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TELECOMMUNICATIONS LAW UPDATES

FCC Asked To Consider Effect of Proposed AT&T/TCI Merger on Advanced Services Market

When Congress passed the Telecommunications Act of 1996, it was widely believed that cable systems would soon become one of the principal competitors to incumbent local telephone carriers. Now, nearly three years later, many believe the proposed merger between AT&T and TCI may at last make competitive local telephony over cable facilities a reality. However, despite the efforts of AT&T and TCI to focus regulators' attention on the merger's potential impact in the local exchange market, much debate about the merger is centered on the merger's potential impact in the market for "advanced" or "broadband" services, such as high speed Internet access.

In acquiring control of TCI, AT&T will acquire cable facilities passing about one-third of American homes. AT&T also will acquire TCI's majority stake in @Home, an Internet service provider that offers high speed Internet access and content over improved cable systems. According to press reports, @Home was a key component of the merger deal; AT&T's goal is not just to get into cable television or local telephony, but rather to establish itself as a leading participant in the emerging and fast-growing markets for advanced services and integrated service packages. Upon completing the merger, AT&T reportedly plans to launch an aggressive program to upgrade TCI's cable facilities to enable them to carry voice and data services in addition to video. AT&T would then be in a position to offer consumers a unique package of integrated communications services, including high speed access to the Internet through @Home. AT&T reportedly is pursuing agreements with Time Warner

and other cable providers to extend the geographic reach of such services into areas that TCI does not serve.

Controversy has arisen over the position the post-merger company would hold in these emerging services markets. Potential competitors argue that the cable connection into consumers' homes is an important bottleneck facility, and that AT&T should not be allowed to leverage that transmission bottleneck to exert control in related markets. Internet service providers ("ISPs") such as America Online ("AOL") and MindSpring Enterprises complain that AT&T plans to require any customer requesting a high speed link to the Internet to purchase the content features of @Home as well as the high speed transmission capability. Customers that receive (and must pay for) these content features automatically, as part of their basic high speed access package, will be unlikely to pay an additional amount to obtain comparable content-based services from AOL — even if, other things being equal, the customer would prefer AOL's content to @Home's. To remedy this concern, AOL and other ISPs have asked the FCC to condition merger approval on AT&T's willingness to commit to an "open access" policy, under which customers accessing the Internet via AT&T/TCI's cable facilities would be permitted to select an ISP other than @Home for the content-based portion of the service.

Incumbent local telephone companies, meanwhile, argue that the post-merger AT&T would have an unfair regulatory advantage that it could quickly parlay into an artificially dominant position in

the emerging advanced services markets. Although others may or may not emerge in the future, the principal technologies for delivering advanced services to the home today are cable — in which AT&T would hold a monopoly throughout TCI's service area — and DSL, a technology by which incumbent telcos can upgrade existing phone lines for high speed data capability. The FCC has already ruled that incumbent telco DSL is subject to the same type of burdensome unbundling, resale, and other regulatory requirements that apply to the incumbents' telephone services. The incumbent telcos argue that, if DSL is hampered by such regulations and cable technology is not, then cable will quickly come to dominate the advanced services marketplace. Moreover, the incumbent telcos point out that the rationale for imposing such regulations on phone companies is no less applicable to cable providers such as AT&T/TCI. Both control bottleneck transmission facilities to the home. Accordingly, the incumbent telcos demand regulatory parity.

Of course, regulatory parity could be achieved by relaxing the regulations applicable to DSL. However, the FCC thus far has rejected all calls for such a step. Given the agency's position on DSL, incumbent telcos have asked the FCC to level the playing field in the opposite manner, by making AT&T's advanced cable services subject to the same types of regulations as DSL. AT&T has opposed such suggestions vigorously, arguing that the conditions proposed by the telcos, as well as those proposed by ISPs, would slow the deployment of advanced services to consumers and might even scuttle the AT&T/TCI merger altogether.

The FCC is considering these arguments; on December 14, it held a hearing to review these and other concerns regarding the proposed merger. FCC approval is required for the merger to proceed, and the agency has discretion to impose conditions designed to ensure that the merger will serve the public interest. The FCC's treatment of the access and regulatory parity issues will be important not just for AT&T and TCI, but also for advanced services competition generally. A decision to impose access requirements in the context of the AT&T/TCI merger likely would have reverberations throughout the cable industry; an industrywide rulemaking to consider imposing such requirements on other cable providers would be sure to follow. On the other hand, the Commission has indicated that it may not have the appetite to impose conditions on the merger outside the context of a broader rulemaking. Thus, it is possible that the agency will allow the merger to proceed while promising to initiate a separate proceeding to consider which regulatory obligations should apply to the provision of advanced services over cable systems.

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Whether the Commission decides to take up the issue in connection with the AT&T/TCI merger or in some future rulemaking proceeding, the regulatory treatment of cable providers offering advanced services will have a huge impact on the future shape of the communications industry. The race to deliver the next generation of communications services to residential consumers has begun, and access policies and regulatory handicaps may be key factors in determining the winners.

This letter is for general informational purposes only and does not represent our legal advice as to any particular set of facts, nor does this letter represent any undertaking to keep recipients advised as to all relevant legal developments. For further information on these or other telecommunications matters, please contact one of the lawyers listed below:

Scott Blackmer

202-663-6167

SBlackmer@wilmer.com

Lynn Charytan

202-663-6455

LCharytan@wilmer.com

John Harwood

202-663-6333

JHarwood@wilmer.com

William Lake

202-663-6725

WLake@wilmer.com

William Richardson

202-663-6038

WRichardson@wilmer.com