ARGUMENT SCHEDULED FOR JANUARY 19, 1996

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 95-5137
and consolidated cases

UNITED STATES OF AMERICA,
Plaintiff-Appellee-
Cross-Appellant,

v.

WESTERN ELECTRIC CO., INC., et al.,
Defendants-Appellees,

PACIFIC TELESIS GROUP, et al.,
Appellants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

REPLY BRIEF FOR THE UNITED STATES AS CROSS-APPELLANT

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CERTIFICATE AS TO PARTIES, RULINGS AND RELATED CASES

To counsel's knowledge, the information required by Rule 28(a)(1) is provided in the Brief for the Bell Company Appellants and the Brief for Appellants BellSouth Corporation and SBC Communications Inc., except that, 1) on August 31, 1995, after those briefs were filed, the district court denied the July 7, 1995 motion of four of the BOCs for clarification of the April 28, 1995 order that is the subject of this appeal, and 2) several other motions concerning the interpretation and application of the new section VIII(L)(2)(a) also are pending in the district court.

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*Authorities upon which we chiefly reply are marked with an asterisk.

GLOSSARY

AT&T Br.	-	Brief of Defendant-Appellee AT&T Corp. (Oct. 2, 1995)
BellSouth-SBC Br.	-	Brief for Appellants BellSouth Corporation and SBC Communications Inc. (Aug. 11, 1995)
BOC	-	Bell Operating Company. The BOCs are also known as RBOCs, Regional Companies, Regional Holding Companies or Bell Companies
BOC Br.	-	Brief for the Bell Company Appellants (Aug. 11, 1995)
CAP	-	Competitive Access Provider
JA	-	The deferred Joint Appendix in this case
LATA	-	Local Access and Transport Area
LEC	-	Local Exchange Carrier
MCI Br.	-	Brief of Appellee MCI (Oct. 2, 1995)
MFJ	-	Modification of Final Judgment (reprinted in US Br. Addendum)
MTSO	-	Mobile Telephone Switching Office
Opinion and Order	-	United States v. Western Elec. Co., 890 F. Supp. 1 D.D.C. 1995 (JA 1-10; 10-14) (Order reprinted in U.S. Br. Addendum)
PCS	-	Personal Communications Services
POP	-	Point of Presence
SBC	-	Appellant SBC Communications Inc.
SMR	-	Specialized Mobile Radio
US Br.	-	Brief for the United States as Appellee and Cross-Appellant (Sept. 11, 1995)
US Reply	-	Reply Memorandum of the United States in Response to the Bell Companies' Motion for Generic Wireless Waivers (D.D.C. Sept. 2, 1994) (JA 879)
US Response	-	Memorandum of the United States in Response to the Bell Companies' Motions for Generic Wireless Waivers (D.D.C. July 25, 1994) (JA 589)

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REPLY BRIEF FOR THE UNITED STATES
AS CROSS-APPELLANT

INTRODUCTION AND SUMMARY OF ARGUMENT

In all respects save one, the United States supports the district court's decision allowing the Bell Operating Companies ("BOCs") to provide interexchange services from cellular and other wireless mobile systems separate from their landline local exchange monopolies, subject to continued equal access and other conditions. The district court was correct to impose substantial

conditions on the relief it granted, and the United States strongly disagrees with the BOCs' challenge to the district court's imposition of conditions recommended by the Department of Justice. Indeed, because those conditions are essential to protect competition, the modification should not be affirmed unless those conditions are upheld.

The United States has appealed solely to urge this Court to vacate section VIII(L)(2)(a), which limits the waiver to areas in which at least one non-BOC provides access from mobile telephone switching offices ("MTSOs") to interexchange carriers' points of presence ("POPs").[1] We recognize that, in adding this condition, the district court may have relied upon the BOCs' expansive statements about bypass and underestimated the effect of 2(a). Nonetheless, this one condition should be vacated.

Appellee AT&T Corp. ("AT&T") and intervenor-appellee MCI Communications Corporation ("MCI") -- major interexchange carriers with which the BOCs would compete in serving cellular subscribers if 2(a) were vacated -- seek to defend the alternative access condition.[2] Contrary to their contention, however, the district court did not conduct the full analysis required by section VIII(C) of the decree. Finding a "Mobile Bottleneck," it simply presumed that denial of the waiver was

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[1]Section VIII(L) of the decree, as added by the order under review, is reprinted in the Addendum to the US Brief.

[2]AT&T and MCI did not appeal, and they do not contend that the district court erred in granting the waiver with the 2(a) condition.

required except in areas where a non-BOC provides alternative MTSO-to-POP access. Thus it erroneously equated the competitive effects of the BOCs' control over the limited local exchange facilities used for wireless-originated interexchange calls, with the effects of the BOCs' much broader control over interexchange calls originated on their landline monopoly systems.

AT&T also offers the puzzling argument that denial of the waiver was required, without regard to the likelihood of anticompetitive effects in wireless long distance services, because such services do not constitute a separate antitrust market. AT&T Br. at 39-44. AT&T did not appeal from the grant of the waiver, however, and this argument undercuts its contention that the alternative access condition was required to satisfy section VIII(C). Moreover, to the extent that AT&T contends that VIII(C) does not permit waivers allowing BOCs to provide less than all of the services in a relevant market, it is simply wrong.

Finally, AT&T and MCI contend that, in any event, the 2(a) condition is not anticompetitive. They argue that interexchange carriers could not "veto" BOC provision of interexchange wireless services by failing to use available alternative access services, because 2(a) requires only that alternative MTSO-to-POP access be "provided," not that interexchange carriers use it. See AT&T Br. at 44-47; MCI Br. at 7-9. However, there presently is little if any alternative access -- used or unused -- and there is no assurance that it will develop. Thus, even if provision without

use satisfies 2(a), that condition largely bars BOC services that should be permitted under the VIII(C) standard.

ARGUMENT

1. The District Court's Imposition of 2(a) Rests on a Misapplication of the VIII(C) Standard

AT&T and MCI argue that the United States' appeal challenges factual findings entitled to deference under a "clearly erroneous" standard of review. AT&T Br. at 32-39; see also MCI Br. at 4. The United States, however, does not dispute that the BOCs have a continuing "Mobile Bottleneck" in most areas, i.e., that interexchange carriers depend on BOC landline facilities for connections between their POPs and cellular MTSOs. We contend, however, that the district court erred as a matter of law because, rather than conducting the further analysis required by VIII(C), it deemed the Mobile Bottleneck finding sufficient in itself to require that the waiver be denied or limited to areas in which a non-Regional Company provides alternative MTSO-to-POP access. 890 F. Supp. at 8-9 (JA 8-9).

As the decree plainly states and as this Court has emphasized, the BOCs may satisfy VIII(C) by showing "'that there is no substantial possibility that [they] could use [their] monopoly power to impede competition in the market [they] seek[] to enter.'" United States v. Western Electric Co., 900 F.2d 283, 295 (D.C. Cir.) (quoting VIII(C)) ("Triennial Review Appeal"), cert. denied, 498 U.S. 911 (1990); id. at 300-01 (considering but rejecting argument that monopoly power could not be used to impede competition); United States v. Western Electric Co., 12

F.3d 225, 233-35 (D.C. Cir. 1993) ("Affiliated Enterprise") (noting that court must consider not only whether a BOC may favor its own services but whether such favoritism is likely to have anticompetitive effects).

Although AT&T points to the district court's quotation of the VIII(C) standard, see A&T& Br. at 30 (quoting 890 F. Supp. at 3 (JA 3)), the court did not conduct the full analysis required to determine whether a waiver subject to the Department's conditions would satisfy VIII(C). Rather, because it found a Mobile Bottleneck, it assumed that "anticompetitive behavior" could occur, and it was unwilling to rely on the safeguards proposed by the Department. 890 F. Supp. at 8 (JA 8); see also id. at 4-5 (JA 4-5) (existence of the Mobile Bottleneck "means, of course, that [BOCs] . . . would still have the potential to discriminate against competitors in the cellular interexchange business"; interexchange carrier dependence is "the bottom line"). Concluding that its adoption of most of the Department's proposed conditions "would not eliminate the risk of discrimination, but instead would merely reduce the risk to 'acceptable levels,'" 890 F. Supp. at 8 (JA 8), the court made no factual findings concerning the likely extent or effect of potentially anticompetitive BOC behavior. Thus it did not reach the critical issue of the BOCs' ability to use their monopoly power to impede competition in the market they seek to enter.

Also contrary to AT&T's contention (AT&T Br. at 31), the district court's Triennial Review decision (United States v.

Western Electric Co., 673 F. Supp. 525 (D.D.C. 1987), aff'd in part, rev'd in part and remanded, 900 F.2d 283 (D.C. Cir.), cert. denied, 498 U.S. 911 (1990)) did not foreclose the relief recommended by the Department. That 1987 decision addressed a proposal very different from the waiver now at issue. See Affiliated Enterprise, 12 F.3d 234 (rejecting similar argument with respect to equipment manufacturing prohibition). In the Triennial Review proceedings, the BOCs sought unconditional removal of the decree restrictions as applied to mobile services; the United States argued that equal access should be maintained. In 1987, however, neither the BOCs nor the Department proposed the other safeguards that were an essential part of the Department's 1994 recommendation.

2. The Waiver Conditions Other Than 2(a) Effectively Prevent Abuse of the "Mobile Bottleneck," Which Is Quite Different from the "Landline Bottleneck"

AT&T and MCI contend that, absent 2(a), BOC provision of the limited interexchange services permitted by this waiver would have essentially the same anticompetitive effects as a complete lifting of the interexchange restriction. AT&T Br. at 32-39; MCI Br. at 4-7. They are wrong. The record establishes and the district court recognized that the conditions proposed by the Department, without 2(a), would effectively reduce the risk of anticompetitive conduct to "'acceptable levels.'" 890 F. Supp. at 8 (JA 8). Accordingly, it was unnecessary for the district court to add any further conditions in order to grant the waiver under VIII(C).

The United States does not suggest that conditions such as we proposed for this waiver would be adequate to allow the BOCs to provide interexchange services from landline systems or from any services integrated with landline systems. We emphasize that there are significant differences between the Mobile Bottleneck and the Landline Bottleneck, and that we support only a waiver allowing the BOCs to provide mobile wireless-originated interexchange services. It is solely in this context that we deem the equal access, separation, resale and unbundling and marketing conditions of the order sufficient -- as well as necessary -- to prevent anticompetitive BOC conduct. See US Br. at 28-32, 36-44.[3] Moreover, we do not dismiss the Mobile Bottleneck as a competitive concern. Absent the conditions that the court imposed at the Department's suggestion, the United States would not support this waiver.

As the United States explained below, the facilities and services subject to BOC bottleneck control are far more limited and less complex for calls from cellular systems than for calls from landline systems. See US Response at 40-42 (JA 626-28); US Reply at 6-7, 11-15 (JA 884-85, 889-93); Tr. 32-34 (JA 923-25). For a landline call, the BOC bottleneck encompasses the entire path from the caller to the interexchange carrier and from the interexchange carrier to the called party. In contrast, cellular

[3]The Department of Justice is currently investigating the potential anticompetitive effects of complete removal of the interexchange restriction, as sought by the pending BOC motion to vacate the decree.

calls use a limited and discrete segment of the BOC landline network to connect the cellular MTSO to the interexchange carrier POP. As AT&T concedes, cellular calls do not use BOC bottleneck facilities for "the physical connection between the calling party and the BOC end office switch" (AT&T Br. at 14), nor are cellular calls switched within the BOC landline network before reaching the MTSO. Instead, the cellular system provides the end-user connection and local switching. And while BOC cellular systems have market power, see US Br. at 28-32, competition from a second cellular system places some constraints on their ability to engage in anticompetitive discrimination, see US Response at 42 (JA 628).

It is also significant that the BOC-provided connections between interexchange carriers' POPs and cellular MTSOs are relatively simple and direct. Interexchange carriers may use either dedicated access lines, with no switching, or switched services in which calls from cellular systems are routed through the access tandem. AT&T's assertion that "RBOC-supplied access connections that carry cellular calls to interexchange carrier networks are the same switched and dedicated access facilities and services that carry landline-originated calls," AT&T Br. at 33, is not wrong; it just misses the point. In addition to these "same services," landline calls use bottleneck services and facilities that cellular calls do not use. Therefore, contrary to AT&T's argument (AT&T Br. at 14) "the RBOCs' continued . . . bottleneck control over the facilities that interexchange

carriers need to originate and terminate each mobile-originated call" does not establish that the BOCs have "the same ability to exploit that control to harm competition as they have with respect to landline calls."

The Department's support for a waiver limited to wireless-originated interexchange calls did not rest solely on the nature of BOC monopoly services used by wireless carriers. But it was only in this context that the Department, after extensive review of the submissions from the BOCs, AT&T, MCI, and other interested persons, concluded and recommended to the court that, with a carefully tailored set of conditions -- including equal access, structural separation, resale, and unbundling and separate marketing requirements -- a waiver should be granted under VIII(C). See US Br. at 28-32, 34-46.

The district court largely adopted the Department's conditions, finding they would serve to minimize the risk of anticompetitive discrimination and cross-subsidization by the BOCs. See 890 F. Supp. at 6-8 (JA 6-8). Indeed, while AT&T contends that the Department's conditions must be supplemented by 2(a), it also defends them as safeguards against anticompetitive conduct. See AT&T Br. at 47-50.

The district court correctly recognized that cellular interexchange calls are not as dependent on a BOC bottleneck as are landline calls. See, e.g., 890 F. Supp. at 3-4 (JA 3-4) (distinguishing the "'Mobile Bottleneck'" from "the more familiar 'Landline Bottleneck'"); id. at 4 (JA 4) (BOC control over

wireline calls is "more complex"). The court also understood that "[a] company need not create an entire local network to get around the Mobile Bottleneck; it needs only to create a system to carry calls from the mobile switch to the interexchange carrier's point of presence." 890 F. Supp. at 5 (JA 5). But the court did not complete the analysis of the relevant facts and "seriously consider the Department's economic analysis and predictions of market behavior," Triennial Review Appeal, 900 F.2d at 297; see also id. at 300-04; Affiliated Enterprise, 12 F.3d at 234.[4] Most importantly, it did not consider how the limited nature of the Mobile Bottleneck, combined with the conditions that the Department recommended and the court adopted, would eliminate any substantial possibility that the BOCs could use their Mobile Bottlenecks to impede competition.

Moreover, if the other conditions the court imposed were insufficient to prevent use of the BOC Mobile Bottleneck to impede competition, section 2(a) would not adequately remedy that defect. The development of effective local exchange competition may satisfy VIII(C), for if the BOCs had no local exchange monopoly power, they could not use it to impede competition in other markets. However, the extent to which competition will constrain the kind of anticompetitive conduct the decree was intended to prohibit depends on the extent to which potential

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[4]The district court, however, did not accept or rely on any of AT&T's hypotheses as to how discrimination or other anticompetitive conduct might occur.

victims of such conduct would switch from BOC local exchange services to the services of other providers. A variety of factors bear on this question. These include not only whether such alternative providers exist, but also their prices, the quality of their services, and their present and likely future capacities.

Section 2(a), as the district court recognized, does not call for that kind of analysis, and it does not require effective competition. As AT&T and MCI correctly point out, 2(a) could be satisfied even if prices for CAP MTSO-to-POP services were so much higher or quality so much lower that CAPs would not provide competitive alternatives to the BOC Mobile Bottleneck. See AT&T Br. at 47-48; MCI Br. at 9-13.

3. The Decree Permits Partial Waivers That Replace Prohibitions With Appropriate Conditions

AT&T asserts that the decree prohibits "piecemeal regulatory waivers." AT&T Br. at 39. The point of its contention that wireless-originated interexchange calls do not constitute a separate market is unclear, however; it lends no support to AT&T's defense of the alternative access condition. If AT&T is arguing that the district court cannot grant a partial waiver, allowing a BOC to enter a market but not to provide all the services included in that market, see AT&T Br. at 29, its position finds no support in the decree and is inconsistent with this Court's decisions.

AT&T maintains that wireless-originated interexchange services are not a separate market, and, therefore, that a waiver

limited to such services is not permitted under VIII(C), regardless of whether it would have anticompetitive consequences. AT&T Br. at 39-44. Even if AT&T's view of the relevant market is correct, however, it does not support AT&T's contention that the alternative access condition was justified to protect competition; it undercuts it. AT&T suggests no reason why, if a waiver allowing BOCs to provide wireless-originated services would not allow them to use their local exchange market power to impede competition in those services, such a waiver could nonetheless allow the BOCs to impede competition in a broader interexchange market. To the contrary, if potential effects in the broader interexchange market are the only relevant factor, there is even less reason for concern and less justification for the district court's additional 2(a) condition.[5]

Thus, as AT&T apparently concedes, its market definition contention does not really seek to justify the 2(a) condition; it is an argument that the district court should not have granted any waiver, with or without conditions. See AT&T Br at 41. But

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[5]Accordingly, this Court need not determine whether a wireless interexchange services market is too narrow for purposes of this waiver proceeding. We note, however, that the existence of competition between wireless interexchange services and other interexchange services would not necessarily preclude definition of a wireless interexchange services market in appropriate circumstances. See, e.g., U.S. Dep't of Justice and Federal Trade Comm'n, Horizontal Merger Guidelines §§ 1.11, 1.12. Nor would the ability of suppliers of other interexchange services to provide wireless interexchange services necessarily preclude definition of such a market. Id. §1.32 (potential suppliers may be treated as participants in the market).

that argument is foreclosed because AT&T did not appeal from the grant of the waiver.

In any case, neither the decree nor any rule of law precludes the court from allowing a BOC to enter a market in some limited fashion. The issue under VIII(C) is whether the BOC's entry -- on the terms permitted by the court -- will create a substantial possibility that the BOC could use its monopoly power to impede competition in any market that the waiver would permit it to enter. See e.g., Affiliated Enterprise, 12 F.3d at 233-37 (directing consideration of proposed waiver for certain funding/royalty arrangements); United States v. Western Electric Co., 907 F.2d 160, 164-65 (D.C. Cir. 1990) (suggesting that BOC could move for a waiver to provide interexchange "gateway" service). Indeed, if a waiver with proposed limitations or conditions satisfies VIII(C), the district court must grant relief subject to those conditions. Affiliated Enterprise, 12 F.3d at 233-37. Thus, even if AT&T is correct as to the relevant market, there is no bar to a waiver allowing the BOCs to enter the interexchange services market only to the extent of providing wireless-originated interexchange services on the terms recommended by the Department.[6]

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[6]Indeed, while AT&T did not appeal the order at issue, it does not suggest that the court could grant a waiver for all interexchange services subject to the VIII(L) conditions. Thus AT&T implicitly acknowledges that there is a significant difference between interexchange services provided from wireless systems, subject to the conditions of VIII(L), and other interexchange services.

Judicial review of line-of-business waiver motions properly includes consideration of the practical difficulty of enforcing a partial removal of a decree restriction. See Triennial Review Appeal, 900 F.2d at 309 n.29. Contrary to AT&T's suggestion (AT&T Br. at 39-43), however, the Department did not base its support for a limited and conditional waiver on any particular assumptions about the percentage of total interexchange services that it would allow the BOCs to provide. We did not to seek to prevent growth of the authorized BOC services, but rather to provide safeguards against anticompetitive means of expansion. Accordingly, the waiver is confined to wireless mobile services totally separate from the BOCs' landline monopolies and subject to carefully tailored equal access, resale, unbundling and marketing conditions, but it does not limit the number of customers the BOCs may serve.

Nor does the waiver's potential applicability to interexchange calls originated through personal communications services ("PCS") undermine the waiver's limitations, as AT&T suggests. See AT&T Br. at 43. PCS-originated calls are included in the waiver only insofar as they are "commercial mobile services" provided through a subsidiary separate from the BOC landline exchange, see §VIII(L)(1)(c), and subject to the other waiver conditions. The waiver, therefore, does not provide a means for the BOCs to evade the decree prohibition that continues to apply to all other interexchange services. See US Br. at 37-39.

4. **The 2(a) Condition Largely Negates a Waiver That Should Be Granted Under VIII(C)**

AT&T and MCI do not go so far as to claim that they should control whether BOCs provide interexchange services from wireless systems. They contend, however, that 2(a) does not really give interexchange carriers that power because it "requires only that alternative access be 'provided' . . . not that it be 'used' and not even that it be 'economical.'" AT&T Br. at 45; see also MCI Br. at 7-9.

The United States accepts the view that an available but unused MTSO-to-POP access service could satisfy 2(a). Notwithstanding this theoretical possibility, in practice, 2(a) largely negates the waiver. Only one of the BOC certifications that the Department has reviewed thus far under the new section VIII(L) has identified a non-BOC provider of MTSO-to-POP access.[7] Therefore, the Department has been required to disapprove the other BOC submissions. See US Br. at 16-17.

AT&T not only disregards this present effect of 2(a) but contends that interexchange carriers will not be able to prevent future BOC entry. It argues that "in any area in which CAPs determine that they can offer cost-effective MTSO-to-POP alternatives to the RBOC monopolies, they will build the facilities"; once CAPs have done so, BOCs will be able to provide interexchange service, and interexchange carriers will have no

[7]That sole exception involved MTSO-to-POP access provided by a local exchange carrier that is not a BOC. See US Br. at 17.

incentive not to use CAPs. AT&T Br. at 45-46. However, CAPs' financial incentives to construct facilities and offer MTSO-to-POP services remain unclear.

In any event, whether or not CAPs will construct MTSO-to-POP bypass facilities in the future is not the issue. Under present circumstances, a waiver subject to the safeguards proposed by the Department satisfied VIII(C); 2(a) largely negates that waiver and therefore should be vacated.

CONCLUSION

This Court should vacate the 2(a) condition. In all other respects, it should affirm the district court's order. Alternatively, the Court should remand the motion to the district court with instructions to enter a revised order eliminating

2(a), but retaining the equal access, structural separation, resale, and unbundling and marketing safeguards that the district court properly imposed.

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CERTIFICATE OF COMPLIANCE WITH CIRCUIT RULE 28(D)(1) WORD LIMITS

I certify (based on the word count reported by a word processing system) that this brief, including footnotes, does not exceed the 6,250 words permitted by this Court's orders of July 19 and August 16, 1995.

Nancy C. Garrison

CERTIFICATE OF SERVICE

I hereby certify that on October 30, 1995, the foregoing REPLY BRIEF FOR THE UNITED STATES AS CROSS-APPELLANT (final copy with JA citations) was served by first-class mail, postage prepaid, on:

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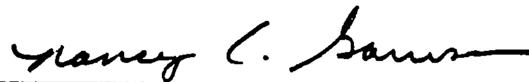

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