VERNER · LIIPFERT
BERNHARD · MCPHERSON AND HAND
CHARTERED

901 - 15TH STREET, N.W.
WASHINGTON, D.C. 20005-2301
(202) 371-6000
FAX: (202) 371-6279

MAY 11 2000

WRITER'S DIRECT DIAL
(202) 371-6206

May 11, 2000

DOCKET FILE COPY ORIGINAL

VIA HAND DELIVERY

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, D.C. 20554

Re: Reply Comments of The Walt Disney Company in CS Docket No. 00-30

Dear Ms. Salas:

Enclosed for filing please find the original and nine (9) copies of the Reply Comments of The Walt Disney Company in the above-referenced docket.

Please stamp and return to this office with the courier the enclosed extra copy of this filing designated for that purpose. Please direct any questions that you may have to the undersigned.

Respectfully submitted,

Lawrence R. Sidman

Lawrence R. Sidman

Enclosures

No. of Copies rec'd 0+10
List A B C D E

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Applications of America Online, Inc.	)	**CS Docket No. 00-30**
and Time Warner, Inc. for	)	
Transfers of Control	)	

REPLY COMMENTS OF

THE WALT DISNEY COMPANY

Lawrence R. Sidman, Esquire
Lawrence Duncan, III, Esquire
Jessica A. Wallace, Esquire
VERNER, LIIPFERT, BERNHARD,
MCPHERSON & HAND, CHARTERED
901 15th Street, N.W., Suite 700
Washington, D.C. 20005
(202) 371-6206

Counsel for The Walt Disney Company

TABLE OF CONTENTS

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Applications of America Online, Inc.	)	**CS Docket No. 00-30**
and Time Warner, Inc. for	)	
Transfers of Control	)	

REPLY COMMENTS OF

THE WALT DISNEY COMPANY

I. INTRODUCTION AND SUMMARY

The Walt Disney Company ("TWDC") submits these Reply Comments in the above captioned proceeding in which the Commission must determine whether the proposed merger between America Online ("AOL") and Time Warner ("Time Warner") is in the public interest. The AOL/Time Warner merger requires careful review by the Commission because of its potentially profound implications for competition, diversity of viewpoints and consumer choice in the emerging broadband services market, which includes interactive television and electronic commerce.

Time Warner is the nation's second largest cable systems operator, passing more than 20 million homes, and it owns many of the most important and popular cable networks, including CNN and HBO. Time Warner and AOL each provide Internet access services.[1] Both Time Warner and AOL provide content over the Internet.[2] And, AOL is the dominant provider of "sticky" online services such as chat and instant messaging ("IM"), commanding a 90 percent

[1] Comments of AOL/Time Warner at 7.

[2] Comments of AOL/Time Warner at 7.

share of the IM market.[3] Thus, the merged entity will not only own the only interactive television capable "broadband" pipeline into millions of American homes, but will also own highly significant content and overlapping Internet services and applications travelling over that pipeline as well. This level of integration of control of content and broadband distribution will create undeniable economic incentives and opportunity for the merged entity to favor its own affiliated content and to discriminate against unaffiliated content providers, thereby limiting and skewing consumer choice. Moreover, the sheer power and sophistication of the technology which supports and enhances the broadband delivery system augments the capacity of its owner to discriminate against unaffiliated content providers. Allowing any entity to have this level of control over this country's broadband future raises issues of profound public interest concerns.

In reviewing this merger, the Commission must be satisfied that the combination of Time Warner and AOL will do nothing to impede the free flow of news, information, entertainment, services, and commerce to consumers. Broadband must remain a highway on which all can travel and not become a proprietary cul-de-sac. Given the vast degree of vertical integration involved, the Commission can achieve that end only by attaching strong conditions of non-discrimination onto the merger as a prerequisite to any possible approval. Without this safeguard, the Commission will risk the potential for discrimination against unaffiliated content providers and Internet services providers, harms that would stifle competition in the emerging broadband services market.

In newly developing technologies, system architecture dictates policy. The public interest genius of the Internet has been its end-to-end connectivity. The network is not capable

[3] *See* Comments of Tribal Voice at 1.

of discrimination.[4] As we migrate to broadband and interactive television, we <u>must</u> have strong government mandates to preserve unfettered consumer choice. Purely voluntary pledges will not suffice.

II. STANDARD OF REVIEW BY THE COMMISSION.

The merger of AOL and Time Warner is the largest in corporate history,[5] and if approved would create the world's biggest media company.[6] The standard for Commission review of this merger is clear: it must serve "the public interest."[7] In applying the standard, the Commission is not wedded to antitrust principles alone.[8] To the contrary, the Commission has a broader charter to assure proposed mergers do not lessen the diversity of voices. "Assuring that the public has access to a multiplicity of information sources is a governmental purpose of the highest order, for it promotes values central to the First Amendment."[9] This is especially so where, as here, the proposed merger threatens to limit consumer choice in news and information.

Here, Time Warner and AOL seek to join two platforms – the cable platform and the Internet platform – proposing to retain for the merged entity gatekeeper control over the pipeline

---

4 Lawrence Lessig, Code and Other Laws Of Cyberspace (1999) ("The architecture of the Internet, as it stands right now, is perhaps the most important model of free speech since the founding." at 207).

5 *AOL, Time Warner Merge to Form Media Giant*, The Business Journal, No. 39, Vol. 17; January 14, 2000 at 16.

6 *Id.*

7 The Commission has unequivocally stated that it will approve the transfer of licenses and other authorizations underlying a merger between communications companies only if the transaction is in the "public interest, convenience and necessity." Applications of NYNEX Corporation and Bell Atlantic Corporation for Consent to Transfer Control of NYNEX Corporation and Its Subsidiaries, File No. NSD-L-96-10, Memorandum Opinion and Order, 12 FCC Rcd 19985, 19987 (1997) ("NYNEX/Bell Atlantic Order").

8 This is not to say, of course, that antitrust concerns are beside the point. Indeed, to meet its public interest test, the Commission has made clear that a merger must be pro-competitive, that is, "if the harms to competition – *i.e.*, enhancing market power, slowing the decline of market power, or impairing this Commission's ability properly to establish and enforce those rules necessary to establish and maintain the competition that will be a prerequisite to regulation -- are outweighed by benefits that enhance competition."

9 *Turner Broadcasting Systems, Inc. v. FCC*, 51 U.S. 622, 663 (1994), "As the Supreme Court recently reaffirmed, 'it has long been a basic tenet of national communications policy that the 'widest possible dissemination of information from diverse and antagonistic sources is essential to the welfare of the public.'" Review of the Commission's Regulations Governing Television Broadcasting; Television Satellite Stations Review of Policy and Rules, 14 FCC Rcd 12903, Report and Order in MM Docket 91-221 (1999). (citing Turner Broadcasting System, Inc. v. FCC, 512 U.S. 622, 663 (1994) ("Turner I") (quoting United States v. Midwest Video Corp., 406 U.D. 649, 668 (1972) (plurality opinion)(quoting Associated Press v. United States, 326 U.S. 1, 20 (1945).

for delivery of video programming and broadband services and a vast array of content flowing over that pipeline. Due to the proposed common control over content and conduit, the proposed merger poses unique competition concerns which extend beyond economics to the potential threat to diverse sources of news and information in the digital age.

For these reasons, the Commission's review must be more rigorous than any of its reviews of the top industry mergers of recent years, including the Bell company mergers and previous cable industry mergers. The Commission is bound by precedent and statutory obligation to conduct a thoughtful and careful public interest analysis and to apply the standard first enunciated in the NYNEX/Bell Atlantic merger.[10]

III. TIME WARNER AND AOL MAINTAIN ENORMOUS MARKET POWER IN THEIR CURRENT MARKETS OF OPERATION.

A. Time Warner's Current Degree of Vertical Integration Already Creates Substantial Market Power.

Time Warner is the second largest cable operator in the United States. Time Warner's cable pipeline serves 13 million subscribers and passes 20.7 million homes.[11] Time Warner is also one of the country's largest producers of content. Specifically, Time Warner owns a broadcast television network, WB, one of the largest movie and television studios, Warner Brothers; and four of the top fifteen cable programming networks: CNN (14th), TNT (3rd), TBS (2nd), and the Cartoon Network (5th), as well as CNNin, CNNSI, and Home Box Office (HBO), the leading premium cable programming service.[12] To round out this vast collection of content

10 *See* Comments of SBC Communications Inc. at 16-18.

11 *Top 25 Cable Operators*, Broadcasting & Cable at 28 (May 1, 2000).

12 Sixth Annual Report, Annual Assessment of Competition in Markets for the Delivery of Video Programming, CS Docket No. 99-230, FCC 99-418, App. D (rel. Jan. 14, 2000).

sources, Time Warner also owns significant print media including Time, People, Sports Illustrated, Fortune, and some twenty-eight other magazines.[13]

Time Warner's vertical integration has already extended into the online world. Time Warner is using the breadth of its enormous cable pipeline system to quickly emerge as a dominant force in the high speed residential Internet services market. Time Warner and its closest affiliates alone already serve 32 percent of all high-speed residential Internet subscribers.[14]

Time Warner's current market power as a conduit into American homes cannot be fully appreciated without taking into account its business ties to cable/phone giant AT&T/TCI and its merger partner, Media One. Assuming approval of the Media One merger with AT&T, Time Warner and AT&T/TCI/Media One would operate as an interconnected consortium passing 83 million U.S. homes – 80 percent of all U.S. households.[15] In addition, Time Warner and AT&T/Media One, which owns its own broadband service Excite@Home, would share control of RoadRunner, the second largest provider of residential broadband Internet access, serving over 550,000 broadband customers.[16] Moreover, AT&T, through Liberty Media, owns 9 percent of Time Warner. Media One owns 26 percent of Time Warner Entertainment with an option to purchase 6.3 percent more. Taken together, the cross interests of AT&T and Time Warner are enormous in the broadband services market, including control of 69 percent of the high-speed

[13] *See* Applications and Public Interest Statement of AOL and Time Warner at 4.

[14] Comments of SBC Communications at 5.

[15] *See* Comments of SBC Communications at 7.

[16] *See* Comments of SBC Communications at 11.

residential Internet access market.[17]

B. AOL is the Dominant Company in the Internet Services Market.

AOL is the world's leader in interactive services, Web brands, Internet technologies, and e-commerce services. AOL operates two worldwide Internet services: America Online, with more than 22 million members, and CompuServe, with more than 2.2 million members; several leading Internet brands including ICQ, AOL Instant Messenger and Digital City, Inc.; the Netscape Netcenter and AOL.COM portals; the Netscape Navigator and Communicator browsers; AOL MovieFone, the nation's leading movie listing guide and ticketing service; and Spinner Networks and NullSoft, Inc., leaders in Internet music. Through its strategic alliance with Sun Microsystems, AOL also develops and offers easy-to-deploy, end-to-end e-commerce and enterprise solutions for companies operating in the Net Economy.

AOL is the dominant provider of access to narrowband Internet services in the United States. AOL's customer base is approximately 40 percent of the market.[18] Viewed another way, AOL has a customer base that is almost 8 times larger than that of its nearest competitor, making AOL the most powerful Internet Service Provider in all areas of the Internet services market. For example, AOL is the dominant force in the instant messaging market. Instant messaging is emerging as an important new market for the rapid delivery of personalized information to consumers that has the potential of tying consumers to the platform on which it is offered. With over 60 million registered users for its ICQ ("I Seek You") instant messaging service,[19] AOL today controls over 90 percent of the instant messaging market.[20]

---

17 *See* Comments of SBC Communications at 5.

18 *AOL/Time Warner: World's First Internet Age Media and Communications Company*, Bus. Wire, Jan. 10, 2000. AOL added five million members in 1999, more than Microsoft's MSN and AT&T's WorldNet online services combined have signed up in the last five years. Marc Gunther, *These Guys Want It All*, Fortune, Feb. 7, 2000 at 70.

19 *AOL's 3rd Quarter Profits Top Analysts' Predictions*, Washington Times, page B9 (April 19, 2000).

20 Comments of iCast at 2-3.

AOL also controls access to the most sought-after content on the Internet, attracting nearly 77 percent of all Internet subscribers in any given month.[21] AOL manages its proprietary "walled garden" of content and services so that its customers spend as much of their time online as possible in AOL's space. These numbers are only expected to increase as a result of AOL's merger with Time Warner and the resulting access to Time Warner's affiliated content.

IV. COMBINING TIME WARNER AND AOL WILL RESULT IN A DEGREE OF INTEGRATION OF CONTENT AND BROADBAND DISTRIBUTION THAT COMPELS THE IMPOSITION OF NONDISCRIMINATION SAFEGUARDS ATTACHED TO ANY APPROVAL OF THE MERGER.

The markets that Time Warner and AOL dominate today are rapidly becoming intertwined as technological convergence blurs the lines of distinction between the delivery of traditional video, interactive TV, Internet services, and e-commerce. In the Internet environment already, streaming media technology has enabled users to access audio, video, and other services without having to first download the information to computers. Today, consumers receive almost CD-quality sound through a variety of web sites, as well as video, which is rapidly emerging as a major growth area for Internet services. These technological developments have become even more significant as Old World analog cable systems are transitioned into high-speed digital delivery pipes. Such dramatic changes in technology and infrastructure in the last five years have ushered in the arrival of a new, dynamic broadband services market that holds the promise of offering consumers a combined assortment of innovative services, including interactive and on-demand video content, enhanced e-commerce capabilities, Internet content, IP telephony, broadcast video, music and personalized content.

The fusion of these innovative services, delivered over one wire, will likely generate trillions of dollars in economic activity as it feeds consumer demand to engage in "one-stop-

---

[21] *See* Comments of SBC Communications at 13.

clicking" for every broadband service, program, and feature imaginable. Technological convergence and the emerging broadband market also will produce new forms of advertising with e-commerce applications that likely will increase advertising revenue dramatically. The economic growth spurred by the Internet today barely foreshadows the potential offered by the emerging broadband services market.

At present there are only two viable broadband connections into the home – Digital Subscriber Line ("DSL") and high-speed cable modem service. However, cable is, and likely will continue to be for the foreseeable future, the leading conduit for broadband technology in America because of DSL's limited ability to reach consumers who do not live in close proximity to telco switching facilities. Moreover, VDSL, which like cable, is capable of providing video as well as data, is in its earliest and experimental stages of development and deployment and, likely, will lag behind digital cable systems for years. The uncertainty associated with telephone company delivery of full screen, full motion interactive TV over their wires may explain why some telephone companies are turning to satellite television offerings. But, while DBS has a large footprint and a high-speed downstream transmission path, it is not yet suitable for high-speed interactive applications because it depends on telephone lines for its return path. Although DBS theoretically could be mated with a DSL line to enable interactivity, the likely costs of such service would constitute a significant barrier to entry for many consumers. As a result, for the foreseeable future, cable will dominate the market for interactive television.

The convergence of technology onto one wire, coupled with the dominance of the broadband cable platform, raises a serious potential for anticompetitive behavior as the historical behavior of vertically integrated entities in the MVPD market has shown. Without the certainty of safeguards to ensure non-discrimination, the fused AOL/Time Warner could be uniquely positioned as the dominant owner of (1) the broadband conduit, (2) broadband content, (3) the broadband operating system and (4) "sticky" applications such as instant messaging. The potential for technological discrimination by AOL/Time Warner was raised most recently in a May 10, 2000 letter to the FCC and FTC from Senators Mike DeWine and Herb Kohl, the Chairman and Ranking Member of the Senate Subcommittee on Antitrust, Business Rights and Competition.[22] The DeWine/Kohl letter alerted the FCC and FTC to the serious harms that could occur from discriminatory use of routing and caching technology, affecting consumer choice, diversity of expression and competition in the marketplace of ideas. In addition, the DeWine/Kohl letter discussed a Cisco Systems White Paper that provides a very troubling roadmap for cable operators seeking to use devises to "promote and offer [their] own or partner's services with full-speed features to encourage adoption of [their] services, while increasing network efficiency."[23] As Senators DeWine and Kohl noted, "Using this technology, it appears that it would be possible, for example, for the combined AOL/Time Warner to slow down traffic to the ESPN web site while speeding it up to its own competing CNN/Sports Illustrated site."[24] In the interest of preserving consumer choice and competition, the Commission simply cannot run the risk of any one company securing a position as the dominant keeper of the broadband pipe, the guard at the broadband gate, the master of broadband's content and interactive services,

---

22 *See* Letter to FTC Chairman Pitofsky and FCC Chairman Kennard from Senator DeWine and Senator Kohl, May 10, 2000, attached as Exhibit A hereto.

23 *Id.* discussing Cisco Systems White Paper Entitled "Controlling Your Network – A Must for Cable Operators."

24 *Id.*

and a principal beneficiary of broadband's economic proceeds.

A. Interactive Television Offers Great Promise As a Feature of the New Broadband Services Market.

Interactive television services are already being made available to consumers today. For example, a viewer can log onto abc.com and play along with the contestants on "Who Wants To Be A Millionaire". The set-up for this "interactivity" is primitive, however, because it requires operating separately a PC and a TV in tandem. The emerging popularity of even these early services provides clear evidence that interactive services are likely to become a leading contributor to the emerging digital economy. The demand for interactive television is certain to grow exponentially when two way interactivity can be readily available with a click of the remote control or the mouse on one appliance, either the television or a PC.[25] The advent of instantaneous, two-way interactivity over one broadband pipe running into a digital television receiver or cable set top box will change fundamentally the viewing experience from a passive one to an active pursuit.

B. Interactive Television Services Will Be A Catalyst for Expanding E-Commerce in the Digital Economy.

Interactive television services also will augment the ability of businesses to reach consumers directly. Instead of today's business practice of running advertisements on the programming of television broadcasts with the hope that the ad will help influence the consumer to purchase products in the future at a "bricks and mortar" establishment, companies will seize the opportunity to use interactive television features to secure purchases of products immediately with the simple click of a mouse or remote control. Moreover, the interactivity accompanying broadband advertising also has the potential to change the fundamentals of television advertising.

[25] For example, the convergence of video and other broadband services will enable consumers to watch shows like "Monday Night Football," while at the same time clicking to see the statistics of the quarterback, or to order a football jersey or a pizza.

Broadband capability will enable advertisers to engage in a digital dialog with viewers, progressively narrowing the scope of the ad pitch and customizing it to a consumer's preferences. The value of high quality, interactive television advertising has the potential to dwarf ad values in today's analog television market. The potential efficiencies of this market will revolutionize the way products are advertised and sold to consumers, providing new opportunities for the owners of television programming like TWDC. It will enhance the explosion of e-commerce by further reducing barriers to the free flow of commerce and products in our economy.

C. Without Strong and Meaningful Nondiscrimination Obligations, Competition in the Emerging Digital Market Will Be Jeopardized by the Enormous Potential for Technological Discrimination.

History has shown that the combination of control over content and distribution in an entity inevitably deters competition and lessens consumer choice. The proposed merged AOL/Time Warner would result in so great a degree of integration of broadband infrastructure and content that those concerns are both present and compelling. If there is a difference, it is only that the potential means of discrimination to favor affiliated content are both more subtle and more profuse. For example, this discriminatory effect could be achieved through higher bit rates and superior customer performance for AOL/Time Warner channels, programs and services, and slower bit rates and inferior customer performance for channels, programs and services offered by unaffiliated providers. Analogizing to today's technology, this would be akin to a cable system providing viewers its affiliated programming in color, but offering unaffiliated programming in black and white only. There is also the likelihood that subscribers will be steered away from the sites, programs, and services of unaffiliated providers, and toward AOL/Time Warner's proprietary interactive television and broadband service offerings. While the potential technological means of controlling consumer choice are vast (and at this point not entirely knowable) there is one simple principle, with strong historical precedent, that can best protect against that outcome, and that is the principle of non-discrimination. The Commission should invoke that principle and condition any approval of a AOL/Time Warner merger on conditions that would preclude the inevitable, the favoring of affiliated content and interactive services over unaffiliated content and interactive television services, especially with regard to down-stream and return path traffic, caching, navigation devices and menus, screen placement, and set-top boxes.

1. Unaffiliated Content Owners And Interactive TV Service Providers Must Have Equal Channel Functionality.

High-speed data transmission and return path rates are critical to the development of interactive television services. To ensure that consumers have the opportunity to choose from among competing content sources, the Commission must remove any chance that the down-stream or return path traffic headed to and from interactive sites owned by unaffiliated providers will be inferior to the traffic speed of affiliated interactive services. Technological differences in down stream and return path traffic could effectively limit consumer choice. Technological discrimination also could tilt the playing field for securing advertising dollars. Corporations interested in placing advertising on electronic media likely will be drawn to sites with superior functionality, and therefore, better access to consumers who are the ad targets. If unaffiliated interactive channels and sites on the AOL/Time Warner broadband cable system are not given assurances of equal technological treatment, they may end up with far less advertising revenue than they would be able to secure in a competitive market.

The implications for such potential technological discrimination on the flow of diverse sources of news and information protected by the First Amendment are even more troubling. Time Warner has a clear incentive in promoting CNN as a source for news. What is to prevent

AOL/Time Warner from using the opportunity of the dominant conduit they control to prevent viewer access to competing news and information source? And even if such access is permitted, there will be no guarantee that AOL/Time Warner will allow these unaffiliated new sources to work properly or at the same speeds as sources affiliated with AOL/Time Warner.

One potentially potent example of use of a discriminatory technological technique to hold up the delivery of information to consumers from rival content owners involves caching, the storage of information and content on local servers which could be located at the headend of the local cable system. Local caching could be used to facilitate the rapid delivery of preferred content, while consumers seeking access to "non-preferred" information and content, such as that offered by an unaffiliated content provider, would be forced to access the more congested public Internet in order to retrieve unaffiliated content, resulting in slower downloading times. Caching's impact on broadband and full motion video services will be even more dramatic, providing the means to differentiate in performance and quality between affiliated and unaffiliated content and services. Caching discrimination could materially restrain competition by enabling AOL/Time Warner to tilt dramatically the broadband playing field in favor of its affiliated products and services.

Caching discrimination also has fundamental implications for access to diverse sources of news and information so critical to the First Amendment rights of viewers. AOL/Time Warner, with sizable interests in news media, might be tempted to use caching discrimination as a tool to "out-scoop" its competition. The first rule of news is that it has to be "new." If AOL/Time Warner were to store its affiliated news locally, while competitive news sources like ABC News are forced to take the long way home through the public Internet, the right of citizens to receive timely and complete information could be seriously compromised. Unfettered and immediate access to multiple sources of news ensures the accuracy and integrity of information. The Commission has a special duty to ensure that the American public's current access to a diversity of news sources is not reduced.

2. There Is A Potential That Screen Bias Will Be Used To Secure A Competitive Advantage.

In the converged world of the Internet and television, and as programming options increase, the first screen viewers see will greatly influence what content they access. As the administrator of the broadband cable system, AOL/Time Warner will be in charge of arranging screen displays for viewers. The principle of non-discrimination is needed as protection against the use of the critical first screen to steer viewers to affiliated content and services, and away from unaffiliated displays. For example, a first screen on an electronic program guide offered on an AOL/Time Warner cable system might consist exclusively of AOL/Time Warner owned programming. In that situation, the viewer would have to scroll to successive screens to access unaffiliated programming. The potential for screen bias to be used as a tool of discrimination in the emerging broadband world is real and should be addressed by the Commission through a condition of non-discrimination. The paradigm for such a safeguard is found in Section 653(b) of the Communications Act.

3. Set-Top Boxes May Be Used to Favor Affiliated Content and Services.

The availability – and growing convergence – of digitally-delivered video programming, interactive data and other broadband services elevates exponentially the importance of set-top boxes ("STBs") with respect to consumer access to digital content. It is critical that these devices not become tools for anticompetitive abuse. New digital STBs have only a single path in and out – the cable – giving the cable operator complete control over consumer choice. And the new Microsoft television operating system features news headlines on the first screen from a news provider selected by the cable operator – a selection that cannot be changed by the consumer.

For consumers, the STB already is becoming an unavoidable addition to the home electronics landscape, particularly if they wish to receive digital cable services or other advanced interactive services, such as Internet access. Much like an Internet home page, the STB's "first screen," as received by the subscriber, serves as the all-critical point of entry for accessing these services and the content they carry. The potential for misusing set-top boxes to create competitive advantage should give the Commission great pause.

V. THE COMMISSION MUST ENSURE COMPETITION, PRESERVE CONSUMER CHOICE AND PROTECT DIVERSITY OF VOICES BY REQUIRING NON-DISCRIMINATORY TREATMENT OF UNAFFILIATED CONTENT AND INTERACTIVE SERVICE PROVIDERS AS A CONDITION TO ANY POSSIBLE APPROVAL OF THE MERGER.

None of the commenters has focused on the overarching imperative of the need for a policy of non-discrimination. However, the New York Times editorial spoke to the risk at hand:

> "The fundamental problem for the F.C.C. is that cable companies like AT&T and Time Warner own not only the cable wire that runs into everyone's home, but also some of the programs delivered over that wire. That puts them in position to discriminate in favor of the information and commercial opportunities presented to cable subscribers. Monopoly is bad enough in the orange juice or suspenders markets. It is downright dangerous when it compromises the public's right to diversified sources of news and entertainment.
>
> ************************
>
> [F]ederal regulators, as they study the merger, should be guided by the same principle in regard to Internet access and digital television services: non-discrimination."[26]

The New York Times had it right. There are myriad ways in which the owner of the broadband pipeline could discriminate against unaffiliated content providers. The technological

[26] *Time Warner's Power Play*, The New York Times at A-25 (May 5, 2000), attached hereto as Exhibit B.

suppleness of the broadband platform and its component parts, such as routers, and consumer interfaces, such as set-top boxes, afford numerous and multifaceted means to disadvantage independent content suppliers.[27] These include, but are not limited to: (1) outright denial of access to the broadband platform; (2) discriminatory pricing tantamount to a denial of access; (3) screen bias on electronic program guides rendering consumer access to unaffiliated content difficult; (4) steering of subscribers to affiliated interactive advertising sites and portals; and (5) technological discrimination on downstream or return paths or through local caching.

A. AOL/Time Warner Must Adhere to Enforceable Conditions of Non-Discrimination.

The Commission should impose a broad, all-encompassing condition that removes any chance the merged entity AOL/Time Warner will discriminate in any manner against unaffiliated content or interactive service providers in the broadband services market. In addition to a "catch-all" prohibition against discrimination, the Commission should impose a series of specific, but not exhaustive, prohibitions of specific practices which clearly would have a discriminatory effect on unaffiliated content providers. These would include, but are not limited to, a prohibition against:

- refusals to deal;
- discrimination in prices, terms or conditions of carriage;
- discriminatory presentation of information or displays on navigational devices or electronic program guides for purposes of enabling subscribers to select program or content offerings;
- discrimination with respect to downstream traffic;
- discrimination on the return path for interactive television services;
- discrimination that undermines interactive advertising opportunities;
- discrimination in set-top box design and architecture that fills up memory with affiliated content before loading unaffiliated content; and
- discrimination in caching practices.

[27] *See* DeWine/Kohl letter discussing Cisco System's White Paper.

There is ample precedent for the Commission to craft prohibitions against discriminatory treatment of unaffiliated content providers. The catch-all prohibition should be patterned after Section 628(b) of the Communications Act. The specific prohibitions against refusals to deal and discrimination in the prices, terms and conditions of carriage should be grounded in Section 616 of the Communications Act. Section 616(a)(3) prevents a multichannel video programming distributor from engaging in discrimination on the basis of selection, terms, or conditions for carriage of video programming, the effect of which is to unreasonably restrain the ability of an unaffiliated video programming vendor to compete fairly. This provision reflected Congress' conclusion that vertically integrated cable operators have the incentive and ability to favor affiliated programming vendors over unaffiliated programming vendors with respect to granting carriage on their system.[28] The main purpose of Section 616 was to increase competition, reduce the undue market power held by cable operators, and protect unaffiliated video programmers and consumers from anticompetitive practices. These concerns apply with even greater force to the converged broadband services market where the ability of the broadband pipe owner to discriminate against unaffiliated content providers has grown exponentially with advances in technology. Even AOL acknowledges this fact. AOL Senior Vice President, Global and Strategic Policy, George Vradenburg stated:

> As we move to the broadband world, real and substantial threats are emerging to the competitive Internet access market that necessitate strong, immediate and unequivocal Congressional action to preserve competition and openness in the Internet marketplace across all facilities.[29]

---

[28] House Committee on Energy and Commerce, H.R. Rep. No. 102-628, 102d Cong., 2d Sess. at 41-45 (1992) ("House Report"); Senate Committee on Commerce, Science and Transportation, S. Rep. No. 102-92, 102d Cong., 1st Sess. at 24 (1991) ("Senate Report"); *See also* House Committee on Energy and Commerce, H.R. Rep. No. 102-862, 102d Cong., 2d Sess. (1992), reprinted in Cong. Rec. H8308 (Sept. 14, 1992) ("Conference Report").

[29] *Hearing on H.R. 1686, "The Internet Freedom Act"* and *H.R. 1685 "The Internet Growth and Development Act of 1999"* Before the House Judiciary Committee, 106th Cong. 1st Sess. (1999).

The third specific prohibition, barring discrimination in the presentation of material to viewers on electronic program guides, menus and navigation devices regarding affiliated and unaffiliated programming or content, finds support in Section 653(b) of the Communications Act.[30] Congress was deeply concerned about the potential for open video systems ("OVS") operators to use their control over consumer access to programming to discriminate in favor of programming provided by vendors affiliated with the OVS operator. To address this fear, Congress prohibited OVS operators from discriminating against unaffiliated entities "with regard to material or information (including advertising) provided by the operator to subscribers for the purpose of selecting programming."[31] The policy concerns underlying Section 653(b) apply with even greater force to this merger because a combined AOL/Time Warner would have unprecedented control over the distribution of and access to programming and content in the broadband services market.

The remaining proposed conditions flow logically from the principles embodied in Sections 616, 628 and 653. It is necessary to impose these specific conditions at this time because the anticompetitive practices to be banned are eminently foreseeable. It is far better to prevent the harm to competition from occurring by imposing conditions now than it is to wait for these practices to occur and then attempt to rectify the injury through case by case adjudications.

B. AOL/Time Warner Must Pass Through All the Bits of Broadcasters.

In recognition of the importance of broadcasters to be able to distribute their programming to as wide a viewing audience as possible (especially in light of the cable industry's "undue market power,"[32]), Congress required cable operators to carry "in its entirety

---

[30] *See* 47 U.S.C. §573.

[31] 47 U.S.C. §573(b)(1)(E).

[32] *See* Conference Rep. No. 862, 102nd Cong., 2nd Sess. 3 Section 2(a)(2) (1992).

… program-related material." Congress acknowledged that powerful cable operators had every incentive to use their stranglehold over the distribution system as an anticompetitive sword to disfavor competing broadcast programming services and threaten the future viability of free, over-the-air broadcasting.[33]

The convergence of the Internet with television, as well as the advent of new exciting interactive services that will enhance the viewer's experience in watching the underlying television program, make the need for this "pass-through" requirement even more compelling. Advances in technology will provide cable operators new means by which to disfavor broadcasters' content to the benefit of their own by refusing to pass through unaltered these new, exciting enhancements that will increasingly come to define the medium. Specifically, a condition must be imposed that requires AOL/Time Warner to pass through unaltered all the free bits of broadcasters because more program services will compete for audience share on the basis of this new, exciting content contained in the bits. In other words, any information or material contained in the broadcast signal that the viewer would have received for free through the use of an antenna must also be delivered over the cable broadband pipeline unaltered to the consumer. The Commission must ensure competition by preventing anyone from blocking consumer access to free programming enhancements provided by unaffiliated content providers.

VI. CONCLUSION

The sheer technological power residing in broadband services platforms greatly augments the potential for harm to competition, consumer choice and diversity of voices which is inherent in the degree of vertical integration present in a merged AOL/Time Warner. Time Warner's broadband pipe and its treasure trove of content and AOL's Internet operating system and services such as instant messaging, joined together with their respective subscriber bases, creates the ability, opportunity and incentive to gain competitive advantage by favoring affiliated content and services. To safeguard against the potential harm to competition and consumer choice which could result from this merger, the Commission must prohibit AOL and Time Warner from discriminating against unaffiliated content and interactive service providers. AOL/Time Warner's acceptance of the fundamental principle of non-discrimination is a prerequisite to a Commission finding that the merger is in the public interest.

Respectfully submitted,

Lawrence R. Sidman

Lawrence R. Sidman, Esquire
Lawrence Duncan, III, Esquire
Jessica A. Wallace, Esquire
VERNER, LIIPFERT, BERNHARD, McPHERSON & HAND, CHARTERED
901 15th Street, N.W., Suite 700
Washington, D.C. 20005
(202) 371-6206

Counsel for The Walt Disney Company

Dated: May 11, 2000

[33] *See* Conference Rep. No. 862, 102nd Cong., 2nd Sess. 3 Section 2(a)(16) (1992).

I hereby certify that on this 11th day of May, 2000, I caused copies of the foregoing Reply Comments of The Walt Disney Company In the Matter of Applications of America Online, Inc. and Time Warner, Inc. for Transfers of Control to be delivered by U.S. First Class Mail, postage prepaid, to the following:

George Vradenburg, III
Jill A. Lesser
Steven N. Teplitz
America Online, Inc.
1101 Connecticut Avenue, NW
Suite 400
Washington, DC 20036

Richard E. Wiley
Peter D. Ross
Wayne D. Johnsen
Wiley, Rein & Fielding
1776 K Street, NW
Washington, DC 20006

Timothy A. Boggs
Catherine R. Nolan
Time Warner, Inc.
800 Connecticut Avenue, NW
Suite 800
Washington, DC 20006

Aaron I. Fleischman
Arthur H. Harding
Craig A. Gilley
Fleischman and Walsh, L.L.P.
1400 Sixteenth Street, N.W., Suite 600
Washington, DC 20036

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, S.W.
TW B204
Washington, DC 20554

James Bird
Office of General Counsel
Federal Communications Commission
445 12th Street, S.W.
8-C818
Washington, DC 20554

Royce Dickens
Cable Services Bureau
Federal Communications Commission
445 12th Street, S.W.
3-A729
Washington, DC 20554

Marilyn Simon
International Bureau
Federal Communications Commission
445 12th Street, S.W.
6A-633
Washington, DC 20554

International Transcription Service, Inc.
1231 20th Street, N.W.
Washington, DC 20036

To-Quyen Truong
Associate Chief
Cable Service Bureau
Federal Communications Commission
445 12th Street, S.W.
3-C488
Washington, DC 20554

Matthew Vitale
International Bureau
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Monica Desai
Wireless Telecommunications Bureau
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Laura Gallo
Mass Media Bureau
Federal Communications Commission
445 12th Street, S.W.
2-A640
Washington, DC 20554

Linda Senecal
Cable Services Bureau
Federal Communications Commission
445 12th Street, S.W.
3-A734
Washington, DC 20554

Stephen A. Weiswasser, Esq.
Executive Vice President and General Counsel
Gemstar International Group, Ltd.
135 North Los Robles Avenue
Suite 870
Pasadena, CA 91101
Of Counsel to Gemstar International Group, Ltd.
and Gemstar Development Corp.

Jonathan D. Blake
Amy L. Levine
Covington & Burling
1201 Pennsylvania Avenue, N.W.
Washington, DC 20004
Attorneys for Gemstar International Group, Ltd.
and Gemstar Development Corp.

J. Maxwell Williams
General Counsel
Memphis Light, Gas and Water
220 S. Main Street
P.O. Box 430
Memphis, TN 38103

Cynthia Mahowald
SBC Communications, Inc.
1401 I Street, N.W.
Suite 1100
Washington, DC 20005

James D. Ellis
Paul K. Mancini
Patrick J. Pascarella
SBC Communications Inc.
175 East Houston Street
San Antonio, Texas 78205

William L. Fishman
Counsel for RCN Telecom Services, Inc.
Swidler, Berlin, Shereff, Friedman, LLP
3000 K Street, N.W., Suite 300
Washington, DC 20007-5116

Stephen C. Garavito
General Attorney
AT&T
295 North Maple Avenue
Room 1131M1
Basking Ridge, NJ 07920

Susan M. Eid
Vice President, Federal Relations
MediaOne Group, Inc.
1919 Pennsylvania Avenue, N.W., Suite 610
Washington, DC 20006

Tara C. Woods
62 Myrtle Street, #2
Somerville, MA 02145

Christopher C. Cinnamon
Rhondalyn D. Primes
Bienstock & Clark
150 South Wacker Drive
Suite 720
Chicago, Illinois 60606
Attorneys for American Cable Association

Harold Feld
Andrew Jay Schwartzman
Cheryl A. Leanza
Media Access Project
950 18th Street, NW
Suite 220
Washington, DC 20006

Jonathan E. Canis
Michael B. Hazzard
Kelley Drye & Warren LLP
1200 Nineteenth Street, NW, Fifth Floor
Washington, DC 20036
Council to Memphis Networx, LLC

Margaret Heffernan
President and CEO
iCAST Corporation
78 Dragon Court
Woburn, MA 01801

William L. Fishman
Swidler, Berlin Shereff Friedman, LLP
3000 K Street, NW, Suite 300
Washington, DC 20007
Counsel for RCN Telecom Services, Inc.

Ross Bagully
President and C.E.O.
Tribal Voice
600 17th Street, Suite 700 South
Denver, Colorado 80202

Meade Emory
University of Washington School of Law
1100 NE Campus Parkway
Seattle, Washington 98105-6617

Respectfully submitted,

Richard Ling

Richard E. Ling

VLDC01-381987.1

EXHIBIT A

United States Senate

COMMITTEE ON THE JUDICIARY

WASHINGTON, DC 20510-6275

May 10, 2000

The Honorable Robert Pitofsky
Chairman, Federal Trade Commission
600 Pennsylvania Avenue, NW, #444
Washington, D.C. 20580

The Honorable William Kennard
Chairman, Federal Communications Commission
445 - 12th Street, SW
Room 8B 201
Washington, D.C. 20554

Dear Chairman Pitofsky and Chairman Kennard:

As Chairman and Ranking Member of the Antitrust Subcommittee, with a mandate to promote competition, we are writing to bring to your attention a matter we have recently been discussing with both America Online and Time Warner. It involves "routing" and "caching" technology that Internet service providers ("ISPs") can use to enable faster and more updated access to some web sites than others. This technology has pro-competitive benefits, to be sure, but also can be employed to unfairly discriminate against the "content" of rivals and, as a matter of principle, we believe an ISP should not give preferential treatment to content owned by its affiliates solely on the basis of such a relationship. Because the possible misuse of this technology has potentially disturbing implications for Internet and media – and, most importantly, for consumers – we urge you to examine this matter, not only in the context of the AOL/Time Warner merger but also as it affects the industry as a whole.

In evaluating AOL/Time Warner and, indeed, Internet and media competition generally, one of our primary concerns has been ensuring that content is delivered on a non-discriminatory basis in order to promote the greatest possible diversity of expression and competition in the marketplace of ideas. In this context, we understand that Cisco Systems makes "routers" that allow cable broadband providers to control access speeds to Internet sites. While we recognize that there are clearly valid uses for this technology – such as ensuring quick access to popular web sites and not dedicating too much broadband capacity to sites that are rarely used – it also raises some concerns because it permits ISPs to give preferential treatment to sites with which the ISP is affiliated. Indeed, a Cisco Systems "White Paper" entitled "Controlling Your Network – A Must for Cable Operators" notes that by using its devices cable operators "could promote and offer your own or partner's services with full-speed features to encourage adoption of your services, while increasing network efficiency." Using this technology it appears that it would be possible, for example, for the combined AOL/Time Warner to slow down traffic to the ESPN web site while speeding it up to its own competing CNN/Sports Illustrated site or for the MSN ISP to slow down traffic to the Fox News site while speeding up traffic to its own affiliated MSNBC site.

Such behavior would be especially troubling because, as with the subliminal advertising which the FTC has in the past prohibited on television broadcasts, consumers would likely change their behavior without actually being aware that access to various web sites was being affected in this manner. Similar issues of discrimination arise with respect to the use of "caching" techniques to enable quicker access to affiliated web sites. Appropriate use of this technology can be of great benefit to companies and consumers; the inappropriate use of these technologies, however, raises questions that might be addressed under the FTC's authority to prevent "unfair methods of competition," 15 U.S.C. § 45(a)(1), or the FCC's "public interest" standard.

On March 6, 2000, we wrote to both AOL and Time Warner expressing our concerns in this regard. In response, the CEOs of both companies made important commitments, pledging to "prohibit[] discrimination in the handling of ISP traffic based on affiliation with AOL/Time Warner . . . including all content provided by the ISP regardless of ownership of the content." Moreover, opening up the broadband "pipe" to competition, as AOL and Time Warner have now pledged to do in their Memorandum of Understanding, is a step towards ensuring nondiscrimination.

Nevertheless, we are writing to you now, and enclosing our correspondence, to ensure that you are aware of this important issue. We believe that you should consider it both in your examination of the competitive effects of the AOL/Time Warner merger and, more importantly, in a broader context as well. With respect to the latter, we believe your agencies should consider investigating the uses to which ISPs are employing routing and caching technology and whether further action is necessary to prevent ISPs from using this technology to discriminate with respect to content based relationships with the content provider. This issue may arise with traditional narrowband ISPs as well as in the broadband context. While we are firmly opposed to increased regulation of this developing industry, we also urge your agencies to carefully examine the uses to which this technology can be applied and its consequences for competition and consumers.

Thank you for your attention to this matter. We have enclosed a copy of the correspondence with AOL and Time Warner discussed above, as well as a document from Cisco Systems describing the technology at issue.

Sincerely,

Mike DeWine

MIKE DeWINE
Chairman, Subcommittee on
Antitrust, Business Rights, and
Competition

Herb Kohl

HERB KOHL
Ranking Member, Subcommittee on
Antitrust, Business Rights, and
Competition

Enclosures

EXHIBIT B

THE NEW YORK TIMES NEW YORK FRIDAY, MAY 5, 2000

Time Warner's Power Play

Time Warner lost more than a skirmish over money with ABC this week when it backed down from kicking the network's programs off its cable service. Its blunt use of monopoly power was an instant public-relations disaster, and in the long run could enter the annals of business history as a famous strategic blunder. For by overriding the information and entertainment needs of millions of customers, Time Warner virtually compelled federal regulators to take a more searching look at Time Warner's proposed merger with AOL.

After all, if Time Warner behaves this way now in response to Disney, the parent of ABC and a media giant itself, how will it behave after it joins forces with AOL? More to the point, will the merged company use its control of cable television's vital electronic pipeline to favor its own programs and deny competing programs fair access to millions of consumers along that pipeline?

Now that federal authorities have been forewarned about Time Warner's muscular, proprietary attitude, they cannot consider approval of the Time Warner-AOL merger a foregone conclusion. If it is approved, the Federal Communications Commission or Federal Trade Commission should impose stiff conditions that would make it impossible for Time Warner to behave in the future as the company behaved this week.

It must be remembered that the F.C.C. has a mandate to protect the public interest in the communications and information industries. Its responsibilities go beyond the narrow questions of anti-competitive business practices examined by the antitrust authorities in the Justice Department or, in this case, the Federal Trade Commission. The F.C.C. must protect the broader public interest in the free flow of information and in open access to electronic commerce.

The fundamental problem for the F.C.C. is that cable companies like AT&T and Time Warner own not only the cable wire that runs into everyone's home, but also some of the programs that are delivered over that wire. That puts them in position to discriminate in favor of the program channels they own, and therefore to filter the information and commercial opportunities presented to cable subscribers. Monopoly is bad enough in the orange juice or suspenders markets. It is downright dangerous when it compromises the public's right to diversified sources of news and entertainment.

What divides Disney and Time Warner is not so much the current financial arrangement as it is the emerging issue of parity of services and future income opportunities along the information highway. Soon cable systems will offer a panoply of digital services — giving viewers the option, for example, of purchasing a biography from a local bookstore about a historical figure in the movie they are watching.

Disney fears that Time Warner will provide better services for its own channels, like HBO or CNN, than it will for Disney's channels. To protect itself, Disney wants federal regulators to require parity, or non-discrimination. Time Warner would be required to provide equivalent services to all channels. Time Warner rejects the idea, asserting that the principle of non-discrimination sounds nice but cannot be defined or regulated before the digital services exist. Besides, it says, the services will be profitable and thus should be a matter of private negotiation, not rule-making from Washington.

Time Warner has a right to make this turf-guarding argument, but the F.C.C. cannot be paralyzed by it. This battle is not just over cable broadcasts of quiz shows. Cable operators like Time-Warner already provide high-speed access to the Internet. But cable customers can use only the Internet services chosen by the cable company. This has to be an open environment, where customers have as full a choice among Internet companies as technology allows. While this page supported the Federal Communications Commission's decision last year to wait before regulating access to the Internet, this week's events remind us of the pace of change and the need for ongoing vigilance. There is now ample reason for the F.C.C. to act.

The point is not that we are siding with Disney, but that federal regulators, as they study the merger, should be guided by the same principle in regard to Internet access and digital television services: non-discrimination. Time Warner says there is no need for federal regulations because it does not in fact discriminate against programs it does not own and has promised to provide open access to the Internet. But the public need not rely on voluntary compliance.

Federal regulators balked last year because they did not know how to enforce non-discrimination. But that need not bring oversight to a halt. They can declare the principle of non-discrimination without issuing a bevy of rules. The mere announcement puts cable companies on notice that, as soon as technology allows, they will be required to treat all Internet companies and cable programmers the same. If they decide to design their systems otherwise, they will be held accountable.

Such a policy would probably serve the long-term financial interests of this newspaper and many other media companies. But the decision, in the end, must be shaped by the public interest. Democracy requires an open communication environment. Monopoly control over cable access threatens the flow of ideas and opinion that feeds the democratic process, not to mention the emerging electronic economy. For now, perhaps, only the principle of non-discrimination can be declared, with the rule book to be written as conditions require. But the Time Warner-ABC conflict proves that it is time to start declaring principles and working on instituting them.