92. Rubinfeld/Sidak further state that some of the services supported by broadband connections are unavailable (or less satisfactory) with narrowband connections. Rubinfeld/Sidak Decl. ¶¶ 23-24. A similar observation could be made about high-end and low-end personal computers. The high-end model may support DVD movies, 3-D graphics and a variety of scientific, engineering and gaming applications that the low-end model does not. Yet the high-end and low-end models compete in the same market if most potential users regard them as substitutes for the computers' predominant uses. In any event, the overwhelming majority of Internet content *is* accessible by both narrowband and broadband last-mile transport; the only difference is the speed or quality at which the content downloads.

93. It is significant in this regard that AT&T has no means of identifying the minority of potential users of broadband for whom narrowband service is *not* an acceptable substitute, and thus has no means of charging higher prices to the minority than the majority. Absent the ability to engage in discrimination of this kind, two distinct products or services do not need a complete overlap in their functionalities, and do not need to be regarded as functional substitutes by all potential purchasers, to coexist in the same relevant market. It is sufficient that most potential purchasers regard the two items as reasonable substitutes for most uses.

94. Finally, Sidak/Rubinfeld rely on the econometric "study" Dr. Hausman provided in the *AT&T-TCI* proceeding. Rubinfeld/Sidak Decl. ¶ 26. In that study, Hausman purports to demonstrate that narrowband and broadband access are in separate markets. We have already demonstrated in our *AT&T-TCI* merger proceeding testimony the numerous fallacies with the Hausman study, and Dr.

Hausman chose not to resubmit that study, or, indeed, *any* study in this proceeding. *See* Ordover-Willig TCI Decl. ¶¶ 13-22. The statistical analyses performed by Professor Hausman were poorly specified, inadequately described, and inapposite to actual market conditions. Indeed, many of these analyses contradicted Hausman's key conclusions and indicated that broadband and narrowband last mile transport are in the same product market.

95. Tellingly, while Dr. Hausman has provided a Declaration in this proceeding, he does not respond to any of these criticisms. Sidak and Rubinfeld likewise simply assert that the Hausman study is accurate without claiming to have independently reviewed the study or responding to any of our criticism.[9]

96. In short, the proponents of forced access regulation offer no legitimate basis for a conclusion that broadband and narrowband-delivered online services are in separate markets today, or will be in separate markets in the foreseeable future.

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[9] Sidak and Rubinfeld also cite a study by Varian, but even a cursory analysis of that piece shows that they have employed it far beyond its valid weight. The cross-elasticities calculated by Varian, presumably the basis for Sidak and Rubinfeld's claim, had large standard errors. Thus, one cannot reject the hypothesis of a positive cross-price elasticity any more than one can reject the hypothesis of a negative cross-price elasticity. Indeed, given the positive (though small) cross-price elasticities that Varian calculated for 96 kbps access, one could cite evidence to the contrary. The point is that with large standard errors no firm conclusion can be drawn. Moreover, as Varian concedes, the sample population he used – which was largely drawn from students at UC Berkeley – is obviously not representative of the US population. Thus, relevant conclusions about demand behavior cannot be validly adduced from the Varian study.

2. AT&T's Services Face Effective Competition From Other Broadband Services.

97. Proponents of forced access regulation respond with speculation that a broadband-only market might develop in the future. That is, of course, possible. But opinions over whether (and, if so, when) that will occur are quite disparate. As noted above, AOL and its contemporaries have been among the most vocal critics of such speculation, predicting that broadband and narrowband will continue to compete – and that narrowband will continue to be the big winner in the competition – as much as five years into the future. But even if AOL's lawyers turn out to be better at predicting the future than its business people, we do not see how it could seriously be disputed that there will at that point likely be lots of broadband alternatives to cable.

98. The Commission has already found, and we agree, that, even ignoring narrowband options, in the near term cable modem service is likely to be one of many nearly equally attractive alternatives with counterbalancing benefits and drawbacks. *See 706 NOI Report* ¶ 99 & Charts 2-3. We likewise agree that the market for Internet and online services is "extremely competitive and highly fragmented," with "no substantial barriers to entry." *AT&T-TCI* ¶ 93. Indeed, recent events have confirmed the correctness of this view. As described in detail in the Public Interest Statement, major industry players have recently announced that they intend to invest billions of dollars in lots of different technologies used to provide last-mile broadband transport, such as DSL, satellites and fixed wireless. *See* Public Interest Statement at 74-82.

99. In this regard, claims that DSL and satellites are fundamentally flawed as broadband alternatives appear to us to amount to little more than histrionics. GTE at 41-44; Declaration of Dale

E. Veeneman and Everett H. Williams, filed on behalf of GTE Service Corp. *et al*, ¶¶ 10-13 (Aug. 23, 1999). Hardly a day passes without confirmation that business leaders and investors think otherwise and are willing to back up their beliefs with billions of dollars of investments. As AT&T and MediaOne detail in their reply comments, all of the major incumbent LECs have been racing to deploy DSL on their networks in the wake of AT&T's proposed mergers with TCI and MediaOne. For example, AOL and GTE – the principal proponent of the argument that DSL is non-viable – just two months ago reached a deal to allow AOL to reach nearly 4 million homes in GTE's service territories by the end of this year with DSL.[10] Indeed, with this deal, and similar arrangements it has made with the Bell operating companies, AOL will have the potential to reach 65 percent of U.S. homes with DSL service.[11] The leading competitive LEC supplier of DSL, Covad, has similarly announced that it will shortly be able to reach 40 percent of U.S. homes.[12] DSL is now growing at a "consistently faster pace" than cable modem services nationwide.[13] With DSL sales "exploding," analysts predict that there will be upwards of 3.0 million DSL customers in the United States by the end of 2000.[14]

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[10] *AOL Expands Broadband Offerings*, InternetNews.com (July 27, 1999) <www.internetnews.com/isp-news/print/0,1089,8_169601,00.html>.

[11] *Id.*

[12] *Covad Expanding Network to 40 Percent of U.S. Homes and Businesses* (Sep. 2, 1999) <www.covad.com/about/press_releases/press-0902996.html>.

[13] U S West News Release, "U S WEST 'MegaBit Services' ADSL Subscriber Rate Jumps More Than 250 Percent In First Half Of 1999" (Aug. 17, 1999) (quoting report by analyst firm *TeleChoice*) <www.uswest.com/news/081799.html>; Gary Arlen, "@Home's September 31 Deadline Nears," *Broadband Week* (Sept. 13, 1999) ("DSL-service providers are trailing cable-modem services by about one year, but catching up fast") <www.multichannelnews.com/b4.shtml>.

[14] Gary Arlen, "@Home's September 31 Deadline Nears," *Broadband Week* (Sept. 13, 1999).

100. Claims regarding the inferiority of satellite-based technologies also appear misguided. GTE at 46-47; Echostar at 3. That satellites currently provide high-speed transmission in only one direction is irrelevant to the vast majority of users who, if they worry about speed at all, are primarily interested in fast download times and do not send significant amounts of information. Satellite service to a household also may have a lower marginal cost than cable broadband service, because installing a satellite receiver in the household does not require wiring the house to a cable network serving the neighborhood, or even wiring the neighborhood at all.

101. Again, investment patterns confirm the commercial reality that satellite is a serious broadband contender. Hughes Electronics Corp. has announced that the DirecPC system is up and running and ready to compete with other high-speed services and has announced a deal with AOL to develop dual purpose AOL TV/DirecTV set top boxes that will provide AOL's Internet access serve nationwide via the DirecPC satellite system. Public Interest Statement at 79. In addition, Hughes and Teledesic have announced that they will each invest billions of dollars in two-way broadband data satellite networks. *Id.* at 79-80. And SkyCache, Inc., which currently serves over 3 million Internet users, announced this week that it is upgrading its satellite datacasting service to T3 speeds with Digital Video Broadcast technology. "Skycache Delivers Big – Global Internet Datacasting Service to 45 Mbps; Company to Broadcast Web Content, Internet Video Up to T3 Speeds By Year End" (Sept. 14, 1999) <www.xdsl.com/newsreleases/xDSL/ 5162.asp>.

102. In short, there is no reason to assume that cable modem service is, or will ever be, the only viable way of providing broadband last-mile data transport.

103. For these and other reasons, we are puzzled by the claim of many of the merger opponents that the principal evil here is the effective merger of @Home and Road Runner. *See* Bell Atlantic at 20-21, 38-39; GTE at 32-33. Although we understand that there will be important limitations on AT&T's ability to control either or both of those entities post-merger, we proceed here for the sake of argument under the counterfactual assumption that AT&T will gain full control of both entities.

104. For what we think are obvious reasons, the merger opponents never bother to explain who would be harmed by this combination (much less how the harm will manifest itself). Certainly, consumers in the areas served by AT&T or MediaOne are not harmed; the cable-based online services available to them will be unaffected by the merger. AT&T@Home service will continue to be provided in existing AT&T service areas and MediaOne Roadrunner service will continue to be provided in the MediaOne service areas (as we understand that AT&T and MediaOne have contractual obligations to provide those services through at least 2002). More fundamentally, consumers will continue to have myriad other competitive sources for online services to the extent any perceive that AT&T's influence over @Home or Roadrunner has adversely affected the price or quality of these cable-delivered services.

105. Nor, as we explain in more detail below, can there be any serious argument that the combination will give AT&T power over content providers or advertisers. Whether considered separately or together, @Home and Road Runner have no monopoly over Internet access facilities,

regardless of whether broadband access alone constitutes a relevant antitrust market. Further, content providers and advertisers have many non-Internet-based means to deliver their messages.

106. Perhaps it is other cable companies, then, that AOL and GTE seek to protect from AT&T. But it is equally clear that they are not at risk. Those cable companies that already have exclusive deals with @Home or Road Runner – most large cable companies, according to AOL and GTE – have locked-in prices under long-term contracts that were established when @Home and Roadrunner were unquestionably competing to supply cable companies. Nor can the merger impact other cable companies that have already chosen to utilize the services provided by competitors of @Home and Road Runner. That leaves only the small domain of "unsigned" cable companies. As set forth in detail in the Public Interest Statement (at 87-88), several other companies compete with @Home and Road Runner for the business of cable companies. Thus, an attempt by @Home or Road Runner to charge unsigned cable systems supracompetitive rates would likely drive these cable systems to a competitor.

107. In this regard, opponents of the merger have not offered any evidence rebutting AT&T's showing in the Public Interest Statement (at 88) that @Home and Road Runner do not control proprietary assets or systems that could not be duplicated by other firms with knowledge of the industry, including the unsigned cable companies themselves. Nor can opponents buttress their arguments by pointing to the fact that @Home and Road Runner currently have an 80 percent share of the cable broadband "markets." *See, e.g.*, Bell Atlantic at 39. Most of that percentage reflects buyers who are business partners or owners of @Home or Road Runner and thus would be a poor indicator of

the strength of these companies with regard to their competitors in attracting unaffiliated cable systems on a going forward basis.

3. Even if it Were Conceivable that AT&T Might in the Future Gain a Monopoly in a Relevant Antitrust Market, that Would Not Justify Regulation Today.

108. Even in the unlikely compound event that in the future a separate broadband market were to develop *and* cable modem-based services were to dominate it *and* AT&T and other cable companies failed to develop satisfactory commercial arrangements with other online service providers *and* someone could devise a regulatory solution for which benefits exceeded costs, that scenario would not justify prophylactic regulation now. Opponents of the merger have not offered any evidence or argument as to why it would be harder to regulate at that time – when the preconditions for access regulation are hypothetically satisfied – than it would be now. Nor could they.

109. That is because AT&T's Internet customers are not "locked in" when they choose to buy cable-based service from AT&T. They pay only monthly charges pursuant to short term contracts. Moreover, contrary to GTE's suggestions, GTE at 47, AT&T and MediaOne Internet customers do not ordinarily purchase cable modems. Rather, a leased cable modem is generally included in the monthly subscriber charges that they pay. Hence, switching from cable modem service to service via satellite or DSL involves virtually no loss of sunk investment by the customer.

110. Nor, as we understand it, does AT&T have plans to install equipment that would make it more costly to "unbundle" cable internet service in the future than today. Indeed, it is quite likely that the opposite is true. Even proponents of forced access concede that multiple ISP access to cable

facilities has been subject to only very limited trials at this stage. And @Home executive Milo Medin describes a number of potential hurdles to that approach, including some that could negatively affect consumers. GTE and others claim that these problems will not arise. But if, as they claim, they plan to roll-out multiple ISP access to their cable facilities more broadly in the future, then their claims will be market-tested and any future commission contemplating forced access could then rely on experience rather than competing claims.

C. The Monopoly Leveraging Claims Advanced By Opponents, Although Certainly Creative, Are Not Remotely Plausible.

111. GTE and others raise a host of arguments as to why AT&T has the incentive and ability to "leverage" broadband "monopoly" power into other adjacent markets (whether through tying, price squeezes, or by foreclosing rivals' access to AT&T customers).[15] All are contrary to basic economic theory. First and foremost, as explained above, AT&T has no monopoly in any relevant antitrust market. Without a monopoly in one market, there can be no "monopoly leveraging" to other markets.[16]

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[15] GTE at 49-55. *See also* MCI at 7-9, 22-25; SBC at 40-43; Qwest at 13; Bell Atlantic at 35-38; CU at 28-31; Rubinfeld/Sidak Dec. ¶¶ 25-28, 52-55; Gertner Dec. ¶¶ 25-27.

[16] In this regard, the Commission should reject out of hand any notion that AT&T would have market power because there is a group of users who have special tastes or needs and are willing to purchase only cable modem services. AT&T obviously cannot aspire to offer service only to those niche groups. Likewise, AT&T cannot price discriminate against them when it offers Internet services to other consumers, and thus even these users will reap the benefits of the competitive marketplace.

112. Further, leveraging into other related markets is not realistic where access to the public Internet is "one click" away. More specifically, as noted above, consumers can access the public Internet and any content accessible thereby without viewing any of the links on the @Home or Road Runner home pages. This access would clearly defeat any "leveraging" strategy were AT&T foolish enough to attempt it. By definition, AT&T's pledge to provide "one click" access to the public Internet – and even to allow its customers to bypass the @Home content altogether – prevents it from foreclosing its customers to any content provider or the home page of any online service. And no content provider would agree to pay AT&T supra-competitive charges for accessing AT&T customers through the AT&T@Home portal or the MediaOne Road Runner portal when those same customers can easily reach the content provider through the public Internet.

113. Just as importantly, AT&T has no incentive to undertake such anticompetitive conduct. As noted, AT&T is a new entrant and has invested billions of dollars of shareholder resources in cable systems. The only way for AT&T to make these huge investments pay off is to gain market share and attract substantial numbers of new customers to its cable-based services such as AT&T@Home. To attract customers, AT&T must offer attractive content. The leveraging/tying strategies postulated by the merger's opponents would all make AT&T's product less valuable by reducing the quantity or quality of the content that would be available via AT&T. In short, AT&T would be shooting itself in the foot at the beginning of the race.

114. Hence, it is unsurprising that AT&T is offering open access to all Internet content and has pledged to continue to do so. Nor is it surprising that there have been press reports that AT&T is

negotiating with other Internet players, including those who claim that only access forced by regulation will give them access to cable. It is in AT&T's interest to come to agreement with any provider that will offer content that AT&T's customers will find attractive. Thus, AT&T has every incentive to enter into commercially reasonable access arrangements with other providers.

115. In all events, the so-called "markets" that AT&T would "leverage" into or "tie" are not markets at all in any relevant antitrust sense and, even if they were, AT&T has no conceivable means to leverage into them. We consider each in turn.

116. *Internet telephony.* Internet telephony is not a relevant market. Indeed, as we understand it, Internet telephony does not yet exist as a commercially available product. Moreover, once it becomes available, it would obviously compete with circuit switched services. Those raising this "leveraging" claim, of course, are monopolists in this market and any claim that AT&T is likely to capture that monopoly should be rejected out of hand.

117. *Internet video streaming.* Again, this is not a relevant market. Internet video streaming clearly competes, at a minimum, with video programming offered by cable systems, satellite companies, and television broadcasters. Further, any attempt by AT&T artificially to limit video streaming would cause AT&T to lose customers to other broadband providers such as the incumbent LECs. We also understand that there are pro-competitive explanations for limits on cable-delivered Internet video streaming including the need, inherent in the shared nature of the cable plant, to ensure that a few bandwidth "hogs" do not slow down and degrade the experience of all users. *See* Press

Release, "Excite@Home Responds to Misleading Claims by GTE and AOL," (June 15, 1999) <www.home.net/news/pr_990615_01.html>.

118. *Internet backbone transport.* Although the Commission appears to regard Internet backbone transport as a relevant market, Memorandum Op. and Order, *In re Application of WorldCom, Inc. and MCI Communications Corp. for Transfer of Control of MCI Communications Corp. to* WorldCom, CC Docket No. 97-211, ¶ 148 (Sep. 14, 1998), the "tipping" effect postulated by the merger's opponents is baseless. Even if AT&T captured 100 percent of current and likely near-term broadband access customers, and even if AT&T were able to require @Home and Road Runner to use AT&T's own backbone transport facilities to carry all this traffic, and even adding the traffic from AT&T's traditional dial-up Internet access service, AT&T would still carry only a small fraction of the total traffic over Internet backbone. This fact alone prevents AT&T from taking advantage of "network effects" and imposing anticompetitive terms on other backbone providers. If anything, it is AT&T that must worry about the terms other backbone providers seek to impose for terminating AT&T's Internet backbone traffic. Currently, the lion's share of Internet traffic is carried by a handful of firms, including two of the principal proponents of forced access – MCI and GTE.

119. *Internet advertising.* This is not a relevant market. There are multiple ways for advertisers to reach consumers beyond the Internet, many of them demonstrably more effective. Moreover, there is little, if any, different advertising for narrow/broadband access. Thus, the relevant market is the *overall* advertising market, which includes print, radio and TV. Even if AT&T had 100

percent of broadband customers in the U.S., as an advertising outlet it would be a virtual drop in the ocean compared with TV and print media.

120. *Internet portals.* Those advocating "internet portal" leveraging theories provide no explanation or evidence that there is independent demand to purchase access to Internet portals. Nor can we conceive of how portals by themselves can constitute a market. Happily, there is no need for the Commission to resolve this issue because, taking Internet portals as a market, it is inconceivable that AT&T could monopolize it. As discussed above, the ability of AT&T@Home and MediaOne-Road Runner subscribers to bypass those services' home pages and access the public Internet allows customers to reach easily other portals. And, as is the case with the other "markets," AT&T has far too few customers to extract any anticompetitive concessions or harm other Internet portal sites.

121. *Navigation Devices.* Speculation that the merger would give AT&T monopsony power or vertical foreclosure over navigation devices is likewise misplaced. AT&T will have no ability to exercise monopsony power against navigation device manufacturers, because these large, sophisticated entities can simply sell to the many other users of these devices, including MSOs both in the United States and abroad. In addition, the Commission has adopted rules that forbid MSOs from restricting use of navigation devices by customers that purchase these devices themselves.[17] Thus, should AT&T

[17] *See* Report & Order, *In Re Implementation of Section 304 of the Telecommunications Act of 1996: Commercial Availability of Navigation Devices*, 13 FCC Rcd. 14775 (1998); Order on Reconsideration, *In Re Implementation of Section 304 of the Telecommunications Act of 1996: Commercial Availability of Navigation Devices*, 14 FCC Rcd. 7596 (1999).

attempt to squeeze manufacturers, they will take their product directly to the consumers. In fact, it is our understanding that a retail market for cable modems has already started to develop.

122. AT&T will also have neither the incentives nor the ability to foreclose navigation device manufacturers. As an initial matter, this effort would be doomed to failure as retail distribution develops. Foreclosure of particular manufacturers would also be pointless. While Liberty holds a small interest in General Instruments, AT&T has no economic interest in Liberty. Thus, a foreclosure strategy would cost AT&T customers – by making their cable offerings less attractive by limiting the type of equipment consumers can buy – while at the same time AT&T would get none of the benefits of such a strategy. And, as explained below for Internet services generally, AT&T cannot gain market power by imposing proprietary standards on manufacturers. Moreover, the acquisition of General Instruments by Motorola will reduce Liberty's ownership interest in General Instruments to 3 percent. Hence, AT&T's economic interest in General Instruments would be highly attenuated, wholly apart from the structural separation of the economic interests of Liberty and AT&T.

123. *Electronic program guides.* None of the parties seeking forced access for electronic program guides ("EPGs") offer any reason to believe that EPGs are a separate product market. First, there are many competing sources of the information offered in EPGs. The dominant firm in the industry, *TV Guide*, sells nearly a billion copies a year. Carl Shapiro and Hal R. Varian, *Information Rules: A Strategic Guide to the Network Economy* 25 (1999). Competing sources include other weekly publications, local advertiser-supported guides distributed for free as stand-alones or with hundreds of daily newspapers, World Wide Web sites, dedicated channels provided to subscribers by

cable operators and other multichannel video programming distributors ("MVPDs"), television sets and set-top boxes with built-in program guides. *Id.* The enhanced features bundled with some EPGs (e.g., links to related Web sites and the Internet, reviews or descriptions of listed shows, and previews) are predictable efforts at product differentiation, but the proponents of forced access have offered no evidence that these features are unavailable elsewhere, let alone sufficiently valuable to render EPGs a separate product market or give any MVPD market power over the supply of information about cable programming schedules. To the contrary, competition between on-line EPGs and printed programming guides is likely to be "heated." *Id.*

124. Second, there are multiple sources of EPGs themselves. Consumers now can obtain an EPG from an MVPD, either a cable system, DBS provider, wireless cable provider, or others. Since consumers can select among different MVPDs to provide a package of programming services, each MVPD will endeavor to provide the best EPG, or even a selection of EPGs, to consumers in order to make their bundle of services more attractive. An EPG will be one of the varied services that an MVPD supplies in order to make their service more attractive.[18]

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[18] An EPG may also be supplied as part of a particular service. For example, Interactive Channel offers a guide as part of its interactive services. Kathy Haley, "New Direction," Broadcasting & Cable, September 6, 1999, pp. 18-36.

125. Consumers also can purchase a television receiver, VCR[19], internet on TV device[20], or personal video recorder[21] with an EPG built in. In fact, consumers will soon be able to purchase at retail cable system compatible navigation devices that can contain an EPG.[22] EPGs supplied with consumer equipment do not require a consumer to have a subscription with a MVPD. Televisions and VCRs are available that provide EPGs that currently receive their information via the vertical blanking interval of broadcast television stations and will soon receive information over the air via paging frequencies. Personal video recorders currently available at retail download guide information, in addition to other information, over phone lines. Consumers can, therefore, select an EPG from a variety of sources other than their current MVPD.

126. *Internet content.* Even if competitive content providers were completely precluded from accessing AT&T subscribers via AT&T's and MediaOne's last mile data transport, they would still be able to reach these consumers through other means, both narrowband and broadband.

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[19] Gemstar licenses an EPG that is available in televisions and soon VCRs from Thompson, Sony, JVC, Philips, and Zenith. Kathy Haley, "New Direction," Broadcasting & Cable, September 6, 1999, p. 18-36.

[20] With a device attached to their television that can browse the internet (for example, WebTV or AOL TV), consumers will be able to select an EPG from virtually any supplier with a website. Kathy Haley, "New Direction," Broadcasting & Cable, September 6, 1999, pp. 18-36.

[21] TiVo and Replay are two personal video recorders that contain EPGs. Large consumer electronics firms and content providers have invested heavily in both firms in order to be prominently included in the EPGs that they offer. Glen Dickson, "Sony hops on TiVo train," Broadcasting & Cable, September 13, 1999, p. 38. Richard Tedesco, "Media giants play PVR field," Broadcasting & Cable, August 23, 1999, pp. 10-11.

[22] Besides the current suppliers of cable navigation devices, most of which contain a native guide, large consumer electronics firms are ready to supply retail devices including Philips and Sony. "New Box Players Gain Ground," Kagan Broadband, No. 17, Tuesday, August 24, 1999.

Moreover, because the @Home and Road Runner consumer base is still very small and is likely to constitute only a small portion of Internet subscribers well into the future, exclusion from such a small customer base would not significantly raise rivals' costs, thereby rendering them less capable competitors or less attractive to consumers. And in all events, "click through" access to the public Internet would defeat such a strategy.

127. Nor is there any basis to scenarios in which AT&T could dominate emerging competition by developing proprietary network and software protocols that would prevent broadband applications provided by AT&T-preferred vendors from being used by other competing technologies. *Cf.* Rubinfeld/Sidak Decl. ¶ 51; Gertner Decl. ¶¶ 17, 26-27. As an initial matter, that would require an about-face by both AT&T and @Home, which we understand is the principal architect of the protocols used by the AT&T@Home service. For a number of reasons, we find credible and consistent with economic logic the statements of the manager of the AT&T@Home service that no such about-face is contemplated. *See, e.g.*, Marshall Decl.

128. As explained below, there exist powerful restorative forces that have proven more than capable of foiling efforts by even dominant providers to impose proprietary standards and protocols on the open internet environment. But, if there were anyone to keep an eye on in this regard, it would not be AT&T, but rather today's dominant players – AOL and the incumbent LECs. AT&T has the difficult task of attracting customers away from its much bigger competitors, and of enticing applications developers and content providers to develop applications and content that will run on its service, notwithstanding that it is has relatively few customers. Thus, it is difficult to understand how

AT&T could have incentives to impose proprietary standards and protocols that would increase the cost to applications developers and content providers and decrease the content available to AT&T customers.

129. Of course, the baseline for any legitimate claim that a firm can profit by establishing proprietary standards must be the total number of customers the firm serves, not just a subset of the relevant market such as customers who obtain service from cable companies. Indeed, even if AT&T had 100 percent of the broadband customers, that would give it *no* ability either to impose proprietary standards or to tie up content providers with exclusive contracts. AT&T would still "control" only a tiny fraction of the consumers of content services. Content providers would thus have no incentive to agree to arrangements that kept them from reaching the vast majority of customers that obtain their online services by other means. Nor would AT&T have any incentive to attempt such arrangements. AT&T cannot afford to deny its customers access to content by imposing proprietary standards or otherwise refusing to carry content. Having only a fraction of the market, but having spent billions of dollars of shareholder resources to purchase TCI and MediaOne, AT&T needs to attract customers away from the industry leaders in order to make its investments pay off. And, establishing proprietary standards that limit the content available to its customers is likely the surest way to discourage customers from making the switch.

130. This claim is also particularly ironic because AOL – the leading ISP – *has* used its dominant position to place its customers in a "walled garden." We understand that AOL customers, unlike AT&T@Home MediaOne-Road Runner Internet customers, *cannot* easily bypass AOL content.

See Marshall Decl. Indeed, AOL has taken actions that make it more difficult for the customers of its applications such as instant messaging even to communicate with customers of competing services. *See, e.g.*, Christa Degnan, "Instant Messaging Salvos Hit Users," *PC Week* (Aug. 23, 1999), p. 10.

131. Finally, and most fundamentally, it is now well established in the Internet marketplace that market forces reward open standards and drive out proprietary standards. The Internet itself has a history of open, compatible standards, which are constantly reviewed and updated by standard-setting bodies such as the Internet Engineering Task Force ("IETF").[23] Compatibility has been the key to the Internet's growth. "The success of the Internet is due largely to its spectacular interoperability."[24] As Lemley observed, "it seems indisputable that the [Internet] market is driven towards standardization by a variety of forces."[25]

132. One reason why a carrier developing an Internet network is likely to select open, compatible standards is to maximize the number of innovative applications developed by content providers. Much of the value associated with an Internet network will come from the customer's ability to integrate software applications. Opponents profess to be afraid that AT&T will adopt proprietary interfaces, so that if a content provider writes an application for AT&T's Internet platform,

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[23] One need only skim through the activities of the IETF's many working groups to appreciate the breadth and depth of its standard-setting activities. *See* <www.ietf.org/proceedings/ 98dec>.

[24] Mark A. Lemley and David McGowan, *Legal Implications of Network Economic Effects*, 86 Calif. L. Rev. 479, 552 (1998).

[25] Mark A. Lemley, *Antitrust and the Internet Standardization Problem*, 28 Conn. L. Rev. 1041, 1045 (1996).

that application cannot be used on any other network. But if AT&T chose this strategy, then content providers would face higher costs (because of the need to accommodate AT&T's proprietary design) and they would be supplying a smaller market (because the software could not be used by customers on other networks). Such a strategy, therefore, would reduce the incentive that content providers have to develop innovative applications for customers who use AT&T's network. In this type of situation – when a firm must depend on the innovative activities of others – there are strong incentives toward cooperative standard-setting, as noted above.

133. Compatibility will also be demanded by customers. They want access to as much content as possible and have no desire to remain in a "walled garden."[26] It is precisely for these reasons that there are near constant announcements that technology companies, particularly those in the Internet business, are adopting open standards.

134. Opponents attempt to invoke the spectre of "Microsoft" on this issue, but all agree that Microsoft initially gained its leadership position because of IBM's support for Microsoft's MS-DOS operating system. Microsoft subsequently introduced a more ambitious operating system, Windows, with a graphic user interface. Significantly, Windows was introduced into a "standards vacuum." There was no set of industry standards or protocols to ensure compatibility among PC operating systems, nor was there any organization supported by major industry participants working to develop

[26] Of course, embracing open standards does not prohibit AT&T, or any other competitor, from innovating and attempting to shape the competitive landscape. AT&T will of course hope that its innovations will play a significant role in the evolution of open IP standards. Without question, however, AT&T has a much higher probability of success if it attempts to help guide development.

such standards. The only "standard" was Microsoft's own: it designed Windows to be backward compatible with its own product, MS-DOS. By contrast, the Internet field and, increasingly, cable-based Internet services are blanketed with standards and protocols, which have been (and continue to be) developed by well-established organizations and supported by the major companies in the industry.

135. In sum, there are strong economic forces that would lead any carrier to adopt open interfaces. Thus, AT&T must recognize that, regardless of what course it chooses, its *competitors* can readily adopt open, mutually compatible interfaces that comply with industry standards.

D. Opponents of the Merger Have Failed To Identify Any Model Of Cable "Open Access" That Is Demonstrably Superior To AT&T's Business Model.

136. Even if – contrary to fact – there were a public policy rationale for regulating access to AT&T's post-merger cable telephony network, imposing by regulatory fiat a business model for the public interest requires knowing what the optimal model is. Even a first reading of the comments on the proposed merger, however, makes clear that one cannot even begin to guess at the optimal model for cable-delivered online services. The shibboleth of "open access" feels good on the tongue, but there are multitudes of views on what the term means. There are no obvious criteria for choosing among them, let alone for preferring the regulatory models proposed by the merger opponents over AT&T's current business model for the merged entity.

137. Because rhetoric has tended to obscure fact in the "cable unbundling" arena, it is important to understand the model that AT&T currently employs. As we understand it, AT&T's

current business model: (a) seeks to use the content and advertising of its AT&T@Home service to create value and revenues to attract subscribers both with the content itself and by using the advertising and other revenue to maintain customer prices as low as possible, (b) nonetheless, places *any* Internet content or service of the user's choice no more than one click away, and, indeed, even allows users who choose to do so to bypass the AT&T@Home content altogether (or, by virtue of the "always on" feature of the service, simply to remain positioned in the content of the online service provider of the user's choice and never to return to the AT&T@Home content), and (c) is open to other commercial arrangements on agreed terms. *See* Marshall Decl.

138. We understand that the approach is not set in stone. Rather, as one would expect in an intensely competitive market, where boring or aggravating customers is punishable by commercial death, we understand that AT&T is continually evaluating what customers want and how best to respond to those preferences. *See* Marshall Decl.

139. From the present perspective, however, it is far from obvious that AT&T's initial choice of business models for cable-delivered online services will not turn out to be the one most consistent with the public interest. In this regard, we note that AT&T's business model bears a remarkable resemblance to what has long been the most common approach in other competitive media industries – and the approach favored by some of AT&T's principal opponents here.

140. AT&T's business model is common among Internet-based businesses. For example, Internet "portal" services such as Yahoo bundle content of various kinds and seek to underwrite their

informational content by building e-commerce pages on their sites, and by charging other businesses for posting advertising and links to other web sites on the portal itself.

141. Of perhaps greatest relevance, AT&T's proposed business model is similar to the model that has been used by many successful online service providers, including AOL. AOL does not offer Internet access alone. It bundles access with content; it charges hefty fees for the right to advertise or post links on its pages, and uses the revenue to hold down the subscription prices for consumers.[27] In one crucial respect, of course, AOL's model is quite different than AT&T's model: we understand that an AOL customer does *not* have the choice of easily and completely bypassing AOL's content.

142. Likewise, Altavista, the 10th largest site on the web, announced in August that it is partnering with several ISPs to provide *free* Internet access to subscribers willing to accept banner ads while on line. The service is available now across most of the United States. Andy Patrizio, "AltaVista Joins Free ISP Brigade," *Wired* (Aug. 12, 1999) <www.wired.com/news/business/story/ 21251. html>.

143. AT&T's business model also looks much like the model that newspapers, magazines, radio and broadcast TV have long employed. The predominant model for these media is to offer both

[27] An 'important component" of AOL's "business strategy is to increase non-subscription based revenues, including advertising and commerce revenues and revenues from the sale of merchandise, which the Company believes are increasingly important to its growth and success." America Online, Inc., 1998 Form 10-K, at 5 <www.aol.com/corp/inv/reports/1998/10k.html>. AOL has entered into "numerous advertising and commerce agreements" with vendors of other goods and services. Several dozen of these contracts provide for payments to AOL of $1 million or more, and some contracts contemplate total payments exceeding $100 million. *Id.* at 5-6.

editorial and advertising content. The advertising content serves two purposes: (1) it helps underwrite a relatively low subscription price for the Internet access and editorial content; and (2) it provides an independent attraction for subscribers. In radio and broadcast TV, the contribution from advertising is so substantial that operators can profitably offer "free" subscriptions, notwithstanding the significant costs of delivery. Communications media with little or no advertising content, by contrast, generally serve niche markets at very high subscription prices (*e.g.*, law reviews and other academic journals, and technical publications such as *Value Line*), or survive on charitable contributions or subsidies from taxpayers (*e.g.*, public radio and television).

144. The only specific criticism of AT&T's business model offered by the proponents of forced access is that subscribers to internet access via the AT&T/MediaOne network must "pay twice" for access to unaffiliated portals or content providers such as AOL. This criticism is unfounded. What forces customers to "pay twice" is charging for *content* – a practice engaged in by AOL and a minority of other Internet content providers. Bundling access with content *reduces* the price that consumers must pay for access to the Internet.

145. We are not asserting that AT&T's business model will (or even should) prevail in the marketplace, or even that one single model will prevail. But it is certainly presumptuous of anyone to claim to know with certainty that the AT&T model is the wrong one for consumers. The industry – one of the most dynamic in the history of capitalism – is simply moving too fast, and its direction is too uncertain. To divine the optimal business model for AT&T's proposed interactive online cable

services at this stage would require a clairvoyance that no one – regulator, entrepreneur or academic analyst – possesses.

CONCLUSION

146. For the reasons explained above, the proposed merger of AT&T and MediaOne should produce immense public benefits from large-scale facilities-based bypass of the local telephone loop. These benefits have already begun to materialize in the anticipatory competitive responses of the incumbent providers, including their accelerated rollout of DSL and other advanced services. Neither the solo efforts of AT&T, MediaOne or other cable companies, nor joint ventures among these firms, are likely to produce comparable public benefits as quickly.

147. Broad new public-utility type requirements for forced access to the cable facilities built and owned by the combined entity would be warranted only if (1) the risk of monopoly power were great enough to warrant the costs and risks of regulation, and (2) the proposed regulatory standards would actually make consumers better off. Neither prerequisite exists here. The merger will neither create monopoly power in any relevant market, nor allow the combined firm to leverage monopoly power into any other market. Furthermore, the proponents of forced access have failed to show that it would make consumers better off, either in general or in particular contrast to AT&T's present choice of business model: offering both editorial and advertising content, using content revenues to hold down subscription costs for consumers, and allowing consumers to access any other Internet site or service with a single click. The regulatory process of implementing forced access