

The AT&T / T-Mobile Merger: So What Happens Now?



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Will the AT&T / T-Mobile merger end from "death by 1000 cuts" if opposition by the DOJ, FCC, competitors and consumer groups proves insurmountable? If so, what happens next?

If you didn't look up from that Thanksgiving turkey leg long enough to follow the news this past weekend, you may have missed one of the most important technology news stories of the year. The deal may be off on the AT&T / T-Mobile merger. As of this date the two wireless companies still say that they intend to salvage their \$39 billion deal but analysts say the firms are unlikely to win their mounting regulatory battles. Indeed, when faced with the news that the FCC had objections, combined with a recent antitrust suit by the U.S. Department of Justice (DOJ), AT&T withdrew its merger application from the FCC last Wednesday, November 23. AT&T also announced it was setting aside the money necessary to pay the "break up fee" it will owe T-Mobile (Deutsche Telekom) if the deal ends up imploding.

It was only weeks ago that the U.S. Justice Department paved the way with an antitrust suit opposing the merger. Now the Federal Communications Commission has taken what amounts to an adverse position against the merger as well based on recently released studies with that agency. For the AT&T / T-Mobile merger it may amount to "death by 1000 cuts" if opposition by the DOJ, FCC, competitors and consumer groups proves insurmountable. So what happens next? In this update Leo and Sharon Wrobel, along with attorney and friend Eddie Pope, take their best guess at what the next AT&T strategy will be, and whether the merger has any hope left.

What Are AT&T's Options Now

It appears that the best option for AT&T at this moment would be to focus its effort by taking on opponents to its merger sequentially. It looks like that is what they are doing. AT&T will probably first try to prevail against the Justice Department in the antitrust case, and then assuming they win, re-apply to the FCC. That won't be easy - even for AT&T and its powerful Washington lobby.

1. First, the FCC process - if one can believe it possible - is slower than an antitrust trial. Attorneys also tell us that the FCC process of assigning an Administrative Law Judge to the case involves different, and less-advantageous-to-AT&T evidentiary standard in the antitrust action.
2. A second possibility may involve sitting back and waiting a while. If AT&T wins the DOJ antitrust case, they may just wait to see who wins the 2012 presidential election. It is possible that Republicans, who as a whole were highly favorable toward the merger, might appoint one or two new, merger-friendly, FCC commissioners. AT&T is probably rooting for Romney, Gingrich or Perry. It will be interesting to watch the trail of campaign money in the coming months.
3. The third and most likely scenario at this point is simply that the deal is dead for now. If so, what can we expect?

The FCC and the DOJ don't want competition by T-Mobile against AT&T and Verizon to go away. Even so, it's not like either of them can force T-Mobile (Deutsche Telekom) to keep running a company they don't want anymore. So if AT&T did not buy T-Mobile, who if anyone would?

A Verizon acquisition is unlikely for a number of reasons. First, Verizon has stated publicly that they are not interested in T-Mobile. (Verizon did however take a *neutral* stand to the AT&T merger, precursor to a Verizon bid for Sprint perhaps?)

The killer card in that deck for a Verizon acquisition or merger is that all the same reasons the FCC and DOJ would block an AT&T / T-Mobile merger apply equally to Verizon. That leaves another possibility: selling T-Mobile to Sprint.

That's not exactly an easy matter either since there are technology differences in the two companies' network. T-Mobile uses a GSM network, which is directly compatible with AT&T, who also uses GSM. Sprint uses an incompatible CDMA standard. (Interestingly enough, like the Verizon network, lend us to further ponder the ease of a Verizon / Sprint merger as opposed to a Verizon T-Mobile merger.)

There are other possibilities with longer odds, which revolve around the likelihood that AT&T may attempt to persuade the FCC to let it buy or lease wireless frequencies from T-Mobile (Deutsche Telekom). Such a deal may be contingent on selling off some assets to other competitors such as Sprint or Metro PCS. Such overtures might also come as part of a settlement offer in the antitrust suit as well. Indeed, by withdrawing its merger application at the FCC, AT&T may be attempting to refocus on its legal defense against the DOJ's suit which, is bent on blocking the merger.

AT&T is taking a \$4 billion charge in the fourth quarter of this year, which by appearances seems to indicate it will breach its promise to close the deal by September 2012. Our finance people tell us that such charges can be fickle. Things written down or charged off now can easily be reversed later if situations change. In fact, AT&T has said it will reapply for the merger at the FCC, and who knows what shape the deal making will take. For example, the Bloomberg News Agency recently reported that AT&T is preparing a settlement offer that would invest 40 percent of T-Mobile's assets. The FCC application has been withdrawn for now, but the dealing has just begun.

There may be other tactical reasons for the strategy as well: Some analysts theorize that by withdrawing the application, AT&T and T-Mobile get to keep confidential FCC documents out of the hands of DOJ attorneys working to block the deal. AT&T has denied the speculation. Had the FCC chosen to block AT&T's motion to withdraw, (we have just learned today that the FCC allowed AT&T to withdraw it without prejudice) AT&T claimed it would sue the agency. According to AT&T General Counsel Wayne Watts, who along with William Drexler have spearheaded the effort for AT&T: *"We have every right to withdraw our merger from the FCC, and the FCC has no right to stop us."* Luckily for AT&T there was no apparent FCC problem in withdrawing the petition.

So what about T-Mobile remaining independent? They are, after all, the nation's fourth-largest carrier. A few billion AT&T dollars certainly won't hurt them. (Indeed, if regulators reject the merger, AT&T will have to hand Deutsche Telekom a hefty divorce settlement of more than \$3 billion as well as frequencies and roaming agreements worth billions more.) Some theorize that cable and satellite Internet service providers may consider T-Mobile as a way to enter the lucrative wireless business by catering to the wireless consumer market. Indeed, the proposed merger had sparked heavy protests from this demographic including consumer groups and rival telecom companies. These points were also not lost on the DOJ. Their antitrust suit noted that with more than 300 million phones, tablets and other mobile wireless devices in service across the country, AT&T, T-Mobile, Sprint and Verizon would dominate more than 90% of the market. Contrary to the AT&T propaganda surrounding the merger might it be possible that other players might get a *better shot* if the deal did not go through? It's quite possible.

When and Why Did This Happen?

FCC Chairman Julius Genachowski first made his position known in a document he circulated to fellow commissioners last Tuesday, November 22. (It is reported that he called AT&T Chairman Randall Stephenson first in advance of the release.) Genachowski recommended sending AT&T Inc.'s proposed merger to an Administrative Law Judge (ALJ) for review and a full hearing. That's code for action the FCC takes when it opposes a merger, and AT&T read the tea leaves immediately.

According to an unnamed FCC official, an FCC analysis concluded the merger would result in *higher* prices for consumers, *less* innovation, *less* investment in the U.S. and *fewer* U.S. jobs. The review also cast suspicion on AT&T's assertions that *only* the merger would allow it to build out "4G" high-speed wireless Internet access. The FCC concluded that AT&T would probably build anyway, if for any reason to remain competitive with Verizon. The official wasn't authorized to speak publicly.

In addition, FCC officials alluded to a 109-page report posted recently on the FCC's web site. The report was uncharacteristically critical of AT&T. Among other things, the report concluded that the combination of two of the nation's largest wireless providers (#2 AT&T and #4 T-Mobile) would indeed harm competition, do little to expand high-speed Internet access (despite AT&T's claims) and would not lead to more jobs. The FCC staff analysis, which took six months and was based on more than 200,000 pages of documents, found that the merger would instead lead to job losses.

What Hurdles Remain for AT&T and T-Mobile?

Both the FCC and the Justice Department must approve the merger, and FCC officials have said they will provide their staff analysis and reports to the DOJ. If AT&T wins the antitrust suit or reaches a settlement with the DOJ, it can reapply for FCC approval. But the usual six-month approval would start over from the beginning. That means that even optimistically, the merger, if it happens at all, would be in 2013.

Since the merger will by all indications not be completed by September 2012, large financial penalties ensue to AT&T. This is the principal reason why AT&T is setting aside \$4 billion in breakups payable to T-Mobile's owner, Deutsche Telekom.

What Other Roadblocks Does AT&T Face?

It's a whole new ball game from when the companies first announced their huge merger plans this past spring, touting the deal as one which would enable AT&T to speed up the spread of next-generation 4G wireless service while increasing competition and lowering prices. As anticipated, however, a whole army of opponents urged the FCC to nix the deal. Those in opposition have included government agencies, consumer advocates and competitors such as Sprint Nextel Corporation. They have also included veteran law firms and consultants familiar with past AT&T performance, including the law firm of Bursor and Fisher, P.A. and longtime AT&T critic TelLawCom Labs Inc. In addition, United States Senator Al Franken of Minnesota took a notably vocal position against the merger as well. His opposition letter to the FCC cited to the record provided by TelLawCom Labs and others in opposition. The opposing side has also included comments from some 10,000 "Mom and Pops" arguing quite logically that combining second-ranked AT&T with fourth-ranked T-Mobile is bad business. For one thing it would far surpass the current largest wireless company, Verizon, in size. According to one think tank, the American Antitrust Institute, the new AT&T company would end up with 75% of wireless subscribers and nearly 80% of wireless revenue. The looming specter of fewer competitive options would cause millions of customers to pay more since fewer suppliers (absent meaningful regulation) inevitably means higher prices. There would be no real incentives to maintain service quality either for the same reason. Force reductions and layoffs would also be likely, since the merger would nix redundant demands for skilled technicians, engineers and other surplus employees. Craig Aaron, chief executive of the public advocacy group Free Press, said in a statement

"This merger would kill competition, put tens of thousands of people on the unemployment line, and leave all of us paying more for our mobile phones. No amount of spin can change the fact that this deal is cooked. It's time for these companies to walk away."

As an aside, Free Press created a hilarious ad campaign based on the T-Mobile Girl that went viral on the Internet. We mentioned it in a previous article, but since then they have chosen a winner from four candidates. Take a look⁴ it's pretty funny.

So What Happens Next?

Late Wednesday, both companies filed to abandon their FCC merger application. The FCC has now allowed them to withdraw the application without prejudice, which means they can in fact re-file again in the future.

In joint statements quietly released Thanksgiving Day (while financial markets were closed) the companies said they would try again for the FCC's go-ahead "as soon as practical" and stressed that they "are continuing to pursue the sale." We will continue to monitor this case and report back to you on any major changes. In the meantime thanks for reading.

About the Authors

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