



**Testimony of Gigi B. Sohn, President
Public Knowledge**

**Before the
U.S. Senate
Committee on Commerce, Science, and Transportation**

**Hearing On:
“XM-Sirius and the Public Interest”**

**Washington, DC
April 17, 2007**

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Chairman Inouye, Vice Chairman Stevens, and other members of the Committee, my name is Gigi B. Sohn. I am the President of Public Knowledge, a nonprofit public interest organization that addresses the public's stake in the convergence of communications policy and intellectual property law. I want to thank the Committee for inviting me to testify on the proposed merger of XM Satellite Radio and Sirius Satellite Radio.

Introduction and Summary

The merger of XM Satellite Radio and Sirius Satellite Radio presents a dilemma for public interest advocates. On the one hand, the only two providers of radio services via satellite, who have vigorously competed over the past five and a half years, are seeking to consolidate, immediately raising questions about the impact on prices and choice for consumers. On the other hand, this vigorous competition has led to a spending war for new and better programming, leaving both competitors weakened in a world where Internet radio, HD radio, cable radio and other multichannel music, entertainment and information services have become increasingly popular.

Some will say that XM and Sirius' current financial state is a problem of their own devising—that a service that was intended largely to provide an alternative for the strict playlists and over-commercialization of broadcast radio spent lavishly and foolishly on radio personalities and major league sports. They will also say that allowing a merger is a government “bail-out.” I agree with both of these statements. But I do not believe that that is where the focus should be.

Instead, the salient question for policymakers is this: if this merger is simply denied, will consumers be better off? Given the financial state of both companies, the slowing growth of their customer base and the increasing competition in the marketplace, it appears likely that in the absence of a merger, both services will continue to limp along instead of investing in new and diverse programming. Might it not be better for consumers to permit the merger under conditions that provide expanded programming and pricing choice, along with temporary measures to keep prices in check? After a great deal of discussion with my public interest colleagues, former regulators and antitrust experts, I believe that the latter is the best course.

Thus, the XM and Sirius Satellite radio merger should be approved only if it is subject to the following three conditions:

- the new company makes available pricing choices such as tiered programming.
- the new company makes 5% of its capacity available to non-commercial educational and informational programming over which it has no editorial control.
- the new company agrees not to raise prices for its combined programming package (as opposed to each individual company's current programming package) for three years after the merger is approved.

Two other points warrant mention here. The first is our strong opposition to any merger condition involving limitations on the ability of consumers to record these satellite radio services. Such a condition would be tantamount to repealing the Audio Home Recording Act, which specifically protects a consumer's ability to record digital music.

The second is to urge Congress and the FCC to permit satellite radio broadcasters to do more, and not less, local programming. Broadcasters' opposition to this merger and to satellite radio's provision of local traffic, weather and emergency information is not only incredibly hypocritical given their own current regulatory efforts to consolidate, but it is also anticompetitive in its own right. Even assuming that broadcasters take seriously their statutory duty to serve local communities with programming that serves local needs (and not just traffic and weather), there is no reason why, in 2007, *any* media service should have a government-granted monopoly over local programming.

Whether the Proposed Merger Would Survive Antitrust Scrutiny is a Close Call and Warrants Thorough Analysis

Let me say at the outset that I am not an antitrust expert. Luckily, I have several colleagues who are. After conferring with them, I can only conclude that the antitrust questions raised here are very complex and ultimately depend on information to which Public Knowledge does not have access.¹

¹A former official of the Department of Justice's Antitrust Division apparently agrees with this assessment. *See* Statement of Charles E. Biggio, Wilson Sonsini Goodrich & Rosati, PC Before the Antitrust Task Force, Committee on the Judiciary, United States House of Representatives Concerning Competition and the Future of Digital Music, February 28, 2007. ("Right now, we do not have all the facts necessary to determine the legality of the merger").

Take, for instance, the critical question of what would be the relevant market. If one views the relevant product market solely as satellite delivered radio service, the proposed transaction could be characterized as a “merger to monopoly,” which would strongly suggest outright rejection. Some of my public interest and academic colleagues, whom I respect enormously, do just that. For instance, the satellite radio broadcasters are the only services that provide listeners with certain programming, available at both high quality and from a mobile device. The satellite services also provide the only continuous national market for certain types of broadcasting. For example, only on satellite radio can a New York Mets baseball fan listen to the team’s baseball games anywhere in the nation, or even as one drives from state to state.

On the other hand, if the market is defined more broadly to include a wide variety of radio, mobile, and multi-channel music services, a regulator might reach a very different result. Indeed, XM and Sirius’ services overlap with and have effects on several different services (including video, if you include their feeds of cable shows). Competitors in this broader market would include over-the-air broadcast and HD radio, Internet radio services, cable (and DBS) radio, and wireless phone music and services like Sprint Radio, MobiTV, and V-Cast, as well as podcasts that can be downloaded onto MP3 players.²

A more broadly-defined market would include all of the services to which consumers would readily turn if satellite radio prices were raised. Anecdotal evidence

² Moreover, it appears that Sirius and XM may soon no longer be the only satellite radio providers. Slacker, a new service, is slated to begin delivering music to consumers via satellite in the near future. *See, e.g.*, Associated Press, *Start-Up Launches 'Personal Radio' Service*, Mar. 14, 2007, available at <http://online.wsj.com/article/SB117388069334336810.html>.

suggests that there is no shortage of substitutes.³ Still, we cannot ignore the fact that there are real differences between satellite radio and its competitors.

For instance, an audiophile colleague of mine is puzzled over my love of satellite radio because he receives all the new music he wants (for free) from Internet radio. In addition to providing highly diverse and specialized programming, Internet radio is becoming more mobile, and as a result is becoming a viable competitor to satellite radio.⁴ However, wireless services still may lack the higher-quality sound of satellite radio, and recent, drastic increases in the already-high webcasting royalty rates may drive a lot of Internet radio services out of business.⁵ Podcasts, which many satellite consumers may consider an easy substitute for satellite programming, are provided via a “pull” technology, where the consumer picks and chooses content. In contrast, satellite radio is a “push” technology in which the consumer may receive new content without specifically selecting it. And while broadcast radio is becoming a clear satellite competitor with multi-channel and some commercial-free HD services, it is a local service that still hews to strict music playlists and is largely advertiser supported.⁶ Of course, a product needn’t

³ See, e.g., David Bank & Ryan Vineyard, *Wedding Bells Are Ringing For XMSR And SIRI*, RBC CAPITAL MARKETS INDUSTRY COMMENT: BROADCASTING AND CABLE TV, Feb. 20, 2007, 1,4.

⁴ A number of mobile carriers are currently providing streaming audio, video, and data to the mobile phone handsets they sell, generally on an exclusive basis between the wireless and content providers. This content is provided to the subscriber for a fee, typically in addition to wireless data fees, as these services are usually IP based. Verizon's VCast provides entertainment, sports, news, and weather video clips, music downloads, and mobile data; Verizon is also employing new MediaFLO technology to directly distribute content to handsets, apart from their data-based network. Clear Channel and MobiTV are exclusive providers of streaming audio and video content to Cingular subscribers. Sprint Mobile currently provides a number of streaming radio channels, from Music Choice, Rhapsody, Sprint Radio, and Sirius; it is also aiming to provide more competition for high-speed data and competitive video streaming with WiMax technology.

⁵ See, e.g., Eliot Van Buskirk, *Royalty Hike Panics Webcasters*, WIRED NEWS, Mar. 6, 2007, <http://www.wired.com/news/culture/music/0,72879-0.html>

⁶ As evidenced by its appearance here today and its strong opposition to the merger, there is little doubt that the broadcast industry views satellite radio as a substitute.

be identical to be substitutable.⁷ While intuitively it would seem that at least some of these competitors could act as substitutes, the important part of this question is not whether consumers can conceivably switch, but if they will, given the switching costs. Evidence of past pricing behavior⁸ and data on how and why consumers choose to spend their money on satellite radio would be most helpful to answer this question.

In the end, whether or not the merger is approved should depend upon its effects for consumers and for the market. If, for instance, the merger increases net efficiencies through the sharing of expensive infrastructure, or if the merger prevents one company's assets from being lost altogether, then these factors would favor approval. We look forward to the antitrust authorities' thorough analysis of the merger's impact on consumers.

The Failed 2002 Merger of DirecTV and Echostar Does Not Provide a Basis for Denying the Merger of XM and Sirius

Some argue that this proposed merger should be denied based on its similarity to the failed 2002 merger of the Direct Broadcast Satellite providers Echostar and Direct TV. But there are significant differences between the two mergers, as well as lessons from the 2002 merger that caution a different result here.

⁷ *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 394 (1956). Although each of these products differs in the technical and legal details of how a user receives audio content, the various products are still competitors to the extent that consumers could migrate from one to another due to a change in price.

⁸ One analyst argues that if XM and Sirius did constitute an entire market, there should be evidence that they are engaging in oligopoly-like behavior, and reaping similar profits. The fact that they are both losing money suggests otherwise. Blair Levin, Rebecca Arbogast, & David Kaut, *XM-Sirius Review: Government Approval Close Call But More Likely Than Not*, STIFEL NICOLAUS TELECOM, MEDIA & TECH Regulatory, Feb. 20, 2007.

The foremost difference between the two mergers is that consumers' options for both audio programming and multichannel video programming have changed drastically over the past five years. Just five years ago, nobody had an iPod jack in their car; cellular phone companies did not provide mobile music services; and WiMax and other mobile Internet services were no more than gleams in technologists' eyes. Similarly, in 2002 neither telephone companies nor webcasters were providing any significant multichannel video services. Given the changes in the multi-channel video market, I am not certain that the Echostar/DirecTV merger would be denied today.

Second, there are important differences between multichannel video and audio services. Most important among these is that many, if not most, subscribers to cable and DBS buy these services to get better (or any) local TV reception.⁹ Thus, "free" over-the-air TV has had little effect on the price of multichannel video services, because consumers do not see one as a replacement for the other, but rather see the multichannel services as a means to receive the free services. This is not the case with multichannel audio services. With a handful of exceptions, local radio stations are not carried on XM and Sirius, and consumers only subscribe to those services because they are willing to pay for content they believe that over-the-air radio does not carry. However, should satellite radio prices rise or competitors such as over-the-air radio provide cheaper and comparable content, there would be much less of a reason for consumers to continue to subscribe to XM or Sirius.

Finally, it could be fairly argued that denying the Echostar/DirecTV merger did not benefit consumers. Supporters of that merger argued that one strong satellite TV

⁹ Before DBS providers were required to carry all local stations if they carried one such station, many rural residents would subscribe to get access to television of any kind, whether local or not.

company would provide better competition to incumbent cable than two weak companies. However, at the behest of News Corporation, which sought to purchase DirecTV, the merger was denied. As a result, cable prices have continued to go up, and two separate, weak DBS companies lack the capacity to provide a competitive broadband service, which is essential to compete with cable. Nor did the DBS companies have the resources to bid successfully for new Advanced Wireless Services spectrum, which might have given them adequate broadband capacity.

I see parallels to the DBS merger here—one strong satellite radio company will be able to push radio broadcasters to provide better, more diverse programming and fewer commercials, particularly as broadcasters provide multiple HD radio streams. This competition could be even stronger if satellite radio providers are permitted to do more local programming, which they are currently prohibited from providing except in narrow circumstances. But two weak companies are unlikely to provide any competitive or political pressure on broadcasters, which goes a long way to explaining that industry's opposition to the merger.

The Proposed Merger Would be in the Public Interest if it is Subject to Conditions Which Promote Diversity, Preserve Consumer Choice and Keep Prices in Check

Even if the merger survives initial antitrust scrutiny, significant competitive concerns remain. Therefore, the public interest would be served only by permitting the merger subject to conditions that promote diversity, preserve consumer choice and keep prices in check.

I reach this conclusion for several reasons. First, over the past several years, both companies have consistently lost money, and subscriber growth has slowed,¹⁰ which makes it less likely that they will take a chance on alternative programming or programming provided to under-served communities. For example, in 2005 XM dropped almost all of its world music channels, including one channel devoted entirely to African music. Around the same time it dropped its alternative Spanish music programming, opting for more popular Spanish fare. The desire to attract the largest number of listeners and the high fixed costs of operating a satellite service will make it difficult for each service, with its relatively small subscriber base, to take chances on alternative programming and/or lower prices. Combining the subscriber base of the two companies would allow the new entity to expand the diversity of its programming to better serve niche preferences of the larger base. Increased program diversity would not only benefit satellite radio customers, it would likely encourage competitors such as broadcast radio to provide more diverse programming.¹¹

Second, consumers would be served by gaining access to channels that they could not receive unless they subscribed to both services. No longer would a consumer have to choose between Major League Baseball and the National Football League, Martha Stewart and Oprah or National Public Radio and XM Public Radio (which features the

¹⁰ See, e.g., Craig Moffett, *XMSR and SIRI: Where to from here?* BERNSTEIN RESEARCH, Feb. 20, 2007, 8-13 (showing projected losses and declining net subscriber growth for both companies). See also Richard Siklos and Andrew Ross Sorkin, *Merger Would End Satellite Radio's Rivalry*, N.Y. TIMES, available at <http://www.nytimes.com/2007/02/20/business/media/20radio.html> (noting combined \$6 billion in losses and slower-than-expected growth). One commentator has surmised that many consumers have hesitated to subscribe to satellite radio services "because they didn't know which company would survive." James Surowiecki, *Satellite Sisters*, THE NEW YORKER, March 19, 2007

¹¹ See, Surowiecki, *supra* note 10.

still-popular former NPR personality Bob Edwards). Moreover, to the extent that the new company will eliminate duplicative channels, there will be more capacity for new and diverse programming (which could even include video programming). In addition, as discussed below, we would urge the FCC to permit the new company to provide increased local programming, including news and public affairs, which would directly compete with over-the-air broadcast radio.

However, the magnitude of this merger indicates that it will increase market concentration to some extent. Existing satellite subscribers may have significant switching costs to other services, and will certainly have no perfect substitutes. In order to ensure that the efficiencies from the merger will in fact result in greater program diversity, increased consumer choice, and better pricing, the merger should only be approved subject to the following three conditions:

- *Consumer Choice.* The new company should make available to its customers tiered program choices. For example, the company could make a music tier or a sports tier available to consumers, which would cost less than subscribing to the entire service.
- *Non-commercial Set-Aside.* The new company should make available 5% of its capacity for noncommercial educational and informational programming over which it will have no editorial control. There is precedent for this kind of non-commercial set-aside. Section 335 of the Communications Act requires a Direct Broadcast Satellite provider to “reserve a portion of its channel capacity, equal to not less than 4 percent nor more than 7 percent, exclusively for non-commercial programming of an educational or informational nature.”¹² This would ensure a diversity of programming choices and would grant access to a national service to programmers who normally would not have any. As with the DBS set-aside, the new company could not fill it with programmers already on its system, and no non-commercial programmer would be able to control more than one of these channels.

¹² 47 U.S.C. § 335(b)(1).

- *Three-Year Freeze on Price Increases.* Because of the expected gains from the merger and because competing services are still nascent, the new company should be prohibited from raising prices for three years after the merger is approved. This price freeze should apply to the combined programming package of the new entity, and not just to the current service of each individual satellite radio provider.¹³

In addition, the FCC should determine whether the new company should divest all or some of the extra 12.5 MHz of spectrum that it will have as a result of the merger. If, as Sirius CEO (and presumptive CEO of the new company) Mel Karmazin has testified, the new company will not be providing local programming even if it is given the authority to do so, there may be no reason for the new company to control double the spectrum that the individual companies have today.

There is a belief among some of that if this merger is approved, then no other merger involving digital media will ever be denied. But that need not be the case if the antitrust authorities and the FCC are clear that the merger is being approved based upon very specific facts and circumstances. This merger involves a national service that has become a luxury item for less than five percent of Americans. As such, approval should have no impact on any questions about any proposed consolidation of local broadcasters.

This Merger Should Not Be Conditioned on any Limits on Consumers' Right to Record Satellite Radio

For the past 18 months, the recording industry and XM Satellite Radio have been engaged in a battle over whether XM should pay an extra licensing fee for selling a

¹³ Ever since Mr. Karmazin promised that the combined company would not raise prices for its service at a February 28 hearing before the House Antitrust Task Force, questions have been raised by FCC Chairman Martin and others about exactly what service would be encompassed in the proposed price freeze. Stephen Labaton, *FCC Chief Questioning Radio Deal*, N.Y. TIMES, Mar. 7, 2007, available at <http://select.nytimes.com/search/restricted/article?res=F10816FB3E550C748CDDAA0894DF404482>.

receiver that allows consumers to record blocks of programming and disaggregate it into individual songs. In the alternative, the recording industry has sought to have XM embed technological protection measures that would prohibit this activity. This dispute is the subject of an ongoing lawsuit in the Second Circuit¹⁴ and pending legislation in the Senate.¹⁵

Public Knowledge is concerned that the recording industry will attempt to use the merger to limit consumers' ability to record satellite radio transmissions. Consumers have been permitted to record radio transmissions since the invention of the tape player, and that ability is specifically protected under the Audio Home Recording Act, 17 U.S.C. § 1001 *et seq.*, which prohibits any copyright infringement action

based on the manufacture, importation, or distribution of a digital audio recording device, a digital audio recording medium, an analog recording device, or an analog recording medium, or *based on the noncommercial use by a consumer of such a device or medium for making digital musical recordings or analog musical recordings.*

(Emphasis added.)

The record companies have questioned whether the Audio Home Recording Act is in need of revision and repeal in light of changing technologies. While this might be a legitimate question, the place to ask that question is before Congress, not in the context of a merger. Moreover, to the extent that such a condition might be sought at the FCC, the federal courts have already ruled that the Commission has no power to require particular

¹⁴ See *Atlantic Recording Corp. v. XM Satellite Radio, Inc.*, No. 06 Civ. 3733 (S.D.N.Y. Jan. 19, 2007).

¹⁵ Platform Equality and Remedies for Rights Holders in Music (PERFORM) Act of 2007, S.256, 110th Cong. (2007).

technological design mandates in the absence of express Congressional authority.¹⁶ Nor does the FCC have the power to require XM to pay a licensing fee in exchange for the ability to sell such receivers.

The Broadcast Industry's Opposition to the Merger is Hypocritical and Anticompetitive

Claiming that it “fully supports competition on a level playing field,” the National Association of Broadcasters opposes this merger for a variety of reasons, including that it would result in “state-sanctioned, monopoly control over the 25 MHz of spectrum allocated to satellite radio service,” that it “will not provide sufficient...public interest benefits,” and that it is “a government bailout for questionable business decisions.”¹⁷

There are many delicious ironies in the NAB's opposition to this merger,¹⁸ but perhaps the most salient to this discussion is that as we speak, the broadcast industry is seeking FCC relief in order to consolidate. And perhaps the primary rationale for requesting that relief is the supposedly uncertain and deteriorating financial state of the broadcast industry.¹⁹

¹⁶ *Am. Library Assoc. v. FCC*, 406 F.3d 689 (D.C. Cir. 2005).

¹⁷ Statement of David K. Rehr, President and CEO, National Association of Broadcasters, Hearing on Competition and the Future of Digital Music, United States House of Representatives, Committee on the Judiciary, Antitrust Task Force, February 28, 2007.

¹⁸ See Gigi Sohn, *From the Unmitigated Gall Department*, PUBLIC KNOWLEDGE POLICY BLOG, <http://www.publicknowledge.org/node/836>. For example, despite its alleged desire for a “level playing field,” the NAB is actively opposing any and all efforts to require their members to pay the same “performance” fees to artists that webcasters and satellite radio pays, going so far as to call that fee a “performance tax.” See <http://www.publicknowledge.org/node/850>

¹⁹ See, e.g., Shira Ovide, *Clear Channel's Profit Declines 54%*, WALL STREET JOURNAL, Feb. 24, 2007 at A6; Associated Press, *Earnings Preview: CBS Corp*, available at <http://www.chron.com/disp/story.mpl/ap/fn/4583381.html>, Feb. 26, 2007 (noting losses in the “troubled radio unit,” apparently caused by “stagnation in the overall radio market”); Comments of the National Association of Broadcasters, FCC Quadrennial Ownership Review, MB Docket No. 06-121 (Filed Oct. 23, 2006) 29-35 available at <http://www.nab.org/Content/ContentGroups/Legal/Filings/2006/QuadrennialOwnership2006Final>

The Committee should take the NAB's opposition for what it is worth—the last in a very long history of broadcaster efforts to place regulatory roadblocks in the path of the satellite broadcast industry. This history started about 15 years ago when broadcasters tried to convince the FCC to impose content and other public interest obligations on satellite radio. It has continued with refusals by at least two broadcast groups to carry satellite radio advertising and by another broadcast group to insist that satellite radio carry advertisements when it programs channels on satellite radio.²⁰ Over the past several years, the broadcast industry has concentrated its efforts to constrain satellite radio at the FCC and in Congress through attempts to limit satellite radio from providing local programming, including weather, traffic and emergency information.²¹

It is no secret that one of the broadcast industry's main goals in opposing this merger is to obtain conditions that would, if not entirely prohibit satellite radio from providing local programming, prevent any increase in that programming. In other words, in order to save local radio, the NAB seeks to have the government prohibit more local radio.

Any conditions on the merger that would limit satellite radio from providing local programming would be profoundly anticompetitive and should be rejected. Setting aside the question of whether "local" broadcasters take seriously their responsibility of serving their local communities with news and public affairs programming (not just traffic and weather), there is no rationale for shielding broadcasters from competing for local

.pdf ("In sum, the combination of competition from cable, satellite, the Internet and other digital technologies is forcing broadcasters to fight even harder in the advertising marketplace.").

²⁰ See Sarah McBride, *Four XM Music Stations Will Start Running Ads*, WALL STREET JOURNAL, Mar. 8, 2006, available at <http://online.wsj.com/article/SB114178705518792190-email.html>; *Clear Channel's New Plan for Satellite Radio: Make it Worse*, TECHDIRT, Mar. 8, 2006, <http://www.techdirt.com/articles/20060308/0836259.shtml>

²¹ See the Local Emergency Radio Service Act of 2007, H.R. 983, 110th Cong. (2007).

viewers and listeners. Indeed, rather than limiting such competition, Congress and/or the FCC should permit satellite radio and other national services to provide more, not less, local programming.²²

Conclusion

The proposed merger of XM Satellite Radio and Sirius Satellite Radio raises complex antitrust questions. If these questions are resolved in favor of the merger, Public Knowledge believes that with conditions that protect consumer choice, promote diverse programming and keep prices in check, the transaction is in the public interest. I would like to thank the Committee again for inviting me to testify and I look forward to any questions you might have.

²²A condition limiting local programming via satellite radio should not be imposed even though Mr. Karmazin has testified that the new company would have no interest in providing such programming. Such a condition would limit the ability of any future satellite radio service or any entity that might in the future purchase the new company to provide local programming, giving broadcasters a “state-sanctioned monopoly control” over local programming.