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August 20, 2003

BY HAND

Marlene H Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re Ex Parte Submission in MB Docket No. 03-124

Dear Secretary Dortch:

Enclosed, pursuant to 47 C.F R ¶ 1.1206(b), please find two copies of the Reply Affidavit of Professor Lynn A Stout of the UCLA School of Law, filed this day on behalf of Advance/Newhouse Communications, Cable One, Cox Communications and Insight Communications (the "Joint Cable Commenters")

Professor Stout's affidavit addresses arguments regarding News Corp.'s proposed Audit Committee made in the Opposition to Petitions To Deny and Reply Comments ("Opposition") filed by News Corp. and Hughes ("Applicants"), and to the Affidavit of Lawrence A. Hammermesh filed therewith

As Professor Stout's Reply Affidavit makes clear, the Applicants and their expert still have not demonstrated that Hughes' independent directors can or will be immune from influence or control by News Corp. as Hughes' majority shareholder. Professor Stout observes that the "proposed Hughes governance structure does not eradicate the problem of controlling shareholder self-dealing. To the extent it addresses the problem at all, it does only on the margin, and to a degree that cannot be assessed in advance but must depend on the particular facts and circumstances of the particular case, including details of the transaction, the process, and the individuals involved " (Stout Reply Affidavit at ¶ 8)

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Most importantly, as Professor Stout concludes, the Applicants and their expert still have not been able to demonstrate whether and how the Audit Committee could detect and deter the competitive harms of the transaction identified by the Joint Cable Commenters. The Joint Cable Commenters' chief concern is that this transaction significantly heightens News Corp.'s incentive and ability to impose cost increases for Fox programming across the universe of all its distributors – including DirecTV. There is no basis for concluding that the Audit Committee would have any capability or authority to prevent News Corp. from imposing across-the-board price increases for Fox programming, particularly in a circumstance in which DirecTV is paying rates which are equal to, or lower than, those imposed upon other MVPDs and their subscribers. As Professor Stout notes

> The bottom line is that, short of excluding News Corp. from having any involvement in the election or removal of Hughes' independent directors, there is no readily available structural mechanism for ensuring that those directors assigned to the Audit Committee will be able to discharge their duties in a manner that is free of controlling shareholder influence. Further, even assuming *arguendo* that an ideal Audit Committee could be created free of all controlling shareholder influence, this would at most protect the interest of DirecTV's non-controlling shareholders – and not the interests of DirecTV subscribers or the subscribers of any other multichannel distributors. Since the harms identified by the Joint Cable Commenters primarily affect multichannel video service *consumers*, it is difficult to see how an ideal Audit Committee, even if such could be created, could be relied upon to prevent such harms. (Stout Reply Affidavit at ¶ 16)

In short, the efficacy of the proposed Audit Committee in addressing concerns that DirecTV's non-controlling shareholders might have about News Corp. self-dealing is, at best, highly uncertain. It is clear, however, that the Audit Committee is a completely inadequate means of addressing and remedying the additional pricing power and bargaining leverage over all programming distributors which News Corp. would gain by acquiring DirecTV.

Sincerely,

Christopher J. Harvie

Enclosure

cc Chairman Michael K Powell
Commissioner Kathleen Q Abernathy
Commissioner Jonathan S. Adelstein

Commissioner Michael J. Copps	
Commissioner Kevin J Martin	
W Kenneth Ferree	
Donald Stockdale	
Simon Wilkie	(via email)
Deborah E Klein	(via email)
Marcia Glauberman	(via email)
Barbara Esbin	(via email)
James Bird	(via email)
JoAnn Lucanik	(via email)
Neil Dellar	(via email)
Douglas Webbink	(via email)
Tracy Waldon	(via email)
Bertram W Carp	(via email)
Qualex International	(via email)

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
General Motors Corporation, Hughes	)	
Electronics Corporation, and the	)	
News Corporation Limited	)	MB Docket No 03-124
Application To Transfer Control of FCC	)	
Authorizations And Licenses Held By	)	
Hughes Electronics Corporation	)	
To The News Corporation Limited	)	

REPLY AFFIDAVIT OF LYNN A. STOUT

1. My name is Lynn A. Stout. I hold the position of Professor of Law at the University of California at Los Angeles (UCLA) School of Law, where I teach basic and advanced courses in securities regulation and corporate law On June 16, 2003, I submitted an Affidavit on behalf of the Joint Cable Commenters in this proceeding The Joint Cable Commenters have asked me to respond to arguments made by the General Motors Corporation (GM), Hughes Electronics Corporation (Hughes), and The News Corporation Limited (News Corp) (collectively, the Applicants) related to corporate governance.

2 At a general level, the Applicants and their expert, Professor Larry Hammermesh of Widener University, have responded to the governance problems raised by the proposed Hughes acquisition primarily by asserting, in many different forms and flavors, that certain interested transaction between Hughes and News Corp. will be subject to the approval of Hughes' "independent" directors.

3. This extended discussion of the standards and requirements for director "independence" is potentially misleading because it glosses over the critical question: independent *of whom*? Delaware corporate law, the proposed NYSE listing standards, and the Sarbanes Oxley Act do indeed set forth numerous requirement for independent director involvement in corporate governance. However, these provisions are designed primarily to assure director independence from the firm's executives and other directors in transactions between the firm and its executives and directors. These provisions do not assume that "independent" directors are also independent of the firm's controlling shareholder in transactions between the firm and its controlling shareholder. To the contrary, controlling shareholders *always* have the potential to influence directors—even "independent" directors—as long as they are able to vote their shares in director elections Furthermore, the Applicants' citation to the Sarbanes Oxley Act is somewhat misleading, as that Act—as News Corp concedes in its Response to the FCC's Information Requests filed July 28, 2003 ("Response to Requests")—is not oriented toward protecting either non-controlling shareholders or consumers from the potentially harmful results of controlling shareholder self-dealing (Response to Request no. I.6).

4. Contrary to the Applicants' insinuations, Delaware corporate law presumes that "independent" directors are not independent of the firm's controlling shareholder. This rule makes sense, because it recognizes that (1) directors owe fiduciary duties to controlling shareholders, and (2) because directors are elected by shareholders, a director necessarily may worry that if he or she offends the firm's controlling shareholder, he or she will lose his or her seat on the Board. A disgruntled controlling shareholder need not remove a director to accomplish this; rather, as News Corp.

discusses in its Response to Requests, the controlling shareholder can simply vote for an alternate candidate of its choosing in the next regularly-scheduled election. (Response to Request no. I.9). This controlling shareholder influence over the Board necessarily implies controlling shareholder influence over the Audit Committee as well since, as the Applicants concede, the members of the Audit Committee are drawn from and serve at the pleasure of the Board of Directors. (Response to Request no. I.4). Every Director faces the ongoing threat of removal or replacement by the controlling shareholder, including no less the members of the Audit Committee.

5 Delaware courts do not always strike down transactions between firms and their controlling shareholders Rather, corporate law adopts a more nuanced approach that presumes that any transaction between the firm and its controlling shareholder is intrinsically suspect. The controlling shareholder can rebut the presumption by providing sufficient evidence that the transaction was nevertheless "fair" and took place on terms similar to those that would have been reached in arm's length negotiations.

6. To do this, the controlling shareholder may argue, *inter alia*, that one relevant factor is that the particular transaction was approved by particular directors who, under the particular facts of the case, were largely free of controlling shareholder influence beyond the unavoidable influence implied by the controlling shareholders' voting power. This has some bearing on whether the transaction will be deemed "fair." It is not determinative, however, and does not guarantee a judicial finding of fairness. Even in a case where a controlling shareholder establishes fairness, the result is not to immunize the controlling shareholder from liability, but simply to shift the burden to the complaining plaintiff to introduce evidence showing unfairness.

7. Moreover, the Applicants' heavy reliance on the independent Directors' ability to review some (but not all) potentially interested transactions is weakened by the fact that, under Delaware law, there is no requirement for Directors to have any measure of subject matter competence. Consequently, it is possible that the Board will be unable to distinguish between contracts that benefit DirecTV and those that benefit News Corp. to the detriment of DirecTV.

8. The end result is that, as a matter of corporate law, the "independence" of Hughes' directors under the proposed Hughes governance structure does not eradicate the problem of controlling shareholder self-dealing To the extent it addresses the problem at all, it does so only on the margin, and to a degree that cannot be assessed in advance but must depend on the particular facts of the particular case, including details of the transaction, the process, and the individuals involved.

9 Professor Hammermesh's affidavit specifically identifies three propositions from my initial Affidavit with which he disagrees. Each is addressed below.

10 First, Professor Hammermesh takes issue with the statement that "no director reliably can be 'independent' of a controlling shareholder's influence" because, in his own words, "Delaware law . . recognizes that independent directors, if duly informed and active, can be effective bargaining adversaries even as against a controlling shareholder." (Hammermesh affidavit at 3).

11. Professor Hammermesh's own words support the point he challenges. The law recognizes that directors *can* be an effective check on controlling shareholders, but it also recognizes that they *can* be ineffective. As discussed above, whether director approval of a transaction with a controlling shareholder shifts the burden to the plaintiff

to establish unfairness depends on the detailed facts of the particular case, including the specific transaction, process, and individuals involved As a result, so long as directors are elected by shareholders, including controlling shareholders, one cannot devise in advance a governance structure that will insure reliably that those directors will act independently of a controlling shareholder in all future transactions.

12. Professor Hammermesh also argues that "Delaware law does not presume that directors are necessarily subservient to persons holding less than a majority of voting shares." (Hammermesh affidavit at 3). This carefully-phrased sentence appears to be raising a second argument, that News Corp. may not become the controlling shareholder of Hughes because it will not hold a majority of shares, just the largest block. However, News Corp's Application concedes that News. Corp. might be deemed to exercise de facto control over Hugh under the Communication Acts (Application at 14). For similar reasons, News Corp. is likely to be deemed Hughes' controlling shareholder under Delaware corporate law.

13. The end result is that Professor Hammermesh's own analysis conflicts with his ultimate conclusion that Hughes' proposed governance structures "dramatically diminish or eliminate altogether any ability on the part of News Corp., to exercise control over the independent members of the Hughes board of directors." (Hammermesh affidavit at 8) Diminish, perhaps, depending on the facts of a particular future case. "Eliminate altogether"? Absolutely not.

14. Second, Professor Hammermesh takes issue with the statement that "'independent' director review and approval of transactions between a controlling shareholder and the firm . cannot suffice to give a clean bill of health to [interested]

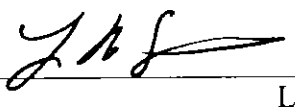
transactions." (Hammermesh affidavit at 8) Again, Professor Hammermesh's own arguments implicitly confirm the accuracy of the statement he challenges, as when he correctly observes that "active and effective participation of independent directors . . will significantly contribute to a judicial affirmation." (Hammermesh affidavit at 9) Significantly contribute, perhaps (again depending on the facts of the case, including whether the court finds the directors were in fact "active and effective"). But as Professor Hammermesh's affidavit impliedly concedes, director approval is not determinative In other words, it does not suffice

15 Finally, Professor Hammermesh suggests that any self-dealing between News Corp. and Hughes will be checked by a "vibrant" and "alert" plaintiffs' bar. (Hammermesh affidavit at 10) With due deference to plaintiffs' lawyers, it should be recognized that they do not always detect frauds and violations of fiduciary duty, do not always bring cases challenging such frauds and violations, do not always succeed in proving such frauds and violations, and do not always settle the cases they prove for damages that fully reflect the costs of such frauds and violation. If they did, it is hard to see why such frauds and violations still occur.

16 The bottom line is that, short of excluding News Corp. from having any involvement in the election or removal of Hughes' independent directors, there is no readily available structural mechanism for ensuring that those directors assigned to the Audit Committee will be able to discharge their duties in a manner that is free of controlling shareholder influence Further, even assuming *arguendo* that an ideal Audit Committee could be created free of all controlling shareholder influence, this would at most protect the interest of DirecTV's non-crontrolling shareholders – and not the

interests of DirecTV subscribers or the subscribers of any other multichannel distributors. Since the harms identified by the Joint Cable Commenters primarily affect multichannel video service *consumers*, it is difficult to see how an ideal Audit Committee, even if such could be created, could be relied upon to prevent such harms

I declare that the foregoing is true and correct:



Lynn A. Stout
Professor of Law

Dated 8/15/03