5. The Merger Opponents Wrongfully Ignore Other MVPD Providers and Potential Entrants

Another part of the strategy of the merger opponents is to argue that, apart from cable and DBS, other MVPD competitive services are "fringe technologies,"[104] with no prospect of "entering the market on a time frame or a scale sufficient to constrain a DBS monopolist."[105] Again, such statements miss the mark.

First, the statements are inaccurate. There are other MVPD services across the country that retain significant subscribership. C-band satellite, Multichannel Multipoint Distribution Service ("MMDS") providers, Satellite Master Antenna Television ("SMATV") systems, and cable overbuilders all compete with DBS and incumbent cable systems. In fact, the combined MVPD market share of these technologies surpasses 3.25 million households – nothing like the dominance of cable, of course, but about one fifth of the total share of DBS subscribership.[106] In addition, the merger opponents do not accurately characterize the extent to which new MVPD market entry is possible or probable. Thus, the Commission itself has recognized that "competitive [MVPD] alternatives continue to develop."[107]

Second, even if there were no other competitive distribution technologies or prospects for additional near-term entry in the MVPD market – neither of which is the

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[104] NRTC Petition at 23. It is odd that NRTC would make this characterization as it is one of the four major distributors of C-Band programming. Eighth MVPD Competition Report at ¶ 67.

[105] Pegasus Petition at 36.

[106] Eighth MVPD Competition Report at ¶¶ 67-76, 107-112.

[107] *Id.* at ¶ 5.

case – the fact remains that the dominant providers in the market remain cable operators, who have a 78% share. These are the providers that need "constraining," and New EchoStar will achieve that goal.

(a) *Satellite Competition.* As indicated above, the formative years of the DBS industry have demonstrated that effective competition against the dominant cable providers in the MVPD market now requires the combination of the facilities and spectrum to which EchoStar and DIRECTV have access. At the same time, other companies have ample opportunity to use satellite spectrum and orbital locations, as well as other technologies, in an attempt to introduce additional competition in the MVPD market. Nothing in this merger will act to preclude such additional entry.

In this regard, Mr. Sidak is simply wrong in his assessment that "[b]ecause orbital slot allocation is governed by the International Telecommunication Union, not the FCC, the number of orbital locations is fixed."[108] In fact, several orbital locations allotted by the ITU to other countries in the Western Hemisphere have the technical capability to serve the entire continental United States. Two of these countries, Mexico and Argentina, have reached agreements with the U.S. allowing satellites from these orbital locations to serve the U.S. direct-to-home market subject to the same FCC licensing requirements that apply to the U.S. DBS orbital slots.[109] Canada also has an ITU allocation for two DBS orbital locations that could be used to serve the U.S. market.

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[108] Sidak Declaration (NAB) at 20.

[109] *See International Bureau Announces Conclusion of U.S.-Argentina Framework Agreement and Protocol for Direct-to-Home Satellite Services and Fixed-Satellite Services*, 13 FCC Rcd. 16581 (1998); *International Bureau Announces*

(Continued ...)

MVPD competition could be brought to bear by any number of Ka-band licensees. Pegasus, for example, is free to use its valuable Ka-band licenses to provide MVPD service throughout the United States. Far from the dire picture of spectrum warehousing painted by opponents of the merger,[110] there is wide dispersion of Ka-band and other FSS licenses among a variety of licensees.[111] In fact, of the full CONUS Ka-band and FSS orbital locations (those from 83° W.L. to 133° W.L. according to Pegasus),[112] licensees other than New EchoStar would hold a majority of the assets.[113]

Non-full CONUS licensees, such as R/L DBS and Dominion, also will pose a competitive threat to New EchoStar. R/L DBS has proclaimed its ability to serve nearly every corner of the United States with regional programming from the 61.5 W.L. orbital location.[114] Assuming this is true, it and its progeny will be able to compete head-to-head with New EchoStar.

Conclusion of U.S.-Mexico Framework for Agreement and Protocol for Direct-to-Home Satellite Services, 12 FCC Rcd. 13105 (1996).

[110] NAB Petition at iii, 11-12; Pegasus Petition at 63-69; NRTC Petition at 50-56.

[111] Even medium-power FSS satellites still lend themselves to various DTH initiatives, as shown for example by BellSouth's recent plan for a DTH offering. While BellSouth has not gone forward with that plan, the fact remains that ample FSS spectrum remains available for medium-power and high-power satellite DTH initiatives.

[112] *See* Pegasus Petition at 71.

[113] Eleven other entities affiliated with neither EchoStar nor Hughes currently control orbital slots in the 83° W.L.-103° W.L. arc, which demonstrates that there are more than enough prime Ka-band slots controlled by others to ensure that the merger will not "stifle" competition in providing broadband services. *See* "FCC International Bureau Authorizes Second Round Ka-Band Satellite Systems," Press Release (Aug. 2, 2001).

[114] *See* Ex Parte Presentation by Howard J. Symons, Petition of R/L DBS Company L.L.C., For Extension of the R/L DBS Direct Broadcast Satellite Construction Permit, Spot Coverage Map (June 6, 2000).

NRTC and its affiliate Pegasus will also likely compete against New EchoStar by using certain facilities of the combined entity if they desire to do so. Specifically, to the extent that DIRECTV's contract with NRTC grants NRTC the right to distribute certain video programming in certain areas, the merger would not alter its contractual rights. Since NRTC and Pegasus would not in those circumstances be constrained by New EchoStar's national pricing commitment, they would be able to continue to charge more to rural subscribers, as they do now, than DIRECTV or EchoStar, separately or together. In fact, however, the DIRECTV/ NRTC agreement makes clear that NRTC's *exclusive* rights are limited and will expire in the future. As a consequence. New EchoStar will be able to compete fully with NRTC/Pegasus throughout those areas where NRTC and Pegasus have distribution rights under their contracts. This may in turn mean that, for commercial reasons, NRTC and Pegasus no longer will be able to charge more than New EchoStar for the same service, but such a result would be a benefit, not a loss, for rural consumers.

C-band satellite services are maintaining efforts to attract rural subscribers. While C-band is certainly not an effective alternative in urban areas, it should not be discounted as an alternative in rural areas. NRTC itself is a major distributor of C-band service even as it resells DBS service. While acknowledging that the number of C-band subscribers has fallen over the past few years, PrimeTime 24, the self-proclaimed "leading provider of network television programming to the C-band marketplace," claims that, as of November 2001, there were almost 900,000 C-band subscribers in the United States.[115]

(b) *Terrestrial Competition.* The Commission has also observed that entrants using a number of different technology platforms are having an impact on MVPD competition that cannot be ignored. Terrestrial services such as MMDS are capable of serving an estimated 36 million homes.[116] Although MMDS subscribership remained steady in the past year, the competitiveness of MMDS video offerings will likely be enhanced by MMDS operators' roll out of high-speed Internet access service, which can be paired with video to create the type of bundled service offering that consumers increasingly find attractive.[117]

The Commission recently recognized "the growing importance of providers that are overbuilding existing cable systems with state-of-the-art systems that offer a bundle of telecommunications services, including video, voice, and high-speed Internet access."[118] The Commission has termed these overbuilders "Broadband Service Providers" ("BSPs"), and noted that despite the challenges inherent in BSPs' strategy of entering markets with entrenched competitors, BSPs such as RCN and Knology are continuing to grow in terms of revenue and subscribership.[119]

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[115] Comments of PrimeTime 24 Joint Venture at 3.

[116] Eighth MVPD Competition Report at ¶ 71.

[117] *Id.*

[118] *Id.* at ¶ 13.

[119] *Id.* at ¶ 109, 111.

Electric and gas utilities are moving forward with ventures involving video distribution. The Commission noted that although the utilities are "not yet major competitors in the telecommunications or cable markets," characteristics of these entities, "such as ownership of fiber optic networks and access to public rights-of-way, could make them competitively significant."[120] Importantly, utilities appear to hold great promise for competition in rural areas, as the Commission observed that "utilities, particularly some municipal utilities in rural areas, are willing to build advanced telecommunications networks offering a full range of services where incumbent cable operators and telephone companies are not."[121]

Finally, the Commission has reported that it is "technically feasible" for a new terrestrial service, which the Commission has dubbed Multichannel Video Distribution and Data Service ("MVDDS"), to share spectrum allocated to DBS in the 12.2-12.7 GHz band.[122] The Commission has adopted a Further Notice of Proposed Rulemaking seeking comment on technical and service rules for licensing the new services.[123] Four companies, Northpoint Technologies, MDS America, Satellite Receivers, Ltd. and PDC Broadband Corporation have sought licenses or otherwise expressed interest in providing such a service. While EchoStar and DIRECTV have opposed the interference levels posited by proponents of MVDDS, they also have stated

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[120] *Id.* at ¶ 104.

[121] *Id.*

[122] *Id.* at ¶ 64.

[123] *Id.*

on the record that competition from such services is welcome so long as no interference occurs.[124]

(c) *Analogous examples of "intermodal competition."* The broad view of MVPD as the relevant market is consistent with that of other agencies regulating different but competing technologies. In their competitive analysis, agencies typically consider not only the provision of service by the particular mode of carriage utilized by the company at issue, but also other competing forms of carriage (frequently referred to as "intermodal" competition).[125]

In an analogous case, for example, the Interstate Commerce Commission ("ICC") took a broad view of the relevant market in approving the merger of the

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[124] *Cable and Satellite Broadcast Competition: The Status of Competition in the Multi-Channel Video Programming Distribution Marketplace Before the House of Representatives Energy and Commerce Committee, Subcommittee on Telecommunications and the Internet* (statement of Charles Ergen, Chairman and CEO, EchoStar Communications Corporation) (Dec. 4, 2001) ("While EchoStar does not oppose the emergence of new competitors in the MVPD market, we are opposing the proposal by Northpoint, because Northpoint's current proposal would cause electrical interference with the satellite reception of our established satellite TV customers as confirmed by the MITRE Corporation's testing."); *see also* Comments of EchoStar Satellite Corporation in CS Docket No. 99-250 (Aug. 16, 1999) at 1, 3 ("EchoStar welcomes new entry into the MVPD market and applauds the Commission's proposal" to open the 12.7 – 13.2 GHz band for use by all MVPD providers… [T]he Commission should consider this band as yet another possible home for the service planned by Northpoint Technology.")

[125] *Market Dominance Determination & Consideration of Product Competition*, 365 I.C.C. 118, 130 (1981); *see also Market Dominance Determinations – Product and Geographic Competition*, STB Ex Parte No. 627, 1 n.2 (served April 6, 2001)(noting that Board's market dominance analysis considers, among other things, "whether the complaining shipper can use other transportation modes, such as trucks or barges, to transport the same commodity between the same points"); *Williams Pipe Line Co.*, 68 F.E.R.C. ¶ 61, 136, at 61, 660 (1994).

Trailways bus line into Greyhound, at a time when those two lines accounted for the vast majority of intercity bus transportation in the U.S. As the ICC stated, "the relevant 'product' market is the intercity transportation of passengers," including private automobile, airlines, intercity bus, and Amtrak.[126] The Commission went on to explain that, essentially, the national pricing of bus transportation was a sufficient safeguard: "bus passengers, even those with limited access to air, Amtrak, or private auto will continue to be protected from unreasonable rates by the market discipline of intermodal competition since remaining bus firms must set rates and service to attract passengers who do have these options."[127] In affirming, the Court of Appeals for the D.C. Circuit cited approvingly the ICC's findings that the market included other modes of transport, that "competition in the national market was necessary to promote the public interest," and that "even in rural markets, the consolidation would have little effect because intermodal competition would provide a sufficient cap on unreasonably high prices or inadequate services."[128]

Like the Greyhound/Trailways transaction, the proposed merger should be evaluated in the broader market. Here, as there, all consumers will be protected because New EchoStar "must set rates and service to attract [consumers] who do have these options."

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[126] *GLI Acquisition Company Purchase Trailways Lines, Inc.*, ICC Decision No. MC-F-18505, at 7 (May 27, 1988).

[127] *Id.* at 10.

[128] *Peter Pan Bus Lines, Inc. v. ICC*, Nos. 88-1532, 88-1566, 88-1567, slip op. at 5 (D.C. Cir. May 8, 1989).

6. Petitioners Cannot Prove the Existence of a DBS Market from Echostar's Pre-Trial Position in a Dismissed Proceeding

Petitioners NAB and Pegasus, among others, try to prove their economic case by recourse to statements that EchoStar made in a 2000 pre-trial request for extension of time in a now dismissed antitrust dispute with DIRECTV.[129] The Petitioners use these statements to suggest that EchoStar believes in the existence of a separate DBS market, that therefore there must be such a market, and that EchoStar has reversed course now only to serve its interest in approval of the merger Application. The Petitioners misread these litigation statements, and in any event their reliance on them to prove their economic case is misplaced, particularly since none of their own economic experts has argued in favor of a separate DBS market.

First, it is certainly not true that EchoStar's belief in a single MVPD market is of recent origin. EchoStar has always held the same view: that there is one MVPD market, in which cable is the incumbent and dominating player, and that DBS competes, although presently with distinct disadvantages, against cable within the MVPD market. It has also consistently recognized that certain factors have historically inhibited DBS from robustly competing with cable.

EchoStar has expressed that view on dozens of occasions, starting as early as 1995. In 1996, for example, EchoStar asserted that "the relevant market includes all

[129] NAB Petition at 37-40; Pegasus Petition at 12-14.

multichannel video programming distributors, not just DBS service providers."[130] In 1997 EchoStar wrote in comments to the Commission: "Ever since it commenced DBS service in the spring of 1996, EchoStar has viewed cable subscribers as its primary target market. Accordingly, EchoStar has priced and structured its offering with the primary purpose of attracting cable subscribers."[131]

In December 1998, EchoStar expressed a similar view with respect to the potential impact of its transaction with MCI: "EchoStar emphasizes that the MVPD market – not any subset of that market – is the relevant market for analyzing the public interest impact."[132] It also noted that "DBS service has emerged as the most likely alternative with the potential for introducing full-fledged competition against dominant cable operators in the MVPD market, but is still a long way from realizing that potential because of various spectrum-related and regulatory constraints."[133] Appearing before a congressional committee in 1999 regarding EchoStar's efforts to compete with cable systems, EchoStar's Chief Executive Officer Mr. Ergen testified: "The relevant market for our service is the MVPD market. DOJ has found extensive evidence of customers

[130] *In re Application of Direct Broadcasting Satellite Corp.*, 11 FCC Rcd. 10494 (1996) at ¶ 8.

[131] Comments of Echostar Communications Corp., *In re Annual Assessment of the Status of Competition in Market for the Delivery of Video Programming*, CS Docket No. 97-141 (July 23, 1997) at 2.

[132] *In re Application of MCI Telecommunications Corp. and EchoStar 110 Corp.* (Dec. 2, 1998) at 7.

[133] *Id.* at ii.

switching from cable to DBS, contrasted with the early days of DBS, when subscribers most often came from uncabled areas."[134]

While this view of the relevant market was certainly the prevalent one in 2000, this does not mean that it was free from any doubt. As zealous advocates, EchoStar's lawyers in the litigation had the duty to explore fully the extent to which any such doubt could be used to bolster EchoStar's case. This was the context of the statements seized on by Petitioners in EchoStar's request for more discovery to shed additional light on the factual issues. In its *Request for Rule 56(f) Continuance to Respond to Defendants' Motion for Summary Judgment*, EchoStar argued that the summary judgment requested by DIRECTV was inappropriate pending ongoing discovery and in light of the need for additional discovery on highly complex issues such as market definition. The statements cited by Petitioners described only beliefs about what the evidence could establish, and they did not purport to be statements of proven fact. Indeed, EchoStar explicitly noted that its assertions were based on a preliminary understanding of the case, stating that "expert witnesses will play an important role on several issues, including the definition of the relevant market."[135]

Finally, even if there were any potential counter-argument about the relevant market in 2000, it has been dispelled by developments that were then in their early stages and that have since matured decisively. As explained above, these

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[134] Charles W. Ergen, Testimony Before the Subcommittee on Antitrust, Business Rights, and Competition, Committee on the Judiciary, U.S. Senate (Jan. 27, 1999) at 3.

[135] *Request for Continuance*, at 3.

developments include: on the one hand, the fuller extent to which DBS providers have since been able to capitalize on the local-into-local opportunity afforded by SHVIA since the end of 1999; and, on the other hand, the aggressive roll-out of digital cable.

B. NRTC, NAB and Pegasus Criticisms Of The FCC's "Homes Passed" Estimate Are Not Persuasive and Rely on Inaccurate Data Sources

In discussing the lack of anti-competitive impact on rural markets of the proposed transaction, the Application referenced the Commission's then-current statement on cable availability, which observed that over 96% of all television households in the United States are passed by cable television systems and that these cable operators continue to be the dominant distributors in the national MVPD market.[136] The Commission has since released its Eighth Annual MVPD Competition Report which places the current percentage of television households passed by cable at 97.1%.[137] NRTC, NAB and Pegasus argue that the statistics cited by the Commission overstate the percentage of TV households that have access to cable. These Petitioners, however, provide nothing but speculation to support their claims. And, even if the parties in this proceeding could agree on a percentage of homes not passed by cable, the practical

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[136] Merger Application at 39-40 (citing Seventh MVPD Competition Report, 16 FCC Rcd. 6005, at App. B., Table B-1).

[137] Eighth MVPD Competition Report at ¶ 17.

significance of this number would be insignificant, since New EchoStar effectively would be unable to isolate such consumers for an anticompetitive action.[138]

In every Annual Report on the status of competition in the MVPD market since the Commission first began issuing them, the Commission has relied on data collected by Paul Kagan Associates, Inc. for the number of homes passed by cable.[139] Likewise, each year the Commission has compared the number of homes passed with the number of television households to obtain a sense of the availability of cable services to television viewers.[140] No Petitioner argues that this is the incorrect comparison for the Commission to make; nor could they, since the availability of cable to unoccupied housing units and occupied households without a television is indisputably irrelevant. Instead, the Petitioners argue that the Kagan data relied upon by the Commission overstates the number of television households in determining the number of homes passed, and that as a result, the percentage of television households passed by cable may

[138] *See* Willig Declaration at ¶ 98 (explaining that the percentage of homes passed by cable is only relevant if New EchoStar is able to "find" the non-cable passed homes, a process that would be extremely difficult and costly).

[139] *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 11 FCC Rcd. 2060, 2068 n. 19 (1995) ("Second MVPD Competition Report") (explaining source of data for First MVPD Competition Report); Third MVPD Competition Report, 12 FCC Rcd. 4358, 4368, 4465; Fourth MVPD Competition Report, 13 FCC Rcd. 1034, 1049, 1174; *In the Matter of Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Fifth Annual Report, 13 FCC Rcd. 24284, 24322 (1998) ("Fifth MVPD Competition Report"); Sixth MVPD Competition Report, 15 FCC Rcd. 978, 990, 1080; Seventh MVPD Competition Report, 16 FCC Rcd. 6005, at ¶ 18, App. B. Table B-1; Eighth MVPD Competition Report, FCC 01-389, at ¶ 17, App. B. Table B-1.

[140] *Id.*

be inaccurate and could be as low as 81% instead of the 97% figure cited by the Commission.[141]

The Petitioners' entire argument in this regard is based on the assertion that cable operators include unoccupied housing units and non-television households in the homes passed data that they provide to Kagan.[142] The assumption underlying this theory is that cable operators have no way to determine the number of television households in their service area.[143] Yet, this assumption is entirely unsupported by the Petitioners. Cable operators have every incentive to determine this figure because it defines their potential local customer base. The figure is relevant to any number of budgeting, marketing and other financial efforts undertaken by cable operators. Moreover, the number of television households in a service area is not unknowable. To the contrary, Nielsen Media Research publishes yearly estimates of TV households on a county-by-county basis for the entire U.S.,[144] and provides studies at an even finer level of granularity at the request of private entities. There is every reason to believe that cable operators are well informed concerning their potential customer base when they respond to Kagan data requests.

Indeed, the Petitioners' own attack on the numerator of the calculation shows that the Kagan number of homes passed may in fact be *understated* in one

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[141] NRTC Petition at 9; Pegasus Petition at 16; NAB Petition at 46.

[142] NRTC Petition at 9; NAB Petition at 46.

[143] NRTC Petition at 9-10 (quoting NTIA/RUS Report at 19 n. 62)

[144] *See* Broadcasting & Cable Yearbook 2001 at B-160 – B241.

important respect. NRTC attacks the data based on each cable operator's uncertainty about which of several possible "homes passed" criteria to use: feeder cables in place nearby; cable television "readily available"; "potential" to be connected; or, households "capable" of receiving service.[145] As Dr. Willig notes, the correct criterion is the broadest one, i.e., the number of homes with the potential for being connected to the cable system.[146] The potential for a home to be connected to a cable system is enough for the purpose of disciplining a satellite provider's conduct. All of the other criteria listed by the NRTC may be read as requiring *more than that* for a home to be considered "passed." To the extent that a cable operator may be using a more restrictive "homes passed" criterion, the number of homes passed may in fact be *understated* from the economic point of view.

Petitioners also attempt to support their theory regarding the Kagan data by citing data from Warren Communications ("Warren") on homes passed in six states, which exceeds the 2000 Census Bureau data on the number of occupied households in those states.[147] However, as Dr. Willig observes, Petitioners make no attempt to explain how data and collection practices by Warren Communications support their theory that *the Kagan* data is erroneous.[148] Petitioners also compare the Kagan data on homes

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[145] *See* NRTC Petition at 10.

[146] *See* Willig Declaration at ¶ 98, n.119.

[147] NRTC Petition at 11-12; NAB Petition at 46.

[148] *See* Willig Declaration at ¶ 98 ("No commenter has provided any evidence that the Warren data are more accurate than the Kagan data.")

passed in the U.S. with Census Bureau data on occupied households in the U.S., but this comparison is likewise unavailing in support of Petitioners' theory because there is no indication that the data collection and analysis practices of Kagan and the Census Bureau are the same or even similar. Simply put, the Petitioners do not make a persuasive case supported by hard evidence that the Kagan data, on which the Commission, industry and investors have relied for years, is incorrect or overstated.[149]

Certainly, the opposite appears to be true for the figures proffered by the NRTC the NAB and their economic experts. As Dr. Willig explains, Dr. MacAvoy and Mr. Sidak both present a series of maps that purport to show areas where cable is available and where cable is not available and purport to show that it is possible to identify these areas with a great deal of precision.

As an initial matter, it is important to realize that these maps are based on information that is provided to Warren Communications by the cable companies. To the extent this information is inaccurate or not kept current, Warren's information will not be accurate.[150]

Dr. Willig independently tested the accuracy of the Warren data in two ways: First, he analyzed DIRECTV churn data and examined whether any customers who lived in zip codes that the Warren data suggest were not passed had churned from

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[149] NRTC also attempts to manipulate the numbers to its own advantage by arguing that 23 million homes do not have access to cable. NRTC Petition at 14; *see also* Pegasus Petition at 17. By NRTC's own analysis this 23 million home figure includes unoccupied housing units and homes without televisions. *Id.*

[150] Willig Declaration at ¶ 95.

DIRECTV to cable. The data that Dr. MacAvoy and Mr. Sidak present suggest that a large number of zip codes are not passed by cable. But the DIRECTV data indicate that *more than one quarter* of the customers who lived in these supposedly non-cable passed zip codes and who left DIRECTV, *left for a cable provider.*[151]

Next, to ensure that the problem is not with misreporting in the DIRECTV churn data, Dr. Willig asked Ginsberg Lahey, LLC, a Washington-based research firm, to check the accuracy of these results by contacting the local cable firms to ensure that subscribers in these zip codes could receive cable service. For a significant number of these zip codes, Ginsberg Lahey was able to confirm the accuracy of the DIRECTV churn data by verifying with the local cable provider that cable service was indeed available.[152] Ginsberg Lahey also contacted local cable firms in zip codes that the Warren data suggested were not passed by cable. In two weeks alone, Ginsberg Lahey discovered that *at least 20 zip codes that Warren indicated were not passed by cable were in fact cable passed.*[153]

In any event, even assuming *arguendo* the correctness of Pegasus's characterization that "[t]here is a range of estimates and some controversy over the number of U.S. homes that lack access to cable,"[154] the homes passed issue is only

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[151] *Id.* at ¶ 96.

[152] *Id.*

[153] *Id.* Ginsberg Lahey found that cable service was available in the following zip codes: 13635, 13690, 24649, 25040, 25205, 30045, 30297, 30127, 37191, 40165, 46175, 47145, 42085, 55783, 63966, 66040, 70577, 72073, 77561, and 77650. The Warren database suggests that each of these zip codes is not passed by cable.

[154] Pegasus Petition at 17.

relevant to the extent that New EchoStar would be able to discriminate against consumers in those areas not served by cable. This is not possible for at least three reasons. First, as described more fully by Dr. Willig, economic theory predicts that in the situation that Pegasus describes, where homes passed data may be unsound and yield uncertainty regarding the identification of customers in non-cable passed areas, a firm is not likely to engage in price discrimination.[155] In particular, New EchoStar would need to be wrong only in a relatively small number of cases to make it unprofitable to charge different prices to non-cabled and cabled customers.[156]

Second, as originally described in the Application, the geographical diversity of those television households not served by cable makes discrimination between television households that are served by cable and those that are not very difficult.[157] Indeed, this latter point is aptly demonstrated by the maps of the fourteen "clusters" of rural areas included in the MacAvoy Declaration.[158] Those maps quite clearly show that census blocks without access to cable are interspersed with census blocks that do have access to cable in a way that would not permit a DBS provider to discriminate between cabled and non-cabled areas. In short, as Dr. Willig observes, even if the Warren (or Kagan) maps and data were accurate, cable franchise areas do not correspond to geographic designations such as DMAs, counties, or even zip codes. Thus,

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[155] *See* Willig Declaration at ¶ 94.

[156] *Id.* (citation omitted).

[157] Merger Application Att. A. Willig Declaration at ¶ 37.

[158] MacAvoy Declaration (NRTC) at 10-25.

even if New EchoStar were to price differently based on the zip code of a customer, the zip code of a customer will not tell New EchoStar precisely whether that customer is passed by cable or not. Therefore, Dr. Willig found, it "cannot be concluded from these maps that New EchoStar could implement a price discrimination scheme based on whether customers had cable available or not.[159]

Finally, New EchoStar's commitment to the one nation, one rate card plan, which is addressed in more detail below, also will ensure that no discrimination occurs. At bottom, the question that the NRTC and others have injected into this proceeding over the number of homes passed by cable is a red herring that is not decisionally significant.

C. Petitioners' Analyses Begin From a False Baseline of Healthy Competition in the MVPD Market

The proposed merger will have significant pro-competitive effects in the relevant MVPD market, and the Applicants' one nation, one rate card commitment can demonstrably address any alleged anti-competitive effects on this market. The Petitioners' assertions that the merger will result in higher prices for consumers are wrong from the starting point. They are based on false, rosy assumptions about the welfare of MVPD consumers today. In particular, as shown above, Petitioners disregard at least two crucial facts: (1) EchoStar's and DIRECTV's services are *not* perfect substitutes for each other; and (2) neither company on its own has been able to rein in the

[159] *Id.* at 63.

behavior of large cable MSOs, which continue to raise their prices well in excess of the Consumer Price Index.

Instead of recognizing these facts, the Petitioners assume implicitly that there is now full-blown competition in the MVPD market between DBS and cable. Starting from that premise, they attempt to show that the merger will destroy much of this competition to the detriment of consumers. The premise is false, however.

To the question of whether MVPD consumers are well off today, the consumers' representatives correctly answer, no.[160] The Commission should not base its evaluation of the merger on the contrary assumptions entertained by the NAB, Pegasus and NRTC – that all is basically well today in the MVPD market.[161]

D. The Merger Will Result In Lower Prices for MVPD Consumers In Urban And Rural Areas

Some Petitioners argue that the merger will decrease the number of competitors from 2 to 1 in some areas, and 3 to 2 in others, thereby resulting in increased prices for MVPD consumers and a net public welfare deficit.[162] In support of this

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[160] Comments of Consumer Groups at 4-7.

[161] NAB Petition at 13-15; Pegasus Petition at 9-10; NRTC Petition at 1-2.

[162] *See, e.g.*, NAB Petition at 52-56 ("a horizontal merger may 'create a single firm with substantial market power, enabling that firm to unilaterally raise prices. . .'" (quoting ABA Section of Antitrust Law, Antitrust Law Developments 493 (4th ed. 1997)); NAB's Sidak Declaration at 21-30 (calculating supposed price increase that would result form "duopoly-to-monopoly merger" and from a 3-to-2 merger); NRTC Petition at 30 (merger would lead to "monopoly prices to rural Americans"); NRTC's MacAvoy Declaration at 47-51 (predicting price increases as a result of merger); Rubinfeld Report (Pegasus) at 3.

proposition, Petitioners pursue two somewhat inconsistent lines of attack: (1) that New EchoStar will seek to maximize profits by instituting a patchwork of different prices in different areas of the country; or (2) that even with a national price commitment, New EchoStar will be able to raise its prices unilaterally in both urban and rural areas; and that the merger will facilitate collusion and allocation of territories between New EchoStar and cable operators.[163] The first category of arguments ignores the Applicants' national pricing commitment, the Applicants' past pricing practices, and the reasons why national pricing makes as much sense for satellite television services as it does for national offerings of Internet access and cell-phone services. The second category of arguments disregards that New EchoStar must set its price to be competitive in the most competitive markets where the largest number of potential subscribers are located. By setting its price above competitive rates or colluding with a cable operator, New EchoStar would forego large pools of U.S. consumers and fail to maximize its profits.

1. The One Nation, One Rate Card Plan Will Be an Effective Constraint on New EchoStar

The Petitioners question the value of New EchoStar's commitment of national pricing as a constraint on prices.[164] Their arguments ignore the fact that national pricing is consistent with the Applicants' efficiency-enhancing incentives and with their prior practices. It is also consistent with the practices of other national providers in

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[163] NAB Petition at 96-98 (Sidak Declaration at 34-35); Pegasus Petition at 53-55; NRTC Petition at 35-38 (MacAvoy Declaration at 52-55).

[164] NAB Petition at 96-98; Pegasus Petition at 53-55; NRTC Petition at 35-38.

comparable network industries. The ability to offer local promotions for installation and equipment will not undermine the effectiveness of national pricing as a constraint. Discrimination in the quality of service has not been a problem in the past, and the same incentives that have prevented the Applicants from practicing such discrimination to date will remain in place after the merger to prevent it in the future.

As set forth in the attached Declaration of Dr. Willig, national pricing, which both EchoStar and DIRECTV have always used, makes sound economic sense. Offering a national price will allow New EchoStar to take advantage of this national footprint when marketing its services – using television advertising, for example, and making the price of the service part of such campaigns. In contrast, tailoring packages to particular areas would cause the loss of the economies of scale inherent in a national marketing campaign.[165] Moreover, customer service and direct sales are also done on a national basis, and implementing local price variations would require customer service representatives to be knowledgeable about a wide range of prices, only some of which would be available to any particular customer.[166]

Even if these efficiencies did not attend national pricing, it would be extremely difficult to charge different programming prices in different areas. As Dr. Willig explains, evidence of this difficulty is demonstrated in areas where NRTC sells DIRECTV service at a price $3 per month higher than DIRECTV charges for the same

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[165] *See* Willig Declaration at ¶ 94. As Dr. Willig observes, while it is true that some local variations exist with respect to promotions, these are largely with respect to equipment, installation and value-added gifts, for example, an umbrella. *Id.* at 60-61.

[166] *Id.*

service. In such areas, EchoStar could maintain or perhaps strengthen its competitive position vis-à-vis DIRECTV and charge an extra $1 or $2 in NRTC areas (which are easily identifiable). However, EchoStar has not reacted to this price disparity by charging higher prices, providing additional evidence of the inefficiencies of regionally pricing DBS services. [167]

Nor could New EchoStar implement a price discrimination scheme based on whether customers had access to cable or not.[168] Dr. Willig shows that the task of isolating consumers without cable is inherently difficult and imprecise (for example, the Warren data used by Sidak and MacAvoy are rife with inaccuracies). And as Dr. Willig explains, it would only be necessary for New EchoStar to be wrong in a relatively small number of cases before it would become unprofitable to charge different prices on this basis.[169] Such a price discrimination scheme, therefore, simply would not make good economic sense.

The fact that in the past the Applicants have used a limited number of local promotions to attract new subscribers in no way undermines their national pricing commitment. In a "Catch-22," the Petitioners attack the notion of national pricing both if New EchoStar renounces the ability to offer local promotions (they say it would be inefficient) *and* if New EchoStar retains that ability (they say local promotions will

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[167] Willig Declaration at ¶ 93.

[168] Sidak Declaration (NAB) at 34-35; MacAvoy Declaration (NRTC) at 52-53.

[169] Willig Declaration at ¶ 94.

undermine the value of the national pricing commitment).[170] The truth is that local promotions can be a valuable tool to the same limited extent that Applicants have used them in the past, for example, in testing a promotion before taking it national, and that such limited promotions will not detract from the effectiveness of national pricing as a safeguard against price discrimination.

The local promotions that EchoStar and DIRECTV have offered over the years have been limited in geographic scope, time, value and number of subscribers affected. In the last year, for example, EchoStar and DIRECTV have offered local promotions in only a handful of areas. These areas have been targeted due to localized, specialized reasons such as cable bounty programs targeted at local rate increases. Importantly, the promotions have been limited in duration and very limited in scope. Over the last year, for example, subscribers gained by local promotions were a very small percentage – less than 5% of EchoStar's total new subscribers for that period. Such limited local promotions for installation or equipment have not affected at all the levels at which the Applicants have set their national rates in the past and, according to Dr. Willig, will not do so in the future. For example, the effect on the profit-maximizing national pricing level would be negligible if New EchoStar were to offer in the first year of its operations only promotions of the same scope as those EchoStar and DIRECTV offered in the past. Indeed the Applicants are willing to commit to reasonable requirements to ensure that national pricing is an effective constraint on pricing behavior, consistent with efficiency and market dictates.

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[170] NAB Petition at 94-95; NRTC Petition at 31-35.

The Applicants also have engaged in no regional discrimination in the quality of service for several reasons. These reasons include the importance of national brand building and the significance of the DBS quality rankings by national consumer services evaluating quality on a national basis, such as J.D. Power. Some Petitioners nonetheless assert that New EchoStar will have an incentive to discriminate in the quality of the service it offers to subscribers with fewer MVPD alternatives.[171] The facts, however, disprove this assertion. Dr. Willig analyzed DIRECTV's customer satisfaction survey to determine whether DIRECTV currently engages in any form of non-price discrimination. Dr. Willig found that "the results suggest that rural customers are just as satisfied with DIRECTV's overall service and customer service as non-rural customers."[172] EchoStar, for its part, has generally received significantly fewer complaints, both on an absolute and a proportionate basis, from consumers in rural areas than from urban households. This fact alone disproves the Petitioners' assertion that New EchoStar will have an incentive to discriminate against customers with fewer choices, for if this speculation were valid, each company today would have the incentive to reduce its service quality in those rural areas. EchoStar has not done so, proving that it values the image of its brand over the alleged incentive to pick and choose to whom it offers its top-ranked customer service.[173]

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[171] Rubinfeld Declaration (Pegasus) at 16; NAB Petition at 98, Sidak Declaration (NAB) at 36; NRTC Petition at 31, MacAvoy Declaration (NRTC) at 55.

[172] Willig Declaration at ¶ 69.

[173] American Customer Satisfaction Index of the University of Michigan Business School, Aug. 20, 2001. *See* http://www.theacsi.org.

2. "One Nation, One Rate Card" Will Translate Effective Competition in Urban Areas Into Benefits to All Households and Renders the "3 to 2" and "2 to 1" Arguments Baseless

Petitioners allege that, even with a national price commitment, New EchoStar would raise its prices or collude with cable operators to maximize its profits. Petitioners specifically argue that the merger will reduce the number of competitors from 2 to 1 in areas without access to a non-satellite MVPD provider, which will permit New EchoStar to charge "monopoly" prices, and that it will also reduce the number of competitors from 3 to 2 in areas served by non-satellite MVPD, leading to higher "duopoly" prices and facilitating collusion.[174] The cost/benefit analysis posited by Petitioners to reach this conclusion, however, assumes that New EchoStar would have no interest in growing its base of subscribers, and the only question would be how to maximize its profits from its existing subscriber base. Under Petitioners' analysis, New EchoStar would increase its prices if the additional profits from *existing* subscribers that have no realistic alternative service exceed the lost revenues from *existing* subscribers

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[174] See, e.g., NAB Petition at 52-56 and Sidak Declaration (NAB) at 21-30 (calculating supposed price increase that would result from "duopoly-to-monopoly merger" and from a 3 to 2 merger); NRTC Petition at 30 and MacAvoy Declaration (NRTC) at 47-51 (predicting price increases as a result of merger); Pegasus Petition at 21-22, 29-30 (speculating that the merger will lead to "unilateral anti-competitive effects enabling a single DBS firm to increase price independently of how rivals behave, or will enable one satellite and one cable firm to coordinate behavior resulting in "greater freedom to raise prices"); CWA Petition at 2 (the reduction of competitors from 2-to-1 or from 3-to-2 will allow the merged firm to raise prices); Letter from the National Consumers League, National Farmers Union and the National Grange to William F. Caton, Acting Secretary, FCC (Feb. 4, 2002), at 1 (merger to monopoly will lead to higher prices).

choosing to cancel New EchoStar's service. However, Dr. Willig explains that such an approach would not be in New EchoStar's economic interests, for the simple reason that New EchoStar would not be maximizing revenue if it restricted itself to existing subscribers.

A subscriber growth strategy is far more profitable for a firm such as New EchoStar that would serve a little more than 20% of the nation's MVPD households with a relatively high cost satellite fleet and uplink centers and relatively low marginal costs. As Dr. Willig explains, given the national pricing commitment, the prospect of gaining even a small percentage of new subscribers from the largest DMAs in the country would be much more valuable to New EchoStar than any prospect of extracting extensive rents from rural subscribers.[175] In other words, the benefits of gaining additional subscribers in the largest DMAs by charging a competitive price would be much more valuable to New EchoStar than the additional margin from any conceivable rate increase above a competitive price. And this comparison does not even take into account the revenue streams from advertising or from pay-per-view, VOD, and interactive services. These services are likely to be relatively more attractive in more affluent, urban areas, and they are more reason why New EchoStar would not want to forgo the huge pools of urban subscribers.

This profit maximizing strategy is consistent with the way in which both DBS companies have uniformly favored growth to date, even though the prospects of growth are dampened by the constraints on EchoStar's and DIRECTV's ability to take on

[175] Willig Declaration at ¶ 39-41.

digital cable as an equal and from their ability separately to offer local channels to all DMAs and thereby compete more effectively with cable providers in all markets. EchoStar, for example, aggressively prices its America's Top 50 and 100 packages at $22.99 and $31.99 per month in order to convert cable subscribers, even though Pegasus and NRTC charge a full $3.00 more per month in rural areas, leaving EchoStar ample room to raise its prices in those areas without losing rural subscribers. This growth strategy will make even more sense post-merger as New EchoStar takes advantage of the spectrum and other efficiencies gained by combining the two companies' resources in order to better compete with digital cable and therefore increasing the prospects for urban subscriber growth.

Therefore, based on current and past practices in the DBS industry, as well as sound economic theory and modeling, there is no question that New EchoStar will set its national price at a competitive level based on the MVPD prices prevailing in the most populous markets in the nation. Precisely because of these profit-maximizing incentives, national pricing will act as a means of bringing to all Americans, wherever they are located, the benefits of MVPD competition, wherever in the country it is the most intense. Competitive pressures from MVPD distributors operating in the largest cities will translate into benefits for consumers that are not directly served by these distributors.

Accordingly, the merger will not, as alleged by Petitioners,[176] be a "2 to 1" in any respect that matters for any area that is not passed by cable any more than it will

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[176] NAB Petition at ii, Sidak Declaration (NAB) at 12); NRTC Petition at v; ACC Satellite TV Comments at 5.

be a "3 to 2" for any household that is served by a cable system. To maximize its profits, New EchoStar will have to set its prices at levels allowing it to compete for subscribers in the most densely populated and most heavily contested markets.

3. There Is No Realistic Possibility of Collusion Among the Cable MSOs and New EchoStar

For the same reasons that New EchoStar will attempt to maximize its profits by competing vigorously with those MVPD distributors serving the largest DMAs, the concerns expressed by Petitioners about collusion among New EchoStar and cable operators are unfounded. First of all, this particular tango would require New EchoStar to dance with as many as 10 cable MSO partners simultaneously. New EchoStar would have to coordinate not only with one cable operator but at least with most, if not all, of the largest cable MSOs operating in the nation's most populated areas.

As explained by Dr. Willig, if any one of the major cable MSOs – AT&T/Comcast, AOL/Time Warner, Cablevision, Charter or Adelphia – were to refuse to participate in a deal to set prices at artificially high levels, a pool of millions of potential customers would automatically become unavailable to New EchoStar, making such a deal among the remaining parties economically unattractive.[177] Nor is Mr. Sidak's postulation of a "tacitly collusive strategy of market allocation" where "DBS would keep the rural customers and cable would be free to take the urban customers,"[178] a realistic

[177] Willig Declaration at ¶¶ 72-73.

[178] Sidak Declaration (NAB) at 34-35.

possibility. Such a deal could not happen for a simple reason, among others: the failure of consideration. New EchoStar would be giving up a huge pool of potential subscribers without getting anything in return. In particular, a promise on the part of large cable operators to hold back from expanding into the few truly unpassed rural areas would be meaningless, as cable operators would be unlikely to find such expansion profitable anyway. In short, under this theory, New EchoStar would be willing to act irrationally by forgoing the opportunity to gain subscribers in the nation's most populated urban areas and getting nothing in return.

Ever since the inception of their services, both EchoStar and DIRECTV have consistently followed a strategy of making their services increasingly competitive with cable systems in order to convert cable customers and obtain a large percentage of new MVPD subscribers. The proposed merger is the next logical step in that direction in order to keep pace with digital cable, and it is illogical to view it as an attempt to revert to the bygone era of rural-only satellite television. Such a strategy would be equivalent to economic suicide for New EchoStar.

E. Rural Cable Operators Will Continue To Be A Competitive Factor

The fear expressed by the American Cable Association that rural cable operators may be forced to discontinue operations is both overblown, inconsistent with the cable industry's representations to the Commission in other proceedings, and ultimately irrelevant.[179] Apparently, what these rural cable companies fear most is that

[179] ACA Petition at 2, 13-20.

due to the efficiencies of the proposed merger, New EchoStar will be able to bring more services to rural America at lower prices. It is this threat of enhanced competition from DBS that they believe will make it more difficult to maintain and expand their customer base.[180]

First, as the cable industry has repeatedly pointed out in the broadband and open access proceedings, rural cable operators can incorporate digital upgrades at an affordable cost, and have increasingly been doing so.[181] Using such technological innovations as the much touted "Headend in the Sky," small analog cable companies unable or unwilling to invest in new facilities can expand their channel capacity to compete with other MVPD providers. Indeed, in its comments to the Commission in the open access proceeding, the American Cable Association asserts that its "ACA Cable Modem Survey shows members are making substantial progress in deploying cable modem service" and that

> [t]he efforts of ACA members are providing hundreds of thousands of consumers the option of high-speed cable modem service in smaller markets. The number of homes passed by ACA members surveyed should exceed 1.7 million within 24 months. Other facilities-based providers have chosen not to invest in these markets. In this way, ACA members deliver a choice of broadband Internet access where none would otherwise exist . . . Emerging

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[180] ACA Petition at 14-23.

[181] *See* Comments of the American Cable Association, CS Docket No. 00-30, at 5-8 (Apr. 25, 2000) (describing progress by ACA members, including Mediacom Communications Corporation, Galaxy Cablevision, Pine Tree Cablevision and Rural Route Video in providing cable modem service to small markets.)

> competition from satellite delivered Internet access should add to consumer choice in even the smallest markets.[182]

And just this past month, NCTA and several smaller rural cable operators lobbied the Commission on their digital upgrades "seeking to demonstrate to policy-makers that cable TV companies were rolling out broadband services in markets outside major metropolitan areas."[183] NCTA's president and CEO is quoted as follows:

> Cable operators – even those serving midsize and rural markets – are widely delivering on the deployment of high-speed Internet service and other broadband services.[184]

Second, even if a particular cable operator were to discontinue operations, the cable plant would remain available for use and would likely be used by a successor entity that could run it more efficiently and avail itself of the decreasing cost of digital upgrades. The possibility of harm to a particular competitor does not constitute the type of harm to competition that the Commission is called upon to evaluate.

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[182] *See* Petition to Deny of the American Cable Association, ET Docket No. 00-185, at 12 (Dec. 1, 2000).

[183] See Telecommunications Reports, "NCTA Touts Cable Modem Deployment in Rural Areas," (Feb. 4, 2002). *See also Ex Parte* Letters from Lisa A. Schoenthaler, NCTA Senior Director, Office of Rural/Small Systems and Association Affairs to William Caton, Acting Secretary, Federal Communications Commission (Feb. 8, 2002).

[184] *Id.*