The Acquisition of T-Mobile by AT&T Mobility:
Merger Review Issues and Questions

INTRODUCTION

The announced acquisition of T-Mobile's U.S. wireless communications business by AT&T raises serious competition policy issues that require careful analysis by the Federal Communications Commission (FCC) and the Antitrust Division of the U.S. Department of Justice (DOJ). On its face, the four-to-three merger of AT&T/T-Mobile appears to be anticompetitive. More definitive conclusions on the likely competitive effects of the proposed merger, however, will be based on a thorough analysis in a forthcoming American Antitrust Institute (AAI) White Paper.[1] In the interim, the briefing points below present a number of preliminary key merger review issues and questions that the AAI believes are relevant to a review of the proposed merger. Finally, if scarce spectrum is the motivating factor for the proposed merger of AT&T and T-Mobile but it is *also* a barrier to entry into the wireless communications market, then the AAI believes that other solutions to the spectrum problem should be explored and made a priority for legislators and regulators.

BACKGROUND ON THE MERGER

- The proposed merger comes at a time when the U.S. wireless industry is in deep transition on a number of key fronts. Smart phone and tablet computer technologies are increasingly popular and the demand for broadband wireless communications to support ubiquitous portable computing is burgeoning, driving the development of fourth generation (4G) networks.[2]

- Scarce spectrum appears to be a constraining factor – and the major justification offered for the proposed merger – which has caused congestion in AT&T's and T-Mobile's largest service areas and potentially limits T-Mobile's ability to introduce a 4G alternative.[3] If the acquisition allows AT&T to relieve congestion on its wireless

[1] The AAI is an independent Washington D.C.-based non-profit education, research, and advocacy organization. The AAI is devoted to advancing the role of competition in the economy, protecting consumers, and sustaining the vitality of the antitrust laws. The AAI is managed by its Board of Directors, which alone has approved this filing. For more information on the AAI, please visit www.antitrustinstitute.org.

[2] AT&T to Acquire T-Mobile USA from Deutsche Telekom," Att.com (March 20, 2011), http://www.att.com/gen/press-room?pid=19358&cdvn=news&newsarticleid=31703&mapcode=corporate|financial.

[3] Karl Bode, "AT&T Tries to Sell T-Mobile Deal," dslreports.com (March 21, 2011), http://www.dslreports.com/shownews/ATT-Tries-To-Sell-TMobile-Deal-113289. AT&T General Counsel Wayne Watts elaborated on the spectrum problem: "For different reasons both AT&T and T-Mobile are facing impending spectrum shortages in major markets. T-Mobile is also limited in its spectrum capacity, so much so that T-Mobile has no spectrum to build out an LTE [long-term evolution] network."

broadband service, AT&T will gain a government-assisted competitive advantage over its rivals in providing nationwide wireless broadband service.

THE MARKET FOR WIRELESS COMMUNICATIONS SERVICES

- The U.S. currently has four significant wireless communications carriers (AT&T Mobility, Verizon Wireless, Sprint-Nextel and T-Mobile) providing service to almost the entire nation. There are also several much smaller carriers, at least one of which provides regional service in most major metropolitan areas.

- Assuming the market is defined as a national market for wireless communications services, the proposed merger would result in about a 45 percent market share for the combined AT&T and T-Mobile, increasing concentration (as measured by the HHI statistic) by over 600 HHI points to over 3,000 HHI in a highly concentrated market.[4] These statistics understate concentration in the industry because only the four major carriers can serve consumers who seek mobile access in most of the nation.

- Under the DOJ/Federal Trade Commission (FTC) revised HORIZONTAL MERGER GUIDELINES, such a merger is presumed to be likely to enhance market power.[5] Substantial barriers to entry – as there are in the case of AT&T/T-Mobile – exacerbate this concern.

- The DOJ or FCC may consider competition between wireless and wire-line access services when evaluating the effects of the AT&T/T-Mobile merger. Markets could be defined more generally as "internet access markets," including both wireless and wire-line access. Under such circumstances, AT&T's broad ownership of both (e.g., DSL broadband and mobile broadband, fixed and wireless telephony) will cause the merger to reduce the number of options available to consumers in AT&T's wire-line service areas.

ISSUES RELATING TO THE LIKELY ANTI-COMPETITIVE EFFECTS OF THE PROPOSED MERGER

- T-Mobile is arguably a maverick firm in the wireless industry and eliminating it through merger increases the risk of post-merger price increases. Early on, the carrier introduced smart phone data plans and technology. T-Mobile's service prices are also generally lower than the prices of the other major carriers. The maverick theory may

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[4] We note that post-merger, the combined market share of the top two firms in the industry (Verizon and AT&T/T-Mobile) will likely be above 70 percent. A more accurate estimate of the change in market concentration due to the proposed merger will depend, in turn, on more accurate estimates of the market shares of AT&T and T-Mobile. As a result, the combined share of AT&T/T-Mobile and the merger-induced change in concentration cited in the text should be considered "ballpark."

[5] U.S. Department of Justice and Federal Trade Commission, HORIZONTAL MERGER GUIDELINES (August 19, 2010), Section 5.3.

depend, however, on whether T-Mobile can be a viable competitor in the 4G market, if not independently, then as part of another company that would be a competitive threat to the leading wireless companies.

- Were prices to increase after an AT&T/T-Mobile merger, smaller carriers such as Sprint-Nextel or the regionals, do not have access to enough spectrum to enable them to serve substantially more customers. Without this constraint on a combined AT&T/T-Mobile, the proposed merger creates a real danger of price increases.

- The merger will tighten the oligopolistic structure of the industry and enhance the possibility of adverse effects through coordinated interaction. This could drive prices higher, reduce choice, and stymie innovation related to easing the spectrum problem. In an industry where consumer unhappiness about service and billing runs high, it is particularly important to maintain an adequate range of choices, so that consumers can switch service providers with relative ease.

- The proposed merger might force a marginalized, less viable Sprint into a merger with Verizon, further concentrating the industry.[6] The effect of a merger on prompting reactive or follow-on consolidation should be an important consideration in evaluating the AT&T/T-Mobile deal.

- The merger could reduce the likelihood that more wireless spectrum will be made available, threatening longer-term competition in wireless broadband communications. Pre-merger, all wireless carriers favor expanding the spectrum for wireless and using an incentive auction to assign this spectrum to carriers. The outcome is uncertain, however, because it pits wireless communications against television broadcasting, which opposes the plan. Post-merger, if AT&T acquires spectrum sufficient to relieve congestion on its wireless broadband networks, the acquisition may cause two advocates of allocating more spectrum to wireless to be replaced by one opponent.[7]

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[6] Not surprisingly, Sprint has expressed concerns about the proposed merger of AT&T/T-Mobile. See, e.g., Ina Freid, "Sprint: AT&T's T-Mobile Buy Would "Dramatically Alter" Market," All Things Digital (mobilized.allthingsd.com) (March 20, 2011), http://mobilized.allthingsd.com/20110320/sprint-atts-t-mobile-buy-would-dramatically-alter-market/.

[7] The National Broadband Plan proposes reallocating 120 MHz of spectrum from TV to wireless communications. But broadcasters also want to use the spectrum, they have to provide new services, including multi-channel pay-TV, as adjuncts to existing TV, which has caused them thus far to oppose the incentive auction.

ENTRY IS UNLIKELY TO DISCIPLINE A POST-MERGER PRICE INCREASE

- Existing spectrum remains insufficient to support expected future growth in high-speed broadband services. Reallocation of spectrum from non-wireless to wireless communications through an incentive auction could reduce these constraints. Sources include spectrum allocated to government and some of the allocation to over-the-air TV, which requires less spectrum for broadcasting each channel due to the switch to digital TV. The outcome of the incentive auction debate, however, is currently unclear. Spectrum scarcity is therefore real, and a barrier to entry if no additional spectrum becomes available.

THERE IS NO EVIDENCE THUS FAR THAT SUPPORTS AN EFFICIENCIES ARGUMENT

- AT&T and T-Mobile argue that by combining their spectrum assets, the combined carriers can provide more advanced wireless services at lower cost.[8] This makes economic sense only if combining the networks of AT&T and T-Mobile captures economies of scale. The FCC and DOJ must determine the validity of the claim that a very large company is more efficient than two already large companies in managing a fixed amount of spectrum. Moreover, the parties will need to show that the benefits of lower costs through economies of scale outweigh the benefits of competition.

- AT&T and T-Mobile claim that one reason to support the acquisition is that it represents an investment and commitment by a U.S. company to "advance America's leadership" in mobile broadband.[9] This is an implicit argument that standard competition policy concerns should be more relaxed for U.S.-owned carriers.[10] But both the FCC and DOJ historically have been unwilling to sacrifice competition policy objectives to protect American-owned firms. And there is little reason to believe that the goal of any wireless carrier, regardless of ownership, is anything other than expanding service as long as it is profitable to do so.

PROBLEMS ASSOCIATED WITH POSSIBLE REMEDIES

- If the FCC and/or DOJ conclude that the deal cannot go through as proposed, two types of conditions are likely to be discussed: (1) transferring spectrum and customers to other carriers in geographic areas where both AT&T and T-Mobile

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[8] "AT&T Makes Its Mobile Case," seekingalpha.com (March 21, 2011), http://seekingalpha.com/article/259292-at-t-makes-its-t-mobile-case. According to AT&T CEO Randall Stephenson, the acquisition "will improve network quality, it will get more customers access to more services, it will bring advanced LTE capabilities to virtually every community across the United States, and it will create substantial value for our shareowners."

[9] This is particularly relevant, given the shift towards building LTE networks.

[10] T-Mobile is not the only wireless carrier with foreign ownership. Verizon Wireless is a joint venture between Verizon (55 percent ownership) and the British firm Vodafone (45 percent).

have a substantial market presence and (2) requiring that the merged entity offer roaming services to carriers that lack spectrum rights in a particular geographic area. These conditions are likely to be problematic.

- Spinning off T-Mobile operations in some cities to another carrier might preserve competition in areas where T-Mobile has a substantial presence. However, since AT&T's rationale for acquiring T-Mobile is to acquire the latter's spectrum rights in congested local markets, a spin-off is unlikely to be acceptable to AT&T. Moreover, a spin-off to: (1) Verizon or even Sprint would make the market *more* concentrated than at present and (2) a regional carrier would not be a substitute for T-Mobile's nation-wide service unless *all* of the service were transferred. These concerns make a spin-off remedy problematic.

- Under mandatory roaming, the FCC could require AT&T to offer wholesale interconnection services to other wireless carriers. However, in the absence of detailed regulation of wholesale rates, mandatory interconnection is unlikely to make the retail market competitive. Because the FCC has pursued a long-standing policy of relying on competition (not rate regulation) to keep wireless prices low, a mandatory roaming remedy would represent a major policy reversal with questionable likelihood of success.