

APPENDIX 1

APPENDIX 1

List of Petitions and Comments Filed in MB Docket No. 02-70 and Cited in Reply to Comments and Petitions to Deny Applications for Consent to Transfer Control

Petitions and Comments	Date Filed	Shortened Citation
Comments of the American Cable Association	04/29/02	ACA Comments
Comments of BellSouth Corporation, BellSouth Entertainment, L.L.C., BellSouth Interactive Media Services, L.L.C., BellSouth Telecommunications, Inc., and BellSouth Wireless Cable, Inc.	04/29/02	BellSouth Comments
Opposition to AT&T Broadband/Comcast Merger of the BEN Asset Group and the Black Education Network, Inc.	04/29/02	BEN Comments
Petition of Blawnox, Pennsylvania to Deny or Dismiss Applications	04/30/02	Blawnox Comments
Comments of Braintree Electric Light Department and BELD Broadband	04/26/02	BELD Comments
Petition to Deny of Lisa Burton, Carmen (Robinson) Gonzalez, Betty Maina, Tracey Massay, Osmisa Peacock, Kizzie Sanders, Anthony Scott, Deborah Maria Shepherd, Maria Smith, Gloria Marie Mitchell Taylor, Zelda Tepper and Patrick Young (filed by Law Office of Dennis J. Kelly)	04/29/02	Kelly Comments
Comments of CapNet in Support of Proposed Merger	04/29/02	CapNet Comments
Petition to Deny of Arizona Consumers Council, Association of Independent Video and Filmmakers, CALPIRG, Center for Digital Democracy, Center for Public Representation, Chicago Consumer Coalition, Civil Rights Forum on Communications Policy, Citizen Action of Illinois, Consumer Action, Consumer Assistance Council, Inc., Consumer Federation of America, Consumer Fraud Watch, Consumers United/Minnesotans for Safe Food, Consumers Union, The Consumers' Voice, Democratic Processes Center, Empire State Consumer Association, Florida Consumer Action Network, IL (Illinois) PIRG, Massachusetts	04/30/02 (Corrected Version Filed as Erratum)	CFA Comments

Consumers Coalition, MASSPIRG, Media Access Project, Mercer County Community Action, MontPIRG, National Alliance for Media Arts and Culture, New York Citizens Utility Board, NC PIRG, North Carolina Justice and Community Development Center, OS PIRG (Oregon State), Oregon Citizens Utility Board, Texas Consumer Association, Texas Watch, United Church of Christ, Office of Communication, Inc., US PIRG, Virginia Citizens Consumer Council, WashPIRG, Wisconsin Consumers League		
Comments of Communications Workers of America	04/29/02	CWA Comments
Comments of EchoStar Satellite Corporation	04/29/02	EchoStar Comments
Comments of Everest Midwest Licensee, L.L.C. dba Everest Connections	04/29/02	Everest Comments
Brief Comment of Charles McCollum	04/24/02	McCollum Comments
Petition to Deny of Minority Television Project Inc., Licensee of KMTP (TV)	04/29/02	MTP Comments
Comments of the Progress & Freedom Foundation	04/29/02	PFF Comments
Comments of Qwest Communications International Inc.	04/29/02	Qwest Comments
Petition of RCN Telecom Services, Inc., to Deny Applications or Condition Consent	04/29/02	RCN Comments
Comments of SBC Communications Inc.	04/29/02	SBC Comments
Petition to Deny of Verizon Telephone Companies and Verizon Internet Solutions d/b/a Verizon.net	04/29/02	Verizon Comments

APPENDIX 2

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)	
)	
Applications for Consent to the Transfer of Control of Licenses)	MB Docket No. 02-70
)	
From COMCAST CORPORATION and AT&T CORP. ,)	
)	
Transferors,)	
)	
To AT&T COMCAST CORPORATION ,)	
)	
Transferee.)	

DECLARATION OF GREGORY BRADEN

I. QUALIFICATIONS AND PURPOSE OF TESTIMONY.

1. My name is Gregory Braden. I am the Executive Vice President For Strategy And Business Development for AT&T Broadband LLC (“AT&T Broadband”). My responsibilities include strategy development and implementation, with a particular focus on voice and data services, corporate investments and transactions for AT&T Broadband, and operating oversight of AT&T Broadband’s Digital Media Center and Headend In The Sky® (“HITS”) business.

2. The purpose of my testimony is to respond to commenters’ claims that the merged entity (“AT&T Comcast”) will not have the ability or the incentive to develop and deploy cable telephony services in Comcast Corporation (“Comcast”) territories. As I demonstrate below, those claims are specious. In fact, the combination of the complementary cable telephony assets

and expertise of AT&T Broadband and Comcast will provide the combined entity with the necessary resources and financial incentives to move ahead with its announced plans to deploy cable telephone services in the Comcast territories and elsewhere.

3. I also address the claims advanced by some commenters that AT&T Comcast will be able to use its ownership of HITS to deter cable overbuilding in the former Comcast footprint. HITS aggregates and transmits digital programming to cable headends using non-proprietary, off-the-shelf equipment and processes. As I detail below, there are other cost effective ways to obtain digital programming, as is confirmed by the fact that cable systems serving more than half of all cable digital subscribers do not purchase HITS service. Moreover, overbuilders can and do purchase the HITS service in both AT&T Broadband and Comcast service areas.

II. THE MERGER WILL PROMOTE EXPANDED DEPLOYMENT OF CABLE TELEPHONE SERVICE.

4. The Public Interest Statement details a number of ways in which the complementary assets and experience of AT&T Broadband and Comcast will put the merged entity on a stronger footing and help increase the pace and effectiveness of local telephone competition in Comcast service areas. *See* Application at 35-42. No commenter provided any evidence to contradict those facts. As the chief operational officer of AT&T's cable telephony business, I can personally attest that AT&T's cable telephony expertise and assets are real and substantial, and unquestionably improve the economics of, and allow the expanded deployment of, cable telephony in the Comcast service areas.

5. I take great issue with Qwest's claim that AT&T has not lived up to cable telephony expectations following the TCI and MediaOne merger proceedings. *See* Qwest Comments at 24. In 1998, when AT&T announced its merger with TCI, cable telephony was

essentially non-existent. Today, AT&T Broadband has over 1.15 million cable telephony customers (far more than any other cable telephony provider domestically or worldwide), is adding more than another 40,000 customers every month, and is already the 10th largest local telephone company in the country. At the beginning of 1999 (after the TCI merger and just before the FCC granted the MediaOne merger application) AT&T marketed cable telephone services to fewer than 700,000 homes. By the end of 2001, AT&T Broadband had increased deployment tenfold, marketing cable telephone service to about 7 million homes.

6. AT&T Broadband has experienced substantial success in winning potential customers away from the entrenched incumbent local exchange carriers, and is bringing real local telephone choice for many customers. AT&T Broadband's current penetration rate is nearly 15 percent of all customers to which it offers service, and in some areas that penetration rate is as high as 30 percent.¹ AT&T Broadband has succeeded in these efforts despite the well documented and on-going failure of incumbent local exchange carriers, including Qwest and SBC, to fulfill their requirements for cooperative interconnection and nondiscriminatory operations interfaces with facilities-based competitors like AT&T Broadband.

7. AT&T Broadband's cable telephony business is now Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA) positive and its financial performance continues to improve. By any measure, AT&T Broadband's cable telephony efforts have been a great success and continue to see strong growth.

¹ For example, take rates in Ogden, Provo, and Salt Lake City have reached 25 percent or more. Similar success has been realized in a number of communities in the Pittsburgh and Seattle areas.

8. I also strongly disagree with the claims by SBC and Qwest that AT&T Broadband will lose the relevant cable telephony assets and expertise when it is spun off from AT&T Corp. AT&T Broadband, not AT&T Corp., bears the primary responsibility for developing and deploying cable-based telephony services. Accordingly, AT&T Broadband has developed the necessary experience and expertise to deploy efficiently cable telephony services, and the groups in which that experience and expertise reside will be transferred to AT&T Comcast. Moreover, the cable telephony-specific assets will be transferred to AT&T Comcast. These assets include, among others, (1) AT&T Broadband's centralized systems to support the design, installation, maintenance, and operation of complex, two-way hybrid fiber-coaxial systems that support digital voice and data applications that interconnect with various technologies used by incumbent LECs; (2) AT&T Broadband's National Operations team which provides support on a wide range of planning, engineering, technical, and operational issues that are faced when deploying complex cable telephony services; (3) AT&T Broadband's National Service Activation Center, which supports the provisioning of customer telephone lines, including switch and headend equipment, third party provisioning, *i.e.*, directory listing, operator service, local number portability, and E911; and (4) AT&T Broadband's existing back office systems that are specifically designed to support cable telephony, including mechanized billing software and processes which were developed over several years.²

9. There is no question that AT&T Broadband's assets and expertise substantially improve the economics of deploying cable telephony on the Comcast systems. The vast majority

² Before the AT&T/MediaOne merger, MediaOne owned all of the expertise for negotiating and managing interconnection agreements with ILECs, engineering, deploying and managing CLASS 5 switching and interconnection facilities, and management of local, intrastate and interstate traffic, revenues and expenses. This expertise and the attendant capabilities continue to be part of AT&T Broadband.

of these assets and expertise are fully scalable and can be applied to deployment of telephony on Comcast systems. And experience counts for a lot. As a result of the merger, Comcast will not have to incur the substantial costs of learning how to deploy efficiently cable telephony. As one example, when AT&T Broadband first deployed its cable telephone service, average field installation time (one of the largest expenses of provisioning the service) was over 4 hours. Today it is just over 2 hours. Similar operational improvements, with attendant lower unit costs, have occurred in technical provisioning activities, customer care, billing and marketing, and sales. AT&T Broadband's experience will provide Comcast with the immediate benefits of this learning curve.

10. AT&T Broadband's assets and expertise in providing circuit switched cable telephony are equally applicable and scalable to an IP telephony environment. Although the transmission and switching equipment differs in IP telephony, AT&T Broadband's marketing experience, back office assets, operations expertise, and other cable telephony assets are extremely useful in any type of cable telephone environment. In my view, the experience and scale of AT&T Broadband's current telephony operations will improve the incremental economics of cable telephone service deployment in the Comcast territories and is a clear illustration of the benefits of the merger.

11. SBC asserts that the local telephone benefits of the merger can be obtained equally well through a joint venture. *See* SBC Comments at 30. That is not true. There are many reasons why a joint venture is not practical in this case. Most importantly, the size and scope of the goals that are contemplated by the merger are too massive to be achieved through contracts. The merger contemplates, among other things, the development and deployment of additional cable telephone services, the sharing and consolidation of cable telephone resources,

and joint marketing of that service. By merging, the incentives of the combined entity will be aligned. However, if the companies remain separate, they will continue to have competing interests, making massive contractual agreements on the scale contemplated by the merger infeasible.

12. Experience has taught me that there are no easy answers to the question of how to reconcile these concerns. Technology and the marketplace are evolving so rapidly that predicting outcomes even six months into the future is risky. In these circumstances, it should be expected that it will be difficult and time-consuming to hammer out commercial arrangements satisfactory to both parties, particularly given the large initial investments involved. It must also be recognized that the boundaries established for the joint venture in the face of great uncertainty could impose limitations on the flexibility of the joint venture as a competitor that would not be encountered in the context of facilities that are fully owned by a merged entity.

13. The difficulties and challenges outlined above are evidenced by the fact that despite numerous attempts in the past to reach agreement on joint ventures to provide cable telephone service, only one such agreement has been reached (between AT&T and Insight Communications).

III. AT&T COMCAST OWNERSHIP OF HITS WILL NOT HARM CABLE OVERBUILDERS.

14. HITS is a wholly owned subsidiary of AT&T Broadband that aggregates and transmits digital video programming owned by others (*e.g.*, Disney, Discovery and Viacom) to multi-channel video programming distributors (“MVPDs”), which then transmit some or all of that content to their own subscribers. To provide this service, HITS obtains the rights from programming networks to compress, multi-plex and uplink their content to HITS’ leased satellite

transponders for transmission to the headends of MVPDs, which have separately contracted with the owners of the video programming for the right to transmit the content to subscribers.

15. HITS was developed to serve TCI cable systems that, in the early 1990's, were trying to find a way to accommodate new pay-per-view and basic channels on their systems that had limited analog capacity. By using HITS, these affiliates could expand their programming offerings without adding additional bandwidth capacity because HITS uses a digital format that is capable of transmitting 10-12 programs in the same 6 MHz bandwidth used to transmit a single analog program. Thus, for example, within one 6 MHz channel, the "HITS 1" package delivers several channels including, Discovery Kids, The Science Channel, Discovery Health, The Golf Channel, ESPNNews, Independent Film Channel, Game Show, Playboy, Fox Sports World, BBC America, Turner Classic Movies, and Noggin. HITS currently leases 15 transponders, 14 of which are currently transmitting programming.

16. The technology and equipment used by HITS is commercially available and is not proprietary. HITS uses Motorola's DigiCipher II equipment and software to digitally convert analog and other digital formats into a uniform digital format (MPEG-2). The Motorola equipment and software also are used to compress and combine the digitized programs into a single signal that contains up to 12 different programs, *e.g.*, HBO, Discovery Channel, etc. These processes take place in AT&T Broadband facilities located in Denver, Colorado.

17. To transmit the digitized signals to its MVPD customers (or "affiliates"), HITS leases transponder space on satellites. Using that transponder space, HITS transmits the digitized signal to the satellite, which, in turn, sends the digitized signal to HITS affiliates. To receive the HITS signal, an affiliate must have satellite receivers located at the affiliate's

headend. The satellite receivers used by HITS affiliates are general purpose (non-proprietary) satellite receivers that are tuned to receive the signals from the HITS transponder (but could also be tuned to receive signals from other satellite transponders). From the affiliate's headend, the signal is transmitted to end-user subscribers over the affiliate's MVPD network. The digitized signals are descrambled by the end-user's set top box as appropriate. HITS signals can be decoded by any of the commercially available set top boxes provided by the leading suppliers of subscriber equipment.³

18. HITS is only one of many methods that MVPD providers can use to obtain digital programming. Almost every network owner offers a direct transmission service from its own leased satellite transponders. For example, HBO, Showtime and the STARZ! networks have their own multiplexes that, like the HITS multiplexes, are digitized and compressed. Even small programmers today offer such multiplexes by pooling resources. Programmers with extra satellite transponder space sub-lease that space to other programmers that combine their programming to produce their own digital multiplexes (called "pods"). For example, A&E Television Networks has combined unaffiliated programming such as Lifetime Movie Network, IFC, MuchMusic, TechTV, Do It Yourself, and CNBC World with its own programming (Biography and History Channel International) and provides that multiplex via direct feed to any interested MVPD. Similarly, E! Network has added unaffiliated services to its transponder. There also are a growing number of program packagers that use digital techniques similar to that employed by HITS and to which MVPD programmers can subscribe. For example, Olympusat is a new entrant that "is bundling and digitally transmitting 'suites' of growing, independent

³ Exhibit 1 (attached) diagrams and describes how different signals from programmers are digitized and transmitted to end user customers.

programming services.”⁴ Likewise, TVN offers a variety of digital programming packages to MVPDs including cable, DBS, and telephone companies.⁵

19. There are more than 92 million MVPD subscribers in the United States. There are 14.7 million digital cable subscribers and more than 30 million total digital subscribers (including DBS). HITS provides programming to cable systems serving 7.2 million digital subscribers’ homes. Thus, MVPD subscribers served via HITS account for less than 8 percent of all MVPD subscribers, less than a quarter of all digital subscribers, and less than half of all digital cable subscribers.

20. An MVPD’s decision as to how it will obtain digital programming reflects a number of considerations. HITS is a convenient method of obtaining programming from a single source. However, HITS decides which programming it will carry, and can add or delete programming from its line-ups at its discretion. MVPDs that seek more control over their own line-up and to decide what, if any, changes will be made to that line-up may prefer to obtain programming from direct feeds.

21. There also are cost considerations. Direct feeds are free. HITS charges per-subscriber transmission fees, which vary based upon which HITS programming the MVPD chooses. For some HITS customers, the fee can be as high as \$800,000/year/headend. On the other hand, acquiring digital programming through HITS may reduce up-front costs for some MVPDs, depending upon how many direct feeds the MVPD would need to acquire the programming for its chosen line-ups, and the compression ratios used in those direct feeds. The

⁴ See <www.olympusat.com>. Like HITS, Olympusat uses Motorola’s DigiCipher II technology to digitize programming. *See id.*

greater the number of satellite transponders from which an MVPD receives programming, the greater the number of receivers, satellite “dishes,” and other reception equipment will be needed.

22. SBC claims that it recently tried to obtain resold HITS service from a HITS affiliate, WSNNet, in an AT&T Broadband service area, but due to the restrictions in the HITS/WSNNet agreement, WSNNet refused to resell the HITS service to SBC. Based solely on this experience, SBC concludes that AT&T Broadband is denying HITS to overbuilders in AT&T Broadband territory, and that the merged entity is likely to extend those restrictions to Comcast service areas.

23. To understand why SBC is wrong, it is necessary to understand the services provided by WSNNet and the contract between HITS and WSNNet. WSNNet collects content from HITS (and others) and resells that content to independent MVPD distributors that primarily serve multiple dwelling units (“MDUs”), *e.g.*, apartment buildings, multi-unit condominiums, trailer parks, and universities. Unlike most HITS customers, WSNNet does not sell programs directly to end-users. The contract between HITS and WSNNet expressly permits WSNNet to sell HITS content in AT&T Broadband service areas to cable operators that serve MDUs (WSNNet’s core business). Moreover, the HITS/WSNNet agreement – which will not expire until at least June 2006 – expressly allows WSNNet to sell HITS programming to *any* cable overbuilder in any Comcast territory. Thus, contrary to SBC’s claims, the merged entity could not prohibit WSNNet from selling HITS in former Comcast territories.

24. Cable overbuilders (in Comcast territories, in AT&T territories, or anywhere else) can also purchase HITS services under AT&T’s existing contract (which runs through at least

⁵ See <www.tvn.com>.

June 2005) with the National Cable Television Cooperative (“NCTC”).⁶ That contract allows any member of NCTC – which is open to overbuilders, including RCN, WOW and Knology – to obtain the HITS service regardless of the territory served by the NCTC member. In fact, Knology is a NCTC member that currently subscribes to HITS, and provides cable services in AT&T Broadband (and Comcast) service areas.⁷

25. But there is a more general flaw in SBC’s claim that AT&T Comcast could deter overbuilding by denying HITS to overbuilders. MVPDs, including overbuilders, can (and do) succeed without HITS service. As explained above, the HITS service uses no proprietary equipment, software, or techniques, and does not own or control the programming it distributes. Rather, that programming is available directly from its owners (via direct feed) or from any other company that chooses to offer a HITS-like aggregation service. Comcast, for example, does not generally use HITS to obtain digital programming. In addition, Charter Communications recently cancelled its subscription to HITS and leased three custom satellite transponders for the purpose of distributing expanded basic programming to its cable systems. Neither RCN nor WideOpenWest uses HITS even though they could obtain the HITS service through NCTC.

26. Other MVPDs obtain transport directly from program owners and assemble their own programming packages and channel lineups. As noted above, MVPDs that subscribe to

⁶ The National Cable Television Cooperative is an organization of independent cable television companies serving more than 12 million cable TV subscribers throughout the United States. Cooperative members (MVPD providers) work together to purchase programming (including HITS), hardware and services.

⁷ Other overbuilders in AT&T Broadband territories that currently obtain HITS are WinFirst in Sacramento, Alameda Power & Light in Alameda, California, and “CLICK” in Tacoma, Washington.

HITS are unable to customize fully their digital channel line-up, and also are subject to changes in the line-up at the discretion of HITS.

27. According to SBC, HITS is a necessary input for MVPDs because the headend set-up costs associated with a HITS subscription can cost almost \$500,000 less than the cost of some undisclosed alternative. SBC Comments at 13. SBC provides no support or explanation of its figures and, as I explained above, no such generalization can be made because the relative costs will depend upon each MVPD's preferences and circumstances. Most obviously, SBC ignores the direct costs of using HITS through per-subscriber transmission fees. And the relative fixed costs will depend upon the individual MVPD's programming choices. An MVPD that chooses popular digital programming from large, established providers like Disney, AOL/Time Warner, and Viacom, or from independent transmission cooperatives like the A&E group that have existing compressed multiplexed packages, may not incur substantially high fixed costs compared to a HITS subscription. On the other hand, an MVPD that chooses a wider range of programming may need to invest in additional satellite receivers and grooming equipment to obtain that programming directly from programmers and to convert the signals into a format that can be distributed over the MVPD's cable systems.

28. Thus, contrary to SBC's claims, the relative cost to MVPDs of obtaining programming transport from HITS compared to obtaining programming directly from the owners of that programming depends on a number of factors. For some MVPDs, HITS will be a lower cost method of obtaining programming, and for other MVPDs, a direct feed or subscriptions to other HITS-like services will be more cost effective. That is why MVPDs that serve more than half of all digital cable subscribers, including many overbuilders (RCN and WideOpenWest, for

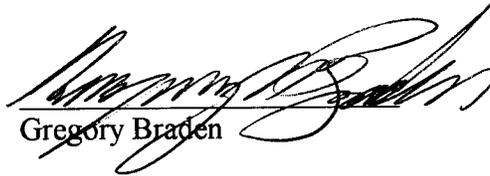
example, are overbuilders that do not use HITS, but provide MVPD service in Comcast and AT&T Broadband territories), do not subscribe to HITS.

IV. USE OF MICROSOFT SOFTWARE IN AT&T BROADBAND SET-TOP BOXES.

29. I understand that several commenters have argued that Microsoft Corporation ("Microsoft") will have undue influence over AT&T Comcast or CableLabs relating to set-top box software. I understand that the reply comments submitted by AT&T Broadband and Comcast fully explain why such a suggestion is incorrect. For its part, AT&T Broadband does not currently use Microsoft software for its set-top boxes, but instead uses the software of other vendors.

VERIFICATION PAGE

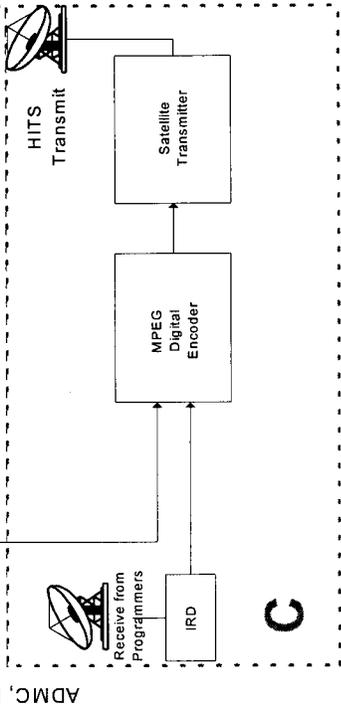
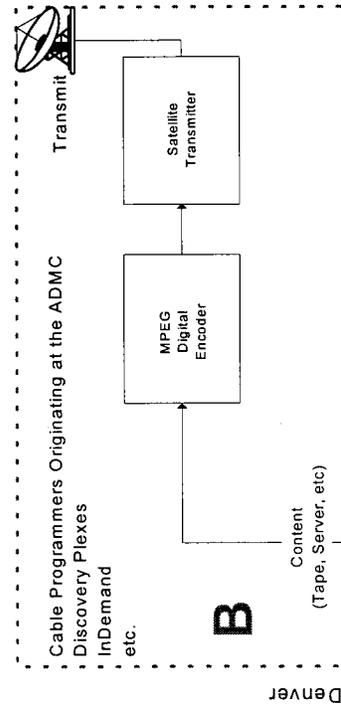
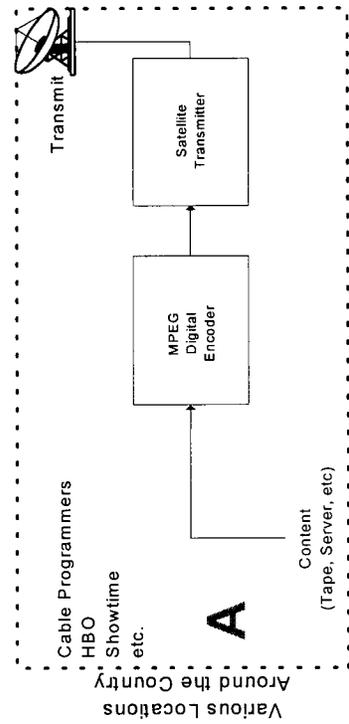
I, Gregory Braden, declare under penalty of perjury that the foregoing is true and correct.


Gregory Braden

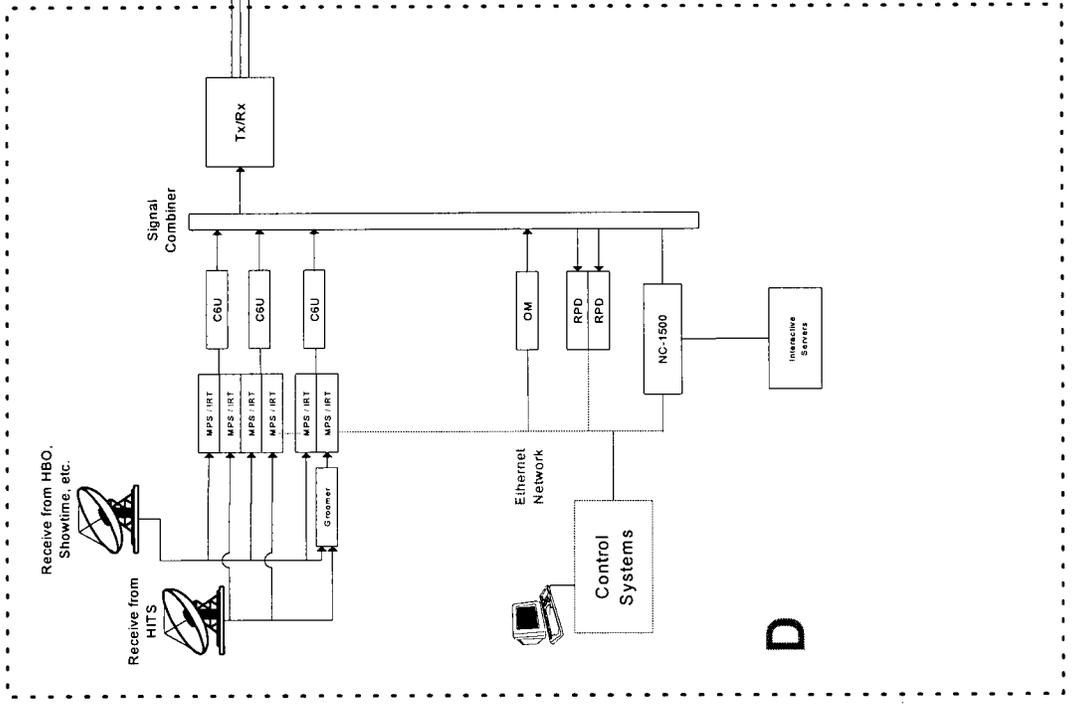
May 17, 2002

EXHIBIT 1

Origination, Transmission, Reception and Headend Processing of Digital Cable Services from HITS and Cable Programmers



Typical Digital Cable Headend (AT&T or Other MSO)



Notes to accompany diagram "Origination, Transmission, Reception and Headend Processing of Digital Cable Services from HITS and Cable Programmers"

Charlie Kennamer
AT&T Broadband
May 4 2002

See Diagram

1. (Reference Section A) - Most cable programmers (HBO, Discovery, etc) originate programming on tape or digital file servers at their own facility. The programs are digitized, compressed and transmitted via satellite directly to cable headends. Programmers typically compress their programming sufficient to deliver 8 or 9 separate program services in one satellite transponder and one cable channel.
2. (Reference Section C) - If a programmer (1 above) has also contracted for carriage on HITS, their signal is received from satellite by HITS for repackaging and retransmission via satellite for reception at cable headends.
3. (Reference Sections B and C)- Certain cable programmers (InDemand, etc) have contracted with the AT&T Digital Media Centers to originate, digitize, compress and transmit their programming via satellite directly to cable headends. If these programmers have also contracted for carriage on HITS their signal may be routed directly to HITS since HITS is located within the ADMC facility.
4. (Reference Sections B and C) - A small number of programmers may elect to have their programming originated by the AT&T Digital Media Centers and transmitted by HITS as their sole means of satellite delivery to cable headends.
5. (Reference Section C) - HITS receives programming from many cable programmers, typically via satellite, and in some cases directly from origination facilities within the ADMC. HITS repackages, digitizes and compresses programming for transmission or retransmission via satellite for reception at cable headends. HITS serves as an aggregator/packager of services and typically compresses programming sufficient to deliver up to 12 separate program services in one satellite transponder and one cable channel.
6. (Reference Section D) - It is common practice at both AT&T and other MSO's headends to receive some programming from HITS and other programming directly from programmers. The programming from either HITS or from direct programmer feeds may be delivered over the cable system "as is" with no changes to the programs being received. Or grooming devices may be used to "mix and match" programs from any combination of HITS or direct programmer feeds to create new combinations of services for delivery over the cable system. Any cable operator may elect to use HITS feeds, direct programmer feeds, or to use grooming devices to rearrange programming to meet their particular needs. The diagram shows examples of direct programmer feeds, HITS feeds and grooming from both direct and HITS feeds. Many headends do in fact employ all three scenarios to create the desired programming packages.

HITS feeds vs direct programmer feeds?

HITS - A cable MSO may choose HITS feeds to take advantage of more aggressive compression (up to 12 program services) used by HITS as compared to direct programmer feeds. Another reason to choose HITS would be to take advantage of program packaging, for example a direct feed from HBO might contain only HBO services, whereas a HITS feed might contain some services from HBO packaged with services from Showtime and Starz. Packaging and aggressive state of the art compression is the value proposition that HITS offers.

Direct - A cable MSO may choose direct programmer feeds to allow them to deliver more services from an individual programmer, or to avoid paying fees to HITS for their service. Direct programmer feeds have a slight quality advantage over HITS feeds due to the additional processing necessary for HITS to aggressively compress and retransmit programming, which may be attractive to some MSO's. Use of direct programmer feeds also avoids any hassles associated with occasional programming changes that may be made by HITS.

Cost differences between HITS and direct programmer feeds:

The headend technology and devices are no different for processing HITS feeds from those used for direct programmer feeds. It is somewhat more common to use grooming devices on direct programmer feeds and the grooming device adds some cost, but the choice to use a groomer on either HITS or direct feeds is a choice the MSO makes based on their programming needs. The only significant cost differences are the fees paid to HITS for their service and the cost difference implied by the compression differences. For example, carrying 36 services all from direct programmer feeds delivering 9 services per satellite transponder (9 to 1 compression) would require four sets of equipment and four cable channels. Carrying 36 services from HITS delivering 12 services per satellite transponder (12 to 1 compression) would only require three sets of equipment and three cable channels, yielding a significant cost savings by using HITS.

Approximate Costs of Key Headend Devices Discussed above:

IRT/MPS	-	\$5,000 - \$15,000
C6U	-	\$3,000 - \$4,000
Grooming Device	-	\$15,000 - \$20,000

APPENDIX 3

AT&T Broadband & Comcast Merger
Joint Analyst Meeting
December 20, 2001
830-1000am ET

Connie Weaver – AT&T

...get everybody in their seat. Good morning. I'm Connie Weaver, Vice President of Investor Relations for AT&T. On behalf of AT&T and Comcast, we are pleased to see you all here this morning, and we'd also like to welcome those of you who are joining us by telephone and those of you who are listening and participating in the live Webcast. I trust you've all had an opportunity to review the press release that we put out last night and you can certainly find that if, if you've not, on either ourselves or Comcasts' Web site. We're very excited to talk about this exciting transaction, which creates the world's preeminent broadband services company.

Joining me here to discuss the program is Mike Armstrong, Chairman and CEO of AT&T; Ralph Roberts, Chairman of Comcast; Brian Roberts, President of Comcast Corporation; Chuck Noski, AT&T's CFO; Steve Burke, President of Comcast Cable Communications; Bill Schleyer, President and CEO of AT&T Broadband; John Alchin, Executive Vice President and Treasurer of Comcast who's joining us right here; Larry Smith, Executive Vice President of Comcast; and, of course, additionally from Comcast, Marlene Dooner, Vice President of Investor Relations is also with us. Additionally joining us is Julian Brodsky, our Vice Chairman of Comcast and Ron Cooper, Chief Operating Officer from AT&T Broadband. Additionally, Greg Braden who runs our Voice, Data and Central Operations with AT&T Broadband, and Mike Huseby, CFO.

Before we get started, we'll have a couple of short remarks and then we're going to turn things over to you for your questions and also open things up to the phones to take questions for those of you who are not able to be with us here this morning. I'd like to point out that the slides accompanying the presentation, for all of you here, were on your chair, so hopefully you all have a copy. They also are available in a downloadable form vis-à-vis both the Comcast and AT&T Web sites. Let me quickly give you those addresses. For AT&T it's att.com/ir and for Comcast it's cmcsk.com. The audio portion of our call today is also being recorded.

Now, before I turn things over to Mike, I'd like to caution all participants that today's presentation may contain forward-looking statements, reflecting managements' beliefs and assumptions concerning future events based on currently available information. Listeners are therefore cautioned not to put too much undue reliance in the forward-looking statements as they are not a guarantee of future performance and may be subject to a number of uncertainties and other factors that could cause actual results to differ materially from forecasts. As more detailed information on these uncertainties become available, you can get them in the press releases from both AT&T and Comcast or through our respective filings with the Securities & Exchange Commission.

Now, without further ado, let me turn things over to Mike Armstrong.

Mike Armstrong/AT&T

Thank you, Connie and good morning, ladies and gentlemen. Thank you on such short notice. I think it was sometime last night that you might have received notice that we

were having the very first analysts meeting of AT&T/Comcast Corporation. I would assure you that this process has been rigorous. I don't know that I ever dreamed of trying to concurrently dialogue or negotiate with multi-parties concurrently over this period of time in order to realize the most value for both sets of shareholders. I think Chuck Noski, probably as we wound down had the best quote on it. He said, "This process is beginning to lose its charm." We're delighted, in fact, we're thrilled today with the combinations that we've put together.

I have a first chart here, if you'd bring it up, please, and it's that vision thing. Let me start with that. Some call it the "bundle" and some call it "convergence." Let's just put it down into the simplest of terms. AT&T did not get into cable in order to do the broadcast analog/video entertainment business per se, but rather to invest in an infrastructure and a reach based upon fiber optic technology that would enable, with the digitization of networks, to carry three businesses over one infrastructure – a video, a voice and a data business, and all the manifestations of them and all the things with the IP protocol that permit them to talk to each other, to converge and to all the eventual devices that will end up receiving them. That's what we had in mind when we started out on the journey and that's indeed what we have in mind as we bring this marvelous combination together of AT&T Broadband and Comcast.

In fact, I know there's been a lot written since the July timeframe. This actually started back in January. Brian and I were at a conference and we took some time out to just sit down and talk about the industry, about technology and services and markets, and the two companies, and we had some things that were really in common. One, that this thing that used to be cable and a pretty much local analog video business was transforming itself into a fiber optic digital business, a broadband business that could do all three services. We agreed that that would make a difference, not only in what it could become in terms of a national scale, but how one would cluster within that national scale so we could leverage your infrastructure versus the homes passed and the multiple services, and the marketing and the support and the care to those consumers. We quickly shared the vision of multiple services as well as that scale would count; that the synergies of these coming together would count. Maybe just to use the old manufacturing term, we really believe that we could be the "low cost" producer.

The third thing is that I get either blamed or, occasionally, attributed that putting three businesses and bringing the convergence of the bundles to the consumers was a good idea, but there was actually somebody who had that thought long before I did. In fact, he had that thought and he named his company after that vision, and, of course, that's Ralph Roberts. Because what do you think Comcast stands for? It stands for communications and broadcast, and that pretty much is the definition of what we've put together today is a very, very powerful communications company and broadcast company who we think has a great future. So Ralph, I will enjoy sharing some of the blame as well as some of the future with you. Congratulations.

Second slide. This is very consistent with what we set out to do. Back in October of 2000, we looked at what we had built, which were four businesses. As you've heard me say, some of us who have been together before, the hand we were dealt in the AT&T company was to transform this company from what was created by Judge Green, the middle of the phone call, into new networks, digital networks, broadband networks, that we could then bundle the services and scale the businesses. As we set out to do that, we recognized that both the capital structure and the equity currency needed to be redefined

in market terms both to deliver the potential of the growth of those businesses as well as the value to our shareholders. We set out to do a four AT&T business distribution to our shareholders. Along the way, we had the opportunity to make a combination out of broadband. But we are still committed to go to our shareholders for a tracking stock, for our consumer business, which in the second half would be dividended to our shareholders, which would enable them, the AT&T company, to be the business services enterprise global data company.

What this does is accelerate that implementation of that original strategy into a defined timeframe. And we believe by the end of 2002, we already have wireless, which was distributed to our shareholders as an asset-based stock in July, that in the second half we would dividend the consumer company, a yield company, to our shareholders and that within the 12 month timeframe we should be through the regulatory process for AT&T/Comcast. So I hope to, both you who assess us as well as those who might invest in us, that we will be able to realize that vision or that distribution and that value and that capital structure and the ability for each of these businesses to have the potential of its capital structure to realize the growth and a currency in which it is judged in terms of the industry it serves. Because the difference between the wireless and broadband growth businesses, the consumer a yield business, and the business enterprise business, which is more of a value business, we now will be able to get the market metric that they deserve.

Next slide. I would like to spend just a few minutes, if I may, on the AT&T, what we call Communication Services Company, made up of Business Services and Consumer. I would submit – the strongest, most powerful enterprise communications company serving our global customers. It is a company that just in the Business side has over 4 million business customers. That's more customers than any other communications company that I know, anyway. We reached a crossover point this quarter in Business Services. For some 100 years, voice long distance had dominated Business Services. As many of you know, we set out to transform it by investing in local, by investing in IP, investing in a network in which we had coast-to-coast reach with a state-of-the-art OC192 network and deployed our functionality intelligence at the edge of the network, invested in a hosting system to sit atop of our fiber optics for an intelligent network, invested in the Services Business. And we crossed over, that for the first time this quarter the non-voice revenue of Business Services will exceed the voice revenue of Business Services. We came, from the 1998 the voice was 76% of our Business Services operation and now it's 49% and that trajectory will continue, because the growth businesses are growing. They're growing in the double digits. We see our Data Business growing at about 20%. If you measure the packets, it's even growing faster than that, our Services Business is growing, our Local Business is growing. In fact, we're probably one of the largest CLEC's, in terms of the business market, in the country. We're in 80 markets, we have some 17,000 route miles of local connectivity. In terms of the enterprise, from an IP reach of data we have some 850 POP's with 60,000 miles of optical cable.

In the Consumer Business, we continue to manage that for its cash flow and margin. To be in that business and selling minutes to consumers, to have a 33.4% margin, I would submit, is being managed very well in some \$4 billion of EBIT DA. Going forward, that business will transform itself from the middle of the call to connect the customers using the resale at the local loop in two fashions: a narrow band fashion with UNI P, where we have both economically and operationally viable opportunity; and with a DSL implementation where our model is a retail model, going to our 60 million customers

who we know how they call and where they call from and what they do in order to offer them a multi-services platform of local, multi-line, feature set, long distance and data in an AT&T package that we believe our customers, in fact, will endorse and accept. And as a result, turn that business from the declining long distance Consumer Business, into a multi-services platform growth business.

Next slide. You can see that the combined AT&T/Comcast is indeed a powerful company. That represents a trailing 12 months of our combined AT&T Broadband and Comcast revenue and EBIT DA. You can see that the projected EBIT DA growth is approaching 20% as we look out into the future. I might speak about the Best Value proposition to the consumer, because I think everybody's been pretty much made aware that the homes passed that this combination presents indeed has an enormous potential. I know it's customary to talk about things in terms of analog video revenue per subscriber, but if you think about where we're all coming from on this combination, a more meaningful definition of the future is how many homes are passed, because all those homes take telephone service; a different configuration to data services. Putting it together so that all those services appeal to all of that market is the underpinning of what we're up to. More services to more people, more quickly.

In terms of the value to the consumers in offering all three services, the first thing is that the customer gets the opportunity to pay less. As some of you know who may live in our markets, when we put the bundles together, somebody pays less for each service if they take more bundles. A pretty fundamental concept.

The second thing we found is that our penetration levels obviously go up greater based upon marketing to the homes passed rather than offer the video base of just the subscribers for that service. We also find we had a lower acquisition cost. We found, for example, that in Boston we did a little study on the 100,000 telephony customers we had and we found two very interesting things. We cut by a huge percent our acquisition costs for either the second service being telephone or data once our consumer said, "I'd really like that telephone service." And of course the telephone business on this infrastructure, we very much are the low cost producer. When you look at both our costs of adding incrementally that application, telephony, and the price structure of what we offer, you're looking at 15-35-40% less price to the consumer for just that service alone. Then finally, we also found that when customers sign up for more than one service, our churn is much less. Those of you familiar with either of the telephony and cable business know that churn is a fundamental determinate of margin.

Then finally, we present a company with the financial strength and flexibility going forward to further participate in strengthening this business, because we'll have an investment grade AT&T/Comcast and a very strong balance sheet for our business service company as well.

In summary, next slide, and I think this is pretty much known by everybody, I would make only one point in order to clarify it, because it caught my eye and I know you will all focus on it. What does "Subject to Adjustment" mean? Of course, some think that Comcast still has more to give and I wanted to spell that. Brian assured me last night he gave all that he could, so we really don't mean subject to that. But rather, you know the transaction's based on a ratio and the .34 of AT&T/Comcast Corp. Class A shares for each share of AT&T, so it's a ratio, not subject to any other adjustment, and that would

be dependent upon the shares outstanding of AT&T. Otherwise, that's pretty straightforward.

Go to the next slide. Just in summary, again, let me comment, if I may, on best of both teams. I think one of the real determinants of the outcome of this vision and the economic potential of this company is obviously rooted in its management team. To bring together the Comcast and AT&T Broadband management team, I would submit, is the "dream team" of the, whether you call it the communications industry or cable industry or any industry. This is one doggone great management team.

How we're going to figure it all out going forward is to have an executive transition team that would be headed up by four executives: Chuck Noski and Bill Schlier from our AT&T side and Steve Burke and Larry Smith from the Comcast side. And with their help, Brian and I will figure it out going forward.

In terms of regulatory approval, we believe that this presents a very compelling case on two fronts for regulatory approval. First, to consumers, we think obviously we're going to offer more choice. We think we're going to offer very competitive, if not lower prices, to our consumers. And, we think we're going to be able to accelerate the broadband data deployment as a result of the financial strength. So I think consumers are going to benefit from this combination.

Second, I think competition is going to benefit. I know that Chairman Powell at the FCC has often spoken that the true competition going forward is facilities-based competition. As some of you know who have listened to me over the years, one of the fundamental underpinnings or principles of our investments have been to be a facilities-based, broadband provider of digital services, and by now bringing this national reach, we bring national competition for those services based upon a facilities approach.

Finally, the last chart, do we believe we're "creating value in the marketplace for our shareholders?" Now, how did we get to 86? We're hopeful that your assessment of our company will make that a very distant memory as the value increases going forward. That's simply multiplying the transaction with the price of the Comcast stock and you multiply that market price times 1.235 billion shares that's in this deal and you get \$86 billion.

There's kind of another interesting phenomena, that if that indeed is the value of this new company, which is simply arithmetic, what's the arithmetic of AT&T Communication Services' Business Services? That puts that value at about two times cash flow at the current market prices. So what we hope we're bringing to our shareholders is the unlocking or unleashing of shareholder value going forward.

With that, I'd like to turn it over to my new partner, Brian Roberts. Brian?

Brian Roberts - Comcast

I think the best part of this transaction is we all get to have a good holiday. We appreciate resolving it and having, at least today and tomorrow, before people run off for their well-deserved holiday's, to talk about the new company and sort of go into some more details about all the hopes and aspirations we have.

There's many other people from Comcast and AT&T in the room today, in addition to the one's Connie mentioned, and some of the advisors and the teams that helped make this day possible and I just want to thank them from the bottom of my heart. I do believe, as you go to the next slide, that this new company really is an engine for shareholder growth, for new products and for sort of an unparalleled opportunity in the cable and broadband business. You'll will have lots of time in the months and years ahead to talk about and find the best ways to exploit that opportunity, but if you just look at where we begin, you will have one of the premier footprints in what is clearly a growth business, not something that's yesterday's business. And I think you couldn't dream of a better opportunity. So whether that is the video space where Comcast has, perhaps, more focus in the past, or AT&T's vision of communications, or data where we've both been going aggressively, it doesn't matter, because it will rise to the top what the right opportunities are.

We think the content opportunity alone, something that I have had a lot of practice and experience watching the value creation from the cable systems, to have a company with 22 million footprint, it's hard to dream of all the opportunities that we're going to be able to think of, I think. We have an entrepreneurial-based model, so there are many business people out there who will say, "Well I can take my idea, come to this company first and see if we can't strike a partnership and make it happen." Not every idea has to come from within the company. Of course, there's a terrific cost synergy opportunity in addition to revenue enhancement.

Next slide. This talks a little bit, we figure we'd bump the price about, depending upon how you analyze it, call it 15%, 10-16%, I'd say. We basically offered 4,000-4,100 per customer and this deal, you'll run your own map, but we think is around 4,500 or so.

Why did we do that? Well, first of all, it was competitive, and Mike and Chuck and their team, they're to be congratulated. They ran a marvelous process, but they gave us a complete and level opportunity to come in and study the company in diligence and spend some time. And what we found was a company that's on a trajectory clearly on its own to radically improve the margins, to realize the telephony investment. I think the changes and the enhancements to the management team that they've made, with Bill Schlier who I've known for a long time, and we both were there at the very beginning of the first idea of a cable modem, sitting around a table with a bunch of people in Cable Labs, that we got more comfortable, not less, that this idea made sense. That gave us the conviction to go for it.

At the same time, as Mike said, we've committed, when you're tripling your company, its size in one moment, to step back and say, "We know realistically that we need help in how to make that happen." And we've committed to both AT&T and to ourselves to find a way to integrate the best of both organizations, and that's going to be a pleasure and a high class opportunity.

Next slide. Let's take a look at the company, because I'm still stunned. How about 80%, 79% of all our systems will have over 250,000 customers per system. When I first got into the business, I was working in Trenton, New Jersey and I got sent to Flint, Michigan, was not happy about that, thought I had done something wrong, and Flint had 50,000 customers and was the one of the largest cable systems in the country at the time. Have 80% of your company and 250,000, that's a totally transforming opportunity.

And if you look on the next slide, as we've said before, this company together has eight of the top ten DMA's where they're a major presence and 70% of the top twenty DMA's. So things that have been sort of unthinkable before, as Mike said, on the national scale, to go to an advertiser and say, "We can deliver you eight of the top ten cities for 100 cable channels for advertising," there's no one place to go shop and be able to do that right now. And whether that is through services and then quickly rolling them out, as I believe time will reveal this opportunity and you have to just step back and say these are high grade, technology upgraded plant facilities with three different businesses that we're trying to go at. We're not going to get ahead of ourselves, but with the integration process that we're going to do with this footprint, it's a remarkable opportunity.

Next slide, please. Just quickly, you can see that if you have a new channel or a new technology or new idea, where would you go first? So I think we get a first look.

Next slide, please. What is that first look going to be all about? Well, clearly, it's each of the new products. So are we done? No. I think cable modems use one channel. People tend to forget that. All the great success, we drove \$40, \$45 in our case, right now per customer, we'll have a million or so very shortly paying \$45 a month for a product that started at zero 24-30 months ago. What if we do five channels, ten channels, to devote more of our bandwidth, we can split the nodes. So whether that's VOD or SVOD or home networking, some of us are going to go to the Consumer Electronics Show next month. Last year the rage was people who, just as when television got started there was one TV in the house, there was one PC in the house. Now, everybody wants their own PC. All my kids want for Christmas is their own computer. It's unthinkable how fast that is changing the way the next generation want to function.

That is what's so exciting about this company, to have the connection that people want. And whether that's video games and the X-box and Nintendo Systems all integrated into your house, that's what we mean by home networking.

And, of course, on the content side, Steve's going to talk a little bit, and I will as well, but the ability to incubate channels. Just want to brag on QVC for one moment. About three Sundays ago, post September 11th, post the bad economy, and it's in one of the newspapers this morning, Dell Computers sold on QVC 32,000 PC's in one day. We sold \$72 million worth of merchandise on one channel, \$80 million worldwide in one day, ...television. So electronic commerce is a huge part of this company's future and we're positioned with the world's leader in electronic commerce. We will do more packages shipped this year than Lands End, LL Bean and Amazon combined.

Slide, please. And, of course, if you believe in digital data, telephony, whichever is your favorite, this company is sitting with nearly 5 million digital boxes, 2 million plus data customers and right about 1 million telephony customers. If growth of new products is where the engine of the future comes from, we think AT&T/Comcast offers that.

Next slide, please. Let me talk about telephony for a moment. That's probably the most interesting and new opportunity that came from the due diligence process. Kind of in the middle of it, Mike and Chuck and some of us sat down and they looked at us and said, "You know, we have a vision, we've done a lot of the hard work and we've taken some of the arrows in the back for being pioneers of a business that could be bigger than your

data business, and you have not fully endorsed that.” And I said, “Well that’s not really right. It is true that we haven’t started in earnest, but there is no greater revenue opportunity than the hundred billion dollar a year local phone business” and this company, when we sat down and rethought it, has a bigger footprint than any single RBOC. And to not even try seemed insane.

Now, AT&T is going to continue on their phone strategies between now and closing, and I think they’re at an inflection point. So we then said, “Well if we could leverage off of that, kind of turn this around, we don’t have to go through some of that pain and suffering to get going. We don’t have to build a new billing system and provisioning system and the switches and the NOC’s and all those things.” And as the world evolves to a digital world, IP world, this company has the ability to get going faster. So this accelerates an opportunity that we have stood up and said that we endorse, and so it takes it from the world of academia to the world of here’s the real world. You’ve got an opportunity, the company’s invested, the capital’s been spent, why not let it take off? And that’s when I think we sort of said we can share a vision that it is a three-service company in the future, not just a two-service company in the future.

Next slide, please. Let me try to go back to the video side, since we spent some time here on the communications side. These are 100% numbers. I just wanted to qualify for those who are keeping score. We don’t own 100% of most of these assets, but the value creation from the video side of this business and the relatively low amount of risk capital. So I think we have a total of \$200-250 million invested in QVC. We own 57%. We have several hundred million dollars in E-Entertainment. The Style Network is just a pure start up. Golf Channel, people thought nobody would ever want to watch a golf channel. Golf Channel is probably one of the best brands in television if you happen to like golf, and that’s what matters with cable, just finding the passion of the consumer. Comcast Sports Net and our strategy in sports I think has paid off. So this new company, we did that with 4 million customers, we got to 8 million in the last couple of years, you just have to step back, take a deep breath and think, what might you do with this new footprint.

Next slide, please. Let me just conclude about what drives me, what drives my father, what drives Julian, Brodsky, who from the moment the two of them and Dan Aaron launched Comcast and dreamed up Comcast at its very founding. And Mike, you’re very gracious in remembering that it’s communications and broadcast and it really has been a very focused company for one overarching goal – shareholder return. It’s an overused phrase, but we are into long-term shareholder returns. Since the inception of the company, of the IPO now close to 30 years ago, we’ve had a 24% compounded return on the stock. My father said to me last night as we were heading back after a long day, “There’s no better opportunity that we’ve seen in all those years than putting these two companies together.” So we look forward to continuing this dialogue and building this great company. Thank you very much.

Let me now turn it over to Bill Schleyer.

Bill Schleyer – AT&T

I don’t think I’ve ever told Brian this story, but when I first tried to get into the industry, back in the late 70s, I think it was 1979, I actually interviewed with Comcast and was in the process of being offered a job in, where else, but Trenton, New Jersey. So I was

pretty excited about getting into the industry and just before I was getting ready to accept the offer, I got a call that said, "Well, the owners son is graduating from college this year and that's the job he would like." So, that's a true story. I obviously went on to other things.

I first met Brian in the mid-80s and that was back when the active leaders in the industry were guys like Amos Hostetter, Ted Turner, of course Ralph, John Malone, Chuck Dolan. I remember meeting Brian and saying, "This guy has the potential to lead this industry some day." And I think today we're basically turning the torch over to you, Brian. So congratulations. We'll look forward to your leadership. It's going to be a fun ride here.

Anyway, I'm here to talk about our platform. The AT&T/Comcast national network is an incredibly powerful platform. I know Brian and Mike talked about it, but we've got about 80% of our plant is state-of-the-art. It's 550 or greater. And we've got about 20% to work on and that is being worked on as we speak and will be state-of-the-art within the next couple of years.

At the same time, our focus is on upgrading the 20%, but at the same time we're focused on building the Comcast, working with the AT&T/Comcast network to get it telephony ready. You can see that we've got 38 million homes that are digital video ready. That's over 95% of our homes. At the end of 2002, we'll have over 30 million data ready homes and we're well positioned to grow that to 38 or so million in the next few years.

Then on telephony, we currently have one million subscribers and that's over about 6.7 million telephony ready homes. By the end of 2002, the joint company will have 11.2 million homes. We should be able to add after that about, we haven't finalized a number yet, but about 5-6 million telephony homes a year, and that really will be the growth engine of the company. By offering all three services – telephony, data and video – that will allow us to press our competitive advantage. So we're obviously really excited about this combination. It's a very powerful footprint.

Let me talk about data for a second. As many of you know, we've built, as did Comcast, a contingency network in the event that @Home were to shut us off, which they wound up doing. Comcast did the same thing and ultimately we will integrate those two networks. But this is a very powerful network. In addition, the new network definitely gives us control of our customers. Never again will we be put in the position where someone can shut off our customers. It just won't happen. And the cost of the network, the operating costs will be lower with this new network than it was with @Home, so that's a real benefit. At the same time, our overall reliability of the network is superior with state-of-the-art technology we're using.

It's designed to support multiple ISP's and the benefit of that to us is we can create a very robust marketplace for the wholesaler market for ISP's and that will be a spectacular development over the next few years, we believe.

In addition, we can offer tiered packages and the benefit to us, again, is we can design packages for the light user, the average user and the heavy user as opposed to just charging one price and everybody gets everything for one price. This will help us drive penetration deeper in the market and at the same time generate more revenues from our heavy users, so the net result of that is a very good thing for us. At the same time, with

our new network, we can generate some new features that I think the consumer's going to find pretty exciting, like remote e-mail.

The long-term results are, we can provide better service to our subscribers with more options, and in the long-run we have a very exciting financial prospects with the integrated network.

I'd like to talk a little bit about telephony. As you can see, this footprint, we finally now have a national scale facilities-based competitor to the ILEC. That is a very, very powerful position. Thirty-eight million passing, we only have one million subscribers. That number will be very, very different in three or four years, very different. You can see the AT&T/Comcast footprint relative to the four ILEC's. They have 100% penetration. We'll be taking a fair amount of share from them over the next few years.

On average, we've got about 15% of our passings who take telephony right now. It's about 15% penetration and that is growing rapidly. We have 40 communities already that are well over 20% and a number of communities that are over 30% penetration. So we will ultimately have millions of customers because we will be providing a better value than the ILEC and at least as good of service.

The economies, the economics of telephony are very powerful for us. We have in place the infrastructure to support telephony here at AT&T. The merger really leverages incredibly well what we've done already. We have a whole infrastructure, both provisioning capability, network operating center capability, customer care capability – all that is installed at AT&T and has a relatively fixed cost to it and that's a very stable fixed cost. So we can lever the Comcast footprint into the new company with very low incremental cost to it.

We've got the roll out knowledge of process. We've spent a fair amount of time over the last few years and we've absorbed a lot of operating losses doing it, but we're right now, in the first quarter of 2002, breaking even on telephony. We believe the margins will explode from there.

We have the AT&T infrastructure to help, and this is AT&T's core business that supports us, 80% of Comcast's subs are in markets where there are AT&T switches. So this makes for a very easy transition for telephony.

The returns on telephony are pretty spectacular in our view. Just to give you a sense by the incremental economics, we'll generate in 2003 roughly \$300 per incremental subscriber. That's with an average revenue per subscriber that's growing because of new feature sets and the introduction of long distance. At the same time, our fixed costs are stable and our variable costs, our unit costs, are declining as we scale the business. This business scales incredibly well. That 300 number could move towards the high 3's by the end of 2005. At the same time, our incremental capital cost is about \$700 and declining. Even without voiceover IP, we think that number heads towards a number that begins with a five sometime by 2005. Surely with a six into the 2003-2004 timeframe. With voiceover IP, depending on the mix of voiceover IP and switch, that number clearly is in the five's. So, think of an incremental capital cost of something in the 500+ range versus an incremental EBIT DA of something towards the high 300 range, and that's a pretty attractive set of economics when you've got your network costs all absorbed.

Again, we expect to break-even on telephony in AT&T in the first quarter of 2002. We can leverage what we've done quite easily over the Comcast footprint and we think that will help make the growth engine pretty spectacular for the joint company over the next three or four years.

So with that, I'll turn it over to Steve.

Steve Burke - Comcast

Thank you, Bill. We've talked a lot already about the platform and really what these two companies look like in terms of the footprint and the clusters and the existing asset base and what I'd like to do is talk about how we're going to try to create value and increase the value creation by putting these two companies together.

What I'd like to do is start with a slide that really talks about the first type of synergies. There's really three major types of value creation or synergy effects by putting these two companies together and the first are just the run off the mill synergies that you get by being larger, by putting two companies together and hopefully getting $1+1=3$.

The first area here is programming cost savings. Both of our companies, the single largest expenditure in our business is programming costs. Our programming costs are going up in a double digit fashion out over the next five years and we believe not only can we take the Comcast programming prices to the AT&T rates, which are better than ours because AT&T has larger scale, but as a combined entity we can get further enhancements. And when you look at the range here of \$250-450 million, if you go out a few years, the combined company's annual programming costs will be about \$5 billion and the annual increase in programming costs will be about \$750 million. So this kind of programming savings is less than the annual increase in just one year and we think it's a very achievable range.

If you then move on to operating efficiencies, the kind of efficiencies you get when you put two organizations together, we feel that there should be, within a one to three year time period, \$200-300 million of synergies. That would be elimination of corporate overhead costs related to Baskin Ridge, that would be elimination of duplication, best practices and systems that we could leverage between the two companies, etc.

National advertising, Brian mentioned that we'll be in eight of the top ten DMA's. We will be the major cable provider in 14 of the top 20. Our footprint will actually be bigger than the own station footprints of the major networks. In affect, we'll be able to go to an advertiser and speak for roughly a third of the United States. And as the targeting and the technology and the growing market share that the cable business has been getting and will continue to get, we feel that this is in many ways underestimated upside to the cable business in general and we intend to pursue it very, very aggressively.

In terms of new products, one of the advantages of the kind of scale we're going to have is we can take a real leadership position in terms of developing new products. I think both of our companies have one thing in common – we are very much new product development, new product focused companies. We've been more focused on video and data, AT&T has been more focused on phone than we have, but key to our strategies is taking the infrastructure that Mike talked about and layering in new products. And when

you have the kind of position in the industry that we're going to have, you can really push your vision of interactive television, your vision of video on demand, your vision of new high speed data applications, and our feeling is having that scale and that leadership position is going to lead to real synergies.

Then finally, telephony was always part of our future and part of our vision, but has never been part of our five-year plan. We spent a lot of time with our colleagues now at AT&T and believe that if we overlay their expertise, their investment financially but also people and systems and their learning on our existing footprint, and roll out telephony to our footprint, it could represent a very significant opportunity over the next five years. So we've included that in the synergy calculations as well.

If you take the midpoint of that range of 1.25 to 1.95 billion, then do a net present value, you come up with \$13.5 billion worth of synergy. If you then divide that by the roughly 13.5 million AT&T subscribers, you come up with approximately \$1,000 per subscriber of synergy, if you attribute it all to the AT&T subscriber base. So when you're thinking through how this transaction works and how the two companies come together and how we create value, we think there's a significant amount from the classic way of looking at synergies. But that's not the end of the story.

In addition to creating synergies by putting the two companies together the way I just described, during the due diligence process and getting to know the AT&T Broadband group better, we became increasingly convinced that this business is going to achieve industry standard margins; that with Bill Schleyer, Ron Cooper, Mike Huseby, Greg Braden and the group, they were well on their way to do that and that this was a very, very large opportunity that was going to be fully realized, frankly, whether we showed up or not. We'd like to think that together we'll have more management depth, we'd like to think that together it might happen more quickly, but we became convinced during the due diligence process that this business was going to get to industry standard margins.

When you do the math, if you take our margin of 42%, the AT&T Broadband margin most recently of 25%, and then the differential of 17%, then you apply that differential to '01 revenue of close to \$10 billion, you get an opportunity in the year we're in of \$1.6 billion if you can bring that margin all the way up to our level. What's particularly exciting about that is that opportunity is going to grow very dramatically because the AT&T revenue side of the equation is going to grow in the 12-15% range. When you start to compound that, that \$1.6 billion worth of opportunity compounds very dramatically.

First area, the \$13.5 billion worth of net present value; second area, taking the AT&T broadband levels up to the levels that are currently enjoyed by Comcast. This slide shows our experience in terms of integrating new systems. We, as a company, have brought about 3.6 million new customers into our company, and you can see in the blue lines shows our EBIT DA and then the graph across shows our margin. Our feeling as a company, and I know Bill shares this, we've talked about this in some detail, is that you can do multiple things at the same time. We have launched close to a million high-speed data customers, over 2 million digital customers and integrated 3.6 million new customers and done it all at the same time. And so our focus as a combined company will be to continue the financial performance while continuing to roll out the new

products, while continuing to integrate with the kind of discipline that we've always shown before.

Then the third bucket, the third segment of synergies is really in some ways the hardest to quantify, but in some ways the most exciting, and that is what can you do in terms of bringing new products and services to customers when you have the kind of footprint that we're going to have. Brian spoke to this, but one point I'd like to make is with 22 million customers, with 38 million homes passed, we have not only the ability to create new cable channels, our history and the history of others in the cable industry on that score is clear, but we also have the ability to create new data applications, we have the ability to do new things in terms of video on demand, really create entirely new businesses as a result of this scale. I think it's very difficult to quantify this third segment of synergies, but if you look out at this company five or ten years from now and you look back today and say, "Well what upside did we underestimate?" I think it's very likely it would be on this slide.

I think one of the exciting things about this deal is when you run the numbers, if you look at these three buckets of synergies, the synergy value of each of these three buckets can be enormous, but the economics of the deal don't depend on realizing the synergies from each of the three buckets. In fact, if you get any one of the three buckets, you can pretty well justify the economics of this deal and we're going to try our best, of course, to try to get as much of all three as we possibly can.

So we couldn't be more excited, we couldn't be more happy to be sitting with the gentlemen up here and putting these two companies together and trying to go and make something better than we could have done, either of us, alone.

With that, I'd like to turn it over to Chuck Noski who did one of the most amazing jobs with this process of anybody imaginable. Chuck?

Chuck Noski – AT&T

Thanks, Steve, and good morning. Probably nobody is as happy to be here as me.

It occurs to me, as well, Brian, that this will be the first time that Mike and I will be able to leave a public building at the same time that you and Ralph do. So we're pleased to be here.

Let me start my remarks by emphasizing that today's announcement creates an entity with a strong credit profile and an ability to improve on its financial position in the future. The combined AT&T Broadband and Comcast have generated an estimated \$4.6 billion in EBIT DA over the last 12 months, and given the strategic and operational initiatives that Bill and Steve outlined for your earlier, we believe AT&T/Comcast will have accelerating free cash flow in the future as a result of merger synergies, ongoing scaling of margins in the telephony and data businesses, and reduced upgrade and infrastructure expenses going forward. From a deleveraging perspective, it's also important to point out that we believe that AT&T/Comcast will have multiple sources for further deleveraging such as our 25.5% investment in Time Warner Entertainment, which will continue to enhance the credit profile of AT&T/Comcast. Between the

benefits of the improving cash flows and monetizations, we anticipate that AT&T/Comcast will attain investment grade ratings.

This slide presents an approximate view of the pro forma AT&T/Comcast Corporation's 2001 results. With this view, the combined entity would have approximately \$18 billion in revenues and 25.6% EBIT DA margin. This should emphasize to you the substantial scale this business will have in the marketplace. With a pro forma net debt balance of approximately \$27 billion, we feel comfortable targeting a solid investment grade rating.

Let me talk for a moment about AT&T Communication Services, the remainder of the AT&T company following the restructuring actions that we've been undertaking over the last year or so and giving effect to the AT&T/Comcast combination. From an AT&T Comm Services perspective, today's announcement reinforces the deleveraging commitment that the AT&T management team has made to the investment community all year. As a result of the many actions we've described to you, throughout 2001, AT&T has eliminated over \$20 billion of debt since the beginning of the year. In addition, the recent completion of our \$10 billion global bond offering refinanced essentially all of our short-term obligations and significantly increased our financial flexibility.

With this announcement, AT&T/Comcast agrees to incorporate \$17.3 billion of short- and long-term debt as well as an additional \$2.6 billion of AT&T broadband related liabilities. In addition, Microsoft has agreed to convert its \$5 billion investment in AT&T quarterly income preferred securities, what we call QUIPS, into 115 million newly created shares of AT&T/Comcast stock.

In the aggregate, the net reduction of AT&T's debt and obligations as a result of the creation of AT&T/Comcast will be approximately \$25 billion. This will insure AT&T Communication Services remains in a strong financial position as a result of this announcement.

With the trailing 12 month revenue profile of over \$44 billion and nearly \$15 billion of EBIT DA, AT&T Communication Services remains a clear industry leader. Mike mentioned earlier, AT&T Business Services holds the leading position in the enterprise customer space, leveraging our unrivaled sales and distribution channels and our comprehensive platform of products and services to further expand our relationships within the global marketplace.

Our AT&T Consumer Services segment continues to be the leader in the consumer telecommunications industry with approximately 60 million customers and an industry-leading margin. We're currently in the preliminary launch phase of our new product combining local and long distance voice services, vertical features and high speed data services, and we're looking forward to this product reaching meaningful scale and scope over the next several years.

Now in terms of where we are in our restructuring and where are we going. To begin with, we plan to continue our deleveraging commitment and that will be part of the ongoing process at AT&T throughout 2001 and throughout 2002. In addition, we currently expect to file a proxy in the first quarter of 2002 and following an expected shareholder meeting in mid summer, and at approval of our proposals we expect to fully

distribute the AT&T Consumer Tracking stock in the second half of 2002. We currently expect that the AT&T/Comcast transaction can close within a year from today.

With this timeline, we should complete our restructuring initiatives by the end of 2002, which I'd like to remind everyone is consistent with the announcement we made in October 2000 regarding the restructuring of the AT&T Corporation.

In conclusion, and it's tough after all of these guys have gotten up here and told you everything about this company, to say much else, but we believe that today's announcement creates one of the leading communications, media and entertainment companies. With 38 million homes passed and 22 million subscribers, this business is starting out with significant scale and reach. Given the experience of our combined management teams, we believe AT&T/Comcast can successfully scale new and innovative products and services to our customers while growing overall profitability. We believe this transaction creates the best value proposition to consumers and to AT&T shareholders, and represents a realization of the AT&T Broadband vision.

With that, I'd like to turn the meeting back over to Connie Weaver who will go over the process for the Q&A. Thanks.

Connie Weaver – AT&T

Thanks, Chuck. We're going to go to Q&A and I'd like to remind everybody that since we have people listening vis-à-vis the phone and by Webcast, please wait for the microphone so the folks listening in can hear your questions. We're going to take questions both from the floor and we're going to take questions from the phone. I'm also going to ask you to limit your questions to one per person, so we can try to accommodate as many of you as possible.

With that, let's start on the floor. Rick?

Rick (Inaudible)

Could you talk about the relationship between the two companies post deal. Brian, you said you don't want to be tied to another carrier when you were referring to @Home. Would cable telephony be tied to AT&T for providing the backbone service for your cable telephony product? Or, are there other relationships between the two companies we should know about?

Brian Roberts - Comcast

Great question. We openly discussed how to find a perfect balance, and I hope we have tried to accomplish that, which is it would be ridiculous not to start out light using AT&T Communication Services to keep these opportunities going at the rate they're going and at the same time not to have a future windfall or loss to either of the two companies that are providing it for below market or providing it for above market. I think Mike and I discussed that, we worked out agreements that allow for a smooth transition and then flexibility that we're both happy with.

Mike Armstrong – AT&T

Rick, we have an intercompany agreement for the backbone services. It is that market. It has terms and conditions to continue to be competitive in that market, so there was no transfer of any subsidization, if that's what you kind of mean, and it's an at-market relationship.

Rick (Inaudible)

No exclusivity?

Mike Armstrong – AT&T

There's a period of time I think in the intercompany agreement in which we do have a commercial arrangement with each other, but we have to be competitive within that timeframe and the ability of AT&T/Comcast to negotiate as well as to outsource to other providers is there.

Connie Weaver – AT&T

Let's take one from the phone.

Moderator

We have a question from Jessica Reif-Cohen with Merrill Lynch.

Connie Weaver – AT&T

Good morning, Jessica. Congratulations on the arrival of your new son. You're back quickly here.

Jessica Reif Cohen – Merrill Lynch

Thank you. Maybe just an add-on to that question, on the telephone side. Brian, is the Comcast cap ex any different from AT&T in terms of upgrading for telephony? And separately, could you discuss the tax liability issue that the *Wall Street Journal* addressed a few days ago?

Brian Roberts - Comcast

Let me begin by dealing with the cap ex question on our model. As you know, Comcast is going to be 95% complete with our rebuild by the end of this year, so we have always been looking for ways to invest in the business and get better than 4% return on cash that you get by putting it in the bank. Hopefully, the opportunity that lays before us is to find ways to, I think that's what made the fit so compelling for us, because as AT&T accelerates it rebuild or completes its rebuild, which is job one, and that Bill talked about, we're able with the combined balance sheet to help make that happen.

As to any liabilities, let me turn it over to Larry, but I think we have our arms around it all, Jessica, and have incorporated it into our comfort zone. I will just say that Microsoft converting the \$5 billion of QUIPS was a huge financial benefit that enabled our balance

sheet to have the left, the combined balance sheet, to achieve what Chuck and Mike talked about for AT&T deleveraging, creating AT&T/Comcast without any burden. Because obviously, this new company has the ability to talk about ... and monetizing that and at some point has the ability to other kinds of financial deleveraging transactions as the cash flow does ramp up. But, there was no single opportunity as quick and as dramatic as converting a preexisting, no new money from Microsoft so it's a total win/win; to take the preexisting \$5 billion liability and turn it into equity from the get-go. So we're very appreciative of that.

Larry, any other points on the....

Larry Smith - Comcast

Well, we studied the tax situation very closely and I think it's inappropriate to get into any real details here. I think we're all very comfortable we've dealt with them in the agreements and we're comfortable that the magnitude of them is not particularly great.

Niraj Gupta – Salomon Smith Barney

Brian, you just spoke to TWE. Have you been in active discussions, I know it's a little bit early, with AOL with respect to some sort of resolution there, because it is a passive asset. And secondly, a lot of talk on telephony today and also ongoing relationships going forward. What's the status in terms of using the AT&T brand as it relates specifically to local telephony? What's the arrangement in terms of paying the parent company?

Mike Armstrong – AT&T

On the AT&T brand question, obviously this is AT&T/Comcast. Services that we offer, whether in telephony, if we wish to use a platform of AT&T to offer telephony, then we'll have some negotiating with AT&T for the use of that brand and give a license and a commercial arrangement. Or, we may choose to use another platform to take that service to the marketplace, and so that's yet before us.

Brian Roberts - Comcast

I would also take it back to you, Mike or Chuck, on TWE because having signed a confidentiality agreement, we could not talk to Time Warner. So the answer is, we have no discussions that have occurred, but I've read a lot of newspapers and I think you had some conversations with them.

Chuck Noski – AT&T

On occasion. Well as many of you know, we initiated earlier this year a registration rights process that's provided for under the TWE partnership agreement. For reasons that are probably obvious to this group, that process was delayed. And now, with the completion of this transaction, we will reinstate the activity that in our expectation will result in the complete monetization of the AT&T/Comcast investment in TWE.

Brian Roberts - Comcast

Let me just add that we've always had a wonderful relationship with Jerry, Dick, all the Time Warner folks. We said from the beginning that that was not one of the assets that we would have focused on retaining. With that said, I have not had the opportunity to have a conversation other than to congratulate Dick on his appointment.

Connie Weaver – AT&T

Jeff?

Jeff (Inaudible)

Thank you. Nobody likes to think about divorce on the way to the altar, but can you elaborate a little bit on what the breakup provisions may be of the agreement, where the regulatory risk resides and if there are any potential adjustments if there's any material change in one or the other parties' income statement on the way to closure of the deal?

Chuck Noski – AT&T

There are reciprocal breakup fee arrangements of about a billion and a half; a very typical, traditional arrangement. We have the, again, traditional and typical MAC provisions and beyond that give us a chance, we've just finished dating. Let's get into bed together.

Mike Armstrong – AT&T

On the regulatory thing, last night Brian and I called Chairman Powell to let him know about both the transaction as well as our commitment to a facilities-based competitive choice for consumers and that we look forward to working with him. We really do think this is good for competition, it's good for consumers. It is our judgment that this will proceed with regulatory approval. We're committed. I know some of you are familiar with the old attribution rules, and as ingenuous as those were, as they were invented during our Media One process, and that they no longer apply. On the other hand, we are committed to monetize TWE, so we do think that the regulatory process, we will be able to get through.

Connie Weaver - AT&T

Another question from the phones.

Moderator

We have a question from Jack Grubman's line with Salomon Smith Barney.

Jack Grubman – Salomon Smith Barney

Good morning. Congratulations to everyone for a great deal all around. Now Brian, you just have to get our hometown basketball team back on track.

Question for Chuck. In one fell swoop you have not only fixed the AT&T balance sheet, but you could almost be accused of being even under levered in the AT&T Communications Business. That's been a while. Given that Dave obviously faces this is the challenge of growing the business, is it fair to guess that this new financial flexibility could result in actions that could be taken to maybe grow the trajectory of the business? Maybe you could talk about some of the stuff that could be done outside of just the tracker.

Given that you guys have been busy, you might not have noticed that Bell South pulled their Georgia/Louisiana 271 applications. If we are going to have a sixth straight year of yet again Bell long distance approvals being far less than people think, it would seem to me that on the consumer side for Betsy's business, maybe some of the doom and gloom projections may not happen. And for Brian and Mike on the broadband side, is it a safe assumption to say that you guys will go for the kill in telephony when you actually have a better voice bundle than most of the RBOC's who can't do long distance, not to mention video and obviously data? Thanks.

Chuck Noski – AT&T

Let me take the first part of your question. I'm not sure I'm familiar with the term "under levered" at AT&T, but I think we are in a much stronger position with the core telecommunication services businesses. You should not expect AT&T to become a free spender following the close of this transaction. We will still respond to the market. Obviously with the conclusion of our Concert relationship, we have some investments to make globally as we build out. But again, we don't expect those to be significant, Jack. We are going to simply get through what is a difficult period in telecommunications, rebuild the balance sheet, maintain our leadership in each of our businesses and, of course, anything that would delay the entry of the RBOC's into long distance is, we think, fundamentally a good thing.

Mike Armstrong – AT&T

Jack, in terms of the telephony opportunity at the end of your question, I think you'll find that we will present a good balance between go for it and being financially responsible as we scale. But there is no question, in at least my mind, that this bundle and this convergence works at the market and works at the bottom line.

Connie Weaver – AT&T

Let's go here.

(Inaudible)

...capital. I commend the deal and I wanted to start by saying that, but I'm hearing no conversation this morning about the thing that I consider to be a very serious flaw. Over the last two years, boards controlled by AT&T have cost shareholders dearly at both AT&T and Excite@Home. Now we have a board structure that is 2/3 AT&T and 1/3, according to the numbers you presented, Comcast. It said 66% voting control AT&T on your slides. So I would like to know, number one, why there was no consideration, or maybe there was, to an independent board where 10 members were from outside and two were from within, and why you have an even number, 5 and 5, who's going to pick those

independent members and how are you going to keep this board from evolving into the dysfunctional mess that has occurred at those other two companies?

Mike Armstrong – AT&T

What a nice question. The board is made up of five Comcast directors, which we've already agreed to. It will be made up of five AT&T directors that Brian and I will agree to. And we're going to pick, between us, two new directors who will be independent of both companies. And so I don't believe that that represents, what you saw in the chart was 56% of the equity interest of the value interest was to AT&T shareholders and that represented it. So, we work very hard to have a balanced board and an independent board.

Now, on the same token, there will be a high vote stock, which will have a 33% combo of Roberts family voting interest. So it will have a vote that is disproportionate to its economic interest, but that was part of the transaction. I think we present a company that is very balanced in its board representation.

Brian, would you want to comment?

Brian Roberts - Comcast

I think we each look at this from different perspectives, so from the Comcast perspective, we wanted to maintain as much of where we've come from and maintain the culture and the family presence that the business has enjoyed that's resulted in the shareholder return. But when we got into a dialogue with AT&T, we agreed that it was appropriate for a company of this size and scope to have outside help from it through independent directors. So the majority of the board will be independent. We are comfortable that with 33.3% of the vote that we'll have a good voice. In the documents that will come out to all the shareholders, it will lay out all the details of other special provisions under this circumstance, what happens and things of that nature. We feel very comfortable with the kind of board that we'll have and ultimately the division of labor is very clear, and I think this is meant to hit the ground running. That's what I think took a lot of time here. This was not something quickly pieced together. This has been pretty much in the works since late summer when we began talking again. We really had ironed out a lot of this part of the process before we even signed the confidentiality agreement. We're invited to come back in and really take a look to see if we could improve our economic perspective and to get to the real fine print of the detail.

I think from our side, we're quite comfortable and very excited that this is going to be a very healthy balance and it's going to work.

Connie Weaver – AT&T

Let's go to Laura and then Tom.

Lara Warner – Lehman Brothers

Thanks. I wondered if potentially, Mike and Brian, you could talk a little bit about some of the contracts that AT&T had previously, and specifically, maybe Starz and

CSG. I know Bill Schleyer has been out talking about his views of those contracts. I'm curious as to whether you believe we could potentially see those contracts resolved prior to closing or, Brian, is that something you're anticipating to move across the combined company going forward? And how does that relate to the synergies and margins we see going forward?

Brian Roberts - Comcast

I don't think it's really comfortable or appropriate to do that. I'm sorry. I think that at the 50,000 foot level we don't see any reason, as Steve said, that in the fullness of time both businesses can't function the same.

Connie Weaver – AT&T

Let's come down here to Tom.

Tom Wolzien – Bernstein Research Call

For Steve, last summer you pointed out that one of the reasons that Comcast had been so successful at assimilating other systems and bringing up the margins was really the single element at a time of addition of new products that allowed a disparate workforce to be able to focus on one thing as opposed to others that had blasted everything out at once. Today you're talking about multiple things at once. Why the change?

Steve Burke - Comcast

I think that's a good question, Tom. What Tom's referring to is we have a stated goal of launching a new product every 12 to 18 months, and we do that for a few reasons. From a consumer point of view, I think it's important that the cable industry take the initiative. Satellite's a real competitive and if you ask people right now who has the technological high ground, most consumers will say that satellite is more technologically advanced than cable. So I think over time, as we launch things like high speed data and video on demand and phone, we can change that.

But another reason why we focus on one new product every 12 to 18 months is because our organization, any cable company consists of lots of people doing lots of jobs at different levels in the organization and it is very hard to get those big groups of people doing multiple things well at the same time. Our product plan, we concentrated first on digital, because we thought it was important to protect our base analog business; we concentrated second on high speed data, which right now is the engine that is powering our growth rate and increasing our growth rate; we're very optimistic about that. We are now moving into a phase where video on demand is going to be very important to us for the next 12 to 18 months. And as we talked through this transaction and looked at all the experience that AT&T had with telephony, we came to the conclusion that the next big product after video on demand should be telephony. And that by serendipity the way the deal works, this deal is going to take probably around a year to close, so the timing would be perfect. So at the time that our video on demand, which is currently in about 3 million of our homes, next year we'll at least double that, by the end of next year we'll be in a position to turn our sites to the next big new product for us, which will be telephony.

Connie Weaver – AT&T

Okay, right here.

(Inaudible)

Mike, you've done an incredible job in creating this platform, which is very valuable. Local connectivity is turning out to be one of the probably most valuable assets in this whole process. How are you thinking about the combination with the long distance unit, the consumers side, more from a retail customer perspective as you bundle or partner going forward? And equally important, on AOL, sort of on the data side, is there any carriage agreements with AOL for this process at this point for them to resell your network? How were you thinking about working with the consumer long distance business going forward?

Mike Armstrong – AT&T

The consumer long distance strategy, which I just briefly touched on in the summary, is to enter in the any distance business, in every state that enables an economically viable entry. Right now for next year, 2002, on a UNI P platform, which would give us the local LD combination as well as with data, and that would be a worldnet platform, that's how we'll brand that, we will be in five states. I wish I could say we would be in 45 states, but as you know, we're getting an average of about a 10% discount off list on the UNI P platform and you just can't make money. You lose a lot of money if that's all you get, versus a Michigan, which has a 40+% discount where you could see the margins and the returns.

So we will go, in the consumer long distance business, we will go as fast as we can to compete. And we've already proven in New York that we can gain share, grow the business and we'll be profitable this year, and we hope to get the law judge changed that you know is in process that the PUC is considering.

Second, we will and we are rolling out behind the North Point acquisition of assets that we did, which put us in about 1,400-1,500 local service office so that we can terminate on a facilities based loop a DSL offering, and we will have a high speed local long distance data offering that we will package and we will target market that. And we intend, as long as the loop's available, and something as silly as a (inaudible) bill doesn't get approved and that loop's available, we will facilities-based use that loop for a multiple systems platform offering. And sure enough, as long distance is either overcome in the consumer world due to technology or substitution or competition, we will be targeting to our high value customers, who we know who they are, we have 60 million of them, and turn that curve around and begin to grow off of both that UNI P as well as that DSL offering.

Now, that's going to be something we have to prove to the market that we can do, because everybody that's tried that space, at least in a wholesale equation with DSL, has not been exactly a roaring success in the marketplace. But we have a different equation. We're on a retail equation, we have the customers today, we know who they are, we know where they are and we can target our marketing with that brand. And so I do believe that the consumer long distance business, as it transforms itself from the long

distance to any distance, will have millions of customers and turn a declining revenue business into a growing revenue business going forward.

Will there be a couple of overlaps where consumers might look and say, "Gosh, I can get that from AT&T/Comcast and I can get that from AT&T Consumer," there will be, but let's not take our eye off the ball. Ninety-eight percent of that market is really owned by the RBOC's and for us to have a little, I think the consumer will figure it out. I can get some AT&T phone service over the telephone line or I can get it over the cable line and we'd like them to pick between those two.

Connie Weaver – AT&T

We're going to take two more questions. Let's go to the phone.

Moderator

We have a question from Frank Governelli with Goldman Sachs.

Frank Governali – Goldman Sachs

This is a regulatory question, somewhat related to what Mike just addressed. The Bell Companies have been getting increasingly vocal lately about what they perceive as the imbalanced regulation that applies to cable versus telco's. And today, not too surprisingly, SBC has taken your deal announcement as an opportunity again to complain that your broadband networks are not open to all competitors as the phone companies must be for DSL, despite the fact you control about 70% of the market. Can you articulate your reaction to that and whatever regulatory or legislative actions you need to take in order to prevent regulation of the cable or complete deregulation of the telco's?

Mike Armstrong – AT&T

First, I haven't seen the statement of my good friends at SBC, so I'll have to read what they said, but let me just react to the openness of this network. AT&T has had, and I believe Comcast has had, a statement of policy that we will be open for multiple ISP carriers. You saw during the presentation of Bill Schleyer, when we had to implement the backup network, we were able to implement a network that could accommodate from the get-go a multiple ISP environment. In fact, Bill mentioned that this is a very good business for us in terms of its return as well as a ramping of subscribers. So offering consumers choice of multiple ISP's is in our economic self-interest and it is a policy statement that we're making at this time, and we hope to proceed with the engagement and negotiations of carrying multiple providers on our network.

Connie Weaver – AT&T

Last question, Doug.

Doug (Inaudible)

Brian, you mentioned hitting the ground running. I was just wondering if you could talk about what the transition team can do and what it can't do to make sure that the

integration goes as smoothly as possible and hits the ground running once the deal closes.

Brian Roberts - Comcast

Well, first, they get a good, long rest. But I think we'll, within the appropriateness of making all the regulatory filings and of course you can't get ahead of yourself, these deals do take a while, but I do think there's such a common view you can see there's very little difference in how we're putting emphasis on where the future is, what job has to get done. The working relationship between Steve and Bill and myself and Chuck and Mike, everybody, Larry, that's why we wanted to establish the people who really had put this together, spent the hours making this happen, in the room right off the bat. So I think better than most this is not something that hasn't been thought about in a long time and I really believe we're in good shape.

I'd like to maybe kick that over to Ralph and your overall assessment of our prospects.

Ralph Roberts - Comcast

Most frequently asked question I usually get, I'm surprised it didn't come up here, is did you believe when you were in Tupelo, Mississippi that one day the company would be renamed AT&T/Comcast? And of course my answer is, "Of course I did."

I think you have to really be optimistic about the future. The way we've been operating our company, I don't think we really ever sold anything, and that is because I believe that the industry was such that it's a long-range opportunity and that if you're willing to stick with it through thick and thin, and we've had some ups and downs, too, that you've got a remarkable business. And this particular merger is really quite unbelievable when you could think, as you've heard, all the synergies and everything that's going to come from putting these two large operations together. There's no question about it. Size is a bonus. And if you have the size and you use it intelligently and properly, you're going to end up with something far better than you ever dreamed. I'd like to see our stock keep going up. If you bought 1,000 shares in 1972 when we went public for \$7,000, it would be worth \$3 million today. So we have always been conscious of our folks who've invested in the company and we'll continue to believe that, and there's the opportunity for everybody and we're thrilled to be part of this thing.

Connie Weaver – AT&T

Thank you and what a great note to close on. On behalf of everybody at Comcast and at AT&T, thank you for taking your time to join us. For those of you on the phone, our Web site, where you can find all the information, again, is att.com/ir and cmcsk.com. Have a great holiday and thank you.

APPENDIX 4

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)	
)	
Applications for Consent to the)	
Transfer of Control of Licenses)	
)	
Comcast Corporation and)	MB Docket No. 02-70
AT&T Corp., Transferors,)	
)	
To)	
)	
AT&T Comcast Corporation,)	
Transferee)	

DECLARATION OF HOWARD A. SHELANSKI

I. Statement of Qualifications

1. My name is Howard A. Shelanski. I am Acting Professor of Law at the University of California at Berkeley. I received my B.A. from Haverford College in 1986, my J.D. from the University of California at Berkeley in 1992, and my Ph.D. in economics from the University of California at Berkeley in 1993. I have been a member of the Berkeley faculty since 1997. In 1998-2000 I was on leave from my faculty position to serve as a Senior Economist to the President's Council of Economic Advisers (1998-99) and then as Chief Economist of the Federal Communications Commission (1999-2000). I rejoined the Berkeley faculty on a full time basis in July 2000. I formerly practiced law in Washington, D.C. with the firm of Kellogg, Huber, Hansen, Todd and Evans and served as a law clerk to Justice Antonin Scalia of the U.S. Supreme Court.

2. I teach and conduct research in the areas of telecommunications regulation, antitrust, and applied microeconomics. My recent publications include articles in the *Journal of Law, Economics and Organization*, the *Yale Journal on Regulation*, the *University of Chicago Law Review*, the *Journal of Law and Economics*, the *University of Chicago Legal Forum*, and the *Columbia Law Review*. I am co-author of the recently published legal textbook *Telecommunications Law and Policy* (Carolina Academic Press, 2001). I am a regular participant in academic conferences related to telecommunications policy and antitrust and lecture regularly on both topics at universities in the United States and abroad. My C.V. is attached.

II. Introduction and Summary of Declaration

3. As discussed in detail below, this declaration responds to certain arguments submitted in response to the above-referenced applications for transfer of control of licenses of Comcast Corp. (“Comcast”) and AT&T Corp. in connection with the proposed merger of Comcast and AT&T Broadband, LLC (“AT&T Broadband”) to form AT&T Comcast Corp. (“AT&T Comcast”). Specifically, I demonstrate why AT&T Comcast will not have the ability or the incentive to harm competition for broadband Internet services by withholding content from competing service providers. I also explain why AT&T Comcast will not be able to foreclose competition in broadband content by blocking access to its subscribers and why the merger will most likely only *increase* the losses that would result from, and hence the disincentives to engage in, such foreclosure strategies. In response to concerns raised by some commenters about potential exclusive deals with content providers, I explain that the merger will not affect the incentives or the ability of AT&T Comcast to enter into exclusive deals and, in any event, that it is highly unlikely that exclusive content deals could harm competition. In

addition, as demonstrated below, the merger will not create any power or incentives for AT&T Comcast to cause broadband content producers to diminish output, decrease quality, or raise prices. Finally, I explain why the merged entity will have strong incentives to pass merger efficiencies through to consumers.

III. AT&T Comcast Will Have No Ability to Harm Competition in Broadband Access by Depriving Competing Internet Access Providers of AT&T Comcast's Content

A. AT&T Broadband and Comcast Do Not Have the Content Arsenal Required for Successful Access Foreclosure

4. Several commentators have argued that a larger cable Internet service provider could, by virtue of vertical integration into "broadband" content, foreclose competition on multiple levels of the broadband market and harm consumers. This argument hinges on the idea that a vertically integrated broadband company could use its content as a means to take consumers from competing broadband service providers, and could use its Internet access services as a means to exclude and take customers from competing content providers. Yet the conditions under which such anticompetitive "foreclosure" of markets could occur are very stringent and do not apply to this case.

5. Any claim that a broadband Internet access provider that is vertically integrated into "broadband" content (assuming that separate broadband markets exist in any relevant sense) could harm competing providers of broadband Internet service by withholding its proprietary content necessarily rests on a premise that the broadband content in question is so important to so many consumers that the competitors would be unable viably to compete if their customers could not access that content. I understand that neither AT&T Broadband nor Comcast today owns any significant broadband content at all, much less content that is so compelling that a broadband Internet service

would be disabled without it. More to the point, AT&T Comcast will control a truly insignificant amount of Internet content, even if one counts traditional video content that could be (but today rarely is) accessed via the Internet.

6. Nor could there be any serious claim that AT&T Comcast would be able to disable competing broadband Internet access providers through control of a broadband Internet “portal.” I understand that Comcast owns only a very small-scale portal that does not even begin to approach the range of content contained in the leading Internet portals, and that the content contained on that portal is composed almost entirely of traditional “narrowband” content. AT&T Broadband apparently uses the same portal for its dial up and broadband services and I have been informed that this portal (www.attworldnet.com) will not be acquired by AT&T Comcast. Recent data show that among portals, Yahoo.Com and AOL.com contained, respectively, 136,000 and 97,000 pages. By contrast, Comcast’s portal (Comcast.net) contained 52 pages, while promotional sites operated by Comcast affiliates (such as QVC.com, eonline.com, the golfchannel.com, *etc.*) account for less than 3,000 pages in total.¹ Measured by customer usage, AT&T Broadband and Comcast similarly prove to be minor players in Internet content. Recent data show that usage on the AOL Time Warner Network and Yahoo! portals constituted, respectively, 33.6% and 7.9% of total usage minutes. By contrast, usage on AT&T Broadband’s web sites made up only 0.3% of total usage minutes. Comcast’s limited Internet properties did not even appear on this list of top 50 web and

¹ Page counts are as of May 13, 2002 and were obtained using the “url://” function on altavista.com. Going to altavista.com and typing “url://[website].com” will yield a count of the number of pages on the website and a listing of individual page names. The AT&T portal, “att.net”, has 84,000 pages. However, this primarily narrowband portal will not be part of AT&T Comcast; rather, it will stay with AT&T’s consumer unit.

digital media properties.² At least for the near future, the AT&T Comcast “portal” will, relatively speaking, be a small-scale operation, with nowhere near the breadth or reach of competitors’ portals.

7. The competitive insignificance of AT&T Comcast’s Internet content presence becomes all the more apparent if one looks at the portals that broadband consumers actually use. Among adults in the United States who have residential broadband access, 66 percent regularly visit Yahoo.com’s portal, 40 percent visit Google.com, 39 percent visit MSN.com, 31 percent visit AOL.com, 23 percent visit Netscape.com, 20 percent visit Excite.com, 17 percent visit Lycos.com, and 15 percent visit Alta Vista.com.³ Neither of the merging parties has any presence among these competitors, nor any current affiliation with Excite.com. Even were AT&T Comcast to develop a relationship with a major player on the list, the company would still be only one of numerous, strong Internet portal rivals.

8. Consider, for example, traditional video content that might be transmitted over an Internet connection. As an initial matter, traditional video content comprises an infinitesimal fraction of Internet content. But even if it were to become a significant purpose for which consumers use the Internet, AT&T Comcast will control less than 1% of impressions (a metric of viewership) for cable content rated by Nielsen.⁴ Comcast does own two local sports franchises in Philadelphia and the rights to the transmission of

² “Jupiter Media Metrix Announces U.S. Top 50 Web and Digital Media Properties For October 2001,” *Jupiter Media Metrix Press Release*, November 13, 2001. See http://www.jmm.com/xp/jmm/press/2001/pr_111301.xml. The Excite Network had 0.8% of total usage minutes; however, these sites are no longer affiliated with AT&T or Comcast.

³ Provided via e-mail dated 5/3/2002 by an analyst at Fulcrum Analytics, formerly Cyber Dialogue, Inc.

⁴ AT&T Comcast holdings, excluding TWE networks, account for 0.9% of average prime-time ratings for cable networks. Including the ad-supported broadcast networks in the total lowers AT&T Comcast's share of ratings to 0.4%. Analysis of average prime-time ratings based on compilation of A.C. Nielsen data

some of their games in that market. Even if these games could someday be considered important Internet content – and today the Internet plainly is not a significant outlet for those games – their importance would be local to specific areas for which the teams have rights and in which Comcast already operates cable systems. The merger thus does not affect Comcast’s incentives or ability with respect to the use of its local sports content.

B. Even a Firm with Substantial Content Holdings Would Likely Find Foreclosure an Unsuccessful Strategy

9. Given the vast sea of content that the web offers, and the heterogeneous purposes of consumers that seek access to that content, it would be extremely difficult for any portal’s proprietary content to be sufficiently important that the portal benefits more from withholding the content and trying to take access customers from competitors than it does from letting competitors have the content and thereby expanding the customer base for the content itself. Google.com states on its home page that its search engine searches in excess of 2 billion web pages.⁵ With that much content available to consumers, it is not an easy case to make that any particular content—even “broadband” content—is likely to make a marginal difference sufficient to attract consumers to the particular Internet access provider over which it can be reached.

10. Moreover, the ability to sustain a long-run content advantage over rival portals is difficult if a firm has no structural advantages over those rivals in the development and marketing of “broadband” content. In the absence of such structural advantages, a firm must constantly stay ahead of its competitors on the merits of its products and must continuously innovate to stay in the lead. Such incentives are likely

reported in Kagan World Media’s Economics of Basic Cable Networks 2002 Databook, pp. 60 and 62. The information regarding AT&T Comcast’s ownership of networks is taken from the Application at 15, 25.

beneficial for consumers and represent the very benefits for which competition policy is designed.

11. In any event, even a portal with substantial and important broadband content would have difficulty using that content to harm competing Internet access providers because such rival providers would have access to portals of equal or superior scale and cost structure. AOL and Yahoo, for example, both have relationships with broadband Internet service rivals of AT&T Broadband and Comcast (Yahoo with SBC's DSL service and AOL with AOL Time Warner's cable Internet service).⁶ Any broadband application that either of those portals offered could take advantage of significant network effects and economies of scale. AOL and Yahoo (and the many other large portals) are also large enough to market themselves widely and aggressively like any other major media company. The position of these established portal competitors not only makes it unlikely that any broadband Internet access provider could use content to foreclose, but more fundamentally makes it a steep challenge for any such company even to move into the competitive company of the leading portals, never mind surpass them.

12. Given the strong competitors in today's Internet content market, any firm that attempted to harm rival Internet access providers by withholding proprietary services or content from those rivals would face swift responses that undermine its strategy. Yahoo or another large portal could step in as a substitute available to any Internet access provider blocked from receiving another firm's content. Even if the foreclosing firm's

⁵ "Benefits of a Google Search," Google website, downloaded May 13, 2002, Benefit 1. See <http://www.google.com/technology/whyuse.html>.

⁶ See "Yahoo gets up to speed with SBC," Cnet News.com, November 14, 2001; and "Comcast Offers New High-Speed Internet Options," NewsFactor Network, February 27, 2002.

content were unique, a rival portal of similar scale could, and would have an economic incentive to, replicate that unique content or at least come up with attractive substitutes.

IV. AT&T Comcast Will Have No Incentive to Deprive Competing Internet Access Providers of AT&T Comcast's Content

13. Given the minimal content holdings of AT&T Comcast and the at best fledgling position of AT&T Comcast compared to its content rivals, it is most unlikely that any consumer would subscribe to AT&T Comcast simply because of its content. That being the case, blocking a competing Internet access provider from offering AT&T Comcast content to its subscribers could not be expected to have any competitively significant effect on the relative number of subscribers of AT&T Comcast and the rival. All AT&T Comcast would have accomplished in that case is to lose customers for its content services.

14. Moreover, even if AT&T Comcast could, notwithstanding its extremely limited content holdings, attract *some* customers from rival Internet access providers through content foreclosure, it would still have to ask whether the gain from additional subscription revenues from broadband users would offset the loss in content revenues that occurs when distribution narrows. At AT&T Comcast's current level of presence in the Internet content market, there can be little serious question about where the balance lies: AT&T Comcast has far more to gain by distributing its content widely and attracting demand across the customers of all access providers than it does by limiting the content to its own subscribers and hoping customers of competitors will switch just to get that content. It warrants emphasis that even if AT&T Comcast could profitably limit distribution of its content and attract more customers to its broadband service, such conduct would not necessarily be anticompetitive. Firms differentiate their products all

the time to attract particular customers who value the distinguishing attributes of the firm's good or service. Only if that attribute is so essential that no firm can viably compete without it may a competition policy issue arise. And if government policy reduces firms' incentives to differentiate, then consumers suffer a reduction in the novelty and diversity of products and services available to them.

V. AT&T Comcast Could Not Harm Competition in Content by Blocking Access to Outside Content by AT&T Comcast's Subscribers

15. The previous two sections dealt with allegations that AT&T Comcast could use content to foreclose competition in Internet services. This section addresses allegations that AT&T Comcast could use its position in the broadband Internet services business to foreclose competition in content.

16. The key condition for successful foreclosure of markets to competing content is that, without access to the customers of the blocked system, the competing content cannot reach a sufficient number of customers through alternative access providers to be economically viable. The system that would prevent its customers from gaining access to particular content must be sufficiently large, then, that there would be insufficient customers on other systems to constitute the minimum viable scale for the content at issue.

17. Scale economies for production of broadband content are likely quite different from the scale economies for production of traditional video content. Crandall equates the economics of broadband content with the economics of video content, implying that there are similar scale requirements: "To the extent that the production costs of broadband content (like traditional video content) are fixed and must therefore be spread across large numbers of subscribers, [content] discrimination could force non-

affiliated content providers to operate below minimum viable level of subscribers.”⁷ This analogy is unlikely to hold, for several reasons. First, the fixed costs for the broadband Internet content that overlaps with traditional media have already been covered by traditional video subscribers, music buyers, and other media consumers. Second, as previously discussed, the cost structure for Internet-based publication and sales can be substantially lower than the analogous cost structure for the traditional channels, enabling more competition from small, independent content providers. Third, the user-generated content has very low or no fixed costs associated with its production on-the-fly. As content becomes more heavily segmented and targeted at small groups or even individual users, the minimum viable scale necessarily decreases.

18. In any case, a content provider can achieve substantial scale with or without AT&T Comcast’s subscribers. AT&T Broadband and Comcast together serve only 23 percent of broadband Internet access subscribers.⁸ So even if one assumes that broadband access is the relevant market, then to support the claim that AT&T Comcast can engage in foreclosure against competing content one would have to argue that access to 77 percent of the market does not afford sufficient scale for a content provider to be successful. This is an implausibly strong claim, and one for which no one has offered any evidence whatsoever.

19. Moreover, this 23 percent market-share figure also overstates the proportion of customers that AT&T Comcast could actually block from receiving competing content, given that competing ISPs will soon be operating on their systems. Although AT&T Comcast will serve 23 percent of broadband subscribers, not all of those

⁷ Crandall Declaration ¶ 18.

⁸ Verizon Comments at 9.

subscribers will use AT&T Broadband's or Comcast's ISP services. Instead, some of those subscribers will use competing ISP services. The competing services will act as alternative access points and distribution outlets for broadband content, further complicating any vertical foreclosure strategy.

20. Quite apart from the questions of AT&T Comcast's static market share and the minimum viable scale for competitive content is the critical issue of how blocking content would affect AT&T Comcast's subscriber base. An Internet access provider presumably could make it more difficult to reach disfavored content simply by not listing it on the provider's home page or by dropping the competitor from search results or denying it preferential caching (although I have no expertise or knowledge whether this is, in fact, technically possible or practical). That would be of limited effectiveness, however, because AT&T Comcast's subscribers could easily shift their home page to a different portal (and, as noted, many already do) that does not "block" the content. So AT&T Comcast customers could reach such competitive content directly via an alternative portal or the content provider's own website server. Any attempt by AT&T Comcast to block access to a particular website or to particular content from a website – which broadband providers do not do – would undoubtedly spark an uproar and substantial consumer backlash. The loss of consumers resulting from any attempt to block competing content on the web would almost certainly far outweigh any competitive gains to AT&T Comcast's own content.

21. It is important to keep in mind what AT&T Comcast will sell to broadband consumers: Internet access. Everything else AT&T Comcast does in the broadband market is trivial in proportion to its basic business of providing access to the

Internet and thus to Internet content. If AT&T Comcast were to attempt to deny its customers access to particular content, it would be compromising its basic business in the interests of a product or service (content) in which AT&T Comcast has no identifiable presence and no demonstrated ability to succeed. AT&T Comcast would risk losing a broadband subscriber in the hopes of recouping the losses through content.

22. To consider such a strategy more closely is to see its folly in this case. Every access customer would know that certain content was being blocked and, even if they did not want to use that content, they might well fear that in the future other content that they do care about would also be blocked. Those customers might, moreover, never make any use of the content AT&T Comcast would allegedly be trying to protect from competition. And even if they did, they would probably prefer to have the option of using the competing, blocked content. AT&T Comcast would thus risk sending its customers to DSL or back to dial-up access, simultaneously losing access revenues and losing customers for the very content it was trying to bolster and protect. In sum, a vertically integrated cable company would engage in content discrimination only if it thought that its gains from content sales would offset its losses in access revenues. A company that provides lots of Internet access but very little content, and whose customers depend on it for unimpeded access to those who do have a lot of content to offer, is in poor position to meet this condition.

23. If a firm has important proprietary content, then the gains from withholding it from rivals and from protecting it by keeping rival content away from its own subscribers might in certain circumstances increase as the firm's relative size increases. A larger network footprint could enable the firm to attract more subscribers

from rivals through foreclosure and gain a heightened competitive advantage in both content and Internet access. But unless a firm can profitably engage in foreclosure to begin with, increased firm size may in fact increase the net costs of any foreclosure strategy. Indeed, one would not predict that a foreclosure strategy would be successful post-merger, unless the individual firms had been profitably foreclosing competitors prior to the merger. If denying content to rivals pre-merger would only have led to a loss of content revenues without gain of compensating access revenue, then spreading the strategy over a larger footprint would only magnify the losses. Given that neither AT&T Broadband nor Comcast can use its content to attract subscribers or benefit its own content by blocking access to rival content by its subscribers, the merger will only increase the potential losses from, and hence disincentives to engage in, such foreclosure strategies.

VI. The Merger Will Not Affect AT&T Comcast's Incentives to Enter Into Exclusive Content Deals

24. As a threshold matter, it is important to recognize that exclusive deals may be highly beneficial and pro-competitive, particularly in a nascent industry like broadband. Potential developers of broadband applications and content face substantial risk and uncertainty about the size of the market for their products and the possibility of engaging in substantial R&D only to find they have been beaten to market by another entrant. Exclusive deals with Internet access providers help to ease the risk by assuring the content provider of carriage to a number of customers. The access provider, in return, gets the chance to get a leg up on its competition by having a unique product to offer consumers. Exclusivity can, therefore, potentially reduce the risk both parties face in

developing and introducing new broadband services, the demand for which may be very speculative.

25. Exclusivity may, of course, be used anticompetitively. If either the seller or the purchaser of the product in question has an extremely large market share, then a large portion of either the upstream or downstream market will be foreclosed from competition. But in order for such an arrangement to harm competition, it is necessary (although not always sufficient) that the content (a) make such a difference to consumers that they will only subscribe to an access provider that has it, and (b) have no substitutes that are available to Internet access competitors from providers other than the foreclosing firm. Neither of these conditions holds for current AT&T Broadband or Comcast arrangements and neither seems likely to hold for any exclusive deals that AT&T Comcast might enter into.

26. First, consider condition (a). For all the reasons already mentioned, it would be difficult for any specific content to tip a critical mass of consumers towards any particular access provider on which that content was exclusively available. That content would have to stand out from the vast universe of applications and content on the Internet and be so compelling that consumers are willing to incur the costs of switching from one ISP or portal to another. Plainly, AT&T Broadband and Comcast have no such content today. Moreover, even if the content did prove so important, policy makers should hesitate before declaring its exclusive distribution to be anticompetitive. Would the content have even been produced without the risk-managing properties of an exclusive deal? If not, then the gains to consumers may outweigh the costs.

27. Consider next condition (b). The content at issue would have to prove sufficiently difficult for the large, experienced rival content companies to replicate or surpass. Yet those rivals would have enormous incentive to enter the market because faced with the make-or-break situation created by condition (a), rival access providers to the one who has the exclusive agreement will be willing to devote a substantial portion of their rents to obtaining a substitute source of such critical content. The exclusivity in this way may prevent the original producer of the content at issue from obtaining a monopoly in its relevant market and may induce competitive development of broadband content.

28. Both conditions (a) and (b) are quite stringent, and it is important to remember that neither of them is close to being present in the current broadband marketplace. They are especially remote for AT&T Broadband and Comcast. With a combined 23 percent of broadband distribution, the companies cannot individually or in combination foreclose enough of the Internet access market to push rivals out or to dissuade entry upstream in the content market. With an immeasurably small share of the Internet content market and a miniscule share of the traditional video content market, the companies have no comparative expertise in developing or identifying content to be distributed exclusively. Even if they did obtain such content, the companies would face immediate competitive response from rivals dealing with other major players at the content level of the broadband market or developing it in-house

29. The merger between AT&T Broadband and Comcast does nothing that would presumptively change the firms' incentives to sign exclusive content deals. Exclusivity is costly. Any content provider that agrees to be distributed on only one system in a geographic market immediately accepts a smaller addressable market for its

product. In return for accepting fewer users, the content provider must be paid a higher price for each user it can reach. AT&T Comcast would thus have to pay for exclusivity and hope that the higher price is compensated for by the additional access revenues that come from attracting subscribers away from the rivals that do not have the content at issue.

30. A merger can affect the price of exclusivity in a number of ways, depending on what the merger does to the market share of the party seeking to have exclusive distribution rights. The critical question is whether the merger increases the proportion of total consumers that the Internet access provider with exclusive rights would serve. If that proportion increases, the price of exclusivity should fall. If the proportion decreases for some reason or stays the same, then the price of exclusivity should either rise or stay the same. So, suppose a cable operator serves 75 percent of the MVPD customers in its geographical markets, with DBS providers serving 20 percent and an overbuilder serving the remaining 5 percent. If the cable operator were to merge with the overbuilder, its geographic market share would rise to 80 percent, content distributed exclusively by the cable operator would miss only 20 instead of 25 percent of consumers in the market, and the content owner would demand a lower price for exclusivity due to this reduced opportunity cost. The key factor here is that the merger reduces the proportion of competitively served consumers.

31. Consider, in contrast, a cable operator that merges not with a direct competitor within its geographical market, but with another cable operator that serves distinct geographic markets. Suppose each of the geographic markets has the 75 percent/20 percent/5 percent structure described above, but this time the two 75 percent

share cable systems merge. If each of them has an exclusive deal in its territory with the content provider at issue, then the merger will change nothing in the costs and benefits of exclusivity. The content provider will still only reach 75 percent of consumers in each market and will demand compensation for the opportunity costs of not serving the other 25 percent. Similarly, the benefits to the cable operators do not change as together the cable systems still place no greater pressure on rival providers than before the merger. That is the situation here.

32. Even if two firms could, by merging, extend the territory over which an exclusive deal applies and thereby increase the potential benefits of the deal, they would simultaneously increase the price they paid for exclusivity. After the merger, the content owner would face not just the opportunity costs of foregone customers in one firm's geographic market, but in the merger partner's market as well. The merged firm would therefore have to pay twice for exclusivity even as it gains twice from the practice. The increase in size achieved through merger thus does not have any systematic net effect on the firms' incentives to engage in exclusive dealing.

33. It is no answer to the above analysis to say that the second exclusive agreement might not come at an increased cost to the Internet access provider because the content provider would be guaranteed distribution where previously, perhaps, it had none. For such a scenario violates both of the conditions necessary for effective exclusivity: it implies either (a) that the content at issue was not so competitively important that broadband providers had to offer access to it, or (b) that there were substitutes for the exclusive content in the second market that would presumably still be available to rivals

if the exclusive agreement were geographically extended through merger. Either one of these is enough to defeat any competitive harm from exclusivity.

34. Because AT&T Broadband and Comcast serve distinct geographic markets, their merger will not increase the relevant market share reached by any exclusively distributed content. The costs of exclusivity will not decline and will increase with any extension of the exclusivity into markets where it previously might not exist. The merger therefore will not affect the incentives or ability of the merging firms to engage in exclusive deals with content providers. Combined with the fact that it is most unlikely that any such deals could harm competition, while they may in fact help to introduce valuable new services, the issue of potential exclusive deals between AT&T Comcast and broadband content providers should be of no regulatory concern.

VII. The Merger Will Not Create Monopsony Power for AT&T Comcast in the Broadband Content Market

35. The merger will not create any power or incentives for AT&T Comcast to cause broadband content producers to diminish output, decrease quality, or raise prices. As with video programming, Comcast and AT&T Broadband are non-rivalrous in their procurement of Internet content. Many of the other arguments for why AT&T Comcast will have no monopsony power in traditional video content apply—and even more strongly—to the acquisition of broadband content. I therefore wish to incorporate by reference the monopsony arguments made by Professor Ordovery in his accompanying Declaration. Several specific points relevant to broadband content acquisition bolster the case refuting monopsony.

36. First, AT&T Comcast's 23 percent share of broadband access customers nationwide affords broadband content providers an enormous alternative market for their

products should AT&T Comcast try to drive too hard a bargain. One would have to make the case that the minimum viable scale for broadband content is virtually the entire market to find monopsony potential in a 23 percent share. There is no evidence for such an exceptionally strong assumption. Moreover, any one firm's consumption of broadband content does not affect the ability of other parties to purchase the same content. So any individual firm's conduct in procuring content—even conduct by a very large firm—will have much less effect in the Internet content market than in the market for a conventional, rivalrous good.

37. Second, any broadband content so important as to drive Internet access providers to bargain to obtain it on specific terms, as opposed to simply letting customers find it on their own on the Internet, is likely to place the content owner in a very strong bargaining position. Even a monopoly access provider would face the prospect of attracting fewer customers without the content at issue and would therefore at best find itself in a bilateral monopoly situation. Of course, AT&T Comcast would not be anything close to a monopoly provider of broadband Internet access and would therefore likely find itself in a bargaining position inferior to that of the content owner.

38. Third, and very importantly, broadband content is distinct from MVPD video content in that it can be sold directly to consumers and bypass the cable operator entirely. Unless an access provider is going to take the unprecedented and probably fatal step of blocking customers' access to the general Internet, a broadband content provider can refuse to sell to any particular Internet access provider or portal and instead let consumers obtain it directly over the Internet. Broadband access providers are thus intermediaries but not necessarily bottlenecks when it comes to Internet content. They

realistically can only become bottlenecks at the election of the content provider to strike an exclusive deal. And in this regard the access provider's bargaining power is limited not only by the presence of other access providers in the content procurement market, but by the powerful presence of consumers who can cut out the intermediary and buy their content directly. Any exercise to prevent direct purchases by consumers will drive them to AT&T Comcast's rivals.

39. Even if, contrary to reality, one assumed AT&T Comcast had monopsony power, it would have little incentive to exercise it. The success of broadband access depends on the availability and quality of complementary content and applications. Any savings AT&T Comcast might therefore obtain through monopsony it would risk losing, with interest, through foregone access revenues. Under competition from DSL and dial-up access, any savings from monopsony might in addition have to be passed through to consumers to stop them from dropping their service. The end result would be a counterproductive mix of lower revenues and fewer customers for the monopsonist.

VIII. AT&T Comcast Will Have Strong Incentives to Pass Merger Efficiencies Through to Consumers

40. AT&T Broadband and Comcast have provided an itemized estimate of the cost savings that should result from this merger.⁹ For purposes of this declaration I take those efficiencies as given and do not provide independent analysis or verification of them. The issue I herein address is whether, assuming those efficiencies do result, consumers will benefit from them. I conclude that, because AT&T Comcast will have strong incentives to reduce prices and expand output to customers, savings from the merger will result in savings and other benefits for consumers.

⁹ See Application, Ex. 9.

41. The case for pass-through of efficiencies is compelling for a firm that faces competition, particularly competition as vigorous as that in the MVPD market. Where there is competition, prices tend to track marginal costs. This is not to say that prices will be set *at* marginal costs. It is well understood that for products that have very high fixed costs and comparatively small marginal costs of production, the long-run equilibrium prices must be in excess of marginal costs. Otherwise the firms would lose money, cease to produce and innovate over time, and waste resources. Video programming is a good for which marginal costs of distribution are negligible but the fixed costs of distribution are very high. The more customers that an operator can serve with its network, the lower the share of these fixed costs that any individual consumer must share and the lower the marginal cost to the operator of distributing programming. Similarly, if a cable operator can achieve procurement efficiencies that lower its costs of obtaining programming to distribute, the operator enjoys lower marginal costs in adding programs to its offerings. A profit maximizing cable operator will then provide more programs at lower prices to consumers. Thus, a merger that expands the number of customers over which programming costs can be distributed and that allows cost-savings in the procurement of that programming will give an operator the opportunity to offer its greater pool of customers more programs at lower prices.

42. Economists generally accept that any firm, even a monopolist, maximizes profits by passing through a portion of marginal cost savings to consumers. For, as costs decline, the profit-maximizing level of output expands and the profit-maximizing price accordingly declines. This is true even for a non-competitive firm that decides price and output levels not based on the marginal cost of production, but on the marginal revenues

of output. For the lower the costs of such a firm, the higher the level of output at which marginal revenues will continue to accrue to the firm. There is, consequently, always going to be some pass-through of cost savings for consumers so long as a firm can increase its output and hence its sales.

43. As discussed above, even a monopolist would have an incentive to take such an opportunity to lower prices and attract additional subscribers. Cable operators are not, however, monopolists and have much stronger incentives to pass through an even greater proportion of any cost savings. As is well documented by Professor Ordober in his accompanying declaration, cable operators face substantial competition from DBS providers. Notwithstanding the contorted efforts of some commentators to dismiss the competitive value of DBS, the market data strikingly illustrate the rivalry between the two kinds of MVPD service. *See Ordober Declaration ¶¶ 16-19, 73, 79.* Even putting aside the other market forces that put competitive pressure on cable operators, the need to battle DBS for every new customer and to retain existing customers will make it highly likely that consumers will share in the efficiency gains from this merger. Reductions in the direct costs of procuring programs will result in both a lower cost per-program for subscribers and in an increased number of programs being made available to subscribers. Every foregone opportunity to provide such consumer benefits is a foregone opportunity for AT&T Comcast to defend its market share from its fast-growing DBS rivals.¹⁰

44. Efficiency gains from the merger may also be passed through to consumers in a less direct way through increased investment in network upgrades and the development and deployment of innovative services. Reductions in current prices and

increases in current output are definitely welfare increasing. But welfare also increases as a result of longer-term investments that improve the quality and range of services a cable operator provides to its subscribers. Increased operational efficiencies add to the resources available for such investment, which provides a second avenue through which merger efficiencies will be passed through to consumers. Competitive pressures drive such dynamic activity no less strongly than they do more immediate price and output benefits for consumers.

45. Dr. Robert Crandall has suggested in his declaration that the competitive landscape is tilted in favor of cable Internet service providers and against DSL rivals because of the disparate regulatory burdens that the respective kinds of service have. The fact that DSL providers are subject to regulations that do not apply to cable Internet service operators does not change the fact that DSL is an important competitor that places great pressure on cable Internet service providers to pass through efficiencies and compete for customers. More fundamentally, however, regulatory parity between two industries is not an issue to be resolved in a case-specific adjudication of a transaction between two firms. The regulation of DSL is an important topic in its own right and is the subject of pending proceedings before the FCC, but it is not within the scope of this merger-specific inquiry.

IX. Reduced Program Procurement Costs Should Not Be Confused with Monopsony Power

46. One of the merger-specific efficiency gains discussed in Mr. Pick's declaration is the ability of the combined company to purchase programming at a lower

¹⁰ In the top 10 major urban markets, DBS penetration averaged an increase of 120% between year-end 2000 and May 2002. See Horizon Media Newsletter, February 2000; Nielsen Media Research, DMA Household Universe Estimates: May 2002.

cost. This ability does not stem from any creation of monopsony power by the merger. AT&T Comcast's lack of monopsony power has been discussed in great detail in Professor Ordovery's declaration and is also discussed above in this declaration, in the context of Internet content. In no way does the ability of the combined firm to purchase programming at lower cost contradict those discussions. As a threshold matter, bargaining power and monopsony power are very different things. Bargaining power is simply the ability of a firm to obtain a greater allocation of the rents from a transaction. If a larger buyer can get a better price from a seller, that generally only means that the seller is taking a lower, but still positive, profit on the transaction. No harm flows from such bargaining power and, to the contrary, it may create substantial consumer benefits.

47. Consider a powerful programmer whose shows command significant viewership. Such a programmer can charge prices substantially above its costs to a cable operator that distributes such programming. Viewers demand it, and failure to provide it will reduce subscription levels, particularly in today's vigorously competitive MVPD market. If a cable operator can reduce the profit margins it pays to programmers and, in turn, passes them through to consumers in some part, then the cable operator has obtained a benefit for itself and its subscribers without any harm to the programming market.

48. In addition, procurement efficiencies are not solely the result of bargaining power. Program producers may charge lower prices to a large video distributor for a variety of reasons, including reduced transaction costs of negotiation and distribution, greater certainty about the number of potential viewers, and hence prospects for success, for a particular program (especially during the early phases of the launch), and promotional undertakings on the part of the distributor. Purely cost-based procurement

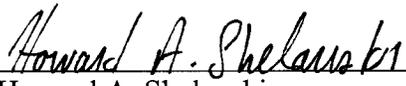
efficiencies have nothing to do with bargaining power at all and hence are equally independent of monopsony consideration.

49. In sum, efficiencies from this merger will benefit consumers. AT&T Comcast has strong incentives to pass through at least a portion of their cost savings to subscribers in order to increase both market share and the size of the MVPD market itself. To the extent the cost savings at issue result from reduced procurement costs, those are benefits that should be embraced without reservation. Procurement efficiencies are real benefits that neither depend on, nor give rise to, monopsony power.

X. Conclusion

50. For the reasons set forth in the sections above, I conclude that the merger between AT&T Broadband and Comcast will not harm competition and promises benefits for consumers. Specifically, my analysis demonstrates that AT&T Comcast will have neither the ability nor the incentive to harm competition for broadband Internet services by withholding content from competing service providers. Moreover, AT&T Comcast will not be able to foreclose competition in broadband content by blocking access to its subscribers and would most likely suffer greater losses post-merger from such foreclosure strategies than either firm would have suffered pre-merger. I also conclude from my analysis that the merger will not affect the incentives or the ability of AT&T Comcast to enter into exclusive deals and that any such deals would, in any case, be most unlikely to harm competition. Nor will the merger create any power or incentives for AT&T Comcast to engage in monopsony conduct. Finally, subscribers will benefit from AT&T Comcast's strong incentives to pass merger efficiencies through to consumers.

I, Howard A. Shelanski, declare under penalty of perjury that the foregoing declaration is true and correct. Executed on May 16, 2002.



Howard A. Shelanski

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Ph.D. 1993; M.A. 1989

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B.A. (history) with high honors, 1986

Phi Beta Kappa; varsity track and cross country

Current Position

University of California at Berkeley, School of Law

Acting Professor of Law. Teaching areas include antitrust law, telecommunications law, regulated industries, and contract law.

Experience

Federal Communications Commission, Washington, D.C.

Chief Economist. 1999-2000.

President's Council of Economic Advisers, Washington, D.C.

Senior Economist, responsible for issues of industrial organization, competition policy, regulation, and trade, 1998-99.

Kellogg, Huber, Hansen, Todd & Evans, Washington, D.C.

Associate, telecommunications and general litigation practice, 1995-97.

Law Clerk to Justice Antonin Scalia, United States Supreme Court,
1994-95.

Law Clerk to Judge Louis H. Pollak, U.S. District Court, Eastern District of
Pennsylvania, 1993-94.

Law Clerk to Judge Stephen F. Williams, United States Court of Appeals, D.C.
Circuit, 1992-93.

Other

Speak French and Spanish;

Enjoy brewing beer, outdoor sports, travel, and playing the double bass;

Admitted to the Bar in the District of Columbia and Pennsylvania.

Howard A. Shelanski, p.2

**Research &
Publications**

"Robinson-Patman Act Regulation of Intraenterprise Pricing," (comment), 80 *California Law Review* 247 (1992).

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"Pricing Access to Incumbent Telecommunications Networks: The Law and Economics of *Verizon v. FCC*," working paper, October 2001.

"From Sector-Specific Regulation to Antitrust Law for U.S. Telecommunications: The Prospects for Transition," forthcoming, *Telecommunications Policy*, Spring 2002.

"Regulation in an Evolving Network Industry: the Case of Broadband Communications," working paper, March 2002.

APPENDIX 5

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554**

In the Matter of)	
)	
Applications for Consent to the)	
Transfer of Control of Licenses)	
)	
Comcast Corporation and)	
AT&T Corp., Transferors,)	MB Docket No. 02-70
)	
To)	
)	
AT&T Comcast Corporation,)	
Transferee)	
)	

**DECLARATION OF
JANUSZ A. ORDOVER
ON BEHALF OF AT&T CORP.**

I. QUALIFICATIONS

1. My name is Janusz A. Ordover. I am Professor of Economics at New York University, which I joined in 1973. At New York University, I teach undergraduate and doctoral level courses in industrial organization economics, the field of economics concerned with competition among business firms and upon which “antitrust economics” is founded. I have devoted most of my professional life to the study and teaching of industrial organization economics and to its application through antitrust and regulatory law and policy.

2. In July 1991, President George Bush appointed me to the position of Deputy Assistant Attorney General for Economics in the Antitrust Division of the United States

Department of Justice (“DOJ”). In this post, I participated in the drafting of the 1992 Horizontal Merger Guidelines, which have been widely used by courts and antitrust enforcement agencies. In addition, I led many merger reviews that employed and developed methodologies to define relevant markets in merger and other cases. I returned to New York University in 1993.

3. I have been actively involved in the formulation of public policy in the telecommunications sector. I have submitted written and oral testimony for AT&T Corp. (“AT&T”) to the Federal Communications Commission (“Commission” or “FCC”) and to state regulatory commissions in the Midwest, New England, and New York on a number of issues, including the pricing of unbundled network elements and access to bottleneck facilities.
4. I have written extensively on a wide range of antitrust and telecommunications topics, such as mergers and joint ventures, predatory conduct and entry barriers. My antitrust articles have appeared in the *Yale Law Journal*, the *Harvard Law Review*, the *Columbia Law Review*, and many other journals, monographs and books, here and abroad. A full list of my articles and other professional publications and activities is presented in my *curriculum vitae*, which is attached as Exhibit 1.
5. I have lectured extensively on antitrust topics to the American Bar Association, the International Bar Association, and the Federal Trade Commission (“FTC”). I have also lectured on regulatory and antitrust policy at colleges and universities in the United States

and abroad, and at many conferences and meetings sponsored by various legal organizations.

6. I have acted as a consultant on antitrust and other competition matters to the DOJ, the FTC, and the post-communist governments of Poland, Russia, and Hungary. I have also consulted for the World Bank, the Inter-American Development Bank, and the Organization for Economic Cooperation and Development in Paris on regulatory and competition policy matters. I have acted as a consultant in numerous antitrust civil actions and investigations, including market definition and competitive conduct matters for the FTC, DOJ and private clients in the United States, Australia, Germany, the United Kingdom and the European Union. I have extensive experience in the analysis of competitive effects of business strategies, including tying and bundling. I have also testified in numerous federal regulatory proceedings following the passage of the Telecommunications Act of 1996.

II. INTRODUCTION AND SUMMARY OF TESTIMONY.

7. One of the main purposes of this testimony is to demonstrate that market conditions and dynamics and unique characteristics of video programming create a particularly poor environment for any anticompetitive exercise of buyer market power by even a very large cable company.¹ I have previously made these points in the context of the Commission's

¹ In this declaration, I use the term "buyer market power" to refer all forms of market power that can theoretically be exercised by a cable company that purchases video programming – *i.e.*, monopsony power and foreclosure power (either to favor affiliated programming or to harm rival programming distributors).

rulemaking proceedings that have addressed these issues on an industry-wide basis.² Here I further elaborate why, for various reasons including the non-rivalrous nature of programming, the ubiquitous presence of Direct Broadcast Satellite (“DBS”) and other alternatives to cable, the many non-multiple video programming distributor (“MVPD”) alternatives open to suppliers of video programming, and the high costs and dubious benefits of foreclosure in the context of cable distribution of content, exercise of anticompetitive buyer power is unlikely. I shall also examine these issues in the context of the proposed AT&T Broadband/Comcast transaction.

8. Indeed, although the precise level at which serious buyer market power concerns might arise continues to be debated in ongoing rulemaking proceedings, I am not aware of any evidence (or even a serious argument) that a cable company that serves only 30 percent of MVPD subscribers – even a cable company substantially vertically integrated into programming – would have the incentive and ability to take anticompetitive actions against suppliers of video programming that would reduce the supply or quality of programming. And buyer market power claims are even less plausible in the specific context of the proposed AT&T Broadband/Comcast transaction, because, as I explain below, those companies have quite limited programming interests.

² In particular, I have submitted two statements on behalf of AT&T regarding the Commission’s cable horizontal ownership limit. See Janusz A. Ordovery, *The Perils Of Static Analysis Of Unduly Narrow “Markets”: Why Even A Cable MSO That Served 45 Percent Or More Of All Current MVPD Subscribers Would Pose No Threat To Video Programmers Or Consumers*, CS Docket No. 98-82 (filed October 1, 1999) (“Ordovery White Paper”); Declaration of Janusz A. Ordovery, CS Docket No. 98-82 (filed Jan 4, 2002) (“Ordovery Cable Rules Dec.”).

9. In this declaration, I respond to the contrary claims of several commenters, primarily the Regional Bell Operating Companies (“RBOCs”). The RBOCs, both in their comments and in their supporting economic declarations, make clear that their primary concern is not with the merger of AT&T Broadband and Comcast but with the regulation of their own high-speed Internet offerings. Although there are a number of misstatements and gaps in logic associated with the “regulatory parity” arguments that they craft in an effort to link their concerns with this merger,³ I understand that the appropriate regulatory treatment of the RBOCs’ services is not at issue here and is being addressed by the Commission in unrelated rulemaking proceedings. I therefore limit my analysis to the monopsony and other video programming-related economic arguments made by the

³ The RBOCs’ premise that DSL-based services are struggling is false. “The proliferation of DSL in the telecom industry has seen one of the fastest technology adoption rates ever recorded.” Robertson Stephens, *DSL Market: Demand Doesn’t Seem To Be An Issue, But Carrier Deployment Execution Does* (January 3, 2001). Verizon reports that its DSL subscriptions increased 122 percent in 2001, Qwest announced a 77 percent increase in DSL customers in 2001, and SBC announced a 69 percent increase. See News Release, *Qwest Communications Reports Fourth Quarter, Year End 2001 Results, Jan. 29, 2002*; News Release, *SBC Reports Fourth-Quarter Earnings* (Jan. 24, 2002). For the first quarter of 2002, SBC expanded its customer base to more than 1.5 million lines, Verizon has 1.35 million DSL subscribers with approximately 150,000 net additions in the quarter, BellSouth added 108,000 DSL customers and now has 729,000 retail customers, and Qwest has 484,000 customers. See http://www.sbc.com/investor_relations/financial_and_growth_profile/investor_briefings/0,5931,272,00.html; <http://investor.verizon.com/financial/quarterly/VZ/1Q2002/1Q02Bulletin.pdf>; <http://bellsouthcorp.com/proactive/newsroom/release.vtml?id=40063>; http://media.corporate-ir.net/media_files/NYS/q/q_4_30_02earnrel.htm. “[T]he number of ADSL subscribers is growing faster than the number of cable subscribers.” *Third Section 706 NOI*, 16 FCC Rcd. 15515, ¶ 16 (Aug. 10, 2001).

RBOCs, a coalition led by Consumer Federation of America and Media Access Project (“CFA”), RCN, and EchoStar.⁴

10. The merger opponents raise three “vertical” video programming-related concerns regarding the proposed transaction. First, they contend that because AT&T Comcast will serve about 30 percent of current MVPD subscribers, it will gain “monopsony power” over video programming suppliers, causing a reduction in the overall volume and quality of programming. Second, they claim that AT&T Comcast will have the incentive and ability to refuse to carry unaffiliated programming that competes with its own affiliated programming and that this “foreclosure” will substantially harm the unaffiliated programmers and enable AT&T Comcast’s programming affiliates to charge monopoly prices to other MVPDs. Third, they claim that AT&T Comcast will have the incentive and ability to cripple its MVPD rivals by refusing to allow them to distribute AT&T Comcast programming or to use AT&T Broadband’s Headend-In-The-Sky (“HITS”) digital programming aggregation and transmission service.
11. I explain below why these claims are not plausible. I note at the outset, however, that these merger opponents have provided remarkably little in the way of support for their claims. Although each of the RBOCs and CFA have submitted economic declarations, these declarations contain little beyond general discussions of the economic theory of buyer market power followed by bare assertions that AT&T Comcast will be large

⁴ These commenters also make buyer market power (and other) claims with respect to high-speed Internet services. Those claims are addressed in the separate declaration of Professor Howard Shelanski.

enough (and have incentives) to exercise such market power. Professor Carlton (on behalf of Qwest and SBC), for example, simply urges the Commission to have a look at the buyer market power allegations made by others (and to “remedy” any problems it might find by deregulating the RBOCs).⁵ A thorough and careful analysis of these allegations, however, confirms that the merger will not endow the merged company with anticompetitive buyer market power over suppliers of video programming, and will not create incentives for anticompetitive foreclosure of rival unaffiliated programmers or MVPDs.

III. OPPONENTS OF THE MERGER DO NOT ADEQUATELY DEAL WITH THE MOST RELEVANT BUYER MARKET POWER CONSIDERATIONS.

12. A buyer who exercises buyer market power imposes on the seller anticompetitive demands and forces the seller to part with its product on terms that are somehow economically unsatisfactory. The net effect of the exercise of such power, in the current context, would be a reduction in the supply of cable network programming as well as a potential reduction in the quality of such programming. Any reasoned analysis of buyer market power and its effects must therefore begin with the analysis of the bargaining (negotiations) between the buyers of cable programming content and suppliers of such content. Briefly, such analysis must deal with basic questions about the seller’s alternatives and the credibility of the buyer’s threat.

13. *First*, traditional buying power arguments are inapplicable here. Basic economics teaches that a fundamental prerequisite of buyer power is that the firm faces an upward

⁵ Qwest, Carlton Dec. ¶ 7.

sloping supply curve for the product (input) in question. In such a situation, a firm with buyer power has an incentive to restrict its purchases of the product in order to reduce the product's price below the competitive level. The economic harm flows from depressed prices and repressed volume of purchases.

14. These market conditions, which are a predicate to any exercise of buyer power, do not exist with respect to video programming. The consumption of a video programming network by a particular MVPD has no impact on the supply of the programming available to other MVPDs. This characteristic of video programming of course undermines any claim that an MVPD provider could exercise "traditional" buyer power to affect the price of video programming it procures for its cable systems.
15. Furthermore, because of the highly differentiated nature of video programming services, a cable MSO does not set a uniform price for all programming content it buys. Rather, the MSOs, small and big, negotiate distinct contracts with each network provider. In such a setting, it is well known that all the parties have an incentive (and also the ability) to reach an efficient bargaining outcome that conduces to efficient quantity and quality of programming.
16. *Second*, and most obviously, any determination whether a purchaser of a product (or service) is likely to possess market power over suppliers of that product requires consideration of all of the realistic alternatives available to the suppliers, because a supplier's production decisions – and, accordingly, its susceptibility to the exercise of market power by any purchaser – are necessarily a function of the alternative channels for

sale or distribution of the supplier's product. A supplier of video programming that is denied carriage by a cable company can turn not only to other cable companies (both incumbents and overbuilders), but also to DBS providers that have nationwide coverage as well as SMATV and other MVPD purchasers of video programming who also offer venues for the delivery of network programming services. Moreover, the content that comprises these network programming services can be (and often is) also distributed in other venues, including not only via U.S. broadcasters, and video-on-demand, videocassette and DVD distributors, but also foreign broadcasters and cable and satellite distributors. As I explain below, the presence of these alternative revenue or distribution sources is highly relevant to any inquiry into the extent to which video programmers require carriage on particular cable systems to cover their costs and thus to any claim that a cable MSO has buyer market power over suppliers of programming. Moreover, the presence of these alternative sources of revenue is also relevant to the analysis of "quality" decisions by video programmers.

17. *Third*, in gauging the ability of a cable operator to "exploit" the programmer one must consider the credibility of the buyer's threat to deny carriage, or to refuse to pay its "fair share" of programming costs. Where, as here, the product in question is an input into the buyer's own products, a reasoned analysis of buyer market power must consider whether a buyer's mistreatment of suppliers that causes a reduction in the quality or quantity of supply of the input product (the only circumstances in which there could be a legitimate public interest concern) would undermine the competitiveness of the buyer's *own* product or otherwise impose costs on the buyer. If so, the buyer could lack the incentive to

exercise buyer market power. Cable operators face retail MVPD competition in all markets from DBS providers (and in some markets from other MVPDs) and also compete with over-the-air broadcasters and others for viewers (and advertising dollars). There is overwhelming evidence that quality and quantity of programming are key competitive drivers and that customers can and do switch if dissatisfied with the programming being delivered. Because the incremental costs of serving additional customers in a built-out cable system are very low, a substantial share of the revenues lost as a result of myopic programming choices would otherwise directly impact the bottom line. The opportunity costs associated with failing to carry programming desired by consumers are therefore very high, and bad programming decisions are very costly even if only a very small percentage of the cable operator's customers vote with their feet (or more exactly, with their eyeballs).

18. Moreover, cable operators have increased cable channel capacity significantly since 1992. This cable channel capacity needs to be filled with attractive programming to make the enormous investments in building that capacity economic. Spurred by competition from DBS, cable operators have been spending billions of dollars to upgrade their systems to provide comparable capacity.⁶ This increase in cable channel capacity further diminishes the relative importance of AT&T-Comcast as a distribution outlet. As the Commission has recognized, increased channel capacity means that a programmer

⁶ Stratecast Partners, *U.S. Cable MSOs: Strategic Market Assessment & Forecast 7* (Sept. 2001) (noting that cable operators' "plant upgrades were/are mandatory, not optional, as part of their efforts to grow their businesses and compete effectively against current and future combatants including DBS and telecommunications service providers").

denied carriage by one MSO is much more likely to be able to obtain carriage by another MSO.⁷ Moreover, AT&T Broadband's and Comcast's own affiliated programming is wholly inadequate to satisfy the merged entity's programming needs.

19. *Fourth*, in gauging the buyer power concerns one must also consider whether the sellers themselves have market power or otherwise have the ability to protect themselves (through contractual or other mechanisms) from opportunistic behavior by cable operators. As several of the opponents of the merger concede, there can be little doubt that cable operators (and other distributors) view many video programming networks as "must have" programming. Indeed, as RCN points out, even "niche" programming networks that appeal to a small subset of subscribers may have significant power over distributors because that subset of viewers values the programming very highly and would switch to DBS (or cancel service) if it was not offered. Moreover, most programming networks are owned by large media companies that routinely "bundle" their most popular networks with new and other, less popular offerings and thereby create incentives for distributors to carry even programming that many consumers do not value particularly highly, rather than foregoing the ability to carry the most desirable programming.

20. Many programmers are themselves affiliated with other MSOs. If an MSO tried to foreclose a programmer, then the affiliated MSO could retaliate and refuse to carry

⁷ See Report and Order, *Amendment of Section 73.658(g) of the Commission's Rules - The Dual Network Rule*, 16 FCC Rcd. 11114, ¶ 12 (2001) ("*Dual Network Rule Order*") ("the increase in channel capacity provides video programming producers a greater opportunity to distribute their programming to consumers").

programming affiliated with the foreclosing MSO. Also, an MSO such as AT&T Comcast would be quite limited in its ability to withhold carriage from a programmer due to the structure of contracts in the industry. Typically, programming is provided to a cable operator pursuant to a long-term contract, usually lasting between five to ten years, with one or more five-year renewal options, although it is not uncommon to observe contracts as long as fifteen years.⁸

21. *Fifth*, the analysis of the various market factors that bear on the issue of monopsony power necessitates a *dynamic*, not *static*, exercise that recognizes the changing nature of the video marketplace as well as the obvious fact that consumers respond to market signals, shifting to suppliers that provide improved price and quality and away from those that do not. Likewise, suppliers also respond to market signals, targeting rivals that falter by failing to optimize the quality of their consumer offerings. Although static market shares can, in some contexts, serve as meaningful proxies for market power, this is not such a context.⁹
22. Thus, for example, a cable operator's incentives and ability to take actions that would reduce the quality of its program offerings must be assessed through a dynamic analysis

⁸ According to James Dertouzos and Steven Wildman, for twelve networks studied, the average length of a contract with an MSO was 4.67 years. J. Dertouzos and S. Wildman, *The Economics of License Fee Discounts*, at 6, Table 1 (submitted on behalf of Ameritech Corp. in CS Docket No. 99-251, Aug. 23, 1999).

⁹ For a more complete discussion of indicia of market power see, e.g., J. Ordover, *Economic Foundations of Competition Policy*, ch. 2 in W. Comanor *et al.*, COMPETITION POLICY IN EUROPE AND NORTH AMERICA: ECONOMIC ISSUES AND INSTITUTIONS (1990); see also D. Carlton and J. Perloff, MODERN INDUSTRIAL ORGANIZATION (2000).

that reflects the *availability* (or capacity) of DBS. The relevant DBS market share figure (if market shares are to be used) is not the existing static market share, but the *potential* DBS share that could be captured if a cable operator actually acted on a threat to refuse to carry competitively priced programming that its subscribers want in order to squeeze more money from the programming network.¹⁰ The willingness of customers to choose DBS over cable is also highly relevant to the programming supplier's own assessment of its available alternatives. Thus, in deciding whether alternative distribution outlets offer sufficient sources of revenue to warrant investment, a video programming network would not look merely at the current static market shares of those alternative distributors, but at the expected number of subscribers (and hence the expected subscriber-based fees) over the entire (lengthy) contract period – recognizing, of course, that a cable company's refusal to carry competitively priced programming would likely accelerate the growth rate of the cable company's rivals' subscriber bases.¹¹

23. The analyses submitted by the opponents of the merger never confront these basic questions. They ignore altogether most of the alternative distribution and revenue sources available to suppliers of video programming as well as the nature of video

¹⁰ Of course, not every threat by a cable company to “drop” a channel evidences market power. For example, it is both reasonable and in the public interest for a cable company to refuse to carry a programming channel whose rates are too high relative to the audience it attracts.

¹¹ For example, the current dispute between YES and Cablevision is costing the cable operator significant numbers of subscribers, underscoring the importance of DBS in disciplining cable. *See, e.g.,* Richard Sandomir, *YES Says No to Cablevision Proposal*, New York Times (March 27, 2002). In addition, I understand that Time Warner in Houston lost 35,000 subscribers when it temporarily dropped ABC from its line-up in a retransmission dispute negotiation.

programming as a non-exhaustible good,¹² and the contractual and other mechanisms that suppliers use to protect their interests. Rather than reflect the critically important effects of competitive pressure from DBS, they use static analyses based upon the untenable assumption that DBS competition has no impact on cable behavior. As I explain below, when these and other marketplace characteristics and conditions are properly reflected, it is clear that the AT&T Broadband-Comcast transaction will cause none of the buyer market power problems that opponents of the merger claim.

IV. AT&T COMCAST WILL NOT HAVE MONOPSONY POWER OVER SUPPLIERS OF VIDEO PROGRAMMING.

24. Qwest and CFA argue that serving slightly less than 30 percent of MVPD subscribers will give AT&T Comcast monopsony power over suppliers of video programming. This claim is flawed on a number of levels.

A. Unilateral Exercise of Monopsony Power.

25. First, traditional monopsony power arguments simply do not carry over into this context. Traditional monopsony theory holds that a firm that buys a sufficiently high percentage of a given (input) may have the ability unilaterally to affect the price it pays for the product. It can accomplish this by either restricting the volume of purchases (which forces the price of the good below the competitive level) or by making a “take it or leave it” offer for the good (with full knowledge of how much input will be forthcoming at that price). In either case, the volume of purchases will fall as will the price of the good in

¹² In other words, it is a good that can be sold to many buyers without reducing its availability to any other buyer. Such goods are also termed non-rivalrous goods.

question, as compared to the competitive benchmark where the buyer is a price-taker.¹³ It is important to note that in order for a firm to exercise this traditional type of monopsony power in an input market, it must face an upward sloping input supply curve and recognize that by buying fewer inputs, it can reduce the price it pays for all the inputs it purchases.

26. The economic literature documenting the ability of companies to exercise this type of monopsony power was developed in the context of “rivalrous” goods—*i.e.*, goods that when sold to one buyer cannot be sold to another buyer.¹⁴ Video programming, however, is non-rivalrous. That is, “[c]onsumption of the programming of a video programming network . . . by one viewer does not reduce the amount of the good available for another viewer.”¹⁵ Obviously, this specific feature of programming flows from a fact that once a program is produced, it can be distributed at virtually zero marginal cost to any one buyer.¹⁶ In such a setting, whether an individual MSO does or does not purchase the programming does not affect the production cost of this particular programming.

¹³ See R. Pindyck & D. Rubinfeld, MICROECONOMICS 352-54 (2000); and D. Carlton and J. Perloff, MODERN INDUSTRIAL ORGANIZATION 105 – 107 (2000).

¹⁴ See *Ordover Cable Rules Dec.* ¶ 67.

¹⁵ *Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act of 1992*, 16 FCC Rcd 17312, ¶ 15 (2001) (“*Cable Rules Remand Notice*”).

¹⁶ See D. Waterman, *Local Monopsony and Free Riders*, 8 Information Economics and Policy, 337-355 (1996) (video programming is non-rivalrous in that the costs of production occur up-front in the creation of the “first copy,” with no costs incurred for subsequent copies).

27. These factors undermine the normal intuition that a very large purchaser may be able to exercise traditional forms of monopsony power over sellers. Demand by one MVPD for an additional programming network does not reduce the number of networks available to other MSOs or other MVPD distributors or the costs of selling programming to them. In fact, just the opposite can be true: if one MSO is willing to pay enough to stimulate additional supply of programming, other buyers will benefit because they too will be able to purchase this new programming.¹⁷
28. Put simply, an MVPD “monopsonist” that is a price setter would choose the same bundle of programming as would a competitive purchaser. That is because where, as here, the goods in question are non-rivalrous and can be distributed at zero marginal costs to all potential buyers, there is no way in which purchasing “less” allows a cable MSO to reduce the price it pays for all of the inputs it purchases.¹⁸
29. Note also that the traditional theory of monopsony harm depends critically on the inability of a purchaser to “price discriminate” in the input market.¹⁹ In contrast, where a buyer can engage in perfect price discrimination, it will not constrict purchases of the input.²⁰ Thus, even if one could ignore the analysis above and pretend that traditional

¹⁷ See J. Perloff, MICROECONOMICS 683 (1999); J. Stiglitz, ECONOMICS OF THE PUBLIC SECTOR 122 (2nd ed. 1988).

¹⁸ More technically, because of the non-rivalrous nature of programming, the MVPD “monopsonist” faces a flat supply curve up to the volume of programming that is available.

¹⁹ This point is not unique to non-rivalrous goods, but is true generally where a monopsonist can price discriminate.

²⁰ The only exception to this would be if the putative monopsonist also gains incremental monopoly power, which, however, is not related to monopsony power.

monopsony concerns were appropriate, there would still be considerable doubt that a cable MSO with putative monopsony power would reduce output because such an MSO would likely engage in price discrimination through efficient bargaining with the content suppliers.²¹

30. Further, as a cable MSO gets bigger, its incentives to buy the quantity and quality of programming that is likely to attract the greatest number of viewers relative to the cost of securing such programming are not affected. In other words, a cable MSO's need for quality programming, as well as for the number of networks carried on the system, is driven by consumer demand and retail competition that are independent of, and would be unchanged by, the acquisition of "monopsony" power over programmers, as long as both parties have the ability and incentives to attain efficient outcomes. It is plain that both suppliers and buyers of content for cable distribution have such incentives and the ability to act upon them. For these reasons, a profit-maximizing cable "monopsonist" does have the correct incentives not to depress the number or quality of the programming options, as compared to the situation where distributors are price-takers. Thus, monopsony concerns are entirely misplaced in this context.

²¹ Given the process by which contracts are negotiated, it is unrealistic to assume that an MSO acts as a perfect price discriminator who makes "take it or leave it" offers to content providers. The interaction between the cable MSO and the network provider is best described as a bargaining problem. The allocation of rents may depend on the relative bargaining strength of the two parties, but the parties (generally) have no incentive to agree to a contract that is inefficient.

B. Free Riding.

31. Messrs. Haring, Rohlf, and Shooshan, filing on behalf of Qwest, correctly eschew the more traditional version of monopsony in arguing that the transaction will harm the quantity and quality of programming. Instead, they note that the production of video programming has high fixed (or “first copy”) costs and that a programmer’s marginal cost of delivery to a cable MSO is therefore much less than the average costs that the programmer must cover (and possibly zero).²² This creates a risk that some distributors will attempt to “free ride” by paying less than average cost (but more than marginal cost), and thereby either disadvantage their distribution rivals (who must then pay *more* than average cost if quantity and quality are to remain constant) or negatively affect the quality or quantity of the available programming (*i.e.*, if other distributors don’t make up the difference, the quality or quantity of programming must suffer).²³
32. Programmers, of course, are fully aware of the possible incentives to free ride and must strive to protect themselves *ex ante* (before sinking the investment) against such risks. Thus, to induce a program producer or packager to make these investments, cable operators and other programming distributors must convince the program producer or packager that it will not be “held up.” But the non-rivalrous nature of programming creates the above-mentioned “free riding” incentives among MVPDs – each distributor would like quality programming to be produced, but each wants its rivals to incur the costs of solving the hold-up problem. Unless the free riding problem can be solved, the

²² See, e.g., D. Waterman and A. Weiss, VERTICAL INTEGRATION IN CABLE TELEVISION, Ch. 5 (1997) (containing an exposition of this argument).

²³ Qwest, HRS Dec. at 3-4.

investment in programming may suffer: fewer and possibly lower quality, less expensive programs will be made.²⁴

33. The existence of such free riding incentives in the video programming context is uncontroversial, as I explained in my declaration in the Cable Rules Proceeding. But, as I also explained there, such incentives exist for *all* purchasers of video programming and thus have nothing to do with traditional “monopsony” considerations. It is important therefore, to examine how these incentives play themselves out in the marketplace and whether the proposed transaction will change the playing field in such a manner as to reduce the quantity and quality of the available programming alternatives below the level that would prevail *but for* this transaction.
34. The ever-increasing production and distribution of video programming confirms that market participants in the video-programming marketplace have found ways to address free riding issues through contractual, reputational, and other means.²⁵ Indeed, there is now a body of academic literature that discusses the many mechanisms that can be used

²⁴ The logic here is that if the free rider refuses to pay its “fair share” of the costs, others must pay more (assuming that they will simply take these higher charges). But in order to be willing to pay more per program, there will have to be fewer programs available, as the marginal benefit to an MSO from an additional program is likely to be declining. Of course, this argument assumes that a programmer believes *ex ante* that it will be exploited and thus needs to “mark up” the price to the price-taking MSOs in order to recover its full, forward-looking cost. As discussed in the text, both sides have strong reasons not to create market-place distortions that result from such *ex ante* expectations.

²⁵ Start-up networks typically obtain carriage commitments from a number of cable MSOs prior to sinking substantial costs in program production. A. Raskovich, *Pivotal Buyers and Bargaining Power*, DOJ Economic Analysis Group Discussion Paper 00-9, at 11 n.4 (2000).

to solve such free riding problems.²⁶ The important point here, however, is that although free riding issues clearly arise in this context, they are not directly linked to cable ownership concentration, but stem primarily from the cost structure and non-rivalrous nature of video programming.²⁷ While it may be the case that a local hospital may have to increase the salaries of all the nurses it employs to induce an increase in the supply of nurses, it is not true of the price-setting dynamics in the market for content.²⁸ For example, an MSO may (and likely will) negotiate a contract (possibly a contingent contract) with an individual network on terms that may be “unlinked” to the terms agreed with other programmers, but that agreement may depend on the terms that the programmer manages to strike with other distributors. Consequently, the assessment of the competitive concerns from “free riding” incentives must take into account the specifics of the negotiations for programming terms between buyers and sellers of content.

²⁶ The seller who has been held up once will not be willing to commit the needed resources in the future thereby leaving the monopsonist without the source of the input. This could be very costly to the free riding distributor who may also have long lived and specialized assets that would be rendered valueless without the input.

²⁷ If each MSO had to pay the full freight of its own programming, there would be no opportunity for free riding.

²⁸ In fact, the analysis of the free rider problem in Waterman and Weiss, *supra*, implicitly assumes that in order to induce additional supply of programming (past some pre-existing level), an MSO must increase payments to all program suppliers. But this simplifying assumption is not appropriate here. If the incremental network is desirable (its production costs are less than the value to the MSOs from its availability) then standard bargaining theory predicts that such programming will be produced.

35. Indeed, if there is any relation at all between cable company size and the ability successfully to free ride – *i.e.*, to pay less than a proportionate share of the programming suppliers’ costs – the academic literature suggests that in some settings, size may be a *disincentive* to free riding. Although perhaps counter-intuitive, the reasons for this are quite simple. Each individual cable MSO would like the other MSOs to make the *ex ante* commitments sufficient to induce a programmer to sink the costs necessary to produce programming of the desired quality. In that way, the “free riding” MSO could hope to negotiate a better deal with the programmer *after* the programmer’s fixed costs are sunk and its marginal costs of an additional sale are very low. A large MSO, however, can less credibly threaten to free ride than a small MSO. The larger the MSO, the more likely that its refusal to contribute its “fair share” of costs would affect the programmer’s ability to profitably produce the programming at issue. In such a case, the large MSO will bear a relatively larger share of the costs of lost benefits from having the programming available. It follows that under plausible assumptions, a large MSO is more likely than a small MSO to internalize the impact of its purchasing decisions on the financial viability of a new program service. And if a single MSO buyer gets so large that it becomes “pivotal” to a video programmer’s production decision – *i.e.*, the programmer cannot economically produce the content without the large MSO’s agreement to purchase the programming – that MSO loses altogether “the ability to abdicate credibly responsibility for ensuring that the supplier’s costs are covered.”²⁹

²⁹ A. Raskovich, *Pivotal Buyers and Bargaining Power*, DOJ Economic Analysis Group Discussion Paper 00-9, at 22 (2000).

36. There is now emerging academic literature that bears on this point. For example, in an already cited paper, DOJ's economist Dr. Andrew Raskovich demonstrates that a "pivotal" buyer of video programming would be unable to exercise significant bargaining power, let alone market power, against programmers. Dr. Raskovich explains that in industries characterized by high fixed costs and low marginal costs, a "pivotal" buyer³⁰ internalizes the effect of hard bargaining on the supplier's decision to sink costs. In other words, a key buyer knows that if it insists on too low a price, a supplier is going to be unwilling to make the investments necessary to produce either the quantity or the quality of the product or service desired by the buyer. "Bigger is not always better in a bargaining context. If a buyer grows so large as to become pivotal to the supplier's production decision, the buyer loses the ability to abdicate credibly responsibility for ensuring that the supplier's costs are covered."³¹
37. Likewise, Professors Chipty and Snyder examine the effect of buyer merger on bargaining power in cable television.³² The authors present a theoretical model of a bargaining game between a single supplier (programmer) and N buyers (MSOs) and demonstrate that buyer merger can weaken the buyers' bargaining position, depending on

³⁰ A buyer is pivotal if the other buyers in aggregate will not provide a supplier with sufficient funds for covering the supplier's fixed costs. Thus, without a contribution from the pivotal buyer, the supplier will be unwilling to sink the fixed costs necessary to produce the good/service at issue.

³¹ *See id.* at 22.

³² *See* T. Chipty and C. Snyder, *The Role of Firm Size in Bilateral Bargaining: A Study of the Cable TV Industry*, 81 *Review of Economics and Statistics*, 326-340 (1999). *See also* T. Chipty, *Horizontal Integration for Bargaining Power: Evidence from the Cable Television Industry*, 4 *Journal of Economics and Management Strategy*, 375-397(1995).

the curvature of the supplier's gross surplus function.³³ In assessing its bargaining position after the merger, the merging parties must evaluate the merged distributor's marginal contribution to the programmer's gross surplus after the merger and compare it to the marginal contribution of each firm individually. Since the buyer's negotiated price for the input depends inversely on the marginal contribution to the supplier's gross surplus, the combined firm will be able to negotiate a better price if its contribution is larger than the sum of the contributions of the two individual firms. This would be the case if the shape of the gross surplus function were convex; that is, if it increased at an increasing rate as the number of subscribers increases. In the second part of their paper, the authors empirically estimate the shape of the gross surplus function for a sample of networks in the cable industry and find that its shape is indeed convex, consistent with the conclusion that the merger between two MSOs actually reduces their bargaining power in the programming market.

38. Merger opponents also suggest that AT&T Comcast may use its bargaining power and the ability to free ride to gain an unfair competitive advantage against overbuilders.³⁴ Under this theory, AT&T Comcast would pay less than its fair share of the fixed costs necessary to develop programming, forcing the programmer to collect a larger portion of the fees from the overbuilder(s). Because of this programming cost differential, the

³³ The gross surplus function is defined as advertising revenues minus cost. Their model assumes a Nash bargaining game in which, in equilibrium, each buyer obtains half of the increment to total surplus generated by its trading with the supplier.

³⁴ See Qwest, HRS Dec. at 5-6.

theory hypothesizes, an overbuilder would not be able effectively to compete against an MSO and would be driven from the market.

39. This argument simply makes no sense. Regardless of how much it sells to other distributors, a programmer has an incentive to charge as high a price as it can for its programming to any particular cable overbuilder. The AT&T Comcast merger would not change a programmer's ability to charge a cable overbuilder a higher price. Thus, if, as hypothesized by Dr. Gertner, a programmer has the ability to force overbuilders to accept higher prices, then it would already be charging those higher prices *before* AT&T Comcast exercise their purported power to gain a lower price.

40. Further, even if this flaw could be overlooked, the basic economics of the production of video programming constrain the prices that a programmer would charge an overbuilder. As I explained above, a programmer will not sink its costs if it does not expect to recover them. If, as the theory assumes, the higher prices the overbuilder would have to pay to make up for the lower prices paid by AT&T Comcast would drive the overbuilder from the marketplace, the programmer would be unable to recover its costs (because the overbuilder would make no contribution to the recovery of costs). Thus, the programmer would have no incentive (or even ability) to agree to AT&T Comcast's demands in the first place. Rather, it would demand that AT&T Comcast pay at least its proportionate share of costs (and the combined firm would have an incentive to do so). Indeed, with respect to pre-existing programming, the overbuilder actually benefits from the willingness of the incumbents to contribute sufficient amounts to bring forth the desirable programming. If the revenue flow from the existing MSO contracts is sufficient to cover

the full forward-looking costs of the content at issue, the late entrant (such as an overbuilder) can be served at a low price, because the revenue from the overbuilder is (essentially) pure profit. In any case, even if AT&T Comcast were to underpay, there is no reason to believe that the effect on overbuilders would be so significant as to put them at a competitive disadvantage.

41. The bottom line then is that the opponents of the merger have not demonstrated that these free riding/monopsony concerns are exacerbated by the merger, or that the suppliers and buyers of video content cannot resolve them through standard contractual means. Free riding is always an issue where there are high fixed costs and low (or zero) marginal costs, thereby creating incentives for a buyer to try to “shave off” a few dollars or cents from the price that is asked and for the seller to try to “stick” some high-willingness-to-pay buyers with high prices and then discount selectively to those whose willingness to pay is low. There is no evidence that these potential concerns would be exacerbated by this transaction. Instead, there is every reason to believe that the parties would recognize the inefficiencies that may result from opportunistic behavior and, as skillful and experienced negotiators, would find mutually beneficial ways of overcoming them.

C. Rent Extraction.

42. Several of the merger opponents suggest that AT&T Comcast may be able to obtain greater programming discounts by virtue of its size.³⁵ The implication is that this would necessarily be anticompetitive, but, as SBC’s economist concedes, paying lower prices is

³⁵ Qwest at 6-8; Qwest HRS Dec. at 19; RCN at 29-32.

anticompetitive only to the extent that it reflects abuse of market power.³⁶ As I explain below, that is not a plausible explanation for the programming savings that AT&T Broadband and Comcast hope to obtain as a result of the merger.

43. Like any purchaser, a cable operator would like to pay as little as possible for programming of a given quality that best fits its market needs. (At the same time, of course, the supplier would like to earn as much as possible.) But even if a large cable MSO were more likely to get lower prices for programming than a small one, this is not automatically a matter of public policy concern. As I explained above, a large MSO must be concerned with the consequences of its bargaining on the quality and quantity of the programming that will be available to it, which will temper its desire to extract all the possible rents from the programmer. Again, as noted previously, a large MSO may, in fact, find itself in a disadvantageous position *vis-à-vis* suppliers if it becomes a pivotal purchaser (or believes that it is a pivotal purchaser). This is not to deny that a large MSO may also gain some countervailing strategic advantage and prevent a sophisticated programmer from saddling it with a disproportionate share of programming costs (in view of the significant costs to the MSO from not obtaining the desired programming). Nevertheless, assuming that the negotiations between buyers and sellers can be arranged efficiently, the likely outcome of the negotiations would be a redistribution of rents without a detrimental effect on the number or quality of networks that will be available to the viewing public. At the same time, if there are no such rents to be reshuffled, the

³⁶ See SBC, Gertner Dec. ¶¶ 24-27.

parties will have strong incentives to implement outcomes that lead to the efficient availability of programming.³⁷

44. In this regard, it is also important to recognize more generally that the fact that large MSOs may pay lower per-subscriber fees than smaller distributors is not inherently anticompetitive or evidence of abuse of market power.³⁸ In cases where a large MSO receives lower prices from a programmer, these lower prices potentially reflect efficiencies gained by the programmer in serving the large MSO, and not any increase in bargaining power. For example, a long-term contract with a large cable operator such as AT&T Comcast would allow a video programmer to mitigate a portion of the substantial risks associated with its large, sunk investment in programming. Economic theory predicts that the reduction of these risks would be reflected in lower prices offered by the programmer to the cable operator.
45. Economics draws a clear distinction between the ability of large buyers to obtain cost-based volume discounts and to redistribute rents in their favor, on the one hand, and buyers' ability to push prices *below* cost-based levels, on the other. It is well recognized that volume discounts are generally pro-competitive when there are high fixed costs and low marginal costs because such discounts stimulate usage.³⁹ Discounts to large MSOs

³⁷ As I have noted, such outcomes can be accomplished through various contractual and pricing provisions (such as two part tariffs, for example).

³⁸ *Accord*, SBC, Gertner Dec. ¶¶ 24-27.

³⁹ See, e.g., J. Ordover and R. Willig, *Economist's View: The Department of Justice Draft Guidelines for the Licensing and Acquisition of Intellectual Property*, Antitrust (Spring 1995) (“[V]olume-sensitive pricing, in particular volume discounts enhance downstream efficiency and thus should be regarded as procompetitive.”); DOJ/FTC, *Statements of Antitrust* (continued . . .)

are also warranted because it is less costly for sellers to deal with larger buyers. For example, serving a large MSO may allow a programmer to avoid certain costs that it would incur in serving multiple, smaller MSOs. Such costs include specific incremental marketing, distribution, sales, administration and legal expenses that are incurred when serving each MSO. The benefits of the reduced costs accrue not only to the programmer and the MSO, but to the consumer as well, in the form of higher quality programming, improved customer service, and potentially lower subscription fees.

46. Volume discounts may also ameliorate the potential free riding issue discussed above. As noted, large MSOs are more likely to be the entities that make the financial commitment necessary to allow the programmer to recover its costs thereby making production of the programming possible. A most-favored-nation clause and/or volume discounts allow a large MSO to protect itself from smaller MSOs obtaining a much better rate from the programmer after the programmer has been assured recovery of its fixed costs from its agreements with the large MSOs, and thereby provide another incentive for the large MSO to make the investment in the first place.
47. Indeed, SBC's economist, Professor Gertner, concedes that one cannot *a priori* exclude the possibility that lower prices merely reflect cost-based discounts, plus payments for

(... continued)

Enforcement Policy in Health Care (Aug. 1996) (“*Health Care Antitrust Guidelines*”) (joint purchasing agreements can allow participants to “obtain volume discounts” that “allow the participants to achieve efficiencies that will benefit consumers”); *see generally* J. Laffont and J. Tirole, *COMPETITION IN TELECOMMUNICATIONS*, Ch. 2 (2000); D. Carlton and J. Perloff, *MODERN INDUSTRIAL ORGANIZATION*, Ch. 10 (3rd ed. 2000).

valuable benefits that a large MSO may provide to the programmer relative to the benefits available from a smaller MSO, rather than squeezing out rents.⁴⁰

48. Prof. Gertner argues that these rents are needed to ensure a competitive supply of high quality programming. I agree, of course, that inasmuch as provision of quality is costly, a program of higher quality is more expensive to produce, and programmers will have to be compensated for the provision of higher quality. However, as I have noted already, there is no reason to assume that a large MSO will have an incentive to induce undersupply of quality any more than it has a myopic incentive to induce undersupply of networks of any given quality.
49. In essence, Prof. Gertner's argument amounts to an implicit claim that, while there may be short-term rents available to the suppliers of content (network programming), there are no long-term rents. Any redistribution of revenue from content providers (and those who provided inputs into the production of content) to the MSOs would have a detrimental effect on the quality and quantity of programming. There is no evidence that suppliers of content are undercompensated and that the supply of high quality programming is "drying up." In fact, programming costs are increasing rather rapidly, perhaps in recognition that (as some say) content is king and thus requires a king's ransom. As the importance of content to the success of any distributor grows, the distribution of the value created by combining the complementary assets of programmers and distributors may actually shift towards content suppliers. Put simply, Prof. Gertner has failed to provide

⁴⁰ See SBC, Gertner Dec. ¶¶ 24-27.

any legitimate evidence of the lack of existence of long-term rents. Indeed, given the inherent product differentiation in the provision of content, it is plausible that some content providers also have market power and earn whatever above-competitive profits the market allows. There is nothing wrong with such rents and there is nothing wrong with hard bargaining over the distribution of such rents.

D. Collusion.

50. There are obvious and formidable obstacles to implementing successful collusion *vis-à-vis* content suppliers. One impediment to collusion among MSOs is their heterogeneity, including variations in cost and markets served. It may be difficult (or impossible) for them to reach an effective agreement as to the “correct” price that should be paid for programming. Moreover, the heterogeneity of programming itself compounds the coordination problem.⁴¹ At the same time, a programmer marketing its product to MSOs would easily detect collusion when it observed that all MSOs demand similar contract terms. Further, inasmuch as MSOs and content programmers are vertically integrated, the ability to implement collusively depressed rates could be limited. Finally, as the Merger Guidelines explain, the threat of collusive conduct is especially enhanced when the merger removes from the marketplace a “maverick” firm – one that is most likely to restrain the ability to implement a collusive outcome. There is no evidence that either

⁴¹ See the speech by Deputy Assistant Attorney General William Kolasky before the ABA Section of Antitrust Law, Washington DC (April 24, 2002) reviewing the factors that hinder and facilitate coordination among firms. William J. Kolasky, *Coordinated Effects in the Merger Review: From Dead Frenchmen to Beautiful Minds and Mavericks*.

AT&T Broadband or Comcast is the stumbling block that prevents distributors from extracting supracompetitive rents.

51. The analysis of free riding above also bears on the concern that the increase in concentration resulting from this merger will facilitate collusion. The presumed objective of collusive behavior in this setting would be to exercise monopsony power by restricting the purchases of programming. A cartel, however, even more so than a single large MSO, would likely lack the incentive to restrict its purchases of programming and free ride. Indeed, as noted by Waterman and Weiss, “a cartel of vertically integrated MSOs controlling all cable systems and all cable networks will eliminate the free rider effect.”⁴² Other than providing an opportunity to gain efficiency-related cost savings, size is not necessarily an advantage in securing programming, and indeed, at some levels could lead to a reduction in buyer power. So, even if a “tacit joint bargaining cartel” could form, it does not follow that it would form or that it could significantly (or at all) improve on the rates paid by each of the cartelists on their own.

V. THE MERGER WILL NOT INCREASE THE THREAT OF FORECLOSURE OF RIVAL PROGRAMMING.

52. The opponents of the merger also claim that AT&T Comcast will have an incentive to “foreclose” various types of programming from its cable systems.⁴³ Foreclosure occurs when upstream competitors of a vertically integrated firm are excluded from selling to the downstream division of the integrated firm and, ultimately, to the customers of the

⁴² D. Waterman and A. Weiss, VERTICAL INTEGRATION IN CABLE TELEVISION 83 (1997).

⁴³ See, e.g., SBC, Gertner Dec. ¶¶ 20-29.

integrated firm. Of course, any firm that refuses to buy from a particular seller or sellers potentially “forecloses” such a seller from access to certain customers. Indeed, the buyer may refuse to purchase content because it believes the asking price is too high, the quality is too low, the supplier is unreliable, there is no “space” for the product, and so on. Such a refusal to deal with a seller generally raises no competitive concerns. Foreclosure is competitively significant only if the integrated firm’s conduct lessens competition in some relevant antitrust market to the ultimate detriment of consumers.⁴⁴ For example, such harm may occur if the foreclosing firm is so large that the inability to sell to its downstream division (and ultimately to the final consumers served by that downstream division) precludes the upstream competitors from covering their costs, thereby enabling the integrated firm’s upstream division to exercise market power over downstream purchasers who may or may not compete with the downstream division.⁴⁵ This transaction will not create incentives for this type of anticompetitive foreclosure.

53. As explained in detail below, AT&T Broadband and Comcast have only very limited ownership interests in programmers. Because foreclosure concerns are generally triggered in the context of a vertical relationship between an MSO and a programmer, the *de minimus* level of such relationships in this transaction is fatal to the foreclosure claims advanced by the opponents. Indeed, AT&T Comcast would have little to gain by engaging in activities that affect the value of firms in which it has little or no interest.

⁴⁴ For a technical discussion of these issues, see B. Douglas Bernheim and M. Whinston, *Exclusive Dealing*, 106 *Journal of Political Economy*, 64-103 (Feb. 1998).

⁴⁵ This is frequently termed “non-coincidental market effect.”

54. Furthermore, it is important to recognize that a cable MSO's dollar losses from foreclosure in its own cable systems tend to increase as it grows larger. Foreclosure (of the anticompetitive variety, at least) necessarily implies refusing carriage of programming that otherwise would be a valuable addition to the programming line up of the MSO, given the rates that could be negotiated and the quality of the programming itself. As explained above, the consequence of such refusal is fewer subscribers. Obviously, numerically at least, a large MSO stands to suffer greater customer losses from reductions in the overall quality of its programming choices than a small MSO, hence higher foregone revenues in dollar terms. And, as I explained above, because cable companies incur high fixed costs regardless of the number of subscribers served, the loss of even relatively few subscribers could have a significant impact on the profitability of the strategy. This is especially so if the lost viewers not only subscribe to the basic offering but also to the upper (or premium) tiers.
55. At the same time, the dollar benefits from the foreclosure strategy depend on the size of the market that is not foreclosed and in which the foreclosing MSO hopes to gain a competitive advantage for its affiliated programming. Of course, the larger the MSO, the *smaller* the open market and thus the smaller the dollar gains from foreclosure strategy aimed at content suppliers. That is because the larger the foreclosing MSO, the smaller is the number of subscribers served by other distributors. And the fewer the subscribers served by other distributors, the lower the revenues to be gained by the MSO's programming affiliate from exercising market power over those other distributors. Consequently, for this type of foreclosure strategy to make economic sense, the

foreclosing MSO must be large enough to inflict competitive damage on an unaffiliated programmer but not so large that the losses on its own account cannot be recouped (and more) by means of higher prices charged to other MVPDs. This is a fine balance indeed. I am aware of no evidence that serving 30 percent of MVPD subscribers generally, or in this transaction in particular, would shift the profit calculus toward foreclosure and away from unimpeded access to the AT&T Comcast cable subscribers.

56. It is also relevant to note that extant regulations prevent AT&T Comcast from entirely foreclosing unaffiliated programming even on its own systems. Programmers can sell content to broadcast stations that are guaranteed basic tier carriage by the “must-carry” rules or to any of the many programming networks that are *de facto* must-see cable programming networks by virtue of their popularity with consumers (and hence the costs to an MSO in lost subscribers if an MSO were to refuse to carry them). So, even if a network can be foreclosed (in principle), it does not mean that the content that would be available on that network would be necessarily lost to viewers. If content is not lost to viewers, then the profits from foreclosure are likely to be less than if all of the content disappeared.⁴⁶

57. The “Big 3” broadcasters remain strong, and PBS, Fox, UPN, WP and PaxTV also now serve most major markets.⁴⁷ The “must carry” provisions of the 1992 Cable Act require cable systems to carry broadcast stations (and to include them in “basic” tier service).⁴⁸

⁴⁶ See, e.g., *Big Networks Show “Sopranos” Respect*, New York Times (May 13, 2002).

⁴⁷ See *Dual Network Rule Order* ¶¶ 3, 20 n.46.

⁴⁸ 47 U.S.C. § 534.

These are very attractive venues for producers that want to launch various types of programming. Consequently, the availability of these distribution channels means that some content producers do not have to arrange direct distribution on cable (*i.e.*, on channels whose carriage is at the discretion of an MSO) in order to reach viewers.

58. For these reasons, incentives for anticompetitive foreclosure of programmers are likely to be weak or non-existent. Indeed, as Dr. Besen's testimony in the cable rules proceeding shows, *no* cable company that serves only 30 percent of subscribers (or even many more) would find it profitable to implement programmer foreclosure because the expected gains (in increased programming revenues) from such a strategy would almost surely be outweighed by the expected losses (in decreased subscriber revenues).⁴⁹
59. Dr. Besen's analysis of the effects of increased concentration on the incentives of MSOs to engage in foreclosure suggests that 1) AT&T-Comcast would not have incentives to foreclose rival program services, and 2) any such incentives actually would decrease post merger.⁵⁰
60. In his analysis of the incentives to foreclose, Dr. Besen assumes that, if an MSO drops a rival programming service, and this causes the rival service to exit the industry, then 1) the MSO can raise the price of its affiliated programming to other cable companies

⁴⁹ See Declaration of Stanley Besen, CS Docket No. 98-82, ¶¶ 5-6, 41-57 (filed Jan 4, 2002) ("Besen Cable Rules Dec.").

⁵⁰ See *id.*

because competition is reduced, and 2) the MSO would lose some subscribers because its content is worse than before and its subscription rates remain unchanged.

61. For the 20 largest basic programming services, Dr. Besen calculates the average program service penetration, average annual per-subscriber affiliate fee revenue, and average per-subscriber total revenue.⁵¹ In addition, he assumes that the cable MSO has annual net revenues per subscriber of \$359.83, a 25 percent ownership share of a program service, and a 30 percent share of MVPD subscribers.⁵² Under those assumptions, Dr. Besen finds that even a loss of just 0.79 percent of MVPD customers would render a foreclosure strategy unprofitable.⁵³
62. Furthermore, Dr. Besen's analysis demonstrates that as the size of the cable MSO increases, the critical number of subscribers that the MSO would need to lose to make foreclosure unprofitable actually decreases.⁵⁴ For example, under the assumptions above, an MSO controlling 50 percent of the MVPD market would find foreclosure unprofitable with a loss of only 0.76 percent of MVPD customers.⁵⁵ Applying this analysis to the instant case, AT&T Comcast's incentives to engage in foreclosure actually would *decrease* post merger.

⁵¹ *Id.* ¶ 44.

⁵² *Id.* ¶ 44, Table 3A.

⁵³ *Id.*, Table 3A. The analysis assumes that foreclosure enables a 5 percent increase in the cable MSO's advertising and affiliated programming rates. *Id.*

⁵⁴ *Id.* ¶ 52.

⁵⁵ *Id.*, Table 3A.

A. Foreclosure to Benefit Affiliated Programming.

63. As most of the merger opponents recognize, foreclosure concerns are generally triggered when a cable MSO has a (significant) stake in a programmer (cable network). To the extent that a cable MSO has only minority ownership interests in the pertinent network programming services, its incentives to engage in anticompetitive foreclosure are reduced.⁵⁶ As is further elaborated below, other factors impinge on these incentives as well.

64. **Demand Side Considerations.** To assess the claims of programmer foreclosure, it is important to examine the extent to which the combined firm would control a sufficient percentage of all distribution channels to which video programmers could turn so that foreclosure would, in fact, significantly raise the excluded programmers' costs or impede entry of desirable programming content. Second, any analysis of foreclosure must be a *dynamic* inquiry that assesses not only the *static* shares of each of the available distribution alternatives, but also their capacity to win customers from cable operators that sacrifice quality in pursuit of foreclosure. Foreclosure claims here are necessarily premised on the assumption that the vertically integrated firm can competitively cripple

⁵⁶ More specifically, AT&T has in the last year significantly reduced its ownership of programming services. As a result, AT&T now owns minority interests in only three national program services (E! (10 percent), Style (10 percent) and iN DEMAND (44 percent)). And it has interests in three regional programmers, New England Cable News (50 percent), Pittsburgh Cable News Channel (30 percent), and Fox Sports New England (50 percent)). Comcast has interests only in six national program services, E! Entertainment (40 percent), Golf Channel (92 percent), iN DEMAND (11.1 percent), QVC (57 percent), Style (40 percent), and Outdoor Life Network (100 percent), and in several regional program services, Comcast SportsNet (100 percent), Comcast SportsNet Mid-Atlantic (100 percent), Comcast Sports Southeast (50 percent), and cn8 (100 percent). Comcast and AT&T Broadband each own minute 2% interests, in the Florida News Channel.

unaffiliated programming suppliers by denying them carriage. Only then could the integrated firm hope to gain market power over other programming distributors and charge them higher rates for its own, affiliated programming. The opponents do not offer any concrete evidence that even complete foreclosure from a 30 percent share of MVPD subscribers would competitively cripple a program supplier and confer market power on the affiliated content. As discussed before, these potentially foreclosed programming suppliers would continue to have many alternative distribution/revenue outlets in which to defray their programming costs. Even using static market shares, the unaffiliated programmers would still be able to reach deals with firms that serve the remaining 70 percent of MVPD subscribers.⁵⁷

65. The post-merger level of maximum foreclosure is insufficient to make it profitable for AT&T Comcast to engage in anticompetitive foreclosure of rival programmers. It is generally recognized that controlling 30 percent of purchases (counting only MVPD subscribers and ignoring all other sources of revenues) is unlikely to create market power, for the simple reason that such a small share leaves sellers with far too many alternative purchasers for their services.⁵⁸ For that reason, under the *Horizontal Merger Guidelines*,

⁵⁷ In fact, as explained below, because of must carry rules and other considerations, the “open field” that would remain to programmers would be much wider than 70 percent.

⁵⁸ See *Syufy Enterprises*, 903 F.2d at 666-67 (finding movie distributor with 75 percent of box office revenues and 36 percent of exclusive showings could not exercise buyer power).

entities with market shares under 35 percent are generally considered to be unable to exercise unilateral market power.⁵⁹

66. The Commission has found in this precise context that serving 30 percent or fewer of MVPD subscribers does not confer on an MSO an ability to engage in anticompetitive foreclosure of unaffiliated programmers. In its *1999 Horizontal Order*,⁶⁰ the Commission revised its rules that limited the number of subscribers any cable MSO could serve. Employing an “open field” analysis designed to ensure that all video programmers could reach the minimum number of subscribers necessary to be viable, the Commission concluded that a 30 percent threshold was sufficient to ensure that no single MSO, acting unilaterally or collusively, could exercise buyer market power or foreclosure power. The D.C. Circuit in *Time Warner II*⁶¹ subsequently vacated that order on the grounds that

⁵⁹ See DOJ/FTC, *Horizontal Merger Guidelines* § 2.22 (Apr. 2, 1992, rev. Apr. 8, 1997). On behalf of Qwest, HRS also contend that the Commission cannot look to the antitrust authorities or antitrust decisions for support, because “[a]cquisition of monopsony power by an MSO . . . has nothing to do with the standard interpretations of concentration indices that are based on the potential for effective implicit or explicit collusion.” Qwest, HRS Dec. at 9 n.14. As one of the principal authors of the 1992 *Horizontal Merger Guidelines*, I can categorically state that concentration indices are used by federal antitrust agencies to gauge the potential for exercise of market power on both the selling and buying sides of the relevant product and geographic markets. As those guidelines explain, such market power can be exercised jointly, through coordinated actions of independent firms, as well as unilaterally, by actions of the merged entity. See DOJ/FTC, *Horizontal Merger Guidelines* § 0.1 (Apr. 2, 1992, rev. Apr. 8, 1997); *Health Care Antitrust Guidelines* at 18. Federal antitrust authorities use the same “analytical framework” to assess the “exercise of market power by buyers.” *Horizontal Merger Guidelines* § 0.1. Indeed, the reason that antitrust policy guidelines are concerned with collusion is that it allows several firms to make pricing/output decisions as if they were a single firm.

⁶⁰ Third Report and Order, *Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992 Horizontal Ownership Limits*, 14 FCC Rcd. 19098 (1999).

⁶¹ *Time Warner Entertainment Co. v. FCC*, 240 F.3d 1126 (D.C. Cir. 2001).

there was no substantial evidence supporting a number of assumptions made by the Commission in reaching this 30 percent limit, particularly the Commission's assumption that the two largest MSOs would necessarily collude to exploit programmers.⁶² The court also found that the Commission had inappropriately equated market share with market power and, as a consequence, had failed to account properly for the way that the ubiquitous "availability" of DBS can constrain the possible exercise of market power by cable MSOs.⁶³

67. Thus, revisions to the Commission's analysis can only result in a *higher* subscriber limit than the 30 percent limit adopted by the Commission in the *1999 Horizontal Order*. Further, since 1999, DBS has experienced even more explosive growth, cable channel capacity has increased, and the extent of vertical integration between cable MSOs and video programmers has declined.⁶⁴ *A fortiori*, a merger that results in an entity with 30 percent of the MVPD "market" today cannot be considered to threaten the viability of video programming suppliers.⁶⁵

⁶² Without that assumption, only a 60 percent subscriber limit would have been justified under the Commission's analysis. 240 F.3d at 1131.

⁶³ *Id.* at 1134.

⁶⁴ See Eight Annual Report, *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 17 FCC Rcd. 1244, ¶¶ 13, 32, 157, 186 (2002) ("2001 Video Competition Report").

⁶⁵ This is particularly true, given that the Commission also assumed a much more concentrated industry than exists today or is likely to ever exist. See *1999 Horizontal Order* ¶¶ 45-47 (assuming only four cable MSOs in the U.S., with the two largest each having 30 percent of the MVPD "market" and the two smallest each having 20 percent of the "market").

68. That is not just economic theory, but proven fact. The merger opponents claim that a threat of denial of carriage by AT&T Comcast – *i.e.*, that the rival video programming network would have access to “only” about 64 million of the approximately 92 million U.S. MVPD subscribers – would be equivalent to a “death threat.” But they do not even attempt to demonstrate that for programmers the minimum viable scale is so large that foreclosure from only 30 percent of subscribers would significantly weaken the unaffiliated suppliers of content and confer on the foreclosing MSO market power *vis-à-vis* other MSOs in the provision of content. Instead, they cite anecdotal evidence noting that AOL Time Warner and the National Basketball Association (“NBA”) have announced that they will not launch their new sports network until they sign up MSOs with 25 million subscribers.⁶⁶ Whatever one makes of this statement, AOL and the NBA could easily reach that figure without AT&T Comcast. It also seems implausible that AT&T Comcast would have an incentive to foreclose what could be an important potential network in order to protect or enhance its own sports programming: in fact, no evidence has been offered to suggest that the standard economic calculus would warrant such conduct (and it defies belief to think that a joint venture between one of the world’s largest media conglomerates and the NBA would lack bargaining power in negotiations with even the largest cable operators – assuming, of course, that there is consumer interest in the network’s programming).⁶⁷

⁶⁶ See SBC at 6 n.13.

⁶⁷ Furthermore, sports programming, like any type of programming, has the particular feature that the number of subscribers needed for viability depends on how much the programming service pays to “talent.” Consequently a basketball network that has less ubiquitous coverage
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69. A substantial number of successful networks operate today with distribution to fewer than 60 million MVPD subscribers. In fact, as set forth in AT&T's comments in the Cable Rules Proceeding, close to 50 national cable programming networks have been successfully launched and that remain in operation today with fewer than 15 million MVPD subscribers.⁶⁸ This group includes a number of well-known networks that were launched years ago such as BET on Jazz; Discovery Kids Channel; and STARZ!, as well as more recently launched networks, such as Oxygen and National Geographic Channel. Many networks, including some that are more than five years old, have fewer than 3 million subscribers.⁶⁹

70. Moreover, some programming services may be able to adjust their costs in response to changes in penetration, so as to remain viable even at lower subscriber levels. Indeed, such cost reductions may occur even without a decrease in quality if much of the programmer's costs are "rents", *i.e.* payments that exceed the opportunity costs of the inputs needed to produce the programming. Exclusion from AT&T Comcast's systems might simply reduce the network's rents without imposing a threat on its viability. Of

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may have to pay less to the league and the players. The opponents of the merger do not demonstrate that this would either render the proposed network unviable or be detrimental to the future of professional basketball in the United States

⁶⁸ Comments of AT&T, CS Docket No. 98-82, at 60-61 (filed Jan. 4, 2002) ("AT&T Cable Rules Comments").

⁶⁹ A new VOD service currently available on some Cablevision systems will feature niche programming on various subjects such as birding, Shakespeare, weaving, the Bible, classic cars, vegetarian eating, and weddings. Presumably, the number of subscribers needed to ensure viability will be fewer than 15 million. See Marc Gunther, *Finding Riches in Niches*, Fortune (Apr. 1, 2002).

course, such an outcome would remove the benefits associated with AT&T Comcast's presumed foreclosure strategy, as its affiliated programming would not be able to exert increased market power.

71. Professor Gertner claims that the “launch support” that programming networks routinely pay to new cable (and satellite) distributors demonstrates cable company buyer market power over suppliers of video programming.⁷⁰ Professor Gertner provides no support for his claim that launch support payments reflect the exercise of buyer market power by large cable operators over weak suppliers of programming, and the marketplace facts conclusively refute his assertion. I understand that networks pay launch support to even small distributors and that even the large media companies that own the most popular networks pay launch support. Indeed, all of the launch support examples that Professor Gertner gives pertain to very large and very successful programming networks (Fox News, Animal Planet, Sci-Fi Channel). Launch support thus appears to be a function, not of buyer size, but of the rational desires of programming suppliers to encourage distributor marketing of the new channel to attract viewers (and the associated subscriber and advertising revenues).
72. Haring, Rohlfs, and Shooshan argue more generally that making purchases for 30 percent of MVPD subscribers means more than making 30 percent of purchases in other market settings.⁷¹ If anything, just the opposite is true. Given the many non-MVPD distribution

⁷⁰ See SBC, Gertner Dec. ¶ 52.

⁷¹ See Qwest, HRS Dec. at 8.

and revenue alternatives available to programmers, a denial of carriage by a cable company that serves 30 percent of U.S. MVPD subscribers does not equate to cutting off 30 percent of potential revenues.

73. This is so for at least two reasons I mentioned earlier. First, static “market” share figures are very poor measures of market power given that consumers face relatively low costs of switching to DBS, for example, for alternative sources of programming.⁷² Indeed, the ability of DBS providers to quickly and easily serve MVPD customers throughout the United States means that AT&T Comcast could not, in fact, cut off even 30 percent of a video programming supplier’s potential sales. If AT&T Comcast refused to carry a program that subscribers valued, they could simply go to DBS.⁷³ Thus, an attempt by AT&T Comcast to exercise market power against video programmers – and thereby weaken the quality of its overall service – would not only leave the more than 60 million subscribers of other MVPDs available to the disfavored programmers, but AT&T Comcast’s existing base of 25+ million subscribers would be potentially up for grabs.⁷⁴

⁷² This principle should be familiar to the Commission. For example, the Commission applied it in finding AT&T “non-dominant” – *i.e.*, unable to exercise market power – in the domestic long distance market when AT&T had significantly more than half of all customers. As the Commission recognized there, the ability of other long distance providers to serve the demand and the ability and willingness of consumers to switch carriers rendered static markets shares meaningless. Order, *Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, 11 FCC Rcd. 3271 (1995).

⁷³ In fact, competition with DBS is such that AT&T Broadband has been adding networks to improve its programming offerings. For example, according to AT&T Broadband executive Allan Singer, the company has added Food Network, TV Land, and YES, as well as revamped its Hispanic and Arabic programming in response to DBS.

⁷⁴ Perhaps the most vivid recent example of this principle was the DBS targeting of Time Warner customers in New York when Time Warner and Disney reached impasse on carriage negotiations. Chris Rohrs, *Electronic Media*, at 12 (May 15, 2000) (“It is clear to everybody that
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As a result, a cable MSO has a strong disincentive to drop a network from its channel line-up, but even if negotiations were to break down and a network is dropped, the evidence is clear that DBS is an attractive distribution alternative to cable.⁷⁵

74. Second, video programming suppliers have many alternative non-MVPD distribution and revenue alternatives, both domestically and abroad. At home, program producers can sell their output to TV broadcasters and other “must have” networks, thereby obtaining cable carriage without any need to deal with a cable operator. More and more programming produced in the U.S. is being distributed abroad by MVPDs and TV broadcasters, and foreign sales are becoming a significant portion of many programming networks’ revenues. This trend is bound to increase as a result of the sustained growth in cable and satellite television worldwide and the current conversion towards digital television in many significant markets, such as Australia and Europe. This important distribution and revenue channel – which is ignored by the sole reliance on MVPD market shares – obviously reduces these video programming suppliers’ financial dependence on U.S. sources of revenues and is an additional reason why the postulated 30 percent “market

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the Time Warner-Disney dispute gave a boost to the already growing satellite television industry.”) Indeed, Disney even offered to subsidize consumers that switched to DBS. Diane Mermigas, *Electronic Media*, at 30 (May 8, 2000).

⁷⁵ As noted above, the current dispute between YES and Cablevision is costing the cable operator significant numbers of subscribers, underscoring the importance of DBS in disciplining cable. *See, e.g.*, Richard Sandomir, *YES Says No to Cablevision Proposal*, *New York Times* (March 27, 2002). In addition, I understand that Time Warner in Houston lost 35,000 subscribers when it temporarily dropped ABC from its line-up in a retransmission dispute negotiation.

share” is not the correct indicator of market power that could be hypothetically wielded by AT&T Comcast after the transaction.⁷⁶

75. As an example of the reach of many U.S. networks, we note that nine out of the top 20 networks measured by subscribers have worldwide distribution and twelve have distribution beyond the U.S. It is not surprising that the most popular networks are able to obtain international distribution. More important is the fact that about one-third of all networks have distribution beyond the U.S. That is, even less popular networks, such as New Life Network, My Pet TV, or KAlive Television, are carried internationally.
76. Qwest contends that even if AT&T Comcast’s purchases of programming – that potentially could reach 30 percent of MVPD subs – will not generally be enough to confer buyer market power, the particular markets that AT&T Comcast serves will give it power.⁷⁷ In particular, Qwest analogizes to a national long distance company that needs access to customers nationwide and cannot compete effectively with “holes” in its coverage. The analogy is flawed. A long distance telephone provider would indeed be disadvantaged without the ability to ensure that calls by its customers to any number

⁷⁶ For example, among Viacom’s program networks, MTV reaches 370 million households in 140 countries; Nickelodeon is seen in over 300 million households worldwide; VH1 reaches 100 million households worldwide; and BET International reaches 30 countries in Europe and 36 countries in Africa. See Viacom Inc., *The Facts* (available at <http://www.viacom.com/thefacts.tin>). And U.S. video programmers also sell to foreign broadcast networks. According to Disney, Walt Disney Television International owns 13 broadcast channels around the world and distributes more than 4,200 hours of programming in 120 countries. Disney-branded shows now air in 42 countries. Disney 2001 Annual Report at 24.

⁷⁷ Qwest, HSR Dec. at 9.

would be completed. But that is because universal interconnection with other telephone owners is a key feature of such telephone services. Video programming customers, in contrast, do not use that service to communicate with each other, and a video programming network therefore does not need ubiquitous coverage to have an effective offering. Indeed, there are many networks that have limited geographic coverage, simply by virtue of their content. Thus, a video programmer need only ensure that it has sufficient coverage to cover its costs, and it is clear that much less than complete national coverage is required to meet that constraint for many networks. As detailed above, many successful national programming services are carried on cable systems that serve 20 percent or fewer of all U.S. MVPD subscribers. Moreover, regional programming – and there are at least 80 regional networks -- is specifically aimed at a regional subscriber base and absence of national footprint is not an impediment to success.

77. Haring, Rohlfs, and Shooshan also argue that if a programmer were prevented from delivering its content to the eight DMAs out of the 10 largest in the U.S. served by AT&T Comcast post merger, the “quality of its advertising ‘avails’ would be significantly degraded” and would need to be sold at substantially lower rates in order to be attractive.⁷⁸ This argument relies on the unsubstantiated assumption that advertisers require access to some “critical mass” of certain DMAs in order to induce them to purchase advertising time on a network.⁷⁹ These commenters offer no evidence that these

⁷⁸ *Id.*

⁷⁹ Advertising rates may have to be reduced if coverage is denied in these DMAs, but advertising rates would fall if coverage decreases anywhere. The question is whether any reduction in such rates would result in a network not covering its costs and exiting.

eight DMAs are sufficiently different from other groupings of DMAs with comparable demographics and population levels from the point of view of advertisers. Moreover, there is no evidence provided that combining AT&T's major DMAs with Comcast's would tip the competitive balance in such a manner as to impact the viability of networks that AT&T Comcast does not carry.⁸⁰

78. But even if the claim that a programming network cannot be viable without access to some of the top DMAs were theoretically valid, its force is greatly diminished by the fact that AT&T Comcast will not serve New York or much of Los Angeles, the two *largest* DMAs (which alone account for about 40 percent of the households in the top ten DMAs). In addition, MSOs other than AT&T and Comcast also have franchises in some of the top ten DMAs, and DBS providers serve *all* DMAs.
79. Furthermore, the “*availability*” of DBS means that AT&T Comcast would suffer significant losses should it attempt to foreclose desirable programming from its line up, reducing further its incentives to foreclose.⁸¹ As discussed above, consumers view DBS and cable as substitutes and have demonstrated that they will readily switch from cable to DBS if they view the MSO's offering as inferior.

⁸⁰ Of course, it is not a proof of anticompetitive exercise of market power that an MSO with an attractive subscriber base should receive higher consideration for providing access to these customers.

⁸¹ *Time Warner II*, 240 F.3d at 1134 (citing *AT&T Corp. v. Federal Communications Commission*, 236 F.3d 729, 736 (D.C. Cir. 2001)).

80. Thus, by foreclosing popular programming AT&T Comcast would only succeed in transferring a valuable share of its customers to DBS.⁸² On the other hand, potential benefits from disadvantaging a low quality offering by a rival to create market power for one's own low quality programming are likely to be negligible since, as I noted above, buyers will not overpay for low quality programming that likely has many equally good substitutes.

81. There are at present two DBS providers that have the ability and capacity to serve virtually every cable subscriber in the United States. Four out of five new multichannel video customers now are choosing DBS over cable,⁸³ and almost one-half of existing DBS subscribers are former cable customers.⁸⁴ Further, existing cable customers can freely (and are being encouraged by DBS providers to) switch to DBS, particularly with DBS operators routinely running promotions that eliminate the up-front costs of switching.⁸⁵ Thus, as I have argued in great detail in the Cable Rules Proceeding, any attempt by a cable operator to lower the quality of its services – such as refusing to carry competitively priced programming that subscribers demand – would impose substantial

⁸² Of course, it is conceivable that failure to carry some services might result in small subscriber losses. However, because these would be services on which subscribers place relatively low value, or services for which there are many good substitutes, their foreclosure would be unlikely to permit AT&T Comcast to raise the price of its affiliated programming service.

⁸³ See AT&T Cable Rules Comments at 18.

⁸⁴ See J.D. Power & Assocs., *2001 Syndicated Cable/Satellite TV Customer Satisfaction Study*, at 79 (Sept. 2001).

⁸⁵ See Deutsche Banc Alex. Brown, *DBS Signals*, at 3 (“*DBS Signals*”).

costs on the cable operator in the form of (existing and future) subscribers lost to rivals.⁸⁶ Program suppliers would consider this competitive reality in assessing the credibility of any cable company threat to refuse carriage or impose anticompetitive carriage terms.

82. It is also the case that the putative “targets” of such foreclosure strategy have potent counter-strategies available to them. Most cable network programmers are large multi-national firms that own several different programming networks.⁸⁷ Even if AT&T Comcast were relatively indifferent as to whether it carried a given network, most of these programmers hold exclusive rights to one or more very popular networks that, if not carried, would place a cable MSO at a significant competitive disadvantage with DBS. A threat by AT&T Comcast to drop one of these programmers’ “second tier” networks in order to advantage its second tier offerings could thus be met with a threat by the programmer to retaliate by denying AT&T Comcast carriage of its entire package of programming, including the programmer’s most popular networks. In fact, it is quite common for programmers to use “bundling” in this fashion to gain “bargaining power” as well as to lessen the competitive pressures on their “weaker” offerings that face more ready substitutes.⁸⁸ For example, according to AT&T Broadband executives, Disney has bundled its popular ESPN with SoapNet and PlayHouse Disney in its negotiations with

⁸⁶ Ordover Cable Rules Dec. ¶¶ 19-24.

⁸⁷ See *2001 Video Competition Report*, App. D.

⁸⁸ Note that I do not oppose bundling as being per se anticompetitive or evidence of abuse of market power – it is often a way to bargain for a more advantageous distribution of rents, for example. Hence the examples in the text are just illustrations of how skilled and sophisticated parties attempt to deal with many complex issues regarding rates and carriage of cable network programming.

AT&T. In addition, News Corp. has bundled its highly coveted regional sports networks with its Health Network and its National Geographic channel. Finally, in a recent dispute with EchoStar, Disney's strategy was to bundle carriage of ESPN Classic with ABC Family.⁸⁹

83. **Supply Side Considerations.** Profitable foreclosure requires that AT&T Comcast gains the ability to substantially increase the price of its programming sold to unaffiliated MSOs and DBS. Otherwise, AT&T Comcast would have to offset the losses from refusing to carry valuable programming only with the programming cost savings from not carrying the foreclosed network.⁹⁰ To determine whether the merger would give AT&T Comcast an incentive to engage in foreclosure that otherwise would not be profitable requires a rigorous examination of the economics of the markets for content. Where, as here, the market for content is not concentrated and entry is possible, this alone suggests that AT&T Comcast is unlikely to gain significant pricing power by foreclosing rival programming from its cable systems. Entry into the provision of video programming has been occurring at a rapid pace. For example, the Commission's *2001 Video Competition Report* identified 51 new programming services that are being planned.⁹¹ This strongly suggests that entry impediments are low, especially given the seemingly insatiable

⁸⁹ R. Thomas Umstead and Linda Moss, *Tensions Are Rising: Nets, Ops Face Testy Contract Talks*, *TV Insite* (Feb. 25, 2002).

⁹⁰ Of course, we know that if AT&T or Comcast carry given programming this calculation alone would predict that the program would not be dropped post merger.

⁹¹ *2001 Video Competition Report* ¶ 160.

demand for new and attractive content.⁹² Furthermore, since 1995, over 100 new networks have been launched.⁹³

84. As a general matter, where several programmers compete with the foreclosing MSO's programming, simply disabling one or two would not be sufficient to gain market power, because the remaining programmers would still constrain the rates the MSO's affiliated programming can charge. Here, given the number of programmers that are in the same "space" as AT&T Comcast programming, and the strength of many of these programmers (many of which are aligned with major media/content providers, like Disney, Viacom and AOL Time Warner), even a foreclosure attempt that successfully drove a rival programmer out of business would be unlikely to be profitable. Of course, since AT&T Broadband and Comcast do not have significant ownership interests in programmers, their post-merger incentive to engage in anticompetitive foreclosure is further diluted.

85. Even if sports programming faced competition (for eyeballs) only from other sports programming (and, of course, other programming and entertainment also compete for those eyeballs), the regional sports programming interests in which AT&T Comcast

⁹² To be sure, there are possibly a handful of networks that offer highly unique content and for which there may be no close substitutes. There may be high barriers to entry into the provision of this type of programming, as measured by the magnitude of sunk costs and a high minimum viable scale. However, these programs are also generally the ones that are considered to be "must carry" in the industry, and it is implausible that a cable MSO would attempt to foreclose one of these programs because doing so would be very costly to the bottom line of the MSO. Thus, I concentrate my analysis on those programs that could be more easily duplicated and that, at least in theory, could be potential targets of a foreclosure strategy.

⁹³ *2001 Video Competition Report*, App. D.

would hold an interest (Fox Sports New England, Comcast SportsNet, Comcast SportsNet Mid-Atlantic, Comcast Sports Southeast,) face numerous well-established competitors, including but not limited to Fox's sports channels, and, most critically, the ESPN family of programming. This sports programming also competes with local news and sports programming widely carried on broadcast TV networks – programming that can gain access to AT&T Comcast cable systems as a matter of right under the Commission's must carry rules. And, of course, this programming competes more broadly against non-sports programming and other entertainment for viewers as well. Thus, it is quite implausible that AT&T Comcast could gain power in this segment of programming, even if it foreclosed its sports programming rivals from the AT&T Comcast cable systems.

86. Further, to the extent that most of this programming is “regional,” the national increase in AT&T Comcast's subscriber base is irrelevant. Clearly, the fact that through this merger Comcast's “footprint” includes new cable systems in, for example, Massachusetts, does not give it any greater ability or incentive to foreclose regional programming in the Mid-Atlantic region that might compete with its Mid-Atlantic service. Thus, arguments that AT&T Comcast will foreclose to favor existing regional programming are largely, if not wholly, non-merger specific.

87. With regard to national programming, the case for foreclosure is just as dubious. Because established national programming interests are an essential part of basic cable packages, such programming could not be realistically foreclosed. As an initial matter, each program competes with most if not all other programs making foreclosure by AT&T

Comcast implausible. Even assuming that each program competes with only programs in the same “genre,” foreclosure still would not be a viable strategy. For example, the Golf Channel competes with many large networks for major tour coverage. In particular, ESPN, USA, CBS, and ABC, among others, provide competing coverage of tour events. It seems highly unlikely that AT&T Comcast could or would foreclose any of these major networks in order to gain market power for the Golf Channel. Likewise, Outdoor Life, an adventure TV channel, competes with the Outdoor Channel, the National Geographic Channel, and Discovery Wings. Cox holds a financial interest in the latter, and Cox could retaliate by denying carriage to Outdoor Life if AT&T Comcast were to attempt foreclosure. HSN and ShopNBC are well-established and strong competitors to QVC (which also faces competition from a variety of other retail channels – such as department stores, electronics stores, discount stores, Internet retailers, direct mail, marketers and many others). E! Entertainment competes directly with Disney’s SoapNet, a channel featuring current and classic soaps, as well as news and information from the world of soaps, and also with MTV and VH1. Disney bundles SoapNet with ESPN in its carriage negotiations with MSOs, basically eliminating the feasibility of foreclosure, and MTV and VH1 are “must-have” networks. Lastly, there appear to be low barriers to entry into the type of “fashion” coverage carried by Style, as two different networks are already planned to directly compete with Style – the Fashion network, and FAD TV.⁹⁴

⁹⁴ The argument that AT&T Comcast could gain market power for its iN DEMAND service vis-à-vis MSOs is not supported by evidence. This pay-per-view and video-on-demand network offers titles from major Hollywood and independent studios, plus sports, subscription sports packages and entertainment events through its 65-channel, digital pay-per-view multiplex service. Including all possible categories of competition facing the content provided by this (continued . . .)

88. On the other hand, even if it could be shown that AT&T Comcast controlled unique “must have” content – as the merger opponents allege⁹⁵ – whatever incentive it may have to engage in foreclosure is plainly either muted or non-existent. With respect to this type of programming, driving out programming “rivals” does not add much if at all to market power but surely lowers the value of the AT&T Comcast cable franchise. In other words, if AT&T Comcast were to control truly unique programming in the future and if barriers to entry in the provision of such programming were high, AT&T Comcast would be able to exercise the legitimate market power from product differentiation. A refusal to carry other programmers would likely not significantly change the rates it could charge to other MSOs but, as noted, it would forego the benefits from showing the unaffiliated and imperfectly substitutable offerings of the rival(s).

B. Collusion Among MSOs To Favor Affiliated Programming.

89. SBC attempts to shore up the deficiencies in its claim that AT&T Comcast will control sufficient distribution to foreclose rival programmers by speculating that AT&T Comcast will collude with other MSOs.⁹⁶ The evidence so far shows no basis for this argument.

(. . . continued)

network, it is hard to see how foreclosure of a rival would increase the combined firm’s market power in the sale of the service to MSOs. Categories of competitors include premium channels such as HBO and Showtime, pay-per-view channels such as TVN, VOD platforms, and home video rental and sales. In any case, there is no evidence from the opponents of this transaction that another vendor of such a service could not effectively launch a competing service and offer it to the MSOs that are not affiliated with iN DEMAND. And, since AT&T and Comcast already have an ownership stake in the service, the transaction changes nothing, including the incentives of the owners.

⁹⁵ RCN at 25-29; SBC, Gertner Dec. ¶¶ 43-45.

⁹⁶ SBC at 9.

Despite the fact that cable consolidation has led to fewer cable distributors than in the past, there is no evidence of collusion among the remaining MSOs.⁹⁷ Indeed, the whole notion of “coordinated” action against content suppliers seems dubious at best. MSOs unaffiliated with a particular video programmer whose content is to be favored have no incentive to foreclose rivals to that programmer.⁹⁸ The effect of such collusion would be to make the unaffiliated MSOs services less attractive. The further problem is that since these unaffiliated MSOs would be among the “targets” of the foreclosure strategy – the principal reason to weaken the rival programmer is to be able to raise the prices the affiliated programmer charges to other MSOs – they would be disadvantaged on both accounts. Consequently, the owner(s) of the affiliated programs will have to compensate -- one way or another -- the MSOs without affiliated content for the potential diminution in the availability of programming and potentially higher prices. SBC and its economists have not demonstrated that such a compensation scheme is feasible (profitable for all participants) and that the collusive arrangement would remain undetected by the harmed parties or the antitrust enforcement agencies.

90. Even if theoretically possible, there is no “safety in numbers” here that would overcome the central reason why a single large MSO could not credibly threaten to drop programming that customers desire and advantage its programming in a competitive content marketplace. As described above, even while there has been an increase in

⁹⁷ *Cf. id.* at 7-8.

⁹⁸ I abstract from the possibility that the MSOs would collude with DBS providers. It does not appear that the commenters raise this as a realistic case.

consolidation in the cable industry, the competitive presence of DBS has grown dramatically. These competitors are ready, willing, and able to serve all cable customers. Indeed, the incremental costs of serving an additional household are very low for a DBS vendor. With this all too real competitive threat hanging over the “cartel’s” collective head, it is difficult to imagine a group of cable MSOs agreeing to foreclose a particular programmer given the risk of losing customers that each of them would face. In short, even if cable ownership were much more highly concentrated than it is, coordinated exclusionary behavior is not likely to be successful or long-lived.

C. Foreclosure To Favor TWE Programming.

91. SBC contends that AT&T Comcast would have an incentive to favor TWE programming.⁹⁹ This is false. The nature of the ownership interest that AT&T Comcast would have in TWE eliminates any incentive AT&T Comcast would have to foreclose TWE rivals.

92. The lack of incentive is enhanced by the fact that there is no direct way for AT&T Comcast to share in the “benefits” of foreclosure that benefits TWE. TWE currently pays AT&T Comcast no dividends, and I understand that AT&T Comcast will have no rights or ability to influence TWE to provide dividends. In fact, AOL Time Warner, which controls TWE, has every incentive to ensure that TWE earns the maximum revenues possible and that these revenues remain with TWE and do not flow to AT&T Comcast.

⁹⁹ SBC at 9-10.

93. I understand that both AT&T Comcast and AOL Time Warner view the AT&T interest in TWE as a short term interest. Even a successful foreclosure strategy that raises TWE rivals' costs would take time to bear fruit. In many instances, TWE has signed long-term carriage agreements with other cable companies that do not allow TWE to unilaterally raise rates for programming until some time in the future. Likewise, AT&T and Comcast would not be able to exclude TWE rival programmers immediately but would, in many cases, have to wait until the expiration of current carriage deals. Thus, foreclosure could potentially take years to bear fruit and all of the benefits would go to AOL TW after AT&T Comcast has given up direct financial interest in TWE.

94. But even if AT&T Comcast could find a way to share in these foreclosure "gains," its full losses from foreclosure – *i.e.*, reduction in subscribership from eliminating programming valued by subscribers – would likely not be compensated. This is because AT&T Comcast would only gain, at most, a fraction of the increased revenues earned by TWE, given that AT&T holds only a minority interest (approximately 25 percent) in TWE.

D. Foreclosure To Favor Unaffiliated Programming.

95. SBC also argues that a combined AT&T Comcast would be in a better position to advantage an unaffiliated programmer in exchange for a share of any ensuing increase in rents. According to SBC's economist, Prof. Gertner, a "company that has the power to make another entity a monopolist [by excluding its rival and driving it out of business] can negotiate for some of the monopoly rents."¹⁰⁰ The anticompetitive result is that the remaining programmer would charge higher rates to all other MVPD providers.

¹⁰⁰ SBC, Gertner Dec. ¶ 22.

Alternatively, the remaining programmer would be made unavailable to other MVPDs, thereby lowering their quality.

96. Prof. Gertner uses an example to illustrate these two possibilities, one to reduce competition among suppliers of content, the other to reduce competition among MVPDs. In the first case, a programming network, SkiTV, signs an exclusive deal with AT&T Comcast that forecloses Ski Channel, in exchange for a better price, from the AT&T Comcast cable systems. Without carriage by AT&T Comcast, Prof. Gertner argues, the Ski Channel would be forced out of business and SkiTV would be able to charge “monopoly rates” to all other MVPDs.
97. The second case instanced by Prof. Gertner, considers AT&T Comcast entering into an exclusive deal with SkiTV whereby the merged entity would not carry the Ski Channel, and SkiTV would be prohibited from signing up with other MVPDs. Such a deal would apparently cause Ski Channel to fail and also will strengthen AT&T Comcast *vis-à-vis* other MVPDs who will have no access to desirable ski-centric programming.
98. The critical assumption underlying Prof. Gertner’s argument – that without carriage by AT&T Comcast, a network would either fail or fail to reach a minimum viable scale – is the main stumbling block for this familiar theory. For the reasons explained above, AT&T Comcast will not be sufficiently large to become an essential distribution facility for programmers (cable networks). MVPDs offer access to a large number of subscribers that could provide the necessary minimum base of subscribers to enable an existing network to remain viable or a future network to launch.

99. In any case, inasmuch as the purpose of foreclosure is to hamper the currently existing programming networks, it is clear that these rivals should be able to protect themselves against an attempt by a network to buy its way into inefficient exclusivity.¹⁰¹ Indeed, AT&T Comcast would be better off if it could carry *all* of its desirable programming at attractive rates. Consequently, if a network, *i.e.* the Ski Channel, fears anticompetitive foreclosure it should be able to offer AT&T Comcast terms that would make it unprofitable for AT&T Comcast to cooperate with SkiTV to create a monopoly in the provision of skiing-centric programming. Similarly, those MSOs who fear enhanced market power from the supplier of content, *i.e.* SkiTV, could deploy strategies that would ensure the survival of the excluded network. For example, they could increase their payments just enough to ensure the viability of the Sky Channel, but not so much as to be worse off than in the case of SkiTV as programming monopolist. This argument applies especially to those distributors that are large enough to provide the necessary minimum base of subscribers to enable an existing network to remain viable.
100. Regarding future networks, their ability to launch likely would not be impaired since, as I have discussed before, post merger there will remain a large number of MVPD subscribers outside of AT&T Comcast systems as well as other sources of programmer revenue that could ease the adverse effects of exclusion from AT&T Comcast systems.

¹⁰¹ In fact, as a paper by two former Deputy Assistant Attorneys General for Economics demonstrates, the adverse effects from an exclusionary contract are most likely to arise when the foreclosed prospect cannot participate in the initial contract negotiations. *See* R. Gilbert and C. Shapiro, *Antitrust Issues in the Licensing of Intellectual Property: The Nine No-No's Meet the Nineties*, BROOKINGS PAPERS ON ECONOMIC ACTIVITY: MICROECONOMICS (1997).

101. In addition, if the threatened network is affiliated with another MSO, then exclusion may lead to retaliation against AT&T Comcast's affiliated programming. Likewise, if AT&T Comcast attempted to foreclose programming controlled by a large media company who also owned other programming, the media firm could retaliate by refusing to provide its other programming. Firms such as Viacom and AOL Time Warner, for example, own programming whose exclusion from AT&T Comcast's systems would be very costly for the merging entity.
102. *The Claim that Foreclosure (and exit) of the Ski Channel leads to increased rates to other MVPDs for SkiTV, but reduced rates for foreclosing MSO.* Such a strategy is unlikely to be profitable from the standpoint of AT&T Comcast. If, as shown above, foreclosure designed to benefit affiliated programming is not in AT&T Comcast's best interest, it is even less likely to be profitable when it is implemented by an exclusionary contract with an unaffiliated programmer. Under the contract strategy, AT&T Comcast still must bear all the costs of foreclosure but it now has to share the benefits of the strategy with the advantaged programmer. The opponents have not shown that there exists a contract that makes AT&T Comcast indifferent between exclusion and non-exclusion while leaving enough in benefits to the programmer.
103. *The Claim that Foreclosure (and exit) of Ski Channel disadvantages rival MVPDs.* As noted earlier, the purpose of this strategy is not necessarily to diminish competition in the provision of programming but, rather, to lessen competition in distribution of programming. It seems rather obvious that from the standpoint of a programmer, any restriction on its ability to reach as many subscribers as possible is of rather dubious

benefit. Hence, it will have to be compensated for the reduction in carriage with higher fees (unless it gains the side benefit of weakening its head-on rival in the provision of ski-based content). The benefit to AT&T Comcast from entering into an exclusionary arrangement with a programmer is that it would put other MVPDs at some competitive disadvantage. The extent of this disadvantage is hard to gauge. For example, there is a chance that the exclusive network is not a commercial success. In such an event, the whole strategy will prove to be a fiasco, and a possibly expensive one. On the other hand, if the network is well established and successful, AT&T Comcast may not be able to pay enough to obtain exclusivity, even if the strategy also bolsters the exclusive programmer. For example, if the exclusive contract deprives SkiTV of DBS revenues, the foregone amount may be large relative to the gains accruing to AT&T Comcast in its franchise areas from (marginally) reducing the quality of DBS. Moreover, if DBS vendors were deprived of SkiTV and if skiing networks were important, they would have only enhanced incentives to promote the Ski Channel. The financial viability of such a deal is further complicated by the need to specify how long the exclusivity arrangement has to last.

104. Besides, if the real concern is that AT&T Comcast would sign an exclusive to weaken a direct competitor such as DBS, such a concern is not related to the merger. Any (non-vertically integrated) network is now free to “sell” itself on an exclusive basis to either DBS or to MSOs. Since the MSOs do not compete with each other, if the object of the exclusive arrangement is to competitively weaken DBS, this strategy would work best if the programming were available to all MSOs and not to DBS. But, given the continuing

growth of DBS, it may be very costly for a network to sign up on such an exclusive deal or, stated another way, the MSOs may be unable to compensate the network for the exclusive arrangement *and* gain enough market power in their own markets to make this a profitable deal. Of course, a weak network may find such a deal attractive under any terms but then again denying a weak network to DBS is not likely to change the competitive balance.

VI. THE MERGER WILL NOT INCREASE THE THREAT OF FORECLOSURE OF RIVAL DISTRIBUTORS.

105. Commenters also claim that the merger will give the merged firm the ability to put rival video programming distributors out of business by denying them access to programming or services affiliated with the merged firm. This issue has already been touched upon in the previous section. Here I address this issue further.

A. Denial of Programming to Competitors.

106. RCN contends that after the merger, AT&T Comcast will deny overbuilders access to its video programming that the overbuilders allegedly need to compete against the merged company.¹⁰² As an initial matter, I understand that AT&T Comcast does not legally have an unfettered right to refuse to deal with overbuilders and other rivals such as DBS. Program access rules prohibit a vertically integrated MSO from denying competitors access to its affiliated programming. There is a narrow exception from the program access rules for terrestrially delivered programming, but with the exception of SportsNet Philadelphia and cn8, all Comcast programming is transmitted via satellite.

¹⁰² RCN at 25-34.

107. Further, RCN's argument is not merger-specific. RCN claims that Comcast already controls "must have" content and has the incentive to deny that content to RCN in Philadelphia. The merger does not "enhance" Comcast's (alleged) control of "unique" programming or affect Comcast's incentives to sell or deny RCN that programming in Philadelphia.
108. In any event, the fundamental predicates of RCN's claim are invalid. None of the programming interests that would be owned by AT&T Comcast approach the popularity of programs like ESPN, HBO, and CNN. To the contrary, as described above in response to the merger opponents' foreclosure arguments, there are viable substitutes available to cable overbuilders for all of the national programming networks that would be held by AT&T Comcast.
109. As noted in paragraph 87, Comcast's regional sports programming faces a wide array of competitors, including (but by no means limited to) national sports programming offered by ESPN, Fox, the various sports leagues, and others as well as over-the-air broadcasts of games. This programming also faces competition from other types of video programming and entertainment activities. However, it is difficult to accept RCN's assertion, without any evidence, that access to this programming is essential to an overbuilder's ability to compete.¹⁰³ This is not a matter of theory, but of fact. DBS operators continue to thrive and lure away substantial numbers of Comcast cable subscribers in the Philadelphia market without access to Comcast's regional sports

¹⁰³ Actually, Comcast does sell this programming to RCN and other overbuilders in its service areas.

programming. Finally, I understand that many games of the sports clubs that appear on Comcast's regional sports programming are carried by local broadcast TV stations, and, therefore, overbuilders and DBS providers can gain access to the same underlying content by carrying local broadcasters. And, of course, all of this sports programming must compete against other programming more generally.

110. In this regard, SBC's claim that DBS subscription rates in Philadelphia are well below the national average does not establish that this is due to the unavailability of Comcast's sports programming on DBS.¹⁰⁴ Obviously, there are many factors that affect rates as well as penetration rates, of which availability of regional sports programming may be only one. For example, DBS's penetration rates in most urban areas are somewhat lower than rural areas because DBS began marketing later in urban areas. That said, as a result of DBS's aggressive marketing campaign, half of DBS's customers reside in urban areas and two-thirds of new customers are urban.¹⁰⁵
111. In any case, insofar as regional sports programming is an attractive feature, the question arises as to the proper compensation for access to such programming by rival MVPDs. Neither Prof. Gertner nor other commenters demonstrates that AT&T Comcast would be less willing to deal on compensatory terms with other MVPD operators than Comcast is prepared to deal right now.¹⁰⁶

¹⁰⁴ SBC at 11.

¹⁰⁵ CFA, Cooper Report at 13.

¹⁰⁶ See, e.g., W. Baumol and G. Sidak, *The Pricing of Inputs Sold to Competitors*, Yale J. Reg. 171 (1994) for a discussion of pricing of such inputs to rivals.

112. DBS also offers a number of exclusive sports programs, including the highly desirable “NFL Sunday Ticket,” “NBA League Pass,” and “NHL Center Ice.” Additionally, DBS has exclusive rights to out-of-market broadcasts of the men’s NCAA basketball championships (for the fourth straight year) for 2002.¹⁰⁷ These sports networks provide a valuable line up of sports programming with which DBS can and does compete vigorously against Comcast’s sports line up.
113. In any event, it is simply wrong as a matter of economics and public policy to assume that exclusives or other vertical limits on distribution are necessarily anticompetitive. To the contrary, it is well known that such vertical arrangements can be pro-competitive.¹⁰⁸ “Antitrust laws generally favor the express or de facto exclusive distributorship as a pro-competitive means of encouraging competition between brands (‘interbrand competition’) despite the possible loss of ‘intra-brand’ competition.”¹⁰⁹ In this context, vertical limits on distribution allow a cable operator to differentiate its services from a competitor’s and thereby may create stronger incentives to promote and otherwise market the content and its service. To that extent, such arrangements may create better incentives for investment in some forms of new programming and thus inure to consumers’ benefit. Certainly to the extent the merger allows for the development of new programming that

¹⁰⁷ “DIRECTV Secures Exclusive National Rights to CBS Out-of-Market Broadcasts of Men’s NCAA Basketball Championship for Fourth Straight Year,” DIRECTV press release, http://www.directv.com/DTVAPP/aboutus/headline.jsp?id=12_10_2001A.

¹⁰⁸ See D. Carlton & J. Perloff, *MODERN INDUSTRIAL ORGANIZATION*, ch. 12 (3d ed. 1999).

¹⁰⁹ David Saylor, *Competition Issues Faced By Multichannel Video Distributors And Internet Access Services Providers And By Programmers And Other Content Vendors Under The Antitrust And Communications Laws*, 694 PLI/Pat 7 (2002) (summarizing case law).

would not otherwise have been produced, that is pro-competitive, even if that programming is exclusive to AT&T Comcast or otherwise limited in its distribution.

B. Denying Access to HITS.

114. Merger opponents contend that AT&T Comcast will deny HITS to overbuilders.¹¹⁰ As explained more fully in Mr. Braden's declaration, AT&T's ownership of HITS does not raise any competitive issues and the merger does not change the incentives to provide or deny this service to overbuilders.

115. As Mr. Braden explains, because HITS has very high fixed costs and very low marginal costs, the opportunity cost of denying service to paying customers is high. On the other hand, the benefits from denying HITS to an MVPD competitor are potentially low and also speculative. The facts detailed in Mr. Braden's declaration also make clear that HITS is not an essential facility: HITS provides satellite-delivered multiplexed content to systems that serve less than half of all digital cable subscribers (and less than a quarter of all digital subscribers, including DBS). Cable operators that choose not to purchase HITS can get direct feeds of the content available through HITS from virtually all programmers; they can turn to HITS-like alternatives, and in some cases can get terrestrial delivery. Because multiplexed digital programming is available from sources other than HITS, it is difficult to see how denying HITS to a distribution competitor would have a sufficiently significant impact on that competitor's ability to vie for subscribers to warrant foregone revenues from refusal to sell the HITS service.

¹¹⁰ SBC, Gertner Dec. ¶¶ 53-56.

116. In any event, the only possible merger-specific question is whether an alleged post-merger refusal to serve overbuilders could be expected to impact competition in the areas served by Comcast (because AT&T's incentives with respect to offering HITS to overbuilders in its territory are unchanged by the merger). As Mr. Braden's declaration makes clear, it would not.

VII. CFA'S CLAIM THAT DBS COMPETITION IS IRRELEVANT IS BASELESS.

117. The RBOCs and CFA recognize that there can be no credible claim that AT&T Comcast can exercise buyer market power if consumers can and are willing to switch to DBS should they become dissatisfied with AT&T Comcast's price or quality. Hence, they are forced to argue that DBS is not an effective competitor to cable apparently because cable rates are rising faster than the rate of inflation.¹¹¹ But the issue here is not whether cable MSOs have power over subscribers in *local retail* markets, but whether AT&T Comcast can, by owning a certain percentage of all cable systems in the country, exercise market power over *video programmers* and thereby impede the flow of programming to consumers. In order to potentially have such market power over programmers, AT&T Comcast must control a sufficient percentage of all relevant national and international distribution channels. On that score, these opponents of the merger have nothing to offer.

118. But even SBC and CFA's analysis of the effect of DBS on retail competition is flawed. Both SBC and CFA ignore the fact that the costs of the video programming purchased by cable operators—a significant component of their costs¹¹²—have increased even faster

¹¹¹ See SBC at 12; CFA, Cooper Report at 5.

¹¹² See *Report on Cable Industry Prices*, 16 FCC Rcd. 4346, ¶¶ 5, 34 (2001).

than cable rates.¹¹³ According to the NCTA, between 1996 and 2000, the cable industry spent over \$36 billion on basic and premium programming – roughly 75 percent more than the \$20.6 billion it spent during the previous five years.¹¹⁴ Prices for the most desirable programming in particular have skyrocketed. Disney, for example, recently increased the price for ESPN by 20 percent for the fourth straight year.¹¹⁵ Of course, it is entirely plausible that the cost of producing and acquiring desirable content has gone up very rapidly as well. Still, whatever the reason, programming costs are increasing faster than inflation.

119. Similarly unavailing is CFA’s reliance on “q ratio” statistics.¹¹⁶ According to CFA, the high ratio between the market value of video programming distribution assets and the “reproduction costs” of those assets shows that cable systems do not face effective competition from DBS. CFA, however, fails to recognize that the market value reflects more than the assets used to provide video programming. For example, when AOL purchased Time Warner, it acquired considerably more than just those assets used to

¹¹³ See, e.g., Seventh Annual Report, *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 16 FCC Rcd. 6005, ¶ 24 (2001) (“2000 Video Competition Report”) (noting that programming expenses rose 12.2 percent in 1999, and were projected to rise an additional 10.9 percent in 2000); *1999 Video Competition Report* ¶ 26 (reporting that programming costs increased 13.9 percent in 1998). See also *2001 Video Competition Report* ¶ 22 (programming costs for 2001 expected to exceed \$9 billion).

¹¹⁴ See Robert Sachs (NCTA), *Prepared Testimony before Senate Committee re: Cable and Video: Competitive Choices* (April 4, 2001).

¹¹⁵ See Steve Donohue & R. Thomas Umstead, *ESPN 20% Fee Hike: Maximum Headache*, Multichannel News, May 7, 2001, and Harry Berkowitz, *For Cable TV, Change Adds Up*, Newsday.com, April 12, 2002 (noting that ESPN “has been increasing fees 20 percent per year”).

¹¹⁶ CFA, Cooper Report at 51-52.

distribute video programming. It acquired Time Warner's music, publishing, and movie studio businesses, as well as various other assets in addition to its MVPD business. Thus, a comparison between the "reproduction" costs of a cable system and market value improperly mixes apples and oranges.

120. CFA also claims that an informal consumer survey conducted by Consumers Union supports CFA's contention that consumers do not view DBS and cable as close substitutes but instead as separate products.¹¹⁷ As an initial matter, the conclusions CFA seeks to draw from the informal survey are exactly the opposite of rigorous, empirical work. For example, in a recent order, the Commission reported the results of its regression analysis of the effects of DBS on the demand for cable services and concluded that "DBS is a substitute for cable service."¹¹⁸

121. The GAO reached this same conclusion in its July 2000 study, concluding that "the acceptance of satellite television services among consumers has enabled these providers to become the cable industry's most viable competitor."¹¹⁹ Moreover, due to satellite's ability to offer local broadcast networks since 1999, GAO stated that "it seems likely that DBS will become a more important competitor to cable systems in the near future."¹²⁰ GAO found further that penetration of DBS was correlated with increased non-price

¹¹⁷ *Id.* at 17-23.

¹¹⁸ *Report on Cable Industry Prices* ¶ 53.

¹¹⁹ U.S. General Accounting Office, *The Effect of Competition from Satellite Providers on Cable Rates*, at 12 (July 2000).

¹²⁰ *Id.* at 7.

competition between DBS and cable companies. “In particular, where DBS penetration was high, cable systems tended to provide more channels to subscribers.”¹²¹

122. Likewise, in a recent paper, Professors Goolsbee and Petrin collected data on the purchase decision of 45,000 households in 132 urban markets to estimate a system of demand equations for over-the-air TV, DBS, expanded basic cable services and expanded basic and premium cable services.¹²² From their estimated elasticities and shares, one can compute diversion ratios, which is a measure of substitutability between goods.¹²³ Using the Goolsbee-Petrin data, the diversion ratio from *basic* cable to DBS is between 0.41 and 0.43, which means that 41-43 percent of basic cable customers who would leave cable in response to an increase in cable prices would choose DBS instead. These diversion ratios are significant and imply that DBS and basic cable are close substitutes.¹²⁴ Indeed, as a comparison, in residential long-distance service, diversion

¹²¹ *Id.* at 4.

¹²² A. Goolsbee and A. Petrin, *The Consumer Gains from Direct Broadcast Satellites and the Competition with Cable TV*, University of Chicago Graduate School of Business Working Paper (February 2002). I note that the results presented in that paper are preliminary and subject to change.

¹²³ See C. Shapiro, *Mergers with Differentiated Products*, 10 *Antitrust* 23-30 (Spring 1996). If two goods are substitutes, then as the price of good one increases, its quantity sold decreases, and the quantity sold of good two increases. The diversion ratio (from good one to good two), measures how much of the quantity lost by good one is gained by good two and equals $(e_{21} * q_2) / (e_{11} * q_1)$, where e_{ij} is the price elasticity of demand for good “i” with respect to the price of good “j” ($i, j = 1, \dots, N$), and q_i is the volume of sales of good “i.”

¹²⁴ CFA claims that Goolsbee and Petrin reached the opposite conclusion, but they cite an outdated version of their paper, which has subsequently been revised. See CFA, Cooper Report at 4 (citing October 2001 version). Further, the cross-elasticity results obtained by Goolsbee and Petrin do not undermine the diversion ratio results that show DBS and cable compete. The
(continued . . .)

ratios from WorldCom to Sprint and from Sprint to WorldCom have been estimated to be 0.05 and 0.11, respectively, and there is little debate that Sprint and WorldCom long distance services are close substitutes.¹²⁵

123. Importantly, these inferences from the Goolsbee and Petrin econometric results likely underestimate the competitive interactions between cable and DBS. The data relied upon Professors Goolsbee and Petrin predate passage of the SHVIA, which eliminated the prohibition on DBS delivery of local network signals. As the Commission itself has recognized, the elimination of this restriction has significantly enhanced the competitiveness of DBS relative to cable.¹²⁶

124. But even if the survey relied upon by CFA could substitute for rigorous econometric analysis,¹²⁷ was conducted appropriately, reported accurately, and showed, as CFA claims, that cable is attractive primarily to customers who want a low cost “lunch bucket”

(. . . continued)

cross-elasticity of demand for cable with respect to the price of DBS is smaller than that of DBS with respect to cable price mainly because of cable’s larger subscriber base, as Goolsbee and Petrin explain in the latest version of the paper.

¹²⁵ See Declaration of Jerry Hausman, CC Docket No 99-33, Table 1 (filed Feb. 18, 2000).

¹²⁶ 2000 Video Competition Report ¶¶ 68-71.

¹²⁷ This is particularly unlikely given that it is well recognized in economics that surveyed preferences, particularly drawn from the type of unscientific survey relied upon by CFA, may not closely track actual preferences. See P. Diamond and J. Hausman, *Contingent Valuation: Is Some Number Better Than No Number*, 8 J. Econ. Perspectives 45-64 (1994).

service, CFA's conclusion that DBS does not prevent the exercise of cable market power against programmers does not follow.¹²⁸

125. CFA's argument assumes, without basis, that *all* "lunch bucket" customers have the same preferences – *i.e.*, that no "lunch bucket" customer would leave a cable operator for a "high end" DBS service if the cable operator were to reduce quality or raise the price. In reality, however, consumer preferences are heterogeneous, and many "lunch bucket" customers would shift to DBS if cable quality declined. In fact, the survey itself reveals that nearly 20 percent of all cable customers, and nearly one-third of those dissatisfied with their cable service, would consider switching to DBS.¹²⁹ As Dr. Besen has explained in the Cable Rules Proceeding, the loss of a far smaller number of customers would cause a cable operator to lose more profits than it could ever hope to recoup, even assuming it could both foreclose programming rivals and also gain market power over buyers of its own affiliated programming.¹³⁰ Thus, CFA's survey data *confirm* that DBS does prevent the exercise of market power against programmers, by ensuring that a cable MSO that degrades the quality of its offerings will lose more revenues through lost customers than it could possibly gain through a foreclosure strategy.

126. Nor is it true, as CFA contends, that DBS is a different product that does not compete with cable for "lunch bucket" consumers. To begin with, CFA's claim ignores the fact

¹²⁸ See CFA, Cooper Report at 24.

¹²⁹ *Id.* at 14.

¹³⁰ See Besen Cable Rules Dec. ¶¶ 41-57.

that cable providers have tens of millions of customers receiving digital services that, by CFA's own admission, compete head-to-head with DBS.¹³¹ Importantly, contrary to CFA's assertions, DBS does in fact offer a "lunch bucket" service. Both DirecTV and EchoStar offer "value" packages that give customers the option of buying less than the full array of DBS programming at a price very comparable to basic and expanded basic cable services. For example, DirecTV's Total Choice package is priced at \$31.99 per month and gives customers 105 non-premium channels.¹³² EchoStar likewise offers "America's Top 50" for \$22.99 per month.¹³³

127. Indeed, DBS operators themselves confirm that they compete with cable on price. DirecTV and EchoStar set their prices with "the objective . . . to gain market share by luring away consumers from the leading cable providers."¹³⁴ They have also eliminated up-front charges to make it easier for cable subscribers to switch.¹³⁵ According to the DBS operators, "the companies collect detailed data on cable pricing of many systems and, as necessary, adjust their pricing to remain competitive on a national basis."¹³⁶ Not only do cable and DBS compete on price, they also compete on quality. "DirecTV and EchoStar have been luring away cable's most lucrative customers by offering more

¹³¹ See CFA, Cooper Report at 13, 23.

¹³² See <http://www.directv.com/programming/programmingpages/0,1093,135,00.html>.

¹³³ See http://www.dishnetwork.com/content/programming/packages/at_50/index.asp?viewby=1&packid=548&sortby=1.

¹³⁴ EchoStar/DirecTV Application, Willig Dec. ¶ 11 (Dec. 3, 2001).

¹³⁵ See Deutsche Banc Alex. Brown, *DBS Signals*, at 3 ("*DBS Signals*").

¹³⁶ *Id.*

channels . . . and more movies and sports, greater pay-per-view (PPV) offerings.”¹³⁷ EchoStar continues “to utilize a ‘rifle’ approach aiming aggressive marketing campaigns at cable operators that have a material portion of their systems that have not been upgraded (or [that] EchoStar perceives [are] weak in their marketing effort).”¹³⁸ DBS providers have also featured the “DBS-only” availability of certain content – particularly sports programming – in promotions to lure subscribers away from cable service.¹³⁹

128. CFA’s assertion that the average DBS subscriber spends more than does the average cable subscriber does not prove that these two delivery modes do not compete.¹⁴⁰ Even if CFA’s claim is true, this does not show, as CFA mistakenly believes, that the *price* of any given service is higher on DBS than it is on cable. This “evidence” suggests only that DBS subscribers either take more premium services or buy packages that include more channels (and therefore, are higher priced) than those packages typically purchased by cable subscribers.¹⁴¹

¹³⁷ *Communications Daily* (Aug. 28, 2000).

¹³⁸ Jeffrey Wlodarczak, CIBC World Markets, *The Cable/Satellite Battle Continues to Heat Up at 1* (Oct. 8, 2001). CIBC predicts that “even with cable’s plethora of new services, consumers (especially in the current economic environment) are likely to be attracted by an increasingly rich EchoStar offer.” *Id.*

¹³⁹ See, e.g., DIRECTV Press Release, *DIRECTV Secures Exclusive National Rights to CBS Out-of-Market Broadcasts of Men’s NCAA Basketball Championship for Fourth Straight Year* (http://www.directiv.com/DTVAPP/aboutus/headline.jsp?id=12_10_2001A).

¹⁴⁰ See CFA, Cooper Report at 17-18.

¹⁴¹ See, e.g., Marc E. Nabi, et al., *Eye in the Sky 3Q01 Preview*, Oct. 8, 2001, at 22 (reporting that DBS subscribers on average ordered pay-per-view movies and events much more frequently than cable subscribers); John K. Martin, Jr., et al., ABN AMRO, *Cable TV Industry -- The Five Year Plan*, Jan. 2, 2002, at 83 (estimating that nearly 3 million DBS subscribers take the “NFL Sunday
(continued . . .)

129. Lastly, the “fact” that some subscribers bought both cable and DBS service likewise does not demonstrate that the two are complements and not substitutes.¹⁴² Rather, this is simply a relic of the legal limitation that prevented DBS from offering local programming. Prior to the passage of the Satellite Home Viewer Improvement Act of 1999 (“SHVIA”), DBS consumers that wanted local broadcast programming needed either to buy basic cable or use an antenna. Further, since the enactment of SHVIA, DBS operators have been aggressively adding local broadcast programming.¹⁴³ More fundamentally, the fact that a small fraction of consumers are still purchasing both basic tier cable and DBS¹⁴⁴ cannot call into question whether DBS and cable compete vigorously for the lion’s share of video programming distribution customers.

(. . . continued)

Ticket” package, which is not available on cable). CFA also says, without citation or support, that DBS has “high[] front end costs.” CFA at 155, 168. That is false. As noted, DBS providers have eliminated up-front charges, as part of their effort to lure existing and prospective cable subscribers. *See also* <http://www.dishnetwork.com/content/getdish/FreeSatelliteSys/index.shtml> (noting that Dish Network will provide satellite TV system and installation to new customers at no charge).

¹⁴² *See* CFA, Cooper Report at 22-23.

¹⁴³ *See 2001 Video Competition Report* ¶¶ 59 & 122. DBS operators will launch several new spot-beam satellites in the next year that will “provide hundreds of additional local channels to television households across the country.” Press Release, DirecTV, Inc., *DIRECTV Successfully Launches Spot Beam Satellite* (Nov. 26, 2001) (<http://www.directv.com/press/pressdel/0,1112,443,00.html>).

¹⁴⁴ *See 2001 Video Competition Report* ¶ 57 n.190 (citing report that 2 million households – or 2.2 percent of MVPD households – subscribe to both DBS and cable).

VERIFICATION PAGE

I, Janusz A. Ordover, declare under penalty of perjury that the foregoing is true and correct.



Janusz A. Ordover

May 18, 2002

March 2002

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EDUCATION

- 1968-1973 Columbia University, New York, New York
Graduate Department of Economics and European Institute of the School of International Affairs
Doctoral Dissertation: Three Essays on Economic Theory, May 1973. Ph.D. 1973.
- 1967-1968 McGill University, Montreal, Canada
Departments of Economics and Political Science
- 1963-1966 Warsaw University, Warsaw, Poland
Department of Political Economy. B.A. (equiv.), 1966.

HONORS

- 1973 Columbia University: Highest distinction for the doctoral dissertation
- 1971-1972 Columbia University: Honorary President's Fellow
- 1969-1971 Columbia University: President's Fellow
- 1967-1968 McGill University: Honors Student
- 1964, 1965 Warsaw University: Award for Academic Achievement, Department of Political Economy
- Who's Who in the World
Who's Who in America
Who's Who in the East

PROFESSIONAL EXPERIENCE

- June 1982 - Professor of Economics
present Department of Economics, New York University, New York, New York
- Sept. 1996 - Director of Masters in Economics Program
present Department of Economics, New York University, New York, New York

Summer 1996-2000 Lecturer
 International Program on Privatization and Reform
 Institute for International Development, Harvard University, Cambridge, Massachusetts

Aug. 1991 - Oct. 1992 Deputy Assistant Attorney General for Economics
 Antitrust Division
 United States Department of Justice, Washington, D.C.

Sept. 1989 - July 1990 Visiting Professor of Economics
 School of Management, Yale University, New Haven, Connecticut

 Lecturer in Law
 Yale Law School

Mar. 1984 - June 1988 Visiting Professor of Economics
 Universita Commerciale "Luigi Bocconi", Milan, Italy

June 1982 - Feb. 1985 Director of Graduate Studies
 Department of Economics, New York University

Sept. 1982 - June 1986 Adjunct Professor of Law (part-time)
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Feb. 1982 - June 1982 Acting Director of Graduate Studies
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June 1978 - June 1982 Associate Professor of Economics
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Sept. 1979 - May 1990 Lecturer in Economics and Antitrust
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Sept. 1977 - June 1978 Member, Technical Staff
 Bell Laboratories, Holmdel, New Jersey

 Associate Professor of Economics
 Columbia University

 Visiting Research Scholar
 Center for Law and Economics, University of Miami, Miami, Florida

Sept. 1973 - Aug. 1977 Assistant Professor of Economics
 New York University

Summer 1976 Fellow, Legal Institute for Economists,
 Center for Law and Economics, University of Miami

Summer 1976 Visiting Researcher Bell Laboratories, Holmdel, New Jersey

OTHER PROFESSIONAL ACTIVITIES

1997 – 1999 Consultant, Inter-American Development Bank, Washington, D.C.

1997 – present Board of Editors, *Antitrust Report*

1995 - present Consultant, The World Bank, Washington, D.C.

1998 – present Senior Affiliate
Applied Economic Solutions, Inc., San Francisco, California

1995 - 2000 Senior Affiliate
Cornerstone Research, Inc., Palo Alto, California

Fall 1995 Testimony, Hearings of the Federal Trade Commission
"Anticipating the 21st Century: Competition Policy in the New High-Tech, Global Marketplace,"
Washington, D.C.

1994 - 1996 Senior Affiliate
Law and Economics Consulting Group, Emeryville, California

1994 - 2000 Senior Affiliate
Consultants in Industry Economics, LLC, Princeton, New Jersey

1993 - 1994 Director
Consultants in Industry Economics, Inc., Princeton, New Jersey

1992 - 1993 Vice-Chair (*pro tempore*)
Economics Committee, American Bar Association, Chicago, Illinois

1992 - 1995 Senior Consultant
1990 - 1991 Organization for Economic Cooperation and Development, Paris, France

1991 Member
Ad hoc Working Group on Bulgaria's Draft Antitrust Law
The Central and East European Law Initiative
American Bar Association

1990 - 1991 Advisor
Polish Ministry of Finance and Anti-Monopoly Office
Warsaw, Poland

1990 - 1991 Member
Special Committee on Antitrust
Section of Antitrust Law, American Bar Association

1990 - 1991 Director and Senior Advisor
Putnam, Hayes & Bartlett, Inc., Washington, D.C.

1990 - 1996 Member
Predatory Pricing Monograph Task Force
Section of Antitrust Law, American Bar Association

1989 Hearings on Competitive Issues in the Cable TV Industry
Subcommittee on Monopolies and Business Rights of the Senate Judiciary Committee
Washington, D.C.

1989 Member
EEC Merger Control Task Force, American Bar Association

1988 -
present Associate Member
American Bar Association

1987 - 1989 Adjunct Member
Antitrust and Trade Regulation Committee, The Association of the Bar of the City of New York

1984 Speaker, "Industrial and Intellectual Property: The Antitrust Interface"
National Institutes, American Bar Association, Philadelphia, Pennsylvania

1983 - 1990 Director
Consultants in Industry Economics, Inc

1982 Member
Organizing Committee
Tenth Annual Telecommunications Policy Research Conference, Annapolis, Maryland

1981 Member
Section 7 Clayton Act Committee, Project on Revising Merger Guidelines
American Bar Association

1980 Organizer
Invited Session on Law and Economics
American Economic Association Meetings, Denver, Colorado

1978 - 1979 Member
Department of Commerce Technical Advisory Board
Scientific and Technical Information Economics and Pricing Subgroup

1978 – present Referee for numerous scholarly journals, publishers, and the National Science Foundation

MEMBERSHIPS IN PROFESSIONAL SOCIETIES

American Economic Association
American Bar Association

PUBLICATIONS

A. Journal Articles

"Entrepreneurship, Access Policy and Economic Development: Lessons from Industrial Organizations," with M. A. Dutz and R. D. Willig, *European Economic Review*, vol. 4, no. 4-6, May 2000.

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"Problems of Political Equilibrium in the Soviet Proposals for a European Security Conference," in *Columbia Essays in International Affairs*, Andrew W. Cordier (ed.) Columbia University Press, New York, 1971, 1951-197

D. Other Publications

"Predatory Pricing," in Peter Newman (ed.), *The New Palgrave Dictionary of Economics and the Law*, Grove Dictionaries, New York, 1999.

Book review of L. Philips, *Competition Policy: A Game Theoretic Perspective*, reviewed in *Journal of Economic Literature*, vol. 35, No.3, September 1997, 1408-9.

"The Role of Efficiencies in Merger Assessment: The 1997 Guidelines," *Antitrust Report*, September 1997, 10-17.

"Bingaman's Antitrust Era," *Regulation*, vol. 20, No. 2, Spring 1997, 21-26.

"Competition Policy for High-Technology Industries," *International Business Lawyer*, vol. 24, No. 10, November 1996, 479-82.

"Internationalizing Competition Law to Limit Parochial State and Private Action: Moving Towards the Vision of World Welfare," with E.M. Fox, *International Business Lawyer*, vol. 24, No. 10, November 1996, 458-62.

"Economists' View: The Department of Justice Draft for the Licensing and Acquisition of Intellectual Property," *Antitrust*, vol. 9, No. 2, Spring 1995, 29-36.

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"Poland: The First 1,000 Days and Beyond," *Economic Times*, vol. 3, no. 9, October 1992, 6-7.

"Interview: Janusz A. Ordover: A Merger of Standards? The 1992 Merger Guidelines," *Antitrust*, vol. 6, no. 3, Summer 1992, 12-16.

"Interview: U.S. Justice Department's New Chief Economist: Janusz A. Ordover," *International Merger Law*, no. 14, October 1991.

"Poland: Economy in Transition," *Business Economics*, vol. 26, no. 1, January 1991, 25-30.

"Economic Analysis of Section 337: Protectionism versus Protection of Intellectual Property," with R.D. Willig, in *Technology, Trade and World Competition*, JEIDA Conference Proceedings, Washington, D.C., 1990, 199-232.

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"Understanding Econometric Methods of Market Definition," with D. Wall, *Antitrust*, vol. 3, no. 3, Summer 1989, 20-25.

"Proving Entry Barriers: A Practical Guide to Economics of Entry," with D. Wall, *Antitrust*, vol. 2, no. 2, Winter 1988, 12-17.

"Proving Predation After Monfort and Matsushita: What the New 'New Learning' has to Offer," with D. Wall, *Antitrust*, vol. 1, no. 3, Summer 1987, 5-11.

"The Costs of the Tort System," with A. Schotter, Economic Policy Paper No. PP-42, New York University, March 1986. Reprinted in *Congressional Record*, U.S. Government Printing Office, Washington, D.C., 1987.

"An Economic Definition of Predation: Pricing and Product Innovation," with R.D. Willig, Report for the Federal Trade Commission, October 1982, 131 pp.

"Market Power and Market Definition," with R.D. Willig, Memorandum for ABA Section 7 Clayton Act Committee, Project on Revising the Merger Guidelines, May 1981.

"Herfindahl Concentration Index," with R.D. Willig, Memorandum for ABA Section 7 Clayton Act Committee, Project on Revising the Merger Guidelines, March 1981.

"Public Interest Pricing of Scientific and Technical Information," Report for the Department of Commerce Technical Advisory Board, September 1979.

"Economics of Property Rights as Applied to Computer Software and Databases," with Y.M. Braunstein, D.M. Fischer, W.J. Baumol, prepared for the National Commission on New Technological Uses of Copyrighted Works, June 1977, 140 pp. Reprinted in part in *Technology and Copyright*, R.H. Dreyfuss (ed.), Lemond Publications, 1978.

Book review of O. Morgenstern and G.L. Thompson, *Economic Theory of Expanding and Contracting Economies*, reviewed in *Southern Economic Journal*, September 1978.

"Manual of Pricing and Cost Determination for Organizations Engaged in Dissemination of Knowledge," with W.J. Baumol, Y.M. Braunstein, D.M. Fischer, prepared for the Division of Science Information, NSF April 1977, 150 pp.

UNPUBLISHED PAPERS

"Economics, Antitrust and the Motion Picture Industry," C.V. Starr Center Policy Paper, July 1983.

"On Bargaining, Settling, and Litigating: A Problem in Multiperiod Games With Imperfect Information," with A. Rubinstein, C.V. Starr Working Paper, December 1982.

"Supervision and Social Welfare: An Expository Example," C.V. Starr Center Working Paper, January 1982.

"Should We Take Rights Seriously: Economic Analysis of the Family Education Rights Act," with M. Manove, November 1977.

"An Echo or a Choice: Product Variety Under Monopolistic Competition," with A. Weiss; presented at the Bell Laboratories Conference on Market Structures, February 1977.

GRANTS RECEIVED

Regulation and Policy Analysis Program, National Science Foundation, Collaborative Research on Antitrust Policy, Principal Investigator, July 15, 1985 - December 31, 1986.

Regulation of Economic Activity Program, National Science Foundation, Microeconomic Analysis of Antitrust Policy, Principal Investigator, April 1, 1983 - March 31, 1984.

Economics Division of the National Science Foundation, "Political Economy of Taxation," Principal Investigator, Summer 1982.

Sloan Workshop in Applied Microeconomics (coordinator), with W.J. Baumol (Principal Coordinator), September 1977 - August 1982.

Economics Division of the National Science Foundation, "Collaborative Research on the Theory of Optimal Taxation and Tax Reform," July 1979 to September 1980, with E.S. Phelps.

Division of Science Information of the National Science Foundation for Research on "Scale Economies and Public Goods Properties of Information," W.J. Baumol, Y.M. Braunstein, M.I. Nadiri, Fall 1974 to Fall 1977.

National Science Foundation Institutional Grant to New York University for Research on Taxation and Distribution of Income, Summer 1974.

APPENDIX 6

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)	
Applications for Consent to the Transfer of)	
Control of Licenses)	
)	MB Docket No. 02-70
From COMCAST CORPORATION and)	
AT&T CORP.,)	
)	
Transferors,)	
)	
To AT&T COMCAST CORPORATION,)	
)	
Transferee.)	

DECLARATION OF MARK A. COBLITZ

I. QUALIFICATIONS AND PURPOSE OF TESTIMONY

1. My name is Mark A. Coblitz and I am Senior Vice President for Strategic Planning at Comcast Corporation (“Comcast”). I have been with Comcast since 1989 and have held my current position since 2000.

2. I am responsible for evaluating and analyzing new products and services, particularly those involving emerging technologies, for potential deployment to Comcast customers. In this capacity, I was involved in Comcast’s initial decision to develop a high-speed Internet service in the mid-1990s, as well as its decision to launch this service in partnership with At Home Corp. (“At Home”). I have also had responsibilities relating to the deployment by Comcast of cable telephony, interactive television, video-on-demand, and home networking products.

3. In addition, I have represented Comcast in CableLabs and have worked with CableLabs to develop specifications for cable modems, set-top boxes, and other

cable-related equipment and software. I am a member of the CableLabs Technical Advisory Committee, and I chair CableLab's Packet Cable Committee and CableLab's Open Cable Business Committee.

4. I submit this declaration in support the above-referenced license transfer application of Comcast and AT&T Corp. and in connection with the proposed merger (the "Merger") of Comcast and AT&T Broadband Corp. ("AT&T Broadband") to form AT&T Comcast Corporation ("AT&T Comcast").

II. SET-TOP BOXES

5. I understand that several commenters have suggested that, following the Merger, Microsoft Corporation ("Microsoft") will have undue influence over AT&T Comcast or CableLabs relating to set-top box software. This suggestion is wrong for many reasons, several of which are summarized below.

A. Microsoft and AT&T Comcast

6. AT&T Comcast will have a powerful incentive to avoid becoming dependent upon a single software vendor for the operating systems or middleware used on set-top boxes. It is not in Comcast's interest and it will not be in AT&T Comcast's interest to allow Microsoft (which will control less than 5 percent of AT&T Comcast's vote) or any other software vendor to supply such a large percentage of set-top box operating systems or middleware that the vendor could dictate prices, features, standards or other terms relating to set-top boxes. Such market power would only serve to enrich the software company at the expense of AT&T Comcast and cable customers.

7. For this reason, Comcast has historically insisted on working with at least two vendors in most product areas. And despite the fact that Microsoft at one point invested approximately \$1 billion in Comcast, Comcast has not deployed Microsoft

software in its set-top boxes, but instead has deployed software designed by other vendors.

8. This policy (of dealing with multiple vendors) is reflected in Comcast's term sheet agreement with Microsoft regarding Microsoft's interactive TV middleware. This agreement does not obligate Comcast to deploy this middleware commercially unless: (i) Microsoft completes successful trials and meets other significant conditions; (ii) *either* the deployment meets Comcast's reasonable business objectives *or* Comcast deploys an alternative middleware solution for the current generation of set-top boxes; and (iii) Microsoft's middleware is competitive with alternative middleware solutions. Moreover, even if these conditions are met, Comcast will not have any obligation to roll out Microsoft middleware to more than 25% of its newly installed middleware customer base, and the agreement does not apply to future generations of set-top boxes.

9. Comcast has deliberately preserved its ability to test and deploy alternative set-top box middleware, and has not allowed – and will not allow – Microsoft to control its decision-making concerning the optimal middleware solution for current or future set-top boxes.

B. MICROSOFT AND CABLELABS

10. One of the purposes of CableLabs is to develop common specifications for cable-related hardware and software so that these products can be sold to consumers across the United States and used on different cable systems. All of the major cable companies (with the exception of Cablevision Systems Corp.) are represented on the board of CableLabs.

11. As a practical matter, all major CableLabs decisions are arrived at by consensus. This is because the basic purpose of CableLabs would be undermined if its members adopted different technical specifications for their individual systems.

12. CableLabs – with AT&T Broadband’s and Comcast’s support – has promulgated a technical standard for set-top box software that will allow both the operating system software and the middleware to be interoperable with alternative software combinations. The key to this approach to set-top box software was the adoption of common application program interfaces (“APIs”) that allow any software company to write software that will function with different operating systems or middleware. This modular approach to operating systems and middleware was adopted deliberately to foster competition among software companies and to avoid the risk of creating a monopoly for operating systems or middleware.

13. The specifications that CableLabs has published for the next generation of set-top boxes (“advanced set-top boxes”) will require middleware software vendors to incorporate Java software code into their middleware. Java, a product of Sun Microsystems, is one of Microsoft’s most vigorous competitors. CableLabs considered, but rejected, Microsoft’s alternative solution.

C. SET-TOP BOXES FOR DSL

14. I understand that one commenter has suggested that AT&T Comcast might attempt to block the development of set-top boxes that can integrate video programming and broadband services provided by DSL. In fact, point of deployment (“POD”) technology has already been developed that permits the function of controlling access to premium cable services to be separated from the remaining functionality of the set-top

box. A set-top box manufacturer could make a set-top box that uses POD technology to access video programming and uses DSL technology for broadband services.

D. RETAIL SALES OF SET-TOP BOXES

15. I understand that one commenter has suggested that the merger may affect the extent to which set-top boxes are sold at retail outlets. This makes no sense. AT&T Comcast (along with the entire cable industry) will continue to have a strong incentive to encourage the retail sale of set-top boxes. This is so because DBS is well established in the retail set-top box market and currently captures the vast majority of new subscribers interested in purchasing their own set-top box equipment. After the merger, AT&T Comcast would have the same interest that AT&T Broadband and Comcast currently have in fostering the development of a retail market for set-top boxes as a competitive response to DBS.

16. I note that AT&T Broadband, Comcast and the other members of CableLabs have actively supported retail sales of set-top boxes by promulgating the OpenCable Application Platform (“OCAP”) specifications. Equipment manufacturers are currently developing set-top boxes that can comply with OCAP specifications. These set-top boxes will be able to be either rented to subscribers or sold at retail (using POD technology). Moreover, television manufacturers are currently exploring the possibility of integrating set-top box functionality into televisions themselves, which promises to create a whole new dimension of competition in retail set-top box sales.

III. BROADBAND INTERNET ISSUES

A. FACTUAL BACKGROUND

17. Comcast launched its broadband Internet service commercially in late 1996 in partnership with At Home. In order to launch this service, Comcast was required to

invest substantial resources in, among other things, upgrading its cable plant to permit two-way, high-speed communications by means of hybrid fiber-optic coaxial (“HFC”) cables running from the headends in Comcast’s cable systems. At Home had substantial responsibilities relating to the maintenance and operation of many of the facilities linking Comcast’s cable network to the Internet.

18. In connection with the formation of At Home, Comcast entered into a distribution agreement with At Home that required Comcast (with certain exceptions) to use At Home as its exclusive Internet Service Provider (“ISP”). Comcast entered into this exclusivity obligation for a number of reasons, including its belief that the agreement would provide an appropriate incentive for At Home to invest in developing its Internet service and its conclusion that there were a number of significant technical complexities associated with dealing with multiple ISPs.

19. At Home filed for bankruptcy in September 2001 and ceased operation in February 2002. As a result of this, Comcast was required to transfer – at significant expense to the company – all of its high-speed Internet customers to a network that is currently managed by Comcast.

20. As of the first quarter of 2002, Comcast had approximately 1.041 million high-speed Internet customers out of approximately 11.299 million “marketable” homes passed (that is, homes passed that are located in areas where Comcast has launched its Internet service). This represents a penetration rate of approximately 9.2% for Comcast’s high-speed Internet service.

B. COMPETITIVE CONDITIONS

21. Comcast’s Internet service faces stiff competition from a number of Internet access providers. As an initial matter, Comcast faces competition from “dial-up” or

“narrowband” providers. The vast majority of residential Internet users in the United States subscribe to “narrowband” dial-up service as compared to high-speed broadband services. Comcast views dial-up access providers – such as AOL, Earthlink and others – as serious competitors and implements competitive strategies and programs (i) to persuade narrowband customers to switch to broadband and (ii) to convince broadband customers not to switch back to narrowband.

22. In addition, Comcast faces competition from so-called broadband access providers, using DSL and other technologies. Among the largest and best-financed of these competitors are the Regional Bell Operating Companies (“RBOCs”), Verizon, SBC, BellSouth, and Qwest. These firms are tenacious competitors. For example, when Comcast was forced to migrate customers from the At Home network to its own network on short notice, some of the RBOCs announced special promotions designed to take advantage of the customer confusion and disruption caused by these emergency measures.

C. INTERNET CONTENT

23. To date, the arrangements between Internet content suppliers and Comcast have generally been distribution and marketing arrangements. In these arrangements, Comcast agrees with the content owner to display the content (or a link to it) on its portals (comcast.net and quickclicks.tv), where it is likely to be seen by web users.

24. Comcast has virtually no interests in or agreements relating to “broadband content” – which I understand refers to content that is customized or optimized in some way for viewing over a broadband connection. Comcast’s affiliated websites (such as www.comcast.net and www.quickclicks.tv) display a few links to websites that could be

said to distribute broadband content. To my knowledge, Comcast's only ownership interest in so-called broadband content is an approximately 3 percent interest in a start-up Internet video-on-demand company called Intertainer, which could arguably be said to provide "broadband content."

25. Most subscribers to Comcast's Internet service use this service to access traditional "narrowband" content – such as news, stock quotes, chat rooms, and the like – not content that is customized in any way for "broadband." Comcast obtains its portal content from a widely known Internet content aggregator (Screaming Media) on a non-exclusive basis.

26. Comcast has not attempted to prevent consumers who subscribe to competing Internet services from accessing the content displayed on Comcast's portals. Instead, consumers using any ISP can access Comcast's portals and view the content simply by typing the URL for these portals (www.comcast.net or www.quickclicks.tv). Alternatively, these consumers can simply go directly to content owners' own website.

27. In addition, consumers who subscribe to the high-speed Internet service offered by Comcast are able to access any other content they wish on the Internet. Comcast has never attempted to censor or otherwise limit the content that subscribers access. (Like many Internet services, however, Comcast offers customers the ability to use parental control software to control the access of children to particular types of content.) In fact, subscribers can even select an alternative homepage (such as Yahoo! or AOL) and never view the content offered by Comcast at all. Many subscribers do just this. Even if customers keep the Comcast portal as a home page, they can simply type in

an alternative URL and go to that location on the Internet. Comcast currently imposes no time limits on streaming videos.

28. Comcast has no intention of attempting to block its subscribers' access to any Internet content. It is my understanding that, post-merger, AT&T Comcast will continue this policy. AT&T Broadband and Comcast Internet subscribers, like most Internet users, are accustomed to accessing whatever content they want. I believe that, if Comcast (or AT&T Comcast) were to start blocking or otherwise disadvantaging desirable broadband content, it would cause an uproar among its subscribers and damage its Internet business – ultimately driving customers to switch to Comcast's competitors. As explained below in paragraph 29, instead of blocking content, AT&T Comcast will have the incentive to encourage the development of a broad and diverse array of "broadband content" so as to encourage consumers to switch from dial-up Internet services to broadband services.

29. As noted, Comcast has a relatively low penetration rate for high-speed Internet services (approximately 9.2%). Comcast believes that an important way to increase that penetration rate and to respond to its many competitors is to encourage and facilitate the creation of diverse and compelling broadband content. AT&T Comcast will have every incentive to continue to encourage the creation and distribution of new broadband content. This is so because, if such content were created, it would attract more customers to broadband and would help encourage broadband customers to switch from dial-up services. Indeed, if a supplier of broadband content were to create a highly compelling "broadband" application, any effort by Comcast to block or disadvantage this

application would only drive customers away from Comcast and to other competing Internet services.

D. INDEPENDENT INTERNET SERVICE PROVIDERS

30. Comcast recently entered into an agreement with United Online, Inc. (“United”) – an Internet Service Provider (“ISP”) created by the merger of Juno and NetZero – which provides that United may offer an ISP service to consumers using Comcast’s broadband network. Comcast entered into this agreement with United within several weeks of the end of its exclusivity obligation to At Home. I understand that AT&T Broadband has also entered into such agreements with independent ISPs.

31. I believe that Comcast and, following the merger, AT&T Comcast will have ample incentive to enter into other agreements with independent ISPs in the future. As noted earlier, penetration rates for the broadband services offered by AT&T Broadband and Comcast are still relatively low and both companies face stiff competition from DSL and other emerging broadband platforms, as well as from dial-up providers. In this highly competitive environment, AT&T Comcast will have a strong incentive to contract with independent ISPs because these ISPs have the potential to attract new customers to AT&T Comcast’s network.

32. For example, independent ISPs can market broadband to their existing narrowband customers or develop applications and content that will attract new customers to broadband. To the extent that these ISPs have negotiated arrangements with AT&T Comcast, the company will share in some of the revenues generated by these new customers. Alternatively, if these ISPs affiliate with competitive broadband platforms, AT&T Comcast will miss the opportunity to gain new customers and revenues. For this

simple reason, AT&T Comcast will have a significant incentive to continue to work with independent ISPs.

33. I note that there are still significant technical and operational complexities associated with dealing with multiple ISPs. Comcast continues to work to analyze and address these complexities. Comcast expects that its experience in implementing the United agreement will provide additional information concerning the technical and operational issues raised by dealing with multiple ISPs.

I, Mark A. Coblitz, declare under penalty of perjury that the foregoing declaration is true and correct. Executed on May ^{11th}, 2002.



Mark A. Coblitz