

Testimony of Mr. Mel Karmazin

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**Before the House Energy and Commerce Committee's
Subcommittee on Telecommunications and the
Internet**

**Regarding The Digital Future of the
United States: The Future of Radio**

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Mr. Chairman,

Good afternoon. Thank you, Chairman Markey, Ranking Member Upton, and members of the Telecommunications and Internet Subcommittee for the invitation to talk with you about the future of radio, and how our merger with XM Satellite Radio will strengthen that future.

I'm Mel Karmazin, the CEO of SIRIUS Satellite Radio. Before I came to SIRIUS in 2004, I was president of Viacom, and before that, president of CBS. I've spent almost 40 years in radio, and just about my entire working life in the broadcast industry.

With me here today is Gary Parsons, the chairman of XM. Gary is a veteran of the communications business, a real leader in the world of satellite radio. Gary and I are both looking forward to working together to create an exciting new company.

Gary's leadership and talent are crucial to the future of radio. Gary, together with XM's CEO Hugh Panero, built XM into the success it is today. I should point out that XM has the largest digital radio facility of its kind in the country, and is headquartered right here in Washington where the combined company will continue to have a significant presence.

As this hearing and this panel demonstrate, audio entertainment in the United States is a very competitive and rapidly evolving market. The AM/FM radio broadcasting industry is highly competitive with respect to listeners and advertising revenues. Radio comes as a standard feature in every vehicle manufactured without an additional cost to the consumer. Some radio

stations have begun reducing the number of commercials per hour, expanding the range of music played on the air and experimenting with new formats in order to compete with other stations and satellite radio. Several major radio companies have launched advertising campaigns designed to assert the benefits of traditional local AM/FM radio.

While most traditional AM/FM radio stations broadcast by means of analog signals, the radio industry has made significant strides in rolling out advanced digital transmission technology. Digital broadcasting offers higher sound quality than traditional analog signals and the multicast of as many as five stations per frequency, significantly increasing the quality and quantity of content available to consumers. Digital radio broadcast services have been expanding, and an increasing number of radio stations in the U.S. have begun digital broadcasting or are in the process of converting to digital broadcasting. I understand that over 1,150 radio stations in the United States currently broadcast digitally. Like with traditional radio, digital radio is offered to consumers for free. BMW recently became the first automaker to offer factory-installed HD digital radio receivers as an option across all of its 2007 model year vehicles, and retail HD digital radios are available nationwide at many large retailers, including the nation's largest retailer, Wal-Mart, which announced this week it will begin to sell HD radios.

A number of leading radio broadcasters have joined together to form the HD Digital Radio Alliance to accelerate the successful rollout of digital radio. The HD Digital Radio Alliance has announced a \$250 million on-air advertising campaign to spur the adoption of digital radio.

Internet radio is also becoming a growing force in the market. A 2006 Arbitron study found that weekly listeners increased 50% in just the past year, and now approaches one in five Americans among key demographic segments. Internet radio broadcasts have no geographic limitations and can provide listeners with radio programming from around the country and the world. Improvements from higher bandwidths, faster modems and wider programming selections will make Internet radio an even more significant competitor for listening in the home and office. Technologies like WiMax will also make internet radio more pervasive. In addition to the many free Internet streams, subscription Internet music services offer unlimited and fully-customizable play lists for a small fixed fee per month.

Several of the largest wireless providers currently offer radio-like services music to cellular phones, and a number of phones now contain FM radio receivers. For example, Sprint Nextel currently offers streaming music from a variety of providers plus a music store for purchase; Verizon Wireless offers the V CAST music service that can be played directly on a phone; and AT&T offers a variety of streaming content and has also partnered with Apple to offer the upcoming iPhone. Further, next generation wireless protocols will offer unprecedented broadband coverage and broadcast capabilities.

Lastly, a number of other entities have announced plans to deliver entertainment and media content through cell phones and other wireless devices, including: MediaFLO USA, a subsidiary of QUALCOMM; Modeo LLC, a subsidiary of Crown Castle International Corp.;

HiWire, an affiliate of Aloha Partners; and a joint venture of Sprint Nextel, Comcast, Time Warner Cable, Cox Communications and Advance/Newhouse Communications.

In addition, radio faces competition from numerous recorded media, including CDs, MP3 players and iPods. In fact, a large percentage of the new vehicles produced today come with an auxiliary jack in the radio solely to make MP3 players and iPods easier to use.

Contrast all of this amazing innovation with the market back in 1997, when the FCC granted licenses to SIRIUS and XM. Ten years may not seem long ago, but it was a different era in the evolution of audio entertainment. In 1997 there were no MP3 players, there was no HD radio, there was no Internet radio and no streamed music to cell phones. Satellite radio was in its infancy, and had yet to even launch its satellites or service. The 1997 market is not relevant to business decisions today, and it should not guide policy decisions in 2007. Indeed, if we have learned anything over the last 10 years about technology-driven transformation, it is that the only thing certain about audio entertainment is that it will continue to change rapidly in the years ahead.

So in this fast changing environment, how will the merger of SIRIUS and XM benefit consumers?

- First, it will increase consumer choice. Today, consumers have many choices in the audio market, but for those who choose satellite radio services, there really are only forced choices: You can get great music plus the NFL, NASCAR and Martha

Stewart on SIRIUS; or, Major League Baseball, PGA Golf, Oprah and great music on XM. But if you want all of this, or the best of both, you need to subscribe to two services, buy two radios, and pay two monthly fees. Not surprisingly, only a small number of consumers make this choice. But if our merger is approved, we will offer consumers a much more attractive choice: the best of each service on one radio at a price well below the cost of the two services today.

- Second, we will not raise prices. In fact, we expect to use savings from the synergies of the merger to lower the costs to consumers. In other words, subscribers who want to stay with their current SIRIUS or XM service will be able to do so, and they will not pay any more after the merger. Those who want to take advantage of new services, like the best of both program line-ups, will be able to do so for less than this would cost today – all with their current radio.

I want to emphasize that we view better prices for consumers as a win-win: something that would save consumers money and would strengthen our merged business at the same time. After all, we compete today with free terrestrial radio. About 14 million people have signed up as subscribers for either SIRIUS or XM and now pay \$12.95 per month. The key to getting more subscribers for our merged company is not to widen the price gap between free and \$12.95. Instead, it is to offer consumers a better value – meaning, more quality programming at better prices.

- Third, no radio will become obsolete. After the merger, subscribers will be able to continue receiving either their present or expanded services using the radios they have today. At the same time, we fully expect that the merger will stimulate innovation by concentrating engineering talent and resources and accelerating the development of highly portable, low-cost, easy-to-use, multi-functional devices.
- Fourth, in the long-term the merger will help increase programming diversity. Both SIRIUS and XM already broadcast a wide range of commercial-free music channels, exclusive and non-exclusive sports coverage, news, talk, entertainment and religious programming, channels in Spanish, Korean and French, as well as weather and traffic information for many cities. In the long run, the merger synergies will make it possible to use our channel capacity to enhance this diversity; and
- Fifth, we believe that the merger strengthens competition in the audio entertainment marketplace. Proud as we are of what we have accomplished in 10 years, the fact is that our combined 14 million subscribers translate into about 3.4% of national radio listeners, according to the Fall 2006 Arbitron Survey. Interestingly, Arbitron found that satellite radio listeners are heavy listeners to radio in general, and spend even more time listening to AM/FM radio than they do satellite programming. Compare that to 237 million vehicles with AM/FM radios, 223 million weekly AM and FM listeners, or even the 230 million PCs that can access Internet delivered programming. XM and SIRIUS are relatively small players in a highly competitive and rapidly evolving audio entertainment marketplace: welterweights in an arena of

heavyweights. The merger will make satellite radio a competitor with more choices and better prices, and consumers will be major beneficiaries of these changes.

These commitments to provide more choice, better prices, and utilize today's radio are more than just words. We are prepared at the appropriate time to discuss each of these issues with regulators and to guarantee these benefits as a condition of our merger approval. From our standpoint, these guarantees are not only good for consumers, they also are essential to the long term success of the combined company.

From our inception, satellite radio has been a subscriber-based business dependent on meeting consumer expectations on both price and programming. The dynamic growth in audio technology over the past 10 years has given consumers an impressive array of new and additional choices.

It has only been 10 years since satellite radio was licensed. Could we have predicted 10 years ago that the audio entertainment marketplace would look the way it does now? One reason for all the new technological advancements is that competition in the audio entertainment market is robust. We are seeing new entrants on a regular basis as the market continues to meet the needs of the consumer.

Given the expansive market – within which satellite radio is only one of many alternatives – we are certain that an accelerating level of competition will exist post-merger. There is little doubt that satellite radio faces stiff competition from many of the technologies and

entertainment platforms that I have already described. In fact, I would like to note for the Committee that in the SEC filings of traditional radio companies, they readily acknowledge that they compete with satellite radio in a larger market for audio entertainment:

- From *Clear Channel Communications* 2005 Form 10-K; page 24: **“Our broadcasting businesses face increasing competition from new broadcast technologies, such as broadband wireless and satellite television and radio, and new consumer products, such as portable digital audio players and personal digital video recorders.”**

- From *COX Broadcasting / COX RADIO* 2005 Form 10-K; page 8-9: **“In addition, the radio broadcasting industry is subject to competition from new technologies and services that are being developed or introduced, such as the delivery of audio programming by cable television systems, by satellite digital audio radio service and by digital audio broadcasting. Digital audio broadcasting and satellite digital audio radio service provide for the delivery by terrestrial or satellite means of multiple new audio programming formats with compact disc quality sound to local and national audiences.”**

Clearly, we are in the middle of a rapid evolution of the audio entertainment industry marked by continuing innovation and expanding choice. It is not surprising in such a competitive and changing environment that some competitors would seek to use government to prevent others from gaining any ground. But it is ironic that many who raise questions about our

proposed merger are working overtime themselves to consolidate their own positions in the audio entertainment market.

We are also pleased that the announcement of our merger already has resulted in some welcome harmony. There are few – if any – issues where you’ll find the LOS ANGELES TIMES, the WALL STREET JOURNAL, USA TODAY, and the CHICAGO TRIBUNE in agreement. All four newspapers found that our merger is meritorious. The LA TIMES concluded that the audio entertainment market “is very competitive, particularly among the national players.” USA Today wrote: “the merged entity would represent a more potent competitor to entrenched broadcast interests, one that would offer its customers a more enticing and complete product.”

Chairman Markey, Ranking Member Upton, and members of the Committee, the audio entertainment market today is vibrant, competitive, and innovative, and every indication is that it will be even more so in the future. We believe that the combination of SIRIUS and XM will be good for consumers as it will intensify this competition, expand the choices for consumers and accelerate the pace of innovation in the market. We appreciate this opportunity to share our views with you, and look forward to answering any questions you may have.

Thank you.