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October 4, 2002

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW – Room TW-A325
Washington, D.C. 20554

Re: Ex Parte Notice –Consolidated Application of EchoStar Communications Corporation, General Motors Corporation and Hughes Electronics Corporation for Authority to Transfer Control, CS Docket No. 01-348

Dear Ms. Dortch:

In accordance with Section 1.1206 of the Commission's Rules, 47 C.F.R. §1.1206, EchoStar Communications Corporation, Hughes Electronics Corporation and General Motors Corporation, Applicants in the above-referenced merger proceeding, submit this letter to report that representatives of the Applicants met with Legal Advisor Susan Eid of Commissioner Powell's office on October 3, 2002. The Applicants discussed the status of the proceeding, and then gave a presentation focused on the substantial transaction-specific benefits of the proposed merger, the absence of anticompetitive effects, the market forces that dictate Applicants' current nationwide pricing practices and Applicants' ongoing commitment to national pricing post merger. The main discussion of these points was led by Applicants' economic experts, and a copy of the presentation materials distributed at the meeting, which contains the specific points discussed, is attached.

An original and one copy of this *ex parte* notice (and two copies of the attachment) are being filed with the Commission. If you have questions concerning this notice, please do not hesitate to contact the undersigned.

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Respectfully submitted,

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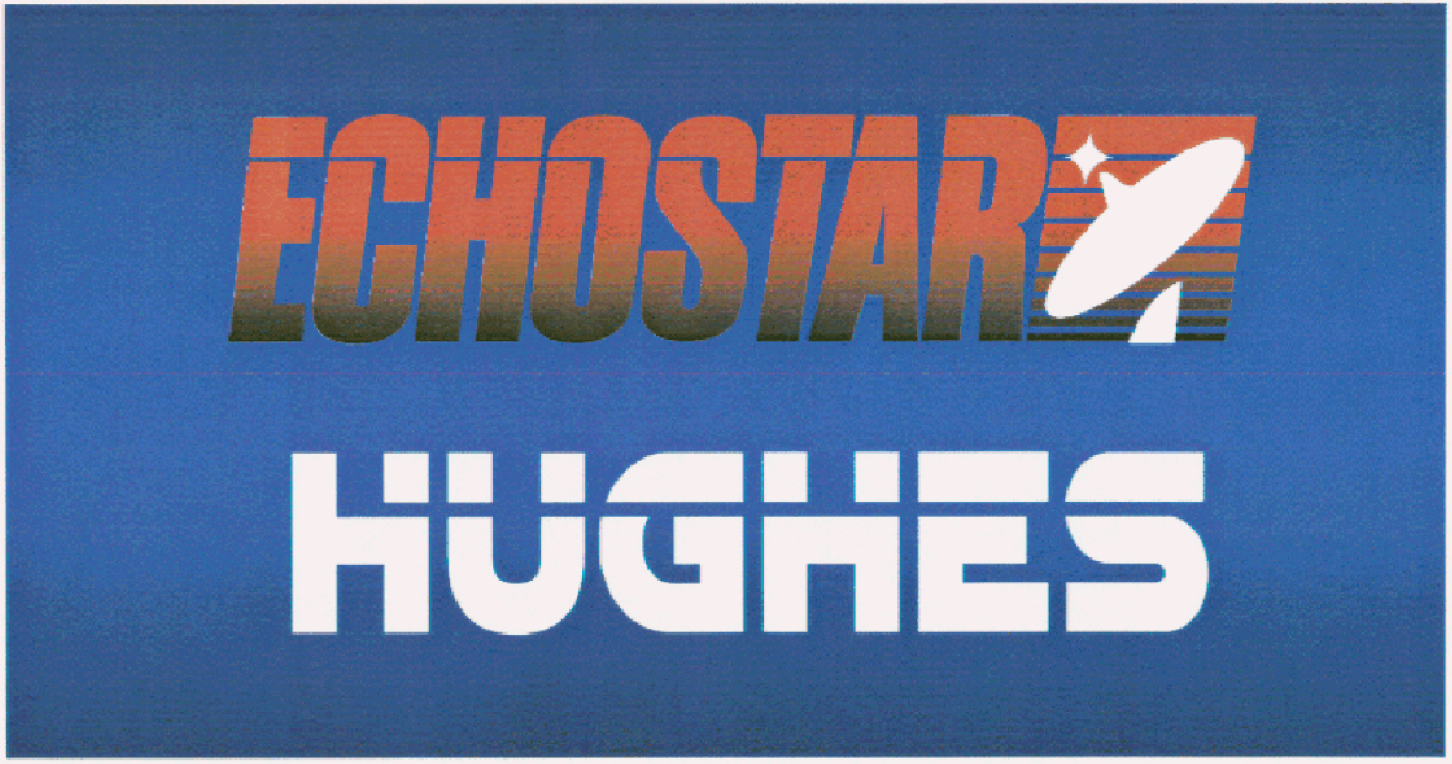
Presentation to the

Federal Communications Commission

October 3, 2002



Reasons for the Merger

- Free Up Scarce Spectrum, Allowing "Local-into-Local" Satellite Service to All DMAs, 12 High Definition Channels, Near Video on Demand and Other Services
- Allow the First True Residential Broadband Service by Satellite
- Create Effective Competition with Dominant Cable Providers – Curb Soaring Cable Rates
- Result in Consumer Benefits Significantly Greater than $1 Billion a Year

Only Accomplished via a Successful Merger

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Proceedings to Date

- Over the last 9 months we have provided a vast amount of legal, engineering and economic information in support of the merger:
  - Filings in the Merger Application Proceeding
  - Filings in the New EchoStar 1 Satellite Proceeding
  - Interrogatory Responses and Document Productions
  - Series of Seven In-Person Briefings/Meetings
  - Merger Simulation Model, Synergies Model, Local-Into-Local Models, Broadband Models
  - CEO Presentations by Charlie Ergen and Eddy Hartenstein

This meeting is intended to provide the "economic foundation" for the merger

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ANALYSIS OF THE ECHOSTAR-HUGHES MERGER: COMPETITIVE EFFECTS AND NATIONAL PRICING

Dr. Andrew Joskow
National Economic Research Associates

Dr. Robert Willig
Consultants in Industry Economics

October 3, 2002

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Key Points of Analysis

- Pre-Merger State of Competition: Cable Providers Are Each DBS Firm's Closest Competitors
- Spectrum Benefits and Other Merger-Specific Efficiencies, Including Local Broadcast Stations and Residential Broadband Service to All Americans, Promote the Public Interest
- Competitive Effects Analysis: Post-Merger Economic Simulation Show Consumer Welfare Benefits Significantly In Excess of $1 Billion Annually
- National Pricing: A Post-Merger Price Increase Based on Customer Class Or Location Is Not a Plausible Outcome

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Key Point #1: Cable Providers Are Each Firm's Closest Competitors

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Key Point #1: Cable Providers Are Each Firm's Closest Competitors (continued)

- Additional data show that cable providers are each firm's closest competitors. That is, the DBS firms are primarily constrained by cable
  - *Data on New Subscribers:* [ ] of new DIRECTV subscribers are former (or current) cable subscribers, while fewer than [ ] are former EchoStar subscribers.
  - *Data on Promotions:* Promotions targeted at DIRECTV have gained EchoStar only [ ] of the subscribers gained by EchoStar promotions targeted at cable

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Key Point #2: Merger-Specific Efficiencies Are Significant

- The merger will generate new and expanded DBS product offerings. The key efficiencies are the freeing up of spectrum and scale economies. New EchoStar will provide:
  - All DMAs With Local-into-Local Service (instead of about 70 DMAs)
  - More High-Definition Television Channels
  - Residential Broadband Service Available to All Americans
  - More Programming Diversity (e.g., Special Interest)
  - More Pay-Per-View or Near Video-on-Demand Capability
  - More Interactive Services
- The merger will also lower marginal costs
  - Lower Programming Costs
  - Lower Hardware and Installation Costs Per New DBS Subscriber Due to Standardization and Economies of Scale

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Key Point #2: Merger-Specific Efficiencies Will Force Competitive Response by Cable Providers

- We find that the introduction of local-into-local service by DBS providers produces important benefits:
  - ***Subscriber Lift:*** We find that the introduction of local service by DBS has raised EchoStar's local penetration by [ ] ***percentage points*** and DIRECTV's local penetration by [ ] ***percentage points*** (after three years)
  - ***Lower Cable Prices:*** We find that the introduction of local service by DBS lowers the average expanded basic cable price by roughly ***$1.03 per month*** in the first year and ***$1.57 per month*** in the second year following introduction of local-into-local
  - ***Consumer Welfare Benefits:*** As a result of subscriber lift and lower cable prices, the merger will produce additional consumer welfare benefits of between [ ] ***per year*** from the introduction of local service in all 210 DMAs

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Key Point #2: Merger-Specific Efficiencies Will Force Competitive Response by Cable Providers (continued)

- DBS has forced cable providers to expand capacity/quality and HDTV product offerings
  - For example, National Cable and Telecommunications Association (NCTA) President and CEO Robert Sachs: "Being digital from the start, and having the advantage of substantially greater channel capacity, DBS spurred cable operators to replace hundreds of thousands of miles of coaxial cable with fiber optics so that they too could offer consumers hundreds of channels of digital video and audio services."
- Looking to the future, the merger may help to "jump start" the nascent market for HDTV. New EchoStar's offering of 12 (or more) HD channels will likely spur cable operators to increase their planned offerings of roughly 5 HD channels

Key Point #3: Competitive Effects Analysis: Post-Merger Simulation Estimates Significant Consumer Benefits

- We use a "nested logit demand system" to simulate the impact of the merger on prices and consumer welfare
- We calibrate the model to the data on diversion between DIRECTV and EchoStar
- We include the consumer benefits resulting from subscriber lift and lower cable prices following the introduction of local service

- The two main findings of the simulation are:
  - If we incorporate the merger-specific marginal cost savings of the merger, we estimate that prices of both DBS *and* cable will fall.
  - The combination of lower DBS and cable prices – along with the introduction of local service in DMAs 71-210 – will produce estimated consumer welfare benefits in excess of $1 billion

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Key Point #3: Competitive Effects Analysis: Post-Merger Simulation Estimates Significant Consumer Benefits

- The estimate of consumer welfare benefits of greater than $1 billion per year is conservative and does not include other benefits:
  - Based on the parties' projections of incremental subscribers from new services, the merger simulation model suggests that an additional $663 million in consumer welfare benefits will result the introduction of additional HDTV channels, more programming diversity, a competitive broadband service, and more interactive and VOD/PPV services
  - Additional consumer benefits, which are more difficult to quantify, will likely result from cable's competitive response to New EchoStar's new product offerings. As noted above, the historical evidence suggests that cable has responded to the introduction of an improved DBS product offering (e.g., the impact of local service, HD channels, etc.)
  - Additional consumer benefits will flow from the availability to all Americans of residential broadband service

Key Point #3: Competitive Effects Analysis: Post-Merger Simulation Estimates Significant Consumer Benefits

- Given the structure of the market, there is no valid concern that New EchoStar will coordinate its prices with cable providers
  - The data show that the market is too diverse for coordination: There is significant variation in expanded basic price levels *and* expanded basic price changes between cable MSOs *and* within cable MSOs (even within the same state)
- New EchoStar's incentives would be inconsistent with coordination
  - New EchoStar faces a powerful incentive to grow subscribership.
  - New EchoStar will need to attract new subscribers rapidly as digital cable and broadband bundles spread and make cable's installed base "stickier"

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Key Point #4: A Post-Merger Price Increase Based On Customer Class Or Location Is NOT a Plausible Outcome

- Both EchoStar and DIRECTV price their programming service on a national basis
- The commitment to a single national price serves to reinforce the current practice

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Key Point #4: A Post-Merger Price Increase Based On Customer Class Or Location Is NOT a Plausible Outcome

A market test exists TODAY for whether EchoStar will take advantage of apparent opportunities to price discriminate by location on programming prices

- EchoStar does not charge higher prices in areas where it competes with Pegasus even though Pegasus charges $4.50 more per month for the equivalent package
- Despite the higher price set by a supposedly rural provider, EchoStar has kept its programming price national and uniform
- Also, EchoStar and DIRECTV do not provide different commissions to retailers based on location

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Key Point #4: A Post-Merger Price Increase Based On Customer Class Or Location Is NOT a Plausible Outcome

- EchoStar customers gained through local promotions in the past have represented an exceedingly small share of the subscribers gained by EchoStar
- EchoStar and DIRECTV have not used localized promotions in a strategy to price discriminate

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Key Point #4: A Post-Merger Price Increase Based On Customer Class Or Location Is NOT a Plausible Outcome

TARGETING CONSUMERS WITH NO ACCESS TO CABLE WOULD NOT BE PROFITABLE

It is difficult to identify the class of customers that are non-cabled

- For example, [ ] of people who left DIRECTV and who supposedly (according to the best available public data) live in areas without cable said they were switching to cable

It is difficult to target well-defined areas – even those that appear rural – that are without upgraded (digital) cable systems

- Approximately 80% of housing units in the bottom twenty DMAs are passed by digital cable

Without being able to accurately screen for those who do not have a cable alternative, price discrimination by NewEchoStar would lead to a loss of profitable customers that DO have a cable alternative

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Key Point #4: A Post-Merger Price Increase Based On Customer Class Or Location Is NOT a Plausible Outcome

RETAILERS WOULD NOT BE A CONDUIT FOR DISCRIMINATION

- Use of national retailers – who seek to sell their equipment in competition with cable – provides protection for consumers in seemingly non-cabled areas
- **National retailers** generally offer products at a uniform national price. The ubiquity of these retailers allows areas without cable to benefit from this uniform price
- Survey of **independent retailers** we conducted shows that the upfront DIRECTV equipment and installation price is the same in cabled and non-cabled areas. Competition from cable and national retailers drives consumer prices to equality across cabled and non-cabled regions

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Conclusions

- The merger will generate new and expanded DBS product offerings, such as local-into-local service in all 210 DMAs and more competitive satellite-based broadband service
- The merger will create consumer welfare benefits significantly in excess of $1 billion per year
- The merger will stimulate – rather than stifle – competition in the MVPD market
- New EchoStar has committed to pricing its product nationally, eliminating any residual concern about implausible price discrimination
- The merger is thus in the public interest

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