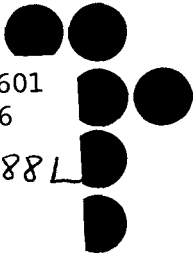


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"DIAL ENTERTAINMENT"

November 10, 1988

Seminar Notes

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"DIAL ENTERTAINMENT"

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AT&T

Sherry Bellamy, Esq.
Jones, Day, Reavis & Pogue

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Today dial information services are available by phoning 976 numbers provided by the local telephone companies or via AT&T's DIAL-IT[®] 900 numbers. The term "audiotex" is often used to describe the larger category of dial information and entertainment services, including enhanced 800- and 700-type services. The "dial-it" industry has had to contend with the nagging public relations problems resulting from "sex" line and "gab" line operations. Although the industry may have been tainted by these types of programs, Information Providers (IPs) and telcos have continued to actively market innovative entertainment and informational programming beyond these controversial offerings.

This session brought together three individuals with unique perspectives of the state of affairs of the dial-it services industry. Andrea West represented the telco perspective with an overview of AT&T's 900 service technology and marketing with comments on the regulatory environment market players like AT&T face in this industry. Next, Sherry Bellamy summarized the legal decisions related to dial-it services and raised questions about future concepts for call-blocking and user access to such services. Robert Lorsch spoke from the Information Provider's perspective giving details about how his company operates and providing background on the innovative entertainment, advertising, and fund-raising programming his company delivers via 900 service.

The first speaker, Andrea West of AT&T defined "Dial-It" services for the audience. She characterized DIAL-IT 900[®] service as an AT&T exclusive service which usually refers to "call count" arrangement for polling or information arrangement--supports a live or prerecorded "information" or "announcement" arrangement. Andrea compared its 900 service to AT&T's 800-type services. While 800 service is usually toll free to the caller, 900 service can be caller-paid or sponsor-paid. Also, AT&T's 800 service cannot support as many incoming calls as its 900 network; the latter can handle approximately 100,000 callers per minute in a polling arrangement and 7,200 for an information arrangement. The 900 network can also be used for specialty applications. For example, broadcast of the Indianapolis 500 race was broadcast to specific radio stations around the country via the 900 network. Furthermore, AT&T can set-up a 900 program such that a caller can be referred to an 800 number to talk to someone about a specific need.

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According to Ms. West, the first live event to be broadcast using 900 service was the launching of the NASA Space Shuttle in 1981. NASA wanted a mechanism to provide ongoing information to the information-hungry press. The first polling arrangement using 900 service was set-up in 1980 for the Carter-Reagan debates. With the recent presidential campaign, AT&T's 900 service became a frequently used mechanism for opinion polling. Particularly within the past year 900 tie-ins with television commercials and shows have burgeoned. The game show "Sweethearts," modeled after the TV classic "To Tell The Truth," is actually the first game show to incorporate the 900 service as a regular part of its programming. According to Andrea West, NBC and the Fox network have become the leading users of the DIAL-IT 900 service to tie-in with their programming.

Andrea showed the audience a video clip of a comical "Saturday Night Live" episode starring Eddie Murphy in which DIAL-IT 900 service was used to poll the audience on whether Larry the Lobster should be boiled or saved. In fact Ms. West noted that every time interim poll results were flashed on the air call volumes increased significantly. According to Andrea this TV episode was a classic, but a Dick Clark special asking listeners to register their favorite bands (History of Rock and Roll) accounted for the highest call volume on their 900 service thus far.

Andrea went on to explain how a company would set-up DIAL-IT 900 service program. For instance, to set-up an information arrangement, a company would contract with AT&T for the use of a 900 number paying a set-up fee of \$125 and pay 25 cents per call for calls not realized under 2000. Consumers are usually charged 50 cents per call to participate in a call count arrangement and 45 cents per call to access information services. These AT&T 900 services are accessible throughout the United States and from more than eighty foreign countries. Callers from overseas are informed that international rates apply to their 900 calls.

Ms. West showed the audience several examples of promotions, especially free standing inserts (FSIs) which incorporated AT&T's DIAL-IT 900 service from Miller Lites's Halloween promotions to Nabisco's Oreos, and numerous other consumer goods companies. She noted that these promotions are typically caller-paid, while special uses of 900 service like the Tylenol hot-line have been sponsor-paid.

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Andrea explained how AT&T operates its 900 service for both "information" and "call count" offerings as a tariffed offering. For billing services AT&T enters into contractual agreements with Information Providers. In such an arrangement, AT&T is actually an agent providing billing and collection services to an information provider; the sponsor is paying the transport charges. This tact also provides AT&T with some leverage in its attempt to keep "undesirable" programming off its 900 numbers. Andrea admits some of this might appear to be a form of "censorship." However, AT&T can determine with whom it wishes to "partner."

Ms. West explained how AT&T's network has eight nodes located around the country that support its 900 services. For example, all services are provided through an AT&T network hub in Kansas City, MO. AT&T's 900 network supports transport; by law it is not allowed to actually create or store messages on its network. AT&T does not provide related equipment. AT&T's 900 service does not currently provide ANI (Automatic Number Identification), since AT&T's billing is processed through the local telephone companies. She also noted that it is not possible to make 900 calls from a pay phone or with a credit card. Since the system does not provide routing, the calls are handled by the closest services node, e.g., a caller located in New Jersey will always have his calls routed to AT&T's node in Newark. Lastly, she does not foresee AT&T's 88 channel capacity being increased in the near future. Expansion is targeted for after 1990.

Andrea mentioned AT&T's plans to offer an interactive service in the next few months. According to West, it would be a caller-paid service offering premium billing to Information Providers; it will not apparently be a mass announcement service. AT&T hopes to see its network really being pushed to the limits (call volume) by mass announcement arrangements which may reach call volumes of millions of calls per hour. So far volume capacity is substantial. Andrea also alluded to Columbia Picture's recent talks with AT&T about possibly tying-in AT&T's 900 service with "Wheel of Fortune"; to date, legal constraints have put this concept on hold.

Andrea concluded by addressing some common issues which relate to the dial-it industry. She believes that unfortunately the taint of pornography is going to continue to plague this industry since some programmers have found this to be a very lucrative

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content market. She believes that its not just the "gab" lines and "sex" lines that give the industry a bad name; there are some sports lines which are not so wholesome either. AT&T favors the callers rights to "block" calls. Blocking has recently become an offering of the local telephone companies. AT&T is evaluating whether it can or should also implement blocking on the business (consumer) or network side.

The second speaker, Sherry Bellamy is an attorney with the firm of Jones, Day, Reavis & Pogue. She noted that dial-it services "exploded" in the U.S. in 1983/1984 and have generated a great deal of controversy. Her talk focused on the controversial adult services. Attorney Bellamy noted the Congress, the FCC and the Courts "have been engaged in efforts to resolve some of the reasons for the controversy since 1984."

She alluded to the work of Rep. Bliley of Virginia who sponsored legislation passed by the Congress in 1983 which required the adoption of FCC regulations designed to prevent access by minors to adult dial-it services ("dial-a-porn"). Bliley was prompted by calls from parents whose children had run-up bills calling these "adult" services and from companies complaining they could not control their employees calls to such services. This legislation asked the FCC to address the issue of restricting children's access, while maintaining adult access to such programming.

The legislation adopted criminal and civil sanctions, including monetary penalties, to be imposed on the providers of these "pornographic" telephone services if they failed to prevent access by children in accordance with regulations adopted by the FCC. According to Ms. Bellamy, Carlin Communications--a recognized provider of pornographic services--has challenged all such legislation and related rulemakings by the FCC. She pointed to the FCC's recent (November 8, 1988) closing of a dial-a-porn phone service owned by a California company; the owner was fined \$50,000 in what the newspapers described as the "first ever crackdown on dial-a-porn." According to Bellamy, this shows the industry that it cannot get away with operating such services without imposing controls on access by minors.

The Commission, according to Bellamy, studied various mechanisms for restricting minor's access to adult programming,

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including systems for age verification and time-of-day restrictions. The FCC did implement the time restrictions by issuing regulations restricting "dial-a-porn" offerings to the hours of 9:00 p.m. to 8:00 a.m. eastern time. She raised the obvious problems with this system, namely that this restriction assumed that children would be under their parent's supervision during these times and the ruling overlooked the fact that children on the west coast are probably still awake given the three hour time difference between east and west coasts.

Attorney Bellamy went on to summarize the three appeals that Carlin Communications made to challenge in court these FCC restrictions on "adult" services. The Second Circuit court ruled that the regulations were both "overinclusive" and "underinclusive" (Carlin I). The court felt that the "time-channeling" regulations had the effect of preventing adult access during the day and not meaningfully preventing minors' access to such services at night. Bellamy noted that the statute was called overbroad also because "indecent" speech is constitutionally protected, although "obscene" speech is not.

Bellamy went on to describe that the FCC then made a second decision which necessitated that users of "adult" services would have to use access codes or pay for the service(s) with a credit card. She noted that Carlin Communications was able to elude these restrictions since the telephone system in its primary area of operation, New York, was not technically capable of accomodating this access code arrangement. While the Court did stay the enforcement of the order in New York, the restrictions remained in effect elsewhere. Bellamy also mentioned that the FCC had initially rejected another scheme which would have involved the use of a scrambler for access to "adult" programming.

According to Attorney Bellamy, when the Court had the opportunity to review the previous two Carlin decisions, the Court upheld the FCC's actions. In doing so the Court was supporting the FCC's decision(s) to use a regulatory scheme which would involve access codes, scrambling, and credit card payment (Carlin III). In the Court's opinion, this was a feasible way of restricting access by children, while not unreasonably impeding access by adults.

Sherry emphasized that up until this point the Court had never actually addressed the "underlying constitutionity of the statute itself." She noted the constitutional question of FCC restrictions

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on certain speech had been addressed by the Supreme Court in FCC v. Pacifica Foundation. This case dealt with the FCC's reprimanding of a radio station for the broadcasting of George Carlin's "Seven Dirty Words" monologue. According to Ms. Bellamy, the Supreme Court had held that "because of the 'pervasive' nature of broadcasting, the FCC was within its authority in regulating speech which was merely indecent, although not obscene."

Bellamy noted that even though Congress argued that the Pacifica case could clearly be applied to dial-a-porn, there was still doubt expressed by others, including the FCC. She also pointed out that while the Pacifica case did not demand criminal prosecution, the dial-a-porn statute did. It is her belief that the Congress wanted to be able to impose criminal penalties on those who blatantly failed to take steps to prevent minors' access to "adult" programming.

Ms. Bellamy believes that "bottomline," the Court and the FCC cannot police "adult" dial-it services effectively. In her opinion, corporations will have to take matters into their own hands by either instituting customer premises blocking (e.g., blocking calls at the PBX in the customer's premises) or central office blocking (e.g., notifying your local telephone company to block access to certain outside numbers from your premises). She noted that offering these options only for the blocking of dial-it services have put communications companies in a predicament because the Communications Act mandates it offer services to all.

Bellamy explained that many communications companies are either imposing restrictions of their own or refusing to provide services to dial-a-porn providers. She noted that at least one Circuit Court has upheld the right of a telephone company to refuse to provide adult-oriented dial-it services altogether. The Supreme Court has declined to review this case.

According to Bellamy, some telcos are even setting-up separate prefixes for the provision of adult services. She noted that this poses certain risks for the telcos since it jeopardizes their traditional common carrier role, namely the provision of transmission with no discrimination based on content. Rep. Bliley has apparently raised this concern with telcos like Bell Atlantic. He believes that the telephone companies cannot deny responsibility for these services if they are aware of the message content and have segregated the "adult" services accordingly.

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Ms. Bellamy concluded her talk by emphasizing that "this is not an area which is easily resolved." She acknowledged that the FCC has done the best job possible under the circumstances. She believes that the Courts will be the final arbiters on all these issues. Lastly, she sees the telephone companies in a catch-22 situation since there is a tension in balancing their roles as "common carriers" versus their need to respond to public outcry to segregate "adult" services.

The third and final speaker was Robert Lorsch, founder and President of Teleline, Inc., an Information Provider in the dial-it services market. Mr. Lorsch announced to the audience that legitimate Information Providers are "the victims" of the telephone company policy and pornographer abuse. He noted that his company does not deal at all with pornographic programming or gab lines. He believes the most "controversial" program his company offers is "Dial Santa Claus."

In general, Teleline offers family-oriented entertainment and cause-related (fundraising) programming. He noted that Teleline is unique in offering gift tie-ins usually worth more than the cost of the call; those customers that call in to his company's Dial-It 900 programs can receive gifts if they send Teleline a copy of their telephone bill with their 900 number(s) calls circled as proof of purchase. Teleline has also been successful in obtaining exclusive licenses to a number of cartoon, movie and toy characters, including Woody Woodpecker, K.I.T.T. from "Knight Ridder," Mighty Mouse, Ken & Barbie, Masters of the Universe, etc.

Mr. Lorsch pointed out that in the "dial-it" services market "the telecommunications industry is being almost 'married' to the entertainment industry. He alluded to the 900 tie-in with TV ads and programming. Lorsch noted that the secret to success in using 900 and 976 numbers is proper marketing and advertising.

Some of Teleline's earliest promotions utilized 976 numbers in California and featured programs such as "Santa Claus," "Harry the Easter Bunny," and science education programs. Mr. Lorsch showed the audience a video clip of the Easter Bunny spot which later ran as a 900 service offering. All three of these programs involved fundraising tie-ins; the first two netted more than \$120,000 for the Special Olympics and the third more than \$94,000 for the California Museum Foundation.

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According to Robert Lorsch, at one time Teleline was utilizing more than 189 "976" lines in the Los Angeles area. Today, Teleline uses no 976 services. It is actually suing Pacific Bell for tainting the dial-it industry by offering pornographic programming. He noted one incident in which Teleline was accused, along with a number of other information providers, of influencing a teenage boy in California to rape a young girl, since Teleline's "Woody the Woodpecker" service number appeared on the boy's phone bill along with call to "dial-a-porn." Lorsch emphasized that once the nature of Teleline's program was explained to the plaintiff's counsel, Teleline was immediately cleared from any scrutiny.

Lorsch explained that today Teleline relies on AT&T's hub in Kansas City to support its "900" services. Technically, Teleline can run 15 programs at its California facility, which are then transmitted over dedicated or "800" lines to AT&T's Kansas City node. Teleline offerings also tie-in with 800 numbers enabling callers to be forwarded to an 800 number for additional information.

Lorsch explained the entry barriers that Information Providers encounter in choosing to go national with voice information programs, most notably the decision to buy "900" channels or build a national 976 network. Until the Fall of 1988, according to Lorsch, there were literally no permanent AT&T "900" channels available. The only service one could obtain was intermittently available temporary service. In September of 1987, he noted, that AT&T informed him that 40 new (long awaited for) channels would soon be coming on-line. Mr. Lorsch stated Teleline originally bought four of the newly released 40 "976" channels from AT&T at a cost of \$250 each. He believes that given the limited supply of numbers--there are approximately 80 numbers in total worldwide--they are worth substantially more money in the open market today. Again, he noted that the most expensive part of his business operations is advertising.

According to Lorsch, Teleline was the first information provider named as a co-marketing partner for AT&T's 900 service. He noted that Teleline has a very good working relationship with AT&T and relies on this to develop policy that impacts his company's offerings. He noted a number of times when AT&T had helped Teleline and/or one of its clients navigate regulatory policy, e.g., in the case of Spuds McKenzie ads which involved a sweepstakes program conducted over a 900 number network.

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Lorsch summarized a number of innovative services Teleline provides, including its work with Touche Ross on the development of Teltrac which provides Teleline's and its advertising customers with expanded demographic information within 24 hours of consumer calls. Teleline also develops its own mailing lists of callers by matching telephone numbers to the national yellow pages and Donnelly directories; these lists are sold as an adjunct to its dial-it business.

Mr. Lorsch emphasized the time and expense that go into negotiating contracts for content. He alluded to Teleline's recent disappointing negotiations for the rights to air the June 1988 Tyson fight. According to Lorsch, Promoter Don King awarded the rights to broadcast the fight to a third party who blocked King from honoring an earlier agreement with Teleline. However, Teleline still profited from "900" service offerings of pre- and post-fight programs which were part of a compromise reached between Teleline and King.

In concluding his talk, Mr. Lorsch gave the audience his vision of the future. He believes that dial-it services in the future will include homeshopping programs, more cause-related marketing, and sweepstakes offerings. Teleline is currently working on the development of a national voice information medical systems network which will utilize AT&T's new interactive service, 800 services, and ultimately AT&T's 700 services to allow callers to receive information on more than 3000 health topics 24 hours a day. On a humorous note, Lorsch raised the possibility of even putting microphones into race cars at the Indianapolis 500 to broadcast the drivers' during the course of the race. In closing, he noted that future information gateways will lower the entry costs for anyone looking to provide an information line.