Testimony of

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Consumers Union is extremely concerned about the enormous concentration of control over multichannel video distribution systems - predominantly cable and satellite - which has prevented the growth of vibrant competition. Attached to our testimony is an Appendix entitled "Cable-Satellite Competition (And Other Myths That Are Distorting Mass Media Policy)," prepared by Dr. Mark Cooper, Research Director for the Consumer Federation of America, which describes in great detail the market structure and concentration levels for multi-channel video services.

Direct broadcast satellite (DBS) stands as the most likely competitor to today's cable monopolies. While further consolidation in the satellite industry could be dangerous to consumers, it also holds the potential to make satellite more competitive with cable monopolies. We believe that antitrust issues related to satellite mergers should be reviewed in the overall context of policies designed to foster more competition in the multichannel video market.

It is important to understand that, while antitrust is an excellent tool to prevent monopolization or substantial dilution of competition, it may do nothing to create new competition or explode existing monopolies. Consumers need both - strong antitrust enforcement and strong pro-competitive policies.

SATELLITE

Over the last three years, there has been a great deal of consolidation within the satellite TV industry. The number-one provider, DirecTV, bought two of its competitors, PrimeStar and United States Broadcasting. Meanwhile, the number-two company, EchoStar, acquired the assets of American Sky Broadcasting.

Today, EchoStar and DirecTV serve nearly every home that has a satellite dish. And now EchoStar is attempting to buy DirecTV.

If this merger is approved, it would combine the dominant players in the satellite TV market to become the second-largest pay-TV company in America, behind AT&T's combined cable holdings. See Appendix at 35 (describing AT&T's full and partial cable ownership interests, covering as many as 30-40 million households).

The potential antitrust problems presented by this merger are serious and substantial. Currently, most consumers have three choices for pay-TV services: EchoStar's Dish Network, DirecTV, or their local cable company. This merger would reduce their choices from three to two. For rural America, the prospects are even grimmer. Approximately 13 million homes in rural areas are not wired for cable TV. These consumers can only choose between DirecTV and EchoStar. Thus, the merger would leave them with EchoStar as their only option.

Therefore, Consumers Union believes that this proposed merger poses significant antitrust problems and must be rejected, unless the problems are adequately addressed before the merger is completed. Under certain circumstances, we also believe the merger could offer consumers some significant benefits, such as more local broadcast channels and better high-speed Internet options available via satellite. We believe that government approval should be contingent on specific market-opening preconditions and protections against anti-competitive practices. These would involve antitrust consent decree requirements to prevent monopolistic pricing and inferior service, plus Federal Communications Commission (FCC) action to encourage competition.

CABLE

To understand the full set of trade-offs related to this proposed merger, we believe that the issues surrounding satellite concentration should be viewed in the overall context of persistent cable monopoly dominating the multi-channel video programming market.

Sixteen percent of American households have satellite dishes, while about 68 percent have cable. A substantial portion of satellite subscribers also purchase cable in order to receive local broadcast programming or to satisfy multiple TV viewing needs. Thus far, satellite has failed to provide price competition to cable. As one industry analyst writes:

We believe that more than 95% of all cable churn is caused by factors other than DBS competition. Competition generated churn rates of just 1.3% per year during the past five years, suggesting that former cable customers make up less than one-third of DBS's current customer base. The implication of this finding is significant because it suggests that the vast preponderance of DBS's growth depended on first-time multi-channel video (MVC) subscribers. We believe that growth in the MVC market will drop off in the next several years as the potential population of first-time MVC subscribers dwindles.

Every year, cable rates keep going through the roof. In the five years since the Telecommunications Act became law, cable subscribers have seen their rates go up 36 percent. That's nearly three times the rate of inflation. Cablevision recently announced a 7 percent rate hike, two weeks after AT&T announced a 7.4 percent hike. In cities all around the country, cable companies are raising rates with an alarming pace. The following are just a sampling of rate increases: Wichita, KS - 14%, St. Louis, MO - 14-26%, Reno, NV and Memphis, TN - 15%, Boston, MA - 12%, Vancouver, WA - 9%, Atlanta, GA and Austin, TX - 10%.

Unfortunately, the 1996 Telecommunications Act phased out cable rate regulation. It gave consumers the impression that cable competition would expand sooner rather than later, and cable prices would go down, not up.

The law assumed that the elimination of legal barriers to entering the cable business would unleash a torrent of competition from local telephone companies, electric utilities and others.

Unfortunately, it just hasn't happened. The local telephone companies have virtually abandoned their efforts to compete with cable, and electric utilities have had difficulty breaking into the market. Without the benefit of regulations that prevent cable price gouging, only consumers in the few communities where two wire-line companies engage in head-to-head competition for cable services are receiving the benefits promised in the 1996 Act. FCC data show that head-to-head competition saves consumers 14 percent compared to prices charged by cable monopolies (where satellite service is also available), and independent research indicates that competition can save consumers as much as 32 percent on their cable bills.

Unfortunately, two-wire towns are the exception to the rule in today's marketplace. Large companies that are well-positioned to block competition increasingly dominate the cable industry. Currently two companies (AT&T and AOL Time Warner) together own cable systems serving more than 50% of the nation's cable subscribers and are partially co-owned through Time Warner Entertainment. In most places, the local cable company is the only cable company. As cable TV pioneer Ted Turner recently said: "I think it's sad we're losing so much diversity of thought and opinion.... We're getting to the point where there's going to be only two cable companies left."

Cable companies often argue that programming costs and capital outlays account for the increase in rates. But these arguments simply do not hold up under scrutiny.

For one, cable industry data show that a substantial portion of the increase in programming costs are offset by corresponding increases in advertising revenue. As programming gets more expensive, cable companies get more revenue from advertisers who run commercials during the programming.

Secondly, the largest cable system operators have financial interests in about one-third of all national and regional programming. So when cable companies complain about having to pay more for programming that they partly own, some are simply taking money of the right pocket and putting it in the left pocket.

Even at the local level, the cable industry's complaint about rising programming costs does not hold water. Since the passage of the 1996 Act, cable revenues have increased much faster than costs. Since 1996, total revenues have increased by 50 percent, while operating revenues are up 43 percent. Average operating revenues (total revenues minus operating costs) have actually increased by 32 percent. Most notably, the revenues that are associated with the expansion of systems -- advertising, pay-per-view and shopping services, advanced services and equipment -- are up 123 percent. The dollar value of revenue increases for new and expanded services since 1997 alone swamps the increase in programming costs. Virtually all of the increases in basic and expanded basic service revenues have been carried to cable's bottom line in the form of increases in operating profits.

COMPETITION
So how does satellite TV stack up against cable? Cable companies may contend that satellite is a serious rival, but evidence shows that, thus far, satellite is not an effective competitor to cable. For most consumers, satellite is still more expensive and less attractive than cable. Installation and multiple TV hookups make satellite significantly more costly than cable. In addition, poor satellite reception is a problem for some consumers in urban areas, and most consumers still cannot get all of their local TV stations from satellite. The attached Appendix illustrates how satellite serves a rural, unwired-niche market (about 40% of satellite subscribers, or approximately 6 million households) and a mega-service market that cable has just entered with

digital services, but satellite fails to compete with cable's 42 million basic and enhanced basic "lunch bucket" customers. See Appendix at 13.

If satellite can provide local channels in more areas and continue to bring down up-front equipment costs, it could be well-positioned to be the most likely competitor to cable in the future.

One of EchoStar's major arguments for a merger with DirecTV is that combining the dominant players of the satellite industry is the only way for them to compete head-to-head with the cable monopolies. We do not believe this combination alone would guarantee that satellite becomes an effective competitor to cable TV. However, the combined companies would have additional satellite capacity to beam local channels into more markets than they do now. They would also be able to reduce costs per subscriber and possibly speed up the availability of high-speed Internet service in rural areas. Once again, all of these would increase the likelihood that satellite could become a price and service competitor to cable.

Nonetheless, the only way that antitrust and other competitive concerns about this merger can be addressed is to require the conditioning of the merger with two significant safeguards.

First, EchoStar should be required to implement a broad array of protections for rural subscribers. The company should have to agree to offer the same prices, terms, and conditions to consumers in rural areas as it does to consumers in more competitive areas. The same installation options, program packages, promotions, and customer service that EchoStar provides in the closest, most competitive markets would then be available where consumers have cable and only one satellite choice. An alternative approach to achieve the same result would require a structural separation (divestiture) of enough satellite capacity to serve rural customers through a new satellite competitor that could challenge the combined Echostar/DirecTV.

The second safeguard we would suggest is aimed at improving competition. If consumers are going to lose one competitor in the multichannel video market, particularly when it means unwired markets will go from two choices to one, the FCC should move forward to open the door to another competitor.

For example, Northpoint/Broadwave is a promising potential competitor to both cable and satellite TV. It is trying to secure a license for its service, but it is caught in a regulatory morass at the FCC. Two of the companies that have pressed the FCC to reject the application are the companies that could see the stiffest competition - EchoStar and AT&T.

The addition of Northpoint/Broadwave or a comparable firm to the marketplace could offset the loss of a satellite competitor as a result of this merger. Therefore, we are asking the FCC to approve licensing of Northpoint/Broadwave -- if the service can be provided without interfering with satellite service -- before the antitrust officials complete their review of this merger.

In conclusion, I would like to recall the last telecommunications merger to receive this kind of attention from Congress - the merger of America Online and Time Warner. Some of you probably remember the antitrust concerns that were raised when AOL first unveiled its merger plans.

I know that former FTC Chairman Pitofsky remembers them well. And thanks to his insight and leadership at the FTC, that merger was transformed from a potential threat to consumers to a model for the protection of consumers.
That merger was very different in many ways from the merger under discussion here today. But they do have at least two things in common.

Like the merger of AOL and Time Warner, the merger of EchoStar and DirecTV presents serious problems that could be dangerous to consumers. But as the government's approval of AOL Time Warner demonstrated, problems can be fixed if the companies and federal officials are willing to do so.

Rather than reject this proposal out of hand, we would urge the federal government to seize an opportunity to improve consumers' standing in the marketplace and bring some sorely-needed competition to the multi-channel video market.