THE AD HOC APPROACH TO TELECOMMUNICATIONS MERGERS: THE PUBLIC INTEREST COMPROMISED?

By Warren Grimes[1]

I. INTRODUCTION

It is difficult to find consistency in the U.S. Justice Department's ("Antitrust Division") responses to the wave of telecommunications mergers. AT&T was barred from purchasing T Mobile. Comcast was warned not to acquire Time Warner Cable. Other comparably sized mergers have been given the green light, albeit some with conditions, including Comcast's purchase of NBC Universal and AT&T's acquisition of Direct TV. More mergers are in the works.

Each case has unique features. The Antitrust Division's differing decisions may be rationally and perhaps persuasively explained.[2] Case-by-case analysis is, after all, the best way of dealing with the horizontal and vertical intricacies of this vital industry. Or is it?

If the goal is to make competition work in providing consumers meaningful telecommunications choices and universal access, the Antitrust Division and the Federal Communications Commission must articulate clear goals and be resolute in implementing them. In particular, mergers must be judged by the unique conditions in this industry, with sensitivity to the importance of the industry to quality of life and the needs of consumers. Generalized merger guidelines are not adequate to protect competition in this vital industry. Telecommunications-specific goals should be articulated in guidelines that are tested in public debate and, after implementation, guide industry firms, enforcers, and the courts in addressing telecommunications mergers.

Merger enforcement policy in the U.S. telecommunications industry has special importance because of the nation's commitment to minimize government control and regulation in the supply of vital telecommunications services. With the FCC on watch, no one could claim the U.S. telecommunications industry is unregulated. Still, more than most nations, telecommunications remains in the hands of private

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[2] *See* Assistant Attorney General Bill Baer, *Video Competition: Opportunities and Challenges*, Keynote Address at *Future of Video Competition and Regulation*, Duke Law School (Oct. 9, 2015), *available at* <http://www.justice.gov/opa/speech/assistant-attorney-general-bill-baer-delivers-keynote-address-future-video-competition>

firms that make decisions relatively free of government interference. The intent is to let privately competing firms supply consumers with high tech choices when telephoning, texting, transmitting data, e-mailing, or obtaining video programming (by over-the-air broadcast, cable, or internet). This free market approach has succeeded in some cases—and failed miserably in others.

II. BRIEF HISTORY AND CURRENT STATUS

A bit of historical perspective is helpful. For traditional land-line telephone service, universal access was obtained only with the help of government subsidies needed to reach small town and rural customers. By the 1950s, this goal had been largely achieved, but customers dealt with a single regulated monopoly provider. With some delay, a similar model evolved for traditional cable television, where most consumers could obtain this service from a local monopolist provider by the 1970s. The monopoly model, even with some constraining regulation, offered only minimal consumer choice and generated substantial discontent.

Technology helped to generate competition for telephone service and was potentially helpful for cable as well. For example, by the 1970s, there was competition in providing long distance service for land-line customers. By the end of the 20th century, wireless cell phone service provided a meaningful alternative, to the point that it has displaced much of the demand for land-line service. Today, there is meaningful competition in cell phone services, thanks in part to maverick firms such as T Mobile that have given consumers choices in purchasing cell phone service, including relatively low cost and unbundled plans that allow the consumer to purchase a phone separately from a subscription plan.

The market mechanism has so far failed for two other telecommunications services: cable television and high speed internet access. Most urban consumers have a choice of two or three cable providers, but no meaningful choice in avoiding an elephantine bundle of 180 or more channels, only 18 of which the average subscribing household actually watches.

There are enormous costs to this forced bundling. The lack of choice means consumers pay more—lots more. The growing cost of the expanded basic bundle (already averaging roughly $100 per month) is attributable in significant part to expensive sports programming, which half or more subscribers do not watch. Even among sports enthusiasts, many are forced to pay for sports programming that they do not watch. Some analysts claim that bundling is an efficient way of delivering cable programming. That may be, but Canadian consumers with greater choices pay substantially less per month for cable programming. Using the Canadian system as a base, one estimate is that U.S. cable consumers overpay somewhere between $27 to $34 billion each year.[3]

A second cost of the bundling system is that cable customers, through no fault of their own, suffer blackouts of popular programming, with some of these blackouts lasting months or even years. In Southern California, the majority of fans of the Los Angeles Dodgers have, over the past two seasons, been unable to receive Dodger telecasts because of an intractable bundling dispute. Time Warner Cable owns the television rights to the games and insists that the telecasts be included in the expanded basic bundle at an additional cost of roughly $5 a month, notwithstanding that most cable consumers won't watch the games. Most cable distributors are willing to carry the games on an a la carte basis, but have refused to add to the unwieldy and very pricey bundle. Meanwhile, most Dodger fans, through no fault of their own, cannot watch the televised games. None of this could happen if forced bundling ceased.[4]

[3] Warren Grimes, *The Distribution of Pay Television in the United States: Let an Unshackled Marketplace Decide,* 5 J. INT'L MEDIA & ENTERTAINMENT L. 1, 16-17 (2014).

[4] Consumers also lack choice in buying cable boxes and continue to pay yearly fees averaging $231 per year to rent these units from the distributor. CONSUMER REPORTS, 12 (Nov. 2015).

For high speed internet access, the competitive situation is no better, a matter of special concern because internet streaming is increasingly chosen as a way around the pricey TV bundles. Even in urban areas, almost all consumers have only one or two choices for obtaining broadband access. Under the FCC's new high-speed internet standards, 70 percent of all broadband users have no choice or only one choice.[5] Although FCC Chairman Tom Wheeler has made internet availability a priority, as long as hard-wired connections are required the likelihood of a quick fix providing consumers meaningful competition is slim. Even for a consumer with two choices, tacit parallel supracompetitive pricing and look-alike offerings will continue to be the norm.

III. CREATING A MORE COMPETITIVE TELECOMMUNICATIONS INDUSTRY

So what would a more competitive telecommunications industry look like? Here are three goals that should guide telecommunications antitrust policy, including treatment of mergers.

A. There Should Be a Minimum of Four Providers for All Major Telecommunications Services.

This goal has been achieved for cell phone service and was within reach for cable TV. By approving the AT&T acquisition of Direct TV, the Government lost ground on this goal for cable. For high speed internet, where most consumers, if they have access at all, have only one provider that can meet the FCC's standards, creating meaningful choices and competition will be more difficult.

The government's conditions imposed on the AT&T acquisition of Direct TV were intended to generate more broadband access. The FCC and the Justice Department apparently concluded that, for the future, broadband access is more important than choice among cable providers. That may be correct. Competition, however, cannot be mandated. Assuming that AT&T promptly expands its broadband network as promised, it is still likely to be a monopolist or duopolist in most markets it serves, a condition unlikely to lead to aggressive price competition and varied low cost options.

The government may have given up a bird in the hand (competition in cable distribution) in pursuit of an elusive bird in the bush. Will the government enforcers continue to sacrifice competition in one telecommunications market for uncertain competitive benefits in another market? Shouldn't merger policy be designed to preserve competition in all significant markets? More access and more competition is needed in the market for broadband, but that goal should be independently and comprehensively addressed, not through ad hoc settlements in merger cases that compromise competition in other important markets.

B. Abusive Bundling Practices Should Be Prohibited.

Antitrust enforcers (and the FCC) have missed opportunities to prohibit the noxious bundling practices in cable TV, with the result that disgruntled subscribers have paid billions in overcharges over the past decades.[6] These bundling practices are under siege as many younger consumers vote with their wallets not to subscribe to cable TV.

The bundling system, however, may endure for some time yet, particularly since some of the same firms implicated in the bundling practices also control broadband access, the major alternative for streaming video programming. In addition, multi-product and vertically integrated firms bundle various telecommunications services (cable, cell phone, broadband) in ways that undercut consumer choice and harm equally efficient firms that lack integration potential.

[5] Address of Assistant Attorney General Bill Baer, *supra* note 2.

[6] Grimes, *supra* note 3.

C. Vertical Integration Issues Must Be Taken Seriously.

Antitrust analysts have long paid lip service to the axiom that effective competition is superior to regulation. Unfortunately, when assessing telecommunications mergers, the agencies have not been resolute in protecting the conditions needed for effective competition. An example is the 2011 Comcast acquisition of NBC Universal. The merger combined the largest cable and broadband distributor with NBC's very substantial video programming content. The vertical restraint issues involved in this transaction were quickly recognized. Content providers expressed concern that the combined entity would favor its own content in making distribution decisions. The agencies, however, gave the green light to the transaction, subject to conditions, including one that required Comcast not to "unreasonably discriminate" in providing broadband service to content providers.[7]

Did this condition provide meaningful protection? The twentieth century history of the Bell System's discriminatory favored treatment of the integrated firm's products and services ought to have been a strong warning. Two events since that 2011 merger suggest the futility of this sort of regulatory decree. The first is that Netflix, a major independent content provider, felt compelled to sign an expensive agreement with Comcast to ensure that Netflix customers continued to receive favorable internet access through the Comcast pipeline.[8]

The second is the FCC's decision to implement net neutrality regulations to ensure equal and non-discriminatory access. The Comcast acquisition of NBC Universal contributed to the support for regulation (Netflix and other content providers joined the push for net neutrality). That regulation, if it survives judicial review, will be less effective and more costly to implement than a regime in which distributors are barred from owning or controlling content. Had the Antitrust Division and FCC stood resolutely against vertical integration, there likely would be little need for broad-based net neutrality regulation.

IV. THE NEED FOR INDUSTRY SPECIFIC GUIDELINES

The idea of industry specific guidelines is not new. Although not specifically addressing mergers, the Antitrust Division and the FTC have already issued specialized guidelines for the healthcare industry. Other prime candidates for narrowly tailored guidelines are industries most affecting quality of life, including food and drink industries and telecommunications. Each of these industries involves the sale of essential products and services to consumers. Concentration levels in these industries are of greater concern not only because of quality of life issues but also because consumers typically cannot exercise countervailing power. Consider the steel industry, where many downstream customers are themselves large firms, such as the automobile industry. The countervailing power that could discipline steel prices is absent when products and services are sold directly to consumers.

The first set of antitrust guidelines came in 1968, under the leadership of former Assistant Attorney General Donald Turner. The Merger Guidelines Turner championed were intended to anchor antitrust law in economic principles, providing certainty and manageability for attorneys, enforcers, and counselors. Those goals have been elusive for a variety of reasons. Certainly one reason is that industry-specific conditions generate widely disparate anticompetitive concerns.

The Antitrust Division has substantial expertise and interest in competition in telecommunications

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[7] Department of Justice Press Release, Justice Department Allows Comcast-NBCU Joint Venture to Proceed With Conditions (January 18, 2011), *available at* <www.justice.gov/opa/pr/justice-department-allows-comcast-nbcu-joint-venture-rpoceed-conditions>

[8] *Comcast and Netflix reach Deal on Service*, N.Y. TIMES (Feb. 23, 2014), *available at* <http://www.nytimes.com/2014/02/24/business/media/comcast-and-netflix-reach-a-streaming-agreement.html?_r=0>

services. The recent address of Assistant Attorney General Baer, focusing on the need for competition and neutrality among internet pipeline providers, is helpful.[9] But more is needed. The goal of achieving clarity and certainty would be fostered by guidelines specifically addressing telecommunications mergers and other related competition issues. Levels of concentration that may be tolerable in some industries are objectionable in an industry so vital to consumers. Vertical integration that may be relatively unproblematic outside telecommunications is troublesome when providers of popular content wield substantial leverage over distributors.

Guidelines, perhaps jointly issued by the FCC and the Justice Department, could also lessen the propensity of government enforcers to compromise away the public's strong interest in competition. Any merger investigation brings the intense involvement of agency staff on the one side and well-schooled attorneys for the merging parties on the other side (many of these attorneys are former agency staffers). Faced with conflict, there is a tendency for any Government official making enforcement decisions to compromise. An agency head may prefer a compromise solution rather than face the costs and risks of litigation. That tendency would exist, with or without specific industry guidelines. Nonetheless, if the agency's guidelines address an issue with clarity and force, the impact of the merging parties' push for a compromise will be dulled. Enforcers will have increased resolve in adhering to competition values.

There will always be a need for case-by-case analysis of mergers. Merger enforcement, however, will strongly benefit from area-specific guidelines. Specific telecommunications antitrust guidelines could generate more competition, give the consumer more choices, and provide more clarity to industry participants than the current ad hoc approach to telecommunications mergers. Government regulation is clearly a second best choice, but the United States will continue to slide down the slippery slope toward more regulation unless there is a resolute antitrust telecommunications policy implemented by area-specific guidelines.

[9] Address of Assistant Attorney General Bill Baer, *supra* note 2.