T-Mobile/Sprint Ruling Elevates Tech Market Merger Analysis

By Jeffrey Eisenach (February 12, 2020, 6:38 PM EST)

Going into this week, it was considered even money whether U.S. District Judge Victor Marrero of the U.S. District Court for the Southern District of New York would side with attorneys general of New York and 12 other states in their effort to block T-Mobile's proposed acquisition of Sprint.

Much of the scuttlebutt focused on whether the 79-year-old judge was up to the task of assessing a complex, high-tech transaction. Some observers speculated his decision would turn on atmospherics, such as whether DOJ’s proposed remedy — a divestiture and carriage deal with potential new entrant Dish Network — was somehow tainted by text messages[1] between Assistant Attorney General Makan Delrahim and Dish's Charlie Ergen.

Instead, Judge Marrero's decision represents a significant step forward in the jurisprudence of merger analysis in high-tech industries. Demonstrating a sophisticated understanding of both the complexities of mobile communications markets and the nuances, and limitations, of empirical economic analysis, the decision provides a compelling case for considering technological change and market dynamism in assessing competitive effects.

Building on U.S. District Judge Richard Leon's 2018 decision to greenlight AT&T Inc.'s acquisition of Time Warner Inc., it demonstrates that courts are ready to consider the particular characteristics of high-tech markets when assessing competitive effects.

Structurally, the decision is entirely conventional, embracing the familiar burden-shifting framework in which plaintiffs can establish a presumption of anticompetitive effects by demonstrating a significant increase in concentration in a relevant market, thereby shifting the burden to defendants to rebut with evidence casting doubt on the structural presumption. If defendants are successful, the burden shifts back to plaintiffs to prove by a preponderance of the evidence that the transaction is reasonably likely to harm competition.

As one would expect with a four-to-three transaction, Judge Marrero found the structural presumption easily satisfied in this case. But, for Marrero, that is only the beginning, for as he explains, citing the U.S. Supreme Court decision in Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, "'[a]ntitrust analysis must always be attuned to the particular structure and circumstances of the industry at issue.'"[2] With that in mind, Marrero concludes that "[i]n this case, HHI measures may not be as informative as they might first appear in light of complexities particular to the [mobile wireless] market."

The complexities Judge Marrero has in mind fall into two main categories, product differentiation and dynamism, which he discusses in a 20-page stand-alone section of the opinion titled "Particularities of the Wireless Telecommunications Industry." The section begins by noting that mobile wireless services are differentiated products which would "not exist" if the communications services were not bundled with "mobile devices and software programs produced by other distinct industries."

In such markets, Judge Marrero explains, "pricing tends to be relatively non-transparent. ... For this reason, unilateral and coordinated
pricing strategies are likely more difficult to achieve."

The remainder of the "particularities" section focuses on market dynamism. Distinguishing markets in which "the composition of goods and services tends to be static over time" from those in which "the essential qualities of the goods and services can shift quickly from year to year," Marrero cites cases like Federal Trade Commission v. Tenet Health[3] and, most prominently, United States v. AT&T[4] to show that:

courts have recognized that certain markets should be characterized as dynamic by reason of constant innovation and other rapid changes, and that analysis of antitrust effects of specific transactions in such markets warrants more particularized consideration than courts accord under traditional economic analysis, to that extent counseling greater caution in judicial intervention.[5]

The mobile wireless industry, Marrero finds, "aptly illustrates the fluctuations characterizing dynamic markets," with rapid increases in capacity, speed, quality and efficiency producing "performance measures unimaginable just a few years ago."

As a result:

it commands no stretch of the imagination to predict that many of the defining features and standards that characterize the wireless telecommunications industry today may be considered outmoded and unmarketable in the not to distant future, much like the brick phones of not long ago, and the flip phones that replaced them.

Thus, the decision concludes, success in such industries is "indeed to the swift," since it demands that firms constantly invest in new businesses, upgrade plant, improve quality, adjust pricing plans to reflect shifting consumer preferences and grasp new competitive opportunities.

Importantly, these findings are not dicta, but instead form the foundation for Judge Marrero's conclusions on the central issues of the case.

For example, T-Mobile's claimed efficiencies are credible in part because they rest on the ability of the combined firm to "dedicate spectrum to 5G more quickly than either standalone firm could," thereby increasing the availability of 5G services not only to Sprint and T-Mobile customers, but also to customers of AT&T and Verizon, who would be pushed by the competition to "adopt pro-consumer offerings," ultimately resulting in "the earlier creation of new applications and services not currently possible in the 4G/LTE environment."

Similarly, the decision grounds its embrace of the defendant's arguments regarding the competitive significance of the three main actors — Sprint, Dish and T-Mobile — largely on dynamic grounds. Sprint, it concludes, simply lacks the wherewithal to compete effectively in the rapidly changing mobile wireless market.

Dish, on the other hand, has "innovative market plans [which] demonstrate that construction of its network will be less costly and time-consuming than might be expected" because it will deploy a "'virtualized network' that relies more heavily on software and cloud-services hosted by potential partners like Amazon."

As for T-Mobile, "it would defy reasonable expectation of future conduct by reasonable corporate executives in complex and dynamic markets for a business that as staked out a role as an aggressive competitor ... suddenly to embrace a passive outlook."

All of these factors, the decision concludes, cast doubt on the predictions of classical economic models of coordinated and unilateral effects.
For example, it finds that plaintiff economist Carl Shapiro's predictions of price increases from coordinated effects fail to account for "the rapidly changing nature of mobile wireless technological offerings" that may "materially alter the terms of competition." It also finds that his upward pricing pressure model of unilateral effects is unreliable because it would require the court to "assess how slowly or quickly T-Mobile would lower its prices or offer non-price benefits such as high definition Netflix," which is a "necessarily speculative" inquiry in such a "rapidly changing industry."

All in all, "in this intensely competitive and rapidly changing environment in which complex and dynamic markets operate, the anticompetitive business strategies and market effects Plaintiff States predict are unlikely."

Judge Marrero’s decision will be remembered by many for its prologue, which describes the adversarial process in merger litigation as a battle of competing experts whose abstract models and overly precise predictions fail to capture the reality of market dynamics, forcing judges to fall back on more traditional judicial tools — assessing the credibility of witnesses, the likely behavior of real-world actors and the qualitative aspects of the competitive process, which are not easily captured in an econometric regression.

Fair enough, but there is a risk of overinterpretation. What the decision really says is that all of us — economists, practitioners, courts and enforcers — need to keep advancing the art of assessing competitive effects in dynamic markets. By paying attention to the particularities of one such market, this decision represents a step in the right direction.

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Disclosure: Jeffrey Eisenach filed an expert declaration on behalf T-Mobile in the Federal Communication Commission’s review of the transaction but was not directly involved in the state litigation.

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