



Washington Update — Confidential & Privileged — February 28, 2006

I. Legislative Branch Activity

In early February, the President signed into law the Digital Television Transition and Public Safety Act. The Act directs the Federal Communication Commission (FCC) to take all steps necessary to require that, by February 18, 2009, all full-power television stations stop analog broadcasting, and that full-power television stations broadcasting in digital format conduct such broadcasting on channels 2 to 36 and 38 to 51. This enables spectrum now reserved for TV channels 52 to 62 and 65 to 67 to be auctioned, and channels 63, 64, 68, and 69 to be used for public-safety purposes. The Act also establishes a set-top box subsidy program so that consumers that lack a DTV-ready set and do not subscribe to a multichannel video service will still be able to receive television signals after the transition.

The Senate Commerce Committee is progressing through an aggressive schedule of hearings on rules and policies governing media and telecommunications. Below is a list of hearings and related information.

- Update on Early Hearing Issues -

The January Update covered hearings on Decency (Jan. 19) and the Broadcast and Audio Flags (Jan. 24). Commerce Committee Chairman Ted Stevens' staff recently stated that a video broadcast flag provision is likely to be added to a broader telecommunications law reform bill that the Committee expects to introduce this year. That bill also may address outstanding DTV transition issues, such as cable's downconversion of broadcasters' DTV signals, and allowing unlicensed wireless devices in the "white spaces" between broadcasters' DTV channels. While Chairman Stevens' staff has publicly praised efforts by broadcasters and others to educate consumers about parental controls, staff still expects the Committee to move forward on legislation to raise indecency fines this spring.

- Recent Hearings -

Tuesday, January 31, 2:30 PM - Video Content. Witnesses expressed concerns about vertical integration of programming content and distribution. DirecTV's Dan Fawcett discussed the difficulties faced by competing multichannel video programming distributors ("MVPDs") seeking access to incumbent cable operators' affiliated programming content. The America Channel urged Congress to address barriers faced by independent programmers seeking carriage on cable systems. Both DirecTV and The America Channel emphasized the need for conditions on the Comcast/Time Warner-Adelphia transaction. Issues concerning a la carte pricing models and retransmission consent transactions also were discussed. Few members of the Commerce Committee were able to attend this hearing, and there are no legislative proposals currently circulating on the program access, program carriage, or retransmission consent bundling issues raised in the hearing. Senator McCain has announced plans to introduce an la carte bill.

Tuesday, February 7, 10:00 AM - Net Neutrality. Some are concerned that neutrality protections are needed to ensure that consumers have unfettered access to all Internet sites. They believe that in order to preserve the open and interconnected nature of the Internet, there must be regulation to prohibit Internet access providers from restricting or slowing access to certain Internet content and applications. Others contend that there is little evidence that any Internet access providers restrict or otherwise hinder subscriber access to any Internet content or applications. These issues were discussed by witnesses at the Commerce Committee hearing. Because members of Congress in both the House and Senate have divergent views on net neutrality, it is unlikely that there will be action on this issue in the near term.

Wednesday, February 8, 2:30 PM – Protecting Consumer Phone Records. This hearing examined unauthorized third party access to phone records, potential legislative solutions, and the roles of the FCC and FTC in protecting consumer privacy. Interest in this issue has been rising due to reports that some data brokers have accessed consumer cell phone records under false pretenses and then offered the records for sale on the Internet—a practice known as “pretexting.” Legislation introduced in the House and Senate would criminalize phone record pretexting. As discussed further below, the FCC also is taking steps to prevent unauthorized disclosure of consumer records. Because pretexting has quickly become a hot button consumer issue, there is a strong likelihood that members of Congress will reach consensus around proposed legislation in this area.

Tuesday, February 14, 2:30 PM - State and Local Issues and Municipal Networks. Witnesses at this hearing presented their views on the authority of localities to establish municipal broadband wireless networks. There are a number of state-level proposals that would bar the creation of such networks. Federal legislation introduced by Senators McCain (R-AZ) and Lautenberg (D-NJ) would restrict the ability of states to enact this legislation. Other legislative proposals would require cities to compete with private companies and win the right to provide municipal broadband wireless networks.

Wednesday, February 15, 10:00 AM - Video Franchising. This hearing examined what regulatory treatment should apply to new entrants into the market for video programming distribution, and whether new entrants should be granted some relief from the local franchising process that normally applies to video programming distributors. A number of bills and less formal proposals circulating in both the House and Senate would streamline the local franchising process for telecommunications carriers offering video services. These bills also would apply some aspects of the regulatory regime for cable operators to telecommunications carriers. Senate Commerce Committee members Burns (R-MT) and Inouye (D-HI) have expressed concerns about the diminished role of local franchising authorities (“LFAs”) under the proposals being considered. The Senators have issued a policy statement announcing that any federal legislation designed to introduce competition into the video marketplace also should: (1) establish beyond doubt the prominent role of states and localities in the video franchising process; (2) facilitate competition by promoting speedy entry on mutually favorable terms; (3) promote fairness for both consumers and localities on a level playing field for providers.

We understand that, on video franchising issues, there is an increasing likelihood that Congress will move forward on a standalone bill. Given the competing interests at issue and the amount of time left on the legislative calendar, however, it is far from certain that franchising will be addressed this year.

Other hearings:

Tuesday, February 28, 10:00 AM - USF Contributions
Thursday, March 2, 10:00 AM - USF Distributions
Tuesday, March 7 10:00 AM - Rural Telecommunications
Tuesday, March 14 10:00 AM Wireless Issues/Spectrum Reform
Tuesday, March 14 2:30 PM - Wall Street’s Perspective on Telecommunications
Date TBA - Competition and Convergence
Date TBA - FCC Activities and Policy
Date TBA - Voice-over Internet Protocol (VoIP)

Subsequent updates will address these hearings and related legislative developments.

II. Federal Communications Commission (FCC) Activity

A. McDowell Nominated to FCC

On February 3, President Bush nominated Robert McDowell to the available Republican seat at the FCC. As we mentioned in the January update, McDowell currently serves as Senior Vice President and Assistant General Counsel at COMPTTEL, the principal trade association for competitive local exchange carriers ("CLECs"). Assuming that McDowell is successfully confirmed, his appointment will last until June 30, 2009.

B. Meetings and Actions

1. February FCC Meeting. At the February 10, 2006 FCC meeting, the FCC unanimously adopted its twelfth Annual Video Competition Report, a report to congress on the state of the multichannel video programming industry. The report has not yet been released.

For the first time, the report also will contain a further notice of proposed rulemaking ("FNPRM"). The FNPRM will seek comment on whether the "70/70 test" has been met. Under Section 612(g) of the Communications Act, when cable systems with 36 or more activated channels are available to 70 percent of households within the United States and when 70 percent of those households subscribe to them, the Commission may promulgate any additional rules necessary to promote diversity of information sources. The Commission seeks further public comment on methodologies and data to measure the 70-percent thresholds and, if the thresholds have been met, what action might be warranted to achieve the statutory goals.

2. Enforcement of Children's Programming and Public File Rules. The FCC has been processing a number of license renewal applications that raised issues concerning compliance with children's programming rules and public inspection file rules. When the FCC grants these applications, it has also admonished or issued notices of apparent liability ("NALs") for forfeiture for the rule violations. So far this year, the FCC has issued five NALs for violations of children's programming rules. Six other stations were admonished.

The FCC has issued seven NALs in connection with renewal applications where there were violations of the FCC's public inspection file rules. Four of these NALs, however, involved the same stations that violated the children's programming rules as described above. Some of the public file rule violations were related to failure to place material concerning compliance with children's programming rules into the station's public file; others concerned a failure to place quarterly issues/program lists into the file; still others violated both requirements.

3. Phone Record Privacy/Pretexting. On February 14, the FCC initiated a proceeding to consider whether additional security measures could prevent the unauthorized disclosure of sensitive customer information held by telecommunications companies. Section 222 of the Communications Act requires carriers to take specific steps to ensure that customer proprietary network information ("CPNI") is adequately protected from unauthorized disclosure. The FCC seeks comment on a variety of issues related to customer privacy, including what security measures carriers currently have in place, what inadequacies exist in those measures, and what kind of security measures may be warranted to better protect consumers' privacy.

4. A La Carte Redux. On February 9, the FCC's Media Bureau issued a Further Report on the Packaging and Sale of Video Programming Services to the Public (the "Further Report"). Contrary to the findings in a 2004 report on the same subject, the Further Report posits that consumers might be better off under an a la carte regime. According to the Further Report, the 2004 report relied upon a Booz Allen Hamilton study that, among other things, failed to consider the cost of broadcast stations in calculating the average cost per cable channel under a la carte. Nonetheless, even after accounting for these errors, the new report finds that a subscriber could receive no more than 20 channels (which includes six broadcast signals) without seeing an increase in his or her monthly bill.

5. Proposal to Revise Designated Entity ("DE") Rules for Auctions. The purpose of the FCC's DE rules is to promote small business entry into the telecommunications marketplace through a system of bidding credits. As

we noted in the January Update, many expected that before another major spectrum auction took place, the FCC would release new rules governing the permitted relationships between DEs and larger telecommunications companies. The FCC took the first step in this process earlier this month, when it issued an NPRM proposing to modify its DE rules to establish further safeguards to preserve the award of DE benefits. Under the rule changes being considered by the FCC, an auction applicant would be unable to qualify as a DE if it has certain financial or operating relationships with larger incumbent carriers in the same market. Specifically, if an applicant obtains a material portion of its total capitalization from a large in-market carrier, or has a material operational or financial arrangement with such a carrier, it would not qualify as a DE. The FCC also seeks comment on whether it should also restrict the award of DE benefits in cases where an otherwise qualified DE has a material relationship with a large entity that has a significant interest in the provision of communications services, such as voice or data providers, content providers, equipment manufacturers, other media interests, and/or facilities or non-facilities based communications services providers. The FCC has stated that it expects to complete this proceeding so that the rules will be in effect prior to the July 29, 2006 Advanced Wireless Services (“AWS”) auction.

C. Pending Proceedings. There are several pending proceedings that are likely to generate FCC action in the near term, including the following. New items are in red:

Proceeding	Issue(s)	Likely Timing of FCC Action
Broadcast and Wireless Auctions	<ul style="list-style-type: none"> • FM Auction #62. 96 Bidders won 163 permits; down payments were due 2/23/06. • Full Power TV Auction #64 (11 permits) • 800 MHz Air-Ground Radiotelephone Service Auction #65 • 1710-1755 and 2110-2155 MHz Advanced Wireless Services Auction • Digital LPTV Auction # 85 – LPTV stations can convert to digital operations on their analog channels or by obtaining a companion digital channel. LPTV stations seeking a companion digital channel must file applications between May 1 and May 12, 2006. 	<p>Auction closed</p> <p>Begins 3/15/06 Begins 5/10/06</p> <p>Begins 7/29/06</p> <p>Not yet scheduled; expected summer 2006</p>
Annual Video Competition Report	Routine “state of the industry” report; may also signal important policy/regulatory plans.	Adopted 2/10/06; not yet released.
A la Carte/Themed Tiering	Report and/or rulemaking proceeding concerning a la carte or themed tier offerings by MVPDs.	Report released 2/9/06
Time Warner/Comcast – Adelphia	Proposed conditions would ensure: MVPD access to merged entities’ regional sports networks (RSNs); carriage of unaffiliated programming content; and net neutrality on Comcast and Time Warner broadband platforms	1Q or 2Q 2006
Local Franchising NPRM	Rules would facilitate the franchise approval process for telcos seeking to enter the video market.	Action likely in 2Q 2006
Designated Entity (DE) Rules for FCC Auctions	Proposed new rules may restrict the permitted relationships between incumbent carriers and DEs. FNPRM released 2/3/06.	Order expected 2Q 2006

Proceeding	Issue(s)	Likely Timing of FCC Action
Cable Horizontal and Vertical Ownership Limits	May 2005 further notice seeks to update stale record. An earlier notice sought comment on how to address D.C. Circuit remand of cable ownership regulations.	3Q 2006
IP-Enabled Services	Will address the regulatory treatment of IP-enabled services, including video services.	4Q 2006
Program Access Rules	Rules governing MVPD access to certain programming owned by cable operators will sunset in October 2007. FCC to evaluate whether sunset date should be extended.	4Q 2006
2006 Quadrennial Review of Broadcast Ownership Rules	FCC must respond to Prometheus remand and reconsideration petitions and begin 2006 review.	By statute, NPRM must issue in 2006
"White Spaces" Proceeding	FCC proposes to allow unlicensed radio transmitters to operate in the broadcast television spectrum at locations where that spectrum is not being used; seeks comment.	4Q 2006
Digital Must-Carry	Outstanding issues include: material degradation, program-related material, DBS carriage of DTV signals.	3Q or 4Q 2006
Digital Television Distributed Transmission System ("DTS") Technologies	Allows broadcasters to use transmitters to fill-in service gaps caused by geographic barriers such as terrain. FCC is currently considering rules for permanent DTS operation.	3Q or 4Q 2006
DTV Second Periodic Review	Outstanding issue concerning upgrades to open v-chip.	3Q or 4Q 2006
Plug & Play	One-Way: FCC action on reconsideration pending; Court of Appeals held in abeyance. Two-Way: Ongoing negotiations and reporting to FCC throughout 2006; potential NPRM.	3Q or 4Q 2006

III. Executive Branch Activity: The National Telecommunications and Information Administration (NTIA)

NTIA is sponsoring a workshop on Improving Spectrum Management through Economic or Other Incentives on February 28 - March 1, 2006 at the National Academy of Sciences. The workshop will elicit views and proposals regarding the use of economic or other incentives to increase spectrum management efficiency.

IV. Antitrust Agency Activity/Deal Announcements

A. Pending Transactions

We previously described the Comcast/Time Warner-Adelphia transaction pending before Federal Trade Commission (“FTC”) and the Intelsat-PanAmSat transaction pending before the US Department of Justice (“DOJ”). On January 31, 2006, the FTC closed its investigation into the Adelphia transactions, finding that the transactions did not raise antitrust concerns. FCC review of the transactions remains pending.

B. Deals Announced

Disney-Pixar. In late January, the Walt Disney Company and Pixar Animation Studios announced plans for Disney to buy Pixar in a stock transaction valued at about \$7.4 billion. Disney would exchange 2.3 of its shares for each Pixar share, valuing Pixar at \$59.77 a share. Stephen P. Jobs, Pixar’s chairman and chief executive, will get a seat on Disney’s board and also will become Disney’s largest single shareholder. Jobs is currently serves as both senior executive and major shareholder at Apple. Jobs’ roles as executive and largest single shareholder of both Disney and Apple place the companies in a strategic position in the market for distribution of video content distribution over portable devices. Shareholders of Pixar have not yet approved the acquisition. The transaction also will be subject to antitrust review.

Demise of WB and UPN networks; Formation of New Networks. In late January, CBS and Time Warner announced that WB and UPN would cease operation at the end of the summer. The companies announced formation of “The CW,” a new network jointly owned by CBS (50%) and Time Warner (50%). The companies also announced a 10-year affiliation contract between The CW and Tribune Broadcasting. News Corp. announced the formation of a new network called MyNetworkTV which will debut this fall. The ten News Corp. stations that were left without affiliations because of The CW’s formation will carry the MyNetworkTV programming. Although these affiliation changes and the formation of new networks has drawn lots of attention, the events do not trigger transaction review by antitrust agencies or the FCC.

ABC Radio-Citadel. Disney announced plans to merge its radio holdings with those of Citadel Communications. After the merger, Citadel Communications will be comprised of 177 FM stations and 66 AM stations and the ABC Radio Networks.

Univision announced that it is available for sale. Potential bidders include Grupo Televisa, News Corp., and Time Warner.

IV. Litigation

CALEA. Several VoIP providers and organizations concerned with consumer privacy have appealed the FCC’s decision to extend the lawful intercept obligations of the Communications Assistance for Law Enforcement Act (CALEA) to VoIP services. Appellants contend that the Commission’s extension of CALEA obligations to VoIP providers is contrary to Congress’ intent and the FCC’s own regulatory treatment of information services, which include IP-enabled services like VoIP. Briefs for appellants and the FCC have been filed, but no date has been set for oral argument.

COPA. In August 2005, the DOJ issued subpoenas for search records from Google, America Online, Microsoft’s MSN and Yahoo in preparation for litigation to defend the constitutionality of Child Online Protection Act (COPA). Google resisted the request, while the other companies complied, reportedly without releasing individual information. In late January, the DOJ filed a motion to compel Google to comply with the subpoena. The motion has been briefed before a federal district court in San Jose, and hearing on the motion is set for March 13.

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