STATEMENT

Submitted on behalf of

Common Cause
Consumers Union
The Consumer Federation of America
Free Press
Media Access Project
Prometheus Radio Project

regarding

"The XM-Sirius Merger:
Monopoly or Competition from New Technologies"

before the

Senate Committee on the Judiciary
Subcommittee on Antitrust, Competition Policy and Consumer Rights

March 20, 2007

Common Cause,[1] Consumers Union (CU),[2] Consumer Federation of America (CFA),[3] Free Press (FP),[4] the Media Access Project[5] and the Prometheus Radio Project[6] urge the Congress, the Federal Communications Commission and anti-trust authorities to hold the line against the growing threat to an increasingly homogenized and concentrated media sector: mergers that concentrate ownership in too few hands. The XM-Sirius Radio merger exacerbates long-standing concerns regarding excessive concentration in the media market and its effects on programmer access and consumer choice. But concerns regarding this merger extend beyond general media consolidation concerns: based on the evidence available today, the proposed transaction is a merger to monopoly in a distinct product market that threatens to increase consumer costs and reduce competition and choice.

The proposed merger of the only two satellite subscription radio companies should raise a red flag for both antitrust officials and communications regulators whose job is to promote competition and consumer choice in the marketplace. Not only were XM and Sirius prohibited from merging as a condition of getting their licenses to use the public airwaves to deliver their services, but also, as demonstrated by the enormous growth of satellite subscription radio service at very substantial monthly charges and consumer equipment costs over just a few years, this service is, in fact, a distinct product and could develop into a vibrant competitive market. We believe the companies who seek to merge so soon after they

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[1] Common Cause is a nonpartisan nonprofit advocacy organization founded in 1970 by John Gardner as a vehicle for citizens to make their voices heard in the political process and to hold their elected leaders accountable to the public interest. Now with nearly 300,000 members and supporters and 36 state organizations, Common Cause remains committed to honest, open and accountable government, as well as encouraging citizen participation in democracy.

[2] Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the state of New York to provide consumers with information, education and counsel about good, services, health and personal finance, and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life for consumers. Consumers Union's income is solely derived from the sale of *Consumer Report*s, its other publications and from noncommercial contributions, grants and fees. In addition to reports on Consumers Union's own product testing, *Consumer Reports* with more than 5 million paid circulation, regularly, carries articles on health, product safety, marketplace economics and legislative, judicial and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

[3] The Consumer Federation of America is the nation's largest consumer advocacy group, composed of over 280 state and local affiliates representing consumer, senior, citizen, low-income, labor, farm, public power an cooperative organizations, with more than 50 million individual members.

[4] Free Press is a national, nonpartisan organization with over 350,000 members working to increase informed public participation in crucial media and communications policy debates.

[5] Media Access Project (MAP) is a thirty five year old non-profit tax exempt public interest media and telecommunications law firm which promotes the public's First Amendment right to hear and be heard on the electronic media of today and tomorrow.

[6] The Prometheus Radio Project is a non-profit organization founded by a small group of radio activists in 1998. Prometheus Radio Project believes that a free, diverse, and democratic media is critical to the political and cultural health of our nation, yet sees unprecedented levels of consolidation, homogenization, and restriction in the media landscape. The project works toward a future characterized by easy access to media outlets and a broad, exciting selection of cultural and informative media resources.

began competing and offering consumers innovative new services; so soon after they demonstrated that subscription radio is attractive to consumers and could be much more so with consumer-friendly pricing; and in total disregard of the licensing conditions they accepted in order to use public resources, carry an enormous burden to demonstrate why public officials should abandon all normal rules associated with competitive markets and spectrum licensing to allow this merger.

To date, the public has been given no evidence that would support such a showing. Therefore, the Department of Justice (DOJ) and Federal Communications Commission (FCC) should reject this merger unless and until XM and Sirius present clear-cut facts demonstrating how consumers will benefit from less satellite radio competition.

This merger raises the most fundamental issues in antitrust law and poses a substantial threat to consumers and competition. In order to exercise their responsibility under the competition laws, the federal agencies must start from the assumption that the XM-Sirius merger is a merger to monopoly — a merger between the only two firms in the market for national subscription radio service. The product and geographic market characteristics of satellite radio are easily identifiable and quite distinct from other mobile and stationary audio products. It is national, mobile, programmed radio entertainment. The two services deliver and require consumers to purchase huge bundles of well over 100 channels. There are two, and only two, entities providing such a service. The alternatives the companies suggest are substitutes do not possess this set of characteristics and, therefore, cannot be said to compete directly with the service. Entry into this market is restricted by the need to have a license to broadcast at frequencies that enable the service to be provided nationwide. Consumer switching costs are substantial. The original licenses were issued under strict conditions that the two entities are not allowed to merge. There is no circumstance more disturbing from the point of view of the antitrust laws and the Communications Act than a merger within a distinct product market that takes the number of competitors from two to one. Merger to monopoly is antithetical to the competition laws, perhaps the worst offense against the basic principle that competition is the consumer's best friend.

XM and Sirius offer a number of arguments in support of their proposed merger that have not been supported by reliable evidence. We remain unconvinced by the excuses we have heard offered to justify the merger.

The merging parties claim that national subscription radio service competes, indirectly, with a variety of partial substitutes. While AM/FM radio, iPods and other music recording and listening devices can offer similar prepackaged music or local signals similar to what satellite radio offers, none of them can offer immediate national programming, including live professional sports games from across the country to listeners across the nation. The track record of intermodal competition disciplining anticompetitive abuse is poor at best. "Bank shot competition" — the claim that partial or poor substitutes that are fundamentally different than the target product serve as competitors — has failed to protect consumers in similar situations. The result of relying on such competition in both merger and regulatory reviews has been rising prices and stagnation.

A perfect example is cable television. In the 1980s, federal policymakers claimed that cable TV competed with over-the-air broadcasting. Based on that understanding, the FCC deregulated cable systems in communities with three or more broadcast signals. Cable rates subsequently skyrocketed. By the late 1980s, the failure of this intermodal competition to discipline cable pricing was so obvious that the FCC proposed to increase the number of over-the-air stations necessary to represent effective competition to six. Seeing the results of this failed policy, Congress re-regulated cable in the early 1990s, and intervened in the market to help DBS satellite compete against cable (another form of intermodal competition).

In the decade after the Telecommunications Act of 1996, which largely deregulated cable rates, intermodal competition between cable and satellite failed to discipline cable rate increases. Average monthly cable bills have doubled since the 1996 Act. In short, intermodal competition from neither over-the-air TV nor from digital satellite distribution disciplined cable rates. The former had more limited channel capacity; the later had greater channel capacity. It did not matter. The empirical evidence from the cable market is clear. Only head-to-head competition delivers clear relief from anti-consumer, anticompetitive pricing.

In the satellite radio service product space, we face a similar configuration of products. Traditional broadcast radio, digital Internet distribution and mobile handheld devices, like iPods, that allow consumers to store and play music from their own collections or from online music sites, are touted as the intermodal competitors that will discipline prices. Yet there are distinct differences in product quality, listener experiences and mode of delivery. The touted competitors are not national, not mobile or not programmed. The growth in subscribership and revenues for Sirius and XM, based on their SEC 10-5 filings, reinforce the uniqueness of satellite radio's product offerings. Between 2005 and 2006, satellite radio subscribership rose from 9.3 million to 13.7 million — a nearly 50 percent increase. And combined revenue grew by nearly 100 percent. These data are not consistent with a market that competes with the growing market for digital listening devices. Experience and careful analysis suggests that the effort to position satellite radio as merely one product option in a broader product market should be rejected.

Consumers in the satellite radio space are afflicted by the very same pricing practices that afflict consumers in the cable space. Not only are prices high, but also the consumer is offered only large bundles of channels over which they have no choice. Consumer choice and consumer sovereignty are denied. In a product market where the marginal production cost of adding subscribers is almost zero, the bundling strategy is largely anti-consumer.[7] This merger promises to make matters worse, with large capacity systems joining to create larger consumer bundles at higher prices. The merging parties have suggested they may provide consumers greater choice over the channels they pay for if the merger is approved, perhaps by offering tiers of programming. However, it is unclear whether their willingness to hold prices

[7] The marginal production costs are certainly every low, if not zero, but we are told that the marginal transaction costs (i.e. customer acquisition costs) are high. However, it appears that this problem is a function of the bundling strategy. Having set such a high threshold price, the companies are forced to market aggressively to much narrower market segment.

near current levels does anything more than freeze pricing for yesterday's services. It appears that their promises not to raise prices above the current $12.95/month price for a period of time does not apply to new packages that include the combined services of the two companies – like channel packages that could include Major League Baseball with live NBA basketball and NFL football games. In fact, it is very likely that the "merger benefits" of combining these offerings will require consumers to pay much more than $12.95/month. Yet, in the absence of a merger, it is not clear why prices should not fall far below $12.95/month for existing services if both companies continued to compete against each other and attempted to expand their base of customers.

The merging parties have suggested that post-merger, XM and Sirius subscribers will be held harmless not just on price but also on their current services — that they will receive the same programming they receive now. The purported benefit of the merger is that they will also have the option of receiving additional programming offerings without losing existing channels. Channel capacity will not be a limiting factor, the companies assert, because data compression technology allows them to fit more programming within the same bandwidth. Thus, we're told, XM subscribers would get every channel they get now, plus some Sirius channels, and vice versa. However, many are calling that assertion into question. Coverage of the merger in the March 19, 2007 edition of the *Washington Post* found substantial disagreement whether available technology would allow the companies to add more channels without losing existing channel offerings or degrading audio quality.[8] If that is the case, then there is little consumer benefit to the merger. Consumers seeking content from both providers will need two sets of equipment because dual platform receivers are not yet available. Even when they do become available, it is unclear what they'll cost and whether the parties will offer them to consumers at reduced cost.

The suggestion that free, over-the-air radio will discipline pricing or packaging abuses after the satellite radio firms merge to monopoly, even though it did not restrain their pricing practices up to now is difficult to take seriously. Claims that existing or emerging distribution systems, like cell phones or Internet radio, will discipline the satellite radio monopolists pricing practices are equally suspect. The iPod has been around for a while and has been phenomenally successful, but it sells a very different service and its existence has not disciplined satellite radio pricing practices. There is no reason to believe that it will do a better job if a satellite radio monopoly is allowed to come into existence.

Although the specific product — satellite radio — is new, having been made possible by recent technological advancement, it has achieved a size that establishes it as a distinct product and makes it worthy of public policy attention. Annual revenues exceed $1 billion per year. Abuse of market power in this space could impose a substantial cost on consumers.

Perhaps the most outlandish of all the claims being circulated by the merging parties is the argument that consumers will be better off with a benevolent monopolist than they would be with two competitors. In this ultra-short term view, competition is defined as wasteful,

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[8] Charles Babington, "Radio Deal Could Face Technical Difficulties," *Washington Post*, D1, March, 19, 2007.

since redundant facilities lie unutilized. The monopolist can serve everyone while using less resources and the monopolist promises not to abuse the market power that would result. Without the stick of competition, however, the cost savings simply will not be passed through to the consumer. Indeed, the increase in market power will allow the post-merger monopoly to raise rather than lower prices.

The promise of benevolent monopoly is not worth the paper it is written on. The merging parties suggest the merger will increase consumer choice by giving consumers more than the 130 to 170 channels now available to them by consolidating their offerings, omitting the duplicative offerings while retaining highly demanded and niche channels — these are options that consumers can only have to date by subscribing to both services and buying two radios. Yet there is little discussion of the fact that it is the parties' own practices that have denied consumers choice in the past. Despite requirements by the FCC and the terms of their own patent dispute settlement to develop and provide interoperable radios that would have allowed consumers to switch providers without switching equipment, the companies have failed to meet that commitment. Claims by XM and Sirius that they were required only to "develop" the radio, but not to take steps to ensure it was commercially available provides little comfort to consumers denied choice nor should it ease criticism that these parties sought to comply with only the narrowest interpretation of the commitment. Now, we're told dual platform radios are on the cusp of development and will allow consumers to receive both signals simultaneously, easing technological challenges of the merger. But technology that allows consumers to switch services or subscribe to both if they choose should have been available independent of a merger. Yet instead of promoting consumer choice, the merging parties have forced consumers to invest in equipment that works with just one service, and once so invested, they are stuck with that choice.

Greater enthusiasm by the merging parties for interoperable and dual platform radios prior to the merger would have facilitated the very choice they now purport to offer consumers under the merger but *without* the necessity of a merger. It's important to point out that in their discussion of consumer choice, the merging parties fail to consider the loss of choice between the two providers as a meaningful one. The two parties have not, as a matter of business practice, offered consumers the most fundamental choice – which channels to pay for. They stuck with a high-priced, high volume bundle, which is anti-competitive and anti-consumer.

Moreover, under the scant details released to date, it remains unclear what additional equipment costs will be imposed on consumers as a result of the merger and whether, if consumers fail to invest in additional equipment, they will enjoy benefits the parties purport to provide to their subscribers. For policymakers inclined to accept the notion that consumers are better off with one rather than two satellite radio providers, we recommend, that the spectrum occupied by one of the current licenses be divested and made available for other consumer services. If all we need is one satellite radio company, why not auction half of the XM/Sirius spectrum for other commercial uses? Surely a free-market auction would enrich the Federal Treasury with plenty of money to compensate satellite radio subscribers for any sunk equipment costs, offer consumers new broadband or other wireless services, and still enable Sirius and XM to combine their best offerings with substantial channel capacity.

Because this is a unique product market, once the competition is eliminated, prices will rise over time. More importantly, the primary driver of innovation and progress in both programming and technology – competition in the market – will be eliminated. Innovation will slow to the pace preferred by the monopolist and consumers will be much worse off in the long run. This is a Faustian bargain that America rejected over a century ago when we affirmed our commitment to competition by enacting the Sherman Act and later the 1934 Communications Act. The short-term benefit of a monopolist who is subject to political oversight is simply not worth the long-term costs of abandoning the competitive engine of economic progress.

Offers of conditions on the mergers should also be taken with a grain of salt. The recent track record of conditions has been abysmal and the satellite radio industry has already proven that it cannot be trusted to live up to conditions imposed on it. The satellite radio licenses were issued subject to the condition that the licensees never merge. Yet here they are asking to be excused from that condition. The licensees promised to offer the public interoperable radios that would work with both systems. Yet, ten years have passed and there is no such interoperability because the providers narrowly interpreted their obligation. We are told interoperable radios have been developed but are too costly and thus manufacturers will not install them. Yet we have no ability to verify whether the lack of commercial availability of interoperable radios is due to cost, is the result of technical barriers, or instead is a strategic decision to impose barriers to prevent consumers from switching services. In short, from day one they have failed to meet the conditions of their licenses and the public has suffered as a result.

A satellite radio merger to monopoly is about an avalanche of mergers. There was a key moment a decade ago when the Department of Justice decided that a large monopolist is no worse then two smaller monopolists and allowed the Bell Atlantic-NYNEX merger to go forward. That decision opened the door to a wave of mergers that doomed head-to-head competition in telecommunications. The old telephone monopoly was recreated as two huge geographically distinct monopolies that rarely, if ever, compete.

A satellite radio merger to monopoly will perform a similar bellwether function. If the agencies with oversight adopt a loose definition of products and markets and allow a merger to monopoly on the basis of intermodal competition, then a tsunami of mergers could ripple through the digital space at the worst possible moment. The firms that have declared their undying hostility to the open flow of products in the digital economy (broadcasters, telephone/cellular companies, cable companies), will be empowered to capture and stifle the alternatives, under the premise that every media and telecommunications product competes with all others and that new technologies and services will come along to protect the consumer in any case. That relief, however, will be slow and insufficient because the competitive core of the digital economy will have been damaged and the critical terrain of the digital economy will be controlled by entities that have the same anti-competitive, anti-consumer objectives as the merging parties in this case.

We urge the Congress to tell the FCC and antitrust authorities to put the brakes on the proposed XM-Sirius merger unless and until significant questions on competition and consumer impacts are fully addressed and satisfactorily answered. It is time to hold the line against the greatest threat to a competitive and diverse media: mergers that concentrate ownership in too few hands.

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