More Thoughts on the Road to Monopoly

It has been six months since that now famous weekend in late October over which General Motors Corp. and Hughes Electronics Corp. shocked virtually everyone and signed an agreement to sell Hughes and its DirecTv unit to Charlie Ergen's EchoStar Communications Corp. instead of Rupert Murdoch's News Corp.

Since then, much has been said and written about whether combining EchoStar and DirecTv into the nation's only mainstream DBS service would be good for competition, and thus for American TV consumers. The political and public relations battle has drawn an enormous amount of attention, and is now one of the most visible such fights in Washington—where EchoStar, Hughes, and their opponents have hired a small legion of lobbyists, lawyers, and others to do their bidding.

In these pages in the week following the EchoStar-Hughes announcement, the proprietor of this space argued that the marriage of the nation's only two DBS services would create a satellite TV monopoly that would represent the single biggest setback to competition in the video marketplace in the past 20 years, and lead to significantly higher prices for satellite and cable consumers in the immediate future (See *Satellite Business News*, Nov. 7, 2002).

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Nothing EchoStar and Hughes, or anyone else, have said or done over the past 180 days have changed that view one iota. Indeed, the public debate over the EchoStar-Hughes deal has only reinforced that conviction.

To truly understand why, it is important to carefully analyze the main points EchoStar and Hughes have employed to make their case for approving the merger, and to extract the realities from the hype.

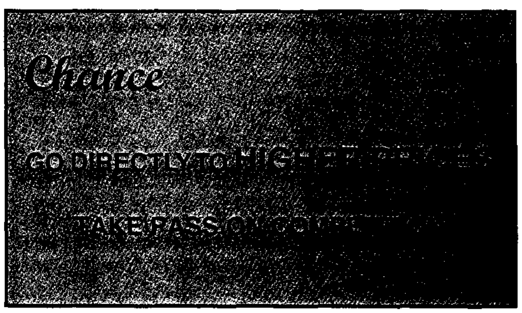
During these past six months, EchoStar and Hughes, and those who are opposing the transaction, have had three Congressional hearings, two rounds of comments at the Federal Communications Commission (FCC), and dozens and dozens of press releases, letters, and events to propound their views. Inasmuch, the EchoStar and Hughes' arguments boil down to a few core issues:

- That EchoStar and DirecTv, as separate companies, were not viable competitors to cable TV and that the only way to provide true competition to cable is for there to be one big satellite TV company going head to head with the cable provider in each community.
- That consumers in rural areas, who would be losing the ability to choose between EchoStar and DirecTv, and thus have only one option for multichannel TV, would be protected by a so-called national pricing plan that would have them paying the same subscription prices as urban and suburban customers.
- That the creation of this satellite TV goliath is the only way that satellite TV will be able to sell local TV stations via satellite to dish owners in rural TV markets.
- That the combined EchoStar-Hughes will be the only company in a position to offer two-way Internet services via satellite.

In essence, since EchoStar and Hughes have to find some argument to counter the most obvious result if their merger is approved—the creation of a DBS monopoly and a dramatic reduction in competition—they have settled on marketplace blackmail: All the things that will never happen if they are not allowed to become a monopoly. It is the "gun to the head" approach, particularly when one of EchoStar and Hughes' other tactics is figured in. Almost since the deal was announced, the companies have launched a quiet whispering campaign in Washington that basically says DirecTv will die if it is not absorbed by EchoStar, or, worse yet, Murdoch may gain control of DirecTv if the Hughes-EchoStar deal is blocked. They have tried to make Murdoch the villain, to not only foster antagonism against Murdoch, who is not well liked in some quarters, but to eliminate Murdoch as someone who can pick up the pieces if the deal is blocked.

Perhaps, then, EchoStar is holding itself out as the "lesser of two evils."

News Corp. is, rather obviously, lobbying to stop the EchoStar-Hughes deal in hopes of getting another shot at buying DirecTv. That is not a tactic all that unfamiliar to EchoStar, as witnessed by its activities during the 110-degree DBS orbital auction debate and Primestar-Murdoch episodes. And as has been repeatedly stated by the proprietor of this space, Murdoch's offer for Hughes and DirecTv was not the greatest in history. It had problems. But it would have left the nation with competing DBS services, and thus far more effective competition to cable. And above all else, that is the best option for American consumers. Any alternative to the formation of a DBS monopoly has to be preferable, and it is not Washington's responsibility to protect General Motors and Hughes shareholders from the mistakes of management. Murdoch or Liberty Media's John Malone would be great owners for DirecTv. But they are not the only other possibilities, and the benefits of keeping DirecTv and EchoStar from merging into a monopoly far outweigh anything else.



That said, a point-by-point examination of the EchoStar-Hughes political talking points follows:

- Perhaps the biggest fallacy advanced by EchoStar and Hughes is the very idea that neither DirecTv or EchoStar have provided much competition to cable as separate entities, are strong companies by themselves, and need to merge to battle cable.

Could anything be farther from the truth? Could anything so contradict both companies' repeated statements over the years?

Were EchoStar and Hughes portraying an accurate picture on this point, both would have had to have made repeated false statements to the Securities and Exchange Commission (SEC), the courts, and Congress over the years time and time again. Along the same lines, Hughes lawyers, in particular, have completely misrepresented the now 6-year and often hostile fight between DirecTv and EchoStar in the marketplace. Even Wall Street analysts, not the most discerning or knowledgeable lot, had to laugh when Hughes' lawyers tried to suggest that both companies were never really focused on each other but each on cable.

If that was the case, the price of DBS systems would still be $699. If that were the case, EchoStar would have never filed an antitrust lawsuit against irecTv. If that were the cas , EchoStar and Hughes would not have publicly excoriated each other so many times in the past six years. It is simply an abject falsehood to state that DirecTv and EchoStar have not been arch enemies, have not passionately competed with each other, and were not more than holding their own against cable.

Just ask anyone in the cable business.

Just look back at the number of times EchoStar and DirecTv launched "bounty" programs to steal each other's satellite subscribers, and paid retailers hundreds of dollars to convert a DBS customer to their service.

Then there are the companies' own abundant statements. Both companies' attorneys have often tried to downplay the significance of EchoStar's antitrust lawsuit against DirecTv. They have basically argued that what is filed by lawyers in a federal lawsuit should not be taken all that seriously, that attorneys are advocates for their companies. But statements made by both in the lawsuit are so forceful, so clear cut, and so specific that would not both companies be guilty of some level of perjury if the statements they have made about the lawsuit in the past six months were true?

In a filing in the antitrust case less than nine months before announcing its bid for DirecTv, EchoStar wrote that, "DirecTv and EchoStar react primarily to each other when setting equipment and service prices." Again, that statement was made, under penalty of sanctions or worse, in a federal court filing less than nine months before EchoStar announced a formal bid for Hughes.

DirecTv and Hughes told the court much the same, saying in an earlier filing of their own that they "admit that

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*Monopoly, and its game cards, are property and trademarks of Parker Brothers.

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EchoStar competes with DirecTv to provide multichannel video programming in market."

In its court filing, EchoStar wrote, "Cable television is an imperfect and comparatively weak substitute for DBS." EchoStar also stated that, "If not constrained by EchoStar, DirecTv could raise its prices above the competitive level without experiencing a significant constraint by cable." EchoStar also argued that, "DBS is a separate product market from alternative sources of programming, including cable television."

Even more to the point, was EchoStar submitting false statements to the SEC as recently as one week, yes one week, before finalizing its agreement to buy Hughes? In that SEC filing, EchoStar wrote its antitrust suit "alleges that DirecTv has utilized improper conduct in order to fend off competition" from EchoStar. DirecTv, according to EchoStar, "has acted in violation of federal and state antitrust laws in order to protect DirecTv's marketshare."

Hughes described the antitrust lawsuit to the SEC in a similar way. In a March 6, 2001, filing, it told the SEC the "allegations" leveled by EchoStar against it and the other defendants were that they "have entered into agreements with retailers and program providers and engaged in other conduct that violates the antitrust laws and constitutes unfair competition."

Thus, in order to believe EchoStar and Hughes' current positions, the marketplace would have had to radically and entirely change in the past year, when it obviously has not. And if the companies are allowed to simply ignore what they have told the courts and the federal government so acutely in the recent past, then why should there be any presumption that any company is ever being totally forthright?

Likewise, EchoStar and Hughes' argument in this area illustrates one of the many obvious contradictions in their positions. On one hand, they argue that neither DBS service on its own saw the other as its main competitor, saw cable as the bigger foe, and thus never really reacted to each other (contrary to what everyone else observed and the companies said), but to cable. On the other hand, they now say they must merge into one company to compete with cable. So were they ever competing with cable, or just each other, or some other imaginary foe?

●As virtually anyone in the satellite TV business sadly understands, a combined EchoStar-DirecTv will be crippled for years, some say as long as seven years, trying to integrate the two competing services' complicated, vast, and sometimes unwieldy operations. Operating a DBS service is inherently more complex by a factor of 10 than running a cable system is. Over the past few months, employees from both DBS companies have come to realize that trying to put these two services together—from technical, billing, customer service, broadcast operations, conditional access/security, and management information systems perspectives—is going to be nothing short of a nightmare. Though they cannot say as much, there are growing numbers inside both DBS services who question whether it can be done without essentially starting a whole new company from scratch.

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There has also been much debate about how this transition will impact subscribers to the services.

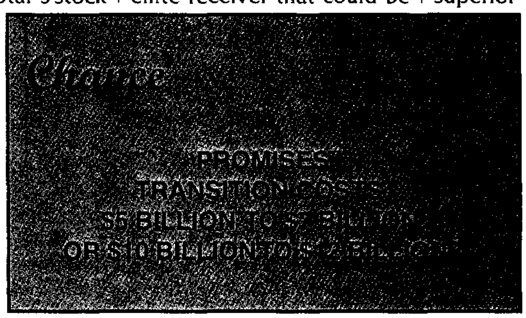
EchoStar and Hughes maintain that they will transition to one technology, but that customers of the service whose technology is abandoned will receive free equipment and installation of the new equipment. This is among the most crucial promises EchoStar and Hughes have made to Washington, and to their subscribers.

But, like many of the other promises the companies have made, it may be impossible for them to live up to it for a variety of reasons. But first and foremost, one of the most important questions to keep asking when judging the veracity of the companies' commitments is: Can EchoStar afford to live up to those promises?

There are many who suggest that EchoStar will not be able to.

At the time the deal was announced, Hughes and EchoStar said the new EchoStar would have a market capitalization of $33 billion and a debt load of $11 billion. In the months hence, that valuation has changed a bit because of Vivendi's investment in EchoStar, some other funding moves, and occasional upticks in stock prices.

Based on current stock prices, and depending on whose equations can be believed (these financial matters often depend on who is crunching the numbers), the new EchoStar will have a market capitalization of $35 to $40 billion and carry a debt load of $10 to $12 billion. That could change in the next few months, and, of course, Hughes and EchoStar's stock price will impact the final market cap to debt ratio.



Some believe that since the new company's projected debt load really has not changed, but has momentarily looked better at points over the last few months because of stock prices. But, like the shares of any company, stock prices are subject to big swings. The share prices of Hughes and EchoStar have fluctuated, and have dropped in the last couple of weeks.

Regardless, what is vital to note is that the new EchoStar will be extremely limited in how it can raise capital for up to two years after it would complete the Hughes purchase.

According to SEC filings, the new company will be prevented from selling additional equity to raise money for two years after the merger would close, and will be limited to returning to the debt market. That will make it very difficult for EchoStar to raise substantial amounts, because it will have to entice investors into buying notes of a company already carrying a mountain of debt and piling on more to raise money.

This is one of the most fundamental ingredients to factor into any appraisal of the EchoStar-Hughes deal. In the post-Enron era, companies that already have large debt loads, particularly those with modest market cap values, are going to face increasing scrutiny in capital markets which are already tight. The fact that DirecTv recently had to restate its subscriber numbers from years past is going to make it even more difficult for EchoStar to raise capital through debt financing.

Even accepting EchoStar's estimates on what it will cost to convert existing customers to new subscribers, build new satellites, pay for the transition, and roll out new services, it will need to spend $5 billion to $7 billion. That is the "promise price tag," by EchoStar's own accounting. Most industry hands say that EchoStar is significantly lowballing those costs, which they put in the $10 billion to $12 billion range. And the cost of the transition is likely increasing by the day. A satellite receiver that could be used for either service, which Hughes and EchoStar said would be distributed six months after their October announcement, appears no where close to hitting the market.

Likewise, there is not a single knowledgable person in the satellite TV businesses who believes EchoStar and Hughes' claims that the merger will produce the $2 billion to $3 billion in "estimated 2005 synergies" the companies trumpeted when they announced their agreement. The use of the word "estimate" aside, that claim gives "smoke and mirrors" a whole new meaning. So much so, that even those inside the companies think the amount of savings through so-called "synergies" will ever materialize. Interesting enough, the companies have mostly stopped talking about "synergies" in recent weeks.

The cost of the conversion is likely one of the reasons that DirecTv has so far refused to agree that its transmission and conditional access systems should be scrapped in favor of EchoStar's. DirecTv's 10.56 million subscribers, and some 15 million to 16 million receivers (counting second sets, commercial establishments, and the like) will be far more expensive to trade out. There is now some thought that some newer DirecTv boxes, such as some of which are Wink-enabled, will not have to be changed because their software can be upgraded over the satellite. But that is only a small fraction of DirecTv units.

EchoStar, on the other hand, can upgrade almost all of its 7.2 million homes, and 10 million boxes, via satellite, though each would require a new security card.

Problem is, there is universal agreement that EchoStar's transmission technology, and its conditional access/security system, are superior to DirecTv's. And while EchoStar's system is compromised, and has suffered some real setbacks in the past eight months, it still is far more robust than DirecTv's. Even more importantly, EchoStar has all but made clear that it will fight tooth and nail to keep its technologies. Some contend EchoStar will never agree to change out its subscribers to DirecTv's system or ever agree to use DirecTv's conditional access/security system, which was developed by a Murdoch-controlled company.

Most hackers say they would prefer DirecTv's conditional access system to live

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on forever, but opinion is divided over whether it would be easier for hackers if they had only one system to focus their attacks on versus two.

Money aside, most agree with EchoStar's view. Because DirecTv has control over what features are included in receivers for its service, hardware manufacturers such as Thomson Consumer Electronics Inc. and others have been prevented from incorporating many new features in DirecTv receivers. As a result, EchoStar's boxes have leapfrogged DirecTv's in many aspects.

And under almost any scenario mentioned by EchoStar and DirecTv, almost all of both firm's subscribers would need some new equipment and/or service call to re-point or replaces their dishes.

So again, the question is whether EchoStar will be able to pay for a conversion without at some point trying to get consumers to pay all or part of the bill? EchoStar has repeatedly said it will keep the costs of the conversion down by allowing customers to "upgrade" boxes to get new features and acquire new capabilities. How many times will EchoStar try to "sell" new equipment, making all kinds of promises, to consumers before it actually gives consumers a free conversion? And given EchoStar's past, what it will call a "conversion" versus an equipment "upgrade"—which it will charge customers for—will make Bill Clinton's famous line, "it depends on what the meaning of the word 'is' is" look credible.

•Many of the same financial realities will also prevent EchoStar from fulfilling one of its other most ballyhooed claims, that it will be the only company able to deliver two-way satellite Internet services. That pledge has been at the heart of EchoStar's wooing of rural America and the lawmakers who represent rural constituents.

Putting aside the pomposity and hyperbole of that claim, here again, the amount of money EchoStar would need to achieve that goal make it virtually impossible to understand how it can deliver. In Congressional testimony on December 4, 2001, EchoStar estimated that it could take at least $1 billion to develop a two-way satellite Internet service. Some argue that projection is low to complete the construction and launch of enough Ka-band satellites to make a two-way satellite data service a viable national competitor.

To date, Hughes has invested around $1 billion in its planned satellite data service, called Spaceway. EchoStar has spent considerably less to develop its own service. So it would take another $3 billion to $4 billion to deliver the satellite broadband services according to EchoStar and Hughes' own estimates. Add a couple of more billion dollars in the real world, where these types of services always cost more than initial cost projections.

It would be difficult for any company to raise that type of money for any new, unproven service in today's economy and market. How tough will it be for a company being weighed down by a huge pile of debt, and restricted from raising money through certain means, to do so? EchoStar and Hughes may have trouble launching such services on their own. They may need to look to other companies to participate. But turning to each other will make it all but hopeless financially.

EchoStar points to the problems other companies such as StarBand, WildBlue, Astrolink, and others, have had in developing such services. Those companies have struggled, but in the case of StarBand and WildBlue, corporate politics, much of which was engineered by EchoStar—which owns a stake in both—were the main reasons for the difficulties.

Unincumbered by debt and distractions from attempting to put two competing companies together, there may be other corporations in a far stronger position to deploy satellite Internet services on a national basis. Liberty Media's Malone is trying to do just that, and as he said a few months ago, if there is a market for two-way satellite data services, there will many companies eager to invest the capital to develop them.

In fact, due to the financial and operational burdens that will challenge the new EchoStar, it could be argued that EchoStar may be in the worst position to try and roll out a new generation of Ka-band two-way Internet satellite services.

•The matter of how rural America will be impacted by a potential EchoStar-DirecTv combination has been among the hottest topics of debate these past six months.

Any way this is viewed, rural Americans will lose. Big time.

Above all else, the elimination of competition resulting from having only one choice for satellite TV will hurt rural consumers more than any others. Not only are many rural Americans without a cable TV option at all, but those rural areas with cable TV are often the oldest, most antiquated systems with the fewest channels.

> ## Community Chest
> ### RURAL AMERICA
> **"Any way this [merger] is viewed, rural Americans will lose. Big time."**

Yet again EchoStar's own words in a filing in the antitrust lawsuit sums it up best. "Millions of potential DBS customers also live in areas that do not have access to cable," EchoStar wrote. "For these millions of customers and potential customers, if there is no competition between [DirecTv] and [EchoStar], there is no competition at all."

To counter this, EchoStar says it will not charge rural consumers any more for programming than subscribers in other areas under a self-described "national pricing" plan. That sounds good, but few believe it is remotely workable.

EchoStar itself has cast a shadow over its "national pricing" idea by also saying it would have to be allowed to "have the ability to respond" in individual markets when the cable operator offers a special promotion. It is not hard to envision cable operators intentionally crafting such promotions with the sole goal of baiting EchoStar to react. If EchoStar bites, as it probably would, the cable operator will immediately claim that EchoStar is violating its own national pricing pledge.

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Indeed, were there only one cable operator in each market competing with the sole DBS service, these types of promotion squabbles would likely be the only fleeting competition there is. Imagine that. Price promotion and competition would be giving way to political price baiting. The minute the political rhetoric died down, the promotions would head for the hills and the lower prices vanish into the heavens.

After unprecedented opposition from rural lawmakers surfaced in the months after the Oct. 29 merger announcement, EchoStar and Hughes realized they were losing the political battle, and the rural question was among the main reasons why. Since having only one real option for multichannel video service in rural America is not a great selling point for any potential deal, the DBS firms made what at the time was widely viewed to be a very shrewd political hail-mary. During a Feb. 26 press event, they announced that if they were allowed to consolidate, they would begin the process of distributing local TV stations in every place in the nation some two years after the merger closed.

At the time, the murkiness of the timeline offered aside, many thought the announcement would quell much of the rural opposition and as a result greatly improve the companies' chances.

For the most part, that has not happened. For the most part, the announcement has produced very little political benefit for EchoStar and Hughes.

Many thought the idea made no economic sense to begin with. According to Nielsen Media, the top 100 TV markets in the nation account for some 86 percent of all U.S. television homes.

Since it is now clear that EchoStar and DirecTv could each serve those 100 markets with local stations were the merger not approved, one of the main justifications for their merger into a monopoly is providing local TV stations via satellite to about 14 percent of American TV homes.

While few assert that the concerns of rural Americans should be dismissed or ignored, many also argue that it would be unfair for 86 percent of American homes to be forced to pay significantly higher prices so that 14 percent have the availability of local TV stations via satellite.

And consumers in all parts of the nation would pay higher prices. The lack of competition would not only lead to skyrocketing prices, but the amount of money it would cost to provide local stations in the rural markets for limited subscriber revenue would only make it worse. The equation is simple: it basically costs the same amount to uplink a TV station to a satellite for reception in Glendive, Montana, the country's 210th and smallest TV market as it does to uplink a TV station for viewing in New York, the nation's biggest TV market.

There are 7.3 million TV homes in the New York market for satellite TV services to market to, according to Nielsen.

In Glendive, Nielsen statistics indicate, there are 3,900 TV households.

The fundamental financial formula of operating satellites and fundamental economic realities dictate that the viewers in New York will have to help pay the bill for those in Glendive. And Americans in both places, in all markets,

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will end up with much higher bills. There is no escaping that.

National pricing, even if it came to pass, does not mean low pricing.

Once again, it must be emphasized that no one favors shortchanging rural America. But a far better way must be found to help defray the costs of providing local channels via satellite, and other new services, to rural homes than EchoStar and Hughes have proposed. Many other companies have to be part of the solution, many other ideas have to be explored. It will not be an easy task, but it may be almost infeasible for a company operating under an immense pile of debt, devoting billions of dollars and taxing its human resources trying to turn two large and complicated companies into one.

For these reasons, the EchoStar and Hughes promises of national pricing, local stations for all, as well as almost everything else the companies say they will deliver, are nothing more than that: promises. And at best, they are political promises, the most fleeting and unenforceable.

Simply stated, EchoStar will become an unregulated, and, more importantly, untouchable monopoly if the government blesses its acquisition of Hughes and DirecTv.

The reasons of why invariably lead to, and set the stage for, a discussion about whether the Department of Justice could craft a consent decree to protect consumers from abuse by the EchoStar monopoly.

EchoStar has publicly said it would agree to a consent decree covering the so-called national pricing and all local channel vows it had made. So what?

What would happen if, and when, EchoStar fails to live up to both? Or any of the other things it has committed to?

For all practical purposes, nothing.

The Justice Department, as a matter of general practice, is loath to enter into consent decrees that require it to either have an ongoing role in seeing that a company is actually doing what it agreed to or one that requires a company to spend money to build something.

It almost always prefers what are known as structural remedies, which involve one-time moves by a company, such as the divesture of certain assets or facilities, that allow it to find that a merger would not hurt the public interest.

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In this case, there are only two such remedies that anyone can think of, and they have no chance of being accepted by EchoStar. Many have proposed that EchoStar be forced to sell one of the full-CONUS DBS orbital slots it would own after the deal closes, the only three such slots over America.

EchoStar has already indicated that is the proverbial non-starter. And in this case, it is easy to see why. Spending $26 billion to buy DirecTv if the full-CONUS orbital slot DirecTv owns is not part of the deal could not be justified under any scenario. And even if EchoStar would agree, few experienced industry executives think a new DBS service could be launched from scratch, and provide any real competition to EchoStar, via one DBS orbital slot.

The other idea, mostly floated by the rural co-ops, would mandate that EchoStar essentially become a facilities based wholesale service provider to a host of distributors. Almost like the "video dialtone" service once envisioned by telephone companies, a concept that was flushed down a multi-billion buck drain.

EchoStar will never agree to such a provision for similar reasons. Similarly, it would do little to promote competition and instead lead to marketplace confusion. The most telling case study of why this idea would be a miserable failure is the Telecommunications Act of 1996. One of the paramount reasons that bill has been considered a flop by most has been the continuing and successful efforts by entrenched local telephone companies to stop competitors from offering a competing local telephone service using the existing phone lines running into homes. EchoStar would have the very same ability to hamper use of its pipeline into satellite homes. It would also make it virtually impossible for EchoStar to control piracy.

So the Justice Department would have few options left but to agree to EchoStar's other terms. Justice, and, perhaps, the Federal Communications Commission as well, would have to keep an eye on EchoStar in perpetuity.

In other words, the government of the United States would have to establish "The Office of EchoStar Oversight."

What would happen if EchoStar, two or three years from now, announces it no longer makes financial sense to uplink all local TV stations, or as it turns out, its technical calculations were incorrect? Or every time someone accuses it of violating the national pricing plan? Or if it never launches a national two-way satellite service? Or it raises its prices year after year?

What will "The Office of EchoStar Oversight" do? Will it employ thousands of federal employees to investigate each and every claim made by consumers, broadcast stations, cable operators, and anyone else? Will it force EchoStar to spend as much money as required, launch as many satellites as needed, and allocate non-existent DBS orbital slots to accommodate all local stations and/or launch two-way data services?

Will it opt to fine EchoStar for failing to meet its commitments, whether they were included in a consent decree or not? How long would that take to enforce in court? How big a fine would it take to get EchoStar to act?

Assuming the government could legally compel EchoStar to spend money, or impose hefty fines for other consent decree breaches, it would wind up pushing an already enormously indebted company toward the financial abyss. Or would EchoStar just raise its subscription prices to pay the fine? And after satellite and cable prices repeatedly go up, will Congress act to impose strict rate regulation on both industries? How big a disaster would that be, even if price controls could be imposed in some rational way, in light of how highly leveraged EchoStar and the nation's largest cable companies are?

Since the government's approval of the EchoStar-Hughes deal would leave EchoStar as America's only mainstream national DBS service, the government would have a vested interest in making sure EchoStar stayed in business. There would be no alternative. There would be no practical enforcement or recourse that would not hurt the very consumers the government wants to protect.

Perhaps five or six years from now, the federal government, realizing the colossal failure, could reverse course and decide to "break up" EchoStar. That would make the break up of the old AT&T look good.

If EchoStar manages to put this Humpty-Dumpty together, it is never ever going to be broken apart. The logistics and cost would be overwhelming and astronomical.

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GET OUT OF COMMITMENTS SCOTT-FREE

"EchoStar will be transformed into the first unregulated, untouchable government-sanctioned monopoly."

Thus, in almost all ways, EchoStar would have the government over a barrel. When someone owes a bank $10 million, the bank "owns" that person. When a person owes a bank $10 billion, that person "owns" the bank.

EchoStar will be transformed into the first unregulated, untouchable, government-sanctioned monopoly.

The Justice Department's Antitrust Division is now run a by a very smart lawyer in Charles James. By all accounts, he is not the political hack that his predecessor, Joel Klein, was. If James signs off on a consent decree based on the unenforceable national pricing or all local stations promises, he will otherwise be signalling approval of the EchoStar-Hughes merger but bowing to his bosses who will want to claim they got concessions from EchoStar.

For in reality, as lawyer after lawyer has argued, there is not a more blatant violation of antitrust law than this merger poses. The Justice Department's own criteria for determining this would seem to be explicitly designed to address the EchoStar-DirecTv merger.

In February, the Justice Department told the FCC that its "view has been that relevant geographic markets for [multichannel video] services are fundamentally local because the only viable choices for a consumer are those firms that offer services directly to the consumers' homes."

Any way the numbers are crunched on this deal, any way the math is done, any way the industry or local market is defined, allowing EchoStar and DirecTv to become one service will dramatically reduce the "viable choices" for every American TV consumer. It will cut those choices from three to two in most areas, and from two to one in other areas. Competition gets cut by 33 percent or 50 percent.

There is just no other way to look at it.

The importance of having two DBS services cannot be overstated. Cable operators, of course, do not compete with each other, so even though six or seven cable companies will soon own almost all cable subscribers, that does not change the number of multichannel choices available to most consumers. And after squandering billions of dollars over the past 15 years, telephone companies and would-be cable overbuilders have either closed up shop or had virtually no impact on the market. The idea that there could be a second wire-line/cable video distribution channel to the home on a large scale basis has been

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pronounced all but dead. And anyone who believes the Internet will become a mass video distribution channel in the next 20 years should just "pass go" and move right to selling aluminum siding or hot tubs.

In reality, the two video options that exist today—satellite and cable—will be the only two for the foreseeable future. Thus, the number of DBS services will be the sole factor in determining how many alternatives consumers will have to their cable system. EchoStar or DirecTv, as individual companies, are the only "third choices."

There is no better example of why having that third choice is essential than the recent spats between the new YES regional sports network in the New York area and Cablevision, that region's dominant cable operator, and the equally nasty but now settled dispute between Disney/ABC and EchoStar over carriage of two of Disney's cable channels.

In most places in the New York area at this moment, the only way to watch the YES Network and the New York Yankees is through DirecTv. EchoStar and Cablevision have not agreed to terms with the channel. Imagine if there was only one cable operator and one satellite service? Both could easily hold out against any channel without fear. The "third choice," whether, in this case, it is DirecTv, EchoStar, or Cablevision, is the "wild card" that affords consumers a modicum of protection against being victim to distributors who would become gatekeepers with more raw market power than ever before.

Some may argue that dynamic could help keep programming prices down. That will never happen. The two distributors will not only be able to dictate terms to programmers, but they will have so much clout that they will be in a position to exercise control over content. As far as prices go, when only a handful of companies—the aforementioned small group of cable operators and EchoStar—have unchallenged market control, the ceiling on what they will charge will creep up every year.

If the EchoStar-DirecTv deal closes, a $60 price tag for a basic package of programming—with no movie channels, sports, or other additions, will become the national average in a couple of years. And it will go up from there.

At that point, consumers can also forget about seeing many new programming services, especially niche or specialized channels. If there are only two video distributors in each local market, and particularly since many cable companies still have limited channel capacity, EchoStar will become the bottleneck of bottlenecks. It will be able to extract any term if wants from any potential new service. As a result, such start-ups will have to pay EchoStar for distribution, or give up equity to EchoStar, or otherwise agree to whatever EchoStar wants. The barriers to entry for any new channel will be virtually unassailable, especially for a service that is trying to introduce a new concept to the market and is not a spin-off of an existing service owned by a major company. Do not for a second think that EchoStar will be unable, for example, to demand that any programming service that wants carriage on its DBS service also pay PanAmSat, the Hughes unit EchoStar would then own, for C-band and/or medium-power Ku-band transponder capacity to distribute such a channel to cable headends and the dwindling C-band system user base.

> **"There is a better chance that the actual Rock of Gibraltar will fly over the United States than there is that SES' plan will fly. The whole idea has to get the 'SkyPix Award' so far for 2002. Maybe it should be called, 'The Crock of Gibraltar.'"**

(On the other hand, do not for a second think that EchoStar would be unwilling to give up PanAmSat as a way to win Justice Department approval. PanAmSat would give EchoStar more leverage over programmers, something Hughes and DirecTv have never figured out how to capitalize on, but not so much that EchoStar would be at all opposed to signing a consent decree whose main provision is jettisoning PanAmSat.)

Along the same lines, some have also suggested that as a monopoly EchoStar would have unilateral and absolute power to dictate terms and conditions to more than just programmers, but hardware manufacturers, component and service suppliers, and retailers. This is referred to as "monopsony" power, which some say is just as important a principal in antitrust law. Regardless of that complexity, many independent satellite dealers call it the end of their businesses. Once the conversion/upgrade is over, many predict that thousands of independent satellite retailers will close up shop. Even with DirecTv and EchoStar in competition, these retailers argue, they now have little leverage over the DBS services. If there was a satellite monopoly, they argue, the only minor leverage they still have—the threat to stop selling one of the services in favor of the other, disappears.

> ## *Community Chest*
>
> **ANTITRUST LAW**
> **"...NOT A MORE BLATANT VIOLATION...THAN THIS MERGER POSES."**

•So the next question then becomes, could there be another wireless competitor to the EchoStar monopoly?

As of today, there are only a few such potential competitors even on the drawing board, and most will do well to even launch no less provide a real competitive option for consumers.

EchoStar claims that even if it buys DirecTv, new competition will develop, including DBS services, in the future. Not so. EchoStar will own all three full-CONUS DBS slots. The only other high-power DBS service even licensed at this point is a group led by Cablevision, the nation's seventh largest cable operator, which has received much attention of late because of its refusal to carry the YES Network in the New York area. The Cablevision group owns 11 frequencies at the half-CONUS 61.5-degree DBS orbital slot, but may get use of two unassigned frequencies there. That slot, as the FCC has noted, cannot serve the entire country, so at best, Cablevision could attempt to launch a regional service. Nor could a DBS service with 11 or 13 frequencies remotely hope to compete with one that owns every full-CONUS DBS frequency and 137 total frequencies. Many on Wall Street have also criticized Cablevision, which is not in the best financial shape in its history at the moment, for even thinking about spending the money which would be needed to even get a DBS satellite into space.

EchoStar also claims that potential terrestrial Ku-band services, like the ones Northpoint Technology Ltd., Pegasus Communications Corp., and Satellite Receivers Ltd. want to launch, could become competitors. That is ridiculous. Even if the legal quagmire that proceeding has become is ever resolved, the amount of spectrum the FCC allocated for each market is not enough to provide true competition. And the whole interference issue that this type of service will pose will never fade away. Terrestrial sharing of the DBS spectrum is, and will always be, one of most lame-brained concepts ever. It will never come to pass on a widespread basis, if at all.

EchoStar also argues that the Ka-band, where companies such as WildBlue, Astrolink, and Pegasus have licenses, could be used for video service in addition to two-way data services. This may be the case in terms of ancillary services, such as providing additional spectrum for local channels, but not as a full-blown competitor to the EchoStar monopoly. For one thing, there are not enough adjacent slots held by any one company that would enable a new service to launch with sufficient channels to challenge the EchoStar monopoly. And, as EchoStar itself told the House Judiciary Committee in written testimony in December, any proposed Ka-band service would be "risky because this band is subject to more rain interference than the Ku-band and may have technical problems."

Then there is the SES Americom announcement last month about using alleged Gibraltar DBS slots for a U.S. business. Could anything be more absurd? There is a better chance that the actual Rock of Gibraltar will fly over the United States than there is that SES' plan will fly. The whole idea has to get the "SkyPix Award" so far for 2002. Maybe it should be called, "The Crock of Gibraltar." The proposal advanced by SES was so light on facts and heavy on fertilizer, that the question has to be asked is SES is doing some sort of favor for EchoStar and Hughes? As noted here before, it costs big companies peanuts to put out press releases, sucker the most gullible in the consumer press, make some noise, and file something at the FCC.

With the chances of getting their deal approved getting longer every day, EchoStar and Hughes need all the help they can get trying to convince Washington that there is the possibility that someone could one day compete with the satellite monopoly they are trying to forge. A year or two from now, this preposterous SES idea will be buried in the file cabinet of the ridiculous, just like SkyPix, the BellSouth DBS plan, and so many others.

The FCC and Justice Department will focus on that reality. As any good antitrust attorney knows, Justice and the Federal Trade Commission have made clear in their own guidelines on mergers that the promise of future and entirely potential competition that is two or more years away cannot be used as a mitigating factor to argue in favor of a merger. The government, according to the guidelines, "generally will consider timely only those committed [new service] alternatives that can be achieved within two years from initial planning to significant market impact."

There just is no way to argue that there are any new potential and speculative

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competitors that could challenge monopoly EchoStar, or the cable industry, in any real way in the next five years at the minimum. This also highlights yet another of Echo-Star-Hughes' inconsistent positions. At the same time they argue they must be allowed to merge into this behemoth monopoly in order to effectively compete, they also claim that these start-ups can provide true competition in the short term. It cannot be both.

From a financial perspective, the barriers to entry, and later to effective competition to the EchoStar monopoly, would almost be insurmountable for a new DBS entry. Since such new entrants, even if they had enough spectrum, would be three or four years away at best, they would be 20 million homes behind EchoStar, and, of course, even more behind the cable industry. Raising the billions it would take to launch an effective competitor to the Echo-Star-cable duopoly would be extremely difficult.

The most critical tests the Justice Department applies to mergers are determining the "timeliness, likelihood, and sufficiency" of any new competitors that might enter a market. Every single thing that Echo-Star and Hughes have tried to shine the spotlight on as proof they will not be monopoly fails all three.

•Perhaps there is no more meaningful way to look at the pending EchoStar purchase of Hughes than to delve into the histories and corporate personalities of both companies.

EchoStar maintains that it could do a better job of the running the combined companies than DirecTv has done running its business this past 10 years. It would be tough to argue with that just by looking at the subscriber numbers. EchoStar is slowly catching up with DirecTv, despite being considerably out spent and outsized, and giving up a 2-year head start to DirecTv. (DirecTv launched on June 17, 1994, EchoStar on March 16, 1996.)

But that is a long way from concluding that EchoStar's style and more dynamic leadership could make the transition into running the nation's only DBS service. The monopoly Echo-Star would control the only three full-CONUS DBS orbital slots. Thus, in addition to ruling on the antitrust and competitive aspects of this proposed transaction, state and federal officials are also obliged to judge whether EchoStar would be the best custodian of that immense chunk of spectrum and able to live up the public trust obligations that custodianship entails.

"But maybe, just maybe, this deal affords government officials a rare opportunity to simultaneously satisfy their political agendas and act in the best interest of American consumers, to prevent the formation of an unregulated, untouchable government monopoly that will, without any doubt, result in far higher prices for satellite and cable subscribers in the near future."

The same overriding leadership and management principles have guided EchoStar for its 20 years. EchoStar operates with the same mentalities it did when the company was founded: a guerilla marketing, push the proverbial legal envelope until it tears, take no prisoner approach. It has worked for EchoStar.

But at some cost. The FCC, in a footnote at the end of its recent decision on EchoStar's practice of utilizing two dishes to meet its must-carry obligations, went so far as to note that, "EchoStar has previously been fined by the commission for rule violations and admonished for its 'disingenuous' behavior and lack of candor." The footnote recounted various "degree[s] of misconduct, lack of voluntary disclosure, and continuing violation[s]" of FCC rules by EchoStar, that the DBS company previously had "willfully violated" federal law and FCC rules, and "failed in its duty of candor" when providing the FCC information.

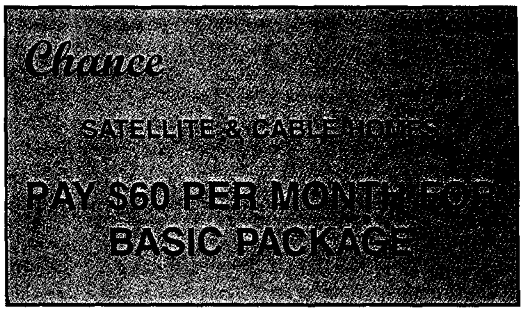
Many viewed the FCC footnote as the commission all but labeling EchoStar as a "bad actor," a quintessential Washington term ascribed to companies rather than using more colloquial terms that many other people would choose.

It was not the first time such charges have been leveled against EchoStar.

In a court filing dated March 13, 2000, Hughes and DirecTv charged, "EchoStar has committed and/or conspired to commit unfair, unlawful and fraudulent business acts and business practices and unfair, deceptive, untrue or misleading advertising in California and throughout the United States that offend established policy and are unethical, oppressive, unscrupulous, and/or substantially injurious to customers."

That perception of EchoStar was only reinforced in many minds only a few weeks ago. Just days after making a very public oath to carry every local TV station in ever market, Echo-Star was part of a Supreme Court appeal of the must-carry rules. That appeal included a footnote in which EchoStar said that if the merger is completed, it "does not intend to carry all channels in every market unless the [must-carry decision] is upheld."

DirecTv, on the other hand, still suffers from the plodding, bureaucratic, conservative heritage of its Hughes parent, which started life as a defense contractor. Throw in the General Motors bureaucracy on top of that, and it is easy to see why DirecTv has so often been left to react to aggressive and decisive marketplace moves by EchoStar rather than the other way around.



DirecTv will never reach its full potential until it is emancipated from Hughes and GM. And DirecTv, which is about to celebrate the eighth anniversary of its service, is badly in need of new leadership and some energetic new management that can both regain the trust and loyalty of rank and file employees and bring some new vitality and perspective to the DirecTv corporate suite.

Though DirecTv could use a dose of EchoStar, and EchoStar could use a dose of DirecTv, that does not mean that combining these two into a national monopoly can work. To the contrary, it will be a disaster in every aspect.

Yet if the government moves quickly and decisively, it can, in fact, result in two stronger DBS companies emerging—and therefore not only provide more choice and competition against cable but against each other.

But time is running short. EchoStar had four main goals when it filed its antitrust lawsuit against Hughes and DirecTv little more than two years ago. It wanted to throw a monkey wrench into what it new was about to become a serious bid by Murdoch to gain control of DirecTv; it wanted to gain distribution through big consumer electronics chains that DirecTv spent millions maintaining its exclusive in (quick question to Hughes' lawyers: why did DirecTv spend millions to keep EchoStar out of the chains if it was not really competing with EchoStar?); it saw the lawsuit as a means to obtain sensitive information on DirecTv through the discovery process; and it hoped to force DirecTv into giving up its DBS exclusive sports packages, most notably the NFL Sunday Ticket package (same question to Hughes' lawyers!).

It is beyond dispute that EchoStar has achieved the first three goals. Some go much further, and now believe Echo-Star is dismantling DirecTv bit by bit, or, at the very minimum, wiping out any advantages DirecTv had in the marketplace. Of course, that is the very reason many believe Echo-Star will not be all that unhappy if the deal is blocked, even if it pays Hughes a $300 million or $600 million break up fee—not that many think EchoStar will ever fork over a nickel of that. Every day that goes by, they suggest, helps EchoStar.

But here again, EchoStar's brilliant manipulation of Hughes and DirecTv could actually wind up helping to promote competition and keep prices. By whittling away at some of DirecTv's most valued advantages, EchoStar is strengthening its ability to compete. If the merger is blocked, and GM and Hughes finally sell DirecTv to another group, which will undoubtedly bring in the new management DirecTv needs, those things DirecTv has lost to EchoStar during the merger review process could be more than offset by the emergence of two even stronger competitors to cable.

And there is no doubt that if their deal is blocked, EchoStar and DirecTv could still find a way to share some spectrum to offer local channels in smaller markets, assuming of course, they can put the companies' egos aside. (That was the lone reason, the singular reason, they failed to reach a spectrum sharing agreement three years ago.) But the government has to act now. Before there is little left of DirecTv to resurrect, before EchoStar knows everything about its rival there is to know.

It is often said that the facts have little to do with the politics of the nation's capitol. But in this case, they appear to be in complete alignment. The antitrust laws seem overwhelmingly on the side of the preventing EchoStar and DirecTv from becoming a monopoly. As for the politics, those opposing the deal represent a wide range of political and social viewpoints: how often do Sens. Trent Lott (R-Miss.) and Orrin Hatch (R-Utah) agree on such a hotly debated issue with The Teamsters Union and Al Sharpton?

The lobbying and mudslinging on this deal will continue for some time. Predicting what will happen is a roll of the dice, because far too often politics overshadows everything else, and the political winds of Washington can change as often as EchoStar's public promises and statements.

But maybe, just maybe, this deal affords government officials a rare opportunity to simultaneously satisfy their political agendas and act in the best interest of American consumers, to prevent the formation of an unregulated, untouchable government monopoly that will, without any doubt, result in far higher prices for satellite and cable subscribers in the near future.

Satellite TV remains the greatest television reception product ever introduced. Just maybe government will act to keep that way.■

—*Bob Scherman*