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AT&T Wireless–Cingular: Revealing a Lack of Regulatory Progress

Its impending merger with Cingular has been the biggest story amidst a rush of news regarding AT&T Wireless during the past few months. What is not often discussed around this merger it what it will mean to both wireless and wireline markets in the United States. Despite some surface struggles, if this deal is permitted to go through, it will reflect the strength and ability of the RBOCs to manipulate the telecom environment.

AT&T Wireless has had two consecutive unprofitable quarters. Much has been made of the fact that AT&T Wireless lost several hundred thousand customers since wireless number porting became available in November. In reality, the percentage of customers moving between carriers as a result of WNP is small – less than 2% of the total customer base according to the FCC. Many customers are bound by long-term contracts and do not have the freedom to switch providers. Regardless of any potential customer losses that could fall out of this merger, the Cingular-AT&T Wireless entity will be a dominant force.

Largely overlooked in this deal is its relationship to the wireline market and deregulation. Whatever the telecom act of 1996 may have hoped to achieve in moving away from monopolistic policy has hardly been accomplished. A review of FCC published documents reveals significant market aggregation by the RBOCs. Post-merger, the entities behind Cingular - BellSouth and SBC - would control a collective 37% of the US wireless market and 44% of all local access lines. When the total customer numbers are summed, SBC and BellSouth will control roughly 41% of the 300 million or so wireline and wireless accounts in the U.S.

SBC and BellSouth are not alone in building lofty numbers. Verizon holds 31% of all local access lines. Along with its wireless partner, Vodafone, Verizon holds 30% of the wireless market. In contrast, the collective CLEC market share of access lines has reached a whopping total of 14.7%. This is up from last year's 11.4%. The rise in percentage, however, may be due to a decrease in the total number of wireline accounts resulting from customer migration to pure wireless phone service. The total number of ILEC access lines actually fell from 167 million in 2002 to 155.9 million in 2003. During the same period, total mobile subscribers increased from 129 million to 147.6 million.

When RBOCs cry for help against the incursions of mobile and cable, it is difficult to take them seriously because of their control over both wireline and wireless markets. Even the 3rd through 5th largest mobile operators are not as strong as the largely RBOC

owned leaders. Sprint PCS has 15.9 million customers, T-Mobile 13.1 million, and Nextel 12.3 million. Their collective market share is only 33% - barely more than Verizon holds alone – and they naturally have little or no share of the local wireline market. Ultimately, the Cingular-AT&T Wireless merger is a yardstick for where the regulatory environment stands and for what it has perhaps failed to accomplish in promoting broad competition.

In related news…

The Bells have argued for years that cable-delivered voice should be subject to common carrier regulation. The cable industry had avoided the issue successfully arguing their networks were built on private capital. An October 2003 ruling has muddied the issue, however. On October 6 the 9th Circuit US Appeals Court overturned the FCC's March 14, 2002 "information service" cable broadband classification. The three-judge panel declared cable a "telecommunications service," thus subject to common carrier regulations. On April 9, however, the cable industry and the FCC won a delay of a ruling that would open cable systems to rivals to offer Internet services. If an appeal to the U.S. Supreme Court is filed by June 30, the delay will remain in effect until the high court finishes with the case, according to the 9th Circuit Court's order.

Regulation Generates Cash for States, U.S. Treasury

During the past 12 months, nearly every major incumbent carrier in the United States was fined for at least one violation of competition rules. While the fines are common, they are not necessarily proving to be effective as many carriers continue to persist and pay further fines.

Verizon was fined $5.7 million for violating a federal ban on marketing long distance services in its local region prior to FCC authorization. Verizon also broke affiliate transaction rules, failing to keep its BOC arm structurally separate from its long distance affiliate. Further, the FCC awarded $12 million to Core Communications as compensation for Verizon denying the company access in the Washington Metropolitan area, a gross violation of Section 251 rules.

BellSouth was fined $1.4 million for violating long distance marketing rules and for refusing to provide long distance services to certain CLEC customers. Cingular Wireless and T-Mobile were each hit with E911 violations. T-Mobile was fined $1.25 million for its Phase I violation, Cinglar Wireless $675,000 for its Phase II violation. Meanwhile, AT&T was fined a mere $780,000 for Do-Not-Call violations.

SBC and Qwest have been busiest at drawing fines. SBC was fined $1.35 million for long distance marketing violations. An amazing 38-month streak of SBC/Ameritech Merger term violations ended for SBC in November 2003 – not because the violations ceased, but rather because the requirement to report wholesale performance standards did. The

latest round of fines SBC/Illinois paid to the state of Illinois was $801,661, for a total of $57.3 million since July 2000. Across its 13-state territory, SBC has been fined more than $1 billion by state and federal regulators for wholesale performance standards violations. The U.S. Treasury has received $724,475 from SBC for a final total of $85.3 million in federal fines for anti-competitive behavior since 2000.

Qwest was fined $6.5 million for its long distance marketing violations. The FCC fined Qwest $9 million for failing to follow rules designed to ensure competition for local phone service in Minnesota and Arizona. This follows Qwest's settlement of $21 million in Arizona and a fine of $26 million in Minnesota, which is under appeal. Qwest asked the Arizona Corporation Commission (ACC) to keep secret the amount of restitution it would pay to individual CLECs if it adopts Qwest's latest proposed settlement of charges. The charges surround allegations that Qwest made secret preferential deals with selected CLECs in order to buy their silence regarding violations. Qwest proposed to pay restitution to 3 CLECs who weren't offered closed-door deals. It does not end there. Qwest and the Colorado Office of Consumer Counsel agreed to a settlement of charges that Qwest made secret preferential agreements with selected CLECs in order to get them to drop their opposition to Qwest's regulatory initiatives, such as its long distance entry bid. Qwest is paying $7 million to settle the charges.

It is unnerving to see these kinds of violations. Even the language of the statements is uncomfortable. The following quote, "SBC has agreed to make a voluntary payment of $1.35 million to the United States Treasury," is from the October 1, 2003, FCC news release. How many of the $1 billion dollars in fines paid by SBC were given voluntarily? If they were given voluntarily, it suggests SBC has much to gain through paying fines and failing to meet wholesale performance standards – thus hamstringing their competition.

Lastly, WorldCom is emerging from bankruptcy as MCI. WorldCom recently agreed to create 1600 jobs in Tulsa in exchange for dismissal of fraud charges the state of Oklahoma has brought against the company. This has occurred despite the fact that $64 million was lost from the Oklahoma state pension fund specifically as a result of WorldCom's $11 billion accounting scandal.