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AT&T and T-Mobile: Good Deal, Bad Process

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The battle over AT&T's proposed acquisition of struggling wireless carrier T-Mobile officially began last month when AT&T filed papers with the Federal Communications Commission (FCC) requesting approval. The deal seems to be a sensible one, potentially benefiting T-Mobile's and AT&T's subscribers.¹ Not so sensible, however, is the process regulators will use to review the deal.

From Five Million to 300 Million. To say the wireless industry is dynamic is like saying Tibet has a few hills. Two decades ago, cell phones were a novelty with barely five million subscribers nationwide. By 2000, there were 100 million subscriptions. Today, the number tops 300 million.²

But the biggest change has been the devices themselves. Wireless devices are no longer used simply—or even primarily—to talk. Increasingly, they are used to send and receive data and video, with today's "smart" phones providing everything from Internet access to GPS.

The growth in such services has been phenomenal. In its FCC filing, AT&T reports that its mobile data traffic grew 8,000 percent from 2007 to 2010. Others in the industry have experienced similar growth—and it is continuing. In the first six to seven weeks of 2015, AT&T expects to carry as much mobile traffic as it did in all of 2010.³

Despite this vastly greater functionality, the cost of wireless service has not increased. The average consumer's bill last year was \$47 per month, about the same as in 2002 and a far cry from the average of \$70 two decades ago.⁴

More Megahertz. All of this innovation takes resources to achieve. Wireless carriers invested some \$35 billion in their networks last year alone. But dollars are not the only resource needed. Megahertz are also required.

Finding the necessary spectrum to fuel this growing sector isn't easy. That's why AT&T set its sights on T-Mobile. The Deutsche Telekom AG subsidiary has long been struggling to keep up in the über-competitive wireless marketplace. A relative lack of resources has held it back in the race to provide ever more advanced services to consumers.

And it can't count on its parent company to close that gap. Deutsche Telekom has said it wants T-Mobile to be self-funding. AT&T's acquisition opens an alternative source of investment for T-Mobile.

At the same time, AT&T subscribers could gain access to T-Mobile's spectrum. This doesn't mean that frequencies will be shifted away from T-Mobile to AT&T; neither carrier has excess megahertz lying around. But combining the two firms' frequencies into a larger pool can improve service quality. Wireless network engineer Richard Bennett puts it this way:

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It's like the difference between having one credit card with a high limit and two cards with smaller ones... [J]ust as it's easier to use the one big card that has a high limit, it's easier to manage a network with a large spectrum pool.⁵

Famous Failure. Of course, there are no guarantees. The business landscape—especially in the tech sector—is littered with phantom synergies from mergers past that never materialized. For instance, the merger of AOL and Time-Warner famously failed to provide the synergies its supporters had touted. At the same time, however, it also failed to give the merged firm the level of market power that critics of the deal feared.

The lack of certainty provides no excuse to block the deal. The job of regulators should not be to choose the best market strategy. It should be simply to make sure that the marketplace itself is working. In wireless, it's working remarkably well, and there is every reason to believe it will continue to do so after the acquisition is completed.

Combined, the two firms would serve about 40 percent of wireless subscribers, surpassing the 30 percent or so served by Verizon Communications, Inc. The remainder is served by a variety of smaller players, led by Sprint Nextel Corporation. It's no surprise that these market shares are higher than those of many other industries. This isn't the dry-cleaning industry—given the economies of scale, no one should expect mom-and-pop providers on every corner. Still, many industries with two dominant players are famously competitive: Think Coke vs. Pepsi and Boeing vs. Airbus.

Double Review. The market structure resulting from this deal is not worrisome, but the regulatory

structure in place to review it is. The acquisition undergoes not one but two separate reviews: one by antitrust authorities—in this case, the Department of Justice (DOJ)—and a second by the FCC.

The difference? While DOJ will evaluate the competitive implications of the deal, the FCC, using its authority to approve transfers of spectrum licenses, undertakes a far broader and nebulous task: to determine whether the transaction is in the “public interest.” The “public interest” standard has never been defined in any meaningful way. There is general agreement that the standard allows the FCC to consider issues broader than competition, but what, exactly, those issues are is ambiguous. While concepts such as “diversity” and “universal service” have been cited, the “public interest” standard itself is notoriously vague and arbitrary. This leaves the FCC virtually untethered in its review, unlike the antitrust authorities, who follow well-established rules in evaluating the competitive effects of a merger.

The FCC can and does use this discretion to reject proposed transactions. More often, however, it uses its review authority to further its own agenda by imposing conditions on proposed transactions. Often, the restrictions and mandates imposed in this way are only tangentially related to the transaction at hand.

Most recently, for example, the FCC considered the proposed merger of Comcast and NBC. Even though the two firms largely do not compete against each other, the commission approved the merger only with an extensive list of conditions regulating Comcast's operations, ranging from minimum speeds for broadband services to expanded children's programming to providing computers at a discount to low-income households.⁶

1. See “Acquisition of T-Mobile USA, Inc. by AT&T Inc., Description of Transaction, Public Interest Showing and Related Demonstrations, Filed with the Federal Communications Commission April 21, 2011” (AT&T filing), at <http://fjallfoss.fcc.gov/ecfs/document/view?id=7021240421> (May 13, 2011).
2. CTIA, “Semi-Annual Survey, Year-End 2010,” at http://files.ctia.org/pdf/CTIA_Survey_Year_End_2010_Graphics.pdf (May 13, 2011).
3. AT&T filing, pp. 2, 4.
4. CTIA Semi-Annual Survey.
5. Richard Bennett, “Why Is It Good to Combine Networks?” High Tech Forum blog, March 23, 2011, at <http://www.hightechforum.org/why-is-it-good-to-combine-networks> (May 13, 2011).
6. See Josh Wright, “FCC Approves Comcast–NBC Merger With Conditions,” Truth on the Market blog, January 20, 2011, at <http://truthonthemarket.com/2011/01/20/fcc-approves-comcast-nbc-merger-with-conditions> (May 13, 2011).

Net Neutrality Condition? The T-Mobile acquisition could be subjected to similar conditions. One real possibility is that AT&T Wireless could be required to abide by the FCC's "net neutrality" rules.⁷ This would enable the agency to keep the restrictions in place for AT&T even if the rules themselves are thrown out in court, as they are expected to be.

Today's dual system of merger review is unnecessary and harmful. In the regulatory marketplace, two is simply too many. Congress should restrict the FCC's authority, limiting its review to a simple confirmation that the new licensee is eligible to hold the

license, leaving merger review to the competition authorities.⁸

Wireless today is perhaps the world's most innovative and dynamic service. The acquisition proposed by AT&T promises to make it more so while allowing robust competition to continue. Those potential gains could be lost, however, should the FCC or DOJ—acting on a simplistic "big is bad" credo—wrongly move to block the transaction or use it as a vehicle to achieve other policy goals.

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7. Wendy Davis, "Lawmaker: Make Net Neutrality a Condition of AT&T/T-Mobile Merger," Daily Online Examiner, March 23, 2011, at http://www.mediapost.com/publications/?fa=Articles.showArticle&art_aid=147315 (May 13, 2011).

8. See Diane Katz, "Rolling Back Red Tape: Twenty Regulations to Repeal," Heritage Foundation *Backgrounder* No. 2510 January 26, 2011, at <http://www.heritage.org/research/reports/2011/01/rolling-back-red-tape-20-regulations-to-eliminate>.