July 22, 2011

VIA HAND DELIVERY AND ECFS

Marlene H. Dortch, Esq.
Secretary
Federal Communications Commission
Office of the Secretary
445 Twelfth Street, S.W., Room TW-A325
Washington, DC 20554

Re: *Applications of AT&T Inc. & Deutsche Telekom AG for Consent to Assign or Transfer Control of Licenses & Authorizations*, WT Dkt No. 11-65
REDACTED – FOR PUBLIC INSPECTION

Dear Ms. Dortch:

In accordance with the First and Second Protective Orders[1] in the above-referenced proceeding, AT&T Inc. and Deutsche Telekom AG (collectively, the "Applicants") are jointly filing herewith, two redacted copies of a submission to address staff inquiries about the competitive significance of AT&T's local promotional activities. More specifically, this submission addresses: (I) the significance of handset discounts as a percentage of contract revenue; (II) the effect of local competitive initiatives, including handset discounts and other promotions that reduce the up-front cost of purchasing mobile wireless service, as well as non-price mechanisms, such as network improvements and retail distribution decisions; and (III) T-Mobile USA's recent restructuring of its sales and marketing organization to better focus on and respond to local competition.

[1] *In re Applications of AT&T Inc. & Deutsche Telekom AG for Consent to Assign or Transfer Control of Licenses and Authorizations*, WT Dkt No. 11-65, Protective Order, DA 11-674 (WTB rel. Apr. 14, 2011) ("First Protective Order"); *In re Applications of AT&T Inc. & Deutsche Telekom AG for Consent to Assign or Transfer Control of Licenses & Authorizations*, WT Dkt No. 11-65, Second Protective Order (Revised), DA 11-1100 (WTB rel. June 22, 2011), *modified*, DA 11-1214 (WTB rel. July 19, 2011) ("Second Protective Order").

This filing includes two paper copies of a redacted version of the Applicants' submission. The redacted version of the submission is also being submitted via ECFS. An unredacted version of this submission, is being filed contemporaneously with your office under separate cover.

The Applicants are also submitting two copies of the Highly Confidential filing to Kathy Harris of the Wireless Telecommunications Bureau or her designee under separate cover.

If you have any questions or require further information, please contact us at 202-942-5404 or Wilson.Mudge@aporter.com, or (202) 719-7344 or nvictory@wileyrein.com. Thank you for your assistance.

Sincerely,

/s/

Wilson Mudge
Counsel for AT&T Inc.

/s/

Nancy J. Victory
Counsel for Deutsche Telecom AG

Enclosures

cc (via email): Best Copy and Printing, Inc.
Kathy Harris, Esq.
Ms. Kate Matraves
Jim Bird, Esq.

REDACTED - FOR PUBLIC INSPECTION
WT DOCKET NO. 11-65 BEFORE
THE FEDERAL COMMUNICATIONS COMMISSION

INTRODUCTION

In recent discussions, Commission staff have inquired about the competitive significance of AT&T's local promotions, including handset discounts, both generally and relative to the total revenue AT&T would expect to earn over the life of a customer's contract. This paper addresses those questions by discussing: (I) the significance of handset discounts as a percentage of contract revenue; (II) the effect of local promotions, including handset discounts and other promotions that reduce the upfront cost of purchasing mobile wireless service, and non-price mechanisms, such as network improvements and retail distribution decisions; and (III) T-Mobile USA's recent restructuring of its business to better focus on and respond to local competition.

I. Handset Promotions as a Percentage of Revenue Over Contract Period

Handset discounts are one of the most common and powerful tools that AT&T's twenty-seven Vice President/General Managers ("VP-GMs") employ to respond to customer demand. Staff have asked how such handset discounts compare to the total revenue AT&T would expect to earn over the life of a customer's contract. Because of the variability in the handset discounts and other local promotions that our VP-GMs undertake, it is not possible to provide a definitive comparison; however, even this imperfect metric reveals that our handset discounts can be quite material. Consider:

- The average revenue per user ("ARPU") that AT&T derives from a subscriber is approximately **[Begin Highly Confidential Information] [End Highly Confidential Information]** over the life of a two-year contract.[1] This figure varies by device type, from a low of approximately **[Begin Highly Confidential Information] [End Highly Confidential Information]** for a basic phone user, to **[Begin Highly Confidential Information] [End Highly Confidential Information]** for a quick messaging device ("QMD") user, to a high of approximately **[Begin Highly Confidential Information] [End Highly Confidential Information]** for a smartphone user.[2]

- Thus, to take a common example, a $50 rebate on the price of a QMD represents approximately **[Begin Highly Confidential Information]**

[1] It is more appropriate to consider device subsidies or rebates relative to the two-year term of a contract than relative to the customer's "lifetime" with AT&T because a subscriber generally would have the opportunity to select a new subsidized phone with each contract renewal.

[2] The figures presented here represent AT&T's internal estimate of average revenue per postpaid user, by device type, over a contract term of twenty-four months, based on information as of May 2011.

[End Highly Confidential Information] of average contract ARPU for that subscriber. This credit would be offered in addition to any applicable handset subsidy.

- A $100 switcher credit, offered to a customer who uses a basic "feature phone," would represent more than **[Begin Highly Confidential Information]** **[End Highly Confidential Information]** of total contract ARPU, and the same credit would amount to **[Begin Highly Confidential Information]** **[End Highly Confidential Information]** of ARPU as applied to a smartphone subscriber.

- Given that a 5 to 10% increase in price is termed "significant" under the Horizontal Merger Guidelines, a local manager's ability to initiate pricing changes in such a range suggests that those managers exert significant influence over total price.

Even so, considering upfront promotions and discounts in this way is unduly narrow, because it fails to take into consideration the ways customers respond to changes in handset pricing and other competitive moves affecting upfront cost. As this paper describes below, AT&T's actual experience in the marketplace demonstrates that these competitive offers get results.

II. AT&T's Local Market Competitive Strategies and Efforts

As AT&T has described in detail in the prior submissions of the parties regarding this transaction, AT&T is organized to respond to competition in significant ways at the local level. Each of AT&T's twenty-seven VP-GMs, with support from Regional and Headquarters Finance, Sales and Marketing teams, develops a competitive strategy that reaches across the many dimensions of local wireless competition to attract and retain wireless customers.

The VP-GMs are incentivized to succeed in these efforts because their compensation depends to a significant degree on **[Begin Highly Confidential Information]**

[End Highly Confidential Information]. It would make little business sense to evaluate managers on the basis of these outcomes without providing managers with the tools to affect them. Simply put, AT&T has invested in this system of organization out of a conviction that VP-GMs can and do affect the company's competitive performance locally in important ways.

One important tool used by VP-GMs to increase net adds and/or reduce churn is to reduce upfront costs to customers of their service or handset. Upfront costs and specific promotions designed to decrease or eliminate these costs are major factors in the customer decision-making process. As such, they are often the focus of marketing

practices undertaken by VP-GMs as they tailor local promotions and offers to the specific customer base and competitive needs in a given locality. Practices designed to reduce upfront costs may include free or discounted handsets, waiver of activation fees or "switcher credits" to offset early termination fees imposed by a customer's former carrier.

A. Handsets

Handset pricing is often the largest component of the upfront costs borne by wireless customers, particularly for smartphones, and handset discounts are a commonly used tool in local competitive strategies. Indeed, where a customer may wish to switch from his or her existing carrier to a comparably priced competitive plan, the upfront cost of purchasing a handset can be prohibitive, or at least may play a major role in the customer's decision-making process. **[Begin Highly Confidential Information]**

[End Highly Confidential Information]. These local promotions are based on local circumstances: for example, certain handsets may be more popular in one local area than they are in another, and **[Begin Highly Confidential Information]**

[End Highly Confidential Information]. Region-wide discounts and promotions also are sometimes offered. Both local and regional discounts often reduce the price of a handset significantly, if not eliminate it altogether (i.e., to offer handsets for free), and they have had a noticeable impact in the marketplace, as illustrated by the following examples:[3]

- In Philadelphia, an instant rebate promotion for a free Pantech QMD ran from January 28-31, 2010. Compared to the same period in 2009, the Philadelphia territory saw an **[Begin Highly Confidential Information]**

  [End Highly Confidential Information]. During the Black Friday weekend in November 2010, the same territory ran another instant rebate promotion for QMDs. The territory saw a **[Begin Highly Confidential Information]**

  [End Highly Confidential Information] when compared to the 2009 Black Friday weekend.

- The Virginia/West Virginia VP-GM offered a week-long 50% off promotion on all QMDs in March 2010. The store experienced a **[Begin Highly Confidential Information]**

[3] The examples provided in this paper are intended to be illustrative of local AT&T promotions.

[End Highly Confidential Information].

- In November-December of 2009, the New York/New Jersey VP-GM offered the BlackBerry Bold and Curve handsets at reduced pricing **[Begin Confidential Information] [End Confidential Information]** while the national recommended prices remained steady at **[Begin Confidential Information] [End Confidential Information]**. The New York/New Jersey territory experienced an increase in average daily sales of **[Begin Highly Confidential Information] [End Highly Confidential Information]** for those devices, from **[Begin Highly Confidential Information] [End Highly Confidential Information]**, when compared to the period immediately before the promotion.

Handset promotions also are used as a mechanism to retain existing customers. AT&T may offer early upgrades to customers in order to combat a perceived threat from competitors in a local area. For example, in February 2010, a VP-GM ran a "Friends and Family" offer of $50 off any smartphone (a common promotion that has been run by multiple VP-GMs), **[Begin Highly Confidential Information] [End Highly Confidential Information]**. The churn differential between the treated base and the control base was **[Begin Highly Confidential Information] [End Highly Confidential Information]** basis points two months after the mailing.

B. Other Pricing Mechanisms

In addition to handset discounts, AT&T VP-GMs use a number of other pricing mechanisms to attract and retain local customers. **[Begin Highly Confidential Information]**

[End Highly Confidential Information]. For example:

- In February 2010, the VP-GM for the Desert Southwest territory ran a $75 switcher credit promotion. The territory saw a **[Begin Highly Confidential Information] [End Highly Confidential Information]** during the promotional period when compared to business-as-usual projected estimates. In March 2010, the same VP-GM ran a similar $50 promotion and observed a **[Begin Highly Confidential Information] [End Highly Confidential Information]** during the promotional period when compared to business-as-usual projected estimates.

- AT&T offered a $100 switcher credit along with eight different free handsets during a 2010 "Black Friday" promotion in the Rocky Mountain territory. Over the course of the weekend, the territory had **[Begin Highly Confidential Information]**

  [End Highly Confidential Information] lift over the 2009 Black Friday weekend.

In addition to these "switcher credits," VP-GMs also employ activation fee waivers to increase gross adds. At least **[Begin Highly Confidential Information]**

[End Highly Confidential Information]. These outlets offer an array of wireless choices and handsets from many different carriers, including regional providers and mobile virtual network operators ("MVNOs"). To attract local customers, carriers often waive activation fees in one or several national retail outlets in a given local market. AT&T often must respond to these local promotions by waiving activation fees on a store-by-store basis, often with little notice. For example:

- The Pacific Northwest territory ran a waived activation fee at local Best Buy and Radio Shack stores from March 27-29, 2010, **[Begin Highly Confidential Information]**
  [End Highly Confidential Information]. A similar promotion in local Pacific Northwest Best Buy stores ran from May 27-31, 2010. During that week, the territory experienced a **[Begin Highly Confidential Information]**
  [End Highly Confidential Information].

- From May 16-23, 2010 the Virginia/West Virginia territory ran a "customer appreciation" promotion for both new and existing customers that included waived activation fees on any lines added to a new or existing account. The territory saw a **[Begin Highly Confidential Information]** **[End Highly Confidential Information]** compared to a similar time period where this offer was not available.

C. <u>Non-Price Mechanisms</u>

Wireless customers make purchasing decisions based on a variety of other competitive factors besides price, including network quality, coverage and data speeds, retail store proximity and local marketing and advertising. AT&T VP-GMs have considerable discretion over the decisions that affect these key variables as part of their local competitive strategies, and these measures can result in significant improvements in competitive metrics.

According to AT&T research and third-party studies, **[Begin Confidential Information]**

[End Confidential Information]. AT&T makes local decisions about network improvement **[Begin Highly Confidential Information]**

[End Highly Confidential Information].

In addition, retail distribution and advertising are also key drivers in customer decision-making. As part of the overall strategy for a given territory, **[Begin Highly Confidential Information]**

[End Highly Confidential Information].

III. T-Mobile USA's Recent Reorganization Reflects the Importance of Local Competition

As described in the Declaration of James Alling, in 2010 T-Mobile USA revamped its sales and marketing strategy to allow the company to focus on differing conditions in local markets to enable it to compete more effectively.[4] The company restructured its sales and marketing organization into four geographic areas – West, Central, South, and East – with senior vice presidents as area heads. These four regions were further subdivided into twenty-three local regions, each operated by regional general managers. Under the new structure, each of the twenty-three regional teams tailors **[Begin Confidential Information]**

[End Confidential Information].

The twenty-three regions **[Begin Confidential Information]**

[4] Declaration of James Alling, Chief Operations Officer and Executive Vice President, T-Mobile USA, Inc., at ¶¶ 12-13 (Jun. 10, 2011).

[End Confidential Information].

Though the new structure has only been in place for a short time, T-Mobile USA has already run several local promotions, some of which are targeted directly at specific competitors in each region:[6]

- On July 11, 2011, **[Begin Confidential Information]**

  [End Confidential Information].

- In June 2011 the regional team in Boston offered a special promotion under which customers received a free Motorola Defy and car mount upon signing a two-year "Truly Unlimited" contract.

- Beginning in mid-May 2011, multiple regional teams launched a marketing campaign in Los Angeles, Miami, Atlanta, New York, Philadelphia and Chicago promoting their "Monthly 4G" prepaid product in those areas. This effort is targeted at urban areas where "all-you-can-eat" ("AYCE") carriers, including MetroPCS and Leap, have been gaining significant share, and aggressively promotes T-Mobile USA's prepaid product against those AYCE offerings.

T-Mobile USA's revamped organization adopts a locally focused approach other wireless carriers – including AT&T – have long realized is effective.

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[6] Because T-Mobile USA's structure is relatively new, T-Mobile USA has little data about the effect local promotions have on its ability to attract and retain customers.

IV. Conclusion

As the evidence and examples detailed above make abundantly clear, the local nature of wireless services competition is reflected throughout the organizational structures of both AT&T and T-Mobile USA and in the ways in which both companies respond to competitive challenges and conditions that vary from market to market. These localized competitive responses have significant and quantifiable effects on sales, switching and growth. As such, these facts speak to the importance of local competition and reinforce the conclusion of the 15th Annual Mobile Wireless Competition Report and the practical recognition in prior reviews of wireless mergers, that the relevant geographic market for mobile wireless services is local.[7]

[7] In prior transactions involving mobile wireless licenses, the Commission has evaluated the competitive effects at the CMA level. Annual Report & Analysis of Competitive Market Conditions with Respect to Mobile Wireless, Including Commercial Mobile Services, at ¶ 47 n.117 (June 24, 2011)("15th Competition Report"); *see also,* Applications of AT&T Inc. and Centennial Communications Corp. for Consent to Transfer Control of Licenses, Authorizations, and Spectrum Leasing Arrangements, WT Docket No. 08-246, *Memorandum Opinion and Order*, 24 FCC Rcd 13915 (2009) (*AT&T-Centennial Order*); Applications of Cellco Partnership d/b/a Verizon Wireless and Atlantis Holdings LLC For Consent to Transfer Control of Licenses, Authorizations, and Spectrum Manager and *De Facto* Transfer Leasing Arrangements and Petition for Declaratory Ruling that the Transaction is Consistent with Section 310(b)(4) of the Communications Act, WT Docket No. 08-95, *Memorandum Opinion and Order*, 23 FCC Rcd 17444 (2008) (*Verizon Wireless-Alltel Order*).