

# Telecom Policy Report



*Analysis, Insight and Forecasts on Regulation and Legislative Affairs*

## EMERGING POLICY

### Phoenix Center Report Derides 'Intermodal Competition'

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The non-profit Washington, D.C.-based Phoenix Center for Advanced Legal & Economic Policy Studies has just released a report containing findings that fly directly in the face of assertions by FCC Chairman Michael Powell regarding so-called "intermodal competition." The Center's latest report says that regardless of stories in the popular press about how competition from wireless service is cutting into the market for landline service, fixed-mobile intermodal competition is having very little effect on the ability of incumbent telcos to raise prices on American consumers.

It has long been Chairman Powell's view that because of the number of providers offering a variety of telecommunications modes — all of them aggressively vying for the same customers — a revamp of the rules governing competition may be in order. In fact, in February 2003, when the commissioners voted on the FCC's controversial Triennial Review Order, Powell — who was in the minority — strongly maintained that any threat posed by monopoly telephone companies can be made moot by intermodal competition.

The Phoenix Center study, issued last Thursday (April 1), takes exception to Powell's view. It says there has been far too much reliance on "techno-rhetoric" and not enough serious analysis of the core economic problems facing policymakers. Phoenix contends that "the correct inquiry is not whether two different products can do a similar task for some consumers some of the time, but rather whether the use of one product will restrain adequately the exercise of market power for the other."

#### Is Wireless Supplanting Wireline?

Using the standard tools of antitrust economics, the study finds that even though there may be exceptions, U.S. consumers generally do not consider wireless and fixed-line telephony as close substitutes. Therefore, the ability for wireless to constrain the Bells' market power is minimal. This lack of significant fixed-mobile intermodal competition suggests that efforts to promote "intramodal" competition among wireline services (e.g., the market-

opening unbundling mandates of the Telecommunications Act of 1996) remain essential to preserve the consumer benefits of competition created by the 1996 Act.

A previous Phoenix Center report estimated a consumer benefit exceeding \$10 billion annually as a result of the traditional intramodal competition between wireline carriers. The study also noted that the structure in the mobile telephony industry reduces the potential for meaningful intermodal competition with fixed-line service. As the study explains, wireless carriers Verizon, Sprint, and Cingular (40 percent of which is owned by BellSouth, and 60 percent of which is owned by SBC Communications) are each owned by wireline incumbents that, right now, collectively hold about a 63 percent market share of the domestic wireless market.

If Cingular's \$41 billion acquisition of AT&T Wireless is successful, then the incumbent wireline carriers will service about 82 percent of wireless subscribers. Thus, even if wireless did provide genuine intermodal competition for fixed-line service, the effects of this intermodal competition would be minimized because of the common ownership. In other words, the incumbent wireline carriers have about an 82 percent probability of capturing any customer who cancels wireline service and replaces it with wireless service.

The Phoenix study also explains that not only does the joint ownership of wireline and wireless services reduce the potential for intermodal competition, it also provides the Bell companies with an incentive to raise the price of both services.

"In light of the existing and emerging industry structure in wireline and wireless telephone services, perhaps intermodal collusion rather than intermodal competition is a more accurate description of how the two services are related," the study concludes.

Phoenix Center President Lawrence Spiwak said the Center's findings "should not surprise anyone as they are entirely consistent with the FCC's recent Triennial Review and recent CMRS [Commercial Mobile Radio Services] reports." As a real-world example, Spiwak notes that the Bell companies "bundle" fixed and wireless service offerings. However, "if wireless and wireline are really substitutes, then why should you pay for two services if you really only need one?" Spiwak asked rhetorically.

"What is distressing is that numerous policymakers — including the D.C. Circuit, as well as powerful members of the FCC and Congress — are deliberately choosing to ignore this evidence in order to achieve their own political or ideological agendas in the multi billion-dollar telecom debate."

### AT&T Labs Honcho Weighs In

The Center's report closely comports with conclusions reached more than a year ago by the president of AT&T Laboratories, Hossein Eslambolchi. In that instance, Eslambolchi was inspired to fire off a letter to Powell urging him to rethink his stance on intermodal competition (see *TelecomWeb News Digest*, Feb. 5, 2003, at [www.TelecomWeb.com](http://www.TelecomWeb.com)).

"While we, from a technology standpoint, are exploring all new technologies, public policy in my view ought to focus on whether the new technologies can provide sufficient competitive checks to assure that customers get good service at competitive prices now," Eslambolchi told Powell. "In this respect it is incontrovertible that no intermodal technologies come even close to meeting this test." Fixed wireless has been around for more than a decade. Yet it is not an effective constraint on monopoly behavior, he said. And while the [Bell companies] have been successful in convincing the FCC that they face competition, they continue to exert market power and have been increasing prices "for those so-called competitive services across the board." Neither intermodal competition nor anything else is protecting customers from the abuse of market power, Eslambolchi said.