Creeping Duopoly?

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Does support for robust competition remain the communications policy of the United States? It may sound like a rhetorical question. Yet it is the right question to ask as we witness increasing concentration in most communication markets, including the prospect of *de facto* duopoly in wireless communications. It was the question underlying the AT&T/T-Mobile merger last year. And it is the same question raised by the sale of spectrum and marketing agreements we examine today.

As compared with the spectacle of T-Mobile - AT&T, Verizon's softer strategy may seem a sideshow. But subtle action is often the more powerful, particularly in a distracted age. Verizon holds more valuable spectrum than anyone else, and should it complete this transaction, it will actually be left with spectrum holdings that are, by book value, larger than an AT&T/T-Mobile combination.* Yes, AT&T's challenge to competition was feckless and loud. But Verizon's deal affects the very competitive structure of the communications market.

This transaction (and others like it) does not threaten to be the grand coup that ends competition in our time. The danger, rather, is the prospect of a "creeping duopoly" in wireless, and in addition, a quiet end to the contest once thought to be the most important of all, namely, competition for the last mile. That is why the Commission must examine this transaction as closely as it did in the AT&T/T-Mobile merger.

The usual dangers of excessive concentration are well-known: higher prices, poor customer service, and, over time, a kind of depressing stagnancy. But I would also like to highlight the particular dangers to *innovation* that are the likely byproduct of non-competition between Verizon and the main cable companies.

My testimony covers three points.

1. The Duty to Decide

* *See* Comments of Sprint Nextel Corp., WT Docket No. 12-4, at 18-19.

There is nothing natural about the markets under consideration here, for the United States Government sets the structure of competition. Because spectrum is finite, necessary, and public, every decision the Government makes cannot help but affect the structure of the market. Even a decision not to intervene in a particular sale is a substantive decision with real and important effects on structure.

Unlike in normal markets, the federal government has a particular duty as regards industry structure, for spectrum belongs to the public, and it is the Government's role to make sure their asset is being used properly. That means the Federal Communications Commission cannot sit idly by and say it is allowing nature to take its course. It must, on an ongoing basis, decide whether more competition or more concentration will be better for the people of the United States. This is the essence of the "public interest and convenience" standard – it is simply the duty of managers of any asset to maximize the interests of the actual owners, the citizens.

The choice between concentration and competition is not necessarily easy. Once upon a time, Government believed that concentrated monopolies or duopolies, regulated to avoid abuse, would best serve the people. That was basically the policy behind the Commission's support of the NBC and CBS networks from the 1930s onward, the regulated duopoly in wireless in the 1980s, and even more clearly the theory behind the AT&T monopoly for most of the 20th century. Despite rhetorical nods to competition, that approach remains the favorite of AT&T and Verizon today (without the regulation, that is).

This nation's experience with both concentration and competition tends to suggest that competition yields better results for the public. The communications markets under monopoly were reliable, but began to stagnate; under competition, the same markets have been a source of abundant innovation, economic growth, and new gadgets for one and all. Relying on a few dominant firms is very good for the firms involved, but not so good for spectrum's owners, the public.

It is true that Congress or the Commission remain free to decide that a regulated duopoly or monopoly best serves the people, as it thought it did in the 1920s. But the greater danger is that Congress or the Commission will never actively make that choice. We face the prospect of falling into unregulated duopoly almost as if by accident, through choices never really made but made nonetheless.

If the Commission truly believes that greater concentration in the wireless markets serves the interest of the American public, then it should approve the sale. It is free to choose concentration over competition, if it is willing to explain that choice to the spectrum's owners. But it does the public a disservice to passively support a drift toward duopoly without explaining why we have decided against a policy of trying to maximize competition.

2. There is always a Tradeoff between Competition and Concentration

Verizon, in its filings at the Commission, suggests its gain of spectrum will improve customer service and have no effect on competition. But that, of course, is impossible. In the wireless markets, spectrum is scale. Every hertz that Verizon gains is a hertz denied a smaller competitor. And so neither Congress nor the Commission ought pretend for that tradeoff between concentration and competition does not exist.

Rather, the tradeoff faced is a familiar one. Over the last three decades, in defense of its competition policy, the United States has repeatedly faced the conflict between concentration and competition. Consider cases ranging from the AT&T breakup in 1984, the beginning of spectrum auctions in the 1990s, and most recently, the challenges to the AT&T/T-Mobile merger. In all of these cases the narrative was similar. The dominant firm argued that a more centralized and concentrated communications sector would do a better job of serving the needs of Americans. Bigger is better, the argument went; greater scale and size, said the dominant firm, will yield benefits not just for itself, but for everyone. But in each case the Government declined to take those claims at face value.

When the United States left behind the ideals of regulated monopoly in exchange for a competitive communications policy, it committed itself to a different course. It found that competition, while messier, offers more for consumers over the long run than duopolies or monopolies. This means that the Government must question claims that industry concentration is necessary for better service to consumers, and in every case must weigh any claimed efficiencies of concentration against the competitive harms.

It is true, as Verizon's filings suggest, that scale and size can yield certain efficiencies. There is no such thing as an effective one-man cell phone provider. But at some point the operational advantages of scale end and the strategic advantages begin. More concentration ceases to yield further efficiency, and becomes a means of weakening competitors. That is because a smaller competitor, denied scale (or, its equivalent here, spectrum) will remain at a disadvantage compared to the dominant firms. And so, every time we face a case like this, the question must be: will increased concentration actually be better for the spectrum owners, the people of the United States, or simply provide strategic benefits for the dominant firms?

The consideration of the AT&T/T-Mobile merger was the latest installment of this contest between concentration and competition. AT&T argued (as AT&T has almost always argued) † that a more concentrated industry would yield better service for consumers. The Commission and the Justice Department declined to take AT&T at its word. Instead, the agencies pointed out that the effect on service was ambiguous, that the merger's main effect was to eliminate a "challenger" competitor, and ultimately concluded that the merger would substantially lessen competition.

Today, the Verizon/ – Cable transaction forces us to confront exactly the same problem. Like its predecessors, Verizon argues that concentrating more spectrum (and therefore even more of the industry) in its hands will benefit consumers. But the real question is whether further concentration of spectrum in one firm will actually be good for consumers if it means less competition. The nation's policy demands this question be answered.

3. The Public's Interest in Innovation

Over the last several decades, the public and the economy has benefited enormously from the pace of innovation under a competition policy, as opposed to regulated monopoly. Much of that innovation has been of a highly dynamic, creatively destructive nature. In many cases, the once powerful have been humbled, and the meek have inherited markets.

Concerns for innovation must inform the Justice Department's scrutiny of the marketing agreements between Verizon and the Cable firms. As marketing allies, the firms on each side now have reasons to avoid developing or aggressively promoting products that might seriously threaten the revenue streams of a partner.

Verizon has been an important innovator. It was the first to try bringing fiber optics to the home, with the FiOS project. Its 4G LTE network is the furthest along. And as an innovator, Verizon Wireless is the greatest natural threat to disrupt the cable industry.

Consider, for example, 4G broadband to the home. As *PC Magazine* wrote, "[t]he mobile broadband service that has the best chance of being a true cable

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† With the exception of the years between 1984 and 2006, when AT&T was a "competitive" firm.

replacement is Verizon's new 4G LTE service." The firm's admirable "Home Fusion" product, just launched in rural areas, shows promise. Yet it is clear that 4G to the home is a cable *replacement*, not a complement. And it is not clear how selling a cable replacement can be consistent with promoting cable's products.

While a technology much promised but hard to deliver, the advent of wireless broadband to the home could turn the industry upside down. The promotion of competition in the "last mile" between the consumer and the national information networks is a long-standing policy goal of the United States. Our record of duopoly competition between cable and DSL is better than no competition. However, the potential of a "third wire" has long been something of a promised land, albeit one currently littered with the corpses of firms who have tried and failed to overcome infrastructure economics.‡

The greater, long term concern is that the industry's beloved "quadruple play" (telephone, wireless, Internet, and cable TV service), begun as a convenience for customers, could in time drift into a kind of market allocation scheme. For in truth the consumer benefits less from four services, than when one of the services tries to replace the rest.

The fate of wireless 4G is an example of the danger to disruptive innovation presented by cooperation between the cable and the telephone companies. As allies, neither side has strong reasons to disturb each other's main sources of revenue with highly innovative products. But this is precisely what a strong innovation policy requires.

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The last 30 years have shown that the commitment to actual competition in communications is not a one-time decision. It is not something that can be announced and then ignored, but rather requires constant diligence. The dominant firms in a communications industry, whatever they may say, have little interest in competition. Left alone, history suggests the industry will drift toward monopoly or duopoly. The life in monopoly or duopoly is simply sweeter and more secure, and Wall Street prefers firms that immunize themselves from competitive attack. That is why it must remain the ongoing mission of the United States government to, as Felix Frankfurter put it, "secure the maximum benefits of radio to all the people of the United States."

‡ Verizon itself might be counted as one of the firms to have tasted some of the bitterness of the last-mile with the challenges it has met in FiOS.