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AT&T-Time Warner Merger Overview

On October 22, 2016, AT&T Inc. and Time Warner Inc. announced that they had entered into an agreement under which AT&T will merge with Time Warner. As of September 30, 2017, the total transaction value was about $105.8 billion, including $84.5 billion for the purchase of Time Warner stock, and $21.3 billion for the assumption of Time Warner's debt.

The U.S. Department of Justice (DOJ) filed a civil antitrust lawsuit in the U.S. District Court for the District of Columbia to block AT&T's proposed acquisition of Time Warner on November 20, 2017. The trial, overseen by U.S. District Judge Richard Leon, is set to begin on March 19, 2018. Judge Leon said the trial would last about three weeks.

The Two Companies

AT&T is the largest U.S. multichannel video program distributor (MVPD). It provides programming to subscribers through three subscription services: (1) DIRECTV, a satellite-based service with 20.6 million subscribers, (2) U-Verse, a service that uses the AT&T fiber optic and copper infrastructure and has 3.7 million subscribers, and (3) DIRECTV NOW, an online video service with 787,000 subscribers. (Subscriber figures are as of June 30, 2017.) AT&T is also the second-largest wireless carrier in the United States, and has a substantial, although diminishing, wireline telephone business.

Time Warner's three operating divisions, Home Box Office Inc., Turner, and Warner Bros. Entertainment, create television programs and movies as well as operate cable networks. The company sold its music division, Warner Music, in 2003; spun off its MVPD service, Time Warner Cable (now owned by Charter Communications Inc.), in 2009; and spun off publisher Time Inc. in 2014.

Consumer and Industry Trends

The television industry is in the midst of structural changes driven by a combination of competitive pressures, technological developments, and consumer preferences.

Time Warner is one of four major U.S. media conglomerates that own film studios, television studios, and cable networks. The others are Comcast, 21st Century Fox (Fox), and the Walt Disney Company (Disney). On December 14, 2017, Disney announced an agreement to purchase Fox's movie and television studios and several of its cable networks. Government approval of that transaction is pending.

The conglomerates' studios license movies and television programs to cable networks, broadcast networks, MVPDs, and subscription video on demand (SVOD) services such as Netflix, Amazon Prime Video, and Hulu. The conglomerates' cable networks license bundled packages of programs to MVPDs such as Comcast, Charter, DIRECTV, and DISH.

Changes in the way consumers watch television are having profound effects on the television industry. **Table 1** illustrates this trend. Growing numbers of households have dropped their MVPD service or chosen not to subscribe in the first place. Instead, many are subscribing to SVODs and/or other online video services, which, even after the cost of separately purchasing broadband service, can be less expensive.

Table 1. Television Distribution Sources

(% of U.S. television households)

	2014	2015	2016	2017
Broadcast only	10%	11%	12%	13%
MVPD	88%	86%	85%	82%
Broadband only	2%	3%	4%	5%
Total number of TV households	115.5 million	116.4 million	116.4 million	118.4 million

Source: CRS analysis of data from the Nielsen Company.

Notes: Television household estimates are as of January of each year. Distribution source estimates are as of the second quarter of each year.

Consequently, MVPDs have lost subscribers. As subscriber numbers fall, networks such as Time Warner's HBO, TBS, and CNN earn less revenue from MVPDs, which pay them on a per-subscriber basis to carry their programming, and from advertisers, which pay them fees based on the number of viewers. To combat this trend, Time Warner has launched its own SVODs, including HBO Go and FilmStruck. It also has 10% ownership of Hulu.

Moreover, several firms, including the parent companies of MVPDs, have launched or intend to launch "virtual service providers" (VSPs). VSPs deliver feeds of scheduled or "linear" packages of television programs at the same time as they air on cable or broadcast networks. Some may offer programming on an on-demand basis as well. They mimic traditional MVPD services, but are generally less expensive and do not require long term commitments. **Table 2** describes these services.

DOJ's Concerns with Merger

The Antitrust Division of the DOJ reviewed the transaction to determine whether it would substantially reduce competition, as prohibited by Section 7 of the Clayton Antitrust Act of 1914. DOJ sought to stop the transaction by requesting a preliminary injunction, claiming that the transaction would violate Section 7.

Table 2. Virtual Service Providers

Launch Date	Provider Name	Parent/ Funding Sources	Where Available	Includes Time Warner Networks?
Jan. 2015	fuboTV	Funding from 21st Century Fox and Scripps Networks Interactive	nationwide	no
Feb. 2017	Sling TV	Dish Network Corp.	nationwide	yes; in entertainmen t and news tiers
Mar. 2015	PlayStation Vue	Sony Corp.	nationwide	yes
Nov. 2016	DIRECTV NOW	AT&T Inc.	nationwide	yes
Apr. 2017	YouTube TV	Alphabet Inc. (Google)	84 local television markets	no
May 2017	Hulu with Live TV	Disney (30%); Comcast (30%); Fox (30%); Time Warner (10%)	nationwide	yes
June 2017	Century Link Stream	Century Link	nationwide	no
Sept. 2017	XFINITY Instant TV	Comcast	select areas (XFINITY Internet customers only)	yes

Sources: SNL Kagan, Ian Olgeirson and Deana Myers, *The State of Online Video Delivery, 2017 Edition*, S&P Global Market Intelligence, Charlottesville, VA, October 2017, pp. 14-15. Company websites.

In its complaint, DOJ alleges the combined company would use its control over Time Warner's valuable and popular television networks to hinder its rivals by "forcing" them to pay hundreds of millions dollars more per year for the right to distribute those networks. DOJ claims that if the competing video distributors refused to pay the higher price and subsequently dropped the Time Warner networks, AT&T would nonetheless benefit, because its competitors' subscribers would switch to AT&T's own video services.

In addition, DOJ maintains that the combined company would use its increased power to slow the television industry's transition to new video distribution models, specifically virtual service providers, which DOJ claims AT&T views as "threat[s] to the traditional pay-TV model." According to DOJ, Time Warner's networks are "extremely important for many emerging video distributors." DOJ states that prior to the announcement of the merger, Time Warner "secured a position for its networks as 'anchor tenants'" for virtual service providers.

Parties' Response

In their response to DOJ's complaint, AT&T and Time Warner contend that "Time Warner's networks are not, in any antitrust sense of the word, essential to attracting and retaining [video] subscribers." They note that when Google, which they claim is "one of the most well financed and sophisticated companies in the world," launched YouTube TV as an alternative to MVPD services, it did so without any Time Warner networks.

They argue that rather than reducing competition, the transaction is "necessary to allow the combined company to keep pace in an environment where cable is the incumbent market leader and viewer preferences are rapidly tilting towards the direct-to-consumer platforms of Netflix, Google, Amazon Prime, Facebook, Apple, Hulu, and others."

Structural vs. Behavioral Remedies

For many proposed transactions, rather than seeking to stop the deal completely, DOJ and the parties reach consent agreements containing conditions to alleviate competitive concerns. The agreements are subject to court approval. When Comcast, a distributor of video programming, merged with a supplier of video programming, NBCUniversal, in 2011, both DOJ and the FCC reached agreements with the parties that imposed behavioral conditions, including binding arbitration in the event of a dispute related to those conditions.

In their response to DOJ's suit, AT&T and Time Warner offered, in lieu of a consent agreement, to extend arbitration protections to third-party video programming distributors, similar to those adopted in the Comcast-NBCUniversal transaction. They contend that "this contractual regime is self-executing" and would not require government or court monitoring.

DOJ's suit appears consistent with the philosophy expressed by Makan Delrahim, Assistant Attorney General for the Antitrust Division. In a November 2017 speech, Delrahim stated that he viewed behavioral conditions as "fundamentally regulatory, imposing ongoing government oversight on what should preferably be a free market." He added that he expected "to return to the preferred focus on structural relief [e.g., divestitures] to remedy mergers that violate the law and harm the American consumer."

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