AT&T/DIRECTV Merger –A Review of the Potential Harms and Proposed Remedies by the Federal Communications Commission

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Abstract

AT&T and DIRECTV filed an application to merge on June 11, 2014, in cash-and-stock mergers and acquisition transaction that will see both companies running AT&T's U-verse which offers packages of high-speed broadband, video, and VoIP services and DIRECTV's direct-to-home digital satellite television services. This paper briefly assesses the harms and proposed panacea to the harms by the Federal Communications Commission which approved of the merger but ordered the two applicants to implement the proposed remedies.

Introduction

The federal communications commission hereafter referred to as "FCC", is one of the communications regulatory bodies and it does a great job in overseeing the day to day activities of players in the communication industry, it goes as far as possible to review business transactions between these parties to ensure they do not harm any of the parties involved in the transaction, nor consumers who demand these services provided by these industry players. In June 2014, AT&T and DIRECTV came to a consensus to merge their video services, in what seemed to be two disparate lines of video services (Satellite TV and high speed IPTV), the two parties went ahead to agree to merge these lines of business which would be under AT&T's umbrella of online video products. Under the terms of the agreement of the stock-and-cash transaction, each share of DIRECTV common stock will be equated to $28.50 in cash plus the right to receive AT&T's common stock between 1.724 and 1.905 shares depending on AT&T's stock price prior to closing [1].

The two applicants filed to merge their TV services and served the FCC a copy of the application as required by the FCC. FCC carefully reviewed the deal and as always with both parties and the consumer in mind approved the transaction but raised a few harms that could be caused and proposed remedies to these harms. This review is pursuant to Section 310 (d) of the Communications Act of 1934, which requires that "(d) No construction permit or station license, or any rights thereunder, shall be transferred, assigned, or disposed of in any manner, voluntarily or involuntarily, directly or indirectly, or by transfer of control of any corporation holding such permit or license, to any person except upon application to the Commission and upon finding by the Commission that the public interest, convenience, and necessity will be served thereby [2]. Any such application shall be disposed of as if the proposed transferee or assignee were making application under section 308 for the permit or license in question; but in acting thereon the Commission may not consider whether the public interest, convenience, and necessity might be served by the transfer, assignment, or disposal of the permit or license to a person other than the proposed transferee or assignee" [2].

From an economic point of view, as illustrated by the graph in fig 1.1 plotted from data in table 1.1, the mergers will make both TV Service providers (especially AT&T) the market leader. Prior to the merger, AT&T had 5.94 Million Subscribers, DIRECTV had 20.35 Million customers and Comcast was the market leader with about 23.5% market share by subscriber count (22.38 Million Subscribers). The merger shot AT&T/DIRECTV to become the market leaders with 26.29 Million subscribers representing 21.64% market share pushing Comcast to the second position with 18.42% market share by subscriber count.

TV Provider	Subscriber Count
Comcast*	22383000
Time Warner	10992000
Charter	4293000
Cablevision	2681000
Suddenlink	1138400
Mediacom	890000
Cable ONE	451217
Other Major Private Cable Companies**	6450000
DirecTV	20352000
DISH	13978000
AT&T U-verse^	5943000
Verizon FiOS	5649000
AT&T U-verse^/DirectTV	26295000

Table 1.1 TV Providers by Subscriber Count [3]

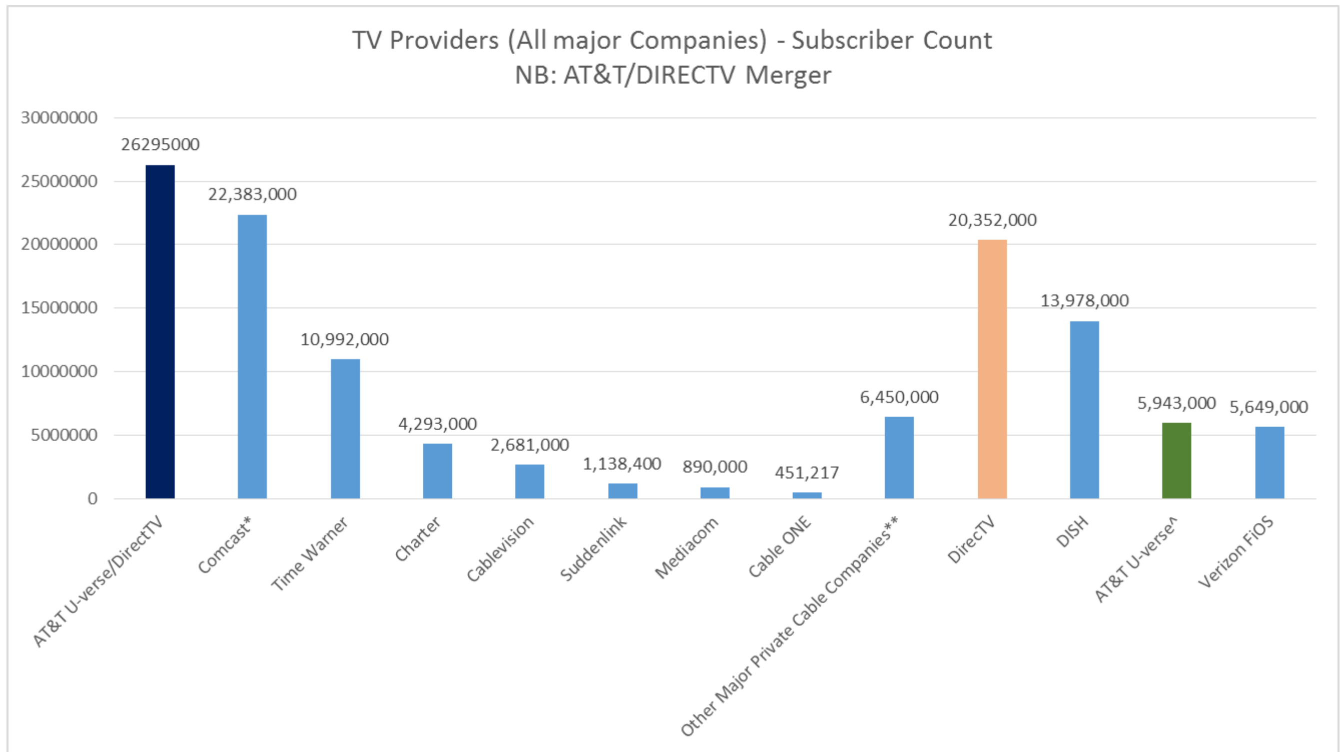

Fig 1.1 All TV Providers in the US – 2014

It is also interesting to note that although HHI calculations by the FCC revealed that the merger would result in a highly concentrated market, the FCC overlooked the high HHI values and instead considered "potential harms" that competition and consumers would suffer.

The Harms of the Merger

1. Increased Incentive to Discriminate Against Unaffiliated OVDs through "data caps" and "bandwidth throttling"

Several stakeholders have expressed concern about the merger, they posit that the transaction would discriminate against unaffiliated OVDs to favor AT&T's own enhanced bundle of MVPD and OVD services through the use of discriminatory data caps, and degradation of interconnection with AT&T's broadband network [1].

AT&T rejected the claim and said it that rather than discriminating against online video, they are encouraging the growth of online video services and providers, including by investing in their own OVD services [1].

The FCC concluded that AT&T had a high possibility of discriminating against unaffiliated OVDs as it had found in similar cases, broadband service providers can disadvantage the operation of other internet-based service providers that compete with their own.

Data caps and interconnection issues were the two major concerns raised by stakeholders and competitors in the market. AT&T could impose data download limits (data caps) on users accessing other content via its broadband service and exempt its customers from these data caps, these are legitimate concerns as neither the FCC nor the other regulatory bodies have access to AT&T's systems to monitor data usage and behavior of the subscribers of other video providers.

Netflix and Cogent complained about AT&T's deliberate throttling of bandwidth at points where Cogent feeds Netflix's content into AT&T's network. Cogent and Netflix claim they had to pay AT&T extra interconnection cost to ensure their customers experienced the best video qualities.

These claims made by stakeholders and competition are worth considering as it can affect not only competitors but the experience enjoyed by subscribers accessing online video from competitor video providers.

Proposed Remedies

The FCC in summary proposed two major solutions to the harms above which ordered AT&T to:

1. Desist from data capping, which would negatively affect subscribers from other competitors.

2. Disclose their interconnection agreement with third parties to the commission after the merger and engage independent companies to access and regularly report on interconnection metrics.

3. AT&T will deploy its highest-speed fiber connections to at least 12.5 million more customer locations (including schools and colleges) within four years of the transaction closing [1].

Brief Analysis of Harms and Proposed Remedies

The FCC and stakeholders did not address the fact that a HHI creates a high market concentration and as such tends to make the market leader a “market power”.

A market power can significantly control price and introduce entry barriers which can make existing competitors and potential market entrants suffer a great deal of financial constraints in terms of operating costs and costs of entry respectively.

Although these remedies seem sufficient, it does not factor the possibility of AT&T deteriorating service/experience delivered to customers at random times, e.g. AT&T could set an algorithm to randomly degrade service/quality delivered to customers accessing online video from other competitors in a way that the bandwidth at interconnection points would be high but the quality of service at the access level (where customers access the video) would be randomly deteriorated (e.g at peak hours).

Also, the FCC just ordered AT&T to refrain from imposing limits on data allowances without proposing how and what would happen if AT&T does not. AT&T in compensation for the data caps can reduce download and upload speeds in accessing these online videos and get away with it.

Conclusion

We have reviewed the AT&T/DIRECTV merger, the potential harms, and proposed panaceas to the harms. We briefly accessed the harms and proposed remedies and considered situations that can arise but were overlooked by the FCC. The merger would create a concentrated market, which reduces competition and creates a market power, however, FCC’s unusual imposition of conditions on approving the merger with the consumer in mind as well as advocating for the roll out of Fiber network to colleges and schools is laudable.

References

[1] Federal Communications Commission, (July, 2015). In the Matter of Applications of AT&T Inc. and DIRECTV for Consent to Assign or Transfer Control of Licenses and Authorizations, [MB Docket No. 14-90]. [Online] Available: https://www.fcc.gov/document/fcc-releases-order-approving-att-directv-transaction

[2] Communications Act of 1934, (June, 1934), SEC. 310 (d). (pp. 162), [Online] Available: https://transition.fcc.gov/Reports/1934new.pdf

[3] Leichtman Research Group, Inc (Dec, 2014). Major Pay-TV Providers Lost About 125,000 Subscribers in 2014 [Online], Available: http://www.leichtmanresearch.com/press/030315release.html