

Unclassified

DAF/COMP/LACF(2011)23

Organisation de Coopération et de Développement Économiques
Organisation for Economic Co-operation and Development

14-Sep-2011

English - Or. English

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

Cancels & replaces the same document of 05 September 2011

LATIN AMERICAN COMPETITION FORUM

Session III: Triple/Quadruple Play in Telecoms

Contribution from the US Federal Trade Commission and the US Department of Justice

13-14 Septembre 2011, Bogotá (Colombia)

The attached document from the US Federal Trade Commission and the US Department of Justice is circulated FOR DISCUSSION under Session III of the Latin American Competition Forum at its forthcoming meeting to be held on 13-14 September 2011 (Colombia).

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JT03306914

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13-14 September 2011, Bogota (Colombia)

Session III: Triple/Quadruple Play in Telecoms

-- CONTRIBUTION FROM THE US FEDERAL TRADE COMMISSION AND THE US DEPARTMENT OF Justice * --

1. Increasingly, providers of residential telecommunications services are marketing multiple services as part of a “bundle.” Traditionally, broadband Internet service has been provided to consumers by their cable company (via cable modem) or their telephone company (via DSL or fiber).¹ However, as the cable companies have become more successful at offering telephony and the telephone companies at offering video, “triple-play” bundles of voice, video, and broadband Internet have become increasingly popular.² Bundles have a number of advantages. From the provider’s perspective, existing connections

* Note: The competitive importance of service bundles was a topic of the November 29, 2007 public telecommunications symposium hosted by the U.S. Department of Justice. Many of the footnotes below refer to the proceedings of that symposium, which are available at <http://www.justice.gov/atr/public/workshops/telecom2007/index.html>. The U.S. agencies are unaware of any cases in the United States involving triple play issues.

¹ See Supplemental Submission of Verizon, re: 2007 DOJ Telecommunications Symposium, Feb. 19, 2008, at 11 (“*Verizon Supp. Submission*”) (as of 2007, 64% of U.S. households receive two or more services from the same provider (citing TNS Telecoms, *2Q07 National Market Tracking Report*, at 9 (Sept. 2007))); *id.* (as of 2006, 46% of U.S. households subscribed to bundles of two or more services (citing Frost & Sullivan, *Move Toward Full Convergence - Communication Services for U.S. Residential Markets*, No. 20-62 (2007))); *id.* (in 2006, 54% of consumers were already purchasing multiple services from a single provider in 2006 (citing Patrick Monaghan, Yankee Group, *Driving Value in the Quad Play and the Future of the Communications Bundle*, at 3 (Oct. 2007))).

² See, e.g., Press Release, Cox Communications Achieves Major Customer Milestones in 2008 (Jan. 27, 2009) (at the close of 2008, just under two-thirds of customers subscribed to a bundle and more than a third subscribe to the triple-play), available at http://media.corporate-ir.net/media_files/irol/76/76341/release012709a.pdf; *Goodman Presentation* at 4 (more than 30% of BSP residential customers purchase all three services); Time Warner Reports 2008 Full-Year and Fourth-Quarter Results at 3 (as of 4Q08, 21.2% of customers were buying the triple-play). Verizon claims that 56% of customers who churned to it did so to get a bundle of three services. *Verizon Supp. Submission* at 11.

generate more revenue from each customer,³ and bundle customers tend to churn less frequently, reducing providers' marketing and transaction costs for adding and retaining customers.⁴ From the consumer's perspective, bundles provide the advantages of a single bill and "one-stop shopping,"⁵ as well as, typically, discounts over stand-alone service prices. The emergence and popularity of bundles raises a number of issues, including those of market definition and competitive impact.

2. Providers, particularly cable companies and telephone companies, are increasingly competing head-to-head with triple-play bundles, and those bundles are typically offered at a discount from individual service prices.⁶ That raises the question as to whether the "bundle" should be viewed as a separate product market instead of, or in addition to, individual service product markets. The relevant question, according to the hypothetical monopolist test in the 2010 DOJ/FTC *Horizontal Merger Guidelines*,⁷ is whether a hypothetical profit maximizing firm, not subject to price regulation, that is the only present and future seller of the bundle would impose a small but significant nontransitory price increase to the bundled offering; if so, the bundled product would be in a product market distinct from those of the stand-alone products. However, the data necessary to make this determination is not readily available, and participants in the U.S. Department of Justice's 2007 Telecommunications Symposium disagreed as to whether there was a definable product market for the triple-play bundle.⁸

3. A related issue is whether firms that are unable to offer all bundle elements will be able to function as significant competitive constraints going forward. This is particularly important as it appears that only the telephone companies, cable companies, and cable overbuilders will be able to offer full triple-play bundles over their own facilities; other providers – particularly the satellite firms and online video providers, such as Netflix and Amazon – cannot.⁹ A number of providers have expressed the view that

³ See, e.g., *Verizon Submission* at 11; *Verizon Supp. Submission* at 10-11; see also Verizon, Investor Quarterly Q4 2008, at 9 (Jan. 27, 2009) (reporting that broadband and TV products now account for more than 31% of consumer ARPU in legacy wireline markets), available at <http://investor.verizon.com/financial/quarterly/vz/4Q2008/4Q08Bulletin.pdf?t=633686488263205267>.

⁴ See Wilkie, Symposium Tr. at 135-36 (discussing effect of bundles on reducing churn).

⁵ Participants in the Section's 2007 Symposium debated whether the "single bill" was really important to customers. See, e.g., *Verizon Submission* at 11 (suggesting that consumers liked receiving a single bill and one-stop shopping); Evan R. Grayer, DirecTV Group, Symposium Tr. at 319-20 (suggesting that a single bill was not particularly important to customers). But see Blair Levin, Stifel Nicolaus, Symposium Tr. at 323-24 (noting a lack of empirical analysis of bundling's impact, but predicting that bundling will become more significant to consumers when firms are able to integrate the functions of the various services).

⁶ Participants in the Section's 2007 Symposium indicated that triple-play bundles can be discounted by as much as one-third over stand-alone services offered by the same provider, particularly if the customer commits to a contract with a term of one year or more. See *DOJ Symp. Report* ch. II.B.

⁷ U.S. Dep't of Justice & Fed. Trade Comm'n, *Horizontal Merger Guidelines* § 4.1.1 (rev. ed. 2010), available at <http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf>.

⁸ See, e.g., *Charter Submission* at 28-29 (arguing for a broad market definition of "integrated communications services," including voice, broadband/high-speed data, and video sold to residential customers, taking into account the increasing sale of these products in a bundle); Sean C. Lindsay, Qwest Communications International Inc., Tr. at 77-79 (contending that competition should be evaluated in terms of competing broadband access suppliers, rather than individual services). But see, e.g., *Singer Supp. Submission* at 5-6 (suggesting that the triple-play bundle might be too broad a product market).

⁹ The DBS firms cannot offer telephony, and can offer only satellite-based Internet – an inferior alternative to cable modem and DSL – in conjunction with other partners like WildBlue. See Grayer, Tr. at 275-76. Broadband wireless firms, such as Clearwire and Digital Bridge, do not offer MVPD, and offer VoIP telephony only in conjunction with partners. See R. Gerard Salemme, Clearwire Corp., Symposium Tr. at 252-53; William F. Wallace, DigitalBridge Communications Corp., Symposium Tr. at 253; R. Gerard

being able to offer all three elements as a package is vitally important.¹⁰ Others, particularly firms that cannot offer the full bundle, such as DirecTV, have suggested that they can nonetheless succeed by selling a stand-alone offering.¹¹ What little evidence is available seems to suggest that firms that are able to offer triple-play bundles may have a significant competitive advantage over those that are not: a 2005 GAO study indicated that satellite penetration is much lower where cable competitors offer the triple-play bundle.¹²

4. The desire to offer triple-play bundles has prompted firms unable to offer them over their own facilities to partner with other firms in joint marketing arrangements,¹³ but it is unclear whether those arrangements are as effective as fully integrated bundles. To the extent they are not, firms may try to merge in order to more effectively offer the triple-play, a strategic rationale largely responsible for rumors of mergers between the satellite firms and the major telephone companies (which still have not built facilities sufficient to offer video throughout much of their footprints).

5. Finally, it is worth noting the potential impact of bundling on consumers. Because providers tend to discount bundles over stand-alone services (potentially reflecting lower cost structures), consumers would appear to benefit. However, the extent to which customers are better off purchasing a bundle from a single provider rather than stand-alone services from two or three providers is unclear. In the future, to the extent providers are able to technically integrate telephony, multichannel video programming distribution, and broadband Internet to provide new features, consumers may see more benefits.¹⁴

Salemme, Clearwire Corporation, “Delivering Personal Broadband and the Mobile Internet,” 2007 DOJ Telecommunications Symposium, at 5 (Nov. 29, 2007); Raclin, Symposium Tr. at 47. Broadband over powerline providers such as Current offer only broadband Internet access, along with the potential for customers to use VoIP telephony services over broadband, but they do not provide a full MVPD service. See Brendan Herron, CURRENT Group, LLC, “Broadband Overview,” 2007 DOJ Telecommunications Symposium, at 4 (Nov. 29, 2007).

¹⁰ See, e.g., Goodman, Tr. at 29-31; *Goodman Presentation* at 8; *BSPA Submission* at 10; see also Stephen Perkins, Cavalier Telephone LLC, Tr. at 99 (explaining that Cavalier is “in triple-play because we have to be; t]hat is where the competitors are going”).

¹¹ See Grayer, Tr. at 273-75 (noting that DirecTV is doing well, and rapidly gaining subscribers, due to a superior video product despite the lack of a bundle, and contending that consumers benefit more by purchasing video from DirecTV rather than by purchasing a triple-play bundle from a cable provider that offers fewer HD channels); Levin, Tr. at 322 (agreeing that DirecTV’s success even without a bundle was attributable to a superior video product resulting from investment in HD); see also Brendan Herron, Current Group, Tr. at 321 (suggesting that the inability of Current, a broadband over powerline provider, to offer a triple-play bundle was not a detriment as many customers are not interested in purchasing a bundle).

¹² See Goodman, Tr. at 32-33; *Goodman Presentation* at 7. DBS penetration rates were found to be highest (36%) where such firms competed against a traditional cable system offering neither broadband nor telephony, and lowest (14%) where they competed against a cable system offering digital video, broadband, and telephony. Government Accountability Office, *Telecommunications: Direct Broadcast Satellite Subscriberhip Has Grown Rapidly, But Varies Across Different Types of Markets*, GAO-05-257, at 11 (Apr. 2005) (“GAO 2005 Study”), available at <http://www.gao.gov/htext/d05257.html>.

¹³ See, e.g., Grayer, Tr. at 274-76 (noting DirecTV’s partnering with several companies – including ILECs, satellite broadband companies, and broadband over powerline providers – to offer broadband and telephony elements of the bundle).

¹⁴ See Levin, Tr. at 323-24 (explaining that the bundle becomes a much more powerful product when it provides integrated services rather than just discounts – for example, allowing users who are watching video programming to have information on incoming telephone calls appear on their TV screens).