

**WRITTEN STATEMENT**

**of**

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**before the**

**U.S. SENATE COMMITTEE ON COMMERCE, SCIENCE AND TRANSPORTATION**

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## **INTRODUCTION**

Good afternoon, Mr. Chairman and members of the Committee. I am John Rooney, President and Chief Executive Officer of United States Cellular Corporation. Thank you for the opportunity to appear before you today. My testimony addresses why the Federal Communications Commission must examine wireless carriers' handset exclusivity arrangements and impose restrictions on these practices. These arrangements harm consumers in rural areas and decrease competition nationwide and do not enhance innovation.

Expanding wireless broadband services is an important public policy, and the dominant carriers' handset practices should not be allowed to continue impeding this goal. We also ask the Committee to examine the business practices of dominant carriers in a broader context, to protect robust competition and ensure that consumers have the ability to choose the handset *and* the network that best suit their needs. We think the bi-partisan letter from some members of this Committee of earlier this week to the FCC requesting expeditious examination of the issue and decisive action if such arrangements are found to unfairly restrict consumer choice or adversely impact wireless competition is a really good step.

## **WIRELESS MARKETPLACE**

U.S. Cellular provides wireless services in nearly 200 markets located in regional clusters across the country. We serve many of the states represented on this Committee, including West Virginia, Texas, Maine, California, Kansas, Minnesota, Missouri, Nebraska, Virginia, and Washington. The overwhelming majority of the geography we serve is rural.

We continue to expand our network to increase coverage, call quality and the availability of broadband services. In 2008, U.S. Cellular deployed new cell towers to bring wireless service to unserved and underserved areas in every state where we provide service. As

we aggressively upgrade our CDMA networks with third-generation technology (EVDO rev-A), we have been or are likely to be the first provider of broadband wireless services in many rural markets.

Satisfying customers with excellent network quality and customer service is central to U.S. Cellular's operations. For the seventh consecutive time, U.S. Cellular received the J.D. Power and Associates award for overall call quality in the North Central Region. Moreover, people in our service areas increasingly look to our network for advanced wireless services, as shown by the 36 percent increase in our data revenues in the most recent quarter.

U.S. Cellular serves over 6.2 million customers, making us the country's fifth largest wireless carrier. Yet, we are tiny compared to the two wireless industry giants -- Verizon Wireless is about 14 times our size, and AT&T is about 13 times larger. Together, these two dominant carriers account for about 60 percent of subscribers nationwide. The next two leading carriers are part of the excessive concentration in this industry -- Sprint Nextel is over 8 times our size, and T-Mobile is over 5 times larger. These four carriers, which collectively hold a 90% market share, have come to dominate the industry not through superior network quality or efficiency, but rather because the FCC and Justice Department approved a long string of acquisitions in this decade.

Despite their size and huge spectrum holdings, the Big Four carriers have decided not to serve many rural areas. These carriers focus on providing service in densely populated urban areas, and their coverage is much more limited in rural areas, especially away from major highways. For example, many rural residents of Alaska, Arizona, Colorado, Idaho, Kansas, Maine, Montana, Nebraska, Nevada, New Hampshire, New Mexico, North Dakota, South Dakota, Utah, West Virginia and Wyoming are not served by AT&T network facilities. Many

rural residents and businesses look to U.S. Cellular and other smaller carriers to provide them with important voice and data wireless services to raise their productivity, give them access to public safety and health care services, and improve their quality of life.

## **HANSET EXCLUSIVITY**

One manifestation of wireless market concentration is the ability of dominant carriers to tie up almost all of the most advanced, attractive handsets through exclusive arrangements. While U.S. Cellular sells about 3 million handsets annually, each of the two largest carriers sell that many in four weeks. The Big Four exert their enormous buying and marketing clout over handset manufacturers. Recently, nine of the ten most popular handsets were offered exclusively by one of the Big Four carriers.

In rural areas where none of the Big Four carriers offers service, their exclusive handsets are simply not available to consumers at any price. Where the Big Four have built networks, people who want to use Apple's iPhone have to sign up for service with AT&T and people who want Blackberry's Storm have to take service from Verizon Wireless, even if their prices, network quality, and customer service levels do not measure up to their competitors.

The handset exclusivity period negotiated by the dominant carriers is often five years or, in some cases, for the lifetime of the device. In some cases they apply to handsets not yet developed. Handset technologies and features are advancing rapidly, with the lifecycle of handsets averaging about twelve months after initial commercial offering. Consequently, even an exclusive period of six months — together with the five or six months needed to test and launch a handset on another network — can greatly impair the availability of that handset through other carriers.

As I will explain, the dominant carriers' handset practices harm consumers in rural areas and decrease competition nationwide. The remainder of my testimony is organized in

three sections: (1) harms to rural consumers and broadband expansion; (2) decreasing competition nationwide; and (3) actions the FCC should take to promote the public interest.

## **1. Harms to Rural Consumers and Broadband Expansion**

The four dominant wireless carriers have locked-up almost all of the advanced, highly desired devices. Consumer harms from these practices are especially severe in rural areas. Since the Big Four carriers have decided not to build high-quality networks in many rural areas, many rural residents cannot use some or all of these advanced handsets. Inability to use the best devices impairs business productivity and quality of life for rural residents.

Although U.S. Cellular and other smaller carriers are aggressively expanding their networks and broadband wireless deployment, they cannot offer certain handsets. Many rural consumers are left unsatisfied by inferior wireless service from the Big Four and an inability to access the most desirable devices from competitors.

In rural areas where one of the Big Four carriers provides service, it can attract customers to its exclusive handsets and services even with higher prices and inferior network coverage. The handset advantage dulls a Big Four carrier's incentive to invest in improving its service quality and network coverage in rural areas. Moreover, a decision to invest in network facilities that can deliver advanced services is greatly complicated when you cannot offer the most advanced handsets to attract customers.

Despite the public policies and programs supporting comparable telecom services in urban and rural areas, the dominant carriers are consigning rural businesses and residents to second class status for some handset-enabled capabilities. We are not talking about just sleeker cases or cooler video games. For example, some leading education applications for medical professionals and students are only available to AT&T's customers through the Apple iPhone.

These applications and features are not available in many rural areas, even though smaller carriers serve those areas and are eager to provide the most advanced services there.

Congress is to be commended for expanding rural broadband wireless services via the American Recovery and Reinvestment Act of 2009. This legislation wisely provides grants through the Departments of Agriculture and Commerce for broadband wireless infrastructure projects. These projects are vital for the economic health of rural areas and for the economic recovery of the entire nation. Additionally, they can contribute to rural education, health care, public safety services and quality of life. However, infrastructure projects alone will not bring the most advanced wireless broadband services to rural areas. The federal government must ensure that rural citizens have reasonably comparable choices in telecommunications products and services. This hearing is an important step in eliminating the detrimental effects on rural areas of the dominant carriers' handset exclusivity arrangements.

## **2. Decreasing Competition Nationwide**

While rural areas suffer particularly severe harms from handset exclusivity arrangements, these practices hurt businesses and consumers in markets nationwide by lessening competition in wireless services. Smaller carriers are drivers of wireless competition and innovation, but are handicapped by these practices. There is no evidence showing that these practices create significant pro-competitive benefits.

Congress recognized the competitive importance of smaller wireless carriers in directing the FCC to disseminate licenses among a wide variety of applicants and to avoid excessive concentration of licenses. Wisely, Congress sought to avoid the harms to consumers and the nation from an oligopoly in this critical industry. Nevertheless, the FCC has approved a series of transactions and rules leading to domination of the wireless market by just four carriers.

And among those four, two are exerting increasing power with each acquisition. These carriers have recently leveraged their huge subscriber bases and dominant spectrum holdings to obtain exclusive distribution arrangements for almost all of the hottest handsets. While several smaller carriers have been acquired by the Big Four, there are many markets where other smaller carriers remain significant competitors, many markets where smaller carriers are expanding their networks, and many markets where smaller carriers are entering.

Smaller carriers like U.S. Cellular have been able to achieve excellent network quality and offer competitive prices. In part our success in building competitive networks in rural areas has been a direct result of our participation in the federal universal service program. We have used federal universal service funds to build cell sites and improve network quality in rural areas that would not otherwise receive such investments. The increased competition in the areas where we are building networks has delivered tremendous consumer benefits including:

- Improved health and safety through our CDMA technology's superior E-911 accuracy, along with improved coverage enabling critical and sometimes life saving calls to be placed;
- Improved economic development opportunities in every area where businesses need mobile wireless services to improve efficiency and productivity;
- Lower prices as a result of our wider local calling areas, enabling many rural citizens to avoid expensive toll charges on competing networks;
- Increased availability and improved telecommunications services encourages all other carriers to improve service quality; and
- Job creation in two areas: (1) jobs created by the construction and operation of new network facilities, and (2) jobs created through the "multiplier effect", that is, the presence of a mobile wireless network driving secondary investments from industries that use our technology.

Economic development benefits described above will increasingly require a smartphone, which is capable of voice, messaging, and Internet access. Many businesses increasingly rely on applications available over the Internet, which cannot be accessed on a traditional telephone device. It is frustrating for rural consumers to be denied the ability to purchase the best smartphone devices and place them on the network that delivers the best coverage. It scarcely bears mention that network quality is important to a business user. Unfortunately, the Big Four's control over the most advanced, attractive handsets has made it significantly harder for smaller carriers to attract and retain subscribers, and to effectively compete in rural areas, even with federal universal service support.

Our perspective that the Big Four carriers have less interest in providing high-quality service to rural communities is borne out by our experience. We know that in almost every area where we are investing federal universal service funds, our network quality is superior. Beyond just our experience, however, it is important for the Committee to understand that at a time when we are experiencing the worst economic crisis since the Great Depression, a time when job creation and business investment are critical to helping citizens, Verizon Wireless and Sprint have voluntarily agreed to withdraw from receiving federal universal service support as a condition to approval of large merger transactions.

What is the takeaway from these actions? From our perspective, these carriers may wish to free themselves from the additional regulatory burdens associated with the receipt of universal service support, a valid motive if their business plan does not include providing high-quality service throughout the rural areas where their universal service obligations attach. Our problem is not their choice to forego universal service – it is that we cannot offer the best devices to consumers in areas where we are providing the best network quality.



In this respect, our parochial business interest aligns with the interests of rural citizens, who are paying into the federal universal service fund and deserve to have the benefits of telecommunications services that are reasonably comparable in quality and price to those available in urban areas. I understand that this is what Congress intended, and that is why we are here. If these practices are allowed to continue, competition in many markets will fall and consumers will pay more for inferior network services.

Of course, the dominant carriers have proclaimed that their exclusive handset arrangements foster innovation and competition. The experience of U.S. Cellular in about 200 markets across the country does not bear out these claims. Moreover, it is counterintuitive that handset manufacturers with access to a customer base of over 300 million users in the United State alone, would want or need exclusive arrangements that limit the pool of potential customers who can buy their products. In fact, we cannot identify a single market the size of the U.S. handset business that requires exclusive contracts to improve innovation and competition.

This Committee would not approve if a rural customer could not buy an Apple computer because it could only be connected to a particular Internet Service Provider that did not serve that customer's home. We see no reason for a different result in the mobile wireless industry. Moreover, handset exclusivity for Smartphones is just the beginning. We are already seeing exclusivity arrangements being used in the market for netbooks, and if Congress takes no action it will likely spread to other device categories as they are invented.

Consumers would benefit if smaller carriers could offer the most attractive handsets and compete with the dominant carriers on the basis of network quality, customer service and price, as well as handset features. Our subscribers who have enjoyed our leading network quality and customer service would not have to choose between, (a) inferior service but

the hottest handsets from another carrier, or (b) remaining with U.S. Cellular but using a less productive set of handset-enabled applications and features. Additionally, manufacturers would be driven to innovate by rapid distribution to the entire base of nearly 300 million handset buyers, including our 3 million sales annually.

Dr. William P. Rogerson (Professor of Economics at Northwestern University and Chief Economist of the FCC in 1998-99) recently examined the arguments and available evidence on this issue. In an economic analysis filed at the FCC in February 2009, he found no evidence showing that any of the Big Four carriers played a significant role in advancing handset technology. In particular, he concluded that AT&T played almost no role in developing the iPhone, and that the carrier likely made relatively insignificant network and other investments to support this innovative handset.

As wireless markets have become increasingly concentrated this, handset exclusivity (along with decreased roaming opportunities, high special access rates and certain other practices) has emerged as a major threat to competition in markets nationwide. In the next section, I describe the actions that the FCC must take to address this threat.

### **3. Actions the FCC Should Take to Promote the Public Interest**

U.S. Cellular supports the petition for rulemaking filed by the Rural Cellular Association (RCA) at the FCC over one year ago. Along with consumer groups and most wireless carriers, we urged the FCC to commence a rulemaking proceeding to examine the effects on consumers of exclusivity arrangements between wireless carriers and handset manufacturers, and to adopt rules necessary to promote the public interest in competition, innovation and expansion of broadband services. There is convincing evidence in the record demonstrating the need for the FCC to take these actions. Moreover, we agree with RCA's

position that the FCC has authority under the federal statute to prevent carriers from engaging in unreasonable or discriminatory practices. We applaud the letter of earlier this week from some members of this Committee urging the FCC to investigate handset exclusivity arrangements to protect consumers

To date, the FCC has not commenced a rulemaking or restrained the dominant carriers' harmful handset practices. While this petition has been pending, the FCC approved further industry consolidation for the dominant carriers, via acquisitions by Verizon Wireless, AT&T and Sprint. Two pending transactions would add about 2.6 million subscribers for AT&T. During this period, as the dominance of the Big Four increased, they have locked-up almost all of the hottest new handsets, including exclusives for AT&T on new models of Apple's iPhone, for Verizon Wireless on the Blackberry Storm, for Sprint on the Palm Pre, and for T-Mobile on the Samsung Behold. Rural areas and smaller carriers are suffering from the increased consolidation and these handset practices.

The last time that the FCC looked at wireless carriers' exclusive dealing contracts with handset manufacturers was in 1992. The FCC decided that it had the statutory authority to regulate such dealings, and promised "if in the future, it comes to our attention that carriers' exclusive distribution agreements with [handset] manufacturers are resulting in anticompetitive abuse, we will not hesitate to revisit this area." Not only has the FCC received extensive evidence of anticompetitive abuses in response to the RCA petition, but also the changes in the marketplace warrant prompt re-examination by the FCC.

Subscribers to cellular and similar services have grown from 11 million in 1992 to over 270 million in 2008; each of the two largest carriers now annually sells handsets in volumes that are about four times greater than the total number of cellular subscribers in 1992; these two

carriers have through acquisitions come to control about 60 percent or more of handset sales nationwide; wireless devices and services have become critical for business productivity, health care, public safety and other services; about 41 percent of consumers are likely to choose a smartphone for their next mobile device, according to a recent survey; and access to the most advanced handsets is important to achieving rural wireless broadband expansion and competition in markets nationwide.

The FCC's regulation of landline carriers' practices regarding customer equipment has been an unquestioned success in spurring competition, innovation and consumer satisfaction. Congress should direct the FCC promptly to examine wireless carriers' practices in handset exclusivity and take necessary actions to promote the public interest.

## **CONCLUSION**

I am pleased that this Committee is devoting its attention to the emergence of exclusive handset arrangements for the four dominant wireless carriers, and appreciate the opportunity to testify today. By leveraging their market dominance in negotiations with handset manufacturers, the largest wireless carriers are locking-up almost all of the most advanced, attractive handsets for many months or years. These practices deprive rural areas of leading handset-enabled applications and features, and impede the productivity of rural businesses, important services to rural residents and the expansion of broadband capabilities. Furthermore, these practices impair competition in wireless markets nationwide, and do not enhance innovation. Congress should act so that the FCC promptly examines these practices and adopts rules to eliminate these harms.