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TMUS/S/DISH: Final Notes for How to Watch Before Game Time

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On Monday, the most important trial[1] ever for the wireless industry begins in New York. In this Weekend Update, we provide our final notes on recent developments and how to watch the trial.

We start with a summary of a call we did with antitrust experts last week. While both predicted the States win, both were intrigued by the implications of the Companies still arguing about the deal rather than just focusing on the fix. Both also offered advice on what witnesses and issues to watch for indications of how the Judge might be thinking. We then discuss the most important outcomes and revelations of two pre-trial conferences at the end of last week, including the Judge's own description of the issues, the parties' different framings of the core issue and the implications of the first six witnesses, all designed, we think, to allow the States to introduce course of business documents that will undercut the Companies claim of increased competitiveness as the motive for the deal and the fix.

We review some evidentiary rulings we don't believe will ultimately be material but one that has a potential to provide significant headline risk for the Companies. We note some filings at the FCC that go to an issue raised by the States in their pre-trial memo on the reliance of the Companies on proceedings that have not yet concluded. We conclude with a discussion of the importance of Charlie Ergen's credibility as a witness by reviewing how another judge, in a bankruptcy proceeding, viewed his credibility.

We note that we are again splitting our Weekend Updates in two, with a separate update focused on C-Band and the upcoming Senate mark-up on related legislation being published sometime on Monday.

TMUS/S/DISH

We began last week with a lengthy review of the parties pre-trial memos (LINK). The memos did not alter our view that the States have a better than even chance of prevailing in court. The memos did, however, somewhat alter our perception of how the case would be litigated. We had thought the trial would mostly be about the efficacy of the fix (with our review of the legal framework for litigating the fix available HERE). The parties pre-trial memos suggested, however, that they would be spending more time on the legality of the basic deal. Over the course of the week, we had a call with antitrust experts and there were two pre-trial conferences that filled in a lot of the pieces for watching the trial. We review those below.

Summary of Call with Antitrust Experts. On Thursday we had a call with two antitrust experts, Phil Verveer and Jeff Blattner, to discuss what they thought would happen and how to watch the trial to evaluate its likely outcome. (A replay of the call can be accessed HERE.)

Our summary of the highlights is as follows:

Odds favor the States. Mr. Verveer put odds of States winning at 60%-75% and said he would go even higher

save for inherit unpredictability of litigation. Mr. Blattner thought "odds slightly favor the States," with lower odds than Mr. Verveer in particular because of the difficult precedent of allowing States to block nationally approved merger.

Settlement unlikely, appeal difficult. While Wall Street has focused on the possibility of settling before the trial, settlement is also possible during and after, but before the judge releases his decision. On settlement, Mr. Verveer thought the States have very different motives than commercial litigants for settling before trial and therefore settlement is only likely if the judge appears to strongly favor the Companies during trial. While an appeal is also possible, Mr. Verveer pointed out that the trial judge is likely to be especially careful to base his opinion on the facts, making the odds of success of any appeal difficult, [2] though Mr. Blattner noted that on antitrust issues, the Second Circuit is a bit of a "wild card" and therefore the Companies might have a chance.

Trial may be less about litigating the fix than previously thought. While both experts had believed that the Companies would focus their trial efforts on the fix, the Companies' pretrial memos suggest the Companies will focus more on defending the deal itself by focusing on the efficiencies gained through the increased capacity. Mr. Verveer said this was likely because the Companies view their odds of prevailing by focusing on the DOJ's fix as low, so instead they will "throw deep" and see if something sticks, but that ultimately, the Judge's view of the fix would determine the outcome. Mr. Blattner suggested that perhaps it was because the capacity argument was stronger, relative to the fix, and that the States' answer on the capacity issue was weaker. In this regard, Mr. Blattner pointed out that by arguing that the capacity gains are so great as to inherently lead to lower prices, the Companies may prevent the States from making a *prima facie* case of illegality. As to the fix, Mr. Blattner noted that the 7-year MVNO for Dish is a problem for the Companies as it goes beyond the 2-to-3-year window for ameliorating competitive harm that is a core principle for antitrust practice. Both Mr. Verveer and Mr. Blattner characterized the Companies' effort to win on the basic deal as dependent on painting the deal as something of a "unicorn" in terms of the deal's efficiencies. Both also noted how the DOJ complaint, however, undermined the Companies' arguments about the deal, with Mr. Verveer suggesting that the DOJ complaint has essentially "underwritten" the argument for the States.

Witness credibility is key: Ergen and experts top the list. Both Mr. Verveer and Blattner discussed the importance of the credibility of the witnesses. Both thought that Mr. Ergen, the CEO of DISH, would be the most important witness, with the economic experts also likely to be critical. Mr. Blattner knows and has worked with the three principal economic experts and believes Carl Shapiro's—lead economic witness for the States—testimony will be most critical. Mr. Blattner suggested Fiona Scott Morton—another economic expert for the States—may lack experience in testifying in such settings. He also pointed out that Michael Katz, the lead economic witness for the Companies, is brilliant but less detail-oriented than Shapiro. A question arose about Judge Richard Leon finding that Shapiro was not be a credible witness in the AT&T/Time Warner case, but Mr. Blattner thought that won't necessarily impact the judge's thinking here. There was also agreement that in light of the importance of the fix, if the judge doesn't think Charlie Ergen is credible, the case for the DOJ's fix is difficult, making the Companies' odds of prevailing even less. (We discuss how another court viewed Mr. Ergen's credibility below.)

The importance of course-of-business evidence. After the call, Mr. Verveer contacted us to note that one thing we did not discuss, but maybe should have, is that the course-of-business documentary evidence could turn out to be more telling of outcomes than the abstruse economics. So, for investors looking for indicators in the midst of the trial, the course of business documents introduced into evidence are probably the most important data points to watch (apart from the judge's reactions during the proceeding). We note that this is consistent with what Matthew Cantor, another antitrust expert we discussed the trial with on an investor call back in September also said. As discussed further below, in light of the first witnesses the States will call, it

appears that the States believe they have strong course of business evidence.

Summary of two hearings. On Thursday and Friday, there were two final pretrial hearings, one before the magistrates and a second one before the Judge. Our key takeaways from the hearings are as follows.

Parties view core question differently. The parties, at the second hearing, did a good job of framing what they saw as the key question in the case in a way that signals how they expect to try the case.

The States' view. The States lead counsel said "we would start and put on evidence that would show that we're entitled to the presumption *(of illegality*), and we would put on certain evidence that would support the anticompetitive effects of the transaction. That would then shift the burden of production to the defendants, and they would put on evidence that there weren't such anticompetitive effects, maybe that we weren't entitled to the presumption, and any defenses they were offering. And I think the issue here comes to the defenses. We see that they are offering three different defenses, and your Honor mentioned all of them: The efficiencies defense, the defense that Sprint is a weakened competitor, and the defense that the remedies they have agreed to with the federal regulators have resolved the competition concerns." In other words, in the States' view, if the States establish the presumptive illegality of the deal and that the fix is not timely, likely or sufficient, the States should win.

The Companies' view. In contrast, the Companies counsel said "The burden that the plaintiff has is to present evidence to the Court demonstrating that the world with the merger would be substantially less competitive than the world without the merger. In doing that, they have to put before the Court evidence of what those two worlds look like and in order to establish their prima facie case they have to establish that one is substantially less competitive than the other." In other words, in the Companies view, the issue before the court is simply judging the relative competitive impact of a world with the deal with the world without it. The Judge should simply be judging the relative competition merits of the two paths going forward.

Both lead to the DISH v. Sprint issue as critical. For some time, we have thought that the Company's strongest element at trial is that it will have two compelling witnesses for how the deal will lead to competition: someone from T-Mobile, and Mr. Ergen from DISH. On the contrary, there will not be any witness from Sprint who will testify how Sprint will bring competition to the market if it continues to be an independent entity. While various experts can speculate on that, an executive saying to the Judge "I will do this" is much stronger than an outside expert speculating "they could do this." The Companies' lawyer confirmed that that will be their approach. Of course, the States have anticipated this and noted in their pretrial memo that "Defendants would have the Court believe that their proposed divestitures to, and their related agreements with, DISH will suffice to create a new wireless operator that can replace Sprint. But Sprint is a company with tens of millions of current customers, a long history in this industry, and a nationwide wireless network. DISH is a company with no current wireless customers, no history in this industry, and no retail wireless network. Even under DISH's rosy projections, it would not come close to addressing the loss of competition caused by the merger over the next few years." Still, given the way the Companies intend to argue, it raises the stakes for testimony about what will happen with an independent Sprint and how does that compare to what T-Mobile and DISH will do.

Judge listed issues. The Judge began the second conference with a discussion of the issues he said were open, by which we think he means were relevant to the decision and on which the parties disagree. We don't think the Judge signaled his own view on any of the issues. Our summary of his statement of the issues follows, broken down into issues related to the presumptive illegality of the deal as proposed and the deal as fixed by various agreements and conditions.

Questions on prima facie case

- Geographic market
  - Nationwide or local? Is less competition in one local market sufficient to block?
  - Are local markets defined by FCC CMAs or something else?
- Product market
  - Is it just retail? Should prepaid be considered separately? Should enterprise?
  - Should the in-home broadband market come under consideration?
  - Should the definition exclude MVNOs and Cable, with the Judge specifically asking, "should the calculations of the HHI exclude substantial competitors, such as mobile virtual operators and cable Companies that provide mobile wireless services now?"
- Presumption of illegality
  - Is the HHI above 2500? Locally? Nationally?
- Efficiencies
  - Are efficiencies verifiable and non-speculative?
  - Will they offset the lost competition?
- Sprint standalone
  - The Judge noted that there are "questions concerning Sprint's current competitive and future viability. There are allegations that Sprint is showing signs of financial competitive weakness, declining customer base, market share, customer dissatisfaction, reduced revenues, and lag in network quality. To what extent are those allegations true or can be corroborated by the evidence? There are counter allegations that Sprint's public financial documentation do not support the theory that it is and will be unable to compete in the near future."

Questions on litigating the fix

- DOJ concluded 4 to 3 is illegal; if 4 is the right number, why go 4 to 3 to 4 instead of just blocking?
- Is the new T-Mobile pricing commitment sufficient to overcome anticompetitive harms?
- Is the new 5G deployment commitment sufficient to overcome anticompetitive harms, especially when T-Mobile and Sprint are deploying 5G on their own?
- Are DOJ's DISH remedies sufficient to over anticompetitive effects?
- Will new DISH be sufficient to replace Sprint?
- Is the fix likely, timely, and sufficient? As the Judge noted, the caselaw suggests 2-3 years is the timeline for "timely".
- Will DISH be able to meet the significant barriers to entry and competitive demands of the wireless market?
- Can DISH replace Sprint in 2-3 years? FCC approvals for certain things can take time, and DISH won't be truly independent for much of that time.
- How does DISH's low-band help them?
- How do the divested assets and MVNO help DISH?

While the questions are not a decisive indicator of how the trial will proceed, we think it suggests that there will be roughly equal time spent on the deal and the fix, rather than a focus on the fix, as we would have expected earlier.

First set of witnesses for States all come from the other side. The States revealed the first six witness they intend to call. They are:

1. Roger Sole, CMO Sprint;
2. Angela Rittgers, SVP of Boost Mobile;
3. Timotheus Höttges, CEO DT;
4. Thorsten Langheim, DT Board Member in Charge of "USA and Group Development";
5. Terence Hayes, SVP for Branded Retail, T-Mobile; and
6. Jay Miglionico, Senior Director and General Manager, Boost Mobile: Sales Distribution.

Why these witnesses? To introduce course of business documents and otherwise undercut the Companies claims. What is notable, of course, is that these witnesses are all "hostile" to the States. We

expect that the reason for calling the witnesses is to enable the States to introduce various "course-of-business" documents that will undermine the claim that the purpose and/or likely outcome of the deal is to increase competition. As we have noted before, to the extent that there are facts we do not yet know, other than facts about DISH's plans to compete on the basis of its MVNO and build out and compete on its own facilities, the facts are likely to favor the States. The question is how damaging to the Companies defenses are these documents? We expect to find out early in the trial.

Evidentiary rulings for the Companies: What do they tell us? Also during the week the Judge granted the Companies motion to exclude evidence of studies of foreign market stock price movements that would have been presented by Dr. Shapiro. This is facially good news for the Companies—they obviously didn't want the testimony at trial—but does it tell us anything material to the outcome? We don't think so.

First, the States did not cite these arguments in their memo, suggesting the studies are not core to their argument.

Second, if the States win on the presumed illegality, as we think they will, the trial turns to the fix, for which the arguments are irrelevant. If the States lose on the product market definition or on the efficiencies/capacity issue, and therefore become more likely to lose on the presumed illegality, the foreign and stock market data would not help.

Third, the language in the order suggests Marrero's prime concern in discarding the evidence is his desire to run an efficient trial. As the order notes, "Even assuming that evidence of foreign wireless services mergers was relevant, though, the Court finds that the limited probative value of such evidence would be outweighed by the undue delay that would result from its consideration at trial… The Court concludes that trial time would be better spent developing the evidence of the Proposed Merger's competitive effects that can be derived from the relevant United States markets at issue, rather than wasting time litigating whether and how mergers in foreign wireless markets might conceivably predict those competitive effects." The court's logic for striking the stock market testimony is more substantive, but again, we think that rather than demonstrating any predisposition on the broader issues, we think it is evidence that Judge Marrero wants parties to hone in on the key arguments.

The Email with the Senior Government Official about another government official: Headline risk in trial. Another interesting evidentiary ruling yet to be done involves, as described by the States' attorney, "some of the exhibits that are still at issue are direct communications between a senior executive at one of the defendants and a senior government official. There are also internal e-mails within one of the defendants in which they're discussing one of the government officials or their strategies. This is their strategy for getting regulatory approval or convincing government official X of something."[3]

The States' attorney argued that these documents are relevant as the Companies are arguing that the judge should defer to the wisdom of the federal government in approving the deal, noting that "there's a remedy with the federal government. They are taking the position that that's relevant in this case and that the judge should give weight to that. If the judge is going to give weight to that, then the judge should know what happened that led to that remedy. And not only should the judge know that, the public should know that because this is our government reaching an agreement with the other side that they're now claiming resolves the competition concerns of a merger that affects virtually every American."

Not certain they will become public. We don't have a strong view on whether these documents will eventually become public[4] in the trial[5], or whether they are really relevant to the economic issues underlying the antitrust case. In a way, however, it may not matter. To make the evidentiary ruling, the Judge will see them and he will determine whether the Companies confidentiality arguments are valid but he will also determine the

extent to which the emails undercut the Companies' defer to the federal officials argument.

Potential headline risk. From a headline risk perspective, however, we would guess these emails may have a significant impact. If released, they are likely to make more news than other ordinary-course-of-business documents and public reaction will likely deem them to lower the odds of the Companies' winning, even if they are only marginally related to the economic case.

Ergen as a witness; Critical, but will he be credible? Given the importance under both sides' framing, of whether or not DISH will provide "timely, likely, and sufficient" competition to compensate for lost competition due to Sprint's leaving the marketplace, his credibility is critical to the Companies' case. We believe he will be a very credible and compelling witness. One cannot accomplish what he has—building a company that took on an entrenched monopolist at that time (cable in the MVPD market) without an ability to be compelling to a large number of constituencies. Further, in our own dealings with him, we have always found him to be well-informed and straight forward.

We decided, however, to see if others, particularly Judges, found him so. We can't claim to have uncovered every case in which he was a witness, but we did find an opinion in which a Judge directly opinined on his credibility. It involved the bankruptcy of Lightsquared, an entity for which Mr. Ergen was a creditor and arguably a competitor.

In that 2014 decision,[6] Judge Chapman wrote that Mr. Ergen's "answers with respect to potential competition between DISH and LightSquared were facile and disingenuous. Moreover, his testimony with respect to actions taken by DISH …defies common sense. Mr. Ergen's testimony on this point was not credible. His testimony with respect to his dealings with Inmarsat was also not credible." The Judge later observed that "Mr. Ergen attempted to disclaim that DISH and LightSquared were competitors…Mr. Ergen later admitted that both DISH and LightSquared today would compete." Later in the opinion, the Judge writes "Moreover, the words and behavior of Mr. Ergen in connection with the December 11 auction are not exactly what one would expect to hear and see from a stalking horse bidder who had snagged assets that were worth, in DISH's hands, billions of dollars of net incremental value." At another point she added "What is in undisputable, however, is that the actions of Mr. Ergen in this regard defy logical explanation."

The point, of course, is not that Ergen lost because of his credibility problems– he didn't. In fact, in that case Ergen benefited from an open-ended decision that required the debtor parties to pay him off. The overall opinion makes clear that Ergen won in spite of his testimony, because the judge in that case didn't see any admirable behavior from anyone. Moreover, the point is not that Judge Marrero in the antitrust case will have the same impression of Ergen that Judge Chapman had of Ergen in the bankruptcy case. The context and facts are very different. Perhaps most important, in the bankruptcy case, the issues involved what Ergen had done. In the antitrust case, while the past is relevant, the testimony will likely focus on what Ergen will do. It is obviously easier to defend one's future views than one's past actions.

The point is simply that part of the uncertainty (and drama) of a trial is that very human reactions to other human beings can color the ultimate outcome. While we believe Judge Marrero will find Ergen a compelling and credible witness, if he starts to see him as Judge Chapman did, it will be much more difficult to for the Companies to prevail.

FCC filing. Last week we noted that the States' memo suggested that "significant aspects of this package of remedies require future action by the FCC. For example, DISH currently faces different pre-existing FCC buildout deadlines, and this package of remedies is contingent on the FCC agreeing to modify those deadlines. Similarly, the network access agreement between DISH and New T-Mobile is not yet executed and depends on

further FCC action. Neither Defendants nor this Court can predict with certainty how the FCC will ultimately resolve these issues. Accordingly, Defendants cannot show, at this time, that this package of remedies and related divestitures 'will actually occur.'"

This week there were various filings at the FCC, such as by the Rural Wireless Association and the Communications Workers of America, objecting to the modifications of DISH's licenses. As a theoretical matter, the States are right. Without knowing how the FCC will rule, it is impossible to accurately gauge how DISH will proceed. As a practical matter, however, we expect the FCC to grant the modifications, as the majority has effectively committed their votes to doing what it takes to get the deal done. We don't see this issue as core to the States' case and, given the Judge's concern for focus and time, would not be surprised to see the issue moved to the side. Still, the Judge did mention it and the need for "FCC approvals, which entail significant bureaucratic process" so the issue does remain another potential wild card in a trial that has many others.

Legal Correction on FCC Clayton Act Authority. In our note on the pretrial memo, we quoted the States' memo, which says "In any event, this Court should not defer to USDOJ's (or the FCC's) decision. USDOJ does not have exclusive jurisdiction to enforce the Clayton Act, and the FCC has no such authority at all." We should have noted that this appears to be technically wrong as 15 USC 21(a) expressly confers Clayton Act authority upon the FCC. The States' point, however, is really about deference, which is a judgement that the Judge has significant flexibility in making.

Trial going forward: Two day heads up. Finally, we note that the Judge closed the conference by noting that "we'll develop the schedule at the end of each day as to who is on deck for the next two days so that each party has a running indication of who to be expected as witnesses from day-to-day." That also means investors should not expect a full schedule at any time in the trial, but will only be getting a couple days heads up on witnesses.

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1. One could argue it was actually the trial that broke up AT&T but at that point, the wireless industry largely existed in the brilliant imagination of some engineers and a young cable executive named Craig McCaw. Wireless was considered so unimportant that the lawyer for AT&T basically gave away the cellular licenses to the Baby Bells without much thought. Because Karma has a weirder sense of humor than any of us can possibly understand, that lawyer eventually became the CEO of AT&T Wireless, which AT&T created by spending $12.6 billion to buy McCaw's company, instead of simply having the original licenses.

2. Generally, Courts of Appeal only overturn decisions of trial courts based on errors of law, accepting the findings of fact as stated by the trial court.

3. We do not have any direct or indirect knowledge of the content of the emails. We simply note that when Pai and the FCC went first, we explained it as a political strategy designed to box Delrahim in, forcing him to choose between Team Red and Team Blue. That view of the tactical reason for going first was reinforced by others, including certain gleeful tweets from Charles Gasparino about Delrahim's political situation, with Gasparino throughout the process being a good gauge of what T-Mobile is telling people. We would therefore guess that the emails are from a TMUS executive to either Pai or Larry Kudlow in the White House explaining the political strategy and casting doubts for any reader as to the Clayton Act bona fides of the DOJ decision. But we admit to just speculating. The emails could be much more benign, or much, much more malignant.

4. We do have a strong view of whether we would like them to be released. In a word YES! YES! YES! We admit to having a prurient interest in the various ways people lobby government officials. Lobbying is not like sex in many ways but it is in this way; it usually takes place in rooms with a small number of people, with the most important part of the activity remaining undisclosed to others. So, while a lot of people have done it, everyone who has wonders how others really do it. So, without any pride and maybe a little bit of shame, we just would say we would sacrifice all other Christmas and Hanukah presents for an opportunity to read these emails.

5. There are other ways the emails could be released. For example, while we don't think House Democrats will investigate Pai about his communications with the White House on C-Band the way Congressional Republicans investigated Wheeler on his White House communications on Title II, (see our upcoming note on C-Band for an explanation) we could see various House Committees having an interest in such communications, even if the trial judge sees the emails as irrelevant to the Clayton Act.

6. The decision was the "DECISION DENYING CONFIRMATION OF DEBTORS' THIRD AMENDED JOINT PLAN PURSUANT TO CHAPTER 11 OF BANKRUPTCY CODE." We seriously advise taking two aspirin before reading. Amazingly, it involves more lawyers than even this antitrust case and the fact pattern is an order of magnitude more difficult to follow.