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October 9, 1998

*NOT ADMITTED TO NEW YORK BAR.
**ADMITTED IN FRANCE ONLY.

Honorable Joel I. Klein
Assistant Attorney General
Antitrust Division
United States Department of Justice
10th Street & Constitution Avenue, N.W.
Washington, D.C. 20530

Re: Request for Business Review Letter
Regarding the Licensing of
Patents for DVD Technology

Dear Mr. Klein:

On behalf of Hitachi, Ltd. ("Hitachi"), Matsushita Electric Industrial Co., Ltd. ("MEI"), Mitsubishi Electric Corporation ("Mitsubishi"), Time Warner Inc. ("Time Warner"), Toshiba Corporation ("Toshiba") and Victor Company of Japan, Ltd. ("JVC") (collectively, "the DVD Patent Licensing Group"), we submit this request for a business review letter pursuant to 28 C.F.R. § 50.6 regarding a proposed arrangement among the six companies under which essential patents covering applications of DVD technology would be licensed in a single portfolio

license and royalties distributed among the patent holders ("the DVD Patent Licensing Program").

I. DVD Technology and Its Applications

DVD technology is a system for high density optical storage in which data encoded in digital form and stored on a disc are read and outputted by means of devices using an optical read-out beam. Widely described as the "next-generation" optical disc storage technology, the present DVD formats are capable of storing up to 4.7 gigabytes of information in each layer, about seven times the capacity of today's compact discs. DVD technology employs a five-inch diameter disc with a .6mm substrate -- half the thickness of compact discs -- which is bonded back-to-back with another substrate of the same thickness, providing the potential for double-sided storage media. Technology exists as well for storing two layers of information on each side of the disc, creating a single disc with a potential capacity of 17 gigabytes -- as much information as would be contained in a stack of telephone books over seventy-one stories high.

DVD technology provides consumers with higher quality, lower cost access to greatly increased quantities of information, home entertainment and computer applications, far surpassing today's products. DVD discs are capable of storing digitally encoded video and audio signals as well as computer data and software. The enormous storage capacity of DVD technology supports a variety of

applications of great benefit to consumers and to the computer, consumer electronics, software and entertainment industries.

DVD discs are capable of storing full-length feature films in a single layer, with cinema-quality pictures and sound. DVD discs provide additional features not currently available on VHS tapes, including up to eight different language tracks, parental lock-out features and multiple-aspect ratios. DVDs also serve as a read-only memory (ROM) medium for computer storage of vast amounts of data. DVD technology, when used in computers, provides complex applications and elaborate games on a single disc. Vast databases are being provided on DVDs. For example, a nationwide telephone directory on a single DVD disc is being offered to consumers. New applications are currently being developed for DVD audio, write-once, and random access memory (RAM). DVD technology performs many of the functions previously provided by incompatible video cassettes, laser discs, compact discs, and CD-ROMs.

From its inception, DVD technology has been developed based on the preferences of members of a wide variety of industries -- motion picture studios, computer, consumer electronics and software manufacturers, among others -- that will employ the technology. These industries have, in effect, acted as proxies for consumers, ensuring that DVD technology will best serve the public welfare. In a process extending over several years, companies involved in DVD technology have developed voluntary specifications for DVD products reflecting consumer preferences. The voluntary specifications for DVD-Video and DVD-ROM systems, including

discs, players and drives ("the DVD Specifications"), have been finalized and made available to third parties to enable them to manufacture compatible DVD products.

The DVD Patent Licensing Group has been organized to make available to licensees patents required to manufacture products in conformity with the DVD Specifications under a portfolio license ("the DVD Portfolio License"), thereby offering the efficiencies and convenience of one-stop shopping. The portfolio licenses will include present and future essential patents of the licensors. That would include all patents that are necessarily infringed when implementing the DVD Specifications for discs and players/drives/decoders and patents that claim technologies for which there is no realistic alternative in implementing the DVD Specifications. The Specifications describe the basic technical functions of DVD and additional features in DVD products desired by consumers (e.g., multiple aspect ratios and multiple language dialogues).

The portfolio license proposed by the DVD Patent Licensing Group is in conformity with the Department's Antitrust Guidelines for the Licensing of Intellectual Property ("IP Guidelines") and offers the same procompetitive features that led the Division to approve the MPEG-2 patent pool. (See Letter from Acting Assistant Attorney General Joel I. Klein to Gerrard Beeney dated June 26, 1997.) Indeed, as shown below, the DVD pool has certain features that are even more procompetitive than in the MPEG-2 case.

Like the MPEG-2 patent license, the DVD portfolio license covers only essential patents and royalties will be imposed only on such patents. The proposed

pool provides for an independent and impartial expert to determine whether patents are essential and to apportion royalties accordingly. The parties have retained Kenneth Rubenstein, Esq., the impartial expert in MPEG-2, to evaluate U.S. DVD patents. He has conducted a preliminary review of the patents and will, as explained below, do an in-depth review within the next two years as to all present and future patents; the parties have also retained an expert to review Japanese patents. All members of the pool are required to make their patents individually available outside the pool on fair, reasonable and non-discriminatory terms, whether or not a licensee elects to use the patents in connection with products conforming to the DVD Specifications. Grantbacks are limited to essential patents and parties giving grantbacks are to be paid fair and reasonable royalties. The "partial termination" rights in the proposed DVD pool are more limited than under the MPEG-2 license.

For these reasons, the DVD Portfolio License will not deter innovation, nor can it be used to disadvantage rivals or facilitate collusion. To the contrary, the DVD Portfolio License, like the MPEG-2 license, serves numerous procompetitive goals, including providing significant cost savings to licensors and licensees, which will be passed on to consumers, by substantially reducing the time and expense that would otherwise be required for licensors to disseminate the rights to each patent and for licensees to acquire them. By facilitating licensing of DVD technology, the Licensing Program will also make the benefits of this new technology broadly available to consumers more quickly and encourage the development of competition

among DVD products, thereby reducing prices and increasing the performance and functionality that consumers may expect in the marketplace.

II. The Development of the DVD Specifications

From the beginning, in the early 1990s, the development of DVD has been driven by market demand as expressed by entertainment, motion picture, software, video game and computer manufacturers and retailers in the United States and throughout the world. The original impetus for the development of DVD technology was the motion picture industry's search for a new packaged storage medium capable of providing prerecorded motion pictures with higher quality video and audio, more attractive features and lower costs than videocassette tapes. The computer industry then expressed great interest in DVD technology because of its enormous storage capacity.

A group of ten companies (Hitachi, MEI, Mitsubishi, Philips, Pioneer, Sony, Thomson, Time Warner, Toshiba and JVC) responded to this market demand. Toshiba, Time Warner and others developed a format known as the Super Density ("SD"), a double-sided bonded disc based on a .6mm substrate (half the thickness of a standard DVD) which permitted greatly increased storage capacity. Sony and Philips, on the other hand, developed their own high density optical storage format, known as MMCD, based on CD technology. MMCD, based on a thicker 1.2mm disc (the standard for CDs), had lower storage capacity than SD.

The motion picture and computer industries formed technical working groups to evaluate and test these competing formats over many months. This

ultimately led, in September 1995, to the adoption of a common voluntary format which was based on the principal elements of SD -- the .6 mm substrate and error correction system -- and the modulation technology proposed by Sony and Philips. The hardware and software industries concluded that this was the best and most robust format from a technological point of view.

Reaction to the common voluntary DVD standard was uniformly positive. For example, in a congratulatory letter to Toshiba, IBM wrote that:

The formation of a common interchange format will not only facilitate the convergence of computer, consumer electronics and home applications, but it will also open the door to new creative ideas that will become economically feasible with this new technology. We, and our customers, are excited about the possibilities for new applications now that media and application authors can focus on a common medium. With less risk of obsolescence, developers will be free to introduce new products, services and applications at an accelerated pace.

Alan Bell, Chairman of the Computer Industry Technical Working Group, stated:

This is the agreement of the decade. . . . It's tremendous news because the new standard is better than either of the individual ones and it is the most robust standard that can be offered to consumers.

Press reports were also uniformly positive.

Subsequent to the adoption of the DVD standard in September 1995, engineers for the companies involved in development of DVD technology prepared a detailed description of the unified voluntary standard, describing the specifications for compatible DVD video discs, ROM discs, players and drives (the DVD Specifications). In August 1996, these voluntary specifications were published and made available to third parties under non-disclosure agreements. The DVD

Specifications are contained in three volumes, which are together referred to as "DVD Specifications for Read-Only Disc Version 1.0 of August 1996," or "the Format Books". The first and second volume include the specifications for DVD ROM discs and players. The third volume describes DVD Video discs and players. The DVD Specifications issued in August 1996 have been further refined, based on experience and commentary from industry participants. Supplementary specifications were published in December 1996 and made available to third parties under non-disclosure agreements. The Format Books are currently available under an Interim License which may be obtained from Toshiba, acting as agent for the aforesaid ten companies with copyright and/or trade secret interests in the Format Books, and will soon be available under a definitive license.

A logo for use in marketing DVD products was developed by Time Warner Entertainment Company, L.P. ("TWE") and adopted by the nine other DVD companies. It is available under interim licenses from Toshiba, which is currently acting as agent for TWE. Definitive logo licenses will soon be available.

Neither the Format nor the logo licenses are included within the patent portfolio to be offered by the Patent Licensing Group. They are available on a non-discriminatory basis to third parties.

Throughout the foregoing process, the Antitrust Division and the European Commission have been kept apprised of the process for creating the voluntary technical standards described above.

DVD video players were introduced in the marketplace in 1997 and have already found wide acceptance. DVD-ROM players have also been marketed with success. Entertainment companies, including motion picture studios and video game manufacturers, have issued a wide variety of titles in the DVD format, starting to build the critical mass of software required to lead to widespread sales of DVD players and drives. The members of the DVD Licensing Group now propose that their present and future essential DVD patents be made available under a portfolio license in order to encourage the proliferation of this new technology on the most efficient basis by offering licensees the benefits of one-stop shopping.

III. The DVD Patent Licensing Group

When the DVD Specifications were adopted, there was agreement on the desirability of being able to provide manufacturers of DVD products a one-stop shop for acquisition of the patents necessary to manufacture products in conformity with the DVD Specifications. The Antitrust Division and the European Commission have been informed of the efforts to form a one-stop patent portfolio licensing arrangement.

The ten companies originally involved in the development of DVD, listed above, own a substantial majority of the essential DVD patents. They created a Licensing Task Force to develop a program for joint licensing of their portfolio of patents. The Task Force held numerous meetings in an attempt to reach agreement on a licensing plan in order to offer the optimal benefits of one-stop shopping. At an

early stage, however, Thomson decided for business reasons to license its patents independently.^{1/} Sony and Philips, although originally supportive of the concept of a 9-party pool, ultimately decided for business reasons to form their own pool, which was later joined by Pioneer.

On October 20, 1997, the six members of the present Patent Licensing Group announced that they would make their DVD-Video and DVD-ROM patents available under a joint patent licensing program. Under the proposed program, Toshiba would be authorized to execute the license agreements, in cooperation with MEI and Hitachi, which will assist in licensing activities on a regional basis. The six companies also propose to make their DVD patents available individually, outside the pool, on fair, reasonable and non-discriminatory terms, whether or not licensees make products conforming to the Specifications. The Patent Licensing Group will welcome other firms with essential DVD patents to join the licensing program. It continues to encourage Sony, Philips and Pioneer to join the broader 6-party pool.

IV. The DVD Patent Licensing Program Agreements

The DVD Patent Licensing Program is described in three basic proposed agreements: the Memorandum of Understanding between the DVD Licensing Group members; the DVD Patent Licensing Program Authorization

^{1/} A trial court has held that certain important Thomson patents are invalid. Thomson is appealing that judgment.

Agreement; and the DVD Patent License. These proposed agreements are summarized below.

A. The Memorandum of Understanding

The Memorandum of Understanding ("MOU") (Exhibit 1) among the six members of the DVD Patent Licensing Group defines the basic structure of the Licensing Program.

The six licensors agree to make available through the DVD Portfolio License all their present and future essential DVD patents now or hereafter owned. (Article 1). Essential patents are defined to include "those patents which are necessarily infringed when implementing the DVD Specifications for DVD-Video and DVD-ROM discs and players/drives/decoders and patents that claim technologies for which there is no realistic alternative in implementing the DVD Standard Specifications." (Article 4). The Specifications, as noted, describe the basic technical functions of DVD as well as the additional and innovative features made possible by DVD technology to meet consumer preferences. The licensors agree that the pool will make the essential DVD patents available to licensees on fair, reasonable and non-discriminatory terms for the manufacture of products conforming to the Specifications. (Article 2). The licensors also agree to license their patents separately, outside the Portfolio License, on fair, reasonable and non-discriminatory terms, whether or not a licensee makes products in conformity with the DVD Specifications. (Article 3). The licensors will list their essential DVD patents in an attachment to the DVD Patent License provided to licensees. (Article 8).

The MOU provides for a review of the patents by an impartial expert, initially two years after the execution of the agreement and at four year intervals thereafter. (Article 8). Details concerning the appointment of, the scope of the authority of and the compensation for the expert are set forth in the DVD Patent Licensing Group Agreement Concerning Patent Expert. (Exhibit 4). The expert will be a person with technical expertise who is totally independent and not an employee of, or related in any way, to any member of the Licensing Group. As noted above, the parties have retained Kenneth Rubenstein to be the impartial expert for U.S. patents and have also retained an expert for Japanese patents. Mr. Rubenstein has already made a preliminary and tentative review of the essential patents pending his final review within two years. Exhibit 5 is a list of those patents that Mr. Rubenstein has thus preliminarily determined, subject to final review, to be essential.

Any patent found not to be essential upon final review by the impartial expert, including those patents, if any, which were accepted upon preliminary review by the impartial expert, will be removed from the Portfolio License although, for their protection, licensees will have the option to include such patents in the Portfolio License for the term of the License without additional charge. Patents will also be removed from the Portfolio License when they expire.

In the MOU, the DVD Patent Licensing Group affirms its belief in the efficiencies of a one-stop-shop licensing program. Accordingly, the parties agree to use best faith efforts to persuade other essential DVD patent holders to join the Licensing Program. (Article 2).

The Licensing Group members agree to appoint Toshiba as their agent to grant patents on a non-exclusive basis, collect royalties and enforce license terms. (Article 3). MEI and Hitachi will assist Toshiba with licensing activities in certain geographic regions. Toshiba, MEI and Hitachi will perform these services for new members that join the Licensing Program if requested. (Article 6). Exhibit 6 is a proposed 3-Party Memorandum of Understanding with respect to MEI's and Hitachi's providing such assistance to Toshiba.

It is proposed that royalties will be 7.5 cents per disc and 4% of the Net Selling Price or \$4, whichever is greater, for players, drives and decoders. (Article 7). The parties agree to maintain these rates as a ceiling if additional parties or patents are added to the Portfolio License, unless doing so causes significant problems in maintaining or expanding the Licensing Program (e.g., by limiting returns so much as to discourage patent holders from contributing their patents to the portfolio).

Royalties will be allocated among the parties based on the selections and evaluations of the impartial expert. (Article 8). By guaranteeing a fair and equitable procedure for sharing royalties, this arrangement will encourage other potential licensors to join the Licensing Program and make their patents available through the Portfolio License, with resulting benefits for licensees and consumers. Royalty allocations will also take into account the expiration of old patents, issuance of new patents, and addition or deletion of members from the DVD Patent Licensing Group. (See Ground Rules for Royalty Allocation (Exhibit 7)).

The parties will erect firewalls and take other necessary steps to protect competitively sensitive information received from licensees, including without limitation the sales volume and selling prices of individual product models by licensees. Accordingly, royalty reports containing sales data as to individual product models or selling prices shall be sent only to employees of Toshiba involved in licensing and accounting activities but not involved in the business of developing or selling DVD product; these employees shall keep such information confidential and not disclose such information to the parties to the joint licensing program or to any other party. (Article 15). The procedures for maintaining the confidentiality of licensee information are more fully set forth in the Procedures for Protecting the Confidentiality of Information Provided by DVD Patent Licensing Program Licensees (Exhibit 8) and DVD Patent Licensing Program: Authorized Employee Confidentiality Agreement (Exhibit 9).

B. The DVD Patent License and DVD Patent License Conditions

The DVD Patent License and Patent License Conditions ("the Portfolio License") (Exhibit 2) implement the DVD Patent Licensing Program in conformity with the MOU. The Portfolio License is entered into between a Licensee and Toshiba, acting as Licensor under the authorization of the members of the DVD Patent Licensing Group. The Portfolio License grants to the Licensee the non-exclusive right to make, have made, use, sell or dispose of products conforming to the DVD Specifications under all essential patents owned by members of the

Licensing Group or that come to be owned by them during the term of the License. (Article 2.1). The Portfolio License expressly excludes patents related to CSS and MPEG-2 data compression. A list of currently-issued essential patents based on the preliminary and tentative review by Kenneth Rubenstein will be attached to the License. (Condition 1.3).

The Portfolio License releases Licensees from claims of infringement based on their manufacture, use or sale of DVD products prior to entry into the License. The Licensee is informed that it has the option to negotiate for patents separately with any member of the Licensing Group, and that each company is required to grant such licenses on fair, reasonable and non-discriminatory terms, whether or not the Licensee intends to make products that conform to the DVD Specifications. (Articles 2.1-2.3).

The royalties proposed under the Portfolio License are as set forth above. Licensees are obliged to submit quarterly statements describing the quantities of DVD products manufactured and royalties payable and to submit their books for review by an independent auditor once annually. (Conditions 2.3, 2.4, 2.6 & 2.8). Royalties are also payable on DVD products manufactured prior to entry into the license in consideration for the release from liability for infringement of the DVD patents in this period. (Condition 2.1)

The Licensee agrees to grant to each member of the DVD Licensing Group and all other licensees a non-exclusive license under any essential patents owned by the Licensee for the manufacture of products conforming to the DVD

Specifications. Such licenses will be granted upon fair, reasonable and non-discriminatory terms. (Article 3.1)

A Licensor has the right to terminate the license granted under any patent if (i) a Licensee brings a claim in a lawsuit or proceeding that the Licensor has infringed essential DVD patents owned by the Licensee by the manufacture, use or sale of a product conforming to the DVD Specifications, and (ii) the Licensee refuses to grant a license to the claimed infringer under the patents on fair and reasonable terms and conditions. Disputes about the fairness or reasonableness of terms and conditions will be determined by an expert jointly appointed by the parties to the dispute. (Article 3.2).

The term of the Portfolio License runs through December 31, 2007, and is automatically renewed for five year terms at the Licensee's option, except that the License immediately terminates when the last of the licensed patents expires. (Articles 5.1-5.2).

The Licensee is entitled to receive notice if the Licensor grants a Portfolio License to any party with more favorable royalty terms, and, at the Licensee's option and subject to certain exceptions, its License may be amended to reflect those terms, provided that the Licensee agrees to be bound by any other terms and conditions in the third party's license. (Article 6.1).

C. The DVD Patent Licensing Program Authorization Agreement

The DVD Patent Licensing Program Authorization Agreement ("the Authorization Agreement") (Exhibit 3), between Toshiba and each of the other

members of the DVD Licensing Group ("a Company"), appoints Toshiba as non-exclusive agent and grants it the right to license the Company's present and future essential DVD patents pursuant to the Portfolio License. (Article 2.1).

Toshiba is authorized to collect and distribute royalties on behalf of the Company. Allocation of the royalties is to be determined based on the selection and evaluation of patents by the impartial third-party expert or panel of experts. (Articles 4.1-4.2). The initial expert evaluation will occur two years after entry into the agreement, and reevaluations will occur every four years thereafter. Royalty allocations will take into account entry of new parties into the licensing program, issuance of new patents, and deletion of patents and members from the Licensing Group. Royalties will be distributed on an equal basis for the first two-year period, with any necessary adjustments made after the expert's first evaluation. (Articles 4.3-4.4).

A Licensor has the right to instruct Toshiba to terminate or deny a license of its DVD patents to any licensee that has brought an action for infringement of an essential DVD patent against the Licensor and has refused to license such patent to the Licensor on fair and reasonable terms. (Articles 2.4-2.5).

Toshiba is authorized to collect royalties and enforce the terms of licenses. (Article 3.1). Royalties are payable in the amounts described above. It is the intention that royalties will not be increased even if patents are added to the Licensing Program, unless failure to do so would cause a significant problem in maintaining or expanding the licensing program. (Article. 5.1).

The parties agree to cooperate to prevent unauthorized uses of the rights licensed by Toshiba, but each party agrees that it is solely responsible for prosecuting unauthorized use or infringement of its DVD patents. (Articles 3.2-3.3).

Toshiba agrees to remit periodic royalty statements and to submit to auditing by an independent auditor at least once a year. (Articles 4.6, 4.9).

Toshiba's fee for administering the Licensing Program is three percent of licensing income up to \$100,000,000 per annum and two percent of any annual licensing income exceeding \$100,000,000. (Article 4.8). MEI and Hitachi will share in these fees to the extent of their respective licensing activities in particular regions of the world. (Article 4.8).

V. Competitive Consequences of the Licensing Program

The Department's IP Guidelines recognize that patent pools, especially in high-technology industries, provide procompetitive benefits. Such joint licensing arrangements "may provide competitive benefits by integrating complementary technologies, reducing transaction costs, clearing blocking positions, and avoiding costly infringement litigation." Id. § 5.5. The proposed DVD Licensing Program meets the goals of the IP Guidelines. The DVD pool, like the MPEG-2 patent pool, offers substantial procompetitive benefits, efficiencies and conveniences inherent in a one-stop-shop for licensees.

We shall now briefly review the DVD Licensing Program under the analytic framework employed by the Division in its business review of the MPEG-2

pool and demonstrate that the proposed DVD pool will provide substantial competitive benefits without curtailing competition.

A. Effect on Rivals

The DVD Licensing Program does not threaten to disadvantage competitors. As in the case of MPEG-2, the MOU here obligates members of the pool to make all of their present and future essential DVD patents available on fair, reasonable and non-discriminatory terms to third parties, whether or not they comply with the DVD specifications. The DVD Portfolio License, as in the case of MPEG-2, includes a most-favored nations clause entitling any licensee to the benefit of favorable royalty terms offered to any other licensee. As in MPEG-2, an independent expert will ensure that only essential patents are included in the pool, thereby excluding the possibility that licensees would be forced to take and pay for unwanted patents. Moreover, licensees who do not wish to take the entire portfolio of patents are free to license individual patents from individual companies outside of the pool. The pool, in short, does not have exclusive rights.

This safeguard parallels the non-exclusive feature which is common in arrangements between collecting societies like ASCAP and their members. Such societies offer users blanket licenses covering all the performance rights of their members but the individual members retain the right to license their intellectual property separately to users of music. The courts have upheld the legality of such pools because the individual members are free to license users independently on a non-exclusive basis. See, e.g., CBS v. ASCAP, 620 F.2d 930, 935 (2d Cir. 1980).

("If that opportunity [to license independently] is fully available, and if [licensors] retain unimpaired independence to set competitive prices for individual licenses to a licensee willing to deal with them, the blanket license is not a restraint of trade.")

The royalty rates proposed by the DVD pool are reasonable, especially when compared to the rates proposed by the MPEG-2 pool for patents used in DVD products or when compared to the rates proposed by the Sony/Philips/Pioneer 3-party DVD pool. The proposed pool, moreover, provides cost-savings and efficiencies inherent in one-stop-shopping. There are additional safeguards for licensees. As noted, licensees have the option to obtain individual licenses outside the pool from each individual member. The parties also agree to maintain the rates charged by the pool as a ceiling if additional parties or patents are added to the Portfolio License unless doing so causes significant problems in maintaining the pool. The MPEG-2 pool, in contrast, reserves the right to increase royalty rates by 25% after two years.

B. Facilitation of Collusion

The Licensing Program will not encourage collusion. The possibility of collusion is curtailed by the erection of firewalls to protect competitively-sensitive information and prevent its disclosure to pool members or any other parties. Additionally, as in MPEG-2, royalties will be a sufficiently small element of the final cost of DVD products so as to preclude them from serving as a device to coordinate downstream product prices.

C. Effect on Innovation

Under the Portfolio License, licensees will use the patents to manufacture products in conformity with the DVD Specifications. A common standard promotes compatibility between different products. It provides comfort to consumers that they will not invest in equipment or software that is quickly superannuated and abandoned, as happened with Beta videocassette players. It promotes competition in price and features within the standard by allowing consumers to choose from a range of compatible products. And it meets the needs of the motion picture, computer and other affected industries, which required a common and compatible standard before investing in a revolutionary new technology.

At the same time, the Licensing Program promotes the policies underlying the IP Guidelines by assuring the freedom to innovate outside the DVD Specifications. Each member of the pool must make its DVD patents available on an individual basis on fair, reasonable and non-discriminatory terms to a licensee who wishes to use them in the development of products that do not conform to the Specifications.

The Portfolio License does not create the risk of exploiting locked-in licensees. Upon its expiration in ten years, the Portfolio License renews automatically for an additional five years, unless terminated by the Licensee.

The MOU and Authorization Agreement, as noted, also provide that royalties will not be increased, even if new members are added to the Licensing Group or new patents are added to the Portfolio License, unless failure to do so

would cause a significant problem in maintaining or expanding the Licensing Program. The MPEG-2 license, in contrast, is of short duration (two years) and, as noted, appears to contemplate a 25% increase in royalties.

The grantback provisions in the Portfolio License are limited to essential patents. Any grantback, moreover, must be on a non-exclusive basis and must be on fair, reasonable, and non-discriminatory terms. As with the MPEG-2 license, this grantback provision will limit a holdout's ability to exact supracompetitive tolls from licensees. The grantback provision will not discourage innovations or the development of new and different products.

As noted above, the impartial expert in the DVD joint licensing program will make decisions affecting the allocation of royalties among the members of the pool. This feature has procompetitive benefits for the reasons set forth (*i.e.*, it will encourage new entrants to join the one-stop shop).

VI. Conclusion

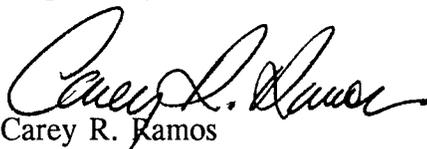
The proposed DVD Portfolio License will, like the MPEG-2 joint licensing program, result in procompetitive efficiencies without limiting competition in any way. The Portfolio License will provide licensees the benefits and efficiencies of one-stop shopping, creating efficiencies and cost-savings that we believe will be passed on to consumers. It will also decrease licensors' transaction costs, again resulting in consumer savings. It will provide fair and reasonable royalties for licensees who elect to license from the pool. It will give licensees the freedom to

obtain individual licenses from individual patent owners on fair, reasonable and non-discriminatory terms outside of the pool for products whether or not conforming to the DVD Specifications. An impartial outside expert will evaluate the patents periodically.

DVD technology has already begun to win widespread consumer acceptance in the United States and around the world. The proposed DVD pool, we believe, will further accelerate that trend by increasing incentives for adoption of this next-generation technology. The Division's positive action on this business review will, we believe, significantly contribute to consumer welfare.

We are available at your convenience to provide any further information you may require.

Respectfully submitted,



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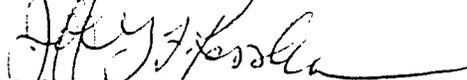
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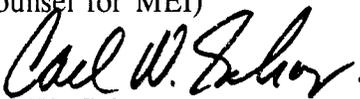
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