

states, with over **3** million subscribers, and has a number of other assets, including sports ventures and programming networks. Rainbow Media Group, which operates programming networks including American Movie Classics, Bravo, WE, The Independent Film Channel, and MuchMusic USA, is one of the most important programmers in the United States, and has seen robust growth in both subscribers and revenues.

Indeed, the effectiveness of the Applicants' proposed remedy has been enhanced even further by Cablevision's recently announced sale of Bravo to **NBC**.³⁴ This transaction will afford Cablevision access to as much as \$500 million of new capital (if, as planned, Cablevision monetizes the GE stock it receives from the transaction). That capital may be used to implement its expanded two-slot, full-CONUS DBS system made possible by this remedial proposal.

Moreover, Rainbow has been moving forward with its DBS plan, even without the spectrum and satellites contemplated by this proposal. The original plan was based on a limited number of frequencies with one satellite at one slot without **full** CONUS coverage. The original venture would have entailed almost the same investment in marketing, distribution, CPE development, and other costs as the new proposal, though Rainbow's product offering would have been far less desirable. It would have also faced the same entry paradigm as other MVPD providers, the need to invest in infrastructure and subscriber acquisition that is not likely to turn a profit for several years. Yet, Rainbow was confident that it could finance the venture as originally conceived, and sustain the ongoing investment needed to achieve profitability.

By contrast, Rainbow's offering with this proposal, based on **62** frequencies with multiple satellites and true nationwide service, will be much more compelling than its previous

³⁴ See Cablevision News Release, *NBC To Acquire Bravo From Cablevision Systems Corporation* (Nov. 4, 2002), available at <<http://www.cablevision.com/company/index.html>> (Investor Information, Financial News).

proposal, yet with relatively low additional sunk costs (the cost of the spectrum and the satellite purchase/leases). With the channel capacity from EchoStar that will enable it to serve the entire United States, Rainbow will readily be able to attract financing and financial partners willing to finance the venture.

3. Entry will be sufficient to deter the potential exercise of market power.

Entry must be sufficient to return market prices to their premerger levels in response to the exercise of market power by the incumbents.

a. Rainbow has no constraint on its ability to serve any potential subscriber.

Here, entry will be sufficient because there is no constraint on Rainbow's capacity: with the divested capacity, Rainbow will be able to serve essentially every household in the United States that the current providers can serve,³⁵ and more. As noted above, Rainbow will have a superior ability to serve much of the East, particularly the Northeast. Rainbow will also be able to provide at least the range of offering of one of the two DBS providers today, and in all likelihood much more. Based on its experience in the MVPD industry, Rainbow is well positioned to obtain other necessary inputs that it needs in order to provide DBS service quickly and on terms that, for the most part, are equal to or better than the current DBS providers. Moreover, Rainbow's ability to attract subscribers would be further enhanced by New EchoStar giving subscribers in need of an upgrade after the merger the option of switching to Rainbow.

³⁵ Once it launches a new satellite at 148° W.L., Rainbow's ability to deliver signals to Alaska and Hawaii will be superior to the current capability of DIRECTV, which must serve these states from the 101° W.L. slot.

b. Rainbow will be able to effectively distribute its products.

Rainbow will not face several barriers that DIRECTV and/or EchoStar faced when they entered. For example, EchoStar was not able to obtain distribution through many major national and regional consumer electronics retailers. Nevertheless, even without access to these important distribution outlets, EchoStar was able to grow against the incumbent MVPD providers. Rainbow will likely have additional channels beyond the traditional DBS retailers available to it.

Rainbow's relationship with Motorola will also help it establish effective distribution channels. Motorola is one of the largest manufacturers and distributors of consumer electronic devices in the United States, and has close relationships with many of the retail chains that also distribute DBS products. Motorola will be able to use those relationships, just as Thomson, Sony, JVC, and others did with DIRECTV and EchoStar, to secure effective distribution for Rainbow's DBS products. This is particularly true if, as is likely, Motorola/Rainbow develop an innovative, value-added receiver that they can differentiate from existing boxes.

In addition to the retail consumer electronics chains, Motorola has relationships with any number of other effective distribution channels for its products. For example, Motorola is also a manufacturer of C-band satellite equipment, such as the 4DTV digital receiver, and thus has relationships with many rural retailers who are focused on satellites. Also, Motorola's distribution network for its mobile telephones is one of the broadest consumer electronics retail distribution channels in the nation. Many of these retailers do not currently carry DBS products, but they could. Moreover, they are likely eager to participate in the DBS revenue stream, and may require substantially less in the way of subsidies for selling the product than the large

consumer electronics retailers. These are only some of the additional opportunities for distribution available to Rainbow. In addition, Rainbow may license other manufacturers to build and distribute its products. Finally, Rainbow and Cablevision can call upon their experience and expertise in direct sales to reduce subscriber acquisition costs (“SAC”).

Thus, Rainbow should be able to obtain efficient distribution. If Rainbow is able to offer differentiated programming, particularly High Definition local sports programming, it will likely end up in a more favorable position with many retailers than the incumbents.

c. Rainbow will be able to obtain programming on favorable terms.

Cablevision is already an established MSO with programming contracts that are likely more favorable than those of EchoStar or Hughes. Moreover, Cablevision’s presence in New York, the most important media market in the nation for any cable-programming provider, gives it negotiating leverage far beyond its sheer subscriber counts. In addition, Cablevision has substantial programming interests of its own with substantial incentives to establish a distribution network outside its own cable footprint. In particular, Rainbow/Cablevision and their affiliates have ownership interests in regional sports programming in key markets such as New York, New England, Ohio, Chicago, Florida, and the San Francisco Bay Area. Rainbow clearly intends to use these and other unique assets to develop and provide regional programming, including sports programming, an area where it has had particular expertise and success, via DBS throughout the country. Finally, as a programmer, Cablevision’s Rainbow Media Group will be able to use Rainbow’s “ad avails” to promote its own programming, an important advantage in driving new customers to its system throughout the country.

d. Rainbow will be able to perform installation/billing/customer service efficiently and effectively.

As an experienced MSO, Cablevision has substantial experience running its own installation, customer service and billing operations, and supervising third party providers of such services. Rainbow can efficiently utilize these existing resources and, when necessary, outsource these services to third-party providers.³⁶ Rainbow has available any number of qualified third party installers across the nation, including retailers and firms who install cable systems, DSL, telephone equipment and alarm services. These firms compete and there is no reason to believe that Rainbow will not be able to negotiate reasonable prices for this service. Competition among retailers and installers will ensure that Rainbow receives acceptable price, service and quality levels from these firms.

e. Competition will not be significantly reduced in Cablevision franchise cable areas.

One potential concern raised about a divestiture of spectrum to Rainbow is the fact that Cablevision provides cable service in **39** cable franchise areas and serves roughly three million subscribers.³⁷ Since affiliated companies will provide DBS and cable services, there is a hypothetical concern that there could be anticompetitive effects in Cablevision's franchise areas, either through a unilateral increase in Cablevision's price or enhanced ability to coordinate pricing.

³⁶ Many, if not most, MVPD providers outsource some or all of their billing, customer service, and installation services. For example, EchoStar outsources some, and DIRECTV outsources substantially all, of its installation services. DIRECTV outsources some of its customer service call centers, and both companies outsource portions of their billing services.

³⁷ According to the 2002 Warren data, Rainbow had **2.9** million subscribers. According to the National Cable and Telecommunications Association, Rainbow had 3.0 million subscribers in March 2002. *See* <http://www.ncta.com>.

In fact, consumers who live in Cablevision's franchise areas will *not* suffer any significant loss of competition because (1) the vast majority of Cablevision subscribers have competitive alternatives beyond Cablevision and New EchoStar and (2) it would be impractical and unprofitable to price discriminate against the small number of consumers without competitive alternatives, particularly since Cablevision's franchises in the New York area are adjacent to those of a very powerful cable operator, and New EchoStar would have to engage in glaring discrimination literally between one city block and the next.

Because of the mostly urban nature of its subscriber base, Cablevision faces substantial competition in its cable franchise areas. Overbuilders have historically played an important role in constraining the prices of cable providers, which is indicative of their effectiveness as competitors in the MVPD market.³⁸ According to the Warren data, overbuilders

³⁸ A dozen academic studies – including four analyses by the Commission – have found that prices in markets with overbuilders are between **8** and **34** percent lower than in markets without them. See Thomas Hazlett and Matthew Spitzer, *Public Policy Toward Cable Television: The Economics of Rate Controls 31 (1997)*. For example, as part of its February 1994 cable rate regulation rulemaking, the Commission used 1992 data on cable prices by area and found that communities with head-to-head competition between cable providers and overbuilders had **16** percent lower cable prices than communities with a monopoly cable operator. See Federal Communications Commission, *In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act – Rate Regulation, Buy-Through Prohibition*, Third Report and Order, MM Docket 92-266 and MM Docket No. 92-262 (adopted February 22, 1994 and released March 30, 1994). See also Jith Jayaratne, *A Note on the Implementation of Cable TV Rate Caps*, 11 Review of Industrial Organization at **823 (1996)**. Similarly, a paper published in the *RAND Journal of Economics* in 1997 concluded that cable prices in areas with overbuilders were **17** to **22** percent lower than areas without them. See William Emmons and Robin Prager, *The Effects of Market Structure and Ownership on Prices and Service Offerings in the U.S. Cable Television Industry*, 28 *RAND Journal of Economics* at 732-50 (Winter 1997). Communities with competition from overbuilders also appear to have higher levels of service that are not fully accounted for in the above-cited literature: The evidence suggests that subscribers in overbuilt areas have more choices of non-broadcast channels and lower installation prices. See Jayaratne, above at **823**; Hazlett and Spitzer, above at **29**; Jennifer Fearing and Charles Lubinsky, *Qualitative Differences in Competitive Cable*

provide service in cable franchise areas covering **69%** of Cablevision's subscribers. Cablevision has frequently acknowledged that it "faces significant competition" from overbuilders, such as RCN, which "provides service throughout much of the New York metropolitan area, and boasts of its 'substantial growth' in the New York market."³⁹

The potential anti-competitive concerns in Cablevision areas are further attenuated by the fact that the National Rural Telecommunications Cooperative ("NRTC) and Pegasus would continue to resell New Echostar's service in cable franchise areas covering **31** percent of Cablevision's subscribers?' Such reselling of New Echostar's service will operate as a competitive constraint on Cablevision's cable service, Rainbow's DBS service, and New EchoStar in Cablevision's cable franchise areas. Indeed, the majority of Cablevision subscribers appear to be in cable franchise areas that are either served by an overbuilder or **NRTC/Pegasus**.⁴¹

Cablevision's cable franchise areas also tend to be in more urban areas, with a significant population living in multiple dwelling units ("MDU"s) or commercial multiple tenant units ("MTU"s). An analysis of Bureau of the Census data on the number of people living in MDUs and MTUs in Cablevision's cable franchise areas shows that that 48 percent of households in Cablevision's cable franchise areas live in MDUs/MTUs, with an estimated nine percent living in MDUs/MTUs with more than 50 units. MDUs/MTUs with more than 50 units **are** often served by Satellite Master Antenna Television ("SMATV") providers – and even if

Markets Prior to Rate Regulation, mimeo (October 1997). Fearing and Lubinsky conclude that installation fees are **16** to **36** percent lower in competitive markets than in monopolistic markets.

³⁹ See Reply Comments of Cablevision Systems Corporation, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Notice of Inquiry, CS Docket No. 01-129, Sept. 5, 2001, at 3-4.

⁴⁰ Analysis of NRTC/Pegasus areas and Warren data.

⁴¹ Analysis of NRTC/Pegasus areas and Warren data.

such MDUs/MTUs are not currently served by SMATV providers, the threat of entry will help to constrain Cablevision's prices in such areas. Cablevision has acknowledged that it "faces significant competition from various providers of SMATV service."⁴²

In sum, the vast majority of Cablevision's subscribers will have at least three independent choices for MVPD service post-merger (counting Cablevision's cable service and Rainbow's DBS service as only one choice), and a subset of these subscribers will have at least four choices. Only an estimated **16 percent** (fewer than 500,000) of Cablevision's subscribers would face an option of only Cablevision (cable), Rainbow (DBS), or New EchoStar (DBS).⁴³

Any potential competitive harm to these consumers would be further attenuated by the potential entry of overbuilders in neighboring communities. The Warren data suggest that nine percent of Cablevision subscribers live in cable franchise areas that are adjacent to cable franchise areas in which overbuilders are present." To the extent that Cablevision fears the entry of an overbuilder in a neighboring community, Cablevision may respond to the *potential* entry by keeping prices low and service quality high. Such a response would be consistent with recent experience in Fairfax County, Virginia. As the FCC noted, RCN "contends that in anticipation of its entry in Fairfax County, a suburb of Washington, D.C., the incumbent Cox announced an upgrade of its plant."⁴⁵

Finally, Cablevision's franchises in the New York area are generally adjacent to those of AOL/Time Warner. For New EchoStar, the logistical and reputational burdens and

⁴² See Reply Comments of Cablevision Systems Corporation, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Notice of Inquiry, CS Docket No. **01-129**, Sept. **5, 2001**, at **3-4**.

⁴³ Analysis of NRTC/Pegasus areas and Warren data.

⁴⁴ Analysis of NRTC/Pegasus areas and Warren data.

⁴⁵ See Eighth Annual Cable Competition Report ¶ 201.

costs associated with attempting to discriminate between consumers living a few doors from one another would be even more formidable than those that have led each DBS provider to shy away from differential pricing to date. New EchoStar would have little incentive or ability to treat Cablevision subscribers any differently than their neighbors, and any attempt to do so would not be profitable. Thus, MVPD subscribers in Cablevision areas will benefit from the more effective competition that New EchoStar offers, while not losing a significant degree of competition in the MVPD market.

f. Rainbow will protect competition nationally without the need for regulation.

Some have suggested that without a nationwide DBS competitor, the merged company could adopt a strategy of price discrimination that would disadvantage rural subscribers. The proposed divestiture ensures that there will be two DBS firms competing on a nationwide basis. While the Applicants do not believe that geographic price discrimination would be a profitable strategy regardless of the number of competitors,⁴⁶ there is no question that with the proposed divestiture Rainbow will compete on a nationwide basis and serve as a competitive check against attempts to raise prices to non-competitive levels on a local basis. As a facilities-based competitor, Rainbow will protect consumers nationwide without the need for a regulatory decree.

g. Scale disadvantages will not prevent Rainbow from constraining prices to pre-merger levels.

The relevant measure for examining competitive effects is the entrant's ability to add new subscribers in response to non-competitive conditions, not the size of the entrant's

⁴⁶ See Economists' Presentation to FCC Merger Task Force on Competitive Effects (July 2, 2002) at **63-83**; Economists presentation to FCC Commissioners and Legal Advisors on Competitive Effects and National Pricing (September 20, 2002).

installed base. As noted above, under the proposal New EchoStar would provide subscribers in need of an upgrade the option of switching to Rainbow, helping Rainbow overcome the scale disadvantage. Furthermore, the resale rights described above would allow Rainbow too to take advantage of the spectrum efficiency benefits unleashed by the merger.

Rainbow will also have some other important advantages. For example, Rainbow may be the only MVPD provider able to offer High Definition local sports networks with the important major league sports teams in many areas. Such unique and valuable programming content would attract both subscribers and distribution partners who may demand substantially less compensation than is typically demanded today, solely because of the advantages to the partner of being associated with that product (*e.g.*, driving a retailer's sales of HDTV sets). Rainbow may also be able to use its experience to expand its direct sales model more broadly into DBS sales, again reducing SAC. Rainbow can leverage ad avails on its own programming to expand awareness of the product and reduce advertising and marketing costs. As noted above, Rainbow also will have a competitive advantage in many parts of the Northeast where customers will have a superior look angle to Rainbow's satellites at **61.5°W.L.**, and in areas where terrain or other line-of-sight obstructions inhibit the reception of DBS service from the traditional CONUS locations.

Finally, it is safe to conclude that, based on Motorola's past history and abilities, Rainbow's set-top box is likely to be innovative and contain value-added features intended to further differentiate Rainbow's offering from New EchoStar's. In sum, while Rainbow may have certain scale disadvantages, such disadvantages would certainly not prevent Rainbow from constraining New EchoStar to pre-merger prices.

h. Rainbow will not face the same obstacles that EchoStar and DIRECTV faced.

Rainbow will not face the same barriers to DBS acceptance that EchoStar and DIRECTV faced in establishing their product in the marketplace. Rainbow has the benefits of the hundreds of millions of dollars in advertising that DIRECTV and EchoStar have spent in promoting DBS acceptance. Indeed, millions of DBS subscribers have churned from DBS and are potential subscribers if Rainbow can overcome whatever objection (*e.g.*, lack of local or regional programming, price) led them to leave DBS. Rainbow also has a unique opportunity to attack New EchoStar's customers during the transition.

E. The Divestiture Proposal Will Give Rainbow Full-CONUS Coverage.

The Commission has expressed a concern with allowing a single company to control all of the U.S. "full-CONUS DBS orbital locations!" Even if the Commission's concern were not misplaced as a matter of law (*see* below), the divestiture proposal should be enough to dispel it. The divestiture of *both* wing slots as opposed to just one will indisputably endow Rainbow with full-CONUS coverage and make it another full-CONUS provider, and the resale rights over New EchoStar's full-CONUS slots proposed herein would further cement Rainbow's status as a full-CONUS competitor.

IV. THE APPLICANTS' AMENDED MERGER PROPOSAL IS ALL THE MORE AMELIORATIVE BECAUSE THE BENEFITS OF THE MERGER ARE LARGER THAN CREDITED BY THE COMMISSION AND THE COMPETITIVE PROBLEMS ARE LESS SERIOUS

The Applicants believe that this ameliorative proposal is more than sufficient to cure all of the competition concerns identified by the Commission, even assuming the worst-case scenario, *i.e.*, if these concerns are viewed in the least favorable light for the Applicants. This is

⁴⁷ *See, e.g., Hearing Designation Order* at ¶¶ 211,284.

particularly the case where, as here, the benefits of the merger are significantly greater than the Commission has estimated in the *Hearing Designation Order*, and the purported competitive problems are conversely less serious.

A. The Benefits From The Merger Are Larger Than Estimated By The Commission.

As the Commission is well aware, two of the primary public interest benefits of the merger that the Applicants have extensively discussed are: (1) the provision of local-into-local service in all 210 DMAs; and (2) the provision of a viable satellite broadband service nationwide (including in rural areas that have *no* meaningful broadband service today, and no reasonable prospect of obtaining such service in the foreseeable future). As the Applicants have explained, neither of these benefits can reasonably be expected to occur without the spectrum efficiencies and scale effects of the merger. Notably, it is not only the Applicants who support this view; other parties, including consumers groups, agree.⁴⁸ In the *HDO*, however, the Commission downplayed these benefits, either by concluding that they can be achieved without the merger or by minimizing their importance even if achieved. For a number of reasons, not all of which need to be enumerated here, this improper mode of analysis fails to comport with the well-established requirements of the Administrative Procedure Act and the Communications Act

⁴⁸ See e.g., *States Reject EchoStar Takeover of Hughes, DIRECTV*, Warren's Cable Regulation Monitor, Nov. 4, 2002 (quoting Gene Kimmelman, Consumers Union Senior Director - Public Policy, "If the Bush Administration officials had lifted a finger to modify this merger, satellite could have offered the same local programming as cable nationwide... It's hard to figure out how the Justice Department and the FCC think that they are helping consumers by blocking, rather than restructuring, this deal."); *Opposition to EchoStar-DIRECTV Deal Picks Up Steam at DOJ*, Satellite Week, Sept. 9, 2002 (quoting Malcolm Wallop, Frontiers of Freedom Chairman, "The DIRECTV-EchoStar merger is the only way to get high-speed Internet services to rural America."); see also Comments of the United States Internet Industry Association, CS Docket No. 01-348 (Jan. 30, 2002); Comments of the Farm Business Council, CS Docket No. 01-348 (May 7, 2002); Comments of American for Tax Reform, Comments of Frontiers of Freedom, CS Docket No. 01-348 (Feb. 1, 2002).

with respect to reasoned decisionmaking. Far more importantly, however, this flawed framework for analysis may lead the Commission to pass up the once-in-a-generation opportunity to achieve public interest benefits that are both critically important and clearly dependent upon approval of the merger.

The HDO specifically appears to apply a double standard in comparing New Echostar's capabilities with the stand-alone capabilities of each company, resulting in an unreasonable diminution of the former and aggrandizement of the latter. The result of this double standard has been to reduce dramatically the Commission's assessment of the difference that the merger will make – *i.e.* the size of the benefits that it will produce. Furthermore, the Commission appears to have subjected the evidence it considered to much higher standards than it has utilized in other proceedings. Finally, the Commission has overlooked most of the numerous submissions made by the Applicants after July 3, 2002. This is especially prejudicial for two reasons: *first*, less than five weeks before the Commission's adoption of the **Hearing Designation Order**, the merger opponents made numerous substantial filings against the merger.⁴⁹ The Applicants, carrying as they do the burden of proof, were entitled to respond to these filings. They did so, but to no avail, as the Commission appears not even to have noticed these responses, and to have accepted many of the opponents' arguments without considering the

⁴⁹ See *e.g.*, **Ex Parte** Presentation from Jack Richards and Steven M. Ryan, Counsel to NRTC, to Marlene H. Dortch (Oct. 8, 2002); **Ex Parte** Presentation from Jack Richards, Counsel to NRTC, to Marlene H. Dortch (Sept. 30, 2002); **Ex Parte** Letter from Patrick J. Grant, Counsel to Pegasus, to Marlene H. Dortch (Sept. 24, 2002); **Ex Parte** Presentation from Jack Richards, Counsel to NRTC, to Marlene H. Dortch (Sept. 20, 2002); **Ex Parte** Analysis of EchoStar and DIRECTV Confidential Documents from James W. Olson, Counsel to NAB, to Marlene H. Dortch (Sept. 11, 2002); **Ex Parte** Notice from Edward P. Henneberry, Counsel to NAB, to Marlene H. Dortch (Sept. 10, 2002); **Ex Parte** Letter from Patrick J. Grant, Counsel to Pegasus, to Marlene H. Dortch (Sept. 6, 2002); **Ex Parte** Comments of the National Rural Telecommunications Cooperative (Sept. 4, 2002).

rebuttal.⁵⁰ *Second*, the Commission's failure to give consideration to those submissions has meant that many of the Commission's findings are contrary to either basic logic or the weight of the evidence submitted.⁵¹

⁵⁰ By way of example, apart from a vague reference in footnote 266 of the *Hearing Designation Order* to the Applicants' omnibus October 8, 2002 *Ex Parte* Reply Comments, a filing that was submitted in response to the aforementioned *ex parte* oppositions submitted after the formal pleading cycle, the Commission makes absolutely no reference to the filing. *See Hearing Designation Order* at ¶ 39, n.266; *see also Ex Parte* Reply Comments of Applicants (Oct. 8, 2002). In addition, none of the following filings by Applicants were ever cited or referenced by the Commission in its *Hearing Designation Order: Ex Parte* Notice from Pantelis Michalopoulos, Counsel to EchoStar Communications Corporation, and Gary M. Epstein, Counsel to Hughes Electronics Corporation and General Motors Corporation, to Marlene H. Dortch (Sept. 25, 2002) (containing additional information regarding the Applicants' diversion analysis in response to staff question); *Ex Parte* Notice from Pantelis Michalopoulos, Counsel to EchoStar Communications Corporation, and Gary M. Epstein, Counsel to Hughes Electronics Corporation and General Motors Corporation, to Marlene H. Dortch (Sept. 13, 2002) (containing additional analysis of the diversion ratios between EchoStar and DIRECTV); *Ex Parte* Notice from Pantelis Michalopoulos, Counsel to EchoStar Communications Corporation, and Gary M. Epstein, Counsel to Hughes Electronics Corporation and General Motors Corporation, to Marlene H. Dortch (Aug. 13, 2002) (containing revised Merger Synergy Analysis providing further detail regarding the cost and revenue synergy model); *Ex Parte* Notice from Pantelis Michalopoulos, Counsel to EchoStar Communications Corporation, and Gary M. Epstein, Counsel to Hughes Electronics Corporation and General Motors Corporation, to Marlene H. Dortch (July 26, 2002) (containing additional backup information on competitive effects and national pricing presentation); *Ex Parte* Notice from Pantelis Michalopoulos, Counsel to EchoStar Communications Corporation, to Marlene H. Dortch (July 19, 2002).

⁵¹ The courts have repeatedly rejected such conclusory agency pronouncements. *See Motor Vehicle Mfrs. Ass'n v. State Farm Mutual Auto Ins. Co.*, 463 U.S. 29, 52 (1983) ("an agency must cogently explain why it has exercised its discretion in a given manner"; there must be a "rational connection between the facts found and the choice made"); *AT&T Wireless Services, Inc. v. FCC*, 270 F.3d 959, 968 (D.C. Cir. 2001) (vacating FCC order that contained conclusory explanations for central matters where there was considerable conflicting evidence); *United States Telecom Ass'n v. FCC*, 227 F.3d 450 (D.C. Cir. 2000) (vacating FCC order that did not examine relevant aspects of the record or articulate a satisfactory explanation for its findings); *Schurz Communications, Inc. v. FCC*, 982 F.2d 1043 (7th Cir. 1992) (vacating FCC order where agency failed adequately to explain key findings); *Committee for Community Access v. FCC*, 737 F.2d 74 (D.C. Cir. 1984) (vacating FCC order where its analysis was superficial and sidestepped the important issues); *Greater Boston Television Corp v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970) (the FCC must "take a hard look at the problem areas, and . . . set forth with clarity" its findings), *cert. denied*, 403 U.S. 923 (1971).

Local-into-Local. In analyzing the benefits of nationwide satellite local-into-local service, it is essential to bear in mind the significance of this benefit to one of the most under-served segments of the U.S. population, namely those living in rural areas. Even under the Commission's analysis, 110-130 areas of the country will likely never get local stations by satellite without the merger.⁵² The *HDO* dismisses that risk by reasoning that these areas account for only a "small percentage" of the nation's population -- 15%-20% of TV households.⁵³ The Commission's casual dismissal of this "small percentage" of TV households is surprising since it includes millions of rural subscribers in numerous states.⁵⁴ In its effort to preserve competition between DBS providers for this "small percentage" of TV households, the Commission has succeeded in preventing these subscribers from promptly receiving *any* local-into-local programming. Moreover, these potential rural subscribers, as well as subscribers in urban areas, will in all likelihood be deprived of satellite-delivered broadband service. With the spectrum capacity and economies of scale that New EchoStar would derive, the merger presents the most realistic way for these rural consumers to receive any broadband service, and it presents

⁵² See *Hearing Designation Order* at ¶ 78 ("[W]e believe that it is reasonable to anticipate that, without the merger, [each] company would be able to offer local broadcasting service to 80 to 100 DMAs within the next one to two years.").

⁵³ *Id.* at ¶ 78 ("This would permit the Applicants to serve about 80-85% of TV households with local-into-local without the merger."); see also *id.* at ¶ 80 ("Therefore, any merger-specific benefits that the merger might produce with respect to local-into-local service would, at best, accrue to a small percentage of potential viewers.").

⁵⁴ See *Notice of Ex Parte Presentation filed by National Strategies, Inc. and RFD-TV* (Oct. 16, 2002) ("It was also noted that even if, as an FCC source recently suggested, but which RFD doubts to be likely, 85% of Americans were to have access to local channels via satellite without the merger, about 40 states would have viewers in the 15% that would be left behind. Some states like Montana, North Dakota, South Dakota and Wyoming would likely have no local channels. That 15% could represent a substantial percentage of the geography of the United States. The status quo represents a "no-opoly" local service and broadband service to thousands of rural Americans.").

an efficient way to create effective broadband competition for all remaining consumers, Nevertheless, the *HDO* seems to conclude that it is in the public interest to deprive millions of rural consumers of the tremendous benefits and advantages that the rest of the country enjoys in receiving local-into-local and broadband services.

Under the Commission's statutory responsibilities, a consumer living in DMA 210 should be treated the same as, and indeed more solicitously than, one living in the largest DMA. To treat the consumers in rural areas otherwise would be to cast doubt on whether the Commission is following its mandate to fully evaluate the public interest, which necessarily includes the "public" in both urban *and* rural areas, under Sections 214(a) and 310(d) of the Communications Act?

Moreover, the Commission's analysis in the *HDO* clearly overstates the number of DMAs that could reasonably be expected to be served by each Applicant individually. In assessing the stand-alone capabilities of each company, the Commission apparently took the number of cities that each company serves (or will serve) with one spot-beam satellite, and then doubled that number on the theory that each company's second spot-beam satellite will result in a doubling of that capacity.⁵⁶ The Commission therefore spent a few lines to dispose of a complex question that the Applicants and their opponents had debated in hundreds of pages.⁵⁷

⁴⁷ U.S.C. §§ 214(a) and 310(d).

⁵⁶ *Hearing Designation Order* at ¶ 78 (“[T]he latest satellites offer significant improvements in spectrum efficiency through the use of spot beams. These new satellites effectively double the capacity to offer local channels for each company. Therefore, given that EchoStar and DirecTV each currently provide local service to approximately 40 markets, we believe it is reasonable to anticipate that, without the merger, [each] company would be able to offer local broadcasting service to 80 to 100 DMAs within the next one to two years.”)

⁵⁷ See, e.g., Opposition to Petitions to Deny and Reply Comments at 3-20 and Exhibit B (Declaration of Dr. Richard J. Bamett) (Feb. 25, 2002) (“*Opposition*”); *Ex Parte* Letter from Pantelis Michalopoulos, Counsel for EchoStar Communications Corporation, and Gary M.

“Conclusory explanations for matters involving a central factual dispute where there is considerable evidence in conflict do not suffice to meet” even the deferential standard of reasoned agency decisionmaking.⁵⁸

Even more important, the Commission did not look beyond technical capabilities to consider the central question of economic viability? That question is related to the huge costs of local-into-local service, including the spectrum opportunity cost resulting from displacement of national programming to make room for local stations. Even NRTC, while vehemently opposing the merger, has acknowledged that these costs preclude each of the two companies from providing local-into-local service to the entire nation.⁶⁰ On that question, the Applicants had shown that “DIRECTV would not likely serve more than about **70** DMAs. . . due to the opportunity costs and expected returns, and likely would serve less.”⁶¹ As to EchoStar, the Applicants had stated that EchoStar expects to be able to serve approximately **50** DMAs from its CONUS capacity with its two spot-beam satellites in place.⁶² Dr. Willig’s Reply Declaration

Epstein, Counsel for General Motors Corporation and Hughes Electronics Corporation, to Marlene H. Dortch (Aug. **2,2002**); *Ex Parte* Reply Comments of Applicants at **5** and Volume I, Exhibit **3**; Pegasus Petition to Deny at **49-53** (Feb. **4,2002**); NAB Petition to Deny at **74-89** (Feb. **4,2002**).

⁵⁸ *AT&T Wireless Services, Inc. v. FCC*, 270 F.3d 959,968 (D.C. Cir. 2001).

⁵⁹ *See Hearing Designation Order* at ¶ 78.

⁶⁰ *See* Joint Comments of the National Rural Telecommunications Cooperative, the National Rural Electric Cooperative Association and the National Rural Utilities Cooperative Finance Corporation at **13-14** (May **30,2002**) (filed with Rural Utilities Service of the Department of Agriculture)(“While it appears to be technologically possible for both carriers to offer all broadcast signals to all Americans, the provision of local signals in smaller markets is not likely to generate enough profit to entice DIRECTV and EchoStar to build additional spot beam capacity for local signal distribution.”).

⁶¹ *Opposition* at **15**.

explained the commercial feasibility and opportunity cost factors.⁶³ In addition, on August 2, 2002, the Applicants submitted detailed econometric models showing that neither company alone would find it economic to serve more than a limited number of cities – again, in all probability, significantly fewer than the 80-100 range reached by the **Commission**.⁶⁴ The Commission disregarded these submissions on the question of the companies’ stand alone capability and opted instead for a back-of-the-envelope calculation that no opponent proposed.

The Commission’s disregard for the cost of local-into-local service in evaluating each company’s capabilities is, moreover, strikingly inconsistent with the Commission’s reliance on precisely that cost to question the merged company’s promise that it will provide local-into-local service throughout the **country**.⁶⁵ In other words, in the Commission’s eyes, cost is not an issue for each company standing alone, but becomes a debilitating problem for the merged company. In reality, of course, the opportunity cost of the spectrum is higher for each stand-alone company, since each applicant is much more spectrum-constrained than the merged company would be, not the other way round, as the Commission would have it.⁶⁶

⁶² *Id.* at 12. EchoStar had also specifically rebutted on technical grounds NRTC’s allegation that these two satellites would enable EchoStar to provide all local stations to 80 DMAs (the low end of the range that the Commission has derived by multiplying the number of cities by two). *Id.* at 13. The Commission never addressed that disagreement.

⁶³ Willig Reply Declaration at ¶¶ 9-17.

⁶⁴ *See Ex Parte* Letter from Pantelis Michalopoulos, Counsel for EchoStar Communications Corporation, and Gary M. Epstein, Counsel for General Motors Corporation and Hughes Electronics Corporation, to Marlene H. Dortch (Aug. 2, 2002).

⁶⁵ *Hearing Designation Order* at ¶ 203.

⁶⁶ Applying the same double standard, the *Hearing Designation Order* questions the Applicants’ plan to serve all 210 DMAs on the ground that the plan assumes carriage of standard definition local channels. *See Hearing Designation Order* at ¶ 202. This is of course correct, but the *Hearing Designation Order* does not explain why it is relevant only to the capabilities of the combined company and not to the stand-alone capabilities of each company. Any requirement of carrying HDTV local feeds would cripple each company in its attempts to provide local-into-

In short, the Commission has no proper basis to minimize the public interest benefits of nationwide satellite local-into-local service. Indeed, under the revised proposal, the Commission has the prospect of not one, but two satellite companies eventually offering **DBS** local-into-local service in all **210 DMAs**. Under the status **quo**, even by the Commission's own estimation, such a result -- which is demonstrably in the public interest -- cannot occur.

Broadband. Again, as with local-into-local service, one of the most important benefits of the merger is the promise of satellite broadband service in all areas of the United States. As the Applicants have shown, neither of them on its own has either the spectrum resources or the financial capacity to offer a true, universal broadband service (a fact that is underlined by the failure of either company to develop a successful broadband model to date). New EchoStar, by contrast, will have the ability to make this vision a reality, bringing much-needed competition to areas already served by cable broadband but, even more importantly, making broadband service available for the first time to areas that have no cable or **DSL** service today and have little prospect of seeing such service in the foreseeable future.

The **HDO** discounts this benefit by applying the same double standard as with local-into-local service: (1) by overestimating the stand alone capabilities of the Applicants in the broadband area and (2) by discounting the capabilities of the merged entity to provide broadband service on a viable, nationwide basis. The Commission seems to have entirely overlooked the Applicants' detailed submissions with respect to each of these two questions. Again, the Commission must not, by failing to give proper weight to this benefit, pass up the once-in-a-generation opportunity provided by this merger to achieve universal broadband service

local service. Each company would only be able to provide such service only in a fraction of the cities it serves now, and would certainly not be able to expand that number, let alone serve 80-**100** cities as the Commission has found.

for rural areas (as well as competitive broadband service for more urbanized areas served by cable and DSL).

As with local-into-local service, the Commission has focused its analysis exclusively on spectrum constraints – a simple multiplication of the number of each company's orbital slots by the number of subscribers that could be served from each slot.⁶⁷ Based on this simplistic arithmetic, the Commission has concluded that one company could reach the critical mass of 5 million subscribers, while the other company could approach that number.⁶⁸

The need for enough spectrum is an important factor, and the Commission erroneously assumed away in its analysis the current constraints on the use of Ka-band spectrum.⁶⁹ But, even more important, if spectrum constraints were the only issue, satellite broadband service would be flourishing today – many possible combinations of Ka-band licensees would have enough slots to serve the needed number of subscribers. The most serious problem, of course, is the high cost of deploying residential broadband service – the cost of consumer premises equipment and corresponding expense of acquiring subscribers. These costs

⁶⁷ *Hearing Designation Order* at ¶ 232.

⁶⁸ *Id.*

⁶⁹ For example, the Commission erroneously assumed in its calculation that Hughes had unencumbered access to 720 MHz of Ka-band spectrum for its Ka-band satellites. *See id.* at ¶ 232 n.554. In fact, however, the Applicants demonstrated that Hughes SPACEWAY has not been able to use 220 MHz of this spectrum for its services, and it is designed to use spectrum only in 500 MHz segments – it is not feasible to change the design of the SPACEWAY system at this late date. *See Opposition* at 102-105. Even though the Commission has just changed its allocations in a manner that may facilitate access to more Ka band spectrum for service to small antennas, there remain significant barriers to actually relocating incumbent terrestrial users from that spectrum. *See In the Matter of Redesignation of the 11.7-19.7 GHz Frequency Band, Blanket Licensing of Satellite Earth Stations in the 17.7-20.2 GHz and 27.5-30.0 GHz Frequency Bands, and the Allocation of Additional Spectrum in the 17.3-17.8 GHz and 24.75-25.25 GHz Frequency Bands for Broadcast Satellite-Service Use*, Second Order on Reconsideration, IB Docket No. 98-172, RM-9005, RM-9118 (rel. Nov. 26, 2002).

have led EchoStar to withdraw from its residential broadband venture and Hughes to announce that it will likely discontinue its own residential satellite-based broadband offering?’ The Commission suggests that EchoStar’s withdrawal from Starband may be inspired by EchoStar’s desire to influence the outcome of the proceeding, and faults EchoStar for not disproving that possibility?’ That reasoning is wrong, for two reasons: *first*, it is based on nothing more than speculation about EchoStar’s motives offered by NRTC. EchoStar should not have to prove the negative.⁷² *Second*, EchoStar has in fact shown that it lost \$100 million in pursuing the Starband venture.⁷³ There is no rational explanation why the Commission should need more evidence of the reasons for EchoStar’s withdrawal.

⁷⁰ See *Opposition* at 98.

⁷¹ See *Hearing Designation Order* at ¶ 239.

⁷² See, e.g., *In the Matter of Application of Ameritech Michigan Pursuant to Section 271 of the Communications Act of 1934, as amended, to Provide In-Region, InterLATA Services in Michigan*, 12 FCC Rcd. 20543,20568 (1997) (“We believe that shifting the burden of production once a BOC has presented a prima facie case that its application satisfies section 271 is appropriate, because parties opposing a BOC’s application have the greatest incentive to produce, and generally have access to, information that would rebut the BOC’s case. In addition, absent such a shift in the burden of production, a BOC applicant would be in the untenable position of having to prove a negative (that is, of coming up with, and rebutting arguments why its application might not satisfy the requirements of section 271.”); *Pub. Citizen v. Dept. of State*, 276 F.3d 634,645 (D.C. Cir. 2002) (finding that “‘the task of proving the negative, that the information has not been revealed, might require the government to undertake an exhaustive, potentially limitless, search’”) (citations omitted); *National Communications Association, Inc. v. AT&T*, 238 F.3d 124, 131 (2nd Cir. 2001) (“[A]ll else again being equal, courts should avoid requiring a party to shoulder the more difficult task of proving a negative. ‘The general rule is that the party that asserts the affirmative of an issue has the burden of proving the facts essential to its claim.’”); *Aubumdale State Bank v. Dairy Farm Leasing Corp.*, 890 F.2d 888, 893 (7th Cir. 1989) (acknowledging “general rule” that “the party that asserts the affirmative of an issue has the burden of proving the facts essential to its claim”) (citations omitted); *Tendler v. Jaffe*, 203 F.2d 14, 17 (D.C. Cir. 1952) (at a minimum, the party asserting the affirmative of an issue must introduce evidence on the issue, and generally has the burden of proof on the issue).

⁷³ See e.g., *Ex Parte* Reply Comments of Applicants at 7 n.16 (Oct. 8,2002).

The Commission has recognized the daunting costs of residential service in the *AT&T/Comcast* proceeding, even though they are a lower hurdle for cable providers than for satellite operators – and a hurdle that cable providers appear to have overcome. In contrast, the Commission did not even acknowledge Hughes’ statements that, precisely **in** light of these costs, the SPACEWAY system will likely be used only for enterprise service if the merger does not occur.⁷⁴ The Commission has ignored this crucial statement and has wrongly assumed that SPACEWAY would be used for residential service without the merger.⁷⁵ Nor did the Applicants confine themselves to citing the unmistakable reality that satellite broadband has simply not taken off. They also submitted detailed econometric models taking into account the significant costs of residential broadband service, and showing that neither company standing alone could, based on the economics, make the case for such a service, while New EchoStar would find it economical to provide it.⁷⁶ The Commission did not even acknowledge that evidence.

Inexplicably, the Commission did point to the dismal reality and prospects of the satellite broadband industry to question the merged company’s promises, but ignored these same facts as inhibiting the stand alone capabilities of each company.⁷⁷ This is another example of the Commission’s double standard in the eyes of the Commission, the state of the industry has no bearing on what each Applicant can achieve without the merger, but becomes relevant only to cast doubt on the prospects of New EchoStar. Again, the reverse is in fact the case: the merger can only lower the obstacles to residential broadband service by allowing the merged company to

⁷⁴ See *Opposition* at 97-98.

⁷⁵ See *HDO* at ¶ 232.

⁷⁶ See Broadband Economic Models; see also *Opposition* at 106-118 and attached declarations.

⁷⁷ See *Hearing Designation Order* at ¶ 239.

reach scale through the virtuous circle of a higher combined pool of **DBS** subscribers, lower equipment cost and lower subscriber acquisition costs. There is no rational possibility that the merger will actually heighten these impediments. It would be terrible if the result of that flawed analysis were to miss the unique opportunity to secure nationwide residential broadband service.

The Commission's disposition of the Applicants' claimed broadband benefits is also inconsistent with the Commission's wholehearted acceptance of much weaker claims in the case of **AT&T/Comcast**. Consistent treatment would create "substantial doubt" as to whether a hearing should be held. As the Applicants have pointed out, the broadband benefits flowing from the merger are in fact less speculative, more credible and more merger-specific in several respects than those claimed by the parties in the **AT&T/Comcast** merger. Here, neither company will likely provide a widely-used residential broadband offering standing alone;⁷⁸ the broadband benefits will result directly from the combination of the two companies' subscriber bases and spectrum resources;⁷⁹ satellite broadband deployment will usher in competition against the cable video/broadband bundle;" and it will benefit all consumers nationwide." Moreover, the

⁷⁸ See, e.g., Applicants' Ex Parte Broadband Presentation to the Commission's Merger Task Force (June 12, 2002) ("Broadband Presentation") at 5-26 (explaining in detail why the economics of the companies' standalone efforts are unfavorable); see also Applicant's Ex Parte Submission (July 30, 2002) ("Broadband Economic Models").

⁷⁹ See *id.* at 28-41 (demonstrating that the combination of subscriber bases and spectrum resources is key to achieving the scale necessary to create a competitive satellite broadband service).

⁸⁰ See Broadband Presentation at 43-48 (explaining that the combination will create effective, facility-based competition with cable modem and **DSL** technology, that will be comparable in price and performance and will serve as a competitive constraint on cable and **DSL** providers' pricing and service).

⁸¹ *Id.* at 44 (the combination will help bridge the digital divide by bringing broadband service to some **40** million households currently not served by **DSL** or cable).

Applicants have submitted detailed and unrebutted econometric models backing their claim that the merger will *create* a viable broadband competition.’’

In the AT&T/Comcast transaction, on the other hand, each company already occupies a dominant position in the provision of high-speed access in its franchise areas. The claimed benefits will allegedly arise chiefly from the merged company’s improved ability to finance broadband deployment. This additional deployment will further entrench cable dominance as opposed to introducing new competition, and it will not benefit consumers outside the parties’ franchise areas. See Applicants’ Ex Parte Reply Comments at 7 n.15 (Oct. 8, 2002). Finally, it appears that the cable applicants did not submit *any* econometric evidence that the merger would even accelerate the existing pace of broadband deployment. Specifically, the Applicants’ review of the public record in the *AT&T/Comcast* proceeding suggests that the applicants provided no support whatsoever backing their conclusory assertion of **\$1.25-1.95** billion in merger synergies.⁸³

Nevertheless, in *AT&T/Comcast* the Commission found that “the merged entity is likely to accelerate the deployment of broadband services in AT&T service areas,” even though, as it recognized, “most cable providers are deploying broadband” anyway. *AT&T/Comcast*

⁸² See Broadband Economic Models.

⁸³ AT&T and Comcast simply included in their application the unsupported assertion that the merger “should result in synergies and efficiencies worth approximately **\$1.25 to \$1.95** billion a year in increased earnings before interest, tax, depreciation and amortization (“EBITDA”).” See AT&T/Comcast Application, Declaration of Robert Pick, at **3**. Later in the proceeding, the applicants merely reaffirmed this estimate, see Letter from A. Renee Callahan, Counsel to Comcast Corp., to Marlene H. Dortch, Secretary, FCC, at **28** (“Value Creations Through Synergies”) (Redacted Version) (July 2, 2002), this time dividing the estimated merger synergies into the following five categories with no further backup: **(1)** “programming cost savings”; **(2)** “continued operating efficiencies”; **(3)** “national advertising platform”; **(4)** “new products”; and **(5)** “Comcast telephony.” See *id.*

Order at ¶112. The rationale for this finding is at every turn inconsistent with the Commission’s complete dismissal of the broadband claims in the Echostar-Hughes merger proceeding.

To justify its conclusion in *AT&T/Comcast*, the Commission reasoned primarily that Comcast “has been able to upgrade its plant more quickly than AT&T,” and therefore “applying this expertise to the AT&T cable systems is likely to have a positive impact on the deployment of broadband to AT&T subscribers that currently do not have access to those services.” *Id.* Comparison of these findings to the *HDO* discussion suggests the absurd proposition that a broadband benefit is more merger-specific when one of the two merger providers is a very effective broadband provider already than when neither provider is an effective provider today.

The Commission in *AT&T/Comcast* next reasoned that:

the greater scale and scope of the merged entity is likely to spur new investment. The development and deployment of new technologies often entails significant up-front, fixed investment. The merged company should have a greater ability to spread those fixed costs across a larger customer base, which should in turn foster incentives for investment by the merged entity. . . .

AT&T/Comcast Order at ¶ 113. This passage is impossible to reconcile with the Commission’s total rejection of these very same claims made by EchoStar and Hughes, especially because the need to spread the huge fixed costs over a large subscriber base is much more evident in the EchoStar/Hughes merger⁸⁴ – after all, each of AT&T and Comcast has been able to overcome these fixed-cost hurdles and to provide substantial residential service on a stand-alone basis, whereas the same obstacle has proved debilitating for Echostar’s and Hughes’ efforts.

⁸⁴ *See, e.g.*, Broadband Presentation at 22 (describing the multi-billion dollar upfront costs needed to implement a competitive satellite broadband service).