Statement of

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INTRODUCTION

Mr. Chairman, Task Force members, thank you very much for having me here today. My name is David K. Rehr, and I serve as the President and Chief Executive Officer of the National Association of Broadcasters.[1]

At the NAB, we are proud to represent more than 8,300 diverse radio and television stations across the United States, as well as broadcast networks. Our members are the backbone of our nation's communities, serving their listening and viewing audiences through public service initiatives, local news and public affairs programming, and vital community information – such as emergency warnings, severe weather alerts, and AMBER alerts.

The National Association of Broadcasters advocates on behalf of all these stations – large and small, urban and rural – before Congress, the Federal Communications Commission and the general public. These stations employ nearly 250,000 hard working Americans, and reach nearly every household. Local radio and television broadcasters provide a free, over-the-air service, keeping their communities – and your constituents – informed and connected.

[1] David K. Rehr holds an M.A. and Ph.D. in economics from George Mason University, as well as a B.S. in Business Administration from Saint John's University. He has nearly 25 years experience in regulatory and anti-trust issues. Previous experience includes serving as a professional staff member of the House Small Business Subcommittee on Antitrust and Restraint of Trade, director of federal government relations for the National Federation of Independent Business, and President of the National Beer Wholesalers Association.

The issue we are here to talk about today is of tremendous importance. It affects not only the future of satellite radio in America, but portends great potential harm to the American public and to the many benefits of free local radio broadcasting.

XM AND SIRIUS ARE ASKING FOR A GOVERNMENT SANCTIONED MONOPOLY

As I explain below, the proposed merger of XM Radio Inc. and Sirius Satellite Radio Inc. must be rejected. Public policy should never allow one entity to acquire state-sanctioned, monopoly control over the 25 MHz of spectrum allocated to satellite radio service. Such a merged entity would control several hundred channels of radio programming in every local market in this country without any realistic check on its ability to assert market power.

One can easily see what XM and Sirius are really asking for here. They want the ability to set subscription prices for national satellite radio service without constraint from a competing service. They want to eliminate the need to compete with another national service provider to acquire programming and talent that wish to reach the national audio market. They want the ability to demand exclusive access to attractive programming, such as sporting events. And, they want to reduce the need to spend money on innovative service and equipment for consumers.

The downsides of a government sanctioned monopoly are clear. Monopolists have the ability to raise prices and discriminate. As we saw in the telephone world for many years, monopoly providers do not respond quickly to consumer needs and wants.

As a result, innovation suffers. While the monopolist may engage in some innovation, the incentive is to protect current investment and slow introduction of new products and services for the public, especially any new products that might compete with the existing products and services being offered by the monopolist. As my testimony demonstrates in detail, there is no possible reason to grant this proposed merger to monopoly in the market for national, multichannel mobile audio programming services.

THE PROPOSED MERGER VIOLATES FCC RULES AND PRECEDENT AND CONGRESSIONAL POLICY

The FCC specifically refused to sanction a monopoly when it allocated spectrum for the satellite digital audio radio service (DARS) in 1997. It chose not to permit a monopoly satellite radio service because "licensing at least two service providers will help ensure that subscription rates are competitive as well as provide for a diversity of programming voices."[2] And, I note, the agency was assuming at that time that each provider would control around 50 channels, not the 282 channels that a united XM/Sirius would have today.

Ironically, the FCC in part based its decision to require multiple satellite radio providers on arguments presented by Sirius. During the FCC's consideration of how many different satellite radio providers it should authorize, Sirius (then called CD Radio) argued strenuously that multiple providers were necessary to "assure intra-service competition," and that the FCC should divide the relevant spectrum evenly among all

[2] *See Establishing Rules and Policies for the Digital Audio Radio Satellite Service*, 12 FCC Rcd 5754, 5786 (1997) (*Satellite DARS Report & Order*).

licensed satellite radio providers.[3] Sirius also maintained that creating multiple satellite radio systems would guarantee a diversity of programming offerings because each satellite radio provider would have "compelling market-based incentives" to differentiate itself from the other providers. CD Radio Comments, at 17.

For these reasons, Sirius explicitly stated that no satellite radio provider should ever be permitted to combine with another provider. Sirius believed that "such a development would have serious anticompetitive repercussions," including reducing the diversity of programming sources and a lessening of price competition. *Id*. at 18.

Even more ironically, Sirius was making these arguments in the context of the FCC licensing scheme proposed at the time, which contemplated four different satellite radio providers. Sirius was thus strenuously opposed to any FCC policy that might allow the shrinking of the satellite radio market from four different competitive providers to three or two. Now, only a few years later, Sirius apparently sees no problem with allowing the satellite radio market to shrink from two competing duopoly companies down to only one, who will have monopoly control over the entire national market.

The point is that it would be entirely inconsistent with the pro-competitive satellite radio licensing scheme created by the Commission to now allow XM and Sirius to combine into a monopoly enterprise. At the urging of the parties, including Sirius, the Commission in 1997 explicitly prohibited any such future merger by determining that, "after DARS licenses are granted, one licensee will not be permitted to acquire control of

[3] CD Radio Comments in IB Docket No. 95-91, at 17.

the other remaining satellite DARS license." *Satellite DARS Report & Order*, 12 FCC Rcd at 5823. There is no basis for reversing that decision now.

In a parallel circumstance, the Commission refused in 2002 to permit a merger of the only two nationwide Direct Broadcast Satellite (DBS) licensees, EchoStar and DirecTV. In rejecting this proposed merger, the Commission found in a unanimous vote that the combination would undermine its goals of increased and fair competition in the provision of satellite television service. The agency also found that the claimed benefits of efficient spectrum use were outweighed by substantial potential public interest harms that might result from the transaction, including reduced innovation, impaired service quality and higher subscription prices. The Commission further stressed that the merger would eliminate a current viable competitor from every market in the country and would result in one entity holding the entire available spectrum allocated to the DBS service.[4] For precisely the same reasons, XM and Sirius should not be permitted to create a nationwide satellite radio monopoly.

Like the rejected EchoStar/DirecTV merger, the proposed satellite radio merger would eliminate a viable competitor providing service across the country and would result in a single company controlling all the spectrum allocated to a nationwide satellite service. As the FCC noted when declining to approve the EchoStar/DirecTV merger, the antitrust laws are "hostile to proposed mergers that would have these impacts on the competitive structure, because such mergers are likely to increase the incentive and

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[4] *See EchoStar Communications Corp.*, 17 FCC Rcd 20559, 20562, 20661-62 (2002) (*EchoStar/DirecTV Merger Order*).

ability to engage in anticompetitive conduct." *EchoStar/DirecTV Merger Order*, 17 FCC Rcd at 20662. Allowing XM and Sirius to hold the entire available spectrum allocated to satellite DARS would similarly increase the incentive and ability of these parties to engage in anticompetitive conduct, to the ultimate detriment of consumers. *Id*. at 20626 (noting reductions in future innovation, declines in service quality and pricing problems as likely to result from satellite television merger).

To allow the proposed merger creating a satellite DARS monopoly would thus be inconsistent with the FCC's order establishing this service, with Commission precedent in the satellite television context, and with its long-standing policy of establishing spectrum-based commercial services with no fewer than two participants per service. Congress should encourage the FCC to retain its faith in competitive markets and refuse to sanction a satellite radio monopoly.

Such a government-sanctioned monopoly would clearly also be inconsistent with congressional policy favoring competition over monopoly, as expressed in the 1996 Telecommunications Act, and with long-standing enforcement of the antitrust laws. Indeed, the courts have held that even mergers to *duopoly* are, on their face, anticompetitive and contrary to the federal antitrust laws.[5] Without question, a merger to *monopoly* would be anticompetitive, inconsistent with antitrust precepts and contrary to judicial decisions.

[5] *See, e.g., FTC v. H.J. Heinz Co*., 246 F.3d 708 (D.C. Cir. 2001).

THERE ARE DISTINCT LOCAL AND NATIONAL MARKETS

XM and Sirius will no doubt argue that they are not proposing a monopoly because, they say, satellite radio competes against AM and FM radio broadcasting, the Internet, and other emerging technologies. And they will ask: how can NAB contend that a single satellite radio provider will be a monopoly while at the same time claiming in the FCC's broadcast ownership proceeding that satellite radio competes with local radio stations? The answer is simple – there are two different markets at issue, a national market and a local market.

NAB's comments in the FCC's ownership proceeding explain that broadcasters face competition today in their local markets from a number of sources including XM and Sirius. Plainly satellite radio affects local markets because consumers in all local markets across the country can receive and choose to subscribe to the satellite radio services. The fact that millions of subscribers in various local markets across the country have chosen to subscribe and listen to satellite radio services, rather than just listening to local stations, clearly affects the numbers of listeners that terrestrial broadcast stations attract (and thus ultimately the advertising revenues earned by these stations).

On the other hand, local stations do not compete in the national market for multichannel mobile audio services. As the FCC has recognized, satellite radio, with its national reach, offers "services that local radio inherently cannot provide." *Satellite DARS Report & Order*, 12 FCC Rcd at 5760-61. For example, satellite radio can provide continuous service to the long-distance motoring public and to persons living in

remote areas. *Id*. Unlike even the most powerful terrestrial radio stations, which can still only reach a mere fraction of American consumers, satellite radio service can reach all listeners across the country with vastly more channels than any single terrestrial broadcaster. Other media industry observers have agreed that "[s]atellite radio is a national platform," thereby clearly differing from locally-licensed and locally-oriented terrestrial broadcast stations.[6] Simply put, only XM and Sirius compete in this national, multichannel mobile radio market, and they are proposing to form a state-sanctioned monopoly in that market.

XM AND SIRUIS WILL BE ABLE TO EXERCISE UNLIMITED MARKET POWER IN THE NATIONAL RADIO MARKET

My training as an economist tells me that XM and Sirius are acting like classic market players. Adam Smith noted in *The Wealth of Nations* over 230 years ago that all companies work toward monopoly. From a company perspective, monopoly is desirable: it allows the company to achieve market power and gives them the ability to set prices unilaterally and act as a gatekeeper without any reasonable competitive check.

More specifically here, having monopoly status would enable the united XM and Sirius to stop agreeing to pay outrageous talent salaries and to exert greater pressure on programming suppliers. Eliminating competition in the national mobile radio market through this proposed merger would also greatly reduce incentives for the combined XM and Sirius to innovate. A monopolistic market structure is inevitably less innovative than

[6] Katy Bachman, *Buyers: Size Not Enough for Sirius/XM Merger*, Media Week (Feb. 26, 2007) (quoting Matt Feinberg, Senior Vice President of Zenith Media).

a competitive one, and the consumers of satellite radio services will accordingly fail to benefit from innovations such as improved programming services and technical improvements. In fact, when declining to approve the EchoStar/DirecTV merger, the FCC specifically found that the satellite television merger "would likely reduce innovation and service quality." *EchoStar/DirecTV Merger Order*, 17 FCC Rcd at 20626.

Perhaps most obviously, enjoying monopoly status would permit a merged XM/Sirius to raise subscription prices without any competitive check on its actions. The complete elimination of competition in the marketplace for nationwide, multichannel mobile radio services would remove competitive pressure on rates and almost inevitably result in rate increases for consumers. For example, the FCC recently determined that cable television rates have increased by 93% since enactment of the 1996 Telecommunications Act.[7] The agency has attributed this tremendous increase to the lack of competition from a second cable operator in most communities. Interestingly, the FCC also concluded that competition from DBS has had minimal effect on cable prices, finding that only the presence of a similarly-situated, directly competing cable operator worked to constrain cable prices.

The analogy to the XM/Sirius merger is unmistakable. Without the presence of a direct competitor, a satellite radio monopolist could raise rates freely. Indeed, the courts have enjoined mergers to monopoly on the grounds that such mergers would allow the

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[7] *See Report on Cable Industry Prices*, MM Docket No. 92-266 (rel. Dec. 27, 2006).

combined company "to increase prices or otherwise maintain prices at an anticompetitive level."[8] To again look to the wisdom of Adam Smith, the "price of monopoly is upon every occasion the highest which can be got."

Beyond resulting in rate increases for consumers, the XM/Sirius monopoly would also likely reduce program diversity. As explained by the Commission when authorizing XM and Sirius, competing satellite radio providers would each have incentives to diversify their own program formats, thus providing valuable niche programming. *See Satellite DARS Report & Order*, 12 FCC Rcd at 5762. Without such competition, program diversity would likely be adversely affected, with consumers losing music and talk formats, especially niche ones. Of course, there is also the very real risk that a combined XM/Sirius will use its market power to force content providers like sports programmers to deal only with them. If the merger is approved, it may only be a matter of time before the American public can listen to their favorite baseball or college football team by paying whatever monopoly rents a combined XM/Sirius chooses to charge. We've seen it happen with cable, and given the obvious incentives, there is every reason to expect the same thing to happen here. In sum, in a monopoly environment, satellite radio subscribers would pay higher prices for less diverse and less innovative programming.

[8] *FTC v. Staples*, 970 F. Supp. 1066, 1081-82 (D.D.C. 1997).

XM/SIRIUS HAVE A LONG TRACK RECORD OF BREAKING THE RULES

The government cannot and should not rely on any promises that a united XM and Sirius, as a government sanctioned monopoly, will not cause harm to consumers. Their past behavior in a number of instances shows otherwise.

First, both companies have violated an FCC rule on receiver interoperability. Despite a clear FCC directive that their satellite radio systems must include "a receiver that will permit end users to access all licensed satellite DARS systems that are operational or under construction,"[9] neither XM nor Sirius markets such a consumer-friendly device. And, while both companies certified nearly 10 years ago that they would comply with this pro-competition, pro-consumer requirement, they have not done so. Instead, the companies contend that they are technically complying by "jointly developing" a common receiver platform while making no apparent effort to make the device a reality. In carefully worded SEC filings, the companies report that technology for a unified receiver standard "is being developed" but "we have no assurances that any manufacturer will build . . . such dual-mode radios."[10] Thus, the companies have undermined the efficacy of this FCC rule designed to "promote competition by reducing transaction costs and enhancing consumers' ability to switch between competing DARS providers." *Satellite DARS Report & Order*, 12 FCC Rcd at 5796.

[9] 47 C.F.R. § 25.144(a)(3)(ii).

[10] *See* Sirius Satellite Radio Inc. SEC Form 10-K at 9 (March 13, 2006); XM Satellite Radio Holdings Inc. SEC Form 10-K at 11 (March 3, 2006).

Second, with similar disregard for consumer interests, both XM and Sirius have violated FCC Part 15 rules, which govern the production and distribution of their receiver equipment.[11] These rules are designed to ensure, among other things, that equipment such as satellite radio receivers do not interfere with broadcast radio stations or other licensed spectrum users. As a result of XM and Sirius producing and distributing receiver equipment that violates – and in a number of cases very greatly exceeds – FCC limits on the power levels for such equipment, many listeners to terrestrial radio stations experience "bleedthrough" and receive the XM or Sirius signal without warning through their radios. As has been widely reported, the FCC has received many complaints from both commercial and non-commercial listeners who suddenly hear uncensored and unwelcome satellite radio programming on their car radios.[12] That's why NAB has been calling on XM and Sirius for months to do the right thing, and recall the hundreds of thousands of satellite radio receivers in the market that continue to interfere with free over-the-air radio broadcasts.

Third, both XM and Sirius routinely and regularly violate FCC technical rules. In particular, these companies have admittedly violated FCC rules in connection with their special temporary authority to use terrestrial repeaters. For years XM operated more than 142 repeaters (or 18 percent of all its repeaters) at unauthorized locations and at least 19 of its repeaters without any FCC authorization at all. Even after confessing and seeking the FCC's forgiveness for its violations, XM to our knowledge currently continues to

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[11] 47 C.F.R. Part 15.

[12] *See, e.g.,* "A Mystery Heard on Radio: It's Stern's Show, No Charge," New York Times, January 26, 2007 at A17.

operate at least four of its repeaters without any authorization from the FCC. Also troubling is XM's confession that for years it has operated more than 221 terrestrial repeaters (or 28 percent of all its repeaters) at unlawful power levels.

For its part, Sirius has engaged in comparable and other technical violations in connection with its terrestrial repeaters. For example, Sirius constructed at least 11 of its repeaters at locations different from what they reported to the FCC, including one in Michigan that is 67 miles away from its reported and authorized location.

Within the past few weeks, the FCC issued a letter to XM about its unlawful repeater network. The agency is presumably seeking information about the actual locations and power levels of XM's repeaters; the circumstances surrounding why XM apparently failed to follow the FCC's rules when installing the network; and why it took XM almost five years to reveal all the problems.

These violations arguably demonstrate a pattern of misconduct and lack of candor that raise serious questions regarding whether the companies can be relied on in the future to comply with FCC rules or with any conditions imposed or offered as part of the merger. This is particularly the case to the extent that the violations may have been intentional. In this regard, Sirius has admitted that its unlawful receivers were the result of specific requests by its employees to manufacturers.[13]

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[13] Sirius Satellite Radio Inc. SEC Form 10-Q at 35 (Nov. 8, 2006) ("certain SIRIUS personnel requested manufacturers to produce SIRIUS radios that were not consistent with these rules.").

Against this backdrop of rule violations, allowing XM and Sirius to create a monopoly in violation of the FCC's anti-merger decision and decades of communications policy could simply embolden them to pay even less attention to the rules of the road in pursuit of monopolistic profits.

THESE ARE NOT FAILING COMPANIES IN SPITE OF MAKING BAD BUSINESS DECISIONS

There is no need to risk all these harms by creating this monopoly. Satellite radio is still in its early stages of development. And, despite protestations in the press, neither XM nor Sirius is a failing company. From an economic perspective, the classic "shut down" analysis illustrates that a firm will exit an industry when its average variable cost exceeds price, which implies that the last unit sold makes a negative contribution to the firm's margins. When applied to XM and Sirius, there is no basis to conclude that either company is ready to exit the industry. Indeed, a review of reports by equity analysts demonstrates that Sirius and XM are currently earning positive margins on their last subscribers. Moreover, as satellite radio penetration rates increase, average variable costs will decrease and thereby generate even larger margins. Thus, there is no basis in economic fact for a failing-firm argument.

You need not take my word about the status of XM and Sirius. XM apparently believes that neither itself nor Sirius will go out of business if the merger does not occur. In a filing with the Securities and Exchange Commission last week, XM disclosed a set of questions-and-answers regarding the merger prepared for and distributed to its

employees. I quote: "Can Sirius and XM succeed as stand-alone companies if the merger is not approved by regulators? – **YES**. That said, we believe a merger is the **preferred** option for Sirius and XM, our shareholders and customers . . . ." Of course Sirius and XM would prefer not to compete with one another, and would prefer to reap the benefits afforded by monopoly status. What company wouldn't? That's why the United Stated has and enforces antitrust laws.

Any suggestion that XM and Sirius are weak or failing businesses based on the amount of debt and the levels of expense must be viewed with a healthy dose of skepticism. It is true that XM and Sirius have had some extraordinary expenses - like the nearly $83 million in stock that Sirius awarded to Howard Stern last month, on his first anniversary on satellite radio. Indeed, the extraordinary costs of locking-up national and regional programming, especially sports programming, on an exclusive basis accounts for a great deal of the cost overhead. But, should companies be able to expect a government bailout for questionable business decisions?

ANY CHANGES IN THE MARKET ENVIRONMENT DO NOT JUSTIFY THE RISK OF MONOPOLY

As for these parties' assertion that the audio marketplace has radically changed and, therefore, the merger is justified, it goes without saying that the audio marketplace is constantly changing. Mere introduction of new audio products, however, can never justify the creation of a government licensed and sanctioned monopoly for satellite radio service. Plain and simply, monopolies are inherently bad. So government should take heed. The history of calculated, intentional rule violations by these two companies

speaks volumes about what kind of conduct you should expect from a satellite radio monopoly, even if the merger were granted with the most extensive set of safeguards and conditions.

Beyond harming consumers, a satellite radio monopoly would have the incentive and the opportunity to engage in unfair competition and anticompetitive practices against other audio service providers, especially radio broadcasters. For example, after a satellite monopoly restructures (unbundles) its program offerings, as promised, we can expect, based on press reports, that the monopoly will attempt to accelerate the acquisition of new subscribers by offering them a lower-cost point of entry -- likely a basic advertiser-supported tier offered for less than the current $12.99 per month. On its face, such a plan may not sound bad, but of course no introductory price would be locked in and a monopoly provider could easily raise this price at a later time to increase profits at the expense of consumers.

Furthermore, the merger parties' announced intention to go after advertising revenue is plainly problematic when one considers the monopoly status of the merged satellite radio operator. With monopoly rents from subscription service, the satellite radio monopoly would have the incentive and ability to cross subsidize its advertiser-supported channel offerings using the monopoly rents from subscription service. Unfair competition in the form of predatory pricing in national advertising markets would be a likely consequence. In addition, the satellite radio monopoly would not stop at national advertising. The combined terrestrial repeater networks of Sirius and XM under common

control would offer substantial opportunities for entry into the local advertising markets by a satellite radio monopoly. The rates for local advertising could be set artificially low with cross-subsidization from monopoly prices. The valuable free, over-the-air service provided by local radio stations – which is entirely advertiser-supported – would be jeopardized by these developments.

THIS MERGER OFFERS NO PUBLIC INTEREST BENEFITS AND SHOULD BE SUMMARILY REJECTED

Worst of all, this merger will not provide sufficient consequential public interest benefits to justify a total monopoly in satellite radio. There are no genuine long-term consumer benefits to this merger, unless you trust a satellite radio monopoly miraculously to put consumers before its profits. Without satellite radio competition, satellite radio subscribers will pay more for what they now receive in a bundle. Without such competition, satellite radio program diversity will be greatly diminished. Without such competition, satellite radio will lose its value as a commercial-free medium to its subscribers. Without such competition, satellite radio subscribers will be left with stranded costs in soon-to-be obsolete receivers. Simply put, all of the consumer welfare benefits described by the merger proponents are short-lived and illusory, compared to the potential permanent harms such a monopoly will pose.

Without question, XM and Sirius will be unable to meet the requisite burden of proof demonstrating the level of public interest benefits necessary to even consider granting a government sanctioned monopoly. As the FCC explained in declining to approve the comparable EchoStar/DirecTV merger: Where "a merger is likely to result

in a significant reduction in the number of competitors and a substantial increase in concentration, antitrust authorities generally require the parties to demonstrate that there exist countervailing, *extraordinarily large*, cognizable, and non-speculative efficiencies that are likely to result from the merger." *EchoStar/DirecTV Merger Order*, 17 FCC Rcd at 20604 (emphasis added). The courts have similarly stressed that proof of extraordinary efficiencies is required to rebut the presumption that a merger in a concentrated market (such as the current duopoly market for nationwide, multichannel mobile radio service) will be anticompetitive. *See, e.g., FTC v. Heinz*, 246 F.3d at 720-21.

Clearly, XM and Sirius will fail to meet this heavy burden. Not only are the parties unable to show "extraordinarily large," non-speculative efficiencies resulting from this merger, the proposed merger will in fact seriously impair marketplace competition and cause cognizable harms to consumers, as I have discussed in detail in this testimony. Thus, there is no reason to approve a merger that would violate FCC rules and precedent, as well as congressional policy, and would grant a state sanctioned monopoly to non-failing companies with a long track record of breaking the rules.

NAB fully supports competition on a level playing field. When all the factors are considered, the proposed merger of Sirius and XM is simply anti-competitive. It is a monopoly in violation of the antitrust laws. It should be dead-on-arrival at the Department of Justice and the FCC. Congress should clearly and expeditiously express its opposition to this merger to both the Administration and the FCC.