Separate Statement of Chairman Pitofsky, and Commissioners Steiger and Varney

In the Matter of

Time Warner Inc.
File No. 961-0004

The proposed merger and related transactions among Time Warner, Turner, and TCI involve three of the largest firms in cable programming and delivery -- firms that are actual or potential competitors in many aspects of their businesses. The transaction would have merged the first and third largest cable programmers (Time Warner and Turner). At the same time it would have further aligned the interests of TCI and Time Warner, the two largest cable distributors. Finally, the transaction as proposed would have greatly increased the level of vertical integration in an industry in which the threat of foreclosure is both real and substantial.[1] While the transaction posed complicated and close questions of antitrust enforcement, the conclusion of the dissenters that there was no competitive problem at all is difficult to understand.

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[1] Both Congress and the regulators have identified problems with the effects of vertical foreclosure in this industry. See generally James W. Olson and Lawrence J. Spiwak, Can Short-term Limits on Strategic Vertical Restraints Improve Long-term Cable Industry Market Performance?, 13 Cardozo Arts & Entertainment Law Journal 283 (1995). Enforcement action in this case is wholly consistent with the goals of Congress in enacting the 1992 Cable Act: providing greater access to programming and promoting competition in local cable markets.

Many of the concerns raised in the dissenting Commissioners statements are carefully addressed in the analysis to aid public comment. We write to clarify our views on certain specific issues raised in the dissents.

Product market. The dissenting Commissioners suggest that the product market alleged, "the sale of Cable Television Programming Services to MVPDs (Multichannel Video Programming Distributors)," cannot be sustained. The facts suggest otherwise. Substantial evidence, confirmed in the parties' documents and testimony, as well as documents and sworn statements from third-parties, indicated the existence of an all cable television market. Indeed, there was significant evidence of competitive interaction in terms of carriage, promotions and marketing support, subscriber fees, and channel position between different segments of cable programming, including basic and premium channel programming. Cable operators look to all types of cable programming to determine the proper mix of diverse content and format to attract a wide range of subscribers.

Although a market that includes both CNN and HBO may appear somewhat unusual on its face, the Commission was presented here with substantial evidence that MVPDs require access to certain "marquee" channels, such as HBO and CNN, to retain existing subscribers or expand their subscriber base. Moreover, we can not concur that evidence in the record supports Commissioner Azcuenaga's proposed market definition, which would segregate offerings into basic and premium cable programming markets.

Entry. Although we agree that entry is an important factor, we cannot concur with Commissioner Azcuenaga's overly generous view of entry conditions in this market. While new program channels have entered in the past few years, these channels have not become competitively significant. None of the channels that has entered since 1991 has acquired more than a 1% market share.

Moreover, the anticompetitive effects of this acquisition would have resulted from one firm's control of several marquee channels. In that aspect of the market, entry has proven slow and costly. The potential for new entry in basic services cannot guarantee against competitive harm. To state the matter simply, the launch of a new "Billiards Channel," "Ballet Channel," or the like will barely make a ripple on the shores of the marquee channels through which Time Warner can exercise market power.

Technology. Commissioner Azcuenaga also seems to suggest that the Commission has failed to recognize the impact of significant technological changes in the market, such as the emergence of new delivery systems such as direct broadcast satellite networks ("DBS").[2] We agree that these alternative technologies may someday become a significant

[2] DBS providers are included as participants in the relevant product market.

competitive force in the market. Indeed, that prospect is one of the reasons the Commission has acted to prevent Time Warner from being able to disadvantage these competitors by discriminating in access to programming.

But to suggest that these technologies one day may become more widespread does not mean they currently are, or in the near future will be, important enough to defeat anticompetitive conduct. Alternative technologies such as DBS have only a small foothold in the market, perhaps a 3% share of total subscribers. Moreover, DBS is more costly and lacks the carriage of local stations. It seems rather unlikely that the emerging DBS technology is sufficient to prevent the competitive harm that would have arisen from this transaction.

Horizontal competitive effects. Although Commissioner Starek presents a lengthy argument on why we need not worry about the horizontal effects of the acquisition, the record developed in this investigation strongly suggests anticompetitive effects would have resulted without remedial action. This merger would combine the first and third largest providers of cable programming, resulting in a merged firm controlling over 40% of the market, and several of the key marquee channels including HBO and CNN. The horizontal concerns are strengthened by the fact that Time Warner and TCI are the two largest MVPDs in the country. The Commission staff received an unprecedented level of concern from participants in all segments of the market about the potential anticompetitive effects of this merger.

One of the most frequent concerns expressed was that the merger heightens the already formidable entry barriers into programming by further aligning the incentives of both Time Warner and TCI to deprive entrants of sufficient distribution outlets to achieve the necessary economies of scale. The proposed order addresses the impact on entry barriers as follows. First, the prohibition on bundling would deter Time Warner from using the practice to compel MVPDs to accept unwanted channels which would further limit available channel capacity to non-Time Warner programmers. Second, the conduct and reporting requirements in paragraphs VII and VIII provide a mechanism for the Commission to become aware of situations where Time Warner discriminates in handling carriage requests from programming rivals.

Third, the proposed order reduces entry barriers by eliminating the programming service agreements (PSAs), which would have required TCI to carry certain Turner networks until 2015, at a price set at the lower of 85% of the industry average price or the lowest price given to any other MVPD. The PSAs would have reduced the ability and incentives of TCI to handle programming from Time Warner's rivals. Channel space on cable systems is scarce. If the PSAs effectively locked up significant channel space on TCI, the ability of rival programmers to enter would have been harmed. This effect would have been exacerbated by the unusually long duration of the agreement and the fact that TCI would have received a 15% discount over the most favorable price given to any other MVPD. Eliminating the twenty-year PSAs and restricting the duration of future contracts between TCI and Time Warner would restore TCI's opportunities and incentives to evaluate and carry non-Time Warner programming.

We believe that this remedy carefully restricts potential anticompetitive practices, arising from this acquisition, that would have heightened entry barriers.

Vertical foreclosure. The complaint alleges that post-acquisition Time Warner and TCI would have the power to: (1) foreclose unaffiliated programming from their cable systems to protect their programming assets; and (2) disadvantage competing MVPDs, by engaging in price discrimination. Commissioner Azcuenaga contends that Time Warner and TCI lack the incentives and the ability to engage in either type of foreclosure. We disagree.

First, it is important to recognize the degree of vertical integration involved. Post-merger Time Warner alone would control more than 40% of the programming assets (as measured by subscriber revenue obtained by MVPDs). Time Warner and TCI, the nation's two largest MVPDs, control access to about 44% of all cable subscribers. The case law have found that these levels of concentration can be problematic.[3]

Second, the Commission received evidence that these foreclosure threats were real and substantial. There was clearly reason to believe that this acquisition would increase the incentives to engage in this foreclosure without remedial action. For example, the launch of a new channel that could achieve marquee status would be almost impossible without distribution on either the Time Warner or TCI cable systems. Because of the economies of scale involved, the successful launch of any significant new channel usually requires distribution on MVPDs that cover 40-60% of subscribers.

Commissioner Starek suggests that we need not worry about foreclosure because there are sufficient number of unaffiliated programmers and MVPDs so that each can survive by entering into contracts. With all due respect, this view ignores the competitive realities of the marketplace. TCI and Time Warner are the two largest MVPDs in the U.S. with market shares of 27% and 17% respectively.[4] Carriage on one or both systems is critical for new programming to achieve

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[3] See Ash Grove Cement Co. v. FTC, 577 F.2d 1368 (9th Cir. 1978); Mississippi River Corp. v. FTC, 454 F.2d 1083 (8th Cir. 1972); United States Steel Corp. v. FTC, 426 F.2d 592 (6th Cir. 1970); see generally Herbert Hovenkamp, Federal Antitrust Policy § 9.4 (1994).

[4] They are substantially larger than the next largest MVPD, Continental, which has an approximately 6% market share.

competitive viability. Attempting to replicate the coverage of these systems by lacing together agreements with the large number of much smaller MVPDs is costly and time consuming.[5] The Commission was presented with evidence thatdenial of coverage on the Time Warner and TCI systems could further delay entry of potential marquee channels for several years.

TCI ownership of Time Warner. Commissioner Azcuenaga suggests that TCI's potential acquisition of a 15% interest in Time Warner, with the prospect of acquiring up to 25% without further antitrust review, does not pose any competitive problem. We disagree. Such a substantial ownership interest, especially in a highly concentrated market with substantial vertically interdependent relationships and high entry barriers, poses significant competitive concerns.[6] In particular, the interest would give TCI greater incentives to disadvantage programmer competitors of Time Warner; similarly it would increase Time Warner's incentives to disadvantage MVPDs that compete with TCI. The Commission's remedy would eliminate these

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[5] See U.S. Department of Justice Horizontal Merger Guidelines, ¶13,103 Trade Cas. (CCH) at 20,565-66, §§ 4.2, 4.21 (June 14, 1984), incorporated in U.S. Department of Justice and Federal Trade Commission Horizontal Merger Guidelines, ¶13,104 Trade Cas. (CCH) (April 7, 1992).

[6] See United States v. dupont de Nemours & Co., 353 U.S. 586 (1957); F & M Schaefer Corp. v. C. Schmidt & Sons, Inc., 597 F.2d 814, 818-19 (2d Cir. 1979); Gulf & Western Indus. v. Great Atlantic & Pacific Tea Co., 476 F.2d 687 (2d Cir. 1973).

incentives to act anticompetitively by making TCI's interest truly passive.

Efficiencies. Finally, Commissioner Azcuenaga seems to suggest that the acquisition may result in certain efficiencies in terms of "more and better programming options" and "reduced transactions costs." There was little or no evidence presented to the Commission to suggest that these efficiencies were likely to occur.