

**Report to the Joint Utility Review Committee
(Commission on Governmental Operations)**

**The State of AT&T North Carolina's Operations
In An Open and Competitive Retail Market**

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Senate Bill 343, "An Act Establishing The Communications Regulatory Reform and Investment Act of 2011," was ratified by the North Carolina General Assembly on April 18, 2011, and signed by the Governor on April 26, 2011. The Bill represented the next step in the continuing evolution of telecommunications regulation in North Carolina, enabling companies to elect a market-based regulatory approach for all retail services and to gain exemption from historical carrier of last resort obligations. In exchange for this market-based regulatory approach, delineated in G.S. 62-133.5(l), telecommunications companies making a subsection (l) election must forgo receipt of any funding from a State funding mechanism, other than interconnection rates, that may be established to support universal service.

Recognizing the continuing evolution of the telecommunications industry, Senate Bill 343 removes retail telecommunications regulations that were left in place by House Bill 1180, An Act Establishing "The Consumer Choice and Investment Act of 2009", for any telecommunications company making a "subsection (l)" election. Though House Bill 1180 removed most Commission oversight of retail services, it left in place carrier of last resort obligations for local exchange companies and retail price controls for standalone residential service lines offered by companies electing to be regulated under the provisions of G.S. 62-133.5(h).

The reporting mechanism to the Joint Legislative Utility Review Commission, put in place by House Bill 1180, continues for companies making a subsection (l) election. That report, delineated in G.S. 62-133.5(k), requires both subsection (h) and subsection (l) electing Local Exchange Companies (LECs) or Competing Local Providers (CLPs) who offer basic local residential service to make an annual report to the General Assembly on the state of its company's operations. The Joint Legislative Utility Review Committee has been given the task of reviewing these reports and determining whether to recommend that the General Assembly take corrective action in response to the reports. Subsection (k) stipulates that the reports shall include the following:

- I. An analysis of telecommunications competition by the Local Exchange Company or Competing Local Provider, including access line gain or loss and the impact on consumer choices from the date the local exchange company makes its election to be subject to alternative regulation under the terms of subsection (h) or (l) of this section.
- II. An analysis of service quality based on customer satisfaction studies from the date the local exchange company makes its election to be subject to alternative regulation under the terms of subsection (h) or (l) of this section.

III. An analysis of the level of local exchange rates from the date the local exchange company makes its election to be subject to alternative regulation under the terms of subsection (h) or (l) of this section.

On October 14, 2011, AT&T North Carolina (AT&T) filed its subsection (l) election letter with the North Carolina Utilities Commission in Docket P-55, Sub 1013M which included a sworn statement that (1) its territory is open to competition from Competing Local Providers; (2) that, it has a statewide rate of \$20.00 for residential basic local exchange service; (3) that, should the Commission establish a state funding mechanism, other than interconnection rates, to support universal service as described in G.S. 62-110(f), AT&T North Carolina would not withdraw from any such fund. As stipulated in G.S. 62-133.5(k), AT&T now submits its first annual report for the year 2011 to the General Assembly on the state of its company's operations since making its subsection (l) election. Prior to making its subsection (l) election, AT&T North Carolina was operating under the provision of G.S. 62-133.5(h) (subsection h) which it elected on October 5, 2009.

I. Analysis of Telecommunications Competition in North Carolina for 2011

All aspects of the telecommunications market in North Carolina continue to be extremely competitive. In the local exchange market, AT&T faces competition in the Consumer and Business markets from traditional competitors, such as Competing Local Providers (CLPs), and from wireless companies, cable companies and others offering voice, data and video services, often as applications on high-speed broadband lines. As a result, AT&T experienced a drop of 148,268 access lines in 2011, which equates to a 13.2% loss. Total residence lines declined at a higher rate, dropping by 117,911 (17.0%) over the same period.

Today's communications market continues to be transformed as consumers increasingly use wireless and Internet services as an alternative to traditional wireline voice lines. CLPs, wireless, cable, satellite and alternative voice and data providers, including Vonage and Skype, compete with Incumbent Local Exchange Companies (ILECs) like AT&T to provide communications options in North Carolina. North Carolina consumers have a wide variety of services, technologies and bundles available to them and these ever-expanding options continue to have a significant effect on the decline in access lines for AT&T and other ILECs.

Wireless - Improvements and innovations in wireless service, devices and pricing have contributed to a continued upward trend in wireless growth and a simultaneous decline in landline connections. According to the FCC, as of December 2010, wireless connections in North Carolina totaled 8.5 million, compared to 3.3 million ILEC and CLP switched access lines.

Nationwide, by June 30, 2011, the number of wireless subscriber connections had risen to 322.9 million, a 7.0% year over year increase. In fact, for the first time in history, the number of wireless subscriber connections surpassed the entire population of the United States and its territories yielding a wireless penetration rate of 102.4 percent. During this same period Smart phones and wireless-enabled PDAs increased from 61.2 million to 95.8 million devices, a 57% increase. Landline access line decline can be substantially explained by the growing number of consumers disconnecting their wireline connections in favor of wireless phones. Preliminary results from National Health Interview Survey (NHIS) indicate that more than three of every ten American homes (31.6%) only had wireless telephones during the first half of 2011, up from 26.6% during the first half of 2010.

Broadband – In addition to wireless, Internet communications services are also expanding rapidly. According to the latest available FCC data, as of December 2010, North Carolina consumers had in place 2.4 million fixed broadband connections, representing 64% of NC households. Total broadband connections including DSL, cable and mobile wireless were 3.96 million residential connections and 848 thousand business broadband connections. The percentage of North Carolina households with access to broadband technology was 93% for DSL and 94% for Cable. As broadband connections have grown, so have Voice over IP (VoIP) services and applications which serve as an alternative to traditional wireline local telephone service. The latest FCC data indicates that by December 2010 VoIP lines in North Carolina had grown to approximately 890,000 lines, with over 90% of these being residential lines. This represents an increase in VoIP lines of 16.2% over December 2009 and 41.3% over December 2008.

Bundled Services – Bundled services, which can include any combination of voice, broadband, television/cable and wireless, continue to provide a means for consumers to take advantage of significant savings when they use one service provider for many of their communications services. Consumers no longer view “plain old telephone service” (POTS) as the single technology for communications. As they have for the past several years, consumers continue to mix different technologies, providers, and services to meet their communications needs.

Bundles continue to evolve based on changing consumer preferences and technological advancements in North Carolina’s telecommunications marketplace. AT&T offers a wide variety of voice, data, wireless and video packages, including our feature-rich U-verse service, which provides advanced television, high-speed Internet access and voice service delivered using VoIP technology. AT&T provides advanced television service through either its IP based U-verse service or through its partnership with DirecTV. During 2011, we continued to grow our U-verse footprint in the Charlotte, Raleigh and Asheville LATAs and expanded into Kernersville, Lewisville, Stanleyville and Walkertown. AT&T’s flexibility in bundling video with these other services was enabled by the North Carolina Legislature’s passage of HB 2047, The Video Service Competition Act, in 2006. Passage of the Act streamlined the video franchise process to encourage

AT&T and other companies to provide home television service through a wired, non-satellite connection.

Social Networking - The growth of broadband and wireless has been largely driven by explosive growth in applications, particularly social networking. For instance, in 2011, Facebook users (who have the ability to communicate using instant messaging, pictures, email and video) totaled over 800 million, a 33.3% increase over 2010 and a 128.6% increase over 2009. More than 350 million active users currently access Facebook through their mobile devices. Twitter, another popular social networking site that offers microblogging, boasted 100 million active users during 2011 who generated 250 million “Tweets” per day. In addition, as of 2011 more than 1 trillion video playbacks had been watched on YouTube or the equivalent of 140 playbacks for every person on earth.

II. AT&T’s Service Quality Results

AT&T contracts with a market research company to conduct surveys within 48 hours of a consumer’s interaction with the company. Customers are asked a range of questions pertinent to their contact with AT&T. These questions address their overall experience in areas including installation, sales, service and repair. The rating scale provided to the customer is Very Satisfied, Satisfied, Neutral, Dissatisfied or Very Dissatisfied. For the years 2009¹ and 2010², 82% of the AT&T’s North Carolina residential customers who were surveyed said they were either satisfied or very satisfied with the experience they had with our company. The percentage for 2011³ was slightly lower at 79%.

III. Analysis of the Level of Local Exchange Rates

In 2011, AT&T North Carolina’s Basic Residence Local Exchange rates were \$20.00⁴ statewide, only \$.05 more than the same rate that was in effect at the time of its subsection (h) election filing on October 5, 2009.

Updated regulatory rules allow telecommunications companies to respond quickly to changing consumer preferences with creative pricing alternatives, including bundles, as driven by the market. This is a far cry from the days when Local Exchange Carriers had to file tariffs in order to receive approval from the North Carolina Utilities Commission to change rates or add services. Prior to the North Carolina Legislature opening markets to competition, consumers were given one choice for a residential line, and paid for each feature individually. Today, in a fully competitive market where Local Exchange

¹ At a 95% confidence level, on an annual basis, the precision is +/- 3.2%

² At a 95% confidence level, on an annual basis, the precision is +/- 2.75%

³ At a 95% confidence level, on an annual basis, the precision is +/- 4.0%

⁴ Rate is before taxes and surcharges

Companies can compete on equal terms with other telecommunications service providers, thanks to the General Assembly enacting H1180 and S343, consumers continue to be the winners both in price and choice.

Customers can realize the greatest benefit from competition by subscribing to a bundled service offering. For instance, a 2011 AT&T promotion, “All Distance,” provided Complete Choice Enhanced (a basic line with 13 popular features included), AT&T Unlimited Nationwide Long Distance Calling, 1.5 Megabit Per Second DSL, AT&T Mobility Nation 450 and a DirecTV Family Package offered the consumer savings of \$288 annually. This is just one example of the many bundled service offerings that were available to consumers in 2011, and how consumers in a highly competitive market have the latitude of selecting a plan that fits both their communications and budgetary needs at home. As more service providers elect a market-based regulatory approach, and as telecommunications services continue to evolve and merge, consumers will continue to benefit through the development of new products, improved service and aggressive pricing options.

AT&T continues to be a strong supporter and promoter of the Lifeline and Link-Up programs that provide low income households with discounted local telephone service. SB 343 specifically retained the North Carolina Utilities Commission’s jurisdiction over these services. AT&T’s self-certification trial program conducted during 2009 was instrumental in the Commission’s 2010 decision to adopt self-certification as the sole means of enrolling Lifeline/Link-Up participants in North Carolina. In response to the Commission’s 2010 Order changing the certification process, AT&T had previously updated both the English and Spanish versions of the Lifeline brochure and in 2011 printed and distributed ½ million brochures and 850 posters to all JobLink Career Centers and DSS offices throughout North Carolina. These brochures and posters contained information on self certification, eligibility requirements and discounts available to consumers who qualify for Lifeline and Link-Up services in North Carolina.