Commission should do.

Finally, in response to the Joint Applicants' argument that merger-related savings are highly speculative and may not be realized, Staff agrees that it would be

inappropriate to attempt to flow-through estimated merger-related savings to AI's customers. This is because the figures resulting from such estimates undoubtedly will either overestimate or underestimate actual savings. However, Staff states that this is no reason not to allocate merger-related savings. Instead, the Commission should, if it approves the proposed merger, condition its approval on the allocation of actual merger-related costs and savings in the manner proposed by Staff (discussed below).

Intervenors' Position

The primary Intervenors addressing Section 7-204(c) were the GCI parties (the AG, CUB, and Cook County). Cook County and CUB mirror Staff's argument that Section 7-204(c) does not contain an express exemption for companies under alternative regulation, and if the legislature had intended to include such an exemption it would have done so. The AG adopts this argument and adds a few of its own. Relying on the principle that statutes should be interpreted as a whole, the AG refers to Section 13-611(a), which, like Section 7-204(c), was part of Public Act 90-561. Section 16-111(a) provides that during the mandatory transition period to competition in electrical service, the Commission, in its orders regarding any merger of an electric utility in a case pending as of May 16, 1997, cannot "impose any condition requiring any filing for an increase, decrease, or change in, or other review of, an electric utility's rates or enforce any provision of any such order," but allows the Commission to approve an electric utility's application to implement an alternative form of regulation at any time. 220 ILCS 5/16-111(a). The AG argues that this provision indicates Section 7-204(c) is intended to apply to all merger applications and that the legislature considered utilities operating under alternative regulation.

The AG also contends that ratepayers have an equitable right to share in the benefits of the merger because they protected AI from business risks when it was a rate-of-return utility. The AG claims that it is an accepted principle of utility ratemaking law that capital gains inure to the party who bears the risk of capital loss, citing Democratic Central Committee of D.C. v. Washington Metropolitan Area Transit Comm'n, 485 F.2d 786, 806-07 (D.C. Cir. 1973).

2. Allocation Methodology and Identification of Allocable Costs and Savings

Assuming that Section 7-204(c) does apply to this proceeding, questions are raised as to (a) the meaning of the terms "savings" and "costs" under that provision; and (b) in what manner should they be allocated.

Joint Applicants' Position

(i) Meaning of "Savings" and "Costs"

There is disagreement as to the meaning of the term "savings" in Section 7-204(c)(i). Staff and the Intervenors take the position that the "savings" should be read to mean "synergies" and, thus, should include not just cost reductions but also all

"revenue enhancements" resulting from the merger. The Joint Applicants argue that this is unsound and unjustified as a matter of law and policy. Section 7-204(c)'s plain language very specifically limits the allocation of merger benefits to "savings." Words in statutes must be given their "ordinary and popularly understood meaning." Texaco-Cities Service Pipeline Co., 182 Ill. 2d at 270; People v. Skirl, 141 Ill. 2d 180, 193 (1990). The Joint Applicants state that "savings" is a word generally understood to mean a reduction in costs or expenses. For example, in Funk &Wagnall's New International Dictionary of the English Language: Comprehensive Edition (1987), the word "save" means "to keep from being spent, expended or lost; avoid the loss or waste of" and "[t]o avoid waste, become economical" (at 1120). See also Black's Law Dictionary at 1343 (6th ed. 1990) (defining "savings" as "economy in outlay; prevention of waste; something laid up or kept from being expended or lost"). (Joint Applicants' Init. Br. at 93-94.)

The Joint Applicants contend that this common meaning of "savings" is consistent with its use in regulatory proceedings before this Commission. Mr. Gebhardt testified that he has been involved personally in numerous AI rate cases and was not aware of a single instance in which the term "savings" had been applied to a revenue change. In fact, in most cases, the term "savings" had been applied even more narrowly to expense decreases, not changes in the cost of facilities that are capitalized on the Company's books. (Gebhardt Rebuttal, SBC/Am. Ex. 3.1 at 64-65; Kahan Rebuttal, SBC/Am. Ex. 1.2 at 69; Joint Applicants' Init. Br. at 94.)

As for Staff's assertion that consumers should reap all synergies (including revenue enhancements) as a matter of equity, the Joint Applicants argue that (1) Staff's opinion does not excuse the Commission from its duty to follow the plain language of the statute, and (2) ratepayers have no equitable claim to revenue enhancements. Under price regulation, consumers do not have to "share" in the form of rate increases if AI experiences decreased revenues or increased costs. Therefore, they conclude, there is no equitable claim that they should "share" in the form of rate decreases if AI experiences increased revenues or decreased costs. Staff's view simply does not comport with price regulation. Further, they state, the that ratepayers pay for the service provided by the Company gives them no "ownership rights" in those management efforts. (Harris Rebuttal, SBC/Am. Ex. 4.1 at 41.) The assets which AI owns were built using shareholder funds. (Cook County Init. Br. at 34.) Finally, it does not appear that any past merger applicants before this Commission — all of which were rate-of-return companies — have been required to flow-through 100% of savings in rate proceedings following a merger, much less 100% of revenue enhancements. (Joint Applicants' Init. Br. at 94.)

As for the meaning of "costs" in Section 7-204(c)(ii) the Joint Applicants agree with Staff that this includes all costs except one-time, investment-related shareholder costs. (Gebhardt Surrebuttal, SBC/Am. Ex. 3.2 at 39.) Of course, they state, if no allocation of "savings" is made, then there would be no allocation of costs (Gebhardt Direct, SBC/Am. Ex. 3.0 at 22.), and if costs are to be allocated, they cannot be determined until the merger actually has been implemented.

(ii) Allocation Methodology

Although the Joint Applicants do not agree that any savings should be allocated to consumers, they do agree with Staff that, if an allocation is ordered, any flow-through should be based on actual results, not projected estimates. (Yow Direct, Staff Ex. 3.00 at 37-38.) Savings are expected to be achieved in the future. However, until the merger actually is consummated, post-merger planning is completed, and the operational changes are made, the amount and timing of the actual savings are speculative. (Kahan Direct, SBC/Am. Ex. 1.0 at 54-56.) Staff recommended that rate changes be made on a yearly basis, reflecting the prior year's actual results, in the annual Alt. Reg. Plan filings. This process would continue until they are made a permanent part of the Plan through the review process contemplated in Docket 98-0252. (Yow Direct, Staff Ex. 3.00 at 26-30.) The Joint Applicants do not object to this approach. (Joint Applicants' Init. Br. at 95.)

Staff also proposed a specific plan for allocating all savings among customer groups, which was significantly modified in Staff's rebuttal testimony in response to certain issues raised by Mr. Gebhardt. (Yow Direct, Staff Ex. 3.00 at 27-30; Yow Rebuttal, Staff Ex. 3.01 at 38-43.) The Joint Applicants believe that Staff's implementation proposal, as modified, is reasonable and could be implemented. (Gebhardt Surrebuttal, SBC/Am. Ex. 3.2 at 40; Joint Applicants' Init. Br. at 95-96.)

Finally, the Joint Applicants state that if the Commission were to apply Section 7-204(c) here and if it rejected Staff's proposal to defer any allocation until actual costs and savings can be determined, the net present value of the estimated merger-related savings that could be allocated to AI is $31 million. (Kahan Direct, SBC/Am. Ex. 1.0 at 57-66; Gebhardt Direct, SBC/Am. Ex. 3.0 at 29-34). They reached this figure by determining the projected savings allocable to the regulated, non-competitive, intrastate operations of AI (the only public utility in this case). (Kahan Direct, SBC/Am. Ex. 1.0 at 57.) They used this figure because the Commission's jurisdiction does not reach beyond Illinois or intrastate services. The Joint Applicants also used a three-year time frame for their estimates, since by three years after the merger is consummated they would expect all of its remaining non-competitive services to be reclassified as competitive. (Id. at 58.) Ameritech Illinois' intrastate share of these merger-related savings was calculated to be $90 million. The Joint Applicants then removed the estimated costs (both expense and capital) associated with the merger, about $67 million, from the estimated merger-related savings. Finally, the Joint Applicants utilized a discount rate of 9.5% and, based on that discount rate, they calculated the net present value of the Ameritech Illinois regulated, intrastate net savings. SBC/Ameritech Ex. 1.00 at 57-66.

Staff's Position

(i) Meaning of "Savings" and "Costs"

Staff argues that "savings" in Section 7-204(c)(i) should be interpreted to include both merger-related expense savings and merger-related "revenue enhancements." (Marshall Direct, Staff Ex. 1.00 at 19-20.) First, Staff contends that any other interpretation of "savings" would discriminate unreasonably in favor of AI at the expense of all other ILECs in the state. This is because under rate-of-return regulation, which is the form of regulation used for all other Illinois ILECs, both merger-related cost savings and enhanced revenues automatically would be reflected in rates following a merger. (Marshall Direct, Staff Ex. 1.00 at 19-20.) Second, it contends that merger-related revenue enhancements are akin to cost savings because, through the enhancement of revenues, they effectively would be spreading AI's shared and common costs over a larger pool of customers. (Tr. 1750.) Third, Staff believes that Joint Applicants' interpretation of savings would deprive its customers of a significant portion of merger-related benefits. Had the merger occurred at the time the Plan was developed, Staff opines, the Commission would have taken revenue enhancements into account both in the rate-of-return analysis as well as in some of the components in the price cap formula, such as the productivity offset and the consumer dividend. Staff contends that excluding merger-related revenue enhancements from the definition of savings in this case would violate the "just and reasonable" requirements of Section 13-506.1 and also would violate Sections 7-204(b)(1) and (7).

Regarding the Joint Applicants' reference to the standard dictionary definition of the term "savings," Staff notes that it does not disagree with that standard definition. Staff however, disagrees with the Joint Applicants' further limitation of the general term "savings" to mean "expense" savings. Staff argues that, the term "savings" is a noun that can be further specified by adding an adjective but that in the case of Section 7-204(c), the General Assembly did not modify the noun "savings" with an adjective. In fact, Section 7-204(c) discusses not only the allocation of "savings" but "any savings" resulting from the proposed reorganization. Accordingly to Staff, the Joint Applicants are attempting to have the Commission read a limitation into Section 7-204(c) which does not exist and as stated previously herein, "the court may not depart from the plain language and meaning of the statute by reading into it exceptions, limitations, or conditions that the legislature did not express." City of Chicago v. Illinois Commerce Commission, 233 Ill.App.3d 992, 999, 599 N.E.2d 991, 995 (Ill.App. 1 Dist. 1992). (Staff Reply Brief at 116).

Staff further adds that the Joint Applicants have consistently touted the fact that the proposed merger will allow the merged entity to achieve operational efficiencies because it will spread the fixed cost of offering service over a larger customer base and the Joint Applicants reiterate those specific claims in their Initial Brief. Joint Applicants' Init. Brief at 31. Staff argues that in stimulating demand for Ameritech Illinois' services following the merger, the merged entity would also be spreading Ameritech Illinois' shared and common costs over a larger pool of customers. Tr. 1750. There is no reason to conclude that spreading costs over new customers is any less a form of "savings" than savings achieved by spreading costs over an existing customer base. (Id. at 117).

With respect to the Joint Applicants' argument that requiring Ameritech Illinois to allocate merger-related expense savings and revenue enhancements to its ratepayers would subject it to disparate treatment from prior merger applicants, Staff provides the following response. Staff notes that in prior merger proceedings, the Commission has required the allocation of merger-related expense savings and revenue enhancements to the utility's customers. Staff cited the CIPS/UE merger and the GTE/Contel merger to support its position. (Id. at 127-129).

Staff argues that "costs" in Section 7-204(c) excludes one-time merger-related costs, such as banker or brokerage fees, legal fees, accounting fees, and proxy costs. These costs relate to the change in ownership of Ameritech and are thus, Staff argues, not related to the AI provision of service. Therefore, Staff believes that no portion of these costs should be borne by Illinois ratepayers. (Marshall Direct, Staff Ex. 1.00 at 21-22.)

Staff does agree, however, that other costs associated with the operations of the merged entity should be recovered from ratepayers. An example of this is the additional cost associated with increased staffing levels anticipated after the merger. (Marshall Direct, Staff Ex. 1.00 at 22.) Staff states that the Commission should allow recovery of the reasonable costs that are directly associated with utility operations. (Marshall Rebuttal, Staff Ex. 1.01 at 10.) Staff closes by noting that the Commission must determine the reasonableness and allowable recovery mechanism of costs when actual data are available.

(ii) Allocation Methodology

As an initial matter, Staff contends that Section 7-204(c) does not require that merger-related savings be netted against any recoverable costs. Rather, Staff believes the Commission must make independent rulings on both savings and costs. (Marshall Direct, Staff Ex. 1.00 at 19-20.)

Staff also contends that the Commission must focus on actual rather than estimated savings and costs, and that such actual figures will not be available for some time. Accordingly, it states that the Commission should order actual savings to be reflected in AI's annual price cap filing as they are achieved. In the Commission's five-year review of the Plan, it then can adopt or adjust the necessary mechanisms to incorporate merger savings. Until that time, Staff states, the Commission should adopt an interim method to ensure that prices under the Plan remain just and reasonable.

Regarding this interim method, Staff recommends that the Joint Applicants be required to track all actual merger-related savings, which should then be allocated to AI based on the Illinois jurisdictional factor for each Uniform System of Accounts ("USOA") category of costs where savings are being achieved. (Marshall Direct, Staff Ex. 1.00 at 20.) Although the Joint Applicants have contended that no breakdown of cost savings by USOA account currently is available, Staff believes that actual cost savings will be identifiable by account as these savings are realized. (Id.) This information would be

provided in the Company's annual price cap filings until an updated price cap formula has been developed in Docket 98-0252. It is Staff's expectation that the updated formula would reflect merger-related savings in some manner, and as a result, this interim method no longer would be needed. In those annual price cap filings, Ameritech Illinois then would be required to flow-through merger-related savings in the manner described below. Staff notes that this allocation would occur in addition to the rate changes typically required by a price cap formula.

Staff proposes that merger-related savings be allocated to Ameritech Illinois' customers in the following manner:

1. Carriers purchasing Ameritech Illinois' UNEs, interconnection, and transport and termination services would benefit from merger-related savings through updated rates resulting from Ameritech Illinois' modification of its TELRIC, shared and common costs. (Yow Rebuttal, Staff Ex. 3.01 at 42-43.)

2. Once the share of the merger-related savings allocable to UNE, interconnection, transport and termination purchasers have been identified, the remaining amount of savings would be allocated to Ameritech Illinois' interexchange, wholesale and retail customers. This would be done by dividing the remaining merger-related savings between interexchange carriers on the one hand and Ameritech Illinois' end users (whether served via retail or wholesale) on the other hand, based on the relative gross revenues of each of these two groups. (Id.)

IXCs' share of merger-related savings would be allocated to those customers through reductions in access charges, including the intrastate PICC. End users' share of merger-related savings would be allocated as a credit on a per network access line basis rather than on a gross revenues basis, to ensure that business customers do not receive a larger portion of the merger-related savings than residential customers.

Intervenors' Positions

(i) Meaning of "Savings" and "Costs"

The Intervenors (primarily the GCI parties) which address this issue adopt Staff's view that the term "savings" includes not just cost reductions but also all "revenue enhancements" (which they refer to collectively as "synergies") resulting from the merger, including all benefits that SBC could not have achieved without the merger, regardless of where in SBC's territory those benefits are achieved. The Intervenors do not address the meaning of "costs" in any detail (except to limit recovery to costs allocable to Illinois), although GCI appears to agree with the Joint Applicants that costs must be netted against savings. (Selwyn Direct, GCI Ex. 1.0 at 76-77.)

(ii) Allocation Methodology

The GCI parties support Staff's methodology for allocating savings and costs to ratepayers. (Cook County Init. Bt. at 48-49, 55.) They disagree with Staff, however, regarding when and how to determine the amount of savings to be allocated. Specifically, GCI relied on estimated figures rather than actual figures and determined synergies based on the "premium" SBC is paying for Ameritech.

Under GCI's approach, the starting point for determining merger synergies is the premium plus the anticipated increase in SBC share value from the transaction. According to GCI, the sum of these figures is $15.4 billion ($13.2 billion purchase premium plus $2.3 billion increased value of SBC shares). GCI viewed this premium-based approach as being appropriate because it reflects SBC's best estimate of the benefits it expects to achieve from the merger and was the result of arm's-length negotiation between sophisticated companies.

GCI then multiplied $15.4 billion by the following ratio:

[11] Merger gains specifically associated with [12] Illinois Bell intrastate noncompetitive services [13] divided by Total merger gains inuring to Ameritech.

GCI believes that this ratio represents the share of aggregate merger synergies allocable to Ameritech Illinois' intrastate noncompetitive services, and thus allocable to ratepayers. This ratio, which was determined to be 8.77%, multiplied by $15.4 billion, resulted in GCI finding $1.4 billion in synergies allocable to Illinois customers.

GCI proposed that the entire $1.4 billion be flowed-through over a ten-year period. Applying a 9.5% discount rate, GCI found annual, after-tax synergies of $216 million. Adjusting this to a pre-tax basis, Dr. Selwyn derived a figure of $343 million, which he said should be the annual rate reduction throughout the ten-year period.

In the event the Commission rejects GCI's methodology, Cook County recommended a "modified version of Staff's proposal." (Cook County Init. Br. at 54-55.) Under this approach, the Commission would flow-through the estimated savings under GCI's methodology immediately , but then track the actual savings data as Staff suggests. Ratepayers then would receive the higher of estimated or actual savings.

Additional Evidence/Arguments on Reopening

At the reopening phase of this proceeding the Joint Applicants were asked to provide a more detailed explanation of certain issues related to the savings calculations they put forward during the initial term of this cause .

Question 8; Attachment A SAVINGS

. ***Provide a total and complete breakdown detailing Joint Applicants' estimates of the costs and savings associated with this merger. Explain***

the methodology and assumptions used to arrive at the estimates for overall Ameritech savings, Ameritech Illinois savings, and SBC savings. Explain how these savings are spread between the Ameritech states. Explain the methodology and assumptions used to arrive at the estimates for overall Ameritech costs, Ameritech Illinois costs, and SBC costs. Explain methodology used to calculate the total estimated costs of this merger, including a breakdown of the component figures which add up to total estimate of costs. **(Question No. 8; Attachment A, June 4, 1999 letter)**

Joint Applicants' Position

Joint Applicants continue to oppose the flow-through of merger-related savings to ratepayers via mandatory, Commission-imposed rate reductions or credits. Nevertheless, SBC states that, during due diligence, it prepared an estimate of annual recurring cost savings, and the one-time, non-recurring investment necessary to achieve those savings, that could result from the merger of SBC and Ameritech. These estimates were based upon the understanding of Ameritech and SBC operations and a general understanding of the business. SBC's estimates were based on available data – some of which were derived directly from FCC ARMIS Reports, experience gained in Pacific Bell's re-engineering efforts prior to the SBC/PTG merger, and significant experience gained in planning for and ultimately implementing the integration of SBC and PTG. SBC also used its experience to estimate the timing and ramp-up (implementation period) of savings and the investment required to achieve those savings. SBC witness Mr. Kahan explained in his Direct Testimony that merger savings at this point are "only estimates" and that the actual savings realized at Ameritech Illinois "could be lower or higher, they could be realized later than anticipated, not be realized at all or be realized in different areas than we estimate or anticipate." (SBC/Am. Ex. 1.0 at 58) Joint Applicants also emphasized that there are substantial costs incurred to obtain savings and that there are significant costs created by the other commitments made by Joint Applicants, in anticipation of the merger and those latter costs are not factored into the total present value of merger savings.

SBC estimated a three-year implementation period would be required to achieve annual recurring cost savings in the amount of $1.43 billion across the combined companies. SBC also estimated that a one-time, non-recurring investment of $1.45 billion would be necessary during the three-year implementation period to achieve the recurring cost savings. The net effect is negative savings in the first year (*i.e.*, more investment than savings), positive savings in the second year, increasing in the third year, and achieving the run-rate amount of $1.43 billion each year thereafter.

Joint Applicants state that the estimated $1.43 billion recurring cost savings includes $1.17 billion in expense savings and $0.26 billion in capital savings. In deriving the cost savings estimate, SBC broke the business functions down between Support Functions, Administrative Functions, Telephone Company Operations, Procurement Functions and Other Lines of Business.

Joint Applicants explained that areas of possible savings could arise from implementation of best practices such as the means of dispatching technicians to handle trouble reports or conducting engineering or data processing on an in-house or outsource basis. They also stated that another area of possible savings could be in the area of deployment of DSL, since SBC's TRI research arm has conducted much research in this developing area and Ameritech therefore would not have to perform such research.

The estimated $1.45 billion one-time, non-recurring investment required to achieve recurring cost savings is a cumulative estimate over the three-year implementation period. Again, SBC relied on experience from the PTG and SNET mergers to derive this estimate. In general, SBC estimated a ratio of recurring savings to non-recurring investment for each category (*e.g.*, a ratio of 50% means $1 of recurring savings requires a $0.50 one-time investment). Specifically, SBC estimated recurring savings in the Support category require a 133% one-time investment, Administration 50%, Telephone company 60%, and Procurement 25%.

The aforementioned estimates apply to a combined SBC/Ameritech. SBC only prepared estimates at the SBC and Ameritech holding company level, not on a jurisdictional basis. For purposes of the Illinois proceeding, Mr. James S. Kahan, with the help of Mr. Gebhardt, prepared similar estimates that would fall under this Commission's jurisdiction. Using the same analysis, Mr. Kahan, at 57-66 of his Direct Testimony (SBC/Am. Ex. 1.0), explained how SBC computed estimated merger savings attributable to Ameritech Illinois' regulated, intrastate services for a period of three years. Of SBC's previous categories, Mr. Kahan excluded Other Lines Of Business, which, by definition, would not be related to any regulated telephone company operations. Mr. Kahan's numbers identify only savings attributable to Ameritech Corporation and exclude savings attributable to SBC Communications Inc.

Since no synergy analyses were done on a state-specific basis, Mr. Kahan explains how each of the categories was factored by 25.3% to appropriately reduce total Ameritech Corporation numbers to Ameritech Illinois, the company whose cost savings would be subject to the Commission's analysis under 7-204(c). (*Id.* at 63).

Mr. Kahan then factored the Ameritech Illinois number to exclude interstate savings that are outside the Commission's jurisdiction (Id. at 63, Table 5), resulting in the total analysis of savings attributable to Ameritech Illinois' regulated, intrastate services (Id. at 64, Table 6). As reflected in Table 6, that savings reached approximately $90 million after three years and the investment of $67 million in costs to achieve those savings. (Id.) After subtracting the cost of achieving savings over those three years and reducing the three years of savings to its present value using a discount rate of 9.5% (*id.* at 65), the total present value of the estimated merger savings attributable to Ameritech Illinois' regulated, intrastate services in the first three years following the merger would be $31 million. Were the Commission to order a savings flow through based upon this estimate via a one time rate credit, the $31 million would have to be grossed up for taxes by a factor of 1.7. The resultant figure ($52.7 million)

represents 100% of the present value of the pretax merger net savings. Taking into account the Alternative Regulation Plan and the commitments made by the Joint Applicants in this proceeding, any allocation of such savings should be limited to no more than 25% of that amount (i.e., $13.175 million).

Staff's Position

Staff agrees with the Joint Applicants that the use of actual data is preferable since it would provide a more accurate result than the use of estimates. Moreover, in this case, SBC and Ameritech have provided only high level estimates with no detailed support. Staff witness Marshall testified that such data is much less reliable than budgeted data or forecasted data based upon a substantive business plan.

According to Staff, a conservative approach to estimating merger savings is initially dictated by the necessity of obtaining the endorsement of financial advisors and approval of shareholders. Additionally, company management would very much like to report to shareholders and the financial community that the actual savings achieved were greater than the estimated savings. On the other hand, Staff notes that in the SBC/PacTel merger, projected savings were underestimated by approximately 100%.

Staff views Ameritech Illinois as uniquely situated for the utilization of actual savings data because of the annual price adjustments that it must file in accordance with its alternative regulation plan, while rate of return regulated companies generally experience a greater regulatory lag. In the event that the Commission orders savings to be shared with ratepayers, Ameritech Illinois and Staff have agreed upon the appropriate mechanism for reflecting such savings in annual price cap filings.

Staff maintains its position that the portion of merger savings allocable to Illinois regulated operations should flow to Ameritech Illinois' customers. As Staff witness Yow previously testified, such an allocation of both enhanced revenues and merger savings would result in Illinois ratepayers receiving approximately 6% of the total anticipated merger synergies. Staff also maintains that use of actual savings is preferable to the use of estimated savings. Staff and Ameritech Illinois have agreed upon a mechanism whereby actual savings would be reflected in Ameritech Illinois' annual price adjustment filing under its alternative regulatory plan.

Staff has previously attempted to obtain detail supporting the Joint Applicants' estimate of savings requesting account specific information in data requests JRM 1.02 and JRM 1.03. The Joint Applicants responded that no data was available by USOA account level. In the re-opened case, Staff again requested supporting data in the greatest level of detail available. The Joint Applicants provided no more detailed information explaining that their estimates were done at a macroeconomic level and did not include any state specific analyses of either savings or the costs to achieve those savings. Staff tells us that the Joint Applicants have agreed to track actual costs and savings following the close of the merger. (Staff Ex. 1.02, Attachment A).

In summary, Staff maintains its position that the Commission should determine the specific types of costs that may be recovered from ratepayers and allow recovery of the reasonable costs that are directly associated with utility operations. While the Joint Applicants have not identified or quantified those costs separately in their calculation of merger synergies, such identification and quantification of specific costs is required in order for the Commission to determine the reasonableness of costs to be recovered from ratepayers. Staff believes that no cost should be netted from savings prior to a determination that such cost is reasonable and should be recovered from rate payers.

In previous matters, Staff notes that the Commission disallowed such costs as corporate aircraft, shareholder lawsuits and contingency funds and also limited the amount of severance costs that can be recovered from ratepayers in evaluating the reasonableness of merger related costs and savings. (Central Telephone Company of Illinois ("Centel"), Docket 93-0252, at. 7-14)). The Commission should also consider whether employee bonuses related solely to the closing of the merger should be recovered from ratepayers and, if so, at what amount.

Staff witness Marshall testified during re-opening that the severance plan associated with a merger is generally more generous than the severance plan absent a merger. (Marshall Direct, Staff Ex. 1.02 at 29-30). The severance plan associated with this merger is also significantly more generous than the amount (limited to no more than one years salary per employee) allowed in the Centel/Sprint merger referenced above. (Id.). For example, an Ameritech employee with 25 years of service will receive two full years salary with the second years salary grossed up for taxes in the event of a merger, but would receive a maximum of 58% of one years salary not grossed up for taxes absent a merger. (Id.). As a result, absent detailed cost information it is not possible to calculate a proposed adjustment to the costs provided by the Joint Applicants.

Staff maintains that the $31 million net present value recommended by Mr. Gebhardt should not be used to allocate merger savings to ratepayers for several reasons. First, as stated above, the use of actual data is preferable. In the event that an estimate is to be used, no net present value calculation is necessary since Ameritech adjusts its rates annually.

Staff also disagrees with the use of a three year limit on consideration of merger costs and savings based upon a premise that the market will be fully competitive within three years. Staff believes that Ameritech Illinois will still offer non-competitive services at the end of three years. Staff notes that in the event that the market does become fully competitive within the three year time frame, adoption of Staff's interim methodology will not harm Ameritech Illinois because its alternative regulation plan will cease. However, limiting consideration of costs and savings to a three-year time period will cause an adverse rate impact on customers if the market does not become fully competitive in that time frame.

In analyzing the proposed merger, the Joint Applicants calculated synergies through the year 2010 which continue to increase in each year. (Staff Exhibit 1.02, Attachment B, Proprietary). Staff believes that use of a three-year time frame is not equitable because all of the one-time costs of achieving on-going economies occur within the first three years. To the extent that these costs are determined to be reasonable, they should be amortized over the same ten-year period during which synergies are expected to be realized, absent the detailed cost information necessary to determine a reasonable recovery period for each specific type of cost.

According to Staff, the Joint Applicants oppose the use of a ten year amortization period and confuse this proposal with the annual adjustment for merger related costs and savings that the Joint Applicants and Staff have agreed to. Staff notes that the use of actual data will allow the Commission to determine the reasonableness of both the amount and the type of each cost and to set reasonable recovery periods. Staff's proposed ten year amortization of merger related costs should be made if a net present value calculation is done.

The GCI Parties' Position

GCI witness Dr. Selwyn testified on the savings issue. Dr. Selwyn asserted that Joint Applicants, by sticking to their original position, have failed to respond to the Commission's request in adequate detail. He further asserted that the data are available to perform a detailed calculation, and that in fact such data were used to describe the merger to shareholders when it was announced.

The remainder of Dr. Selwyn's testimony concerns his revised estimate of merger-related savings. While still applying the same methodology as in the initial stage of this case, Dr. Selwyn adjusted his computations based on an alleged error in the composite factor he had used. This error increases his projection of Illinois merger-related savings to $1.86 billion, which he proposes to flow back to ratepayers in the form of an annual $472 million rate reduction for 10 years. This flow-through could end at any time the Commission determined that effective, price-constraining competition exists in Illinois. Dr. Selwyn stated that Joint Applicants' proposed 3-year flow-through does not take account of merger savings beyond the third year, while his present-value/amortization proposal does. In the alternative, GCI proposes that 50% of $472 million present value savings be allocated to non-competitive ratepayers using Staff's distribution methodology for 10 years.

DSSA's Position

DSSA and Neighborhood Learning Network ("DSSA") argue that savings should be flowed through to ratepayers at $100 million per year for five years. This figure is derived from the same $1.4 billion overall savings figure used by the Joint Applicants as a starting point. Allocating 8.75% of this figure to Illinois (the allocator purportedly used by Joint Applicants) leaves approximately $100 million a year for Illinois. DSSA recommended that, as in the SBC/PacTel merger in California, one-third of the merger

savings should be allocated to an Illinois Community Technology Fund to address market failures that will result from the merger in "underserved" markets.

In the alternative, or in combination, at least one-half of the merger savings should be allocated as shareholder investments in programs in underserved market communities. If savings are $100 million per year, one-third of the savings would be $33 million, and the payment of $20 million would be deducted from that amount, and the remainder added to the Illinois Community Technology Fund.

Joint Applicants' Response

Joint Applicants reiterate that they do not believe any sharing of merger savings is appropriate and that any flow-through that does occur should be based on actual data. They state that the $31 million present value figure is based on the best available information, should the Commission choose to flow through via rate reductions or credits any of the estimated savings allocable to Ameritech Illinois but that such estimates should not be used at all. They also assert that, if any such flow-through of estimated savings is adopted by the Commission, a three-year recovery period is appropriate because, in their view, there will be substantial competition for Ameritech Illinois' services within three years. In addition, they contend that Ms. Marshall is wrong to reject the three-year period, because she focuses solely on the possibility of some services being "noncompetitive" after three years, thus failing to account for the fact that increased competition will drive down prices for other services to an extent that would fully return any expected merger savings to ratepayers. Joint Applicants state that any rate reduction or flow-through should be interim in nature, lasting only until the Commission can deal with the savings issue in the context of Ameritech Illinois' alternative regulation plan in Docket 98-0252.

Joint Applicants state that Staff's 10-year amortization is a throwback to rate-of-regulation, in that such amortizations are fair to the utility only when a reasonable return can be guaranteed, and there can be no such guarantee for Ameritech Illinois. They further claim that Staff's amortization proposal could lead to double-counting of savings flowed-through as part of the amortized amount and as part of the X-factor in the price regulation plan. Finally, Joint Applicants observe that Staff's 10-year amortization proposal is inconsistent with its earlier proposal in this case, which flowed through actual savings on an annual basis and which was more consistent with Staff's stated desire to use actual data. As for Ms. Marshall's (and others') criticisms of Joint Applicants for not producing more specific data, Joint Applicants state that such estimates simply do not exist and that trying to "create" more specific data would require the use of factors and estimates, a task that does not render the end result any more reliable or meaningful.

Joint Applicants contend that the DSSA recommendation is inappropriate because it allocates 100% of savings to ratepayers which is totally inconsistent with Ameritech Illinois' Alternative Regulation Plan and ignores the substantial commitments made by Joint Applicants in this proceeding. They also assert that DSSA's five-year

period is too long and that DSSA incorrectly relies on the absolute size of the savings flow-through in California after the SBC/Pactel merger, ignoring that Pactel is two and a half times larger than Ameritech Illinois.

As for Dr. Selwyn's testimony, Joint Applicants contend that he has simply reiterated his prior proposal, with one purported correction, and that all of the same flaws noted earlier in this proceeding still apply and require rejection of Dr. Selwyn's approach.

Commission Analysis and Conclusion

The interpretation of Section 7-204(c) is, in these premises, a matter of first impression for this Commission. We begin our task with the threshold question raised by the Joint Applicants as to whether this subsection even applies to the instant transaction.

The gist of the Joint Applicants' contentions is that Section 7-204(c) was meant to carve out an exception to a doctrine that pertains exclusively to rate-of-return utilities such that its provisions cannot and should not be applied to a company like AI which is presently operating under an Alt. Reg. Plan. To support their position, they refer us primarily to a historical context for the enactment of this subsection in an attempt to show it to be a legislative response to a pair of Orders the Commission entered, each involving rate-of-return utilities. Staff and several of the Intervenors maintain that there are simply no exemptions or limitations contained within the statute to disqualify AI from its clear and unambiguous provisions such that we need not look further.

It is well settled that the most reliable indicator of legislative intent is the language of a statute and when the language is clear, it will be given effect without resorting to other aids for construction. Bogseth v. Emanuel, 166 Ill.2d 507, 655 N.E.2d 888 (1995). Here, the plain language of Section 7-204(c), which does not contain any type of exemptions to its application, inevitably leads us to the conclusion that its provisions apply in this cause. Moreover, under Illinois law, it must be presumed that the General Assembly acts rationally and with full knowledge of all existing law. Gaither v. Lager, 2 Ill.2d 293, 118 N.E.2d 4 (1954). On this point we observe that at the time of the enactment of Section 7-204(c), both Section 13-506.1 (which established alternative forms of regulation for noncompetive services), as well as our Order in Docket 92-0448 (which approved Ameritech's Plan), were in existence. The statute in question, however, does not specifically exclude price-regulated companies from its provisions nor does it expressly limit its application to rate-of -return companies. On this basis, we can only assume that the subsection at issue was intended by the legislature to apply regardless of whether the company is subject to standard rate-of return regulation or a price-cap plan.

We simply cannot accept the Joint Applicants' position on this matter, for to do so, would require a rewrite of the statute adding in language which does not exist. This, however, is within the exclusive province of the General Assembly, and not the

Commission. In order to comport with our assigned responsibilities, we "shall" apply Section 7-204(c) as written, and make the rulings that the law requires.

To begin, we agree with the Joint Applicants that the term "savings" in Section 7-204(c)(i) refers to an actual reduction in costs or expenses. Undefined terms in statutes are to be given their "ordinary and popularly understood meaning." Texaco-Cities Pipeline Service Co. v. McGaw, 182 Ill. 2d 262, 270 (1998). The "ordinary and popularly understood meaning" of "savings" is a reduction in costs or expenses. See Funk & Wagnall's New International Dictionary of the English Language: Comprehensive Edition at 1120 (1987) ("save" means "to keep from being spent, expended or lost; avoid the loss of waste of" and "[t]o avoid waste, become economical"); Black's Law Dictionary at 1343 (6th ed. 1990) ("savings" means "economy in outlay; prevention of waste; something laid up or kept from being expended or lost.")) Savings does not mean generating more revenue.

Looking to the particulars of Section 7-204(c), the plain language doctrine again leads us to construe "savings" as that term is ordinarily understood, namely, a reduction in costs or expenses. Hence, the urgings of Staff and certain Intervenors that we widen the pool to include "revenue enhancements" are rejected. The mere fact that the parties themselves have consistently drawn a distinction between "expense savings" and "revenue enhancements" reaffirms our belief that "revenue "enhancements" is not what the General Assembly intended when speaking of "savings". Courts are not free either to restrict or to enlarge the plain meaning of a unambiguous statute and we also follow this pronouncement. <u>Ehredt v. Forest Hospital Inc.</u> 142 Ill. App. 3d 1009, 492 N.E.2d 532 (1st Dist. 1986).

As for the meaning of "costs", the Commission agrees with Staff that none of the one-time merger costs which relate to the change in ownership of Ameritech, such as banker or brokerage fees, legal fees, or accounting fees, constitute legitimate costs for present purposes. It is only those costs directly associated with AI's provision of service which qualify under Section 7-204(c). Hence, we agree with Staff's position to allow recovery of only those costs directly associated with the utility's operations.

Given the Commission's strong preference for dealing in matters of certainty, we believe that both the savings and the costs of this transaction as well as their reasonableness, must be determined when actual data, as opposed to estimates, are available. We further note the disparity between the result generated by the Dr. Selwyn and the estimate presented by Mr. Gebhardt, as convincing proof of the need to await actual figures. Moreover, with respect to Dr. Selwyn's savings estimate, we believe that the underlying methodology based largely on the purchase premium paid by SBC for Ameritech is not appropriate for the task. Such an analysis necessarily discounts or excludes the fact that in nearly every transaction of this type there is a multitude of factors and motives underlying both the merger decision and the size of the premium. Because the cost savings of the merger are calculations, at best, only one of the factors taken into account, they simply cannot be equated with the total premium.

Our reading of Section 7-204(c) indicates that the Commission is required to determine how the merger savings, if any, should be shared between ratepayers and stockholders. Unlike the California statute which mandates an allocation of no less than 50% of merger benefits (interpreted as savings) to ratepayers, the Illinois statute leaves the allocation decision to the Commission's discretion. We are mindful, however, that the exercise of that discretion must be guided by sound legal judgment.

We are not convinced that either the 100% allocation of savings to ratepayers urged by Staff and several of the intervenors, or the 100% allocation to shareholders proposed by the Joint Applicants is the correct ratio to be applied in these circumstances. We are led to this conclusion by the record we have reviewed thus far including both the commitments and conditions our analyses have addressed.

At this juncture, we also believe it proper to consider whether the Company is operating under standard rate-of-return or some type of alternative plan which breaks the traditional links of price and cost. We do believe that the General Assembly expected and enabled us to recognize and take account of such differences when making our rulings. Unlike the arguments we have been presented with, however, we do not consider this to be the sole determining factor on the issue of allocation.

The record shows that the Joint Applicants have made certain commitments in this proceeding which we perceive to benefit Illinois customers. By including same in the conditions section of our Order we are holding Joint Applicants to the commitments they have made, including among other things, the utilization of TRI for the benefit of Illinois disabled customers; the maintenance of Ameritech's headquarters in Chicago; the continuation of AI's historic levels of charitable contributions and community activities; and the continuation of AI's commitment to supporting economic development and education in its region. Without the Joint Applicants' agreement we would be, as CUB pointed out, without jurisdiction to impose these terms which are of benefit to the public and of substantial benefit to a certain and often unrepresented segment of the public. Certainly, an account must be taken of the expenditures necessary to meet these commitments, for each carries with it an economic cost.

We also recognize that in imposing certain conditions on our approval, we are further adding to the costs incurred in accomplishing the proposed reorganization. These conditions are seen to be beneficial to the public and warranted by our review of the record. Nevertheless, the record evidence, as cited to by both CUB and the Joint Applicants, shows that just one of our conditions, relating to the OOS problem, could cost as much as $30 million annually. It is not enough for parties to say that this could or should have been addressed anyway, because the fact remains that it has been brought to us now, and we are addressing the situation in this proceeding.

Arguably, if there were no benefits whatsoever to the public from a reorganization where traditional regulation was operative, then a 100% allocation to customers might be proper. So too, if the residential rate freeze imposed through an alternative regulation plan were to remain in effect over the next 5 years, then a 100%

allocation to shareholders would be appropriate. The situation here and the conditions we have determined reasonable to impose in this instance draw in some degree from both of these scenarios and thus, an adjustment to these ratios is warranted.

We fully agree with Staff that the Commission needs to make separate rulings on both savings and costs pursuant to Section 7-204(c) requirements. This we intend to do. However, we are not persuaded by Staff's position opposing the netting of savings and costs. To the extent that costs are incurred to produce savings and are shown to be both reasonable and directly related, we agree with the Joint Applicants that netting is appropriate. As a matter of logic, the only savings that can be experienced are net savings. Moreover, our reading of Section 7-204(c) indicates that just such a result is contemplated. We further conclude on the arguments presented, that 50% of the net merger savings allocable to AI should be allocated to consumers using Staff's distribution methodology. This strikes a fair balance considering the commitment, performance and benchmark costs which will be incurred post-merger.

In keeping with our responsibilities under Section 7-204(c) and based on the evidence of record, we direct the Joint Applicants to follow Staff's Interim Method until the appropriate mechanisms are made in the five-year review of the Plan.

To be specific, Ameritech Illinois is required to track its share of all actual merger-related savings and all merger-related costs, as herein defined, separately for the period beginning on the date that the merger is consummated and ending on March 15, 2000. AI shall submit that information as part of its annual Alt. Reg. filing on April 1, 2000. Furthermore, this information will continue to be provided in Ameritech's annual price cap filings until such time as an updated price cap formula has been developed in Docket 98-0252. In the annual price cap filings, AI is required to flow-through merger savings net of reasonable costs in the manner here described until such time as an updated price cap formula has been developed The Commission shall retain, at the Joint Applicants expense, a third party auditor, which may be a public accounting firm, to develop and establish accounting standards to assist the Commission in identifying such costs and savings and to assist the Commission in tracking and determining the amount of such costs and savings. Any such auditor shall report to and be governed by the directives of the Commission. Further, the Commission notes the difficulty of identifying and determining such costs and savings and therefore requires the Joint Applicants to retain and to continue to provide to the Commission information using the Uniform System Of Accounts for Ameritech Illinois until at least such time as an updated price cap formula has been developed in docket 98-0252.

It is the ruling of this Commission that the net merger-related savings should be allocated to Ameritech Illinois' customers as follows:

(1) Carriers purchasing AI's UNEs, interconnection, and transport and termination services will benefit from merger-related savings through updated rates resulting from modification of its TELRIC, shared and common costs.

(2) Once the share of the merger-related savings allocable to UNEs, interconnection, transport and termination purchasers have been identified, the remaining balance of savings will be allocated to interexchange, wholesale and retail customers. This will be done by dividing the remaining merger-related savings between IXCs on the one hand and end users (whether served via retail or wholesale) on the other, based on the relative gross revenues of each of these two groups.

As per Staff's recommendations, which we find to be reasonable, IXCs' share of the merger-related savings should be allocated to those customers through reductions in access charges, including the intrastate PICC. End users' share of the merger-related savings should be allocated as a credit on a per network access line basis to ensure that business customers do not receive a larger portion of the merger-related savings than residential customers.

I. The Scope of the Commission's Authority Under Section 7-204(f)

1. Statutory Construction

Section 7-204(f) deals with our authority to place conditions on approval of a reorganization, and states as follows:

> In approving any proposed reorganization pursuant to this Section the Commission may impose such terms, conditions or requirements as, in its judgment, are necessary to protect the interests of the public utility and its customers.220 ILCS 5/7-204 (f),

The primary dispute is whether the conditions, that the Commission is authorized to impose, must be related to the findings it is required to make pursuant to Section 7-204(b),

Joint Applicants' Position

The Joint Applicants argue that no conditions of the Commission's approval of the merger are necessary. They, however, do not dispute its authority to impose conditions on its approval in appropriate circumstances. They believe that the appropriate conditions exist only if the Commission finds that a condition is necessary to allow it make one or more of the findings required by Section 7-204(b)(1)-(7). Their argument rests on two main propositions. (Joint Applicants' Init. Br. at 99-100.)

First, the only test for approval of a reorganization is that found in Section 7-204(b), and Section 7-204(f) must be interpreted in that light. According to the Joint Applicants, Section 7-204(f) is intended to relieve the Commission from having to make an absolute "thumbs up or thumbs down" decision under Section 7-204(b), by allowing it to qualify its approval as necessary to meet the standards of that Section.

Second, the Joint Applicants argue that reading Section 7-204(f) in a broader fashion effectively could render Section 7-204(b) a nullity by allowing the Commission to impose any type of condition, regardless of its relevance to the approval standard. They argue that this would violate the rules of statutory construction.

The Hearing Examiners also asked the parties to address whether the Commission could impose any fines or penalties along with any conditions under Section 7-204(f). (Tr. 1799-1800.) The Joint Applicants responded that, while the Commission likely has the authority to impose such penalties if a condition is violated, there was no testimony or other record evidence to support the establishment of any such penalty as part of this docket. Rather, they argued, the Commission should rely on its existing enforcement powers to address any alleged violations if and when they occur. (Joint Applicants' Init. Br. at 100-101.)

Staff's Position

Staff asserted that conditions imposed under Section 7-204(f) do not have to relate to the findings required by Sections 7-204(b) or (c). Indeed, Staff asserted that the only requirements under Section 7-204(f) are that any condition be reasonably required to protect the interests of the public utility and/or its customers. In taking this position, Staff deviates somewhat from the precise text of Section 7-204(f), which refers to conditions being "necessary" to protect the interests of the public utility "and" its customers. Staff contends that the term "necessary" can be read to mean "reasonably required," citing Opyt's Amoco v. Village of St. Holland, 149 Ill.2d 265, 278 (1992). Similarly, Staff argued that the term "and," while usually read as conjunctive, is frequently used inaccurately in statutes and must be read as a disjunctive (and/or) if necessary to give effect to statutory intent. Watson v. House of Vision, 16 Ill. App. 3d 487, 501 (1973); Miller v. Consolidated Rail Corp., 173 Ill.2d 252, 266 (1996). Staff concludes that such a disjunctive reading of "and" is appropriate here because reorganizations often may affect public utilities and their customers in different ways.

Regarding the Commission's enforcement authority, Staff stated that the Commission's authority is generally found in Article V of the PUA. Further, Staff recommended that the Commission adopt self executing penalties to enforce any conditional approval of the proposed merger. While Staff did not recommend any specific penalties be imposed for the majority of the conditions proposed in this matter, it did make one exception. With respect to the evidence showing the persistence of the OSS>24 problem despite an assessment of penalties, Staff proposed that the existing penalty scale be increased.

Intervenors' Positions

The GCI parties argue that conditions under Section 7-204(f) need not be tied to the findings in Section 7-204(b), but rather need only relate to the public convenience or the public interest. They contend that the Commission has discretion to accomplish

any of the objectives that the General Assembly has authorized. In addition, they state that the discretionary authority granted under Section 7-204(f) is separate from, and in addition to, the mandatory findings required by Section 7-204(b). The GCI parties view Section 7-204(b) as merely setting the minimum requirements for any reorganization, and the Commission can exercise its authority to place any further conditions on the merger as it deems necessary to protect the public interest.

Commission Analysis and Conclusion

The AG, Cook County, CUB, Staff and certain other Intervenors urge us to impose conditions on the approval of the merger, and each of them has set out a number of different proposals. The Joint Applicants, on the other hand, generally argue that no conditions are warranted in this situation.

Section 7-204(f) of the Act specifically provides that in approving a proposed reorganization, the Commission may "impose such terms, conditions or requirements as, in its judgment, are necessary to protect the interests of the public utility and its customers." Our authority to impose conditions is simply beyond question. There is, however, some disagreement among the parties as to the type of conditions that we are empowered to impose.

For their part, the Joint Applicants claim that our authority to set conditions in this matter must be defined and circumscribed by the other provisions of Section 7-204. Specifically, they contend that the conditions must be limited to those necessary to make the required findings under Section 7-204 (b). Staff and Intervenors, such as the AG and CUB, argue that our authority is much broader, allowing us to impose any conditions that reasonably relate to the "public interest". We find each of these positions to be somewhat lacking.

Article VII of the Act governs Intercorporate Relations. In a Section 7-204 proceeding such as this, as well as in proceedings arising under other sections of Article VII, the Commission has been given the power of oversight to ensure "the continued financial responsibility and the ability of the utility to render its services" to the public. (See generally, People v. Phelps, 385 N,E.2d 741 (construing what is now Section 7-103 (3) of the Act), See also generally, Estate of Besinger v. Carpentersville, 630 N.E.2d 178 (2nd Dist. 1994. (protection of public utilities is for the benefit of those served by the utilities.)) Indeed, our examination of each of the particular findings we are required to make in Section 7-204 (b) and the manner of phrasing these findings shows that the General Assembly took account of the "interests of the public utility and its customers" most likely in need of protection in a detailed and comprehensive fashion.

We agree with the Joint Applicants to the extent that our conditioning authority is a means by which we can ensure, in a meaningful way, that a reorganization satisfies 7-204 (b) interests. Notably, most of the conditions we believe necessary to impose in this cause arise from our analyses of these fundamental requirements in just that way. We cannot, however, say that no interests other than those specified under subsection (b) could ever be identified and subject to our conditioning authority.

In all of Section 7-204(b) there is no language or other expression from the General Assembly, which limits the Commission from making additional findings if they are supported by the record. On this basis, we view the findings that we are specifically required to make under Section 7-204(b) to be the minimum findings. We

recognize, as indeed we must, that these findings encompass most, if not all, of the interests in need of protection. We believe as a matter of both law and common sense that additional findings based on other interests certainly can be made in Section 7-204 proceedings and when based on relevant evidence, may also constitute a reasonable and rational source for the establishment of conditions. We further note that while these findings may or may not relate "directly" to the specific findings that we are statutorily required to make, there must be a reasonable relationship to the Section 7-204(b) interests articulated by our legislature.

For example, one such interest not specifically identified in subsection (b) is that the utility be in substantial good-faith compliance with all outstanding Commission orders when seeking reorganization approval. We do believe that the subsection (b) requirements are certainly sufficient to embrace this vital and fundamental interest. Should, however, any party argue otherwise, we consider our subsection (f) authority a proper means by which to impose such a condition if and when the evidence so warrants.

Turning again to the statutory language of Section 7-204(f) as the best indicator of legislative intent, the Commission finds that the only limitation put upon our discretion is that the conditions we attach be, in our good and informed judgment, of a type necessary to protect the interests of the company and its customers consistent with the interests outlined by Section 7-204(b). We believe, that it is the evidence of record in the proceeding, relevant to the interests as outlined in Section 7-204(b), which particularly informs our judgment and sets out the scope of our discretionary authority. The exercise of that authority follows in a subsequent part of this Order.

2. Joint Applicants' New Commitments

The reopening proceeding focused, in large part, on a number of additional commitments that the Joint Applicants proposed in their Amended Application and which they supported with evidence. Many of these commitments arose from the Joint Applicant's responses to the Chairman's June 4 questions and were further refined in responses to the Chairman's June 15 follow-up questions. Staff and all of the Intervenors had an opportunity to litigate their concerns through testimony, cross examination, and argument on briefs. In this Section, we review individually each of the Joint Applicants' additional commitments, highlight our related questions and set out the evidentiary responses and arguments, to the extent provided by the parties. We follow with a discussion of the Commission's ruling as to each particular commitment.

a. Interconnection

The manner, necessary actions and timetable by which Joint Applicants would provide to CLECs in Illinois services, facilities or interconnection agreements which SBC has made available to CLECs in its other service territories; **(Question No. 2; Attachment A, letter of Chairman June 4, letter)**

Joint Applicants' Position

Joint Applicants understand this issue to involve the situation where SBC, as the incumbent LEC, provides unbundled network elements ("UNEs"), services, facilities and interconnection agreements/arrangements to CLECs in other SBC service territories. Joint Applicants propose the following commitments with respect to this issue:

1. Interconnection Commitment A

A. Applicants would commit to provide such services, facilities or interconnection agreements/arrangements to CLECs in Illinois subject to the following reasonable exceptions and conditions:

> Joint Applicants would not be required to offer UNEs, services, facilities or interconnection agreements/arrangements in Illinois which are imposed upon SBC by another state as a result of an arbitration (as opposed to a voluntary agreement);
>
> Joint Applicants would not be required to offer UNEs, services, facilities or interconnection agreements/arrangements if they are technically infeasible or if there are state legal reasons in Illinois which would make such offerings unlawful/contrary to state policy;
>
> Joint Applicants would not be required to offer UNEs, services, facilities or interconnection agreements/arrangements in Illinois at the same rates or prices as SBC makes such offerings in other SBC service territories since costs may and do vary by state, since pricing in each state reflects state pricing policies and costs;
>
> Joint Applicants would not waive any right to seek modifications to interconnection agreements which incorporate services, facilities, or interconnection arrangements if changes in applicable law or state or federal requirements change the requirements for such UNEs, services, facilities, or interconnection agreements/arrangements. Indeed, Joint Applicants would not waive their rights with respect to any changes in federal or state law that may affect any of their proposed commitments.

Although this commitment would be immediately implemented upon merger closing, Joint Applicants state that a specific timetable for gauging fulfillment of this commitment cannot be established at this time as the services, facilities and interconnection agreements "ported" into Illinois are dependent upon requests by CLECs and the fact that SBC and Ameritech have not yet engaged in joint post-merger planning and review in this area. Unless otherwise stated, commitments made by Joint Applicants are for a period not to exceed three years after closing.

2. Interconnection Commitments B, C, and D

In addition to Interconnection Commitment A above:

B. Joint Applicants would further commit that within 90 days of merger closing that they would participate in a workshop or collaborative process with Staff and CLECs to compare UNEs, services, facilities or interconnection agreements which SBC has made available to CLECs in other states and which are not currently available and desired by CLECs in Illinois. In establishing any collaborative processes, Joint Applicants expect the Commission to set strict scope and time frames consistent with the specific goals of each such process.

C. Joint Applicants would provide copies of interconnection agreements from other states to the Commission upon request, which would allow the Commission to monitor such developments.

D. Finally, while the Chairman's question involves only SBC offering UNEs, services, facilities or interconnection agreements/arrangements to CLECs, Joint Applicants would also commit that, if a CLEC affiliate of SBC/Ameritech obtains a UNE or interconnection arrangement from an incumbent LEC through arbitration initiated by the SBC/Ameritech CLEC under 47 U.S.C. § 252, then SBC/Ameritech's incumbent LECs would make available to requesting, similarly situated CLECs in their service areas, though good-faith negotiation, the same UNE or interconnection arrangement on the same terms (exclusive of price). SBC/Ameritech would be obligated to provide such UNE or interconnection arrangement(s) where it is technically feasible to do so on or in the network of SBC/Ameritech's incumbent LEC and subject to the unbundling limitations of 47 U.S.C. § 251(d)(2). The determination of whether a UNE or interconnection arrangement is technically feasible, or whether the requesting CLEC is similarly situated, would include appropriate consideration of regulatory, network, and market circumstances surrounding the request of SBC/Ameritech's CLEC and the request made of SBC/Ameritech's incumbent LEC, including but not limited to network architecture, OSS, and universal service reform. The price(s) for such UNEs or interconnection arrangements would be negotiated on a State-specific basis and, if such negotiations do not result in agreement, SBC/Ameritech's incumbent LEC would submit the pricing dispute(s), exclusive of the related terms and conditions required to be provided under this Section, to the applicable state commission for resolution under 47 U.S.C. § 252. Joint Applicants understand that if they seek and obtain UNEs, services, facilities or interconnection agreements in the capacity of a CLEC (other than by a "most favored nations" request), they would have the burden in Illinois of proving why a form of interconnection arrangement or "capability" should not be implemented in Illinois.

Joint Applicants note that Section 252(i) of the Telecommunications Act of 1996 does not contemplate automatic adoption of one state's approval of an interconnection agreement in other states. This is especially so where Ameritech Illinois is not a "party" to interconnection agreements in other SBC states. In addition, Joint Applicants assert that the Commission should not want to abdicate its responsibility to review Illinois

interconnection agreements from an Illinois perspective by automatically adopting the policies of other states.

Joint Applicants Responses to Attachment A-1.

> ***On p. 8 of Exhibit 6, Applicants "generally commit" for a period not to exceed three years (with no set timetable for implementation because no post-merger planning has occurred) to provide services, facilities or interconnection agreements/arrangements to CLECs in Illinois as have been made available in other SBC service territories. However, the Applicants subject this commitment to four conditions, which raise the following questions:***
>
> > **The Applicants except from this commitment UNEs (Unbundled Network Elements), services, facilities or interconnection agreements/ arrangements which are imposed as a result of arbitration. What reasons do the Applicants have for excepting arbitrated agreements? (Item No. 2 (a) (i); Attachment A-I; June 15, 1999 letter)**

Joint Applicants explain that the limitations included in these commitments reflect their understanding of the intended application of the Telecommunications Act of 1996 ("TA96" or "1996 Act"). They state that the framework of interconnection policies of TA96 is premised upon parties first negotiating interconnection agreements and, if that fails, arbitrating before the individual applicable state commission. 47 U.S.C. §§ 251 and 252. Joint Applicants assert that the "limitations" are a direct reflection of the differences in the law and telecommunications regulatory policies in the 50 different states and this is why, at least in part, the FCC does not conduct all interconnection arbitrations. Due to these differences, Joint Applicants believe it is not reasonable to automatically import every term and condition of an interconnection agreement into Illinois without regard to its context, source, or underlying costs, technical or network considerations that may vary from one state and one company to another. (Joint Applicants also state that they assumed for purposes of this question that it is appropriate to resolve interconnection issues in the context of this merger proceeding under 7-204. It is Joint Applicants' position that it is not appropriate to do so but that they made their commitments to address the Commission's concerns nonetheless.)

Joint Applicants acknowledge that their Commitment A is limited to terms and conditions that SBC voluntarily negotiates in its present in-region states. Joint Applicants maintain that any commitment that would impose on SBC an obligation to automatically offer in Illinois a term or condition of interconnection based on a term or condition that was ordered in another state (and to which Ameritech Illinois was not even a party) would provide undue authority to the commissions of other states and would ignore entirely the fundamental differences that may exist in underlying costs, technology, facilities, and systems. They further assert that such a requirement could present the possibility of inconsistent obligations if different state commissions come to

different resolutions on the same issues. Further, Joint Applicants note that a commitment to offer every term and condition ordered in other states would represent an obligation that no other telecommunications provider in the nation would have.

For similar reasons, Joint Applicants have excluded from Commitment D an obligation to provide in Illinois interconnection agreements that Joint Applicants' out-of-region CLEC has obtained solely by taking advantage of its Section 252(i) ("most favored nations") rights. Joint Applicants explain that opting into an existing approved interconnection agreement is a fairly standard CLEC practice used as a means of quickly entering into business before the CLEC completely evaluates its individual needs and negotiates an interconnection agreement appropriate to its business plans, and that Joint Applicants' CLEC will no doubt use this practice. Joint Applicants argue that requiring them to provide interconnection terms simply because they appear in an interconnection agreement that an affiliate of Joint Applicants executed (*e.g.*, with BellSouth in Georgia) suffers from all the flaws of requiring Joint Applicants to offer all obligations ordered by other state commissions, and would flood this State with interconnection terms that may have no bearing on this Commission's policies.

Joint Applicants explain that Commitment D also addresses the allegation of some parties that SBC is uniquely situated to negotiate superior interconnection agreements. If that allegation is true (though Joint Applicants believe it is not), CLECs in Illinois will benefit directly from SBC's ability to secure novel interconnection arrangements for its own CLEC affiliate because, as discussed, Joint Applicants have committed to offer such arrangements in Illinois. Joint Applicants explain that excluding Section 252(i) rights would not impact this benefit because SBC's ability to take advantage of most favored nations rights would have nothing to do with its ability to negotiate novel interconnection arrangements.

The "AT&T Interconnection Agreement" appears to be an integral part of SBC's 271 application in Texas. Is this interconnection agreement excepted from this commitment? (Item No. 2 (a) (ii); Attachment A-I; June 15, 1999 letter)

Joint Applicants state that the agreement in Texas would be excepted because it was an arbitrated agreement (actually, the result of two arbitration proceedings). Joint Applicants explain that, subsequent to those arbitrations and in Southwestern Bell's 271 proceeding in Texas, the Texas PUC decided to utilize the AT&T arbitrated agreement as a base agreement but also imposed additional requirements through a long and involved collaborative process of much "give and take" to produce what is called a "Proposed Interconnection Agreement" or "PIA." Southwestern Bell's willingness to accept such an agreement in Texas was in return for the Texas PUC's stated support of Southwestern Bell's 271 application before the FCC. It is not clear to SBC that if such a PIA were offered in Illinois that this Commission would support an Ameritech Illinois 271 application. In addition, as indicated, there are numerous provisions in the AT&T Interconnection Agreement and the PIA that are arbitrated requirements and as such would be excepted from Joint Applicants' current commitment. However, Joint

Applicants state that if the Commission were to find that the offering in Illinois of the so-called "PIA" from Texas would result in unconditional Commission support for Ameritech Illinois' 271 Application, Joint Applicants would be willing to offer a similar PIA in Illinois.

The Applicants except from this commitment UNEs, services, facilities or interconnection agreements/arrangements which are technically infeasible. By what process and using what standards is the Commission to resolve technically infeasible claims by the Applicants which are disputed by competitors? If a claim of technical infeasibility is made by Joint Applicants and the Commission finds otherwise, by what process is the issue definitively resolved? Please clarify. (Item No. 2 (a) (iii); Attachment A-I; June 15, 1999 letter)

Joint Applicants state that the term "technical feasibility" is a commonly used term in the industry, and that they drew the term "technical feasibility" from TA96, where it is used frequently (*e.g.*, 47 U.S.C. § 251(b)(2)(b)). Moreover, the term is defined in the FCC's rules, 47 C.F.R. §51.5, and has been used in some of this Commission's prior Orders and in Ameritech Illinois' interconnection agreements.

With regard to the specific question, Joint Applicants explain that the issue of technical "feasibility" or "infeasibility" will be addressed in the first instance in interconnection negotiations. Failing resolution in negotiations, the issue of technical infeasibility will be resolved by the Commission in the context of an arbitration or complaint case and any associated proceedings, where Joint Applicants, under FCC rules, would have to establish their position before this Commission by "clear and convincing evidence" (*see* 47 C.F.R. § 51.5) and where, like any other disputed interconnection issue, the Commission would have to reach its conclusion based upon the specific facts of the case.

What pricing methodology do the Applicants propose apply in Illinois for such UNEs, services, facilities or interconnection agreements/ arrangements? Does the Applicants' commitment contemplate the ability for CLECs to utilize an optional plan for paydown of non-recurring charges and installment payment plan for collocation and other substantial non-recurring costs incurred as a result of entering into interconnection agreements? (Item No. 2 (a) (iv); Attachment A-I, June 15, 1999 letter)

Joint Applicants state that the issue of price should be addressed in the first instance in interconnection negotiations. While Joint Applicants are free under TA96 to negotiate prices irrespective of any specific pricing rules, Joint Applicants expect that in any arbitration the Commission would apply the forward-looking pricing rules established by the FCC in its rules implementing TA96 (*see, e.g.*, 47 C.F.R. §§ 51.501-

15) and by this Commission in its TELRIC Order (Docket 96-0486). Joint Applicants have included a limitation on pricing because TA96 and the FCC rules contemplate (indeed, require) that the pricing-related requirements of the Act will be implemented and applied on a state-by-state basis, and because costs vary by state. Joint Applicants observe that this State and this Commission have expended substantial resources in constructing pricing policies applicable to UNEs in its TELRIC proceedings, and anticipate that the Commission will follow those principles.

As to Joint Applicants' commitment to utilize an optional payment plan for non-recurring charges, Joint Applicants agree to commit to the plan outlined in the Ohio merger stipulation. Assuming the overall terms of the Commission's final Order are consistent with the Ohio Stipulation, Joint Applicants would commit as follows:

> As an incentive for local residential telephone competition, Ameritech Illinois will offer a promotional 18-month installment payment option to CLECs for the payment of non-recurring charges associated with the purchase of unbundled network elements used in the provision of residential services and the resale of services used in the provision of residential services. This promotional 18-month installment option will begin on the date 30 days following the Commission's entry of a final appealable order approving the Merger and will terminate 3 years following the Merger Closing Date. No interest will be assessed on the remaining balance during the 18-month period as long as the CLEC continues to purchase the residential unbundled network element or residential resold service. In the event the CLEC does not purchase the residential unbundled network element or residential resold service for the entire 18 month payment period, any remaining non-recurring charge balance shall immediately be due and payable when the service is terminated. Unless an interconnection agreement by its terms specifies otherwise, interest at a rate of 8% per annum will be assessed on any amounts that become immediately due and payable and are not paid within 30 days of same. If a CLEC disputes its obligation to make payment when due, it will place the amount due in an escrow account earning a rate of at least 8% interest, pending a final resolution of the dispute.
>
> As an additional incentive for local residential telephone competition, Ameritech Illinois agrees to waive the Bona Fide Request ("BFR") initial processing fee associated with a BFR submitted by a CLEC for service to residential customers under the following condition: the CLEC submitting the BFR must have, for the majority of the BFR requests it has submitted to Ameritech Illinois during the preceding 12 months, completed the BFR process, including the payment of any amounts due. The BFR initial processing fee will be waived for a CLEC's first BFR following

the Merger Closing Date and for a CLEC that has not submitted a BFR during the preceding 12 months. This BFR fee waiver will be offered for a period of 3 years following the Merger Closing Date.

On p. 9 of Exhibit 6 under Commitment B, the Applicants commit to a workshop or collaborative process to compare items not available in Illinois which are available in other SBC service territories. What is the Commission's role in this process? Have the applicants made a commitment to take action with this information? What is the end goal of this process? Please clarify. **(Item No. 2 (b); Attachment A-I; June 15, 1999 letter)**

Joint Applicants state that they would hope for the active participation of Staff in every collaborative process. Staff's primary role would be that of facilitator. Indeed, based upon SBC's experience in such processes, Joint Applicants believe that the speed, efficiency, and ultimate success of a collaborative process is highly dependent upon whether a commission Staff is prepared to play an active role of "honest broker." Joint Applicants believe that the proper work product of this collaborative process would be a report from Staff summarizing the interconnection terms and conditions that would be made available and the interconnection arrangements that CLECs desired. Of the arrangements desired by CLECs, Staff would summarize those that Joint Applicants agreed to and that Joint Applicants objected to. Where Joint Applicants raised objections, Staff would state its position on the merits of Joint Applicants' objections. It is Joint Applicants' expectation that the Staff report would be leveraged by parties negotiating interconnection agreements as indicative of Staff's likely position in an arbitration proceeding. The Commission would, of course, decide the merits of the issues based on the record developed in the arbitration proceeding.

Joint Applicants did not propose a specific role in this or any other collaborative process for the Commissioners since Joint Applicants believed it would be presumptuous to do so. However, Joint Applicants invite participation of one or more Commissioners in the collaborative process, which they believe was of assistance in Texas. At the same time, Joint Applicants agree that the Commissioners are not required to take any active role in this process unless and until a Section 252 arbitration is brought before them, and state that the Section 252 process provides the Commission with ample enforcement authority to resolve disputes and decide what terms and conditions should be included in an interconnection agreement.

Additionally, Joint Applicants state that once an interconnection agreement is in place, this Commission has ample power under § 13-514 of the PUA to enforce such agreements. 220 ILCS 5/13-514. Section 13-515 provides for an expedited procedure once Ameritech Illinois has § 271 approval. However, in the interim, § 13-515 could nonetheless still be utilized, provided the complaint sets forth a separate independent basis for a violation of § 13-514, even if such alleged acts or omissions may constitute a violation under item (8) of § 13-514. 220 ILCS 5/13-515(b). Section 13-516 provides a unique penalty structure which allows the Commission to fine the carrier up to

$30,000 per day for noncompliance, which is substantially more than the standard penalties under the Act. (Dysart SDR, SBC/Am. Ex. 10.1 at 6-7.) 220 ILCS 5/13-515 and 516.

> ***On p. 9 of Exhibit 6 under Commitment C, the Applicants commit to provide to the Commission copies of interconnection agreements from other states. What Commission action did the Applicants envisage as part of this process, and is public disclosure of all interconnection agreements the contemplated goal of this commitment? If not, why not?* (Item No. 2 (c), Attachment A-I; June 15, 1999 letter)**

Joint Applicants state that the purpose of this commitment is simply to make information conveniently available to the Commission and interested parties. This commitment would provide the Commission and Staff with the ability to obtain information that might be useful to them during the collaborative process and/or thereafter to monitor Joint Applicants' continued compliance with the possible condition of offering agreements from other states in Illinois. Joint Applicants state that while the goal of this Commitment is disclosure to the Commission, the Commission could certainly expand that goal to public disclosure by establishing a repository – similar to the existing repository of in-state interconnection agreements – in this State for all of Joint Applicants' interconnection agreements so that those agreements would be available for review to all CLECs operating in this State, as well as to the public at large.

> ***On p. 9 of Exhibit 6 under Commitment C, the Applicants commit to provide to the Commission copies of interconnection agreements from other states. If "winback" marketing provisions by the ILEC are prohibited in other interconnection agreements, do the Applicants endorse their prohibition in Illinois? If prohibitions on "winback" marketing provisions are not in other interconnection agreements, should their prohibition be considered by the Commission? If so, in what manner? If not, why not?* (Item No. 2 (d), Attachment A-I; June 15, 1999 letter)**

Joint Applicants respond that they are not aware of any "winback" provisions or prohibitions in their interconnection agreements. While aspects of "winback" (a term that Joint Applicants understand to mean the attempt to "win" a customer "back" that has been "lost" to a competitor) have been addressed in arbitrations and collaborative processes involving SBC, Joint Applicants are not aware of interconnection agreement "winback" prohibitions. Joint Applicants strongly believe that "winback" is a procompetitive practice; indeed, it is the essence of competition. As such, Joint Applicants do not believe "winback" prohibitions as to either party to an interconnection agreement would be appropriate. There are numerous regulatory requirements in place to protect competition, including the appropriate use of CPNI and carrier information, etc.

***On p. 9 of Exhibit 6 under Commitment C, the Applicants state that if they obtain UNEs, services, facilities or interconnection agreements in the capacity of a CLEC, that "they would have the burden in Illinois of proving why a form of interconnection arrangement or 'capability' should not be implemented in Illinois." Please clarify this statement.* (Item No. 2 (e), Attachment A-I; June 15, 1999 letter)**

Joint Applicants respond that the presumption created by Commitment D (Commitment C is about providing copies of interconnection agreements) is that, where Joint Applicants' CLEC affiliate negotiates (or obtains via arbitration) novel interconnection terms in SBC/Ameritech's out-of-region states, Ameritech Illinois will be presumed to have to provide such arrangements to CLECs in Illinois. However, if those arrangements rely on capabilities that Ameritech Illinois does not have and therefore are technically infeasible for Ameritech Illinois to provide, Ameritech Illinois would not provide similar arrangements. If Ameritech Illinois took the position that such an arrangement was not technically feasible, it would have the burden of establishing that infeasibility to the Commission in the event of an arbitration. Joint Applicants state that technical feasibility is well defined by the FCC, which definition this Commission and telecommunications providers commonly rely upon.

***On p. 9 of Exhibit 6 under Commitment D, the Applicants commit to provide access to the interconnection agreement of their CLEC affiliate under 47 U.S.C. § 252 if such interconnection agreement is obtained through arbitration. What is the likelihood that such agreement will be obtained through arbitration? Further, if such interconnection agreement is not obtained through arbitration, does this commitment apply? Further, why would the Applicants propose that "the same terms (exclusive of price)" would apply? Does the "exclusive of price" distinction violate the Illinois Public Utilities Act or the Telecommunications Act of 1996 or this Commission's stated pro-competitive policies?* (Item No. 2 (f), Attachment A-I, June 15, 1999 letter)**

Joint Applicants respond that they cannot predict the likelihood that a CLEC affiliate may obtain an interconnection agreement via arbitration (it may also obtain such an agreement via negotiation). Joint Applicants further explain that Commitment D would apply to interconnection arrangements obtained through arbitration or through specific negotiation, and would not apply to terms that the CLEC affiliate obtained solely by exercising its most favored nations rights under Section 252(i). The purpose of this commitment is to give CLECs in Illinois the advantage of obtaining novel interconnection arrangements that SBC/Ameritech are able to obtain. Joint Applicants explain that the exclusion of any pricing terms simply recognizes that pricing in Illinois is dictated by this Commission's TELRIC rules, that costs vary by state, and that importing inconsistent provisions or policies would create unnecessary conflicts. For example, if an element costs $10 in New York and $5 in Illinois, Joint Applicants assert that it would be wrong to require the higher New York cost to be used to set prices in Illinois (or vice

versa). Joint Applicants do not believe that this exclusion would violate the PUA but, in fact, is consistent with it and the requirements of TA96. Joint Applicants nevertheless believe that maintaining the integrity of this Commission's pricing rules would advance this Commission's pro-competitive policies. Indeed, they contend that to simply adopt prices based upon different costs in different jurisdictions would not advance the Commission's policies, but rather would be unlawful.

> ***On p. 9 of Exhibit 6 under Commitment D, the Applicants commit to provide access to the interconnection agreement of their CLEC affiliate under 47 U.S.C. § 252 if such interconnection agreement is obtained through arbitration. Do the Applicants contemplate that their CLEC affiliate will utilize UNEs or resold service to provide service to customers? Are there positive or negative competitive implications for the local exchange market which underlie the use of UNEs by the Applicants' CLEC affiliate?*** **(Item No. 2 (g), Attachment A-I; June 15, 1999 letter)**

Joint Applicants state that their CLEC affiliate will utilize UNEs and resold service and any other lawful means to enter markets and provide services out of region (including utilizing its own facilities). Joint Applicants have committed not to seek local exchange certification for their CLEC affiliate in Illinois until at least January 1, 2003 but instead to "partner" with Ameritech Illinois for the provision of local exchange services to customers in this State. Joint Applicants contend that the implications of the CLEC affiliate's use of any lawful means of entry, including UNEs, is no different from the use of UNEs by any other CLEC.

> ***On p. 9 of Exhibit 6 under Commitment D, the Applicants state that their CLEC affiliate's interconnection agreement will be made available to "similarly situated" CLECs. By what process and using what standards is the Commission to determine if a CLEC is "similarly situated?"*** . **(Item No. 2 (h), Attachment A-I; June 15, 1999 letter)**

By "similarly situated" CLECs, Joint Applicants mean CLECs seeking to obtain interconnection agreements containing the same volume, term, and area of service commitments and the same terms and conditions concerning any relevant issues such as signaling requirements and interconnection arrangements as Joint Applicants' CLEC affiliate's interconnection agreement. Joint Applicants state that if there was a dispute in this regard it would come to the Commission in the form of an arbitration or complaint

> **What are the specific enforcement mechanisms which would be used by the Commission in the event of non-compliance with the commitments made by the Applicants? (Item No. 2 (i), Attachment A-I; June 15, 1999 letter)**

Joint Applicants state that Section 252 of TA96 provides the proper enforcement mechanisms for the Commission to ensure that Ameritech Illinois in fact meets Joint Applicants' commitment to provide in its interconnection agreements with CLECs in Illinois the required terms and conditions that SBC provides to its in-region CLECs and the required terms and conditions that Joint Applicants' CLEC affiliate obtains in other states. Since "non-compliance" with Commitments A and D ultimately would mean that Ameritech Illinois refused to include in an interconnection agreement an arrangement that it is required under this commitment to provide, "enforcement" can be accomplished by the Commission, as arbiter in a Section 252 arbitration, requiring Ameritech Illinois to include the arrangement as requested by the CLEC.

Joint Applicants also explain that the “porting” of “out-of-region” interconnection agreement terms and conditions depends in part on the actions of its customers/competitors in the CLEC community. Joint Applicants maintain that imposing additional penalties, such as monetary penalties, for non-compliance with these commitments would create perverse incentive structures in the negotiation of interconnection agreements and would likely have the end result of being counterproductive.

Joint Applicants stated that to the extent "non-compliance" means that Joint Applicants have failed to meet Commitments B or C by not participating in the collaborative process or providing copies of interconnection agreements to the Commission, the Commission should bear in mind first that non-compliance with Commitments B or C would not affect Joint Applicants' Commitments A or D and second that the Post Exceptions Proposed Order already has an enforcement mechanism in the form of allocating an increased percentage of savings.

Finally, Joint Applicants contend that the Commission should bear in mind that the proposed merger will not change the Commission's existing enforcement authority. Each of these commitments will be fulfilled through the direct actions of Ameritech Illinois, over which the Commission will maintain its full regulatory authority.

Staff’s Position

Staff witness Graves testified that the Joint Applicants’ commitment may increase the types of arrangements/agreements available to CLECs within Illinois. (Staff Ex. 4.02 at 17). He noted however, that it was not possible for Staff to comment on the utility of SBC’s in-region arrangements/agreements because Staff has not had the opportunity to review those agreements. (Id.)

In response to the Joint Applicants’ Commitments A through C, Staff witness Graves testified that Staff does not oppose the Joint Applicants’ position that state specific pricing should not be incorporated into Illinois. (Id. at 18). He noted that the Commission has undertaken extensive proceedings to develop the appropriate prices for UNEs and wholesale services within Illinois pursuant to the requirements of PUA and TA96. (Id.) Mr. Graves opined that it is appropriate for the Commission’s pricing

decisions to govern interconnection agreements within Illinois. (Id.) Furthermore, Mr. Graves noted that Staff supports the Joint Applicants' condition that importation must be in accordance with Illinois state law and policy. (Id.)

In addressing one of the infirmities of Commitment C, Mr. Graves noted that this commitment provides that the Joint Applicants will only provide SBC's out-of-region interconnection agreements (whether negotiated as an ILEC or a CLEC) to the Commission upon request. Amended Joint Application, Ex. 5 at 1. He viewed Commitment "C" to mean that SBC's out-of-region arrangements/agreements will not be available to CLECs in an efficient manner. (Staff Ex. 4.02 at 22). He opined that unless the Commission requests each and every one of SBC's out-of-region arrangements/agreements on an on-going basis, those arrangements/agreements will be filed across the nation, in up to 49 other state commission offices. (Id.) He noted that CLECs will have to peruse the filings in each state commission's office to determine which arrangements/agreements may be available within Illinois.

With respect to Commitment D, Mr. Graves noted that it contains exceptions which are too expansive and which eliminate a large part of the commitment's benefits. (Id. at 19). He testified that that if SBC were to negotiate arrangements/agreements with Ameritech Illinois as a CLEC, other CLECs would have the benefits of those agreements within Illinois pursuant to Section 252(i). (Id.) Mr. Grave notes that Section 252(i) allows all CLECs to opt into agreements (or portions thereof) under the same terms and conditions as the original, negotiating/arbitrating CLEC unless one of two conditions exists, namely that, unless the ILEC proves that (1) the ILEC's "costs of providing a particular interconnection, service, or element to the requesting telecommunications carrier are greater than the costs of providing it to the telecommunications carrier that originally negotiated the agreement," or (2) "the provision of a particular interconnection, service, or element to the requesting carrier is not technically feasible." 47 C.F.R. Sec. 51.809(b).

Mr. Graves testified that the Joint Applicants' exceptions to commitment "D" go beyond Section 252(i)'s exceptions allowing SBC to refuse an arrangement/agreement to a requesting CLEC in Illinois if that CLEC is not "similarly situated." (SBC-Ameritech Ex. 1.3 at 11). He notes that SBC tells the Commission that a determination of "similarly situated" shall be expansive, including (but not limited to) consideration of regulatory and market circumstances, network architecture, OSS and universal service reform. (Staff Ex. 4.02 at 20). He further notes that SBC's "similarly situated" exception clearly goes beyond any exception allowed by Section 252(i). (Id.) According to Mr. Graves, the FCC addressed and rejected allegations by incumbent carriers that Section 252(i) requires requesting CLECs to be similarly situated. FCC Local Competition Order at para. 1302, 1318. Based on this analysis, Mr. Graves reasoned that SBC's expanded exceptions means that CLECs in Illinois will not obtain the same benefits from SBC's provision within Illinois of the arrangements/agreements negotiated by SBC's CLECs out-of-region as if SBC's CLEC negotiated those same arrangements/agreements within Illinois and CLECs were able to opt into those agreements within Illinois pursuant to Section 252(i).

Mr. Graves also opined that SBC's open list of considerations for the determination of "similarly situated" carriers will provide SBC with a means of delaying CLEC adoption of arrangements/agreements within Illinois. (Id. at 20). He noted that Section 252(i) was intended to make the adoption of interconnection arrangements/agreements more efficient and expeditious by removing the need for (and thus the time associated with) negotiation and arbitration. See, FCC Local Competition Order at para. 1311, 1321. Mr. Graves testified that SBC's unilaterally mandated exemptions to Commitment "D" will necessitate CLECs to undertake lengthy dispute resolutions prior to implementation and inhibit the pro-competitive benefits that would otherwise accrue within the Illinois local exchange market if SBC had negotiated the arrangements/agreements within Illinois as a CLEC, thereby automatically making the arrangements/agreements available to all other CLECs within Illinois pursuant to Section 252(i). (Staff Ex. 4.02 at 21.)

AT&T's Position

AT&T specifically addressed Interconnection Commitments A, B and D.

AT&T witness pointed out that with respect to provisions that exist in agreements where the Joint Applicants provide service as ILECs, the Joint Applicants commit to extend these same terms (except for price) to Illinois – but only if the Joint Applicants had (1) voluntarily agreed to the provision initially, and (2) the Joint Applicants believe the provision is not otherwise contrary to state law or policy. AT&T Ex. 1.2 (Gillan DOR), at 10-11.

Mr. Gillan testified that the Commission should not expect Commitment A to improve competitive conditions in Illinois. He noted that there are two significant limitations to this commitment that render its value meaningless. Id. First, the commitment only involves provisions that SBC has voluntarily agreed to in other states. According to Mr. Graves, provisions that actually promote competition, however, are typically the result of arbitrations (either in the initial round or, if overlooked, in the second round). This "commitment" essentially leaves the CLEC in the same position as it started – relying on SBC's management (and its decisions as to what to agree to) as the initial arbiter of its opportunity for interconnection. To obtain anything else under SBC's commitment requires arbitration – but then, the CLEC could have arbitrated to begin with. Id.

Second, Mr. Gillan pointed out that SBC proposes additional interpretative limitations that are as important for their effect on the negotiation/arbitration process as they are for (whatever) their substantive definition is ultimately determined to be. Specifically, he noted that the Joint Applicants will not offer in Illinois any provision if, *in Joint Applicants' judgment,* there are state-specific reasons in Illinois which would make such offerings technically infeasible or unlawful/contrary to State policy. Id. at 12.

Mr. Gillan found it useful to reduce SBC's Interconnection Commitment A to its elemental components. First, he noted that SBC begins with only that universe of interconnection provisions that it already agrees with. SBC then reserves the right to deny an entrant in Illinois access to even this list, if it decides that a provision is inappropriate to Illinois. While the entrant has the recourse to challenge SBC's view in an arbitration proceeding, that process negates the very point of a commitment that should be designed to expedite the importation of provisions that are favorable to competition to Illinois. Id. at 13.

Mr. Gillan pointed out that if Joint Applicants had wished to design a commitment that would accelerate the process while still addressing SBC's stated concerns, they could have provided that Joint Applicants would provide CLECs in Illinois the same services, facilities or interconnection agreements/arrangements (except as to price) that any SBC ILEC affiliate has voluntarily negotiated, or has been ordered to provide under an arbitration in another state. To the extent that SBC believed that a particular provision or agreement is not technically feasible in Illinois (or would be contrary to Illinois law or policy), SBC properly would bear the burden of proving with clear and convincing evidence that it should be relieved of the inappropriate obligation. For instance, within a set time (e.g., 30 days) of the approval of any future interconnection agreement/arrangement containing a provision that SBC believes is inappropriate for Illinois, SBC could request a waiver, accompanied by any evidence or testimony in support of its contention. Absent the grant of an exemption, however, the provision should apply automatically. Furthermore, the Joint Applicants should provide the service or facility at issue during the pendency of all rehearings and appeals, instead of delaying until their final appeal is resolved. Id. at 14-15. Mr. Gillan testified that, contrary to the contentions of Joint Applicants, the Illinois Commission would not be abrogating its role to other commissions, but would simply be establishing its primary stated policy to promote local competition in Illinois. SBC would remain free to argue that a certain provision or arrangement is inappropriate, but it could not use the process to delay or impose costs on its competitors. Id. at 15.

Regarding Joint Applicants Interconnection Commitment B (i.e., to offer in Illinois only the same agreements/arrangements that SBC as a CLEC affirmatively requests in other states), Mr. Gillan testified that this commitment also contains an unreasonable limitation. Mr. Gillan noted that the Joint Applicants' proposal would not even include the agreements/arrangements that the Joint Applicants expect to use in their out-of-region entry. The Joint Applicants acknowledge that they will most likely adopt a preexisting agreement, yet they specifically exclude extending the terms to Illinois of any agreement that they obtain in this manner. Id. at 15-16.

Mr. Gillan pointed out that the most competitively significant provisions from another state will have already been arbitrated by another entrant. Mr. Gillan noted that even this self-executing caveat – a caveat that would effectively eliminate the entire universe of potential agreements that any entrant would want extended to Illinois -- is not the final limitation that SBC would place on its "commitment." He explained that SBC is not even agreeing to offer in Illinois a provision that it has uniquely requested

but, rather, is only agreeing to either offer the provision or assume the burden of proving why such a form of interconnection arrangement or "capability" should not be implemented in Illinois. Id. at 16-17.

Mr. Gillan testified that aside from technical legal questions over the "burden of proof," this "commitment" is not any different than the status quo. He noted that an entrant would raise this issue in arbitration, and that SBC would try to explain it away. There is no improvement in competitive conditions, no simplification of the request/arbitration process, and no real change in SBC's incentive to balance its out-of-region entry with an obligation to open the market here. Id. at 17.

Mr. Gillan testified that the Joint Applicants have also placed additional caveats on this "commitment." He noted that although it is difficult to be certain, it appears that in Exhibit 6 to the Amended Petition, the Joint Application added another critical limitation as to whether a provision that its obtains as a CLEC would be offered in Illinois. This limitation is a determination of whether a UNE, service or interconnection arrangement is "technically feasible" or whether the requesting CLEC is "similarly situated" and that such determination will include consideration of regulatory, network, and market circumstances surrounding the request of SBC/Ameritech's CLEC and the request made of SBC/Ameritech's incumbent LEC, including but not limited to network architecture, OSS, and universal service reform. Id. at 17-18.

Mr. Gillan pointed out that SBC never explains how either technical feasibility – or any legitimate consideration of "similarly situated" – would appropriately comprise regulatory factors, market circumstances or universal service reform. All that can be reasonably concluded from this "commitment," he noted, is that any arrangement that can successfully navigate each of these proposed filters is not likely to present much of a threat to Ameritech's continued dominance in Illinois. Id. at 18.

Mr. Gillan testified that a provision that would have more value to the competitive process would have been to require that any UNEs, services, facilities, or interconnection arrangements contained in an interconnection agreement signed by a CLEC affiliate of SBC/Ameritech with an incumbent LEC to be offered (except as to price) in Illinois. Further, he opined that other CLECs should be able to adopt this agreement using the Most Favored Nations process, as they could with any other agreement. Id. at 19.

Moreover, Mr. Gillan thought it unreasonable to exclude price-related terms on such a blanket basis. Mr. Gillan noted that although SBC legitimately points out that many cost-related factors are state-specific and, as a result, it may not be appropriate to blindly import to Illinois prices established in other jurisdictions, the validity of SBC's observation is not without limit. Mr. Gillan pointed out that although certain cost-factors are state-specific (for instance, the particular configuration of the network in a particular state), there are many cost-factors (such as the cost of network equipment) that are not. AT&T Ex. 1.2 (Gillan DOR), at 20. He stated that the important point is that while the consequence of lower input costs (i.e., lower prices) may not be portable between

states, the lower input values themselves should be. That is, he explained, as other jurisdictions update cost models to reflect more current technology prices, the Commission could require that SBC file with the Commission the lowest input values used by any Commission for comparable equipment. Id. at 20.

Sprint's Position

Sprint specifically addressed only Interconnection Commitments A and D.

Interconnection Commitment A. Sprint essentially echoes AT&T's arguments on this issue. With regard to Interconnection Commitment A, Sprint contends that only non-controversial terms and conditions will be available in Illinois, since most pro-competitive provisions purportedly will have been arbitrated. In addition, Sprint asserts that the limitations with respect to technical feasibility and price mean that this commitment will not be self-enforcing and that CLECs will still have to incur litigation costs to obtain the arrangements they desire, which they could have done anyway under TA96. The terms that CLECs want most have been arbitrated in other forms, not agreed to voluntarily. Thus, Sprint asserts that there is little advancement from the status quo.

Interconnection Commitment D. With respect to Interconnection Agreement D, Sprint argues that the limitations regarding technical feasibility and a "similarly situated" requesting CLEC prevent this commitment from being self-enforcing or doing much to change the status quo.

As to both commitments A and D, Sprint asserts that the lack of specific enforcement mechanisms is troubling. Sprint also argues that there is no reason not to import prices from other states if there is not already a price established in Illinois, and contends that such prices could be used on an interim basis pending approval of an Illinois-specific price. Finally, Sprint urges the Commission to require Joint Applicants to make the Texas Proposed Interconnection Agreement available in Illinois, contending that this represents a "best of class" agreement developed through months of negotiations with several parties, including many involved in this case.

ACI's Position

ACI proposes that Joint Applicants be required to make available to any requesting CLEC any term or conditions in any interconnection agreement that applies anywhere in their combined region, without limitation.

Covad's Position

Covad recommends that Interconnection Agreement A be revised to require Joint Applicants to make available to CLECs any and all terms and conditions from their interconnection agreements in other states, including arbitrated terms and conditions. MGC and ACI support this recommendation. Covad asserts that this will best promote

competitive entry in Illinois and that the Commission would not be abrogating its authority over interconnection agreements because it purportedly would still have the opportunity to review and approve each new agreement. Covad also asserts that SBC's arbitration with Covad in Texas demonstrates that Interconnection Commitment A is a hollow promise, in that the arbitrated terms of any agreements resulting from that proceeding would not be available to CLECs in Illinois.

Nextlink's Position

Nextlink believes that the Joint Applicants should be compelled to offer all UNEs, services, facilities and interconnection agreements/arrangements terms and conditions whether they are offered voluntarily by Joint Applicants or as a result of arbitration. Nextlink disputes that the Commission would be abrogating its authority, and in fact believes that the Commission would be asserting its authority to ensure that best practices are brought to Illinois. Nextlink is also concerned that limiting this condition only to voluntarily agreed to terms would provide Joint Applicants incentive to arbitrate all terms and conditions to preclude them from being offered in Illinois. Nextlink also believes that this condition should apply to the entire SBC/Ameritech region and not just to SBC's current incumbent service territories. Moreover, it is Nextlink's position that this condition also should apply to terms and conditions obtained by a CLEC affiliate of SBC/Ameritech from an incumbent CLEC. In the event a term or condition is found not to be technically feasible, Nextlink maintains that Joint Applicants must, pursuant to a Commission compliance proceeding, take the necessary steps to make such term or condition technically feasible in Illinois unless the Commission approves a reasonable alternative. Nextlink also maintains that penalties should apply if the Joint Applicants fail to fulfill their commitments.

Joint Applicants' Response

Interconnection Commitments A and D. Regarding the criticisms of their proposal to make terms and conditions from their incumbent LEC and CLEC interconnection agreements available in Illinois, Joint Applicants contend that other parties are overreaching. Joint Applicants state that their commitments go far beyond anything that is or could be required under TA96 and, to their knowledge, are unique in the entire industry. These commitments, they argue, were intended to and do address any concerns about SBC's unique negotiating abilities as an incumbent LEC or CLEC. They further assert that the qualifications on their commitments are perfectly reasonable, and note that the Staff generally agrees. Among other things, they explain that other states may well have different policies or concerns and that the mere fact that SBC may have lost an issue in arbitration in another state does not mean that it should be forced to surrender its arguments in Illinois. Finally, Joint Applicants state that requiring them to import arbitrated terms and conditions would, in fact, force this Commission to abrogate its authority, as such terms and conditions would have to be treated as "negotiated" upon review of the agreement, and negotiated terms and conditions are subject to less stringent standards under TA96 than are arbitrated terms

and conditions; indeed, negotiated terms and conditions do not have to comply with TA96 at all.

With regard to the claims that their commitments do little to eliminate the need for arbitration, Joint Applicants state that their commitments were intended to streamline the negotiation process to the extent possible, and in fact do so. They note that their commitments do not eliminate their duty to negotiate in good faith with requesting CLECs, and instead simply eliminate the need to negotiate at all on certain terms and conditions that are being made available from other states. Joint Applicants add that arbitration has not been a routine occurrence in SBC's states; SBC has entered approximately 500 interconnection agreements, but only 34 of those required arbitration. Thus, they contend that the other parties' concerns about litigation costs and delay are overstated. They also contend that Covad's testimony about an arbitration proceeding in Texas is entirely irrelevant to this proceeding on reopening. Moreover, cross-examination showed that testimony to be highly misleading and that the delays Covad complained of were actually caused by itself.

Interconnection Commitment C. As for Staff's concern about the statement that agreements from other states would be provided to the Commission "upon request," Mr. Kahan explained that this term was included to give the Commission flexibility in deciding whether and to what extent it wants to maintain a complete file of all of SBC's interconnection agreements, of which there are more than 500. The "upon request" language simply allows the Commission to control its level of involvement.

Commission Analysis and Conclusion

We conclude that Joint Applicants' proposed commitment, in general, is responsive to our questions; sufficiently detailed to satisfy concerns about its implementation; and subject to effective enforcement measures. We further conclude that the proposed interconnection commitment, as modified by the Commission in this Order, will have procompetitive benefits accruing to both CLECs and end-user customers in Illinois that would not exist absent the merger. Such modifications to the Joint Applicants initial proposal are necessary to further protect the interests of the public utilities' (Ameritech Illinois) customers.

As a starting point, we agree with Joint Applicants that TA96 does not require an incumbent LEC to offer "most favored nation" treatment to CLECs based on interconnection agreements that the incumbent LEC or its affiliate may have in other states. Thus, Joint Applicants' agreement to give CLECs such "most favored nation" treatment with respect to arrangements that SBC has negotiated in other states is a substantial step beyond current legal requirements. However, if the commitment allowed CLECs in Illinois to opt into a potentially much broader range of arrangements than previously was available without certain caveats, it would represent an increased benefit to the customers of Ameritech Illinois that would not exist without the merger through increased competition in the local exchange marketplace. In addition, Joint Applicants have committed to make available in Illinois certain arrangements that they

are able to obtain in their role as a CLEC. This, too, goes well beyond any current legal requirement and could represent a procompetitive benefit for Illinois that would not otherwise exist if properly formulated. One purpose of the follow-up questions in the June 15 letter was to clarify the commitments made by the Joint Applicants and obtain more detail about their implementation. We believe that Joint Applicants have provided the detail we sought. Upon being provided with this detail, however, the Commission feels that the caveats placed on the interconnection commitments by the Joint Applicants limit the effectiveness of the commitments in protecting the interests of the customers of Ameritech Illinois.

Certain parties have criticized Joint Applicants' commitment as being vague or illusory. The Commission disagrees. However, some of Joint Applicants' limitations and exceptions, while helpful, do not go far enough in protecting the interests of customers of Ameritech Illinois. For instance, if Joint Applicants had offered interim pricing, there would be a procompetitive benefit because the negotiated agreements would then not be subject to delay in their implementation in Illinois. Likewise, if the Joint Applicants commitment was clarified as to which SBC companies and affiliates are included in the commitment, this Commission would have more assurance of the procompetitive nature of the commitment. Unfortunately, this commitment does not contain these features. Therefore, this Commission adopts an interim pricing methodology to address the issue of delay due to pricing uncertainty, as well as a concise definition of which SBC companies and affiliates are included in the commitment. "SBC ILEC affiliate" includes any affiliate or subsidiary of SBC thereof upon the closing date of this merger, including, but not limited to its affiliated interests resulting from the acquisition of Ameritech Corporation, its affiliates and subsidiaries as well as any companies acquired or otherwise controlled by SBC, its affiliates or subsidiaries resulting from future transactions upon which this Commission may exert jurisdiction.

Likewise, certain terms of the proposed interconnection commitment as submitted by the Joint Applicants may generate future disputes about whether a CLEC in Illinois is "similarly situated" to the SBC CLEC. Therefore, the Commission strikes this caveat from the interconnection commitment in order to eliminate uncertainty from this commitment. However, with regards to technical infeasibility as an exception from compliance with this condition the Commission concludes that such an exception is reasonable and is not a reason to reject or modify the commitment as proffered by the Joint Applicants. Technical infeasibility is already a limitation on "most favored nation" rights (*see* 47 C.F.R. § 51.809); the only difference now is that Illinois CLECs will have a potentially much broader group of arrangements to choose from in seeking to adopt provisions from other contracts, which benefits the CLECs. These interconnection commitments, as modified by the Commission in this Order, represent a benefit to the customers of Ameritech Illinois that would not exist without the merger. If SBC believes that a particular provision or agreement is technically infeasible in Illinois, or contrary to Illinois law or policy, SBC would bear the burden of proof of same.

Regarding the concern of some parties that Interconnection Commitment D does not include terms and conditions obtained by the SBC CLEC through most-favored nation rights, we agree with Joint Applicants that importation of such terms is not necessary. The theory prompting Interconnection Commitment D is that the SBC CLEC could exercise unique bargaining power to extract unique contract terms from out-of-region incumbent LECs. The exercise of most-favored nation rights requires no bargaining power or special expertise at all; the SBC CLEC would just get the same deal as a prior CLEC. Thus, we will not expand Interconnection Commitment D beyond the specific Commitment made by Joint Applicants.

We believe that the proposed collaborative process among Joint Applicants, Staff, and other parties will help simplify the adoption of terms from out-of-state interconnection agreements and significantly aid us in resolving any disputes that may arise in specific cases. We strongly encourage the parties to work together in this process to resolve disputes short of litigation. We also will seriously consider the proposals that one or more Commissioners participate directly in the collaborative process, though we need not resolve that issue here.

Finally, it should be remembered that these commitments do not affect this Commission's authority over Ameritech Illinois. This Commission will retain its full authority to ensure compliance with each of these commitments and any other provisions of the order approving this merger.

b. Shared Transport, Question 3; Attachment A

> ***The manner, necessary actions and timetable by which Joint Applicants would provide "shared transport" as recommended by the Commission Staff in this proceeding. Further, until the "Illinois version" of shared transport is offered, when the Commission can expect the implementation of shared transport in the same manner as SBC has provided in Texas, and the manner, necessary actions and timetable by which this will be accomplished.*** **(Question No. 3; Attachment A; June 4, 1999 letter)**

Joint Applicants' Position

Joint Applicants maintain that the Supreme Court's *IUB* decision which vacated the FCC's rule establishing a shared transport UNE (Rule 319), as well as the Supreme Court's June 10, 1999 vacatur of the Eighth Circuit's affirmance of the FCC's *Third Order on Reconsideration* in CC Docket 96-98, means that Ameritech Illinois currently has no legal obligation to provide shared transport. Nevertheless, subject to the outcome of the FCC's pending UNE Remand Proceeding, Joint Applicants are willing to implement a form of shared transport within 30 days of the merger closing date in Illinois. Joint Applicants refer to this as the "interim" version. In addition, within one year of the merger closing, Joint Applicants are willing to implement and offer in Illinois the same version of shared transport (involving use of Advanced Intelligent Network ("AIN") facilities to perform a 10 digit number look-up) as SBC has implemented in

Texas. Joint Applicants refer to this as the long-term solution. Joint Applicants believe that the interim and long-term solutions fully comply with, and respond to, concerns raised by Staff and the Commission in this proceeding.

Joint Applicants state that shared transport, also generically called common transport, is a form of interoffice transport and can be provided only in combination with local switching. Joint Applicants define shared transport as a shared interoffice transmission path between Ameritech Illinois end office switches, and between Ameritech Illinois end office switches and tandems, that permits CLECs to connect the local switching element purchased from Ameritech Illinois with shared transport, to transport the local call dialed by end-users using the local switching element to its destination through the use of Ameritech Illinois' transport network. Joint Applicants state that, in order to function, Common/Shared Transport cannot be physically separated from local switching and is not offered separate and apart from local switching.

Joint Applicants' Commitment to Provide Shared Transport

Joint Applicants state that even though there is no current legal obligation under the 1996 Act to provide shared or common transport, they commit to make shared transport available – as described in their submissions – within 30 days of the merger closing date. This commitment would cease if and to the extent that, as a result of the FCC's pending UNE Remand Proceeding or any judicial review thereof, no new legal obligation to provide shared transport is imposed on ILECs. Joint Applicants assert that it would be improper to require the continued provision of shared transport if the FCC, or a court, determines that, for whatever reason, ILECs should not be required to provide shared transport. Indeed, they argue that there is no rationale by which a single entity in the industry should continue to have to comply with such an unnecessary or nullified requirement. However, the final outcome of the UNE Remand Proceeding (including any judicial review thereof) is likely to take one or more years. Consequently, Joint Applicants assert that their commitment will certainly accelerate deployment during this period of legal uncertainty.

1. Interim Solution Within 30 Days Of Merger Closing

To accelerate the availability of a shared transport offering, Joint Applicants commit to deploy an interim form of shared transport within 30 days of merger closing. Joint Applicants state that the interim solution avoids or addresses each of the technical and network issues that Ameritech Illinois identified in its TELRIC tariff filing.

Dedicated links and custom routing. Joint Applicants would not require the use of dedicated transport or custom routing to complete a call using unbundled local switching and shared transport to a third party switch. Rather, Joint Applicants would make available a modified version of transiting that does not require a dedicated end office integration (EOI) transit trunk. This is similar to the shared transport offering that SBC makes available.

Measuring terminating call detail. Ameritech Illinois states that it does not have the ability to record terminating detail based on its current network architecture. However, Joint Applicants would implement an interim solution that involves the use of originating and terminating factors and a settlement procedure with each CLEC purchasing local switching and shared transport to allocate appropriate access charge revenues. Thus, when an end-user customer, who is served by a CLEC using Ameritech Illinois' shared transport facilities, makes or receives an interLATA call, Ameritech Illinois would collect relevant access charges from the interexchange carrier and then make payment to, or receive payment from, the CLEC using local switching based on the difference between access charges and applicable charges for the UNEs used to provide the access service. Factors and settlement procedures have been widely used within the telecommunication industry in many contexts, for many years.

Identifying the originating local carrier. Ameritech Illinois states that it currently does not have the short-term ability to identify the originating local carrier terminating a call to a CLEC's local switching port. However, Joint Applicants would implement a concept known as originating carrier pays to address this limitation. Under an originating carrier pays arrangement, Ameritech Illinois would charge a CLEC using Ameritech Illinois' local switching and shared transport facilities for usage of local switching to both originate and terminate such traffic. Ameritech Illinois, however, would not charge a CLEC using Ameritech Illinois' unbundled local switching for usage at the terminating switch when it is terminating traffic delivered by shared transport facilities. Nor would Ameritech Illinois create message records for such terminating usage, since reciprocal compensation would not be eligible for collection by the terminating carrier in such circumstances. Joint Applicants contend that this approach alleviates the existing network fact that Ameritech Illinois does not have the capability to record terminating local calls. If the originating carrier pays both originating and terminating ULS, recording at the termination office for a local call is unnecessary. Joint Applicants believe that this is a reasonable interim solution which accelerates the availability of shared transport in a way that makes it operationally implementable in the immediate near term.

Providing common/shared transport on an unbundled basis. The Supreme Court has expressly reinstated the FCC's rule which required incumbent LECs to provide pre-assembled combinations of unbundled network elements, assuming each element in the combination is capable of being purchased separately. Although Ameritech Illinois maintains that shared transport is not "unbundleable" as defined by the Supreme Court, that issue will be resolved in the FCC's pending UNE Remand Proceeding. Until that issue is finally resolved, Joint Applicants would provide shared transport combined with local switching (in fact, they state, there is no other way to provide it).

Joint Applicants believe that the proposed interim solution described above should be acceptable to the Commission because: (i) it maximizes Ameritech Illinois' ability to offer shared transport quickly; (ii) it minimizes Y2K implications by avoiding any significant network or billing modifications before the end of this year; and (iii) it

provides a reasonable period of time to implement a more long-term solution that relies on a network technology and that does not require the use of factors or settlements.

2. Long-Term Solution Within One Year Of Merger Closing.

Joint Applicants explain that the major difference between Ameritech Illinois' and SBC's capabilities with regard to the "long-term" AIN-based version of shared transport relates to the type and scope of deployment of different AIN technologies. In Texas, SBC has deployed an AIN network architecture that enables SBC to use AIN triggers to identify UNE ports, which in turn enables billing of usage sensitive charges. This AIN approach eliminates the need for factors or settlements for both local and toll calling. Ameritech Illinois has represented to the Commission that it has not deployed this AIN network capability and that the cost and time to deploy such capability is significant and substantial. However, Joint Applicants commit to begin deploying shared transport in Illinois, in the same manner that SBC has deployed shared transport in the state of Texas (using AIN triggers), starting within one year of the merger closing date. Joint Applicants believe that deployment of shared transport in this manner fully complies with this Commission's TELRIC Order and the FCC's now-vacated Rule 319. Further, Joint Applicants commit that they will offer such shared transport in Illinois, under terms and conditions (other than rate structure and price) that are substantially similar to the most favorable terms offered by SBC to CLECs in Texas as of the merger closing date.

Joint Applicant's Responses to Attachment A-1 Items

> ***The positions stated by the Applicants appear to be a shift from stances originally taken on this matter. However, comments by the intervening parties in this docket will be most helpful in determining the merit of the Applicants' commitments.*** **(Item No. 3 (a); Attachment A-1; June 15, 1999 letter)**

Joint Applicants respectfully disagree with the Chairman that they have shifted their stance on this matter. Joint Applicants state that they have consistently maintained that the "Illinois version" of shared transport, *i.e.*, shared transport physically unbundled from switching, is not technically feasible (or even physically possible). When SBC General Counsel Jim Ellis appeared before this Commission, he committed on behalf of Joint Applicants to use SBC's experience in Texas to work out a solution on the shared transport issue. In response to the Commission's specific questions, the outline of that solution has been provided by Mr. Appenzeller with the background from Mr. Hopfinger's Direct Testimony on Reopening.

> ***Is it correct to say that the Applicants will not provide any version of shared transport in Illinois, regardless of the outcome of this proceeding, if the FCC or the courts rule that shared transport is not a UNE?*** **(Item No. 3 (b); Attachment A-I, June 15, 1999 letter)**

Joint Applicants state that the issue of whether shared transport is a network element that must be unbundled is currently before the FCC in its UNE Remand Proceeding. As a result, the issue may not be definitively resolved for some time. In the meantime, Joint Applicants would begin deploying shared transport in accordance with their commitments. However, if the FCC or a reviewing court ultimately determines that shared transport is not a network element that must be unbundled, Joint Applicants reiterate that they would be entitled to cease providing shared transport at that time.

> ***What are the specific enforcement mechanisms which would be used by the Commission in the event of non-compliance with the commitments made by the Applicants?*** **(Item No. 3 (c); Attachment A-I, June 15, 1999 letter)**

Joint Applicants answered by referring to their previous responses on the issue of enforcement.

Staff's Position

In this reopened proceeding, there were three versions of common transport addressed by the parties. The three versions were: a) the ICC/FCC version (requiring common transport on a stand-alone basis); b) the SBC/Texas "interim solution" (involves the use of originating and terminating factors and a settlement procedure to allocate appropriate access charge revenues) and; c) the SBC/Texas "long term solution" (involves the use of AIN network architecture).

On re-opening, Staff witness Gasparin reiterated his position that the Joint Applicants should continue to explore the issues surrounding the technical feasibility of offering common transport as an unbundled network element on a stand alone basis. (Staff Ex. 5.02 at 2). Mr. Gasparin averred that both this Commission and the FCC have ordered Ameritech to provide common transport on unbundled network basis. While acknowledging that the FCC's rules requiring the offering of common transport were vacated by the U.S. Supreme Court , Mr. Gasparin testified that the Commission's order was still in effect. (Id.).

Although Mr. Appenzeller testified that there are technical difficulties in the provisioning of this service and that the service cannot be provided at this time, Mr. Gasparin recommended that the Joint Applicants continue to explore the technical feasibility regarding the unbundling of common transport and to provide a semi-annual report to this Commission and other interested parties which delineate their activities in exploring solutions to the common transport unbundling issue. He noted that a similar commitment had been made in Texas as shown in the "Joint Applicants' Response to Commission's June 4 List Of Issues And Joint Applicants' Additional Commitments" - in Attachment 3.1 entitled "Local Switching/Shared Transport Texas" at 1.3.1 page 1.

In light of the commitments made by the Joint Applicants, Staff recommends that the commitments made by the Joint Applicants relative to this issue be adopted by the Commission and be included in the final order.

Intervenors' Position

AT&T witness. Turner testified that the UNEs of Shared Transport – also referred to as Common Transport – and Local Switching are essential components of the "UNE Platform" ("UNE-P") or combination of unbundled network elements provided for in AT&T's Commission-approved Interconnection Agreement with Ameritech.

Mr. Turner defined Shared Transport as an unbundled network element consisting of the same interoffice transport facilities used by Ameritech to transport the calls made by its own local exchange customers. As such, Shared Transport is a common interoffice transmission path between Ameritech switches. Mr. Turner explained that CLECs can use the Shared Transport UNE in conjunction with the Unbundled Local Switching element to transport local calls dialed by the Local Switching element to their destination over Ameritech's Shared Transport network. With

Shared Transport, CLECs can utilize Ameritech's common transport network between an Ameritech tandem and an Ameritech end office. Mr. Turner pointed out that Shared Transport has been designated by the FCC as an unbundled network element. The FCC has ordered Ameritech to provide it both in its First Report and Order dated August 8, 1996, and in its Third Order on Reconsideration dated August 17, 1997. This Commission also ordered Ameritech to provide Shared Transport as defined by the FCC in its Order dated February 17, 1998 in Dockets 96-0486/0569. Id. at 3.

Mr. Turner explained that absent the ability to share the in-place interoffice transport facilities, CLECs would need to build or purchase dedicated interoffice transport facilities that essentially duplicate the existing facilities of the incumbent to provide call routing for their local service customers. He noted that this would be prohibitively expensive and wholly unnecessary, since the existing facilities have sufficient capacity to transport current traffic volumes. Moreover, he pointed out that for Ameritech to implement such an arrangement would require incredibly complicated customized routing that would be prohibitively expensive and technically daunting for CLECs and Ameritech to implement. Id. at 3-4.

Mr. Turner described the Platform as an end-to-end combination of network elements that permits a CLEC to offer a full range of telecommunications services to end users and other carriers. He explained that the Platform consists of the Network Interface Device, Unbundled Loop, Local Switching, Shared (*i.e.*, Common) Transport, Signaling and Call-Related Databases, Tandem Switching and Ameritech-provided Operator Services and Directory Assistance. Id. at 4. Mr. Turner testified that Ameritech has not provided the Platform in Illinois. He explained that because Shared Transport is an essential element of the Platform, Ameritech does not offer the Platform as long as it refuses to provide CLECs with the Shared Transport element. Id. at 4.

Mr. Turner testified that Ameritech has adamantly resisted providing Shared Transport and the Platform in a series of regulatory and appellate proceedings dating back to the fall of 1996. With respect to the "interim solution" for shared transport that Joint Applicants have not proposed, Mr. Turner testified that he found it galling for Joint Applicants to present as a "creative" solution today the exact same proposal that AT&T made to Ameritech nearly two years ago. He explained that AT&T and Ameritech in the summer of 1997 discussed many of the issues identified in Mr. Appenzeller's testimony and AT&T devised a proposal – dubbed "Rough Justice" – that was identical to Ameritech's current "interim solution." Mr. Turner noted that Ameritech even included that proposal in its testimony to the FCC in connection with its Section 271 Application in Michigan. Clearly, he noted, Ameritech could have implemented this solution nearly two years ago. Instead, Ameritech chose to manipulate the legal process, at great expense and loss of time to all concerned, in a calculated effort to avoid its legal obligations. Accordingly, Mr. Turner asserted that Ameritech's "interim solution" merely confirms that it has been playing a series of semantics games with the Commission and with CLECs over Shared Transport. Id. at 7-8.

Further, Mr. Turner testified that the "interim solution" veils what in reality is a set of problems associated not with Shared Transport but with implementing the Unbundled Local Switching element. He explained that in 1996, Southwestern Bell, while negotiating access to unbundled elements for its region, determined that it would provide Common Transport (*i.e.*, Shared Transport in Illinois) without dispute. He noted that it was not until the middle of 1997 that Southwestern Bell notified AT&T that it would require the implementation of an AIN solution to solve at least three implementation problems associated with the Unbundled Local Switching (not Shared Transport) element. The AIN "solution" has absolutely nothing to do with the Shared Transport unbundled element, however. In light of the above, Mr. Turner contended that Ameritech's eleventh-hour offer of the AIN solution as the permanent means to provide access to the Shared Transport element is simply its effort to "spin" once again why it has not provided access to this unbundled element up to this point. Id. at 9-10.

Moreover, Mr. Turner testified that the "interim solution," which AT&T developed two years ago, is practically useless in today's circumstances. Without the ability to order the UNE Platform electronically, it might as well not be available at all from the standpoint of a CLEC desiring to serve mass-market customers. Mr. Turner explained that Joint Applicants are saying it will be months before they will have settled on the ordering and other OSS systems that they will implement in the wake of the merger – and these are the systems to which CLECs will have to design and build their systems in order to be able to pass orders electronically to the ILEC. He pointed out that Joint Applicants are, in effect, proposing that CLECs develop complicated and costly systems that are temporary and would soon have to be replaced when the permanent systems become available. Mr. Turner noted that since SBC has indicated that Southwestern Bell will eventually implement its systems in Illinois, the only prudent course of action would be for CLECs in Illinois to develop interfaces to Southwestern Bell's systems if the merger is to be approved. Mr. Turner pointed out that, to date, AT&T has invested tens of millions of dollars and more than two years of effort to establish system interfaces with Southwestern Bell. At its peak, AT&T had over 200 people working on programming and system design efforts to ensure that AT&T systems properly interfaced with Southwestern Bell's systems. In light of the above, Mr. Turner concluded that Joint Applicants' interim solution is a hollow, if not disingenuous, proposal. Id. at 10-11.

Addressing the Joint Applicants "long term" solution, Mr. Turner testified that the "long-term" solution must be assessed in the context of the necessary OSS and other systems development work that must be accomplished both by SBC/Ameritech and CLECs in order to support the ordering of the Platform. Mr. Turner explained that unless the UNE Platform can be ordered efficiently and reliably (and electronically), it cannot be used by CLECs to serve their customers. Accordingly, the Joint Applicants' "long-term" solution for the UNE Platform is inextricably linked to systems issues. Id. at 11-12.

Mr. Turner testified that the ultimate issue is the manner in which the ILEC and CLECs will work to develop and implement adequate (*i.e.*, at parity with the ILEC's) and

reliable operations support systems ("OSS") needed to support the UNE-Platform for the provision of competitive local exchange service. He noted that given that Mr. Viveros' own timeline is two years, it is important to know beforehand whether the system interfaces would be established to Ameritech or Southwestern Bell's systems. Moreover, because Mr. Viveros indicated that Southwestern Bell integrates its acquisitions into Southwestern Bell's systems environment, Mr. Turner testified that the only prudent course of action would be for CLECs in Illinois to develop interfaces to Southwestern Bell's systems in the event the merger were approved. Id. at 14-15.

Mr. Turner pointed out that AT&T and other CLECs have already developed systems that are interoperable with the SBC systems, software, and business rules. Since several CLECs are near entering the market in Texas with a product offering using the UNE-Platform, under the scenario in which the merger were to proceed, the same systems interfaces should be available in Illinois under the same terms and conditions. Id. at 16.

Further, Mr. Turner asserted that it is vital for SBC to have its systems that are interconnected with CLEC systems integrated into Ameritech's systems in a definite period of time. If not, he pointed out that CLECs may build the interface to Southwestern Bell's systems but not have flow-through capability into Ameritech's region due to SBC not completing its own integration with Ameritech. Specifically, the SBC systems that the CLECs will develop interfaces for must be able to interface with Ameritech's provisioning, maintenance, and billing systems in the Ameritech territory so that orders/requests that are sent electronically to the SBC systems are properly implemented in the Ameritech provisioning and maintenance systems. Id. at 16-17.

Mr. Turner testified that adequate testing of OSS systems will be necessary in any event. He noted that when CLECs develop their interface into the SBC gateway systems – systems that permit many different CLECs to interconnect with SBC and the subtending back-office systems – there would still be a need to ensure that orders and requests flow from these gateways into the actual Ameritech systems that perform the work or hold the information. As such, despite the fact that system interfaces developed by Southwestern Bell in Texas will already be in use, there would still be a need to test the flow-through of orders into Ameritech's back-office systems and ensure that the system interfaces are capable of handling the types and volumes of orders that would be anticipated. The OSS test must be end-to-end, and thoroughly test pre-ordering, ordering, provisioning, maintenance and repair, and billing, including the integration of pre-ordering and ordering. Mr. Turner stated that the FCC's orders have required proof of access to these functions, all of which are imperative for full-scale commercial operation by competitors. Moreover, and following this OSS testing, volume stress testing appropriate to the market should be required over multiple days. Stress testing should occur at commercial volumes, as determined by the expected future demand in a competitive local market. Mr. Turner also emphasized that this volume testing would become even more important if Southwestern Bell incorporates more of its territories into a single systems environment. Id. at 17-18.

Mr. Turner testified that it is vital that a truly independent, technically-skilled third party be engaged to design the testing, conduct it, monitor the results, oversee corrections and retest, and report on the test. Mr. Turner offered that the third-party test entity should act as a "pseudo CLEC" in the sense that it creates and transmits the kinds of orders (known as "order scenarios") to be expected from the CLEC community. Importantly, he noted that independent third party testing can expedite the identification and resolution of problems with SBC/Ameritech's OSS, without being sidetracked into the kind of "finger pointing" that can otherwise arise. More specifically, Mr. Turner asserted that the third party should develop a test plan that would clearly define the scope and methodology of the test, and the entry and exit criteria.

Mr. Turner took issue with Mr. Viveros' position that that testing should not be done. Rather than testing, Mr. Viveros thought that the CLECs should simply send orders to Ameritech. Mr. Turner testified that this position showed little no regard for the value that should be placed on the end user customers in Illinois. He noted that for CLECs to simply send orders to Ameritech would place the service of those customers at risk. He also pointed out that this type of testing would not fully exercise in a disciplined way the variety of order scenarios for which the system interfaces would be developed. Finally, Mr. Turner noted that simply sending orders to Ameritech without any assurance that its systems are volume tested would be irresponsible of all parties. Mr. Turner concluded that it is essential that comprehensive third party testing be done prior to sending orders that would impact the service of customers in Illinois. Id. at 20-21.

Mr. Turner also disputed Mr. Viveros' position that no penalties should apply. In light of the fact that SBC and Ameritech would be solely responsible for building to the interface standards already agreed to in the Southwestern Bell territory, Mr. Turner stressed that if delays occurred or if the SBC/Ameritech combined entity did not meet its commitments, penalties would be appropriate, indeed essential. Mr. Turner pointed out that the Bell Atlantic/NYNEX merger is particularly telling in this regard. He explained that one of the conditions established by the FCC in permitting that merger to go through was for there to be a single systems interface for CLECs across the 18 state region of the combined entity. However, this has still not been done. Consequently, Mr. Turner asserted that penalties would be the only viable means to put "teeth" into this requirement. Id. at 21.

MCIW's arguments are similar to AT&T's. MCIW contends that its interconnection agreement already requires Ameritech Illinois to provide shared transport and that, in any event, Ameritech Illinois should be required to provide shared transport to CLECs as a condition of this merger regardless of the outcome of the FCC's UNE Remand Proceeding. Sprint also maintains that shared transport should be available to competitors on an unbundled basis regardless of the outcome of these proceedings.

Joint Applicant's Reply

Joint Applicants assert that all of the arguments by AT&T and MCIW about what may have been required in the past are irrelevant to their specific commitment here. Ameritech Illinois also denies that shared transport is required by its interconnection agreement with either AT&T or MCIW, and notes that we specifically rejected MCIW's request to require common transport during arbitration of the MCIW/Ameritech Illinois interconnection agreement. As for AT&T's and MCIW's suggestion that shared transport should be mandated regardless of the outcome of the UNE Remand Proceeding, Joint Applicants state that such a requirement would be unfair and discriminatory, singling Ameritech Illinois out from all other incumbent LECs in the country. Accordingly, they argue that AT&T's and MCIW's proposals should be rejected. With regard to Staff's proposal, they state that there is no way to provide shared transport separately from unbundled local switching, but that they will report to Staff regarding any advances on this topic as they occur, or at the least, on a semi-annual basis.

Commission Analysis and Conclusion

We agree with Staff that Joint Applicants' shared transport commitment is responsive to our questions and concerns. We also find that the shared transport commitment is sufficiently specific and subject to adequate enforcement mechanisms. CLECs, especially the large carriers, have long argued for shared transport, and it now will be made available to all who amend their interconnection agreements consistent with Joint Applicants' commitment. Thus, Joint Applicants have committed to do what Ameritech Illinois has stated it would not do on its own, and the commitment therefore represents a procompetitive benefit that will accrue to both CLECs and end-users and that would not exist absent the merger. We also note that the FCC staff has found this commitment to be acceptable.

Thus, Joint Applicants are ordered, consistent with the commitments made during this re-opened proceeding and pursuant to the Commission's authority under Section 7-204(f), to provide this Commission with proof of the implementation of the "SBC/Texas interim version" of shared transport in Illinois prior to the close of this merger. We define "SBC/Texas interim version" to mean the interim form of shared transport discussed by Joint Applicant witness Appenzeller in his direct testimony on reopening. (See SBC/Ameritech Ex. 12.0 at 3-11). The filing of a tariff with this Commission containing such SBC/Texas interim version and our approval of such tariff (which must occur before the Joint Applicants may close on the merger) shall constitute compliance with this condition. Prior to our approval, such tariff shall be reviewed by Commission Staff with a Staff recommendation to the Commission for approval or disapproval. We further order the Joint Applicant's to import the rates agreed to in Texas for the interim version of shared transport to Illinois until such time as Illinois-specific rates can be determined. At such time, the interim rates would be subject to a true-up.

Furthermore, within one year of the merger closing, the Joint Applicants are ordered to implement and offer in Illinois the same version of shared transport that has

been implemented by SBC in Texas utilizing AIN facilities. Finally, the Joint Applicants are ordered to continue reviewing the issue of offering shared transport and report to Staff as soon as any change in facts occur on a semi-annual basis.

We find that this condition to provide Shared Transport should continue even if the FCC eventually decides that unbundling Shared Transport is not proper in its UNE Remand docket. Section 7-204(f) gives this Commission the power to impose terms, conditions or requirements on this merger which protect the interests of Ameritech Illinois' customers. The Commission determines, in its judgment, that it is in the best interests of those customers to have access to an open local exchange market in Illinois. Shared transport is crucial in developing this open market. The offering of shared transport by Ameritech Illinois to its competitors obviates the need for CLECs in Illinois to build or purchase dedicated interoffice transport facilities which are duplicative of existing Ameritech Illinois facilities. Since building or purchasing existing facilities is prohibitively expensive, the Commission deems the offering of shared transport as lowering the barriers to entry for CLECs in the Illinois local exchange market and thereby improving the environment for competitive entry. Any condition which leads to a more open local exchange market and real telecommunication service options for customers, as this condition does, serves the interests of the customers. Thus, we find that we do have the authority to impose this condition.

In the event that the FCC reverses its previous position and decides in its remand docket that shared transport should not be unbundled, the Joint Applicant's are directed to file with this Commission within 30 days of the FCC decision a petition seeking an Illinois-specific determination of the propriety of unbundling Shared Transport under Section 13-505.6. 220 ILCS 5/13 - 505.6. While that Illinois-specific docket progresses, the Joint Applicants will continue to provide Shared Transport as herein described until such time as this Commission comes to a final determination on the merits and issues an order in such procceding.

c. Operations Support Services ("OSS"): Implementation

Implementation timetables regarding integration of Joint Applicants OSS processes. (Question No. 4, Attachment A, Chairman's letter June 4, 1999 letter)

Joint Applicants state that, as a threshold matter, it should be remembered that OSS systems have been developed over time in the 13 states involved in this merger. The OSS systems were in most cases originally developed in a monopoly environment, and were not designed for ordering of UNEs. Joint Applicants further explain that this is a complex and difficult area, complicated by the lack of uniformity of demand by CLECs and the limited number of qualified employees who can perform this work, Y2K work and other ongoing tasks, and that OSS development and integration is not something that can happen overnight. Nevertheless, Joint Applicants have proffered a number of OSS commitments designed (a) to create a comprehensive plan of integration for the Ameritech and SBC's OSS processes; (b) to subject that plan to a collaborative process

that will incorporate CLEC input into how OSSs are made available; and (c) to make that SBC/Ameritech OSS process available on a uniform basis throughout the post-merger SBC/Ameritech states.

OSS Commitments

Joint Applicants assert that there can be no single unified timetable for integration of Ameritech's and SBC's OSS. These systems must be considered on a case-by-case basis, in order to provide CLECs in Illinois the benefits of the combined experience and systems of the two companies, with a separate transitional period that is appropriate for each function. That said, Joint Applicants commit to implement a comprehensive plan for improving the OSS systems and interfaces available to CLECs in Illinois. This plan includes the following elements, which address each of the concerns identified in Items 4 and 5 of Attachment A of the June 4 letter. Joint Applicants' plan, which depends in part upon the systems, expertise, and resources that would become available to Ameritech Illinois as a result of the merger, consists of the following commitments:

Application-to-Application Interfaces Commitments

Joint Applicants commit to deploy, within two years after the merger closing, commercially ready, application-to-application interfaces as defined, adopted, and periodically updated by industry standard setting bodies for OSS (*e.g.*, Electronic Data Interchange ("EDI") and Electronic Bonding Interface ("EBI")) that support pre-ordering, ordering, provisioning, maintenance and repair, and billing for resold services, individual UNEs, and combinations of UNEs. Such interfaces would meet the requirements of 47 U.S.C. § 251(c)(3).

Deployment of the application-to-application interfaces would be carried out in three phases.

Phase 1: Within 5 months after the merger closing, Joint Applicants would develop a complete plan of record (including assessment of Ameritech Illinois' and SBC's existing OSS interfaces, business processes and rules, hardware capabilities, data network, and security protections).

Phase 2: Joint Applicants would seek to obtain collaboratively, within 4 months after completion of Phase 1, agreement with CLECs on OSS interfaces, enhancements, business requirements, and a change management process, including a 12-month forward-looking view of process changes and deployment schedule. In the event Joint Applicants and the CLECs are unable to reach a written agreement within 2 months, any issues in dispute would be resolved through arbitration by an independent third party arbitrator in consultation with subject matter experts from Telecordia Technologies, with the expenses of the arbitration

to be shared by Joint Applicants and the CLECs that are parties to the disputed issues.

Phase 3: Within the sooner of 18 months after the completion of Phase 2 or 24 months after the merger closing, Joint Applicants would develop and deploy, on a phased-in basis, system interfaces, enhancements, and business requirements consistent with the agreement reached in Phase 2. Any dispute between Joint Applicants and a CLEC over whether or not Joint Applicants have implemented the agreement reached in Phase 2 would be resolved through arbitration by an independent third party arbitrator in consultation with subject matter experts from Telecordia Technologies, with the expenses of the arbitration to be shared by Joint Applicants and the CLEC(s) that are parties to the disputed issues.

Graphical User Interfaces

Joint Applicants would deploy, within 2 years after the merger closing, graphical user interfaces (*e.g.*, SBC's Toolbar interface) for OSS that support pre-ordering, ordering, provisioning, maintenance and repair, and billing for resold services, individual UNEs, and combinations of UNEs. Such interfaces would use industry standards as appropriate and will meet the requirements of 47 U.S.C. § 251(c)(3). Deployment of graphical user interfaces would be carried out on the same three-phase schedule as application-to-application interfaces.

Direct Access to Service Order Processing Systems

Joint Applicants would offer -- *in addition to the application-to-application and graphical user interfaces described herein* -- to develop and deploy direct access to SBC's SORD or Ameritech's SOAC service order processing systems for resold services, individual UNEs, and combinations of UNEs, provided that a CLEC requesting such direct access enters into a contract to pay Joint Applicants for the costs of development and deployment. The access developed would meet the requirements of 47 U.S.C. § 251(c)(3). Joint Applicants' offer to develop direct access to SORD or SOAC would be available for a period of 30 months after the merger closing, and Joint Applicants will agree to develop and deploy the interface contracted for within one year of a completed contract with the CLEC.

Additional OSS Commitments

To the extent that OSS issues in addition to those identified above are raised in any collaborative process, Joint Applicants would make such issues part of the appropriate collaborative processes.

> ***On p. 17 of Exhibit 6, the Applicants state their willingness "to commit to the following timetables and milestones regarding integration of OSS processes in Illinois." In the very next line of the document, Applicants state that "there is no single timetable for integration of Ameritech's and SBC's OSS" and that systems will be considered on a case-by-case basis. What specific commitment are the Applicants making here? Do the Phase 1, 2 and 3 commitments cover all (100%) OSS of both SBC and Ameritech which the Applicants currently deploy or plan to deploy? Or, do these OSS commitments only cover certain aspects of Applicants' OSS? What aspects of Ameritech Illinois' OSS do the Applicants envisage will be covered by this 3 phase process?*** **(Item No. 4 (a) Attachment A-1; June 15 letter)**

Joint Applicants explain that they are committing to a three-phase approach to defining and implementing enhancements to existing Ameritech OSS and/or deploying existing SBC OSS in Illinois. First, Joint Applicants would develop a "plan of record," a phase that took several months after the SBC/PacTel merger. Second, Joint Applicants would participate in a collaborative process with CLECs on OSS issues. Joint Applicants note that this is a process that is not within their control and is dependent upon the cooperation of CLECs and assistance of the Staff. Joint Applicants state that this process took several months in Texas. The last phase is the develop and deploy stage, which is also an involved process. The overarching timetable for this three-phase approach is 24 months (assuming that the collaborative process is completed within the timeframe proposed by Joint Applicants). However, this commitment is based on an individual evaluation of each of the functional areas of Ameritech Illinois' OSS, *i.e.*, pre-ordering, ordering/provisioning, maintenance/repair and billing and as such it is Joint Applicants' expectation that enhancements or integration of systems will vary both by functional area and degree as well as by interface type, *i.e.*, GUI vs. application-to-application interface.

Joint Applicants state that they will not wait two years to engage in a flash cut to any OSS enhancements. Improvements, whether or not developed by the processes described above, will be integrated over time on a schedule that will allow Joint Applicants and CLECs to absorb them. Joint Applicants contend that neither side would benefit from a flash cut approach.

Joint Applicants further explain that Phases 1, 2 and 3 would cover all OSS functions. To the extent that the functions are dependent on back-office system capabilities, those systems would be included. However, Joint Applicants believe it is important to note that, given the implementation window involved, not all potential integration of systems can be included. Joint Applicants state that legacy systems cannot be integrated or changed out overnight; 24 months after the SBC/Pacific Telesis merger, integration and consolidation efforts are well underway, but are still not complete. SBC would continue to enhance and evolve its systems capabilities for retail

and wholesale operations alike, across all operating territories, including Illinois, if this merger is approved. After the 24 month implementation window, any subsequent improvements would be communicated and introduced to all affected CLECs following guidelines developed for change management.

Will the interfaces employed by the Applicants comply with the latest industry standards/guidelines developed under the auspices of the Alliance for Telecommunications Industry Solutions ("ATIS")? **(Item No. 4 (b) Attachment A-1; June 15 letter)**

Joint Applicants stated that they are strong proponents of using industry standards or industry guidelines where available. To the extent that using the latest standard/guideline does not result in any loss of functionality, Joint Applicants expect that their proposed plan of record would take into account both the latest version available for implementation as well any known timeframes for release of the next version of guidelines/standards.

What are the specific enforcement mechanisms which would be used by the Commission in the event of non-compliance with the commitments made by the Applicants? Should the Commission engage in third party or carrier-to-carrier testing of OSS to ensure compliance by the Applicants? If so, who should the Commission engage to perform such (third-party or carrier-to-carrier) testing? If there should not be third-party or carrier-to-carrier testing, why not? **(Item No. 4 (c) Attachment A-1; June 15 letter)**

With regard to enforcement mechanisms, Joint Applicants referred to their answers on this topic in response to other questions. In particular, these commitments will be covered by the Commission's residual enforcement mechanisms, both to the extent that they fall within the ambit of Section 13-515 of the Illinois PUA and to the extent the Commission orders a potential allocation of savings to reflect non-compliance with certain conditions as set forth in the Post Exceptions Proposed Order.

In Joint Applicants' view, neither third-party nor carrier-to-carrier testing is required to ensure compliance. Joint Applicants contend that the best measure of their compliance is carrier-to-carrier testing and, ultimately, the actual use of the enhanced OSS by CLEC customers. (Viveros SDR, SBC/Am. Ex. 7.2 at 4.) They also point out that even the carriers that insist on third-party testing do not agree on how or when it would be conducted and completed. Joint Applicants do, however, support carrier-to-carrier testing and encourage CLECs to actively participate in the development process, which will necessarily include testing. As Mr. Viveros stated in his Rebuttal Testimony on Reopening, "if CLECs are willing to develop *and test* during [Phase 3 of the OSS collaborative process] and the Commission remains involved to quickly address unresolved issues or disagreements, not only is third party testing unnecessary but the result would be inferior to the results from SBC's proposal." (SBC/Am. Ex. 7.3 at 7) (emphasis added.)

Should any CLEC feel that SBC/Ameritech has not implemented what was agreed to, the commitment already includes an adequate enforcement mechanism, *i.e.*, arbitration, to resolve the dispute. Joint Applicants also note that Telecordia is performing third-party testing in Texas with the agreement of the Texas PUC, and that such testing could have beneficial findings for Illinois. Joint Applicants further state that it cannot be overemphasized that they have every incentive to provide appropriate OSS functionality which is critical to a successful 271 application, and that in this process there are factors not within the total control of Joint Applicants.

Staff's Position

Staff believes the Joint Applicants were generally responsive to the Commission's questions regarding OSS. As Staff indicated in its Direct Testimony on the Re-Opening, the OSS proposal has the potential to provide CLECs with parity service eventually since it allows for Commission oversight of the collaborative process.

Staff was concerned with certain aspects of the dispute resolution mechanisms proposed by the Joint Applicants. Under their proposal, any disputes that arose during Phase 2 and Phase 3 of the collaborative process would be addressed through an independent third party arbitrator with expenses being shared equally by the Joint Applicants and the CLECs.

Staff raised the concern that arbitration costs might deter smaller CLECs from raising important issues during the collaborative process that might lead to a dispute. As a result, Staff recommended that the Commission serve as a final arbiter to any disputes arising under the collaborative process. Staff reasoned that the Commission, as opposed to an independent third party neutral, was the entity best able to resolve both policy and technical matters impacting telecommunications operations in Illinois. More importantly, Staff pointed out that with the Commission as final arbiter, any associated arbitration expenses would be kept at a minimum for all involved parties.

Staff also does not believe that independent third party testing is necessary in this instance to ensure that Joint Applicants OSS is fully functional. Staff's underlying reasoning is twofold. First, the fact that the Commission itself would serve as arbitrator of disputes during the OSS collaborative process obviates the need for third party testing. As an active participant in the process, the Commission would be fully informed of all disputed issues while it timely resolves all such issues as they arise. Second, there is a danger in waiting until the end of the two year process to institute a third party review since such a delay may easily result in a backlog of unresolved issues.

Staff acknowledges that its OSS testing recommendation in this docket differs from the one made in another telecommunications merger case involving GTE and Bell Atlantic (Docket 98-0866). As Staff explained on re-direct during the evidentiary hearing, there is a perfectly reasonable explanation for the different recommendations.

Tr. 2615-2616. Although Staff did initially recommend the utilization of third party review in the GTE/Bell Atlantic proceeding, that recommendation was based on the fact that GTE supplied Staff with inadequate information regarding the status of its OSS. In the sur-rebuttal phase of that proceeding, however, the carriers countered with an alternative proposal which is very similar to the one the Joint Applicants have made in this proceeding (ie. providing for specific benchmark, penalties, timelines). Subsequently, Staff revised its position regarding the necessity of third party review.

AT&T's Position

AT&T contends that what Joint Applicants have provided in response to the Commission's request for specific and detailed information are vague and indefinite promises about OSS. Consequently, AT&T asserts that the Commission still has no idea what system changes and OSS enhancements Joint Applicants will actually make, much less even propose to make, in Illinois. Joint Applicants offer only future promises to discuss and negotiate with CLECs on these issues five to six months after the merger closes.

The cross-examination of Mr. Viveros, SBC's OSS witness, AT&T points out only served to highlight the vagueness of Joint Applicant's OSS "commitment." Mr. Viveros conceded that Joint Applicant's FCC commitment to deploy "uniform" application-to-application and graphical user interfaces subsumed their Illinois OSS commitments. Tr. (Viveros), 2171. Moreover, when asked whether Joint Applicant's commitment to deploy "uniform" application-to-application interfaces meant that the same interfaces would be deployed throughout SBC/Ameritech's region, Mr. Viveros coyly answered "not necessarily." Tr. 2157. Similarly, when asked whether that meant that SBC/Ameritech would deploy the same version of a particular interface and whether the commitment to implement "uniform" business rules would be the same throughout the 13-state region, Mr. Viveros carefully hedged his answers, twice repeating "not necessarily." Tr. 2158-58.

AT&T opined that what the Commission should take from these non-answers is that Joint Applicant's OSS commitments do "not necessarily" amount to anything. Mr. Viveros' non-committal answers give Joint Applicants unfettered "wiggle" room for the future in defining what they have, or have not, committed to in relation to developing and deploying new OSS interfaces in Illinois. Indeed, AT&T noted that there is nothing on the record to indicate that Joint Applicants have committed to changing the status quo in any way in regard to Ameritech's OSS systems.

Although, the Joint Applicants attempt to blame the vagueness of their OSS commitments on their alleged inability to conduct post-merger planning (SBC/Ameritech Ex. 7.2 (Viveros DOR), at 2), the Commission, AT&T contends, should lend little credence to this self-imposed excuse. Indeed, AT&T pointed out that the record established that while SBC/Ameritech were negotiating their OSS commitments at the FCC – and before their testimony was filed in the Illinois re-opening case – not less than three meetings have taken place between SBC and Ameritech personnel

regarding Ameritech's OSS systems. Cross Ex. B; Tr. 2165-2168. SBC's OSS witness Mr. Viveros was present at those meetings and admitted that he used them to attain "a much better understanding of what systems Ameritech currently offers its CLEC customers." Tr. 2167-68.

AT&T contends that not only are Joint Applicant's OSS promises vague, but they are illusory. They are based on the wholly unrealistic presumption that in just two months (one month under the Proposed FCC Conditions) SBC/Ameritech can come to an amicable agreement with Illinois CLECs regarding a complete revamp of Ameritech's OSS interfaces and corresponding business rules. AT&T explained that any dispute between Ameritech and the CLECs automatically triggers (under their proposal) an open-ended arbitration process that would indefinitely delay all of Joint Applicant's commitments to deploy even those systems or rules that CLECs and Joint Applicants may have agreed on in the collaborative.

AT&T contends that Joint Applicant's schedule for developing and deploying OSS changes is too long and subject to the likelihood of substantial delays which could preclude them from ever being achieved. The two-year time – including the 18 month deployment and development Phase III – is itself is too long. AT&T notes that in Ohio Joint Applicants have committed to implement all OSS improvements resulting from the merger within six months of merger closing. Ohio Stipulation and Recommendation, Section IV.A.3. Joint Applicants have given no excuse why it should take them so long to implement such OSS improvements in Illinois.

Moreover, AT&T pointed out that the already elongated two-year period is applicable if and only if all of the CLECs participating in either the FCC or ICC collaborative workshops fully acquiesce within one or two months in all aspects of whatever implementation plans proposed by Joint Applicants. If all CLECs do not so acquiesce, AT&T explained that the plan is subject to arbitration that is unlimited in duration and virtually certain to delay substantially the deployment of the application-to-application interfaces. Obviously, SBC has a strong incentive, and absolute unilateral ability, to take a "take it or arbitrate it" position and thereby force these federal and state collaboratives to submission or the delays of arbitration.

AT&T contends that the schedule is as grossly unfair to CLECs as it is unrealistic. AT&T explained that In Phase I, Joint Applicants are given five months to develop a proposal for deploying application-to-application OSS interfaces, while CLECs, on the other hand, are allowed only 2 months in the Illinois Phase II to review all the details of Joint Applicants proposals in regard to: (1) changes in OSS interfaces (2) business rules regarding those interfaces (3) a change management process regarding those interfaces and (4) the schedule for deployment of those interfaces and business rules. AT&T opined that two months is far too short for meaningful CLEC analysis of Joint Applicant's proposed plans, much less for CLECs and Joint Applicants to discuss potential solutions to open issues that might arise in those collaboratives. AT&T also pointed out that Illinois CLECs have engaged in negotiations pertaining to the implementation of EDI version 7.0 for more than a year with Ameritech, and have

been discussing the implementation of EDI 10.0 since November of 1998. Moroever, AT&T noted that Joint Applicants admit that "[t]he collaborative process in Texas lasted approximately nine months." SBC/Ameritech Ex. 10.0 (Dysart DOR), at 6. In California, the collaborative process took approximately seven months to come to a conclusion. Tr. (Viveros), at 2178-79. And neither of those collaboratives concerned wholesale changes in the underlying BOC's OSS interfaces and business rules.

AT&T pointed out that the consequence of not accepting Joint Applicants' proposed plan in full within two months, on the other hand, is a delay in the deployment of OSS interfaces and business rules through an arbitration process which is unbounded in duration. The indefinite nature of this process could easily extend for many months or even (with possible appeals) years – well past the 3-year sunset date on which the Proposed FCC Conditions cease to be effective and binding on Joint Applicants.

AT&T noted that while Joint Applicant's readily agree that their Illinois OSS commitments are subsumed within the FCC OSS commitment to implement "uniform" interfaces and business rules (Tr. (Viveros), 2172), and that the FCC and Illinois OSS collaboratives will address identical issues during similar timeframes, Joint Applicants offer no explanation regarding how these two commitments, or how these overlapping collaboratives, would possibly function. AT&T pointed out that Joint Applicants fail to explain what would happen if the FCC collaborative and the Illinois collaborative – or, more likely, the arbitration decisions resulting therefrom – result in differing conclusions. While Joint Applicants admit that there is a "potential" for inconsistent results, Joint Applicants offer vague and unenforceable suggestions of a "coming together" of regulatory entities to "agree on some sort of single adhesive process, rather than manage these processes independent of one another." (Tr. (Viveros), 2184-85). Joint Applicants fail to explain how this unprecedented convergence would take place.

AT&T pointed out that the FCC and the ICC are not the only entities that affect Joint Applicant's OSS commitment. When totaled, there are no less than eight collaboratives taking place all in or around the same time: (1) Three collaboratives at the FCC dealing with "uniform" interfaces, business rules, and access to xDSL systems; (2) Three collaboratives in Illinois, one dealing with interfaces and business rules, another dealing with performance measures and liquidated damages; and a third with interconnection; (3) And two collaboratives in Ohio, one dealing with OSS interface changes and the other dealing with performance measures and remedies. AT&T explained that since all these collaboratives take place concurrently and deal with the same issues, it would be difficult enough for entities the size of AT&T, MCIW and Sprint to be able to staff and juggle them effectively; certainly smaller Illinois CLECs will have even less ability to do so. And the state commissions and FCC have similar staffing and financial constraints. AT&T contended that these overlapping collaboratives raise the likelihood of a "collaborative train wreck" which would make an open-ended arbitration all the more likely.

AT&T contends that Joint Applicants' all-purpose answer to OSS issues is to place them in collaborative processes, but it is clear that that is simply a device to avoid having to commit to any substantive plan for OSS harmonization and improvement while getting this merger approved. And given the overall three-year time frame in which OSS "commitments" will be in effect, there is a strong potential that they will never come about in the first instance. AT&T urges the Commission looks behind all the paper promises of future proposals and processes, where it will find no OSS improvements are specified at all, much less improvements that are enforceable or that a CLEC could use to develop a business plan for market entry.

Sprint's Position

Sprint proposes five charges to implement uniform OSS. Sprint argues that the 24-month period for integrating OSS systems is far too long. Sprint also contends that third-party OSS testing is necessary to ensure that the OSS systems work properly and that parity is achieved in accordance with Mr. Turner's testing proposals. Sprint proposed that there be appropriate OSS upgrades: Also, for advanced services OSS, requesting carriers should have daily access to a loop inventory database.

MCIW's Position

MCIW argues that the Commission should require Ameritech Illinois to implement uniform GUI and uniform application-to-application industry-standard interfaces in Illinois prior to consummating the merger.

MCIW also contends that implementation of working OSS is extremely complex, and therefore that third-party testing is essential. MCIW specifically recommends that the Commission require the consulting firm KPMG, which is performing third-party testing of OSS systems in New York, Pennsylvania, and Georgia, be retained to conduct third-party testing in Illinois. In addition, MCIW asserts that third-party testing alone is not sufficient, and that carrier-to-carrier testing also should be required.

Other Intervenors

Several CLEC Intervenors in this proceeding also raised issues related to the provision of xDSL and the associated OSS of Ameritech Illinois utilized by CLECs to gain access to Ameritech's network information. They raised the issue of gaining access to pre-loop qualification information in Ameritech Illinois' operating territory which would indicate the presence of equipment that may prevent the provisioning of service to end-use customers. (See Gentry Direct, ACI Ex. 1.0 at 2-17, Conn Direct, McLeodUSA Ex. 1.0 at 4-6, ACI Br. on Reopening, MGC Br. on Reopening, McLeodUSA Br. on Reopening, Covad Br. on Reopening).

Joint Applicants' Response

In response to Staff's concerns that Phases 1-3 of the OSS commitment be completed within 24 months, Joint Applicants committed to meet that deadline. Regarding Staff's concern that the Commission arbitrate OSS disputes arising from the collaborative process, Joint Applicants explain that they are not opposed to the Commission's involvement, but offered the option of an independent arbitrator in order to give the Commission flexibility. More importantly, however, Joint Applicants state that OSS issues will have to be resolved on a region-wide basis. Thus, state-specific arbitrations could be counterproductive and cause conflicts. They therefore suggest that the Commission consider working with other regulatory entities to agree on a single cohesive process for resolving any disputes that might arise during the OSS integration and enhancement process.

As for AT&T's request that Joint Applicants immediately adopt SBC's Texas OSS in Illinois because Joint Applicants purportedly plan to do so eventually anyway, Mr. Viveros explained that AT&T's request is not (and is contrary to) what he proposed. Rather, Joint Applicants propose to evaluate both companies' systems for similarities and differences and to evaluate the feasibility of certain changes, as well as the benefits that would accrue to *all* CLECs, not just AT&T, of using or enhancing existing systems. When that evaluation is complete, Joint Applicants will work with Staff and CLECs to create a plan that benefits all parties. Mr. Viveros explained that AT&T's concern about knowing "whose" system to build to may be legitimate in the abstract, but that once Joint Applicants have committed to use industry-standard interfaces (as they have), the CLEC does not need to know whether it will be SBC's or Ameritech's interface that is being used.

Turning to Sprint's claim that the OSS timetable is too long, Joint Applicants explain that to create a system that builds off of the experience and capabilities of both companies, and to do it correctly, takes time. Joint Applicants added that they will not perform a "flash-cut" of all OSS improvements at the end of the 24-month deadline. Rather, improvements will be implemented on a rolling basis, allowing both Joint Applicants and CLECs to absorb them over time.

Regarding the desire of several parties for third-party testing, Joint Applicants first note that Staff witness McClerren has agreed that such testing is not necessary. Indeed, Mr. McClerren acknowledged that Ameritech Illinois' existing OSS interfaces for resale services and UNEs (primarily unbundled loops) are already being used by CLECs to a significant extent (Tr. 2614-2615). In addition, Joint Applicants argue that since the parties will be jointly developing either new interfaces or enhancements to existing interfaces, part of the development effort will include internal testing and joint testing with CLECs. Also, they note that the FCC has recognized that third-party testing is no substitute for actual CLEC usage and that direct testing and development with CLECs will provide the most benefits to everyone; indeed, if that occurs, third-party testing would be not only unnecessary, but inferior to the results of Joint Applicants' proposal.

Commission Analysis and Conclusion

We believe that Joint Applicants have been generally responsive in setting out a process for the planning, development, and deployment of fully operational and commercially available OSS in Illinois. However, we find that a more certain and expedited schedule and rigorous third-party testing and involvement are necessary to foster competition and to protect customers under the authority of §7-204(f) of the Illinois Public Utility Act.

We are persuaded by a number of intervenors that the schedule and approach volunteered by the Joint Applicants is too indefinite. As perhaps few other elements of telecommunications provisioning are more critical to the flow of benefits from competition to consumers we find that the process for OSS development and deployment should be well defined and involve Commission input when necessary. The Joint Applicants have offered conflicting evidence on their asserted commitment to build a viable OSS system. While "committing" to having an operational OSS in 24 months the Joint Applicants phased plan would actually seem to require more than two years (5 months for Phase 1; 6 months for Phase 2; and 18 months for Phase 3) assuming no arbitration is necessary. The Commission is interested in establishing a definitive process which from beginning to end holds the Joint Applicants to their original two year time commitment. As discussed above, OSS are critical to engendering competition in the local exchange marketplace and protecting the interests of Ameritech Illinois' customers. The Commission's three-phase process discussed below establishes an 18 month timeframe for competition, with ample opportunities for extensions if needed by the parties. While this timetable proceeds on an expedited basis from the Joint Applicants original suggestions, the Commission notes that it has directed Staff to closely monitor the FCC's OSS integration process. In this way, Ameritech Illinois' customers will benefit from both the federal and state efforts in the area of OSS integration.

With regard to the specific process for integrating OSS systems, Joint Applicants' three-phase proposal, in principle, strikes us as a reasonable approach to what will certainly be a complex and expensive process. While some parties may disagree with the degree of complexity, the integration of OSS systems will require the active participation of the Joint Applicants, Staff, CLECs, third-party experts, and the Commission. The main purpose of our inquiry was to obtain some firmer idea of what the Joint Applicants plans are for integration and to ensure that the integration process will not have an adverse impact on competition in Illinois. We are satisfied that, with the following modifications, the Joint Applicants' proposal will not adversely affect competition in Illinois and is subject to appropriate enforcement mechanisms. Applicants shall, within 3 months of closing, prepare and submit to the Commission a "plan of record." Phase 2 shall begin at the conclusion of Phase 1 and consist of a 3 month collaborative process which may be extended by a majority of CLECs, or by any party with permission of the Commission. A majority of CLECs may request arbitration by the Commission after one month. In Phase 3, the Joint Applicants shall develop and deploy, on a phased-in basis, systems interfaces, enhancements, and business

requirements consistent with the outcome of Phase 2. Phase 3 shall be completed 12 months after Phase 2 or a final decision on questions arbitrated by the Commission.

With regard to third-party testing, we disagree with Staff that there is no need to appoint a specific entity to perform such testing as part of this case. Third-party testing has been successfully employed in other states confronting the difficult task of managing the transition to a competitive marketplace and it has been suggested by a number of intervenors in this case. We also share Staff's concern that the costs of participation in the process, especially for small competitors, may be prohibitive. The Joint Applicants therefore are required to pay for an independent third-party, retained by the Commission, for technical assistance to the Commission as an arbitrator and to Staff throughout the phased OSS implementation process. The third-party shall report to the Commission, and monitor and assist in the phased process as directed by the Commission, and conduct "New York" style testing during Phase 3 as defined by the Commission. Joint Applicants' commitment includes a collaborative process open to all CLECs. We would expect that process to lead to agreement on most or all issues and to include both internal and CLEC testing of the OSS systems. We also note that, while we are willing to serve as arbitrator of disputes arising from the OSS collaborative process (as Staff suggests we should) and will do so if asked, we expect all parties involved in the process to make a good faith effort to work cooperatively with attention paid to the interests of uniformity and rapid implementation.

Thus, the Commission finds the Joint Applicants' OSS proposal, as modified, allows for Staff involvement in the collaborative process as well as very detailed benchmarks which will enable the Commission to closely monitor the Joint Applicants' OSS performance. Staff is directed to monitor progress made at the federal level in terms of OSS integration and implementation and to specifically advise the Commission as to differences between the state and federal processes and the advisability of opting into the FCC process. The Commission may also be able to take advantage of the third-party auditing and verification that Joint Applicants have proposed to have included as a condition with the FCC which Joint Applicants will make available in Illinois.

The Commission recognizes the importance of advanced services in serving the interests of Ameritech Illinois customers in an age of consumer reliance upon technology to conduct business, communicate efficiently and avail themselves of such applications as the Internet. Unfortunately, the Commission notes that Joint Applicants did not directly respond to these claims made by CLECs. The Commission first notes that CLECs observed that SBC currently provides pre-loop qualification information in some form to CLECs in California. (See Gentry Direct, ACI Ex. 1.0 at 14). The Commission also notes that in the proposed FCC voluntary commitments which were included as part of the record in this proceeding, the Joint Applicants did address the issue of pre-loop qualification information with certain commitments. (See Kahan Rebuttal, SBC/Ameritech Ex. 1.5, Attachment 1 at 13-14). The Commission notes this evidence as a sign that the Joint Applicants are not only responsive to the concerns of

CLECs who provision advanced services, but also recognize the importance of providing this information to CLECs to protect the interests of customers.

The Commission concurs with the CLECs arguments related to pre-loop qualification information and the uncertainty which the untimely furnishing of this critical information creates. Therefore this Commission, in order to protect the interests of customers of Ameritech Illinois under section 7-204(f), further instructs the Joint Applicants to address the concerns raised in this proceeding by CLECs regarding pre-loop qualification information in the three phase collaborative process which has been proposed and subsequently modified by this Commission. Specifically, Joint Applicants shall ensure that OSS systems, once modified in the three-phase process to interface with CLECs, provide the following information in an online format available 24 hours a day: (a) physical medium of loops; (b) loop length in equivalent 26 gauge; (c) length and location of bridged taps and (d) the presence of load coils, repeaters, DLC systems, DAMLS or any other interferers or equipment which parties to the collaborative process deem necessary to provision loops for xDSL service in a non-discriminatory fashion. With regards to such online information, costs shall be borne by the parties in a manner similar to other issues addressed in the OSS collaborative process established by this Commission. Beginning upon the close of the merger, and until such time as this information is available in an electronic fashion, Joint Applicants shall provide requesting CLECs with such information manually within the lesser of five business days or the time equivalent to that provided to Ameritech's advanced services provider. Such manual provision shall not apply for blanket requests by CLECs, and all manual response times by Ameritech Illinois for unreasonably large quantities of requested information should be reasonably related to the time required to retrieve loop makeup information. The Joint Applicants may recover the reasonable direct costs of manually providing the above information about loop conditions.

As for the pricing associated with special construction charges related to the provisioning of advanced services, the Commission concludes that there is simply not enough information contained within the record in this proceeding for it to make an equitable and reasoned determination on this issue. (See Gentry Direct, ACI Ex. 1.0 at 2-17, Conn Direct, McLeodUSA Ex. 1.0 at 4-6, ACI Br. on Reopening, MGC Br. on Reopening, McLeodUSA Br. on Reopening, Covad Br. on Reopening). Pricing of these services to CLECs should not be excessive or discriminatory, unfortunately the record in this proceeding does not sufficiently elaborate upon this issue. The Commission notes however that in Section G of this Order, Joint Applicants are being ordered to submit revised TELRICs, LRSICs, shared and common cost studies. The Commission will address the issue of pricing special construction charges when examining those larger pricing issues.

d. Operations Support Services: Deployment of Interfaces

A timeframe for the Commission to expect deployment of either application-to-application OSS interfaces which support pre-ordering; ordering; provisioning; maintenance, repair, and billing of

resold services; unbundled network elements and combinations thereof, which would include support of graphical user interfaces. Alternatively, when Ameritech Illinois would offer CLECs direct access to its service order processing systems. **(Question No. 5, Attachment A; June 4 letter)**

Joint Applicants' Position

Joint Applicants state that this question has been answered in response to issue "C" above. They add that Ameritech Illinois already provides CLECs with direct electronic access to its service order processing systems and has deployed a full range of application-to-application and GUI interfaces.

Commission Analysis and Conclusion

We agree that this question is covered by our discussion and analysis under C above question 4 and thus incorporate here our analysis and conclusion on that question.

e. Unbundled Local Switching

Provision of local switching in a commercially feasible manner, including customized routing of operator services and directory assistance. **(Question No. 6 Attachment A)**

Joint Applicants' Position

Ameritech Illinois states that it is already in full compliance with any requirements to provide local switching in a commercially feasible manner, including customized routing of operator services and directory assistance.

As a threshold matter, Joint Applicants note that the United States Supreme Court vacated the FCC's rule which had required ILECs to provide unbundled local switching ("ULS"). (*AT&T Corp. v. Iowa Utils. Bd.*, 119 S. Ct. 721, 734-36 (1999)). Therefore, Ameritech Illinois states that it currently has no legal obligation to provide ULS as an unbundled network element.

However, Ameritech Illinois also acknowledges that it is a party to numerous interconnection agreements with various CLECs, which contain the terms and conditions by which Ameritech Illinois will provide ULS on both an end office and tandem switch basis. This Commission has approved these agreements, and they are on file with the Commission's Clerk. Ameritech has committed in its "status quo" letter (Amended Joint Petition, Attachment 6.1) to continue to provide ULS, pursuant to those agreements, at least until the FCC enters its order in its pending UNE Remand Proceeding.

Ameritech Illinois states that the ordering procedures for ULS products are described in the Ameritech Illinois product guides. The ULS product guides list the standard due dates and service intervals associated with these products. Ameritech Illinois explains that these intervals are comparable to intervals established for other network elements in Ameritech Illinois' approved interconnection agreements, and the intervals Ameritech Illinois provides for bundled services of comparable complexity.

Staff's Position

Staff testified that the Joint Applicants' answer is responsive to the Chairman's inquiry. (Gasparin Direct, Staff Ex. 5.02 at 4). Staff also testified that with the provisioning of shared transport it anticipates that CLECs will begin ordering unbundled switching. (Id.).

Commission Analysis and Conclusion

We agree with Staff that Joint Applicants have been responsive to our question. We also find that Joint Applicants' explanation of Ameritech Illinois' ULS product, including customized routing of operator services and directory assistance, is adequate, and conclude that there is no need for any condition on our approval of the merger with respect to ULS.

f. Unbundling and Wholesale Services

***Provision of telecommunications services on a wholesale level, including but not limited to providing the unbundled network platform without operator services and directory assistance; customized routing of all categories of traffic; volume discounts; competitive classifications of services in the ICC number 19, part 22, tariff; appropriate charges to be applied when a customer converts to a reseller on an "as is" basis; branding of resold OS/DA services; 911 services; and access to Advanced Intelligent Network triggers.* (Question No. 7, Attachment A; June 4, 1999 letter)**

Joint Applicant's Position

Joint Applicants contend that the vast majority of the issues listed in this question have already been the subject of an investigation in Docket 97-0553, a pending proceeding initiated by the Commission to address issues relative to Ameritech Illinois' noncompetitive wholesale tariffs. The parties there are waiting for the issuance of the Hearing Examiner's Proposed Order. The issues include: (1) unbundled operator and directory assistance services; (2) volume discounts; (3) the appropriate charges to be applied when a customer converts to a reseller on an "as is" basis; (4) the branding of operator and directory assistance services; (5) 911 services; and (6) access to AIN triggers. Joint Applicants state that a full record was developed in that proceeding and briefing was completed in August of 1998. Ameritech Illinois further contends that it has resolved the technical problems associated with the selective routing and unbundling of OS/DA traffic and filed a tariff offering this service on May 1, 1998 which became effective on June 16, 1998. Ameritech Illinois also stated that with respect to AIN triggers, Staff held workshops in Docket 97-0553; based upon the information developed in those workshops, Staff concluded that no further action was necessary in that docket and that monitoring of technological developments and industry forums should be pursued instead.

Joint Applicants state that the competitive classification of certain Ameritech Illinois' wholesale services was the subject of an investigation in a companion proceeding initiated by the Commission at the same time as Docket 97-0553. Subsequently, Ameritech Illinois reclassified all competitive wholesale services to noncompetitive status. By agreement of the parties, this action rendered the proceeding moot.

Joint Applicants state that they are uncertain what the Commissioners intended by the phrase "customized routing of all categories of traffic." In Joint Applicants' experience, this phrase is used in relation to the selective routing of operator and directory service traffic as a resale option. This issue was addressed in Docket 97-0553. Joint Applicants are not aware of any pending requests by CLECs reselling services in Illinois for selective routing of any other categories of wholesale traffic.

Staff's Position

Staff witness Graves agreed with the Joint Applicants that the unbundling issues identified in the Commission's question have been addressed in other proceedings and listed the issues in Staff Ex. 4.02, at. 15. Mr. Graves also noted that the parties had determined that insufficient information existed at the time of the filing of the testimony to address the appropriateness of Ameritech Illinois' failure to offer mediated or unmediated access to AIN triggers. (Id.).

Mr. Graves further testified that Staff had identified problems with Ameritech Illinois' method of unbundling and rebranding of OS/DA services, and Ameritech Illinois' unilateral imposition of excessive restrictions on the aggregation of services. In order to provide the Commission with a complete understanding of these issues, Staff witness Graves attached Staff's Initial and Reply Brief from Docket 97-0553 as Attachments 5 and 6, respectively, to Staff Ex. 4.02

Staff witness Gasparin testified that Staff had held workshops regarding access to AIN triggers and will continue to monitor the national and industry forums which will set the standards for interconnection to the incumbents network. (Staff Ex. 5.02 at 4). A major concern of Staff regarding access to the triggers is the security to the incumbents network and protection of proprietary data of the other competitive providers who may supply AIN services. Staff is supportive of allowing competitors to provision AIN type services on a fully competitive basis which would allow for future access to these triggers once the security and protection criteria are established. Mr. Gasparin testified that Staff would continue to monitor the progress of the national and industry forums to assure that the goals of this Commission are met. (Id.).

Intervenors' Position

MCIW witness Lichtenberg testified regarding its desire for the UNE Platform. MCIW argues that the UNE Platform is essential to the ability of CLECs to provide competitive local exchange services to residential and small business customers on a mass market basis for the foreseeable future. According to Ms. Lichtenberg, MCIW's experience shows that self-provisioning of facilities or use of individual UNEs does not allow for mass-market service to such customers at this time. MCIW also asserts that an important part of providing the UNE Platform is certainty in pricing, including associated non-recurring charges. In addition, MCIW believes the Commission should prohibit any "glue charge" for Ameritech Illinois' combining UNEs that are already combined in its network.

MCIW asserts that the UNE Platform is not available in Illinois today and that the Joint Applicants have ignored the Commission's questions regarding the UNE Platform. Consequently, MCIW recommends that the Commission require Joint Applicants to provide the UNE Platform without restrictions, and also require Ameritech Illinois to begin transitioning resale customers to the UNE Platform and allowing CLEC customers to be served through the UNE Platform *prior* to consummation of the merger. MCIW

believes this should occur without disconnection of the customer's existing service, and therefore without a charge.

Sprint proposes that SBC provide unrestricted availability of combinations of such UNEs, including shared transport and the UNE-Platform or UNE-P without any non-cost-based non-recurring charges, sunset period (other than as stated herein), 'glue' charge, or geographic restrictions, consistent with 47 C.F.R. §51.315, AT&T Corp. v. Iowa Utilities Board and other applicable law. As used herein, the UNE-Platform or UNE-P means access to the combination of UNEs necessary to provide a telecommunications services at the total element long-run economic cost (TELRIC) of such UNEs.

Also, in any central office where the ILEC (or any of its regulated or unregulated affiliates) has begun to offer xDSL services, then for all loops served by that central office, the ILEC shall make available the xDSL network elements (including all DSL functionalities such as DSLAMs) on a combined basis as a UNE-Platform. This obligation is in addition to and independent of the obligation of the ILEC to make individual UNEs available or its obligation to make its xDSL retail services available at a wholesale discount.

MGC and ACI made similar proposals:

- They contended that as conditions of the merger, the Joint Applicants should be required to work with Commission staff and CLECs to develop an xDSL-capable loop offering within the next 45 days that is not length or technology restrictive and is available to all CLECs.

- The Joint Applicants should immediately make available on a preordering basis data regarding loop characteristics and makeup.

- The Joint Applicants should be prohibited from providing their xDSL services to customers in any central office where a data CLEC can demonstrate to the Commission that it is routinely unable to provision 90% or more of the loops ordered for the provisioning of advanced services.

Joint Applicants' Response

With regard to the UNE Platform issue, Joint Applicants explain that Ameritech Illinois will provide CLECs with pre-existing combinations of UNEs in its network, including the shared transport/local switching combination. They also state that this commitment is, of course, subject to the outcome of the UNE Remand Proceeding at the FCC and to each of the desired elements of a pre-existing combination being required by law. As for pricing of such combinations of UNEs, Joint Applicants state that there will be no "glue charge" for "combining" UNEs that are already combined in Ameritech Illinois' network, but that there will be a cost-based charge for ongoing network administration and maintenance of that existing combination. Joint Applicants

also note that they have committed to the FCC to make the UNE platform available to residential customers, subject to certain conditions, as part of the proposed FCC conditions package. If the FCC approves the merger subject to those conditions, the conditions would apply in Illinois. Joint Applicants have not committed to provide the UNE platform for business customers either in this proceeding or as part of the FCC conditions package agreed to by the FCC staff, because vigorous competition for those customers already exists, both in Illinois and elsewhere.

Commission Analysis and Conclusion

We agree with Staff that Joint Applicants have been responsive to our question. We further conclude, based on Joint Applicants' testimony and other record evidence, that the commitments proffered by Joint Applicants sufficiently address the concerns we had with respect to matters referred to in question 7. As Joint Applicants and Staff explain, most of the issues cited in question 7 are already being addressed in other dockets. We believe it is appropriate to leave those issues to their own proceedings and not prejudge those other cases as part of our decision here. Any ruling in those cases will, of course, apply to the merged SBC/Ameritech and specifically to Ameritech Illinois.

One issue which generated comment concerns the so-called UNE Platform. Joint Applicants have explained their commitment to provide pre-existing combinations of UNEs, with no "glue charge," subject to the outcome of the FCC's UNE Remand Proceeding, and their FCC commitment to make the UNE platform available for residential customers, subject to certain conditions. We find this approach to be acceptable. As explained with respect to shared transport under question 3, above, Joint Applicants should not be required to forfeit in this proceeding any legal rights that they may have when the FCC issues its decision in the UNE Remand Proceeding. In the meantime, however, Joint Applicants have committed to provide shared transport and to also abide by the "status quo" under their interconnection agreements, even though one could argue that the Supreme Court's vacatur of FCC Rule 319 relieves them of any obligation to do so. We therefore find that Joint Applicants' commitments represent a procompetitive benefit to Illinois CLECs and end-users that would not be available absent the merger. We note, however, that Joint Applicants' agreement to maintain the status quo was made without regard to the current merger proposal.

g. Section 251

A clear demonstration in the record regarding compliance with Section 251 of the Telecommunications Act of 1996 in Illinois. If there is not compliance, a clear explanation why compliance is not feasible. Also, Joint Applicants should immediately establish, upon an amended filing, a collaborative process to address any concerns raised by Staff regarding compliance with this section. **(Question No. 10, Attachment A; June 4, 1999 letter)**

Joint Applicants' Position

Ameritech Illinois states that the proper gauge of "compliance with" Section 251 is whether the incumbent has negotiated and entered interconnection agreements as required by Section 252 and is meeting its obligations under those agreements. Ameritech Illinois states that it has a solid record of such compliance, in that it willingly negotiated and arbitrated interconnection agreements with every requesting CLEC and is currently a party to over 60 different agreements, all of which are on file with the Commission. Every one of these agreements has been reviewed and approved by the Commission under Section 252(e) as being non-discriminatory and consistent with the public interest and/or Section 251. Moreover, Ameritech Illinois has been successfully meeting its myriad contractual obligations under these Commission-approved agreements.

Section 251 Commitment

Although Ameritech Illinois strongly argues that it already is satisfying Section 251, in order to address any concerns regarding Ameritech Illinois' ongoing compliance, Joint Applicants would commit to meet with Staff within 30 days of closing to address any current issues Staff may have regarding Section 251. In addition, Joint Applicants would commit to meet with Staff on a quarterly basis to address any Section 251 concerns that may arise over time. Joint Applicants assert that these commitments, combined with Ameritech Illinois' compliance to date, should put to rest any concerns the Commission may have regarding Section 251.

Staff's Position

When Congress enacted TA96, Congress found that significant barriers to entry existed in the local exchange market because of the ILECs' control of the local exchange network. Congress designed Section 251 and 271 to eliminate some of those barriers to entry. Id. At this time, neither SBC nor Ameritech have been found to be fully compliant with those sections. To the extent that Ameritech Illinois is not in compliance with those sections, barriers to entry exist within the Illinois market. (Id.)

Accordingly, in the event the Commission is inclined to approve the merger, Staff opines that the Commission should require AI and SBC to demonstrate compliance with Sections 251 and 271 of TA96 in Illinois to the Commission. (Id. at 72-73). Staff states that such action would not exceed the Commission's jurisdiction. The Commission would not be acting to determine whether the Joint Applicants should receive Section 271 authority to provide in -region interLATA service or even to enforce the Joint Applicants to comply with the sections' mandates. (Id. at 78). Instead, the Commission will merely be reviewing compliance as a prerequisite to merger consummation in Illinois. (Id.)

Staff states that the Commission has two methods for reviewing compliance. First, the Commission could enter an interim order and begin a collaborative process

immediately. (Staff Initial Brief at 72-73). At the end of the period, the Commission could reopen the record in this proceeding to provide the Commission with information about the process and its results. (Id. at 73). Second, Staff explains that the Commission can deny the merger because of its failure to satisfy subsection 7-204(b)(6). (Id.) At the same time, the Commission could institute a collaborative process. (Id.) At the conclusion of that process, Staff states that the Joint Applicants could seek to have their proposed merger approved based on the results of the process by refilling their petition with the Commission. (Id.)

Commission Analysis and Conclusion

We find that Joint Applicants have been responsive to our question and that their commitment to a collaborative process with Staff satisfies our concerns. That commitment also represents a procompetitive benefit for both CLECs and end-users in Illinois that which would not exist if there were no merger. The requirements of Section 251 of TA96 are the cornerstone of introducing competition to the local exchange. CLECs take advantage of those requirements by entering into interconnection agreements with incumbent LECs. Ameritech Illinois has executed over 60 such agreements. While issues regarding the precise requirements of Section 251 continue to arise, that is to be expected under what is still a relatively new statute, and the mere fact that there are disputes is not evidence of Ameritech Illinois' bad faith or unwillingness to follow the law. Moreover, we believe that the collaborative process proposed by Joint Applicants should help identify and resolve any concerns of Staff that exist today or arise from time to time regarding interconnection agreements and Section 251. Such a process is not required by statute or rule, and therefore represents an additional merger-related benefit to Illinois.

h. Enforcement: Liquidated Damages Provisions

The manner, necessary actions and timetable by which Joint Applicants would incorporate incident-based, liquidated damages provisions into interconnection agreements in Illinois. **(Question No. 11, Attachment A; Chairman letter June 4, 1999 letter)**

Joint Applicants' Position

Joint Applicants attached to the Direct Testimony on Reopening of SBC witness William Dysart a full scale proposal for the incorporation of incident-based liquidation damage provisions into interconnection agreements in Illinois. (Attachment 2 to Dysart DR, SBC/Am. Ex. 10.0; *see also* Dysart SDR, Ex. 10.1 at 7-8.) In addition, in their rebuttal testimony, Joint Applicants confirmed that they would make the performance remedy plan as agreed to in Texas available to CLECs in Illinois through all new interconnection agreements or amendments to existing interconnection agreements with the caveat that the Texas Tier 1 and Tier 2 cap for liquidated damages and assessments would have to be adjusted to $90 million for Illinois based upon the number of access lines in Illinois as compared to Texas. (Dysart RR, SBC/Am. Ex.

10.1 at 5-6.) However, as Mr. Dysart explained on cross examination (Tr. 2317), that liquidated damage plan can be applied to whatever set of benchmarks ultimately results from the Illinois collaborative process on measurements and benchmarks.

Performance Measures, Benchmarks and Liquidated Damages Commitments

Joint Applicants would commit to implement in Illinois a comprehensive set of performance measures and benchmarks, with associated liquidated damages and other payments, on the following terms and conditions:

1. Within 60 days following the Merger Closing Date, SBC/Ameritech would establish a joint SBC/Ameritech task force comprised of their performance measurements subject matter experts to develop a plan to implement OSS and facilities performance measurements, associated standards/benchmarks, and remedies in Illinois.

2. The task force would review the economic and technical feasibility of adopting in Illinois each of the OSS and facilities performance measurements and related standards/benchmarks that SBC has agreed to implement in Texas as a result of the Texas collaborative process (which are outlined in the Ohio stipulation and could be made available upon request). This review would identify the differences, if any, between the underlying legacy systems and equipment, including computer, manual and data generating systems and equipment, in Texas and Illinois which may make it economically or technically infeasible to implement certain agreed to performance measurements and/or related standards/benchmarks in Illinois. If no such differences are identified for a particular measurement or standard/benchmark, SBC/Ameritech would implement that performance measurement or standard/benchmark in Illinois. As of February 23, 1999, SBC had agreed to implement in Texas 105 such performance measurements and Agreed To Standards/Benchmarks, which include the performance measurements identified in a U.S. Department of Justice March 6, 1998 letter. Should SBC agree to implement additional measurements or standards/benchmarks in the Texas collaborative prior to the date the task force is established, the task force would include such additional measurements or standards/benchmarks within its review. Additionally, should SBC agree to remedies (*e.g.*, damages, penalties, and credits) associated with one or more Agreed To Standards/Benchmarks in the Texas collaborative prior to the date the task force is established, the task force would also review such agreed to remedies to determine whether it is appropriate to implement such remedies in Illinois considering any relevant differences between Texas and Illinois.

3. Within 90 days following the Merger Closing Date, in conjunction with such task force, SBC/Ameritech would work with the Commission Staff,

CLECs, and any other interested parties in a collaborative process to develop the initial performance measurements, standards/benchmarks, and remedies to be implemented in Illinois. SBC/Ameritech would meet with the collaborative participants on a regular basis to review the status of implementing each of the agreed to performance measurements, Agreed To Standards/Benchmarks, and/or remedies in Illinois. Such review would include either:

A. the timeline for implementing the performance measure, associated standard/benchmark, and remedy in Illinois; or

B. an explanation of why SBC/Ameritech believe it is not economically and/or technically feasible to implement either the performance measure, standard/benchmark or remedy in Illinois, in which case SBC/Ameritech would discuss any substitute measure(s), associated standard(s)/ benchmark(s), and/or remedy(ies) that would be appropriate.

4. Within 150 days following the Merger Closing Date, the task force would complete its initial review of performance measurements/ standards/benchmarks/remedies with the collaborative participants.

5. Beginning 120 days following the Merger Closing Date and completing within 210 days following the Merger Closing Date, SBC/Ameritech would implement in Illinois (subject to any required Commission approval, which would be timely sought), each of the Agreed To Standards/Benchmarks that they determine are economically and technically feasible to implement. Implementation would occur on a rolling basis as each Agreed to Standard/Benchmark is tested and becomes operationally ready and will fully apply to both resale and facilities, where applicable, when implemented. If SBC/Ameritech determine that it is not economically or technically feasible to implement one or more Agreed To Standards/Benchmarks in Illinois within 210 days following the Merger Closing Date, they agree to implement such Agreed To Standards/Benchmarks as soon as it is economically or technically feasible to do so.

6. Within 300 days following the Merger Closing Date, Ameritech Illinois will implement in Illinois at least 79 of the 122 performance measurements and related standards/benchmarks. Ameritech Illinois will not raise economic or technical feasibility as an excuse for noncompliance with this commitment. Within 310 days following the Merger Closing Date, SBC/Ameritech will file a letter in this docket and serve such letter upon all CLECs with whom Ameritech Illinois has an approved interconnection agreement attesting whether or not Ameritech Illinois has met this commitment. Such attestation is subject to review by the Commission. If

SBC/Ameritech attest that they did not, or the Commission finds that they did not implement in Illinois at least 79 of the 122 performance measurements and related standards/benchmarks within of 300 days following the Merger Closing Date, SBC/Ameritech will make a payment of $30 million, as follows:

a. $26.25 million, as payments to CLECs providing end-user service within Ameritech Illinois' service area as of the date 300 days following the Merger Closing Date as follows:

A. A CLEC's Access Lines, for each CLEC, shall be its total number of access lines in service, including, without limitation, residence access lines, business access lines and end-user trunks, and ISDN lines, whether resold or not, measured as of the date 300 days following the Merger Closing Date, within Ameritech Illinois' current service area. Each CLEC that desires to receive any of the $26.25 million in payments must provide to the Commission Staff, no later than 330 days following the Merger Closing Date, a report identifying the number of such lines and trunks for that CLEC. Such report shall separately identify: i) the number of resold Ameritech Illinois access lines; ii) the number of unbundled loops purchased from Ameritech Illinois; and iii) all other such lines and trunks in service within Ameritech Illinois' current service area. Each CLEC submitting such a report will certify to the Commission Staff the accuracy of such report. The Commission Staff will notify each qualifying CLEC of its pro-rata share of the $26.25 million. Thirty days after the date of such notice, the Commission Staff will provide notice to SBC/Ameritech as to the appropriate disbursement of the $26.25 million. Within 60 days of receiving this notice from the Commission Staff, Ameritech Illinois will issue checks totaling $26.25 million made payable to each qualifying CLEC for the disbursement amounts listed in Staff's notice to Ameritech Illinois.

B. Total CLEC Access Lines shall be the sum of A. above for all qualifying CLECs submitting a timely report.

C. A CLEC's Pro-Rata Share shall be the ratio of A. above for that CLEC, divided by B.

D. Each affected CLEC within Ameritech Illinois' current service area shall receive a payment equal to $26.25 million multiplied by the CLEC's Pro-Rata Share; and

b. $3.75 million to the Community Technology Fund described below.

7. If Ameritech/Illinois reports that it has met the commitments as provided and that is disputed, the Commission may issue an order to resolve that dispute and may set forth-appropriate time frames.

8. For each Agreed to Standard/Benchmark to be implemented in Illinois that has an SBC agreed-upon remedy in Texas, SBC/Ameritech would discuss with the collaborative participants the proposed remedy to be attached to such Agreed to Standard/Benchmark in Illinois. After SBC/Ameritech implement an Agreed To Standard/Benchmark in Illinois, they would also implement (subject to any required Commission approval, which will be timely sought) any remedy to be associated with such Agreed To Standard/Benchmark consistent with the approach used in the Texas collaborative process. If the collaborative participants agree, SBC/Ameritech would refrain from implementing a particular remedy. Regardless of whether or not SBC agrees to remedies (*e.g.*, damages, penalties, and credits) associated with one or more Agreed To Standards/Benchmarks in the Texas collaborative, the Illinois collaborative process is not precluded from considering any proposed remedy or remedies.

9. If any participant in the collaborative process disputes SBC/Ameritech's determination that it is not economically or technically feasible to implement a particular Agreed To Standard/Benchmark in Illinois, either at all or within the 210 day time period, the collaborative participants would collaborate to resolve such dispute in the collaborative process. If any such dispute cannot be resolved through the collaborative process, any participant may ask the Commission to resolve such dispute. In any such dispute that may arise before the Commission, SBC/Ameritech retain the burden of proving to the Commission that it is not economically or technically feasible to implement an Agreed To Standard/Benchmark in Illinois.

10. Ameritech Illinois would provide a report to the Commission Staff on the results of its performance measurements on a quarterly basis, beginning the first full calendar quarter in which Ameritech Illinois has at least one full month of data for one or more performance measurements, and would report with respect to transactions affecting Illinois CLECs relative to their provision of service to end users in Illinois. If it is not economically or technically feasible, as discussed in the collaborative process, for Ameritech Illinois to report transactions on that basis, reporting would be done either on an Ameritech-wide or SBC-wide basis as reasonably determined by Ameritech Illinois after consulting with Commission Staff. Performance measurement reports would be provided to CLECs in

conformance with each CLEC's interconnection agreement and would be made available electronically if so requested.

11. For a minimum of one year following the Merger Closing Date, and thereafter on an as-needed basis as determined by Staff, participants in the collaborative process would collaborate to implement any additions, deletions, or changes to the performance measurements, standards/benchmarks, and remedies that are implemented by SBC/Ameritech in Illinois. Any participant may propose such addition, deletion, or change based upon experience with such implemented performance measurements, standards/benchmarks, remedies, or any other factor. If a dispute over any such addition, deletion, or change cannot be resolved through the collaborative process, any participant may ask the Commission to resolve such dispute. The participant proposing the addition, deletion, or change retains the burden of proving that such addition, deletion, or change should be adopted in Illinois.

Joint Applicant's Replies to Attachment A-1 (Item (a)

On p. 32 of Exhibit 6, the Applicants refer to their willingness to discuss with the Commission mechanisms currently contemplated by the Applicants and the FCC with regard to incident-based, liquidated damages provisions. Applicants should address such developments in filings with the Commission in this proceeding. (Item No. H (a) Attachment A-1; June 15 letter)

Joint Applicants state that the answer cited by the Commission refers only to the fact that other incident-based, liquidated damages provisions may result from the outcome of the FCC merger process, and that Joint Applicants' commitment in this proceeding is to provide the incident-based, liquidated damages provisions structured in Texas through the collaborative process. That process, Joint Applicants noted, was a product of much "give and take" by the participants.

On July 1, 1999, Joint Applicants and the FCC Staff reached agreement on a multitude of conditions that would enable the FCC Staff to recommend approval of the merger. In his Rebuttal Testimony on Reopening filed on July 9, Mr. Kahan further responded to question 11(a) by providing this Commission a copy of the proposal made to the FCC and by giving this Commission the option of adopting the FCC benchmark proposal in lieu of the so-called Texas benchmark plan. Here is the sum of Joint Applicants' responses and commitments:

> Under the FCC performance plan, as it impacts the Illinois commitments, payments would be made under the Illinois commitments, assuming the Illinois Commission includes those commitments in its final order. Thus, for the CLECs operating in Illinois, payments would first be made to the CLECs under the Illinois plan up to the Illinois cap, and then be made to the CLECs under the FCC

performance plan and up to the Tier 1 federal cap, if it exceeds the Illinois cap. If the state plan requires assessments to the state – as the Illinois commitments would – then similarly, payments would be made to a public interest fund designated by the State of Illinois under the state plan up to the Illinois cap, and then to the federal public interest fund up to the Tier 2 federal cap, to the extent that it exceeds the Illinois cap. (Tr. 2268, Dysart.)

At the hearing, Joint Applicants' witness Mr. Dysart testified that the cap in Illinois will be approximately $90 million, based on the relative number of access lines in Texas, which is approximately 9.8 million, as compared to the approximately 6.9 million access lines in Illinois. (Tr. 2268-2269, Dysart.) It is Joint Applicants' understanding that Staff concurs in this method of calculating the Illinois cap. (*See*, Tr. 2273, Dysart.)

Were Illinois to forego the state assessments, then payments would be made to the federal public interest fund under Tier 2 of the federal plan, assuming SBC is not providing parity or benchmark performance for three months in a row or more than six months in any calendar year.

Finally, although this does not directly impact Illinois, if SBC is not providing parity or benchmark performance for three months in a row or more than six months in any calendar year, it must pay into the federal public interest fund under Tier 3 of the FCC performance plan in any event.

In short, in each instance, the CLEC would pursue any penalties available to it under the Illinois-ordered conditions to the full extent of those penalties. If the penalties available to the CLEC in Illinois are less than what the CLEC would be entitled to in Illinois as a result of the FCC conditions, the CLEC would be entitled to pursue its FCC remedy for any overage. (Tr. 2269, Dysart).

On pp. 33-37 of Exhibit 6, the Applicants have incorporated a recommended course of action with regard to performance measures, benchmarks and remedies similar to that reached in the stipulated agreement with the Public Utilities Commission of Ohio. How have the Applicants addressed the Commission's desires (as expressed in Attachment A, Item 11) for the incorporation of incident-based, liquidated damages provisions into interconnection agreements in Illinois with this proposal? (Item No. 11 (b); Attachment A-1; June 15 letter)

Joint Applicants respond by referring to Attachment 2 to Randy Dysart's Direct Testimony on Reopening, which is the Texas plan for incident-based, liquidated damages provisions that Joint Applicants have committed to made available to CLECs in Illinois through all new interconnection agreements. In addition, Joint Applicants state that they would be willing to amend existing Ameritech Illinois interconnection agreements on request by the CLEC to include these provisions.

As discussed in response to Commission question No. 11(a), Joint Applicants also have proposed a liquidated-damage provision to the FCC. While that liquidated-damage provision proposed to the FCC is substantially identical to the liquidated-damage provision proposed in Illinois (*see* Tr. 2267, Dysart), the FCC provision will, if adopted by the FCC, apply to the 20-benchmark FCC proposal as compared to the 122-benchmark plan established in Texas and proposed in Illinois.

As Joint Applicants indicated in the rebuttal testimony on reopening of James Kahan, the Commission has the option of choosing the Illinois benchmark and liquidated-damage proposal or the FCC liquidated-damage proposal. (Kahan RR, SBC/Am. Ex. 1.5 at 26-27.) However, regardless of which proposal the Commission chooses, Joint Applicants state that the implementation of the two plans will dovetail to form a complementary regime under which liquidated-damage assessments will first be available to the full extent ordered by this Commission and then, to the extent that the FCC proposal allows for any additional liquidated damages, the overage will be available under the auspices of the FCC plan.

> ***Under the proposal on pp. 33-37 of Exhibit 6, the Applicants propose a solution to the issue of technical infeasibility. By what process is the Commission supposed to resolve technically infeasible claims by the Applicants which are disputed by competitors? If a claim of technical infeasibility is made by Joint Applicants and the Commission finds otherwise, by what process is the issue definitively resolved? Please clarify. (Item No. 11 (c); Attachment A-1; June 15, letter)***

Joint Applicants refer to their response to Commission question 2(a)(iii) above. They further add that SBC's experience in the collaborative process in Texas resulted in no arbitration regarding issues of technical feasibility and, as noted by Mr. Dysart, it is not anticipated that technical feasibility issues will be of particular moment in the Illinois collaborative process. (Dysart SDR, SBC/Am. Ex. 10.1 at 11-12.)

> ***On p. 34 of Exhibit 6 under commitment 6, why have the Applicants proposed implementation of "79 of 105 performance measurements and related standards/benchmarks?" Aside from being the same number in the Illinois stipulated agreement and approximately 75% compliance, how was this number determined? Why do the Applicants feel this level of compliance is appropriate? (Item No. 11 (d); Attachment A-1; June 15, letter)***

Joint Applicants explain that the number of measurements was established based on a determination by SBC/Ameritech as to which measurements could be implemented in an expedited manner. Joint Applicants further state that these measurements are those that directly impact the end-user customer and include the measurements previously recommended by the DOJ. Joint Applicants further promised

to make every attempt to provide more measurements, where feasible, in an expedited manner.

> ***On p. 34 of Exhibit 6 under commitment 6, why have the Applicants proposed a payment of $20 million? Aside from being the same payment in the Illinois stipulated agreement, how was this number determined? Why do the Applicants feel this payment is appropriate? Have the Applicants alternatively considered the posting of a "performance bond" or some other form of enforcement mechanism to be used in the event of non-compliance with this or any other commitment? (Item No. 11 (e); Attachment A-1; June 15, letter)***

Joint Applicants state that the figure of $20 million was a negotiated sum in Ohio after a long process of "give and take" reflecting the input of various parties to that negotiation, including consumer groups and certain CLECs. It was intended to create an appropriate penalty to ensure Joint Applicants' compliance or, in the alternative, adequate remedies to both CLECs and the State if Joint Applicants could not meet their commitments. Joint Applicants note that the Ohio Commission agreed with that assessment in approving the number and the Stipulation. Joint Applicants further explain that the figure has now been increased to $30 million in Illinois to reflect the sizing calculation (based upon access lines) performed by Ameritech witness David Gebhardt in his Direct Testimony on Reopening.

Staff's Position

Staff took no position on question 11(a), which was essentially mooted later by the release of the FCC staff's proposed conditions.

As for question 11(b), Staff believes that the proposed performance remedy plan provides an opportunity for CLECs to obtain liquidated damages on those occasions when Joint Applicants fail to provide adequate service. Just as the recommended performance measures will have to undergo a collaborative process and possible arbitration, Staff envisions this proposed performance plan undergoing a similar collaborative process. Staff believes this performance plan is viable as long as the Commission is deemed the final arbitrator of any disputes connected to the plan. Staff further recommends that the Commission seek assurances from Joint Applicants that the plan will be an ongoing performance assurance program contained in interconnection agreements and not be subject to arbitrary termination at the discretion of Joint Applicants.

With regard to question 11(d), Staff concludes that Joint Applicants have responded adequately. Staff also notes that Joint Applicants' claims of complexities faced in integrating their two respective systems must be given due consideration, and that Joint Applicants are best informed regarding how expeditiously such integration can take place.

With regard to question 11(e), Staff states that while the $30 million commitment for Illinois appears legitimate on its face, it reflects the fact that Joint Applicants are reporting their performance on only 79 of the Texas performance measures. In other words, Staff believes that this penalty amount does not guarantee that Joint Applicants are performing at any particular level of parity. Staff therefore is more interested in the interconnection non-performance damages and assessments described in response to question 11(b). With a total cap of $ 90 million and specific standards and benchmarks to be developed collaboratively or through Commission arbitration, Staff contends that this mechanism provides for a more effective ongoing method of ascertaining parity levels of service to CLECs.

AT&T's Position

AT&T witness Gillan testified that the Joint Applicants have failed to propose an enforcement process that can be expected to reduce litigation, speed entry or otherwise streamline the process. Mr. Gillan contended that the so-called interconnection commitments by the Joint Applicants are virtually worthless as a means to reduce litigation and speed entry. He noted that the problem that these commitments should address is the delay and cost of the arbitration process; the solution proposed by the Joint Applicants, however, is essentially the same arbitration process, with its attendant cost and delay. Id. at 37.

Mr. Gillan observed that the Joint Applicants have fundamentally agreed only to "talk about" creating an automated enforcement mechanism that relies on liquidated damages tied to specific performance measures and benchmarks in future collaborative workshops and hearings. He noted that although preferable to refusing to "talk about it," there has been no real change in either the manner, or the incentives, of the discussion that is likely to occur. Id. at 38.

Mr. Gillan asserted that the principal barrier to local competition has been a recalcitrant ILEC. After the merger, the fundamental circumstance that will change is that the ILEC will be larger, Illinois will be proportionally smaller (to the combined entity), and the true headquarters more distant. Against this backdrop, Mr. Gillan opined that a "commitment" to "talk about a commitment" is of limited value, at best, and it stands in stark contrast to what the Commission has requested. Id. at 38.

Mr. Gillan stated that it is useful to remember that the Commission is reviewing this merger because SBC prefers to adopt the role of incumbent rather than compete as an entrant. He noted that SBC could have come to Illinois with the commercial incentive to tear down Ameritech's entry barriers. Instead, Mr. Gillan testified, because SBC would rather become the incumbent, the Commission's only hope with the merger would be to use regulatory tools and meaningful conditions to try and achieve the same result. Id. at 38.

Mr. Gillan testified that the Commission should view with great skepticism (and attribute little real usefulness to) the enforcement mechanisms that the Joint Applicants have offered. He asserted that either the conditions to be enforced themselves have little substance (how, for example, do you enforce a commitment as heavily caveated as the Joint Applicants' interconnection commitments?), or the Joint Applicants' commitment is only to create an enforcement mechanism in the future. Id. at 38-39.

As an example, Mr. Gillan noted the inherent problems associated with how the Commission would "enforce" the Joint Applicants' commitments to implement "shared transport" with a goal of meaningful competition. He pointed out that the fundamental reason CLECs seek shared transport is to be able to offer broad-scale, mass-market services using the UNE-Platform. As explained by AT&T witness Turner, implementing shared transport in the timeframes now agreed to by the Joint Applicants will have very little real impact in the market. Mr. Gillan explained that this is because the OSS needed to process and provision commercial volumes of orders will not be in place until much later. Id. at 39.

Mr. Gillan pointed out that the central goal of an enforcement mechanism should be to make sure that market conditions change from what they are, to what they can be. While the Joint Applicants have proposed a specific commitment and timetable for shared transport, he noted that they they have made no similar commitment to the underlying OSS that would make the shared transport "concession" significant. Consequently, Mr. Gillan pointed out that there is no enforcement mechanism to achieve the intent of shared transport, because there is no real timetable and commitment to make the shared transport commitment competitively significant. Id. at 39-40.

Mr. Gillan observed that in the absence of incident-based, liquidated damages, the Commission should not expect any less need for regulatory intervention in the future. Mr. Gillan testified that the unfortunate fact is that many of the Joint Applicants' commitments are little more than promises to do what they are legally obligated to do, tied to enforcement mechanisms that are already available: arbitrations, complaints, litigation, etc. Mr. Gillan asserted that the favored enforcement mechanism in the Joint Applicants' proposal remains the status quo. Id. at 40.

Mr. Gillan recounted the old political saying that half a loaf is better than none. The same, however, cannot be said for scissors – a half a scissors simply will not get the job done. Mr. Gillan termed the Joint Applicants' approach to enforcement a "half-a-scissors solution." Shared transport is offered under defined timelines -- but the OSS to make it commercially meaningful are not. Joint Applicants commit to implementing specific performance measures -- but only measures that they choose, and agree only "to talk about" the benchmarks and penalties that will make the measures relevant. Joint Applicants' promise they will extend to Illinois interconnection provisions from other states to avoid unnecessary arbitrations – but the commitment is so laden with restrictions/limitations that arbitrations are all but inevitable. Absent is the full pair of

scissors – i.e., a matched commitment and enforcement mechanism that will automatically improve competitive results.

More specifically, AT&T contends that Joint Applicants' commitments regarding implementing 79 of the 122 agreed to Texas performance measures and benchmarks and the Texas liquidated damage plan concerning those standards/benchmarks are appallingly vague. AT&T points out that Joint Applicants failed to list 43 of the 79 performance measures and benchmarks they will implement in Illinois within 300 days. AT&T asserts that Joint Applicants' ambiguity in this regard is suspect since their testimony discusses at length the criteria they used for choosing the specific number 79. Yet, they repeatedly claimed that they could not name them, other than to say that 36 of the 79 measures/benchmarks will include those agreed to at the FCC. SBC/Ameritech Ex. 10.0 at 7; Tr. 2278-80. Joint Applicants are silent on the identity of the remaining 43. Again, AT&T notes that Joint Applicants have carefully couched their "commitment" in a manner that makes it impossible for the Commission, or Illinois CLECs, to know what it actually is. And again, Joint Applicants have given themselves plausible deniability in regard to what they have, or have not, committed to in Illinois.

Moreover, AT&T contends that Joint Applicants have failed to make any firm commitment to implement any performance measures/benchmarks beyond the 79. Joint Applicants have specifically committed to implementing <u>only</u> those Texas measures/benchmarks (beyond the 79) that SBC/Ameritech believe are "technically and economically" feasible in Illinois. SBC/Ameritech Ex. 10.0, at 3-7. True to form, SBC/Ameritech have conveniently failed to conduct any analysis regarding which of the 122 Texas measurements/benchmarks are technically and economically feasible in Illinois. Tr. 2313-14. Any assessment of technical or economic feasibility would be left to SBC, with a disputing CLEC's only remedy an open-ended arbitration. Tr. 2315-16. In reality, therefore, Joint Applicants have not committed to implementing even one of the Texas measurements/benchmarks beyond the presently undefined 79.

Further, AT&T contends that the existence of a federal performance parity plan that only requires implementation of 36 of the 122 Texas measurements/benchmarks raises the possibility that Joint Applicants will attempt to use that national plan as an excuse (perhaps couched in terms of "technical or economic" infeasibility) for not implementing additional measurements/benchmarks in Illinois beyond the 79. AT&T points out that the Joint Applicants have already begun to apply that pressure on other states. Ameritech Michigan has asked the Michigan Public Service Commission ("MPSC") to reconsider its order requiring performance measurements and to defer application of any requirements that "conflict with the performance measurements adopted, or to be adopted," in this proceeding based on its representation that the MPSC's measurements would require Ameritech "to devote significant resources to implementing processes that would not survive FCC action." Ameritech Michigan's Petition for Rehearing or Clarification, MPSC Case No. U-11654, U-11830, at 5-6 (Mich. PSC June 28, 1999). AT&T notes that Ameritech's excuse for noncompliance in Michigan sounds dangerously similar to an argument that the existence of the FCC plans makes implementation of the Michigan plan economically infeasible. Ameritech's

filing, coupled with Joint Applicants' well-caveated commitments, raise the likelihood that Joint Applicants will attempt to misuse the Proposed FCC Conditions to substantiate a claim that it is "technically or economically" infeasible to implement any standard/benchmarks beyond the 79 in Illinois.

AT&T notes that Joint Applicants have also failed to give any indication concerning how long they will make these performance measures/benchmarks and liquidated damages available to Illinois CLECs. AT&T pointed out that SBC witness Mr. Dysart indicated that those terms would be available for three years, but beyond that he stated on cross examination that "a lot of things could happen." Tr. (Dysart), at 2278, 2308-2309. Presumably, indicating that if a CLEC wished to keep those terms and conditions in future interconnection agreements, the CLEC would be forced to negotiate and/or arbitrate with SBC/Ameritech. Tr. (Dysert), at 2278, 2308-09. Moreover, AT&T observed that this is especially troublesome since performance measurements/benchmarks with automatic liquidated damages will become all the more important if Joint Applicants obtain 271 relief during this three-year period.

AT&T asserts that beyond than their vagueness, Joint Applicants' commitments regarding performance measures and liquidated damages are otherwise flawed. AT&T provided a brief summary of those flaws, which it believes must be addressed prior to their approval by this Commission in this docket or in a follow-up collaborative. In fact, AT&T asserts that the enormity of these flaws raise the likelihood that the collaboratives will result in protracted arbitration.

AT&T points out that all that this Commission knows for sure is that Joint Applicants have committed to making available the 36 performance measures/benchmarks that they have agreed to make available at the FCC. This Commission still does not know what other 43 performance benchmarks/measures Joint Applicants will make available in Illinois. Because of Joint Applicants' caveat of "technical or economic" feasibility, the Commission has no assurance that Joint Applicants will provide more than 79 of those 122 Texas performance measures/benchmarks. While the Joint Applicants have committed to making the Texas liquidated damages plan available in Illinois, they have failed to indicate how long Illinois CLECs could take advantage of this offer. And, as noted, that plan has numerous flaws that must be fixed in the collaborative process. AT&T contends that Joint Applicants' paper promises in regard to performance measures and liquidated damages are, once again, couched with caveats, ambiguities and shortcomings that make Joint Applicants' purported "promises" nothing more than a promise of future arbitration to the detriment of Illinois consumers.

Sprint's Position

Sprint contends that without knowing which specific performance measure will be implemented in Illinois, Joint Applicants' commitment is too undefined to be meaningful. Instead, Sprint contends that at least 60 days prior to closing, either all 122 Texas measurements should be implemented and available in Illinois as a pre-merger

condition or the most current performance measures applicable to SBC in California should be implemented. Sprint contends that measurement standards, which include benchmarks, retail analogs and surrogate retail analogs, should be based upon actual Ameritech Illinois support provided to its retail operations or retail analogs, and that in the absence of directly comparative Ameritech Illinois results, standard levels of performance should be established based upon performance studies. Sprint believes that this will ensure performance levels necessary to give CLECs a meaningful opportunity to compete.

21st Century's Position

21st Century Telecom listed a variety of areas where it believes Ameritech Illinois is not providing service to it at parity with the service it provides to itself, and generally contends that the proposed performance measures and penalties are inadequate to remedy these problems. Ms. Smoot testified about alleged problems regarding Out-of-Service trouble reports, address validation for new orders, ability to re-use spare loops when a customer elects not to port his number, delayed collocation commitment dates at the Franklin Street central office, a recent failure of Ameritech Illinois' signal control point, and delays in "make ready" requests for poles.

Covad's Position

Covad recommends that Joint Applicants be required to post a $300 million performance bond, payable to CLECs (with interest going to fund Commission enforcement efforts and/or to the public-interest funds discussed below), for violations of the interconnection and unbundling requirements of TA96. In addition, Covad proposed that the following condition should be included in the final order to address the provision of unbundled loops, including payment of special construction charges:

> Applicants shall not impose special construction charges for the provision of unbundled loops unless: (1) it can be shown that the costs to be recovered through such special construction charges are not already being recovered through the TELRIC UNE pricing for the loop, and; (2) Applicants would charge their end use customer the same special construction charges if Applicants provided the same service to that end use customer.

Also, Covad proposed that the following condition should be included in the final order to address SBC-Ameritech's provision of loop information to carriers purchasing unbundled loops:

> Applicants should provide CLECs 24 hour on-line access to a computer database which contains information concerning the technical make-up of loops on its system, including physical medium of the loop (i.e., cooper or fiber); loop length in equivalent

26 gauge; the length and location of bridged taps; and the presence of load coils, repeaters, DLC systems or DAMLs.

McLeod's Position

McLeod asserts that Ameritech Illinois is paying reciprocal compensation on Internet-bound traffic only if the terminating company has been a successful Complainant on this issue. Thus, as a merger condition, McLeod proposes that SBC/Ameritech be required to pay reciprocal compensation to all CLECs on calls terminating to the Internet, unless the FCC determines that a different compensation mechanism is appropriate. McLeod also asserts that special construction charges are being unreasonable assessed to CLECs, wherein Ameritech Illinois does not charge its own users to provide the same loop at the same location to the same user. Coincidentally, Ameritech Illinois should be required to reverse its policy and allow CLECs access to it databases, which includes information about the existence of copper facilities the presence and types of digital loop carrier deployed, and the deployment of equipment such as load coils, taps and repeaters, as a condition of merger approval. McLeod also requests that the Commission ensure volume discounts continue to be offered and that wholesale (resellers) be treated fairly.

Joint Applicants' Response

Joint Applicants respond to AT&T by noting that there are numerous enforcement mechanisms in place today that give meaning to their commitments, and that AT&T has not proposed any additions or alternatives to those mechanisms. With regard to 21st Century's allegations, Joint Applicants contend that such specific operational issues have no real relevance here and that, in any event, Mr. Appenzeller refuted each of the allegations. As for Sprint, Joint Applicants state that they do have to bring all 122 Texas measures to Illinois, but that doing so immediately is not possible. They add that all measurement will be adopted to ensure parity within Illinois. Joint Applicants view Covad's suggestion of a performance-bond requirement as unnecessary, excessive, and punitive, in that there are already enforcement mechanisms under state and federal law and because performance bonds are typically for an entity that lacks the financial wherewithal to guarantee the financial aspects of its performance – which is not the situation with SBC or Ameritech.

Commission Analysis and Conclusion

We conclude that Joint Applicants' commitment to import to Illinois the "Texas plan" for performance measures and incident-based liquidated damages provisions is responsive to our question. But falls short of what we consider necessary to safeguard our ability to monitor a thriving and dynamic competitive telecommunications market for consumers. Our goal is to ensure that any conditions imposed in this Order are not illusory, but rather are specific and enforceable, and that enforcement measures are adequate to ensure full compliance with the conditions. The Texas plan, in principle, and the related commitments serve to achieve these goals.

We therefore order that the Joint Applicants implement all 122 of 122 performance measures outlined in the Texas plan within 300 days of the merger closing. Should the Joint Applicants be unable to implement any of the 122 specific performance measures and benchmarks within the prescribed timeframe the Commission may grant a waiver from such a requirement. We are encouraged by the Joint Applicants testimony that technical infeasibility has not been a barrier to implementation in the past and is not anticipated in Illinois. We note, however, that the Joint Applicants theory of economic infeasibility shall not be grounds for waiver of the 300 day deadline for implementation of performance measures and benchmarks in this state.

It is our judgment that an incomplete or piecemeal set of performance measures and benchmarks would fail to give the Commission the breadth of information necessary to protect consumers as required under §7-204(f) of the Public Utility Act and to monitor the competitive health of the market. Furthermore, we are concerned that the Joint Applicant's proposal gives the company too much latitude in determining which measurements and benchmarks are implemented. It is our finding that requiring the implementation of all 122 performance measurements, with the ability to waive the 300 day deadline, maintains the Commission's critical involvement in the process.

If the Joint Applicants fail to implement all 122 performance measurements, minus those waived by the Commission, within 300 days from the merger closing, they shall pay a $26.25 million penalty distributed to CLECs on the basis of access lines and $3.75 million to the Community Technology Fund described below. One hundred and fifty days after the Merger Closing Date, the Joint Applicants shall submit to the Commission for approval a written report detailing the timeline for implementing each of the performance measures, associated standards/benchmarks, and remedies, or an explanation of why SBC/Ameritech contend that implementation any particular measurement, standard/benchmark, or remedy is infeasible. The Commission may grant waivers from certain measurements, standards/benchmarks, and remedies, and shall determine the value of each missed measurement, and standard/benchmark in the event that SBC/Ameritech does not implement a particular measurement or standard/benchmark, or that it does not seek a waiver from such a requirement within 300 days of the Merger Closing Date. The Commission shall look to the Joint Applicants per measure cap as a guide for determining the value of each missed measurement and/or standard/benchmark. Liquidated damages for failure to implement the performance measures shall not exceed $90 million. (SBC/Ameritech, Attachments 1 and 2 to Proposed Order on Re-Opening, p. 9). Our interest is not to penalize the company but rather to have compliance with our order. We have left, largely intact, the Joint Applicants collaborative proposal for the implementation of performance measurements and it is our ardent hope that the process will be productive, cooperative, and result in a thorough set of performance monitoring tools. Thereafter, Joint Applicants shall still be liable for incident based liquidated damages up to an annual cap of $90 million.

Additionally, all performance measures must be based on comparison to performance that the Joint Applicants provide to their own operations and/or subsidiaries. The burden of proof shall remain on the Joint Applicants to demonstrate that no retail analogs exist and that benchmarks should be substituted. The Joint Applicants shall pay for a third-party auditor, retained by the Commission, to ensure accurate and reliable compliance with such processes. Joint Applicants shall issue quarterly performance monitoring reports on a carrier-by-carrier basis in accordance with commitments made to the FCC.

We note that the FCC likely will impose performance and liquidated-damages conditions of its own which, if they exceed the damages available under the Texas plan, would also be available to CLECs in Illinois to the extent of any overage. Thus, Illinois CLECs will have the best of both worlds. With the proper incentives in place, we can be reasonably assured that the conditions we impose will be fulfilled and that CLECs and end-users will reap the benefits.

i. Enforcement: Mechanisms

Reasonable and effective enforcement mechanisms for any condition imposed, including appropriate penalties, economic or otherwise. **(Question No. 12, Attachment A, of June 4, 1999 letter)**

Joint Applicants' Position

Joint Applicants state that they are prepared to implement a rigorous and comprehensive Compliance Program to verify and enforce the commitments they have made in reopening:

Enforcement Commitments

a. Joint Applicants would appoint a corporate officer to oversee implementation of, and compliance with, these commitments; to monitor Joint Applicants' progress toward meeting the deadlines specified herein; to provide periodic reports regarding Joint Applicants' compliance as required; and to ensure that any payments due under these commitments are timely made. The audit committee of SBC/Ameritech's Board of Directors would oversee the corporate compliance officer's fulfillment of these responsibilities.

b. No later than 6 months after the merger closing, and annually thereafter until the expiration of each of these commitments, Joint Applicants would file with the Commission, for the public record, a report detailing its compliance with these commitments. Joint Applicants would make a copy of its most current compliance report publicly available on their Internet site.

c. Joint Applicants would, at their own expense, annually engage independent auditors to verify SBC/Ameritech's compliance with these commitments. The first compliance review would be due 1 year after the merger closing and annual compliance reviews for a period of 3 years after the merger closing would be submitted. The independent auditor would have access to all of Joint Applicants' records, accounts, memoranda, and documentation necessary to evaluate Joint Applicants' compliance with these commitments. The independent auditor also may verify Joint Applicants' compliance through contacts with the ICC, the FCC, or Joint Applicants' wholesale customers, as appropriate. The Commission would have access to the working papers and supporting materials of the independent auditor. The independent auditor's review would be filed with the Commission for the public record. The review would address: the accuracy of the compliance report submitted by Joint Applicants during the period covered by the review and Joint Applicants' compliance with each of the commitments during the period covered by the review, to the extent that compliance is not addressed by Joint Applicants' compliance report. As filed with the Commission, the review report would include: (i) findings and exceptions of the independent auditor; (ii) the response of Joint Applicants to any exceptions of the independent auditor; and (iii) the reply of the independent auditor to the company's response.

d. Joint Applicants would agree that if the Commission makes a determination, after due process, that Joint Applicants have during the effective period of a commitment materially failed to comply with that commitment, the Commission may, at its discretion, extend the effective period of that commitment for a period that does not exceed the period during which Joint Applicants materially failed to comply with the commitment.

e. Joint Applicants would make payments due under these commitments within 10 business days of a determination by Joint Applicants' compliance officer, the Commission, or an arbitrator, that payment is due.

f. The specific enforcement mechanisms that would be established under these commitments would not abrogate, supersede, limit, or otherwise replace the Commission's enforcement powers under State law. Nor would the payments for non-performance specifically required by these commitments, to which Joint Applicants would voluntarily agree, be subject to

> statutory limitations on the size or type of awards that may be assessed by the Commission.
>
> ***For any and all proposed commitments made by the Applicants throughout their June 10, 1999 filing, what are the specific enforcement mechanisms which would be used by the Commission in the event of non-compliance with such commitments? (Item No. 12 (f); Attachment A-1; June 15, letter)***

Joint Applicants state that they have attempted to address the specific enforcement mechanisms appropriate to specific commitments throughout their testimony. In addition to the stated mechanisms, Joint Applicants note that the Commission retains its full authority over Joint Applicants to investigate and/or conduct hearings on any complaints of non-compliance. And in addition to its statutory enforcement mechanisms, the Post Exceptions Proposed Order identified an additional enforcement mechanism to ensure Joint Applicants full compliance with the commitments they have made in this docket, *i.e.*, an increase in the savings allocation flowed through to Illinois ratepayers.

Staff's Position

Staff concludes that Joint Applicants have been responsive to this question. However, Staff noted a possible inconsistency in the responses to questions 11 and 12 regarding the timelines for implementing the 79 performance measurements and for finishing the OSS integration process. (McClerren DOR, Staff Ex. 8.0 at 17-18).

As for question 12(f), Staff agrees with SBC's Mr. Kahan (SBC/Am. Ex. 1.3 at 23-25) that appointment of a corporate compliance officer would be a step in the right direction, but avers that such an appointment should by no means be the sole enforcement remedy available to the Commission. Staff notes that the PUA provides the Commission with the underlying legal authority to use certain enforcement mechanisms in the event of non-compliance with any commitments made by Joint Applicants, and that the Commission will retain all such authority post-merger.

Commission Analysis and Conclusion

Our conclusion here follows from our conclusion regarding question number 11 above. We find that the conditions set out here are adequate to safeguard our ability to monitor the Joint Applicants' performance and to protect consumers as we are bound to do under §7-204(f). Other mechanisms include all of the Commission's usual statutory enforcement tools, along with arbitration or other procedures where appropriate. Perhaps more important, Joint Applicants have agreed to various collaborative processes with Staff and CLECs, which should help identify and resolve (or at least narrow) disputes before formal litigation. For example, the proposal that Staff create a report describing which non-Illinois contractual terms and conditions should be available in Illinois should ease resolution of disputes in that area. As with question 11, then, Joint Applicants' commitments, as modified by the Commission, with respect to question 12 represents a procompetitive benefit to CLECs and end-users in Illinois that would not exist absent the merger.

j. Enforcement: Performance Reports

The manner, necessary actions and timetable by which Joint Applicants would create detailed performance monitoring reports to compare the provision of the following services to CLECs with internal performance standards: network performance, Operations Support Systems (OSS) and customer (i.e. CLEC) service. (Question No. 13; Attachment A; June 4 letter).

Joint Applicants' Position

Joint Applicants refer to their responses to question numbers 4 and 11 above.

On p. 36 of Exhibit 6 under commitment 10, the Applicants describe a report to the Commission Staff regarding transactions "affecting

> ***Illinois CLECs relative to their provision of service to end users in Illinois." It is unclear whether or not this report is intended to be responsive to Item 13 of the original Attachment A. If commitment 10 is the Applicants response to Item 13 from Attachment A, does this report meet the expressed goal of comparing service received by CLECs from the Applicants to service received by the Applicants as they provision it to themselves? What is the form of such reports as proposed by the Applicants? Please clarify. Additionally, how is the Commission to determine the "economic or technical" feasibility of these reports as discussed by the Applicants? Do the Applicants propose to determine this? If so, what remedy does the Commission have available if a CLEC demonstrates otherwise to the Commission in a formal proceeding? (Item No. 13 (g); Attachment A-1; June 15, letter)***

Joint Applicants state that Ameritech Illinois already provides to requesting CLECs reports that compare the service received by CLECs to the service provided by Ameritech Illinois to its retail end users where comparable tasks or functions are involved. These reports also compare Ameritech Illinois' performance in providing services to a particular CLEC with Ameritech Illinois' performance in providing the same services to all CLECs in the aggregate. Post-merger, Ameritech Illinois would continue to provide similar reports. However, Joint Applicants explain, those reports would be revised to reflect the additional performance measures Joint Applicants have committed to if the merger is approved and consummated. Joint Applicants did not intend to imply that the comparison would involve any aspect of CLEC service provision to their end user customers. With that clarification, Joint Applicants believe it is clear that their commitment is responsive to both items 11 and 13 of Attachment A to the June 4 letter.

Joint Applicants also explain that, after merger consummation, they will formulate a team of experts, which will have as its goal the implementation of all committed Standards/Benchmarks. This team will also determine what, if any Standards/ Benchmarks are economically or technically infeasible to implement given the network architecture and systems (including billing and ordering) of Ameritech Illinois. Such a determination will be made available and discussed with participants in the collaborative process discussed above. Joint Applicants have every expectation that any infeasibility determination will be understood and acceptable to collaborative participants, as was SBC's experience in a similar collaborative process in Texas.

Joint Applicants further state that if during the collaborative process any participant challenges an infeasibility conclusion by Joint Applicants and can demonstrate that the infeasibility conclusion was incorrect, Joint Applicants would reverse their conclusion and work to implement the Standard/Benchmark. If there are unresolved disputes between Joint Applicants and collaborative participants on the feasibility issue, these disputes would be resolved in one or more of the Section 252 arbitrations of an interconnection agreement by the Commission. In the event that an infeasibility issue has not been submitted in a Section 252 arbitration at the time a

dispute arises, Joint Applicants agree to have the issue decided by a third party arbitrator. Joint Applicants propose that the costs of the arbitrator be shared by Joint Applicants and the collaborative participants disputing the infeasibility claim. Based upon SBC's experiences in Texas and California, Joint Applicants expect there will be discussions and differences of opinion, but on the issue of infeasibility, participants in the collaborative will usually be convinced that one side or the other is correct and be able to move on to other issues.

Staff's Position

Staff does not cite any specific concern with Joint Applicants' response to this question, but emphasizes to the Commission that it does not favor forcing collaborative participants to pay for an arbitrator, as the cost may be prohibitive to smaller CLECs. Rather, Staff believes that the Commission should arbitrate disputes arising from the collaborative process.

Sprint's Position

Sprint argues that Joint Applicants' commitment to implement 79 of the 122 Texas performance measures in inadequate. Sprint contends that all 122 measures should be implemented as a "pre-merger" condition because all 122 are purportedly necessary to promote competition, and that, even if that does not occur, Joint Applicants should be required to specifically identify which 79 measurements will be implemented and to do so in far less than 300 days, which Sprint views as too lengthy a time period.

Nextlink's Position

Nextlink maintains that the Joint Applicants' commitments are insufficient and very vague. Nextlink states that it is unclear which of the standards will be offered in the initial 79 of the 122 that are proposed by SBC/Ameritech.

Nextlink maintains that the Commission should require SBC/Ameritech to implement in Illinois each and every Texas performance measurement, standard/benchmark and remedy, or a reasonable alternative if not technically feasible, within a date certain or face substantial financial penalties. Instead of a "collaborative process" in Illinois, Nextlink submits that SBC/Ameritech's implementation of these performance measurements, standards/benchmarks and remedies should be reviewed as a part of a compliance proceeding in which the Commission can develop a full record regarding technical feasibility if necessary and enforce the liquidated damages remedies to which SBC/Ameritech has committed if a Texas performance measurement and benchmark is adopted, as well as additional remedies if necessary.

Nextlink also maintains that SBC/Ameritech has made no commitment regarding what is to happen if an OSS performance measure, standard or benchmark is not technically feasible in Illinois, and states that it is not acceptable that once the determination of technical infeasibility is made, that the OSS and facilities performance

measure is then not implemented. Rather, and as a part of its recommended Commission compliance proceeding, in the event the Commission determines that a performance measure or standard/benchmark is not technically feasible, Nextlink states that SBC/Ameritech should be required to make such OSS and facilities performance measure technically feasible within a Commission prescribed period of time or pay Commission prescribed penalties unless SBC/Ameritech has implemented a reasonable alternative which has been approved by the Commission. Nextlink further states that the Commission should require independent, third party testing of the SBC/Ameritech OSS system.

Joint Applicants' Response

In response to parties that questioned why Joint Applicants have not specified which 79 performance measures will be imported from Texas, Mr. Dysart explained that SBC's limited knowledge of Ameritech Illinois's systems and processes limited its ability to specify benchmarks, but that SBC and Ameritech had agreed that at least 79 of the Texas performance measures would imported to Illinois with no questions of technical feasibility. This is the same approach adopted by the Ohio Commission, over the same type of assertions being made by CLECs here. Mr. Dysart added that Joint Applicants fully intend to implement as many of the Texas measurements as possible, hopefully all, and they would convene a joint task force to evaluate that issue within 60 days of the merger closing. This task force would identify any differences in Joint Applicants' legacy systems or processes that could make a measurement technically or economically infeasible in Illinois. Mr. Dysart added that performance measures that are found to be feasible would be provided on a rolling basis beginning 120 days after merger closing, which allows time both for the task force to evaluate the measurements and for the collaborative process with Staff and CLECs.

Regarding Mr. McClerren's concerns about a discrepancy between the timetables for OSS implementation and implementation of performance standards, Mr. Dysart stated that those are totally independent work efforts.

As for remedies for failure to meet performance standards, Joint Applicants state that the performance remedy plan agreed to in Texas will be made available to CLECs in Illinois through interconnection agreements, and that a $90 million cap on damages would apply, based on the number of access lines in Illinois as compared to Texas (which has a $120 million cap).

3. Commission Analysis and Conclusion

We conclude that all 122 performance measurements and benchmarks contained in the “Texas” plan are necessary to adequately shield consumers under our authority in §7-204(f) and to encourage competition in the marketplace. The implementation of all 122 measurements and benchmarks represents a substantial improvement over the status quo in Illinois, and will have procompetitive benefits for CLECs and end-users in Illinois that would not exist absent the merger. The procedures to implement this commitment are reasonably quick, and the incentives we have imposed are adequate to produce useful and necessary tools for monitoring the competitiveness of the market. These measurements, third-party auditing, and regular reporting satisfy our concerns regarding tracking the merger’s potential impact on consumers.

Finally, the Commission notes Joint Applicants’ commitment to issue monthly performance reports to Staff regarding OSS (See Kahan Direct, SBC/Ameritech Ex.1.3, Attachment 1). We would also like to highlight the performance monitoring reports which the Joint Applicants have committed to make available to the FCC and state Commissions (See Kahan Rebuttal, SBC/Ameritech Ex. 1.5, Attachment 1). These performance monitoring reports only provide information regarding the Joint Applicants provisioning of service to CLECs as a group. Since we are interested in overseeing Joint Applicants’ provisioning of CLECs on an individual basis, we order such monthly performance monitoring reports made to this Commission, as well as all website information, be made available on a disaggregated CLEC-by-CLEC basis.

IV. ADDITIONAL COMMITMENTS BY JOINT APPLICANTS

In response to questions and concerns raised by the Chairman’s various letters, Joint Applicants proffered the additional commitments described below. SBC states that its ability to make these commitments is based on the premise that no other material conditions will be imposed that would have the effect of reducing the resources necessary for SBC and Ameritech to meet these commitments. For example, if the Commission were to condition the merger on an increase in the PEPO's flow-through of merger savings, the additional commitments listed here may no longer apply because the Commission would be taking away the resources that would otherwise be available to meet those commitments.

A. Illinois Headquarters Commitment. For not less than 5 years following the Merger Closing Date, SBC/Ameritech agree to maintain Ameritech Corporation headquarters and an Ameritech Illinois state headquarters in Illinois that is staffed sufficiently to at least maintain Ameritech Illinois' current local presence with government entities and community organizations.

B. Ameritech Illinois Employee Commitment. SBC/Ameritech agree that, at the end of 2 years following the

Merger Closing Date, the number of full-time equivalent employees of Ameritech Illinois will be more than the greater of 1) the number of such employees as of the date the Commission enters a final appealable order approving the Merger, or 2) the number of such employees as of the Merger Closing Date.

C. Consumer Education Fund Commitment. SBC/Ameritech will establish, within 3 months after the Merger Closing Date, a Consumer Education Fund ("CEF") and will make $1 million available to the CEF for disbursement by Ameritech Illinois in each of the three consecutive 12-month periods following the date the CEF is established, for a total of $3 million. All allocated funds will remain available to the CEF for the purposes described herein until they are disbursed. Funds shall be allocated to the CEF by Ameritech Illinois, and the use of the funds will be controlled by the CEF Committee. The Committee shall consist of one voting representative each from Ameritech Illinois, Commission Staff, and such other entities as appointed by the Commission, and shall make decisions by majority vote. Tie votes, if any, will be decided by the Commission Staff representative. CEF Committee decisions as to how funds should be distributed and expended are subject to Commission review. At its first meeting, the Committee shall establish rules of governance for the operation of the Committee. No funds shall be disbursed until 30 days after the committee files with the Commission a report of such proposed expenditures

D. Community Technology Fund Commitment. SBC/Ameritech will establish, within 3 months of the Merger Closing Date, a Community Technology Fund ("CTF") and will make $1 million available to the CTF for disbursement by Ameritech Illinois in each of the three consecutive 12-month periods following the date the CTF is established, for a total of $3 million. All allocated funds will remain available to the CTF for the purposes described herein until they are disbursed. Funds shall be allocated to the CTF by Ameritech Illinois, and the use of the funds will be controlled by the CTF Committee. The Committee shall consist of one voting representative each from Ameritech Illinois, Commission Staff, and such other entities appointed by the Commission, and shall make decisions by majority vote. Ties votes, if any, will be decided by the Commission Staff representative. CTF Committee decisions as to how funds should be distributed and expended are subject to Commission review as described below. At its first meeting, the Committee shall establish rules of governance for the operation of the Committee. Additional volunteer committee members, with full voting rights (except the

right to choose additional members), can be selected by unanimous agreement of Ameritech Illinois, Commission Staff and other members. Except for program design and implementation expenses not to exceed $50,000 annually as set forth below, no funds shall be disbursed until 30 days after the committee files with the Commission a report of such proposed expenditures. The CTF shall be dedicated to uses which help assure that rural and low income areas in Illinois have access to advanced telecommunications technology. Such uses may include expenditures for computer equipment and associated software, Ameritech tariffed services, Internet access, technical support, program design and implementation expenses not to exceed $50,000 annually (which amount shall be disbursed to the CTF upon its request, with all expenditures to be reported annually to the Commission), and other associated services and equipment in rural and low income communities. The Commission Staff shall work closely with the CTF committee in implementing this fund and to establish criteria and standards to be used in awarding funds to ensure that it is not administered in a way which has an anti-competitive effect.

SBC/Ameritech will also provide funding of $750,000 in the first year following the Merger Closing, and $350,000 per year for two additional years thereafter, to support a Community Computer Center.

E. Charitable Contributions Commitment. SBC/Ameritech will make philanthropic and community contributions in Illinois in the aggregate of more than $4 million in each of the three consecutive 12 month periods following the Merger Closing Date. Illinois-based employees of SBC/Ameritech will continue to have input regarding the beneficiaries of these contributions.

F. ADSL Deployment. SBC/Ameritech commit that in the event ADSL service is offered as a service to residence customers in any Ameritech Illinois central office, then ADSL service will be offered to residence customers in any other Ameritech Illinois central office where ADSL is subsequently deployed. SBC/Ameritech intend that any deployment of ADSL in Illinois will be done in good faith in a non-discriminatory fashion without excluding any particular area of the Ameritech Illinois service area.

Staff's Position

Staff witnesses Jackson and Marshall testified regarding Joint Applicants' additional Illinois-specific commitments. Ms. Marshall noted that commitments A., B., E., and F. did not, in her opinion, effect any change to the status quo prior to reopening, and therefore did not create any "increased benefit" to consumers. With regard to the CEF and CTF, Ms. Marshall stated that it would be inappropriate and discriminatory to force ratepayers to bear the costs of such special interest funds. She therefore recommended that none of the costs of these funds be netted against merger savings, in which case she would have no objection to establishing the funds.

Ms. Jackson took no position on the CEF and CTF commitments, though she believed that they are a step in the right direction to establish that the merger will benefit Illinois consumers. She did, however, ask a number of clarifying questions of Joint Applicants. With regard to the CEF, for example, she expressed a concern that the fund not be used as a marketing tool and also asked Joint Applicants to explain the Commission's role in reviewing expenditures and providing input on the type of educational materials distributed to the public. She also asked whether Joint Applicants would use an independent third party to design the materials and marketing plan for the CEF. With regard to the CTF, Ms. Jackson asked for clarification of the Commission's role in reviewing how funds are distributed or deciding the type of equipment to be used. She also sought more detail on how the CTF would help rural and low-income areas. She similarly asked for more detail on the operation of the Community Computer Center.

DSSA's Position

DSSA and Neighborhood Learning Networks presented testimony on the CEF and CTF and other issues. DSSA witness Samuelson stated that the CTF should have four major initiatives: educating various "disadvantaged" markets regarding the benefits of the Internet and other advanced telecommunications services; funding public technology initiatives; funding community technology centers; and creating Illinois subsidiaries to implement the National-Local Strategy, to develop advanced telecommunications services, and to commercialize public technology initiatives. Mr. Samuelson stated that some of these initiatives could be modeled on existing initiatives at the national level. Mr. Samuelson further stated that, properly funded, the CEF proposed by Joint Applicants is an excellent start.

Joint Applicants' Response

Responding to Staff witness Jackson's desire for more detail about the operation of the CEF and CTF, Joint Applicants explain that their commitments are based on approved commitments in Ohio and establishes a framework to answer her questions. They further state that they would have no objection to the Commission more clearly delineating the role it envisions for itself and Staff in this area, but that they did not want to presume to dictate those matters.

With regard to DSSA's testimony, Joint Applicants again explain the extent of their commitments, which they believe will help disadvantaged and underserved markets. They add that they have tried to make commitments that provide flexibility in the use of the public-interest funds, and that actual disbursement and operations issues should be determined outside this docket. As for DSSA's request to locate certain subsidiaries in Illinois, Joint Applicants state that their commitment to maintain employment levels and the location of Ameritech headquarters addresses any concerns about a possible loss of jobs. The other subsidiaries DSSA refers to are either already established elsewhere or at a stage where it would be premature to determine a specific location, though Illinois remains a candidate.

Commission Analysis and Conclusion

The additional Illinois-specific commitments proposed by Joint Applicants were not necessary as a response to the questions in the June 4, June 15, and July 9 letters. We therefore accept the commitments, which we believe represent a significant benefit to Illinois that would not exist absent the merger, but have no reason to specifically rule on their details, which in any event will need to be worked out over time. With regards to the CEF and CTF, we agree with Staff that it would be inappropriate and discriminatory for ratepayers to bear the costs of these special interest funds. Therefore, we conclude costs associated with these funds should not be netted against merger savings or otherwise recovered from ratepayers. With regard to the CEF, we also conclude that this fund should not be used as a marketing tool.

V. PROPOSED FCC CONDITIONS AND THE JULY 9 LETTER

Joint Applicants' Position

Joint Applicants take the position that the proceedings at the FCC and in Illinois are distinct and separate and that it is not appropriate to litigate FCC issues in this case. They further note that the proposed FCC conditions are not yet final, and may well be modified or rejected by the FCC itself. Nevertheless, Joint Applicants attached a copy of the proposed FCC conditions to Mr. Kahan's Rebuttal Testimony on Reopening, and cross-examination on those conditions was conducted per the Chairman's direction.

Mr. Kahan and the other witnesses for Joint Applicants emphasized that the proposed FCC conditions and the proposed Illinois commitments are complementary and that nothing proposed to the FCC takes away from any of the Illinois commitments. In fact, if the FCC adopts the proposed conditions, they will be effective in Illinois, subject to this Commission's jurisdiction. In other words, any conditions imposed in this proceeding would apply first, after which parties could refer to the FCC conditions for any additional, incremental requirements. There also may be instances where the proposed FCC conditions impose a requirement that has no counterpart in the Illinois conditions, thereby providing an additional benefit to Illinois.

Joint Applicants explain that even though the proposed FCC conditions would apply in Illinois if adopted by the FCC, there is no need for this Commission to adopt such conditions. Significantly, however, Joint Applicants do not object to the Commission taking the substantive provisions of the FCC proposals (Sections I-VI, VIII-IX, XI-XV, XVII-XX, and XXIV) and incorporating them into the Commission's Order, provided that the conditions are not modified in any material way other than to make them Illinois-specific and ensure that Joint Applicants would not be subject to duplicative payments or damages under the FCC and Illinois requirements. Joint Applicants added that their respective boards of directors would, of course, have to make a final evaluation of any package of conditions imposed by the Commission.

> ***In Section I of SBC/Ameritech's July 1 FCC Ex Parte filing, SBC/Ameritech have committed to the FCC to implement a "Federal Performance Parity Plan" ("FCC performance plan") upon consummation of the transaction. If the FCC were to adopt the voluntary commitments of SBC/Ameritech, how would the FCC performance plan affect the commitments reflected in SBC/Ameritech's testimony on re-opening to implement certain OSS and facilities performance measurements ("Illinois plan")? If the FCC were to adopt the voluntary commitments of SBC/Ameritech, what overlap, if any, would there be in terms of benchmarks, liquidated damages payments, and compliance oversight between the Illinois and FCC performance plans? Also, please explain why the proposed FCC performance plan would extend for three years, while the Illinois plan as proposed extends for only 300 days.*** **(Question No. 1; July 9 letter)**

Joint Applicants' Response - Question No.1

Joint Applicants explain that the FCC performance plan most closely mirrors the liquidated damage remedy plan included as part of the commitments made to Illinois in Mr. Dysart's testimony and, most particularly, in Attachment 2 to Mr. Dysart's Direct Testimony on Reopening. That Attachment is based on a program of liquidated damages that has been offered in Texas and that SBC has committed to implement in all new interconnection agreements in Illinois and in any existing interconnection agreements upon the request by the CLEC.

Under the FCC performance plan as it impacts the Illinois commitments, payments would be made under the Illinois commitments, assuming the Illinois Commission includes them as proposed in its final Order. Thus, for CLECs operating in Illinois, payments would first be made to the CLECs under the Illinois plan up to the Illinois cap, and then be made to CLECs under the FCC performance plan up to the Tier 1 federal cap if it exceeds the Illinois cap. If the state plan requires assessments to the state -- as the Illinois commitment would -- then, similarly, payments would be made to a public interest fund designated by the State of Illinois under the state plan up to the Illinois cap, and then to the federal public interest fund up to the Tier 2 federal cap to

the extent that it exceeds the Illinois cap. (Based on Mr. Dysart's Rebuttal Testimony on Re-Opening, the Illinois cap would be approximately $90 million, based on the relative number of access lines in Texas (approximately 9.8 million) and in Illinois (approximately 6.5 million)). Were Illinois to forego the state assessments, then payments would be made to the federal public interest fund under Tier 2 of the federal plan, assuming SBC is not providing parity or benchmark performance for three months in a row or more than six months in any calendar year. Finally (although this does not directly impact Illinois), if SBC is not providing parity or benchmark performance for three months in a row or more than six months in any calendar year, it must pay into the federal public interest fund under Tier 3 of the FCC performance plan in any event.

In short, in each instance, CLECs would pursue any remedies available to them under Illinois-ordered conditions to the full extent of those remedies. If the remedies available to a CLEC in Illinois are less than what the CLEC would be entitled to in Illinois as a result of the FCC conditions, the CLEC would be entitled to pursue its FCC remedy for any overage.

Joint Applicants also assert that if the FCC adopted SBC/Ameritech's proposal as submitted and this Commission adopted Joint Applicants' commitments, there would be a great deal of overlap in the substance of the federal and state benchmarks. The twenty federal benchmarks are designed to capture the most critical, customer-impacting elements of the 122 Texas benchmarks. If Illinois ultimately adopts most or all of the 122 benchmarks (subject to technical feasibility issues and consistent with the terms and conditions of Joint Applicants' commitment), it will be adopting the substance of the 20 federal benchmarks. Alternatively, if Illinois were simply to adopt the 20 federal benchmarks, of course, the overlap would be exact.

Joint Applicants contend that a comparison of the proposed FCC performance plan's three-year timeline and the Illinois 300 day timeline is not really appropriate. The three-year period referenced in the FCC proposal is a period of time beginning nine months after closing during which the FCC performance plan will be in force. The 300 days in Joint Applicants' Illinois commitments is the period of time during which Ameritech Illinois will implement at least 79 of the 122 benchmarks.

Joint Applicants believe that it would be more appropriate to compare the 300 days after closing that Joint Applicants have proposed for coming into substantial compliance with the benchmarks in Illinois with the nine months (approximately 270 days) that SBC/Ameritech have to come into substantial compliance with the FCC performance plan. Similarly, while the three-year clock begins to run for the FCC performance plan only after nine months, the three-year timeline for the Illinois commitments begins at closing. In essence, the Illinois Commitment will begin one month later and end nine months earlier than the federal proposal. However, Joint Applicants explain that during both the first one month and last nine months, CLECs will have full access to the FCC proposal and remedies.

In Attachment A to SBC/Ameritech's July 1 FCC Ex Parte filing, SBC/Ameritech commit to provide the FCC and CLECs with certain forms of performance measurement results, on a quarterly basis, cataloging SBC/Ameritech's provision of service to the aggregate of all CLECs in each of SBC/Ameritech's states. If the FCC were to adopt the voluntary commitments of SBC/Ameritech, would the Illinois Commerce Commission have equal access to this data? If not, why not? (Question No. 2; Attachment A-2; July 9 letter)

Joint Applicants' Response - Question No. 2

Joint Applicants' answer is Yes. As explained in Paragraph 1 of Attachment A to the July 1, 1999 *Ex Parte* letter filed by SBC and Ameritech with the FCC:

> SBC/Ameritech shall provide the Commission with performance measurement results, on a quarterly basis, demonstrating SBC/Ameritech's monthly performance provided to the aggregate of all CLECs in each of SBC/Ameritech's 13 states. SBC/Ameritech shall also provide the Commission with access to SBC/Ameritech's Internet website, where the Commission can obtain performance measurement results demonstrating SBC/Ameritech's monthly performance provided to the aggregate of all CLECs. SBC/Ameritech shall provide the CLECs with access to SBC/Ameritech's Internet website, where each CLEC can obtain performance measurements demonstrating SBC/Ameritech's monthly performance provided to it on an individual basis, and to the aggregate of all CLECs.

Joint Applicants would make this same data available to this Commission by providing this Commission with access to the same Internet website.

In Section III of SBC/Ameritech's July 1 FCC Ex Parte filing, SBC/Ameritech have committed to the FCC to implement an OSS Process Improvement Plan (the "FCC OSS plan"). This 3 phase FCC OSS plan seems to closely mirror the commitments reflected in SBC/Ameritech's testimony on re-opening. Further, the FCC OSS plan calls for a "single workshop" to work collaboratively with CLECs under the ultimate direction of the Chief of the Common Carrier Bureau of the FCC. If the FCC were to adopt the voluntary commitments of SBC/Ameritech, how would the FCC OSS plan overlap with the proposal put forth here in Illinois? If the FCC were to adopt the voluntary commitments of SBC/Ameritech, do SBC/Ameritech envision that the FCC OSS plan is controlling over Illinois or takes the place of the commitments reflected in their testimony on re-opening? Please explain. (Question No. 3; Attachment A-2; July 9 letter)

Joint Applicants' Response - Question No. 3

Joint Applicants state that if the FCC proposal is not adopted, the commitment made for an Illinois collaborative process will remain in place and will control.

Joint Applicants further state that if the FCC adopts SBC/Ameritech's proposals as submitted and the Commission adopts Joint Applicants' commitments, there would be overlap between the collaborative processes pursued by the FCC and by the Commission. The most important difference is that the FCC OSS process is targeted at creating uniform standards for the entire SBC/Ameritech 13-state region for the application-to-application interfaces, graphic user interfaces, and common business rules for pre-ordering, ordering, provisioning, maintenance and billing issues to be discussed in the collaborative process.

While Joint Applicants do not believe that the FCC OSS process is controlling over Illinois, Joint Applicants believe that, once an FCC Order and an ICC Order are in place, it would make sense to consult among the FCC Commission Staff, the ICC Commission Staff and affected CLECs to determine the most efficient way to proceed with each collaborative process. To the extent that collaborative issues overlap between the FCC and ICC collaborative processes, Joint Applicants believe it will be more efficient for all parties involved to pursue an issue only at the FCC level and thereby ensure not only the development of acceptable standards, but also uniform standards across the entire SBC/Ameritech region. For example, one goal of the FCC OSS process is the development of uniform business rules so that a CLEC can administer its OSS relationships consistently across the SBC/Ameritech region. Joint Applicants believe that development of state-specific rules would be counterproductive to the FCC's goal.

In Section VIII of SBC/Ameritech's July 1 FCC Ex Parte filing, SBC/Ameritech have committed to implementing shared transport in current Ameritech states. Is this proposal to the FCC the same as the commitments reflected in SBC/Ameritech's testimony on re-opening regarding shared transport? Please explain. (Question No. 4; Attachment A-2; July 9 letter)

Joint Applicants' Response - Question No. 4

The Joint Applicants' answer is that the two commitments are the same, except for a minor difference in timing. Specifically, the shared transport commitment as proposed to the FCC calls for the offering of the interim shared transport product no later than the time of the merger closing, while the shared transport commitment in Illinois calls for the offering of that product within 30 days of the merger closing. If the FCC proposal is adopted by the FCC, the same timetable would apply in Illinois.

Additionally, Joint Applicants have made no commitment in Illinois to provide the UNE platform to customers. However, at the FCC, SBC/Ameritech have proposed to make the UNE platform available to residential customers within 30 days after the merger closing subject to certain term and volume limits. If that proposal is adopted by the FCC, it would apply in Illinois.

5) ***In Section XXV of SBC/Ameritech's July 1 FCC Ex Parte filing, SBC/Ameritech have stated that if conditions imposed in connection with the merger under state law grant "similar rights" against SBC/Ameritech to the conditions volunteered to the FCC, affected parties shall not have a right to invoke overlapping aspects of federal and state conditions. If the FCC were to adopt the voluntary commitments of SBC/Ameritech, please explain the legal and practical implications of this statement as they relate to the commitments reflected in SBC/Ameritech's testimony on re-opening. (Question No. 5; Attachment A-2; July 9 letter)***

Joint Applicants' Response - Question No. 5

Joint Applicants respond by referring to Paragraph 69 of the Proposed FCC conditions, which states as follows:

> The Commission recognizes that various offerings and initiatives required by these Conditions, including but not limited to the carrier-to-carrier promotions, OSS requirements, and performance monitoring conditions, may substantially duplicate requirements imposed in connection with the merger under state law. These Conditions shall supplement, but shall not be cumulative of, substantially related conditions imposed under state law. Where both these Conditions and conditions imposed in connection with the merger under state law grant parties similar rights against SBC/Ameritech, affected parties shall not have a right to invoke the relevant terms of these Conditions in a given state if they have invoked a substantially related condition imposed on the merger under state law. For example, carriers requesting unbundled local loops for residential service under promotional terms offered pursuant to state approval of the merger would not also be able to

> invoke the promotional discounts on unbundled loops required by these Conditions. Furthermore, any unbundled local loops provided by SBC/Ameritech for residential service under a substantially similar merger-related PUC imposed promotion in a given state would be deducted from the number of unbundled local loops required to be provided in that State under Paragraph 49 of these Conditions. This Section shall not limit the Commission's powers to enforce these Conditions or the reporting requirements of SBC/Ameritech under these Conditions.

By this answer, Joint Applicants state that they intend simply to ensure that the commitments that they have made to states like Illinois are complementary to and not cumulative of conditions that have been proposed to the FCC. In other words, if the Illinois Commission were to adopt an FCC condition as offered in Mr. Kahan's Rebuttal Testimony on Re-Opening (the unbundled loop discounts is an example), what the Illinois Commission ordered would be counted as part of and not in addition to the FCC condition.

The FCC conditions do not supplant this Commission's powers in any way. Throughout the conditions, state authority is preserved. (See, e.g., Conditions ¶ 24 (loop conditioning pricing); ¶ 29 (advanced services approvals); ¶ 44 (pricing); ¶ 60 (Lifeline plans); ¶ 69 (duplication of state conditions); Attach. A ¶2 (performance monitoring)). The Conditions are intended to support and supplement actions taken by this Commission. They do not and could not affect the jurisdictional balance between this Commission and the FCC. Paragraph 69, as it is currently written, reflects the principle that if this Commission imposes merger conditions, Illinois should get the benefit of any provision in the FCC Conditions that, in the opinion of this Commission, is more favorable, but that the FCC and the Illinois conditions, and the remedies therein contained, should not be duplicative.

Commission Analysis and Conclusion

While we recognize the Joint Applicants' willingness to abide by the substantive provisions of their proposed FCC commitments in Illinois, we do not find it necessary to impose such requirements as conditions of this Order. There is no guarantee that the FCC will adopt all of the conditions as proposed. We will simply take note of the FCC conditions and Joint Applicants' assurance that those conditions, if adopted, will apply in Illinois and will be treated as incremental to the Illinois conditions.

VI. CONDITIONS TO APPROVAL OF THE REORGANIZATION

A. Introduction

The record in this cause, taken together with our analyses in other sections of this Order, reveals that conditions to our approval need to be imposed in order to protect the interests of the Company and its customers.

Many of these conditions are the result of commitments made by the Joint Applicants in the course of this proceeding. While certain of these might be beyond our jurisdiction to impose, we have accepted and relied to some degree on these commitments. Some of the other conditions arise from our reasoned judgment on how to make the Section 7-204(b) findings truly meaningful. Another condition is based on our belief that compliance with outstanding Commission Orders is so basic an interest that it can and should be addressed as part of this Order. Finally, some of the many conditions here proposed have not been adopted primarily for the reason that they either relate to matters beyond our jurisdiction or lie outside the scope of this proceeding.

The record contains assurances that not only will the reorganization not diminish the Company's ability to provide service but that it will enable AI to improve the quality of service it provides. The record also contains assurances that the proposed reorganization is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction, but that it will enhance and promote local exchange competition. We will hold the Joint Applicants to those assurances, and in doing so, we require the Joint Applicants to comply with all of the conditions set forth herein. Except where other termination dates are specifically established, all conditions set out below shall cease to be effective and shall no longer be binding in any respect three years after the Merger Closing Date. Merger Closing Date means the day on which, pursuant to their Merger Agreement, SBC and Ameritech cause a Certificate of Merger to be executed, acknowledged and filed with the Secretary of State of Delaware as provided in Section 251 of the Delaware General Corporation Law, as amended.

B. Conditions:

(1) Headquarters - For not less than five years following the Merger Closing Date, SBC/Ameritech will maintain Ameritech Corporation headquarters and an Ameritech Illinois state headquarters in Illinois staffed sufficiently to maintain Ameritech Illinois' current local presence with government entities and community organizations;

(2) Name - SBC will continue to use the Ameritech name in each state of the Ameritech region;

(3) Charitable Contributions - SBC/Ameritech will continue Ameritech Illinois' historic levels of charitable contributions and community activities and will continue to support economic development and education consistent with AI's established commitments. More specifically, SBC/Ameritech will make philanthropic and community contributions in Illinois in the aggregate of more than $4,000,000 in each of the three consecutive 12-month periods following the Merger Closing Date;

(4) Development - SBC will continue to support the economic development and education in Ameritech's regions consistent with Ameritech Illinois' well established commitments in these areas.

(5) Employment - SBC will ensure that, as a result of the proposed reorganization, employment levels in Ameritech's regions will not be reduced due to this transaction;

(6) Ameritech Illinois' Employee Commitment - At the end of two years following the Merger Closing Date, the number of full-time equivalent employees of Ameritech Illinois will be more than the greater of 1) the number of such employees as of the date the Commission enters a final appealable order approving the Merger, or 2) the number of such employees as of the Merger Closing Date;

(7) Network Infrastructure Investment - AI shall renew and extend the five-year network infrastructure modernization program previously established in its Alt. Reg. Plan. The investment shall total at least $3 billion subject to adjustment in the Commission's subsequent review of the AI Alt. Reg. Plan. The five-year extension shall commence in the year 2000 or in the first calendar year following the merger closing date. AI will retain the flexibility to structure and apportion the total network investment over the five-year period.

AI shall prepare and file an annual report, in sufficient detail, to allow the Commission to determine whether and how the investment was made, whether it serves to maintain the quality of AI's network, and whether the investment is in the interest of all of AI's customer classes. The report shall be examined by the Commission and audited with the assistance of a independent third party selected by the Commission and paid for by AI. Each report must be expressly approved by the Commission. If the Commission rejects a submitted report, AI shall provide any supplemental information necessary to satisfy the reports short comings. The report shall be filed each year for five years, but may be eliminated either upon application or the Commission's Own Motion if the network infrastructure investment has been completed before the end of the five-year period and the reporting requirement is found no longer necessary to protect the interest of AI's customers.

(8) Consumer Education Fund - SBC/Ameritech will establish, within three months after the Merger Closing Date, a Consumer Education Fund ("CEF") and will

make $1 million available to the CEF for disbursement by Ameritech Illinois in each of the three consecutive 12-month periods following the date the CEF is established, for a total of $3 million. All allocated funds remain available to the CEF for the purposes described herein until they are disbursed. Funds shall be allocated to the CEF by Ameritech Illinois, and the use of the funds will be controlled by the CEF Committee. The Committee shall consist of one voting representative each from Ameritech Illinois, Commission Staff, and such other entities as appointed by the Commission and shall make decisions by majority vote. Tie votes, if any, will be decided by the Commission Staff representative. CEF Committee decisions as to how funds should be distributed and expended are subject to Commission review. At its first meeting, the Committee shall establish rules of governance for the operation of the Committee. No funds shall be disbursed until 30 days after the committee files with the Commission a report of such proposed expenditures. Payments made under this subsection should not be included in the revenue requirement or costs studies of Ameritech Illinois;

(9) Community Technology Fund - SBC/Ameritech will establish, within three months of the Merger Closing Date, a Community Technology Fund ("CTF") and will make $1 million available to the CTF for disbursement by Ameritech Illinois in each of the three consecutive 12-month periods following the date the CTF is established, for a total of $3 million. All allocated funds remain available to the CTF for the purposes described herein until they are disbursed. Funds shall be allocated to the CTF by Ameritech Illinois, and the use of the funds will be controlled by the CTF Committee. The Committee shall consist of one voting representative each from Ameritech Illinois, Commission Staff, and other entities appointed by the Commission and shall make decisions by majority vote. Tie votes, if any, will be decided by the Commission Staff representative. CTF Committee decisions as to how funds should be distributed and expended are subject to Commission review as described below. At its first meeting, the Committee shall establish rules of governance for the operation of the Committee. Additional volunteer committee members, with full voting rights (except the right to choose additional members), can be selected by unanimous agreement of Ameritech Illinois, Commission Staff and other members. Except for program design and implementation expenses not to exceed $50,000 annually as set forth below, no funds shall be disbursed until 30 days after the committee files with the Commission a report of such proposed expenditures. The CTF shall be dedicated to uses which help assure that rural and low income areas in Illinois have access to advanced telecommunications technology. Such uses may include expenditures for computer equipment and associated software, Ameritech tariffed services, Internet access, technical support, program design and implementation expenses not to exceed $50,000 annually (which amount shall be disbursed to the CTF upon its request, with all expenditures to be reported annually to the Commission), and other associated services and equipment in rural and low income communities. The Commission Staff shall work closely with the CTF committee in implementing this fund and to establish criteria and standards to be used in awarding funds to ensure that it is not

administered in a way which has an anti-competitive effect. Payments made under this subsection should not be included in the revenue requirement or costs studies of Ameritech Illinois;

(10) Community Computer Center - In conjunction with the Community Technology Fund, SBC/Ameritech will also provide funding of $750,000 in the first year following the Merger Closing, and $350,000 per year for two additional years thereafter, to support a Community Computer Center. Payments made under this subsection should not be included in the revenue requirement or costs studies of Ameritech Illinois;

(11) OSS Reports - AI will submit monthly OSS performance results to Staff for UNEs, resale and OSS (*see also* condition No. 30 below);

(12) LRSIC & TELRIC - AI will file revised LRSIC, TELRIC and shared and common cost studies with the Chief Clerk of the Commission within six months after the last regulatory approval of the proposed reorganization. It is noted that Staff is willing to work with AI to establish a priorities list for such updates. The Commission will utilize the updated studies in its analysis of the Company's request for rate rebalancing and in the two TELRIC investigations;

(13) Cellular Notification - The Joint Applicants will provide the requisite notice to affected cellular customers regarding the pending merger and sale of the cellular property in compliance with Staff’s recommendation. They also should afford the purchaser the opportunity to participate in the specifics of such notice;

(14) 9-1-1 - AI shall obtain Commission approval before implementing any operational charge to its current 9-1-1 system that are attributable to or in connection with the merger. This includes, but is not limited to, changes in policies, processes, and procedures associated with 9-1-1 billing systems and databases. Any operational changes to be implemented shall be transparent to both the 9-1-1 system and its subscribers.

(15) Access to Books and Records - The Joint Applicants agree that Staff will have access to all books and records of SBC and Ameritech Corporation and their utility and non-utility parent, sister and subsidiary companies, as well as independent auditors' workpapers on the same terms as those set forth in the Commission's Orders approving the reorganization of Consolidated Communications in the Order in Docket 97-0300 (dated September 24, 1997) and the Gallatin River exchanges of Sprint Communications in the Order in Docket 97-0321 (dated October 21, 1998);

(16) CAM -

(a) Revisions - The Joint Applicants agree that Ameritech Illinois will file revisions to Cost Allocation Manuals ("CAM") within sixty (60) days of the

date of receipt of the last regulatory approval required for the proposed merger;

(b) AIA - The Joint Applicants will provide Staff with a copy of each affiliate service agreement and the relevant updated CAM pages to resolve any cost allocation issues in a complete and timely manner;

(c) Updates - The Joint Applicants will continue to provide Staff with any and all relevant updates to the CAM before providing service under any new or revised affiliate agreements;

(d) Personnel Training - Applicants agree to inform all relevant company personnel that the CAM has been revised, provide easy access to the revised manual and train personnel as to its proper application;

(e) Third-party Audit - Conditions concerning updated CAMs are to be complied with by the Joint Applicants and reviewed and audited by the Commission, with the assistance of an independent third party selected by the Commission and paid for by the Joint Applicants.

(17) TRI - The Joint Applicants agree to use Technology Resources, Inc. ("TRI") to work on accessibility issues for people with disabilities in Illinois.

(18) Universal Design - The Joint Applicants agree to implement SBC's Universal Design Policy in Illinois for people with various disabilities to provide input on telecommunications accessibility, service, features and design. We require Annual Reports on the details of enforcement;

(19) "Best Practices" Report - The Joint Applicants agree that AI will provide, for a period of up to five years (with 3 years mandatory and 2 years conditioned) after the Merger Closing Date, a confidential Annual Report in which it identifies any proposed "best practices" whose adoption by SBC or its affiliates would affect the provisioning of intrastate telecommunications in Illinois.

This report shall be prepared and filed in the same fashion as other required annual reports and shall be subject to the same Commission review process. (See e.g. Condition No. 7 of this Part). Upon application of AI or on the Commissions Own Motion after 3 years and based on a finding that the reporting requirement is no longer necessary to protect the interests of AI and its customers, the reporting requirement may be eliminated.

(20) ADSL Deployment - In the event ADSL service is offered by AI as a service to residence customers in any Ameritech Illinois Central Office, then ADSL service will be offered to residence customers in any other Ameritech Illinois Central Office where ADSL is subsequently deployed. Any deployment by Joint Applicants of ADSL in Illinois will be done in good faith in a non-discriminatory

fashion without excluding any particular area of the Ameritech Illinois service area;

(21) National-Local Subsidiary - Joint Applicants will not seek local exchange certification for their National-Local Subsidiary in Illinois prior to January 1, 2003;

(22) Section 251 - Joint Applicants will meet with Staff within 30 days of the Merger Closing Date to address any current issues Staff may have regarding Section 251. In addition, Joint Applicants shall meet with Staff on a quarterly basis to address any Section 251 concerns that may arise over time;

(23) OOS>24 - The Joint Applicants shall utilize the six month period following the Merger Closing Date to reach compliance with the OOS>24 hours standard. Fifteen days subsequent to the six month period, AI shall demonstrate to this Commission that it met the OOS>24 hours quality standard for the final month of the six month period designated above. The demonstration shall consist of the same process currently employed to measure OOS>24 hour compliance.

In the event that AI fails to demonstrate its compliance with the OOS>24 service quality standard for the final month of the six month period, the Commission shall assess a penalty of $15 million. This penalty is independent of any rate reductions which might be assessed under the Alt Reg Plan. In each subsequent full calendar year period, AI shall demonstrate to the Commission its compliance with the OOS>24 hour service quality standards or be subject to the assessment of a $30 million penalty. This penalty is independent of any rate reductions which might be assessed under the Alt Reg Plan. The Commission notes that if Ameritech Illinois fails to comply within the six month period and the full calendar year 2000, and the timeframes overlap in 2000, the $30 million assessment will be pro rated to avoid double counting. This penalty structure will remain in place for each succeeding year unless expressly eliminated by the Commission. Such penalties, if assessed, are to be credited to AI's customers under the methodology discussed in Section B of this Order.

(24) Regulatory Staff - AI will maintain a level of regulatory staff reasonably necessary to ensure compliance with all of our Orders;

(25) Enforcement and Compliance Monitoring.

Joint Applicants shall appoint and identify to this Commission a corporate officer to oversee implementation of, and compliance with, these commitments; to monitor Joint Applicants' progress toward meeting the deadlines specified herein; to provide periodic reports regarding Joint Applicants' compliance as required; and to ensure that any payments due under these commitments are timely made. The compliance officer will report directly to the audit committee of SBC/Ameritech's Board of Directors, who will oversee the corporate compliance officer's fulfillment of these responsibilities.

No later than 6 months after the merger closing, and annually thereafter until the expiration of each of these commitments, Joint Applicants will file with the Commission, for the public record, a report detailing its compliance with these commitments. Joint Applicants will make a copy of its most current compliance report publicly available on their Internet site.

Joint Applicants will, at their own expense, annually engage independent auditors to verify SBC/Ameritech's compliance with these commitments. The first compliance review will be due 1 year after the merger closing and compliance reviews covering a period of 3 years after the merger closing will be submitted. The independent auditor will have access to all of Joint Applicants' records, accounts, memoranda, and documentation necessary to evaluate Joint Applicants' compliance with these commitments. The independent auditor also may verify Joint Applicants' compliance through contacts with the ICC, the FCC, or Joint Applicants' wholesale customers, as appropriate. The Commission will have access to the working papers and supporting materials of the independent auditor. The independent auditor's review will be filed with the Commission for the public record. The review will address: the accuracy of the compliance report submitted by Joint Applicants during the period covered by the review and Joint Applicants' compliance with each of the commitments during the period covered by the review, to the extent that compliance is not addressed by Joint Applicants' compliance report. As filed with the Commission, the review will include: (i) findings and exceptions of the independent auditor; (ii) the response of Joint Applicants to any exceptions of the independent auditor; and (iii) the reply of the independent auditor to the company's response.

If the Commission makes a determination, after due process, that Joint Applicants have during the effective period of a condition materially failed to comply with that condition, the Commission may, at its discretion, extend the effective period of that condition for a period that does not exceed the period during which Joint Applicants materially failed to comply with the condition.

Joint Applicants will make payments due under these commitments within 10 business days of a determination by Joint Applicants' compliance officer, the Commission, or an arbitrator, that payment is due.

These specific enforcement mechanisms will not abrogate, supersede, limit, or otherwise replace the Commission's enforcement powers under State law.

(26) Recordation of All Savings and Costs - The Joint Applicants will be held responsible for recording all savings and all costs relating to the merger in the manner described herein with the ultimate result that 50% of the net merger savings be allocated to customers as previously set forth in this Order. We note that his measure puts the burden on the Joint Applicants to affirmatively evidence compliance in all particulars thus conserving Staff's time and resources. The Commission shall hire, at the Joint Applicant's expense, a third-

party auditor to develop accounting standards and assist the Commission in tracking merger related savings as determined by this order. Such a third-party auditor shall be retained by the Commission immediately, or as soon as is practicable. The third-party auditor shall report to, and be governed by the directives of the Commission.

(27) Interconnection - Ameritech Illinois will provide interconnection in accordance with the following interconnection commitments. Such interconnection provisions shall be available for an indefinite time in Illinois.:

Interconnection Condition A

A. SBC through its subsidiary, Ameritech Illinois, shall provide to CLECs in Illinois those services, facilities or interconnection agreements/arrangements offered by SBC ILEC affiliates in their in-region states subject to the following exceptions and conditions:

- SBC and or any SBC subsidiary affiliate in Illinois shall not be required to offer to CLECs in Illinois UNEs, services, facilities or interconnection agreements/arrangements which have been imposed upon SBC by another state as a result of an arbitration (as opposed to a voluntary agreement);

- SBC through its subsidiary, Ameritech Illinois, shall be required to offer to CLECs in Illinois UNEs, services, facilities or interconnection agreements/arrangements, unless it demonstrates by a preponderance of the evidence that they are technically infeasible or unlawful or contrary to Illinois policy;

- SBC through its subsidiary, Ameritech Illinois, shall not be required to offer to CLECs in Illinois UNEs, services, facilities or interconnection agreements/arrangements at the same rates or prices as SBC makes such offerings in SBC in-region territories on a permanent basis since costs may and do vary by state, and pricing in each state reflects state pricing policies and costs. However, Ameritech Illinois should not be permitted to delay implementation of any interconnection provision on the basis of pricing. Accordingly, the Commission further orders the Joint Applicants to import the rates agreed to in the relevant state in which the imported interconnection agreement was originally reached, until such time as Illinois-specific rates can be determined. At such time, the interim rates would be subject to a true-up.

  The Commission finds this condition to be valuable to CLECs and the expansion of the competitive market in Illinois, particularly since Section 252(i) of TA 96 does not contemplate automatic adoption of one state's approval of an interconnection agreement in other states. This is

especially so where Ameritech Illinois is not a "party" to interconnection agreements in other SBC states.

In relation to these interconnection commitments, Joint Applicants shall make available the following optional payment plan for non-recurring charges:

> As an incentive for local residential telephone competition, SBC through its subsidiary, Ameritech Illinois, will offer a promotional 18-month installment payment option to CLECs for the payment of non-recurring charges associated with the purchase of unbundled network elements used in the provision of residential services and the resale of services used in the provision of residential services. This promotional 18-month installment option will begin on the date 30 days following the Commission’s entry of a final appealable order approving the Merger and will terminate 3 years following the Merger Closing Date. No interest will be assessed on the remaining balance during the 18-month period as long as the CLEC continues to purchase the residential unbundled network element or residential resold service. In the event the CLEC does not purchase the residential unbundled network element or residential resold service for the entire 18 month payment period, any remaining non-recurring charge balance shall immediately be due and payable when the service is terminated. Unless an interconnection agreement by its terms specifies otherwise, interest at a rate of 8% per annum will be assessed on any amounts that become immediately due and payable and are not paid within 30 days of same. If a CLEC disputes its obligation to make payment when due, it will place the amount due in an escrow account earning a rate of at least 8% interest, pending a final resolution of the dispute.
>
> As an additional incentive for local residential telephone competition, SBC through its subsidiary, Ameritech Illinois, agrees to waive the Bona Fide Request (“BFR”) initial processing fee associated with a BFR submitted by a CLEC for service to residential customers under the following condition: the CLEC submitting the BFR must have, for the majority of the BFR requests it has submitted to Ameritech Illinois during the preceding 12 months, completed the BFR process, including the payment of any amounts due. The BFR initial

processing fee will be waived for a CLEC's first BFR following the Merger Closing Date and for a CLEC that has not submitted a BFR during the preceding 12 months. This BFR fee waiver will be offered for a period of 3 years following the Merger Closing Date.

While the process for negotiating and incorporating proposed changes to interconnection agreements resulting from Condition A will be dictated by the normal Section 252 negotiation / arbitration process, Ameritech Illinois shall begin reviewing such proposed changes within 30 days of the Merger Closing Date.

Interconnection Conditions B and C

B. In order to coordinate and facilitate matters regarding implementation of these interconnection conditions, no later than 60 days after the Merger Closing Date, Joint Applicants shall convene a workshop or collaborative process with Staff and CLECs to discuss the UNEs, services, facilities or interconnection agreements (and their interim prices) which are now being provided by an SBC ILEC affiliate (in region) and have been made available to CLECs in SBC's in-region states and which are not currently available and desired by CLECs in Illinois. This workshop shall conclude its work within 60 days.

The Commission Staff shall take a primary role as a facilitator. Within 90 days of the initiation of this workshop, Staff shall produce a report summarizing the interconnection terms and conditions that will be made available and the interconnection arrangements that CLECs desired. Of the arrangements desired by CLECs, Staff will summarize those that Ameritech Illinois agreed to and that Ameritech Illinois objected to on the basis of technical infeasibility, or as unlawful or contrary to Illinois policy. Where Ameritech Illinois raised objections based on the above criteria of technical infeasibility or unlawful or contrary to Illinois policy, Staff shall state its position on the merits of Ameritech Illinois' objections. Aside from these criteria, Ameritech Illinois shall have no basis for objecting to the adoption of such negotiated interconnection agreements.

Condition B and this workshop process are ancillary to Condition A. Should any disagreement arise as to whether an interconnection arrangement requested of Ameritech Illinois is subject to the exemptions under Condition A of technical infeasibility or unlawful or contrary to Illinois policy, the Commission expects that any parties negotiating for interconnection terms under Condition A shall make use of the Staff's report in those negotiations. While not limiting in any way participation in such process by the Commission or individual Commissioners, the Commission will not take an active role until its participation is formally

requested. At such time, the Commission shall then render a decision, based upon a preponderance of the evidence, that the interconnection agreements at issue are technically infeasible or unlawful or contrary to Illinois policy.

C. Joint Applicants shall provide ~~copies~~ the following information regarding all interconnection agreements from other states to the Commission prior to the Merger Closing Date:

1. all agreements listed by state;
2. docket number associated with each agreement;
3. date of approval;
4. parties to the agreement;
5. where the agreement can be obtained including a contact telephone number and a relevant internet address; and
6. an attestation by the SBC/Ameritech corporate compliance officer referenced in Section IV of this Order that such information is true and correct.

Such condition, excepting the requirement of timing, will also include any subsequent interconnection agreements entered into by an SBC ILEC affiliate entered into after the date of the merger closing, as well as agreements entered into by an SBC CLEC competing out of region. For interconnection agreements entered into after the date of the merger closing (in region or out of region), SBC should provide the relevant information referenced above regarding such interconnection agreements to the Commission within 15 days of entering into such agreements. The Joint Applicants will make such agreements available for inspection to any requesting Illinois CLEC, either electronically or in a hard copy format.

This condition will make information available that may be useful to the Commission and its Staff during the collaborative process and/or thereafter to monitor Joint Applicants' continued compliance with the condition of offering agreements from other states in Illinois.

Interconnection Condition D

D. If a CLEC affiliate of SBC/Ameritech obtains a UNE or interconnection arrangement from an incumbent LEC through negotiation of that arrangement or through arbitration initiated by the SBC/Ameritech CLEC under 47 U.S.C. § 252, then Ameritech Illinois shall make available to requesting CLECs in Illinois, though good-faith negotiation, the same UNE or interconnection arrangement on the same terms (exclusive of price). Ameritech Illinois shall be obligated to provide such UNE or interconnection arrangement(s) where it is technically feasible to do so on

or in the network of Ameritech Illinois and subject to the unbundling limitations of 47 U.S.C. § 251(d)(2).

The determination of whether a UNE or interconnection arrangement is technically feasible shall follow 47 CFR § 51.5.

The price(s) for such UNEs or interconnection arrangements shall be negotiated on a state-specific basis and, if such negotiations do not result in agreement, Ameritech Illinois shall submit the pricing dispute(s), exclusive of the related terms and conditions required to be provided under this Section, to this Commission for resolution under 47 U.S.C. § 252.

(28) Shared Transport - Ameritech Illinois will provide shared transport in accordance with the following shared transport commitment:

A. Interim Solution Prior To The Merger Closing Date

To accelerate the availability of a shared transport offering, Ameritech Illinois shall provide to this Commission, prior to the Merger Closing Date, proof of the implementation in Illinois of the SBC/Texas Interim version of shared transport. The filing of a tariff with this Commission containing such SBC/Texas Interim version as well as the Commission approval of such tariff (which must occur before the Joint Applicants may close on the merger) shall constitute compliance with this condition. Prior to Commission approval such tariff shall be reviewed by Commission Staff with a Staff recommendation to the Commission for approval or disapproval. In addition, the Joint Applicants shall import to Illinois the rates agreed to in Texas for the interim version, until such time as Illinois-specific rates can be delivered. At such time the interim rates will be subject to a true-up.

As described below, the interim solution avoids or addresses each of the technical and network issues that Ameritech Illinois identified in its TELRIC tariff filing.

Dedicated links and custom routing. Ameritech Illinois will not require the use of dedicated transport or custom routing to complete a call using unbundled local switching and shared transport to a third party switch. Rather, Ameritech Illinois will make available a modified version of transiting that does not require a dedicated end office integration (EOI) transit trunk. This is similar to the shared transport offering that SBC makes available. For example, as SBC has described its common transport offering: “this common transport is employed typically when the CLEC makes use of SBC’s network to send calls to or terminate calls from an IXC, a facility based CLEC and/or an independent local exchange

company." (SBC's Response to Staff data requests RTY-6.04R. *See also* Staff Ex. 5.0 at 8).

Measuring terminating call detail. Ameritech Illinois does not have the ability to record terminating detail based on its current network architecture. However, Ameritech Illinois will implement an interim solution that involves the use of originating and terminating factors and a settlement procedure with each CLEC purchasing local switching and shared transport to allocate appropriate access charge revenues. Thus, when an end-user customer, who is served by a CLEC using Ameritech Illinois' shared transport facilities, makes or receives an interLATA call, Ameritech Illinois will collect relevant access charges from the interexchange carrier and then make payment to, or receive payment from, the CLEC using local switching based on the difference between access charges and applicable charges for the UNEs used to provide the access service. Factors and settlement procedures have been widely used within the telecommunication industry in many contexts, for many years. Indeed, such a factor-based approach and settlement method have been informally approved by the United States Department of Justice and the FCC in connection with Ameritech's Section 271 plans.

Identifying the originating local carrier. Ameritech Illinois currently does not have the short-term ability to identify the originating local carrier terminating a call to a CLEC's local switching port. However, Ameritech Illinois will implement a concept known as originating carrier pays to address this limitation. Under an originating carrier pays arrangement, Ameritech Illinois will charge a CLEC using Ameritech Illinois' local switching and shared transport facilities for usage of local switching to both originate and terminate such traffic. Ameritech Illinois, however, will not charge a CLEC using Ameritech Illinois' unbundled local switching for usage at the terminating switch when terminating traffic delivered by shared transport facilities. Nor will Ameritech Illinois create message records for such terminating usage, since reciprocal compensation will not be eligible for collection by the terminating carrier in such circumstances. This approach therefore alleviates the existing network fact that Ameritech Illinois does not have the capability to record terminating local calls. If the originating carrier pays both originating and terminating ULS, recording at the termination office for a local call is unnecessary in any event. The Commission finds that this is a reasonable interim solution, which accelerates the availability of shared transport in a way that makes it operationally feasible.

Providing common/shared transport on an unbundled basis. The Supreme Court has expressly reinstated the FCC's rule, which required incumbent LECs to provide pre-assembled combinations of unbundled network elements, assuming each element in the combination is capable

of being purchased separately. While Ameritech Illinois contends shared transport is not “unbundleable” as defined by the Supreme Court, that issue will be resolved in the FCC’s UNE Remand Proceedings. Until such time, Ameritech Illinois will provide shared transport with local switching (since, in fact, there is no other way to provide it).

B. Long-Term Solution Within One Year Of Merger Closing.

The Commission finds the proposed interim solution described above acceptable because: (i) it maximizes Ameritech Illinois’ ability to offer shared transport quickly; (ii) it minimizes Y2K implications by avoiding any significant network or billing modifications before the end of 1999; and (iii) it provides a reasonable period of time to implement a more permanent solution that relies on a network technology that does not require the use of factors or settlements.

Despite the apparent confusion in the record regarding shared transport, the major difference between Ameritech Illinois’ and SBC’s capabilities on this issue relates to the deployment of different network technologies. In Texas, SBC has deployed an AIN network architecture that enables SBC to use AIN triggers to identify UNE ports, which in turn enables billing of usage sensitive charges. This AIN approach eliminates the need for factors or settlements for both local and toll calling. Ameritech Illinois has not deployed this AIN network capability. The cost and time to deploy such capability is significant and substantial. However, Ameritech Illinois shall deploy shared transport in Illinois, in the same manner that SBC has deployed shared transport in the state of Texas (using AIN triggers) beginning its roll out within one year of the Merger Closing Date. Deployment of shared transport in this manner fully complies with this Commission’s TELRIC Order and the FCC’s now-vacated *Third Order on Reconsideration*. Joint Applicants will offer such shared transport in Illinois, under the terms and conditions (other than rate structure and price) that are substantially similar to the most favorable terms offered by SBC to CLECs in Texas as of the Merger Closing Date.

C. Further Demonstration

In the event that the FCC reverses its previous position and decides in its remand docket that shared transport should not be unbundled, the Joint Applicant’s are directed to file with this Commission within 30 days of the FCC decision a petition seeking an Illinois-specific determination of the propriety of unbundling Shared Transport under Section 13-505.6. While that Illinois-specific docket progresses, the Joint Applicants will continue to provide Shared Transport as herein described until such time as this Commission comes to a final determination on the merits and issues its order in such proceeding.

(29) Additional OSS - Joint Applicants will comply with the following OSS commitments:

A. OSS Conditions

Joint Applicants will meet the following timetables and milestones regarding integration of OSS processes in Illinois:
Joint Applicants shall implement a comprehensive plan for improving the OSS systems and interfaces available to CLECs in Illinois. The Joint Applicants' plan shall consist of the following commitments.

Application-to-Application Interfaces Commitments

Ameritech Illinois will deploy, in accordance with the schedule noted below, commercially ready, application-to-application interfaces as defined, adopted, and periodically updated by industry standard setting bodies for OSS (*e.g.*, Electronic Data Interchange ("EDI") and Electronic Bonding Interface ("EBI")) that support pre-ordering, ordering, provisioning, maintenance and repair, and billing for resold services, individual UNEs, and combinations of UNEs.

Deployment of the application-to-application interfaces will be carried out in three phases.

- *Phase 1:* Within 3 months after the Merger Closing Date or final regulatory approval, Joint Applicants shall complete a publicly available Plan of Record which shall consist of an overall assessment of SBC's and Ameritech's existing OSS interfaces, business processes and rules, hardware and data capabilities, and security provisions, and differences, and the companies' plan for developing and deploying application-to-application interfaces and graphical user interfaces for OSS, as well as integrating their OSS processes. The Plan of Record shall be accepted, or rejected, by this Commission after an expedited (two week) CLEC comment cycle.

- *Phase 2:* SBC/Ameritech shall work collaboratively with ICC Staff and Illinois CLECs, in a series of workshops, to obtain written agreement on OSS interfaces, enhancements, and business requirements identified in the Plan of Record. Phase 2 shall be conducted under the auspices of the ICC and shall be completed in a total of 3 months unless the parties mutually agree to extend Phase 2, or unless the Commission grants a reasonable request for an extension by a participating party. If the CLECs and SBC/Ameritech have not reached agreement after one month of such sessions (unless there is a mutually agreeable extension or a Commission order extending this date after a reasonable request is made by a participating party to continue negotiations), the parties shall prepare a list of the unresolved issues in dispute and submit the remaining unresolved issues in

dispute to arbitration by the Commission. The parties must submit the unresolved issues to Commission arbitration no later than one week after the conclusion of the collaborative sessions (unless there is a mutually agreeable extension). Any arbitration shall be conducted before the Commission with the assistance of an independent third party with subject matter expertise. The independent third-party shall be hired by the Commission in accordance with state procurement law at the expense of the Joint Applicants. This arbitration shall be concluded within 7 weeks of submission of the unresolved issues (unless there is a mutually agreeable extension). In the event that SBC/Ameritech and the participating Illinois CLECs are able to come to written agreement regarding some OSS issues, but not all, those issues that have been agreed to shall immediately proceed to Phase 3.

- *Phase 3:* SBC/Ameritech shall develop and deploy, on a phased-in basis, the system interfaces, enhancements and business requirements consistent with the written agreement obtained in Phase 2. The date for completion of Phase 3 is 12 months after completion of Phase 2, unless a majority of the CLECs participating in Phase 2 agree to an extension. The completion date shall begin to run after the completion of a written agreement in Phase 2, or the effective date of a final decision by the Commission acting as arbitrator in Phase 2, whichever is later. If one or more CLECs contend that SBC/Ameritech has not developed and deployed the system interfaces, enhancements, and business requirements consistent with the written agreement obtained in Phase 2, or has not complied with the Commission's decision received in Phase 2, they may file a complaint with the Commission which shall arbitrate the issue(s) consistent with the procedures identified in Phase 2 except that this arbitration shall be concluded within 2 months.

The Joint Applicants are required to pay for an independent third-party, retained by the Commission , for technical assistance to the Commission as an arbitrator and to Staff throughout the phased OSS implementation process. The third-party shall report to the Commission, and monitor and assist in the phased process as directed by the Commission, and conduct "New York" style testing during Phase 3 as defined by the Commission.

Graphical User Interfaces

Ameritech Illinois will deploy graphical user interfaces (*e.g.*, Toolbar interface) for OSS that support pre-ordering, ordering, provisioning, maintenance and repair, and billing for resold services, individual UNEs, and combinations of UNEs. Deployment of graphical user interfaces will

be carried out on the same three-phase schedule as application-to-application interfaces.

Direct Access to Service Order Processing Systems

In addition to the application-to-application and graphical user interfaces described herein, Ameritech Illinois will offer to develop and deploy direct access to Ameritech Illinois' service order processing systems for resold services, individual UNEs, and combinations of UNEs, provided that a CLEC requesting such direct access enters into a contract to pay Ameritech Illinois for 50% percent of the costs of development and deployment. The access developed will meet the requirements of 47 U.S.C. § 251(c)(3). Ameritech Illinois' offer to develop direct access to Ameritech Illinois' service order processing systems will be available for a period of 30 months after the Merger Closing Date, and Ameritech Illinois will agree to develop and deploy the interface contracted for within one year of a completed contract with the CLEC.

B. Additional OSS Commitments

To the extent that OSS issues in addition to those identified above are raised in any collaborative process, Joint Applicants shall make such issues part of the appropriate collaborative processes.

(30) Performance Measuring, Benchmarks and Liquidated Damages - Joint Applicants will establish performance measurements, benchmarks and provide for liquidated damages in accordance with the performance measurements, benchmarks and liquidated damages commitment set forth below:

Performance Measures, Benchmarks and Liquidated Damages Commitments

1. Within 60 days following the Merger Closing Date, SBC/Ameritech will establish a joint SBC/Ameritech task force comprised of their performance measurements subject matter experts that is to develop a plan to implement OSS and facilities performance measurements, associated standards/benchmarks, and remedies in Illinois.

2. The task force will review the technical feasibility of adopting in Illinois each of the OSS and facilities performance measurements and related standards/benchmarks that SBC has agreed to implement in Texas as a result of the Texas collaborative process. This review will identify the differences, if any, between the underlying legacy systems and equipment, including computer, manual and data generating systems and equipment, in Texas and Illinois which may make it technically infeasible to implement certain agreed to performance measurements and/or related standards/benchmarks in Illinois. If no such

differences are identified for a particular measurement or standard/benchmark, SBC/Ameritech shall implement that performance measurement or standard/benchmark in Illinois. As of June 18, 1999, SBC had agreed to implement in Texas 122 such performance measurements and Agreed To Standards/Benchmarks, which include the performance measurements identified in a U.S. Department of Justice March 6, 1998 letter. The task force will include these measurements or standards/benchmarks within its review. The task force will also review the remedies agreed to in the Texas collaborative process to determine whether it is appropriate to implement such remedies in Illinois considering any relevant differences between Texas and Illinois.

3. Within 90 days following the Merger Closing Date, in conjunction with such task force, SBC/Ameritech will work with the Commission Staff, CLECs, and any other interested parties in a collaborative process to develop the initial performance measurements, standards/benchmarks, and remedies to be implemented in Illinois. SBC/Ameritech will meet with the collaborative participants on a regular basis to review the status of implementing each of the 122 performance measurements, Agreed To Standards/Benchmarks, and/or remedies in Illinois. Such review will include either:

    1. the timeline for implementing the performance measure, associated standard/benchmark, and remedy in Illinois; or

    2. an explanation of why SBC/Ameritech contend it is not technically feasible to implement either the performance measure, standard/benchmark or remedy in Illinois, in which case SBC/Ameritech would discuss any substitute measure(s), associated standard(s)/ benchmark(s), and/or remedy(ies) that would be appropriate.

4. Within 150 days following the Merger Closing Date, the task force will complete its initial review of performance measurements/standards/benchmarks/remedies with the collaborative participants. One hundred and fifty days after the Merger Closing Date, the Joint Applicants shall submit to the Commission for approval a written report detailing the timeline for implementing each of the performance measures, associated standards/benchmarks, and remedies, or an explanation of why SBC/Ameritech contend that implementation any particular measurement, standard/benchmark, or remedy is infeasible. The Commission may grant waivers from certain measurements, standards/benchmarks, and remedies, and shall determine the value of each missed measurement, and standard/benchmark in the event that SBC/Ameritech does not implement a particular measurement or standard/benchmark, or that it does not seek a waiver from such a requirement within 300 days of the Merger Closing Date. Liquidated damages for failure to implement the performance measures shall not exceed $90 million.

5. Beginning 120 days following the Merger Closing Date and completing within 210 days following the Merger Closing Date, SBC/Ameritech will implement in Illinois (subject to any required Commission approval, which will be timely sought), each of the Agreed To Standards/Benchmarks that are determined to be technically feasible to implement. Implementation will occur on a rolling basis as each Agreed to Standard/Benchmark is tested and becomes operationally ready and will fully apply to both resale and facilities, where applicable, when implemented. If SBC/Ameritech determine that it is no technically feasible to implement one or more Agreed To Standards/Benchmarks in Illinois within 210 days following the Merger Closing Date, they shall seek a waiver of the 300 day deadline from the Commission. The Commission may agree to allow the implementation of such Agreed To Standards/Benchmarks as soon as it is technically feasible to do so.

6. Within 7 days of merger closing, Joint Applicants should provide the Commission with a written list of the 122 ~~79~~ benchmarks and standards they will implement in Illinois. They should also describe which standards and benchmarks may be problematic to implement and a detailed justification for such a determination. Within 300 days following the Merger Closing Date, Ameritech Illinois will implement in Illinois all of the 122 performance measurements and related standards/benchmarks except those waived by the Commission pursuant to paragraphs 4 and 5 above. Within 310 days following the Merger Closing Date, SBC/Ameritech will file a letter in this docket and serve such letter upon all CLECs with whom Ameritech Illinois has an approved interconnection agreement attesting whether or not Ameritech Illinois has met this commitment. Such attestation is subject to review by the Commission. If SBC/Ameritech attest that they did not, or the Commission finds that they did not implement in Illinois all of the 122 performance measurements and related standards/benchmarks within of 300 days following the Merger Closing Date, SBC/Ameritech will make a payment of $30 million, as follows:

    a. $26.25 million, as payments to CLECs providing end-user service within Ameritech Illinois' service area as of the date 300 days following the Merger Closing Date as follows:

        A. <u>A CLEC's Access Lines</u>, for each CLEC, shall be its total number of access lines in service, including, without limitation, residence access lines, business access lines and end-user trunks, and ISDN lines, whether resold or not, measured as of the date 300 days following the Merger Closing Date, within Ameritech Illinois' current service area. Each CLEC that desires to receive any of the $26.25 million in payments must provide to the Commission Staff, no later than 330 days following the Merger Closing Date, a report identifying the number of such lines and trunks for that CLEC. Such report shall separately identify: i) the number of resold Ameritech Illinois access lines; ii) the number of

unbundled loops purchased from Ameritech Illinois; and iii) all other such lines and trunks in service within Ameritech Illinois' current service area. Each CLEC submitting such a report will certify to the Commission Staff the accuracy of such report. The Commission Staff will notify each qualifying CLEC of its pro-rata share of the $26.25 million. Thirty days after the date of such notice, the Commission Staff will provide notice to SBC/Ameritech as to the appropriate disbursement of the $26.25 million. Within 60 days of receiving this notice from the Commission Staff, Ameritech Illinois will issue checks totaling $26.25 million made payable to each qualifying CLEC for the disbursement amounts listed in Staff's notice to Ameritech Illinois.

B. Total CLEC Access Lines shall be the sum of A. above for all qualifying CLECs submitting a timely report.

C. A CLEC's Pro-Rata Share shall be the ratio of A. above for that CLEC, divided by B.

D. Each affected CLEC within Ameritech Illinois' current service area shall receive a payment equal to $26.25 million multiplied by the CLEC's Pro-Rata Share; and

b. $3.75 million to the Community Technology Fund described below.

7. If Ameritech/Illinois reports that it has met the commitments as provided and that is disputed, the Commission may issue an order to resolve that dispute and may set forth-appropriate time frames.

8. For each Agreed to Standard/Benchmark to be implemented in Illinois that has an SBC agreed-upon remedy in Texas, SBC/Ameritech will discuss with the collaborative participants the proposed remedy to be attached to such Agreed to Standard/Benchmark in Illinois. After SBC/Ameritech implement an Agreed To Standard/Benchmark in Illinois, they will also implement (subject to any required Commission approval, which will be timely sought) any remedy to be associated with such Agreed To Standard/Benchmark consistent with the approach used in the Texas collaborative process. If the collaborative participants agree, SBC/Ameritech will refrain from implementing a particular remedy. Regardless of whether or not SBC agrees to remedies (*e.g.*, damages, assessments, and credits) associated with one or more Agreed To Standards/Benchmarks in the Texas collaborative, the Illinois collaborative process is not precluded from considering any proposed remedy or remedies.

9. If any participant in the collaborative process disputes SBC/Ameritech's determination that it is not technically feasible to implement a particular

Agreed To Standard/Benchmark in Illinois, either at all or within the 210 day time period, the collaborative participants will attempt to resolve such dispute in the collaborative process. If any such dispute cannot be resolved through the collaborative process, any participant may ask the Commission to resolve such dispute. In any such dispute that may arise before the Commission, SBC/Ameritech retain the burden of proving to the Commission that it is not technically feasible to implement an Agreed To Standard/Benchmark in Illinois.

10. Ameritech Illinois will provide a report to the Commission on the results of its performance measurements on a quarterly basis, beginning the first full calendar quarter in which Ameritech Illinois has at least one full month of data for one or more performance measurements, and will report with respect to transactions affecting Illinois CLECs relative to their provision of service to end users in Illinois. Performance measurement reports will be provided to CLECs in conformance with each CLEC's interconnection agreement and will be made available electronically if so requested. Joint Applicants are ordered to provide monthly performance monitoring reports and website information to the Commission on a disaggregated CLEC-by-CLEC basis.

11. For a minimum of one year following the Merger Closing Date, and thereafter on an as-needed basis as determined by Staff, participants in the collaborative process will collaborate to implement any additions, deletions, or changes to the performance measurements, standards/benchmarks, and remedies that are implemented by SBC/Ameritech in Illinois. Any participant may propose such addition, deletion, or change based upon experience with such implemented performance measurements, standards/benchmarks, remedies, or any other factor. If a dispute over any such addition, deletion, or change cannot be resolved through the collaborative process, any participant may ask the Commission to resolve such dispute. The participant proposing the addition, deletion, or change retains the burden of proving that such addition, deletion, or change should be adopted in Illinois.

(31) Verification - With respect to all reports required to be submitted to this Commission under any of the preceding conditions to this merger, SBC shall attest to the veracity of each report through the inclusion of and signature to the following language:

> "I am the corporate officer of SBC/Ameritech who is appointed to oversee the implementation and compliance of the commitments and conditions contained in the Order dated September [xx], 1999 of the Illinois Commerce Commission in Docket 98-0555. I have reviewed the information contained in this report and, on behalf of SBC and Ameritech, certify that such information is true, accurate and complete as of the date of this report."

(32) Notice - No later than seven (7) days after the entry of a final Order the Joint Applicants should notify the Commission, pursuant to the provisions of Section 10-112 of the PUA that the terms, conditions and requirements set out above are accepted and will be obeyed.

VII. FINDINGS AND ORDERING PARAGRAPHS

The Commission, having considered the entire record herein and being fully advised in the premises, is of the opinion and finds that:

(1) Illinois Bell Telephone Company d/b/a Ameritech Illinois is a telecommunications carrier certified to provide local exchange and intraMSA interexchange services in Illinois; Ameritech Illinois does provide such services and provides both competitive and noncompetitive telecommunications services;

(2) Joint Applicants request approval of a “reorganization” of Ameritech Illinois that would result from a business combination of SBC Communications Inc. and Ameritech Corporation, two Delaware corporations and holding companies; if that business combination is completed, Ameritech Corporation would become a wholly-owned first-tier subsidiary of SBC Communications Inc. and Ameritech Illinois would remain a wholly-owned subsidiary of Ameritech Corporation;

(3) the Commission has jurisdiction over the parties hereto and the subject matter hereof;

(4) the findings of fact and conclusions of law set forth in the prefatory portion of this Order are supported by the record herein and are hereby adopted as findings of fact and conclusions of law;

(5) with the adoption of the conditions set forth herein, the proposed reorganization will not adversely affect the ability of Ameritech Illinois to perform its duties under the Illinois Public Utilities Act;

(6) with the adoption of and compliance with the conditions set forth herein, the Joint Applicants will satisfy the provisions in Section 7-204(b) (I) - (7), as follows;

(I) the proposed reorganization will not diminish Ameritech Illinois' ability to provide adequate, reliable, efficient, safe and least cost service;

(II) the proposed reorganization will not result in the unjustified subsidization of non-utility activities by Ameritech Illinois or its customers;

(III) costs and facilities are and will be fairly and reasonably allocated between utility and non-utility activities in such a manner that the Commission can identify those costs and facilities which are properly included by Ameritech Illinois for ratemaking purposes;

(IV) the proposed reorganization will not significantly impair Ameritech Illinois' ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure;

(V) Ameritech Illinois will remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities;

(VI) the proposed reorganization is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction; and

(VII) the proposed reorganization is not likely to result in any adverse rate impacts on retail customers;

(7) Joint Applicants voluntary commitments, as modified herein, are adopted as conditions to the approval of the proposed reorganization; those commitments are as set forth in the numbered paragraphs and conditions of Section VI of this Order ;

(8) the provisions of Section 7-204(c) are being applied to the reorganization, so that 50% of the net merger-related savings as previously defined herein, allocable to Illinois, are to be allocated to the merged company's customers in accordance with the determination set forth in the prefatory portion of this Order;

(9) the materials submitted by the parties in this proceeding on a proprietary basis or for which proprietary treatment was requested are hereby considered proprietary and should continue to be accorded such treatment;

(10) any petitions, objections or motions in this proceeding that have not been specifically disposed of should be disposed of in a manner consistent with the Commission's conclusions herein.

IT IS THEREFORE ORDERED, that the proposed reorganization of Ameritech Illinois, as set forth in the verified Joint Petition filed in this proceeding, should be, and hereby is, approved, subject to the conditions set forth in Findings (7) (8), (9)and (10).

IT IS FURTHER ORDERED that any materials submitted in this proceeding for which proprietary treatment was requested shall be accorded such treatment.

IT IS FURTHER ORDERED that any petitions, objections or motions made in this proceeding and not otherwise specifically disposed of herein are hereby disposed of in a manner consistent with the conclusions contained herein.

IT IS FURTHER ORDERED that subject to the provisions of Section 10-113 of the Public Utilities Act and 83 Ill. Adm. Code 200.880, this Order is final; it is not subject to the Administrative Review Law.

By Order of the Commission this 23rd day of September, 1999.

Chairman