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## Regulatory Approval of AT&T-T-Mobile Deal Could Hinge on Market Definition

Regulatory approval of AT&T Inc.'s proposed acquisition of T-Mobile USA Inc. may depend in large measure on whether the Department of Justice and the Federal Communications Commission only examine the effects on competition and consumer prices in local markets, rather than in the broader context of one national market in which AT&T is already a dominant player.

The question has emerged as a central issue in the early stages of the DOJ and FCC merger review process, with AT&T's competitors—namely Sprint Nextel Corp., which has the most to lose from the creation of a new No. 1 wireless carrier—arguing that regulators should scrutinize the AT&T-T-Mobile combination at the national level, not the local level, since AT&T advertises and prices services on a national basis, and since consumers, in most markets, perceive what they are actually buying as a ''national'' service.

Mindful of antitrust concerns, AT&T, for its part, has been trying to call attention to the explosive growth of the market for wireless services over the last several years—but at the local cellular market area, or CMA, level. For example, Metro PCS Communications, the company contends, currently serves about 25 percent of the market in Miami. As a point of comparison, T-Mobile's market share stands at only 11 percent nationally.

Citing 2011 first quarter earnings reports, AT&T further contends that it faces increasing local competition not only from Metro PCS, but also Leap Wireless, Cricket, and Sprint, among other market players. In the first quarter, Metro PCS added 725,000 subscribers, Leap Wireless added 331,000, and Sprint added 1.1 million, while Verizon signed up 906,000 new subscribers to AT&T's 62,000. T-Mobile, meanwhile, lost 99,000 subscribers in the first quarter.

AT&T's position has sparked a vigorous opposition campaign, with Capitol Hill just now beginning to wade into the issue.

**'Losing Forest for the Trees.'** ''Historically, this local market-by-market approach has gotten us in the situation we're in today,'' Ben Moncrief, in-house counsel managing regulatory and legislative affairs for Cellular South, told BNA in a recent interview, referring to the wireless industry, which for the past decade has been marked by concentration and consolidation. ''By focusing on the 'license' level, regulators risk losing the forest for the trees.''

The critical issue to merger opponents like Cellular South, which serves 900,000 customers in Mississippi, the Memphis metropolitan area, the Florida panhandle, and parts of Alabama and Georgia, is AT&T's ''national'' dominance over secondary markets for devices and infrastructure.

The scale that AT&T currently has—and will improve, post-merger—allows the company to exert a disproportionate influence over the production and sale of the latest and greatest mobile phones and devices, Moncrief says, which Cellular South customers naturally want to purchase.

''They ask for that device that's being marketed by AT&T and Verizon nationally, at the same price everywhere in the country,'' Moncrief said. ''You have to have national scale to compete.''

Moncrief expressed concern that despite the FCC's recent decision to require AT&T and Verizon Wireless to enter into data-roaming agreements with competitors on ''commercially reasonable terms and conditions,'' without the interoperability of devices—especially in the 700 megahertz spectrum band, where both AT&T and Verizon are building out 4G LTE (fourth-generation long-term evolution) networks—companies like Cellular South will struggle to compete against the new ''Big Three'' (AT&T, Verizon, and Sprint) on a national level.

''They've [AT&T] argued for years that this a national market,'' Ernesto Falcon, director of government affairs for the public-interest group Public Knowledge, noted on a recent conference call with reporters. ''If the fifth-largest carrier merged with every single remaining regional and local wireless carrier, they would still be smaller than T-Mobile. The wireless market is national and is already dominated by a duopoly.''

In recent weeks, Cellular South, Sprint, the Rural Cellular Association, and a coalition of public-interest groups have been urging the DOJ and FCC to examine the deal in the context of one national wireless market, which is not typically how the agencies analyze mergers and acquisitions.

**'Local v. National' Becomes Debate Flashpoint.** If regulators define the geographic market as national, the presumptive finding will be that a combined AT&T-T-Mobile would control a 40 percent market share. In

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most cities and towns across the United States, AT&T-T-Mobile would control slightly more than 30 percent of the market. Under antitrust law, a post-merger market share of 30 percent and higher is generally considered ''excessive.''

Analyzed on a local-market basis, the deal in most markets would reduce the number of competitors from six to five, or five to four—not four to three.

In AT&T's public-interest filing to the commission, the company points out that the FCC has ''repeatedly concluded'' that the ''geographic market is local rather than national'' and consists of CMAs or, alternatively, CEAs (component economic areas).

The geographic market, the FCC has explained, is the area within which consumers are ''most likely to shop for mobile telephony/broadband services.'' For most consumers, this market will be a ''local area, as opposed to a larger regional or nationwide area,'' according to the commission

The Department of Justice, AT&T notes, has also concluded that mobile services are offered in ''numerous local geographic markets,'' given that customers generally choose among providers that market services ''where they live, work, and travel on a regular basis'' and ''[t]he number and identity of—providers varies among geographic areas.''

''AT&T's own market research confirms these conclusions,'' the company wrote. ''The great majority of AT&T's new customers. . .purchased their wireless service locally, either through a company-owned store, local outlets of chain stores such as Radio Shack, Best Buy, Target, AT&T agent stores, or other local retail stores.''

**Lawyers See Precedent to Reject Deal.** A half-dozen lawyers and economists interviewed for this report were divided about whether the merger of AT&T and T-Mobile, even after a forced divestiture of assets, might still violate established ''safe harbors'' in antitrust law.

One lawyer who declined to be named said the DOJ has ample precedent to reject the deal outright, despite a recent history of endorsing major telecommunications mergers.

In 2000, federal antitrust authorities blocked the proposed $129 billion merger between MCI WorldCom and Sprint, at the time the largest corporate merger in history.

The deal would have combined the No. 2 and No. 3 long-distance companies with one of the top five national wireless phone companies and given the merged company control over a majority of internet backbone traffic.

''The DOJ's actions [in 2000] showed that antitrust officials were very concerned about allowing Ma Bell's market dominance to be recreated,'' the lawyer said.

At that point in history, three companies—Sprint, MCI WorldCom, and AT&T—controlled 80 percent of the long-distance market.

For long-distance services between the United States and overseas nations, MCI WorldCom and Sprint together would have assumed about a 30 percent share of the market, with this ''Big Three'' carrying about 80 percent of the total traffic.

As for international private telecommunications line services, the two companies would have controlled about 37 percent of the market and a monopoly on private-line communications between the United States and at least 12 other countries.

**Big Four to Big Three.** While a Sprint-MCI WorldCom would have spelled the end of the Big Three long-distance carriers, an AT&T-T-Mobile would *create* a new ''Big Three'' in the nationwide wireless market. The No. 2 (AT&T) would acquire the No. 4 (T-Mobile), leaving AT&T, Verizon Wireless, and Sprint Nextel as the remaining three ''nationwide'' wireless carriers, in that size order.

After the merger, AT&T and T-Mobile would serve a combined 130 million users, supplanting Verizon Wireless as the No. 1 wireless carrier in the United States. Together AT&T and Verizon would control 76.2 percent of the market for post-paid wireless voice and data communications services, with Verizon serving 96 million customers. Even after adding net subscribers in the first quarter, Sprint ended 2010 with just 50 million subscribers.

''The DOJ's antitrust division has a simplistic role,'' explained Alan Pearce, a former chief economist of the FCC, during BroadbandCensus.com's most recent Broadband Breakfast Club event. ''Which is: one competitor is better than no competitors; two competitors is better one competitor, three is better than two, and so on. That doesn't do it today. I think [Christine Varney, assistant attorney general for antitrust at the DOJ] has to expand the role to look into many other issues.''

Pearce disagreed with the idea of analyzing the merger based on local markets.

''This is such a big deal and has so many implications attached to it that the barriers against affirmation of the deal are pretty high,'' he said.

One lawyer who declined to be identified out of concern for disrupting the review process said the FCC and DOJ may refer back to the 1999 multi-agency review of Exxon Corp.'s acquisition of Mobil Oil for guidance. In that case, the Federal Trade Commission decided on a broad approach, and reviewed the deal in each area where the companies competed—exploration and production, refining, and marketing—and against the backdrop of an ''ongoing trend of consolidation and concentration'' in the industry.

''The DOJ may be inclined to take a more national, even global view, on the competitive effects and risks to consumers,'' the lawyer said.

**Local-Market Analysis Has Prevailed.** But speaking at the Broadband Breakfast Club event this month, Justin Hurwitz, a visiting assistant professor at the George Mason University School of Law and a former DOJ attorney, expressed confidence that both the FCC and DOJ will conduct an analysis of the merger on a local market-by-market basis.

''This is how both agencies have historically approached transactions like this,'' said Hurwitz, who formerly served as an honors program attorney and practiced in the DOJ antitrust division's Telecom and Media Section. ''The reason for this is that the concern isn't where these services are available or where they may be used, but where consumers go to purchase these services. Does the competition for these services exist at the nationwide level? Or, as a consumer, do you go to your local Verizon or AT&T or Sprint or T-Mobile store to purchase your mobile phone? Most people go to a local store. If you live in Virginia, you don't go to Ken-

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tucky to buy your mobile phone and get your service contract.''

To Hurwitz, the question the DOJ and FCC must grapple with is whether there is some level of local or regional competition occurring in the market.

''Historically, it has been the case that companies like AT&T do have regional promotions and regional sales efforts, and individual store managers have some ability to compete directly with other firms in their local market,'' Hurwitz added.

Some antitrust experts find historical parallels for examining the deal at the CMA level in the last major merger in the wireless industry: Verizon Wireless' $28.1 billion acquisition of Alltel.

In 2008, the DOJ required Verizon Wireless to divest assets in 100 markets in 22 states as a condition of acquiring Alltel.

Those divestitures covered the entire states of North Dakota and South Dakota, large portions of Colorado, Georgia, Kansas, Montana, South Carolina, Utah and Wyoming, as well as parts of Alabama, Arizona, California, Idaho, Illinois, Iowa, Minnesota, Nebraska, Nevada, New Mexico, North Carolina, Ohio, and Virginia.

In acquiring Alltel, Verizon was also forced to divest businesses in six additional CMAs as part of modifications to two existing consent decrees. A 1999 consent decree involved Bell Atlantic Corp.'s acquisition of GTE Corp. and Bell Atlantic's agreement with Vodafone Group plc to create Verizon Wireless.

Several analysts and legal experts interviewed by BNA peg AT&T's arguments about market definition as an attempt to compel regulators to begin exploring possible divestitures, even before they have approved the deal.

''The [FCC and DOJ] must turn to the local market level to decide where they [AT&T] have to divest,'' said one knowledgeable industry source.

**DOJ, FCC Power Over Handset Market Questioned.** Under section 7 of the Clayton Act, in order to prove that a merger violates antitrust laws, AT&T's detractors must show that the effect of the merger would be ''substantially'' to lessen competition ''in any line of commerce''—which would be the ''product'' market—in ''any section of the country''—which would be the ''geographic market.''

Jonathan Lee, a former trial attorney at the DOJ's antitrust division, said the product market in the case of AT&T's acquisition of T-Mobile should be defined simply as ''mobile wireless telecommunications services,'' or the ability to provide customers with voice or data services using radio transmissions.

Most consumers in the United States use voice and data services near their homes, which is why they typically subscribe to service from providers offering service in their home city or town. As such, these market participants, Lee explained, should be viewed as service providers offering service over ''locally, geographically discrete areas,'' defined by their radio licenses issued by the FCC.

To the meet the demands of those consumers, who expect to be able to make calls or download data anywhere in the country, carriers either purchase or build out other license areas, or lease capacity on the networks of other carriers through roaming agreements.

What is more, in a competitive market, carriers take pains to try to ''differentiate'' their services. One way, Lee says, is through the selection of handsets, some of which are exclusive to particular carriers, as Apple's iPhone was to AT&T.

But for the purposes of a merger between providers of mobile wireless telecommunications services, Lee argues that the FCC and DOJ must separate handset market competition, because, while handsets are ''complementary'' products to the actual service being sold, the merger at hand is between ''service providers.''

''The wireless market is its own distinct market,'' Lee told BNA. ''This is because there is nothing that antitrust enforcers, or regulators, can do to make an essentially un-regulated third party—a handset maker—offer its product on anyone's network.''

Lee noted that the only remedy to market concentration is to require divestitures of radio licenses, or spectrum capacity.

''Regulators can block as many wireless service mergers as they want, but they can't make Apple develop an 'iPhone 6' and then offer that phone only to a specific service provider,'' Lee said.

**Economist Sees Intense Competition.** Jeffrey Eisenach, a noted telecommunications industry economist, said that overall, the market is increasingly subject to intense competition between and among platforms.

In assessing national markets, Eisenach believes the larger question for the DOJ and FCC is whether wireless carriers maintain market power in the internet ecosystem relative to handset makers, content providers, and applications providers.

''The answer is no,'' Eisenach said. ''AT&T probably does not have market power over Microsoft, Google, Apple, and Motorola.''

Ultimately, though, Eisenach questions the relevancy of using a national market definition to analyze the AT&T-T-Mobile deal.

One reason is that regulators would have to develop a collusion theory involving both Verizon and AT&T, the so-called ''duopolists'' in a post-merger world.

''When you look at the competitive dynamics, does anybody who turns on the television and watches [AT&T's and Verizon's] ads thinks that AT&T and Verizon are a cozy duopoly not competing aggressively? I don't think so,'' Eisenach said. ''Common sense, then, must transfer into the analysis. All of the market characteristics that make collusion difficult or impossible are present in the market for mobile wireless services. It's a heterogonous product. It's dynamic. If you go down the [DOJ's] list of market characteristics that make collusion improbable, they are all present here. To have a national market, you'd have to be thinking that on a national basis, three carriers are more likely to collude than four, which seems implausible.''

**Market Entry Seen as Vigorous.** Also overlooked, Eisenach says, is the breakneck speed at which players enter the market. He cited Clearwire and LightSquared as two recent entrants to the market for wireless broadband technologies and services, both of which are setting themselves up as competitors in the 4G LTE market.

''Carriers can and do go from 0 to 100 miles per hour in a period of a year or two,'' Eisenach said. ''To say that there are only four carriers is to say that there are only three or four at this instant. But there is the real

potential for a fifth and a sixth. There are not only one or two licensees of spectrum.''

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*To read AT&T's public-interest filing to the FCC, which details the company's arguments about market definition, visit http://bit.ly/eOAaFB.*



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