WIRELESS CONSUMERS ALLIANCE INC.

April 23, 1999

Ms. Magalie Roman Salas
Office of the Secretary
Federal Communications Commission
The Portals
445 Twelfth Street, S.W.
12th Street Lobby, TW-A325
Washington, D.C. 20024

Re: Ex Parte Presentation
CC Docket No. 94-102

Dear Ms. Salas:

In our letter of April 2, 1999, we said that a "market choice" between Strongest Signal and Automatic A/B Roaming was *not possible* under the current marketing regimen because the carriers dominate the wireless handset equipment market as a result of the tying arrangement between the sale of handsets and wireless service. This is not an issue that has been previously raised in this proceeding because there has been no indication prior to this time that the Commission would entertain the notion of giving the carriers the choice between Strongest Signal and the vastly inadequate alternatives of Automatic A/B Roaming and Double Push. We indicated that we were still gathering facts concerning the carriers' control of the handset equipment market and would report further to the Commission. This letter is for that purpose.

The U. S. Supreme Court has defined a tying arrangement as "an agreement by a party to sell one product but only on the condition that the buyer also purchases a different (or tied) product." *Northern Pacific Ry. Co. v. United States*, 356 U.S. 1, 5-6, 2 L. Ed. 2d 545, 78 S. Ct. 514 (1958). Wireless handsets are sold at a price which is *substantially below carrier's cost* to consumers who sign a tying subscription agreement for air time. (See appendix "A"). There is little doubt that the unrecovered cost of the handsets is included in the inflated price of the air time. We are able to draw this conclusion from the published data concerning the growth and the

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robust income stream enjoyed by wireless carriers. This data shows that the number of new "cellular subscribers continue[s] to grow at rates approaching 20 percent."[1] *Operating cash flow margins in 1998 averaged 42 percent.*"[2] Gross revenues per subscriber in 1998 were $612 while operating expenses were $340.[3] "[L]arger companies enjoy an economy of scale that yields [even] lower cost of service."[4] This has led to consolidation which has resulted in six or seven large companies who now dominate the market.

The California Supreme Court discussed some of the issues raised by the practice of tying the price of handsets to cellular service as the situation existed "in the early 1990's." *Cell-Tech Communications, Inc., et. al., v. Los Angeles Cellular Telephone Company*, California Supreme Court, SO66735, *slip op. 3, 1999 Cal. LEXIS 1656* (April 8, 1999). The Court said that "[a]llowing a company to sell telephones at a loss to increase profits on service sales, and to recoup its losses with those profits, might threaten the ability of any company not permitted to sell services to compete in telephone sales." (*Slip op. 30, LEXIS 1656*54*). A 1997 survey of 750 users by the Strategis Group found that these competitors had in fact been driven out of the market and today 96 percent of all handsets are sold to consumers by the carriers or their agents.[5] This is a classic tying arrangement in which carriers have leveraged their control of wireless networks into the consumer handset equipment market and driven sellers of equipment who do not also sell service from the market.[6] The issue here is not was the tie initially justified as a means of helping the carriers establish a new market but rather is the tie justified under the present circumstances.[7] The market for wireless service is now well established. Competition between

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[1] *WirelessWeek*, January 11, 1999, p. 29.

[2] *Id.*

[3] *Wireless Week*, April 5, 1999, p. 19, quoting Strategis Group studies.

[4] *Id.*

[5] *Id.* Only 1 percent were private sales and 3 percent were listed as "other" which may include sales by carriers or their agents.

[6] The use of a tying contract to eliminate independent sources of the tied product can prevent entry by sellers of the tying product who are not able to enter the tied product market. Donald Dewey, *Monopoly in Economics and Law* 201 (1958). "When the seller's share of the market is high . . . or when the seller offers a unique product that competitors are not able to offer . . . the Court has held that the likelihood that market power exists and is being used to restrain competition in a separate market is sufficient to make per se condemnation appropriate." *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 17 (1984).

[7] Cf. *Jerrold Electronics Corp. v. United States*, 365 U.S. 567 (1961).

carriers has resulted in a decline of air time prices and equipment prices but the margin of 42 percent is well above the return of most Fortune 500 companies.[8]

It is also apparent that the carriers' control over the handset market has prevented the manufacturers from offering Strongest Signal to consumers. Common sense tells us that the emphasis on safety and security as the key marketing strategy for the wireless industry would ordinarily cause handset manufacturers to quickly address the well documented dead zone problem for 911 calls. This is especially so after the Commission found in 1996 that the public interest requires a solution to this problem.[9] However, in so far as we know, only one manufacturer responded -- Audiovox -- which installed Strongest Signal in its 405 model handset. Audiovox later apparently removed Strongest Signal from its handsets, obviously bending to the pressure from CTIA and the carriers they represent.[10] Consequently it must be assumed that the carriers will continue to engage in opportunistic behavior to prevent the deployment of handset features which they disfavor by reason of their self interests.

The Commission has previously said "[b]ecause cellular service is a new service for which its mobile equipment has never been tariffed, we will require that it be unbundled and detariffed from the start."[11] The tying arrangement described above is a form of bundling because part of the amount charged for equipment is packaged in the rate for service. Wishful thinking that the carriers' selection between various alternatives allegedly intended to overcome the dead zone

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[8] Most agents purchase handset equipment from the carriers. The very large agents purchase handset equipment directly from the manufacturer but features not wanted by the carrier will not be available from any manufacturer because the carriers are the primary customer in this market.

[9] *In the Matter of Revision of the Commission's Rules To Ensure Compatibility with Enhanced 911 Emergency Calling Systems*, CC Docket No. 94-102, RM-8143, Report and Order and Order and Further Notice of Proposed Rulemaking, ¶ 145 (July 26, 1996).

[10] The opposition of CTIA towards any solution to the dead zone problem is well documented in this proceeding. It was only after three years of building a solid record for Strongest Signal that CTIA was forced to submit Automatic A/B Roaming, a sham which does not provide the consumer with much protection. Audiovox used Strongest Signal in its 405 model. After this fact was brought to the attention of the Commission by the Alliance, Audiovox yielded to the pressure from CTIA and converted from Strongest Signal to Automatic A/B Roaming. The exclusion of Strongest Signal from the handset equipment market violates the Sherman Act. (15 U.S.C., § 1).

[11] *In the Matter of An Inquiry Into the Use of the Bands 825-845 MHz and 870-890 MHz for Cellular Communications Systems; and Amendment of Parts 2 and 22 of the Commission's Rules Relative to Cellular Communications Systems*, 86 F.C.C. 2d 469, 487 § 58; 49 Rad. Reg. 2d (P & F) 809 (May 4, 1981).

problem will be influenced by an unbiased decision for the benefit to the consumer is clearly contradicted by the record in this proceeding. Therefore, if the Commission now allows the "market to decide" between these alternatives it ***must at the same time*** order the complete unbundling of equipment and services. Otherwise there will continue to be a market failure in which the interests of the consumers will be disregarded.

Unbundling may be in the public interest in any event for the following reasons: (1) Consumers can purchase handsets at a retail price of cost plus profit but they cannot purchase air time at an unbundled price. Thus, air time rates are discriminatory as to consumers who use equipment which has been purchased at retail price or fully paid for through air time charges attributable to that equipment purchase.[12] (2) Air time contracts contain penalty clauses for early termination in order to recover equipment costs which have not been paid by air time charges. Such contract provisions inhibit consumers, who may have found dead zones in the areas they normally traverse, from freely moving to another carrier. (3) The carriers purchase a limited selection of handsets. Thus, for example, if a customer wanted an Oki phone and service from AirTouch in San Diego, California, that combination is not available at the bundled price. This has the effect of restricting consumer choice of handset equipment and/or carrier service. It also has the effect of restricting free access to the consumer market by equipment vendors.[13] (4) Finally, it is very unlikely that handset manufacturers would continue to pay tribute to CTIA in the form of exorbitant "certification" fees since the CTIA seal of approval would have no credence at all with consumers -- thus lowering the cost of handsets.[14]

The above discussion shows that the primary handset market as presently constituted is comprised of manufacturers (sellers) and carriers/agents of carriers (buyers). This market caters to the interests of the carriers. The uncontradicted record in this proceeding shows that carrier's self interest will always prevail over the interest of consumers in this market. It would be a certain exercise in futility to expect the carriers to suddenly reflect the consumer's interest after almost four years of resisting Strongest Signal.

We do not regard issues of public safety to be matters for carrier *or* consumer choice. If choice were the criteria there would be no life saving seat belts or air bags today. A seat belt that

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[12] The average length of an air time contract is 2 years. Thus, it is fair to assume that after 2 years the entire cost of the handset has been recovered.

[13] Unbundling will also have the salutory effect of enabling manufactures to speak freely to the Commission. The obsequious Motorola Intelligent Retry proposal is an example of the lengths manufactures feel constrained to go to in order to curry the favor of the industry.

[14] The Commission's type acceptance process is sufficient for protection of consumers. The CTIA fee is reported to be in the vicinity of $5 per handset and we understand that the revenue from this fee is the second largest source of income for CTIA's $30 million annual budget.

works some of the time or every other time would never be seriously considered as an alternative which serves the public interest. This inconceivable proposition is the counterpart to the proposed Automatic A/B Roaming or Double Push. In emergency situations, the public interest requires the use of the most reliable channel of communication available. Based on the record in this proceeding, it is beyond doubt that Strongest Signal is the only proposal before the Commission that will meet that need.[15] The Communications Act requires the Commission to promote "safety of life and property through the use of wire and radio communications."[16] We respectfully submit that there should be no compromise in carrying out this mandate.

Sincerely,

Carl Hilliard

cc: Ms. Karen Brown, Chief of Staff, Chairman Kennard
Mr. Ari Fitzgerald, Legal Assistant to Chairman Kennard
Mr. Paul Misner, Chief of Staff and Legal Assistant to Commissioner Furchtgott-Roth
Mr. Dan Connors, Legal Assistant to Commissioner Ness
Mr. Peter Tenhula, Legal Assistant to Commissioner Powell
Ms. Karen Gulick, Legal Assistant to Commissioner Tristani
Mr. Thomas Sugrue, Chief, Wireless Telecommunications Bureau
Mr. Jim Schlichting, Deputy Chief, Wireless Telecommunications Bureau
Mr. John Cimko, Chief, Policy Division, Wireless Telecommunications Bureau
Mr. Dan Grosh, Special Counsel, Policy Division, Wireless Telecommunications Bureau
Mr. Dale Hatfield, Chief, Office of Engineering and Technology

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[15] We have responded to the Staff's request that we submit a proposal which combines the "merits" of Strongest Signal with Automatic A/B Roaming by drafting a plan using a variable threshold selected by the consumer – not the carrier – with the hope that the consumer will be sufficiently well informed to make that choice. However, we believe that Strongest Signal – not Strongest/Adequate Signal and not Strongest/Adjustable Adequate Signal -- is the choice required by the public interest.

[16] 47 U.S.C. § 151.

ATTACHMENT "A"*

MODEL	***COST***	***CARRIER***	***TIED PRICE***	***TERM OF CONTRACT***	***CANCEL PENALITY***
Audiovox CDM 3000	$290.00	BAM (D.C.)	$109.99	1 - 2 yrs.	$175.00
	290.00	BAM (Boston)	79.99	1 - 2 yrs.	175.00
LGIC 300W	245.00	Cellular One (Phoenix)	119.99	1 - 2 yrs.	200.00
	245.00	GTE (San Diego)	129.95	1 yr.	$25 x # of months remaining
Motorola M70	138.00	BellSouth (Atlanta)	79.95*	1 - 3 yrs. *2 yr. contract	240.00 (pro-rated)
	138.00	Cellular One (San Francisco)	79.99	1 yr.	200.00
Motorola MicroTAC 650e	125.00	BAM (D.C.)	64.99	1 - 2 yrs.	175.00
	125.00	SNET (Hartford)	15.00	1 yr.	175.00
Motorola MicroTAC SC-725	314.00	BAM (Boston)	109.99	1 - 2 yrs.	175.00
Motorola Profile	82.00	AirTouch (LA)	19.00	2 yrs.	150.00
	82.00	Alltel (Las Vegas)	19.95	1 - 2 yrs.	200.00
Motorola 650e	164.00	AirTouch (LA)	39.00	2 yrs.	150.00

MODEL	***COST***	***CARRIER***	***TIED PRICE***	***TERM OF CONTRACT***	***CANCEL PENALITY***
Motorola TAC Lite II	$150.00	Alltel (Norfolk)	$ 29.95	1 yr.	$225.00
Motorola StarTac 3000	233.00	Cellular One (Phoenix)	99.00	1 - 2 yrs.	200.00
Motorola StarTac 6500	250.00	AirTouch (LA)	49.00	2 yrs.	150.00
NEC 820e	85.00	BellSouth (Atlanta)	9.95*	1 - 3 yrs. *2 yr. contract	240.00 (pro-rated)
Nokia 252	125.00	BellSouth (Atlanta)	69.95*	1 - 3 yrs. *2 yr. contract	240.00 (pro-rated)
	125.00	SWB (Dallas)	29.00	1 - 2 yrs.	!50.00
Nokia 918	89.00	SWB (Dallas)	0.00	1 - 2 yrs.	!50.00
Nokia 5120	!56.00	SNET (Hartford)	89.95	1 yr.	175.00
	156.00	Cellular One (Chicago)	49.00	1 - 2 yrs.	150.00
Nokia 6120	202.00	Cellular One (Chicago)	99.00	1 - 2 yrs.	150.00
Qualcomm QCP-820	295.00	BAM (Boston)	119.99	1 - 2 yrs.	175.00
	295.00	BAM (D.C.)	89.99	1 - 2 yrs.	175.00
Sony CM-M1300	275.00	GTE (Oakland)	99.00	1 yr.	$25 x # of months remaining
	275.00	BAM (New Jersey)	149.99	1 yr.	175.00
	275.00	AirTouch (Seattle)	89.00	1 - 2 yrs.	$25 x # of months remaining

* The information in this table is a composite from several sources and believed to be accurate however, we did find a difference of a few dollars in the price paid for the same phone by different carriers. When that discrepancy occurred, we selected the higher price.