



# CPI Antitrust Chronicle

October 2011 (2)

## Will the 2010 Merger Guidelines Survive the DOJ's Complaint in *U.S. v. AT&T*?

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# Will the 2010 Merger Guidelines Survive the DOJ's Complaint in *U.S. v. AT&T*?

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## I. INTRODUCTION

AT&T's proposed acquisition of T-Mobile presents an opportunity for judicial scrutiny of the newest iteration of the Department of Justice ("DOJ") and Federal Trade Commission's (FTC's) Horizontal Merger Guidelines ("2010 Guidelines"). The Agencies revised the 2010 Guidelines with an eye toward increasing transparency and predictability by conforming them to actual agency analysis. The 2010 Guidelines highlight the Agencies' adoption of a more economically sound analytical approach focusing directly upon the competitive effects of proposed mergers and de-emphasizing the importance of market definition and competitive inferences from market structure.<sup>2</sup> But, oddly, the DOJ's complaint reverts to its pre-revision approach, emphasizing a remarkable focus upon market definition and structural analysis. The structure-heavy approach the DOJ adopts in its complaint runs afoul of the standards it espouses in the Guidelines, raising the risk of undermining their continued success as measured by judicial adoption.

## II. The DOJ's Structural Complaint and Divergence from the 2010 Guidelines

Describing the new Guidelines, then-DOJ Chief Economist and one of the intellectual architects of the 2010 Guidelines, Carl Shapiro, points to an "effects-first" approach: "[T]he 2010 Guidelines place less weight on market shares and market concentration . . . . [They] also follow a more integrated and less mechanistic approach. The revised Guidelines emphasize that merger analysis ultimately is about competitive effects."<sup>3</sup> But, contrary to the spirit of its own Guidelines, the DOJ's complaint to prevent consummation of the AT&T-T-Mobile transaction relies heavily upon market structure to make inferences about competitive effects, an analytical framework strikingly reminiscent of the outdated Supreme Court and Agency precedents of the 1960s.<sup>4</sup>

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<sup>2</sup> Carl Shapiro, *The 2010 Horizontal Merger Guidelines: From Hedgehog to Fox in Forty Years*, 77 ANTITRUST L.J. 49, 55-56 (2010).

<sup>3</sup> *Id.*

<sup>4</sup> *See id.* at 50-51.

Moreover, while the revised Guidelines recognize the potential for efficiencies to enhance competition, the DOJ's complaint essentially ignores efficiencies.<sup>5</sup> While in the Guidelines efficiencies analysis is properly integrated into an overall analytical structure aimed at diagnosing the net competitive effects of mergers, the DOJ's complaint contains only one, dismissive sentence relating to efficiencies.<sup>6</sup> The sentence simply reads, without any further discussion, "[t]he Defendants cannot demonstrate merger-specific, cognizable efficiencies sufficient to reverse the acquisition's anticompetitive effects."<sup>7</sup>

Against this backdrop, the Complaint begins by defining the relevant market, which includes definitions of product and geographic markets.<sup>8</sup> The DOJ defines a national market<sup>9</sup> for "mobile wireless telecommunications services."<sup>10</sup> By defining the market nationally and excluding fixed wireless and wireline services, the DOJ maintains that only the four largest carriers<sup>11</sup> compete with each other, and only on a national level, unaffected by smaller, regional competitors as well as those that provide comparable services via different technologies.<sup>12</sup>

After defining the market, the DOJ next addresses potential competitive effects. It is here that the structural nature of the DOJ's analysis is most evident, relying heavily upon the inferences from market shares and concentration. The DOJ alleges that the increased concentration resulting from the merger would exceed the threshold levels articulated in the Guidelines creating a presumption the merger would enhance market power.<sup>13</sup> However, the history of the wireless service market has shown that, in spite of high concentration, prices still decreased and innovation surged, thus evidencing increased competition and gains for consumers.<sup>14</sup> Especially in high-tech markets like the one at issue, structural inferences offer little or no value to the analysis.

The DOJ complaint also claims that coordinated conduct is highly likely in the post-merger market because the markets have "transparent pricing, little buyer-side market power, and high barriers to entry and expansion."<sup>15</sup> Without further allegations concerning the potential for coordinated conduct, and relying only upon a weak argument that T-Mobile is a maverick, the DOJ thus leans almost entirely upon the structural presumption that reducing the number of service providers from four to three would increase the risk of coordination between competitors in the national wireless market.<sup>16</sup>

It employs a similar, though more subtle, reliance on 1960s-style structural analysis in its claim regarding unilateral effects. Describing AT&T and T-Mobile as "head-to-head" competitors, it finds that there would be little diversion away from the merged firm in the face of

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<sup>5</sup> U.S. DEP'T OF JUSTICE & FTC, HORIZONTAL MERGER GUIDELINES § 10 (Aug. 19, 2010) [hereinafter MERGER GUIDELINES].

<sup>6</sup> Complaint at ¶ 46, *United States v. AT&T Inc.*, No. 1:11-cv-01560, 2011 WL 3823252 (D.D.C. Aug. 31, 2011).

<sup>7</sup> *Id.*

<sup>8</sup> Complaint, *supra* note 6, ¶ 11-21.

<sup>9</sup> *Id.* ¶ 19.

<sup>10</sup> *Id.* ¶ 11.

<sup>11</sup> The four carriers are Sprint, Verizon, AT&T, and T-Mobile. *Id.* ¶ 20.

<sup>12</sup> Complaint, *supra* note 6, ¶ 19.

<sup>13</sup> *Id.* ¶ 22.

<sup>14</sup> Gerald R. Faulhaber, Robert W. Hahn & Hal J. Singer, *Assessing Competition in U.S. Wireless Markets: Review of the FCC's Competition Reports* 8 (2011), available at <http://ssrn.com/abstract=1880964>.

<sup>15</sup> Complaint, *supra* note 6, ¶ 36.

<sup>16</sup> *Id.*

a unilateral price increase.<sup>17</sup> This conclusion necessarily depends upon the DOJ's presumption that there are only four competitors in the relevant market. Such an analysis excludes potential diversion to important regional competitors such as LightSquared and MetroPCS.

Upward pricing pressure metrics can be misleading when coupled with an implicitly assumed market definition. For example, Sprint, in its FCC submission opposing the merger, conducts an upward pricing pressure analysis under the assumption that diversion is proportional to the participants' existing market shares.<sup>18</sup> The problem with this practice is that diversion analysis is intended to aid in directly diagnosing the potential for unilateral price effects *in lieu of* an extended market definition analysis,<sup>19</sup> and incorporating a predefined market definition into the analysis thus leads to a meaningless result.

### III. THE COMPLAINT'S IMPLICATIONS FOR JUDICIAL ADOPTION OF THE 2010 GUIDELINES

The complaint is, on its face, inconsistent with the letter and spirit of the standards the DOJ set for itself in the 2010 Guidelines. That inconsistency threatens to undermine the Guidelines' heretofore virtually esteemed credibility in the federal courts. After all, what good are the Guidelines if their own authors refuse to follow their precepts? Rather than applying the Guidelines' modern economic approach to the facts of the AT&T-T-Mobile transaction, the DOJ's analysis ventures dangerously close to the structural inferences employed in the 1960s.

To roughly illustrate this point, we compare the frequency of reliance upon structural analysis in some well-known 1960s-era complaints, modern-era complaints, and the DOJ's complaint against AT&T. As the charts below demonstrate, the AT&T complaint's apparent reliance upon structural analysis exceeds that of both the modern era complaints as well as those of the infamous *Brown Shoe* structural era.

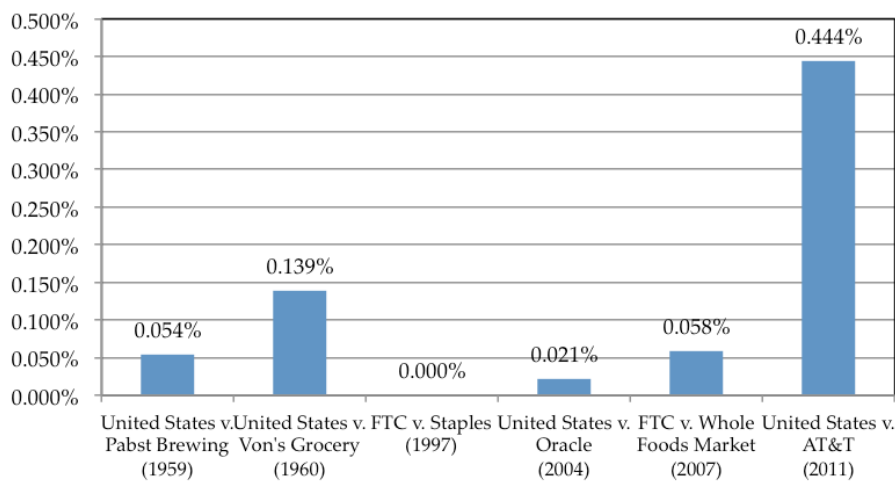
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<sup>17</sup> *Id.* ¶ 37.

<sup>18</sup> Joint Declaration of Charles River Associates ¶ 153, Petition to Deny of Sprint Nextel Corp., Applications of AT&T Inc. & Deutsche Telekom AG, No. 11-65 (FCC May 31, 2011) [hereinafter CRA Decl.].

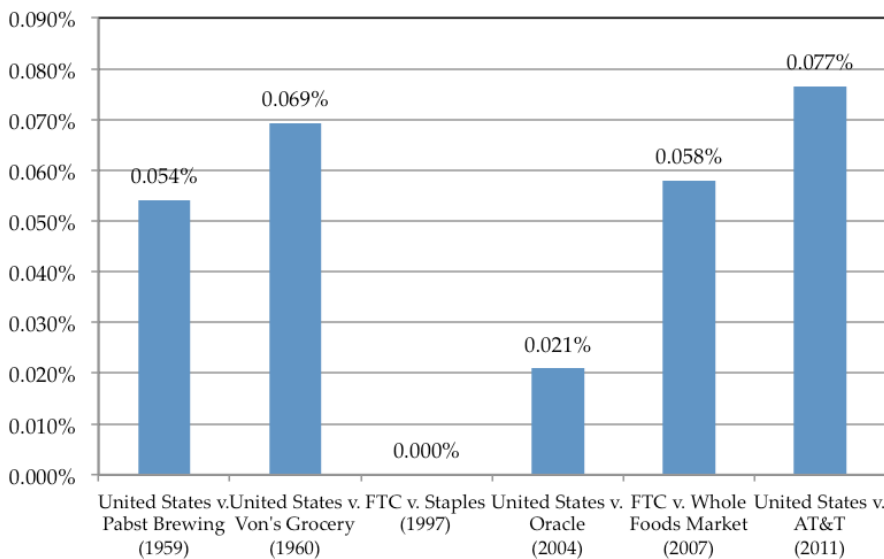
<sup>19</sup> See Shapiro, *supra* note 2, at 71.

Ratio of Structural References to Words in Complaint



Note: Structural References include: "Concentration", "HHI", "Herfindahl", "Market Share", "C4", and "C8".

Ratio of "Concentration" References to Words in Complaint



For the most part, federal courts have been willing to adopt past Guidelines and their economic and analytical approach to merger analysis.<sup>20</sup> The widespread judicial adoption, however, is largely accredited to the Guidelines “economic sophistication and consistency in

<sup>20</sup>Judd E. Stone & Joshua D. Wright, *The Sound of One Hand Clapping: The 2010 Merger Guidelines and the Challenge of Judicial Adoption*, 39 REV. INDUS. ORG. 145, 145 (2011).

application.”<sup>21</sup> The DOJ’s structure-heavy complaint is neither economically sophisticated nor consistent with the Guidelines. The DOJ fails to implement the nuanced, fact-based analysis infused with economic learning it endorses in the 2010 Guidelines.<sup>22</sup> It instead focuses upon the rigid structural presumptions intended to apply to markets for homogenous industrial products, and it does so to the exclusion of real-world market conditions like those in high-tech telecommunications markets. Thus, the DOJ’s inconsistent analysis threatens the judicial adoption of the 2010 revisions.

The Guidelines emphasize that merger analysis ultimately focuses upon competitive effects rather than upon the pre-revision, step-by-step process that always began with market definition.<sup>23</sup> Conversely, the DOJ begins its complaint against AT&T by expressly focusing on defining the product and geographic markets. Although this complies with Section 7’s “line of commerce” requirement to establish a relevant market,<sup>24</sup> the amount of weight the DOJ places on market definition undermines the spirit of the 2010 revisions.

The DOJ also relies heavily upon the argument that the merger is anticompetitive based upon the highly concentrated nature of the wireless market. The DOJ’s competitive effects analysis ultimately is founded upon market concentration theory—that decreasing the number of firms from four to three is anticompetitive—rather than an assessment of plausible actual effects. There is little to distinguish this complaint from the DOJ’s complaint against Vons Grocery in the 1960s.<sup>25</sup> Courts will be hesitant to undertake complex competitive effects analyses that the Agencies do not even employ.

#### IV. CONCLUSION

Economic learning and experience has allowed the FTC and DOJ to make significant advances in merger analysis since the 1960s. Where the Agencies previously relied upon indirect inferences about competitive effects from structural analysis, they have substituted fact-specific analysis aimed at discerning likely competitive effects directly from qualitative and quantitative evidence.

The revised 2010 Horizontal Merger Guidelines reflect this shift in Agency practice; however, the DOJ’s challenge of the proposed AT&T-T-Mobile merger may undermine the credibility of the revised Guidelines and threaten the possibility for judicial adoption of them. The DOJ’s complaint against AT&T evinces an analysis based upon structural inferences rather than rigorous economic analysis of a dynamic, high-tech market. Its inconsistency in application and apparent rejection of the modern approach may cause courts to question the viability of the Guidelines and refuse to adopt them.

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<sup>21</sup> *Id.* at 157.

<sup>22</sup> MERGER GUIDELINES, *supra* note 5, § 1.

<sup>23</sup> Shapiro, *supra* note 2, at 56 (stating that the positioning of the competitive effects analysis near the front of the Guidelines because the Agencies begin their investigations with “theories of harm to competition”).

<sup>24</sup> James A Keyte & Kenneth B. Schwartz, “Tally-Ho!”: UPP and the 2010 Horizontal Merger Guidelines, 77 ANTITRUST L.J. 587, 597 (2011).

<sup>25</sup> See Complaint at ¶¶ 5-12, *United States v. Von’s Grocery Co.*, No. 336-60-MW (S.D. Cal March 25, 1960).