# United States: A Shift to the Right-Sizing? Lessons from Recent Media & Communications Mergers

Horizontal acquisitions are premised on the ability to share fixed costs over a larger base to obtain greater operating economies. Vertical mergers also assume increased efficiency, defined by the merger's demonstration that a "buy" version by which to grow the company is better than a "make" version.

The FCC and the Department of Justice (DOJ) approved a major vertical merger in the cable industry: 2011's Comcast-NBCU merger. Last August, Verizon Wireless's (VZW) $3.9 billion acquisition of AWS spectrum from Spectrum Co.'s three cable partners was also approved. The transaction included commercial agreements for cross-selling of products and a joint research program to harness fixed and mobile broadband innovations. (Hogan Lovells was counsel of record to Verizon Wireless before the Department of Justice and to a Spectrum Co. partner before the FCC.)

Yet, AT&T's 2011's proposed acquisition of T-Mobile was scuttled by DOJ opposition. Smaller horizontal mergers – AT&T's 2011 acquisition of Qualcomm's spectrum and T-Mobile's 2012 acquisition of spectrum as a consequence of the VZW transfer – were approved.

Is there any pattern that can assist ICT (Information/ Communications/Telecomm) companies contemplating mergers or transfers in the U.S.?

Surely, the 1980's whoop of "Synergies!" falls on deaf ears by regulators and bankers. Synergy failures, like the catastrophic 2001 Time Warner/ AOL deal, make vague public interest showings a put-on, or worse.

Nor is there a consensus that vertical integration should be an inevitable goal of ICT companies. In 2009, a year before the Comcast NBCU merger, Time Warner's cable networks and studio split off from its cable company, Time Warner Cable. The same year Viacom split, one company focused on broadcasting (CBS) and the other on cable networks and film holdings. These three respected companies have taken diverging paths toward vertical integration. And there is talk that Vivendi may seek to break itself up.

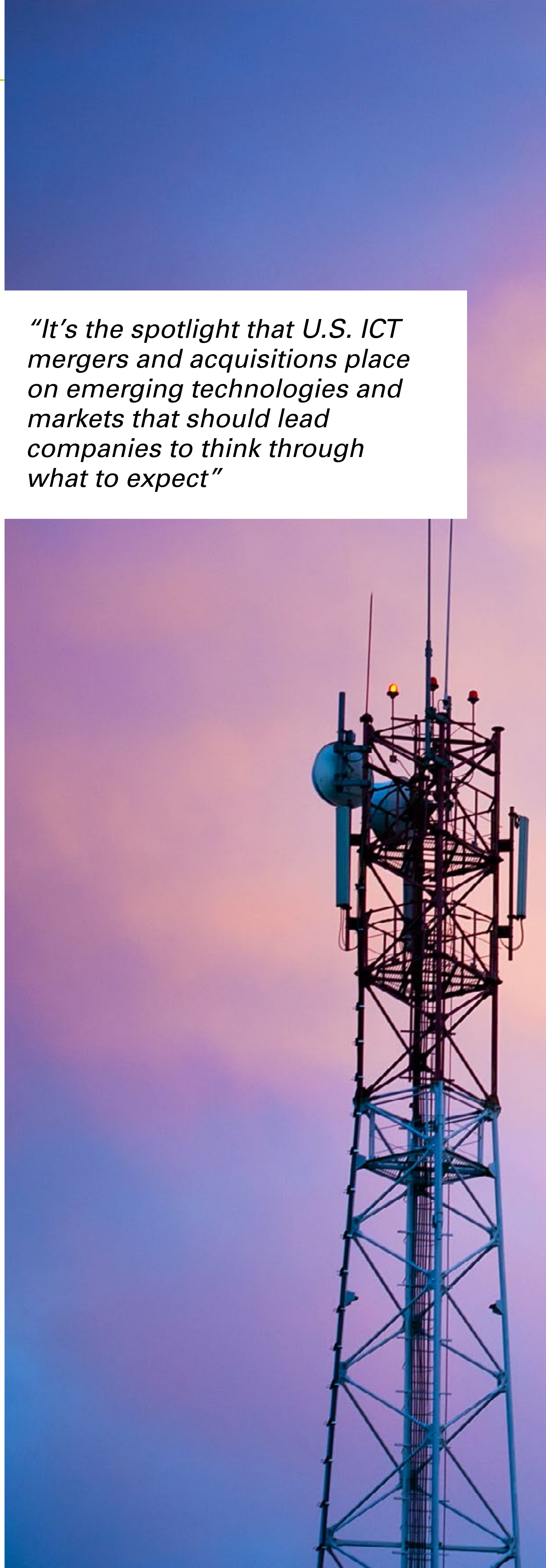
On the horizontal side, what made ATT-T-Mobile impossible but VZW/Spectrum Co. a reality? The former was a classic horizontal acquisition of existing facilities serving existing customers; AT&T might have prevailed in litigation but declined to proceed having gauged the odds. VZW/ Spectrum Co. had easier facts: the seller had no facilities, no customers, and therefore produced no reduction in wireless competition.

Cable companies had bid and won AWS spectrum at the 2006 auction but had never figured out a successful way to create a wireless competitor and a fourth line of business to cable's TV-internet-VoIP triple play. Cox (not in Spectrum Co.) rolled out a wireless offering 2009; it failed by late 2010. If Cox, with its strong an internal telecom base, couldn't figure out how to do wireless, other cable companies, who had spent their own millions plotting a strategy, concluded that the chances of success were low. (Cox sold its spectrum to VZW when Spectrum Co. transferred its licenses.) DOJ obtained changes to the vertically-oriented commercial agreements between the parties. But the transaction was substantially completed as the parties intended.

It's the spotlight that U.S. ICT mergers and acquisitions place on emerging technologies and markets that should lead companies to think through what to expect. For instance, Comcast-NBCU's FCC approval contained procedures for online video distributors to acquire programming that might compete with Comcast's traditional cable service. Online businesses were most nascent at the time the FCC considered the merger. Those conditions have already led to skirmishes at the FCC.

In the VZW/Spectrum Co. transfer, opponents raised two issues on which the FCC declined to propose conditions – cable wireline backhaul and Wi-Fi offload. With wireline backhaul, a cable company builds a tower and wire network to transfer wireless transmissions off licensed spectrum onto its wireline network, which in some cases will build out to the tower location. It's a competitive alternative to offloading to ILEC facilities from Verizon or AT&T or to microwave offload companies.

The concern by some wireless companies is that cable companies would favor VZW in conducting this business. But as Spectrum Co. forcefully showed, cable companies have every incentive to offer backhaul to all wireless providers And they have substantial incentive, once one wireless provider is being backhauled, to add as many other providers to a backhaul tower.



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"Wi-Fi offload" may be less familiar. A counterintuitive truism about the wireless business is that generally speaking, a licensed wireless network is managed to get a customer off that network as cheaply and as quickly as possible. That's because for many portions of wireless network, spectrum is expensive, scarce, and hard to increase in efficiency. Wireline offload is a big part of the solution. Unlicensed spectrum like Wi-Fi may be another.

The cable industry has grown its Wi-Fi hot spot population, primarily to let Internet customers access their cable subscription away from home. This May, several companies created Cable Wi-Fi. Customers of, say, Comcast, can use the Wi-Fi network of Time Warner Cable when outside Comcast's territory. As that network ramps up, it could be a source for offload. So the transfer proceeding became an opportunity to seek conditions by potential users. The FCC declined. That's because cable Wi-Fi offload isn't yet a business. While the FCC will monitor developments, it correctly avoided creating conditions before a business developed.

Caution counts here, because sometimes the FCC gets conditions wrong. When the FCC approved the 2001 Time Warner/AOL merger, it imposed access conditions for what the agency FCC dreamed up as "advanced instant messaging" (AIM). AIM never developed (but texting and Twitter did). The FCC quietly removed the goofy condition in 2003. Nascent markets may be part of a merger or transfer review. ICT companies need to think through those possible conditions carefully, and regulators need to exercise caution in conditioning new businesses before they develop. The FCC's Verizon/Spectrum Co. transfer approval successfully demonstrated both results.

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