

SIRIUS SATELLITE RADIO INC
Form 10-Q
November 08, 2006

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-Q

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2006

Commission file number 0-24710

SIRIUS SATELLITE RADIO INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

52-1700207
(I.R.S. Employer
Identification No.)

**1221 Avenue of the Americas, 36th Floor
New York, New York 10020**
(Address of principal executive offices)
(Zip code)

212-584-5100
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Exchange Act Rule 12b-2).

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer

Indicate by check mark whether the registrant is a shell company (as defined in Exchange Act Rule 12b-2).
Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, \$0.001 par value

1,406,255,531 shares

(Class)

(Outstanding as of November 3, 2006)

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SIRIUS SATELLITE RADIO INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)
(Unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2006	2005	2006	2005
Revenue:				
Subscriber revenue, including effects of mail-in rebates	\$ 155,337	\$ 64,273	\$ 408,154	\$ 155,799
Advertising revenue, net of agency fees	7,130	1,508	22,593	3,094
Equipment revenue	3,579	1,030	10,367	3,300
Other revenue	1,067	20	2,741	48
Total revenue	167,113	66,831	443,855	162,241
Operating expenses (excludes depreciation shown separately below) ⁽¹⁾ :				
Cost of services:				
Satellite and transmission	7,580	7,695	34,279	22,164
Programming and content	79,532	28,397	462,511	78,382
Customer service and billing	14,915	9,556	44,863	27,051
Cost of equipment	6,196	1,453	13,128	4,381
Sales and marketing	49,083	47,823	152,257	137,891
Subscriber acquisition costs	79,812	81,029	329,418	235,576
General and administrative	35,053	20,103	103,261	64,664
Engineering, design and development	21,513	13,135	56,679	50,252
Depreciation	27,583	24,559	78,254	73,640
Total operating expenses	321,267	233,750	1,274,650	694,001
Loss from operations	(154,154)	(166,919)	(830,795)	(531,760)
Other income (expense):				
Interest and investment income	7,750	7,645	26,560	16,922
Interest expense, net of amounts capitalized	(15,921)	(13,693)	(48,705)	(28,219)
Loss from redemption of debt		(6,214)		(6,214)
Equity in net loss of affiliate		(739)	(4,445)	(739)
Other income	5	30	24	82
Total other income (expense)	(8,166)	(12,971)	(26,566)	(18,168)
Loss before income taxes	(162,320)	(179,890)	(857,361)	(549,928)
Income tax expense	(578)	(560)	(1,909)	(1,680)
Net loss	\$ (162,898)	\$ (180,450)	\$ (859,270)	\$ (551,608)
Net loss per share (basic and diluted)	\$ (0.12)	\$ (0.14)	\$ (0.61)	\$ (0.42)
Weighted average common shares outstanding (basic and diluted)	1,405,281	1,328,458	1,398,829	1,322,399

(1) Amounts related to equity granted to third parties and employees included in other operating expenses were as follows:

Satellite and transmission	\$ 490	\$ 467	\$ 2,202	\$ 1,455
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Programming and content	23,615	4,855	297,139	14,793
Customer service and billing	197	140	645	405
Sales and marketing	7,609	9,642	14,878	30,348
Subscriber acquisition costs	(1,051)	12,354	30,748	31,115
General and administrative	11,536	6,137	38,947	21,746
Engineering, design and development	1,022	3,351	10,734	17,020
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total equity granted to third parties and employees	\$ 43,418	\$ 36,946	\$ 395,293	\$ 116,882
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

See Notes to Unaudited Consolidated Financial Statements.

SIRIUS SATELLITE RADIO INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share amounts)

	<u>September 30, 2006</u>	<u>December 31, 2005</u>
	(Unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 317,876	\$ 762,007
Marketable securities	34,425	117,250
Accounts receivable, net of allowance for doubtful accounts of \$2,899 and \$1,550 at September 30, 2006 and December 31, 2005, respectively	17,291	31,688
Inventory	44,979	14,256
Prepaid expenses	64,432	18,248
Restricted investments	25,000	25,165
Other current assets	30,973	42,834
Total current assets	534,976	1,011,448
Property and equipment, net	833,599	828,357
FCC license	83,654	83,654
Restricted investments, net of current portion	58,300	82,450
Deferred financing fees	14,123	16,303
Other long-term assets	85,964	63,150
Total assets	\$ 1,610,616	\$ 2,085,362
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	\$ 314,242	\$ 331,953
Accrued interest	13,083	23,546
Deferred revenue	314,080	251,468
Total current liabilities	641,405	606,967
Long-term debt	1,083,929	1,084,437
Deferred revenue, net of current portion	69,536	56,479
Other long-term liabilities	16,046	12,511
Total liabilities	1,810,916	1,760,394
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Common stock, \$0.001 par value: 2,500,000,000 shares authorized, 1,405,667,870 and 1,346,226,851 shares issued and outstanding at September 30, 2006 and December 31, 2005, respectively	1,406	1,346
Additional paid-in capital	3,386,417	3,079,169
Deferred compensation		(26,694)
Accumulated deficit	(3,588,123)	(2,728,853)
Total stockholders' (deficit) equity	(200,300)	324,968
Total liabilities and stockholders' equity	\$ 1,610,616	\$ 2,085,362

See Notes to Unaudited Consolidated Financial Statements.

SIRIUS SATELLITE RADIO INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(In thousands, except share and per share amounts)
(Unaudited)

	Common Stock		Additional Paid-In Capital	Deferred Compensation	Accumulated Deficit	Total
	Shares	Amount				
Balances, December 31, 2005	1,346,226,851	\$ 1,346	\$ 3,079,169	\$ (26,694)	\$ (2,728,853)	\$ 324,968
Net loss					(859,270)	(859,270)
Issuance of common stock to employees and employee benefit plans	19,885,673	20	19,535			19,555
Issuance of common stock to third parties	34,467,869	35	224,917			224,952
Compensation in connection with the issuance of stock-based awards			85,205			85,205
Reversal of deferred compensation related to the adoption of Statement of Financial Accounting Standards (SFAS) No.123R			(26,694)	26,694		
Exercise of options, \$0.47 to \$3.93 per share	2,764,476	3	3,785			3,788
Exercise of warrants, \$2.392 per share	1,954,886	2	(2)			
Exchange of 3½% Convertible Notes due 2008, including accrued interest	368,115		502			502
Balances, September 30, 2006	1,405,667,870	\$ 1,406	\$ 3,386,417	\$	\$ (3,588,123)	\$ (200,300)

See Notes to Unaudited Consolidated Financial Statements.

SIRIUS SATELLITE RADIO INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	For the Nine Months Ended September 30,	
	2006	2005
Cash flows from operating activities:		
Net loss	\$ (859,270)	\$ (551,608)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	78,254	73,640
Non-cash interest expense	2,332	2,365
Provision for doubtful accounts	5,687	3,294
Non-cash loss from redemption of debt		712
Loss on disposal of assets	889	286
Impairment loss	10,917	
Equity granted to third parties and employees	395,293	116,882
Deferred income taxes	1,909	1,680
Changes in operating assets and liabilities:		
Marketable securities		16
Accounts receivable	8,710	(9,455)
Inventory	(30,723)	(5,413)
Prepaid expenses and other current assets	(34,564)	(14,613)
Other long-term assets	(21,674)	3,131
Accounts payable and accrued expenses	(70,974)	36,331
Accrued interest	(10,460)	6,341
Deferred revenue	75,669	81,805
Other long-term liabilities	(8,051)	(3,522)
Net cash used in operating activities	(456,056)	(258,128)
Cash flows from investing activities:		
Additions to property and equipment	(94,368)	(17,949)
Sales of property and equipment	123	65
Purchases of restricted and other investments	(5,700)	(6,291)
Release of restricted investments	25,000	10,997
Purchases of available-for-sale securities	(118,500)	(128,700)
Sales of available-for-sale securities	201,340	9,935
Net cash provided by (used in) investing activities	7,895	(131,943)
Cash flows from financing activities:		
Proceeds from issuance of long-term debt, net		493,005
Redemption of debt		(57,609)
Proceeds from exercise of stock options	4,030	11,125
Other		(8)
Net cash provided by financing activities	4,030	446,513
Net (decrease) increase in cash and cash equivalents	(444,131)	56,442
Cash and cash equivalents at the beginning of period	762,007	753,891
Cash and cash equivalents at the end of period	\$ 317,876	\$ 810,333

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Supplemental Disclosure of Cash and Non-Cash Flow Information

Cash paid during the period for:

Interest, net of amounts capitalized	\$	56,952	\$	19,511
Income taxes		472		134
Non-cash operating activities:				
Common stock issued in satisfaction of accrued compensation		7,243		4,824
Non-cash investing and financing activities:				
Common stock issued in exchange of 3½% Convertible Notes due 2008, including accrued interest		502		2,177
Common stock issued to third parties		224,952		

See Notes to Unaudited Consolidated Financial Statements.

SIRIUS SATELLITE RADIO INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands, unless otherwise stated)
(Unaudited)

1. Business

We are a satellite radio provider in the United States. We currently broadcast 133 channels of programming to listeners across the country. We offer 69 channels of 100% commercial-free music and feature 64 channels of sports, news, talk, entertainment, traffic and weather for a monthly subscription fee of \$12.95.

We broadcast through our proprietary satellite radio system, which currently consists of three orbiting satellites, 139 terrestrial repeaters that receive and retransmit our signal, a satellite uplink facility and our studios. Subscribers receive our service through SIRIUS radios, which are sold by automakers, consumer electronics retailers, mobile audio dealers and through our website. Subscribers can also receive our music channels and certain other channels over the Internet. As of September 30, 2006, we had 5,119,308 subscribers.

Our music channels are available to DISH satellite television subscribers and certain of our music channels are offered to Sprint subscribers over multi-media handsets. We also offer traffic and weather data services for a separate fee. Subscribers to DISH satellite television, Sprint and our traffic and weather data services are not included in our subscriber count.

In 2005, SIRIUS Canada Inc., a Canadian corporation owned by us, Canadian Broadcasting Corporation and Standard Broadcasting Corporation, received a license from the Canadian Radio-television and Telecommunications Commission to offer a satellite radio service in Canada. In December 2005, SIRIUS Canada launched service in Canada with 100 channels of commercial-free music and news, sports, talk and entertainment programming, including 10 channels of Canadian content. Subscribers to the SIRIUS Canada service are not included in our subscriber count.

2. Principles of Consolidation and Basis of Presentation

The accompanying unaudited consolidated financial statements of Sirius Satellite Radio Inc. and subsidiaries have been prepared in accordance with U.S. generally accepted accounting principles and the instructions to Form 10-Q and Article 10 of Regulation S-X for interim financial reporting. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. All intercompany transactions have been eliminated in consolidation.

In presenting unaudited consolidated financial statements, management makes estimates and assumptions that affect the amounts reported and related disclosures. Estimates, by their nature, are based on judgment and available information. Actual results could differ from those estimates. In the opinion of management, all normal recurring adjustments necessary for a fair presentation of the consolidated financial statements as of September 30, 2006 and December 31, 2005, and for the three and nine months ended September 30, 2006 and 2005, have been recorded. The results of operations for the three and nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the full year. Our unaudited consolidated financial statements should be read together with our consolidated financial statements and footnotes contained in our Annual Report on Form 10-K for the year ended December 31, 2005.

3. Summary of Significant Accounting Policies

Revenue Recognition

Revenue from subscribers consists of subscription fees, including revenues associated with prepaid subscriptions included in the sale or lease price of a new vehicle; revenue derived from our agreement with Hertz; non-refundable activation fees; and the effects of mail-in rebates.

We recognize subscription fees as our service is provided to a subscriber. We record deferred revenue for prepaid subscription fees and amortize these prepayments to revenue ratably over the term of the respective subscription plan.

At the time of sale, vehicle owners purchasing or leasing a vehicle with a subscription to our service typically receive between a six month and one year prepaid subscription. We receive payment from automakers for

SIRIUS SATELLITE RADIO INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued
(Dollar amounts in thousands, unless otherwise stated)
(Unaudited)

these subscriptions in advance of our service being activated. Such prepayments are recorded to deferred revenue and amortized to revenue ratably over the service period upon activation. We also reimburse the automakers for certain costs associated with the SIRIUS radio installed in the applicable vehicle at the time the vehicle is manufactured. The associated payments to the automakers are included in subscriber acquisition costs. Although we receive payments from the automakers, they do not resell our service; rather, automakers facilitate the sale of our service to our customers, acting similar to an agent. We believe this is the appropriate characterization of our relationship since we are responsible for providing service to our customers including being obligated to the customer if there was interruption of service.

Activation fees are recognized ratably over the estimated term of a subscriber relationship, currently estimated to be 3.5 years. The estimated term of a subscriber relationship is based on market research and management's judgment and, if necessary, will be refined in the future as historical data becomes available.

As required by Emerging Issues Task Force (EITF) No. 01-09, Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products), an estimate of mail-in rebates that are paid by us directly to subscribers is recorded as a reduction to subscriber revenue in the period the subscriber activates our service. We estimate the effects of mail-in rebates based on actual take-rates for rebate incentives offered in prior periods, adjusted based on any current take-rate data available at the time. In subsequent periods, estimates are adjusted when necessary.

We recognize revenues from the sale of advertising on our non-music channels as the advertising is broadcast. Agency fees are calculated based on a stated percentage applied to gross billing revenue for our advertising inventory and are reported as a reduction of advertising revenue. Advertising revenue includes advertising sold in exchange for goods or services (barter) recorded at fair value. Revenue from barter transactions is recognized when the advertising is broadcast and goods or services exchanged are received. Goods or services received are charged to expense when received and/or used. Barter transactions are not significant to our unaudited consolidated financial statements. We pay certain third parties a percentage of advertising revenue. Advertising revenue is recorded gross of such revenue share payments in accordance with EITF No. 99-19, Reporting Revenue Gross as a Principal versus Net as an Agent, as we are the primary obligor in the transaction. Advertising revenue share payments are recorded to programming and content expense during the period in which the advertising is broadcast.

Equipment revenue from the direct sale of SIRIUS radios and accessories is recognized upon shipment. Shipping and handling costs billed to customers are recorded as revenue. Shipping and handling costs associated with shipping goods to customers are recorded to cost of equipment.

EITF No. 00-21, Accounting for Revenue Arrangements with Multiple Deliverables, provides guidance on how and when to recognize revenues for arrangements that may involve the delivery or performance of multiple products, services and/or rights to use assets. Revenue arrangements with multiple deliverables are required to be divided into separate units of accounting if the deliverables in the arrangement meet certain criteria. Arrangement consideration must be allocated among the separate units of accounting based on their relative fair values.

We determined that the sale of our service through our direct to consumer channel with accompanying equipment constitutes a revenue arrangement with multiple deliverables. In these types of arrangements, amounts received for equipment are recognized as equipment revenue; amounts received for service are recognized as subscription revenue; and amounts received for the non-refundable, up-front activation fee that are not contingent on the delivery of the service are allocated to equipment revenue. Activation fees are recorded to equipment revenue only to the extent that the aggregate equipment and activation fee proceeds do not exceed the fair value of the equipment. Any activation fees not allocated to the equipment are deferred upon activation and recognized as subscription revenue on a straight-line basis over the estimated term of a subscriber relationship.

Stock-Based Compensation

Effective January 1, 2006, we adopted the provisions of SFAS No. 123 (revised 2004), Share-Based Payment (SFAS No. 123R), using the modified prospective transition method. Prior periods are not restated under this transition method. The stock-based compensation cost recognized beginning January 1, 2006 includes compensation cost for all stock-based awards granted to employees and members of our board of directors (i) prior to, but not vested as of, January 1, 2006 based on the grant date fair value originally estimated in accordance with

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SIRIUS SATELLITE RADIO INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued
(Dollar amounts in thousands, unless otherwise stated)
(Unaudited)

the provisions of SFAS No. 123, Accounting for Stock-Based Compensation, and (ii) subsequent to December 31, 2005 based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123R. Compensation cost under SFAS No. 123R is recognized ratably using the straight-line attribution method over the expected vesting period.

SFAS No. 123R requires forfeitures to be estimated on the grant date and revised in subsequent periods if actual forfeitures differ from those estimates. Prior to the adoption of SFAS No. 123R we accounted for forfeitures as they occurred. For pro forma disclosure purposes in accordance with SFAS No. 123, we estimated forfeitures. As of January 1, 2006, the cumulative effect of adopting the estimated forfeiture method was not significant.

Prior to January 1, 2006, we used the intrinsic value method to measure the compensation cost of stock-based awards granted to employees and members of our board of directors in accordance with Accounting Principles Board Opinion (APB) No. 25, Accounting for Stock Issued to Employees. Accordingly, we recorded compensation expense for stock-based awards granted to employees and members of our board of directors over the vesting period equal to the excess of the market price of the underlying common stock at the date of grant over the exercise price of the stock-based award. The intrinsic value of restricted stock units as of the date of grant was amortized to expense over the vesting period. We accounted for modifications to stock-based awards in accordance with Financial Accounting Standards Board Interpretation (FIN) No. 44, Accounting for Certain Transactions Involving Stock Compensation. FIN No. 44 provided that when the modification of a stock-based award occurred, a new measurement date resulted because the modification allowed an employee to vest in an award that would have otherwise been forfeited pursuant to the original terms. In accordance with FIN No. 44, we also recorded compensation charges or benefits related to repriced stock options based on the market value of our common stock until the repriced stock options were exercised, forfeited or expired.

The following table reflects net loss and net loss per share had stock-based compensation to employees and members of our board of directors been recorded based on the fair value method under SFAS No. 123 for the periods set forth below:

	For the Three Months Ended September 30, 2005	For the Nine Months Ended September 30, 2005
Net loss as reported	\$ (180,450)	\$ (551,608)
Stock-based compensation to employees and members of our board of directors	11,027	38,331
Stock-based compensation to employees and members of our board of directors pro forma	(22,066)	(72,617)
Net loss pro forma	<u>\$ (191,489)</u>	<u>\$ (585,894)</u>
Net loss per share:		
Basic and diluted as reported	\$ (0.14)	\$ (0.42)
Basic and diluted pro forma	\$ (0.14)	\$ (0.44)

Under SFAS No. 123R, we recognized \$16,254 and \$56,525 of compensation cost for stock-based awards granted to employees and members of our board of directors for the three and nine months ended September 30, 2006, respectively. Total unrecognized compensation related to unvested stock-based awards granted to employees and members of our board of directors at September 30, 2006, net of estimated forfeitures, is \$117,936 and is expected to be recognized over a weighted-average period of three years.

Prior to January 1, 2006, we accounted for stock-based awards granted to non-employees, other than non-employee members of our board of directors, at fair value in accordance with SFAS No. 123. Effective January 1, 2006, we account for such awards at fair value in accordance with SFAS No. 123R and SEC guidance contained in Staff Accounting Bulletin (SAB) No. 107. The fair value of equity instruments granted to non-employees is measured in accordance with EITF No. 96-18, Accounting for Equity Instruments That are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services. The final measurement date of equity instruments with performance criteria is the date that each performance commitment for such equity instrument is satisfied.

SIRIUS SATELLITE RADIO INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued
(Dollar amounts in thousands, unless otherwise stated)
(Unaudited)

Stock-based awards granted to employees, non-employees and members of our board of directors generally include warrants, stock options, restricted stock and restricted stock units. Charges associated with such stock-based awards are referred to by us as equity granted to third parties and employees.

Upon adoption of SFAS No. 123R, we continued to estimate the fair value of stock-based awards using the Black-Scholes option valuation model (Black-Scholes). Black-Scholes was developed to estimate the fair market value of traded options, which have no vesting restrictions and are fully transferable. Option valuation models require the input of highly subjective assumptions. Because our stock-based awards have characteristics significantly different from those of traded options and because changes in the subjective assumptions can materially affect the fair market value estimate, the existing option valuation models do not necessarily provide a reliable single measure of the fair value of our stock-based awards.

Fair value determined using Black-Scholes varies based on assumptions used for the expected life, expected stock price volatility and risk-free interest rates. For the nine months ended September 30, 2005, we used historical volatility of our stock over a period equal to the expected life of stock-based awards to estimate fair value. SAB No. 107 favors using a market value of volatility. We estimated the fair value of awards granted during the nine months ended September 30, 2006 using the implied volatility of actively traded options on our stock. We believe that implied volatility is more representative of future stock price trends than historical volatility. The expected life assumption represents the weighted-average period stock-based awards are expected to remain outstanding. These expected life assumptions are established through a review of historical exercise behavior of stock-based award grants with similar vesting periods. Where historical patterns do not exist contractual terms are used. The risk-free interest rate represents the daily treasury yield curve rate at the reporting date based on the closing market bid yields on actively traded U.S. treasury securities in the over-the-counter market for the expected term. Our assumptions may change in future periods.

The following table summarizes the weighted-average assumptions used to compute reported and pro forma stock-based compensation to employees and members of our board of directors for the periods set forth below:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2006	2005	2006	2005
		(pro forma)		(pro forma)
Risk-free interest rate	4.81%	4.12%	4.19%	4.05%
Expected life of options years	4.45	5.59	4.45	5.54
Expected stock price volatility	60%	112%	60%	112%
Expected dividend yield	N/A	N/A	N/A	N/A

The following table summarizes the range of assumptions used to compute reported and pro forma stock-based compensation to third parties, other than non-employee members of our board of directors, for the periods set forth below:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2006	2005	2006	2005
Risk-free interest rate	4.59-4.99%	3.66-4.34%	4.29-5.23%	2.83-4.50%
Expected life of options years	2.50-9.73	1.00-9.27	1.67-10.00	1.00-9.45
Expected stock price volatility	60%	59-116%	60%	57-116%
Expected dividend yield	N/A	N/A	N/A	N/A

SFAS No. 123R changes the presentation of realized excess tax benefits associated with the exercise of stock options in the statements of cash flows. Excess tax benefits are realized tax benefits from tax deductions for the exercise of stock options in excess of the deferred tax asset attributable to stock compensation expense for such options. Prior to the adoption of SFAS No. 123R, such realized tax benefits were required to be presented as operating cash flows. SFAS No. 123R requires such realized tax benefits to be presented as part of cash flows from financing activities. No income tax benefits have been realized from stock option exercises during the three and nine months ended September 30, 2006 and 2005 because a valuation allowance was maintained for all net deferred tax assets.

SIRIUS SATELLITE RADIO INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued
(Dollar amounts in thousands, unless otherwise stated)
(Unaudited)

Research and Development Costs

Research and development costs are expensed as incurred. Research and development costs for the three months ended September 30, 2006 and 2005 were \$12,431 and \$6,291, respectively, and \$26,575 and \$22,119 for the nine months ended September 30, 2006 and 2005, respectively. These costs are included in engineering, design and development expenses in our accompanying unaudited consolidated statements of operations.

Net (Loss) Income Per Share

We compute net (loss) income per share in accordance with SFAS No. 128, Earnings Per Share. Basic net (loss) income per share is calculated using the weighted average common shares outstanding during each reporting period. Diluted net (loss) income per share adjusts the weighted average common shares outstanding for the potential dilution that could occur if common stock equivalents (convertible debt, warrants, stock options and restricted stock units) were exercised or converted into common stock. Common stock equivalents of approximately 193,000,000 and 197,000,000 for the three and nine months ended September 30, 2006, respectively, and 239,000,000 and 235,000,000 for the three and nine months ended September 30, 2005, respectively, were not considered in the calculation of diluted net loss per share as the effect would have been anti-dilutive.

Comprehensive (Loss) Income

We report comprehensive (loss) income in accordance with SFAS No. 130, Reporting Comprehensive Income. SFAS No. 130 established a standard for reporting and displaying other comprehensive (loss) income and its components within financial statements. Unrealized gains and losses on available-for-sale securities are the only component of our other comprehensive loss. Comprehensive loss for the three months ended September 30, 2006 and 2005 was \$162,898 and \$180,450, respectively, and \$859,270 and \$551,584 for the nine months ended September 30, 2006 and 2005, respectively.

Marketable Securities

We account for marketable securities in accordance with the provisions of SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities. Marketable securities consist of certificates of deposit and auction rate securities. The basic objectives of our investment policy are the preservation of capital, maintaining sufficient liquidity to meet operating requirements and maximizing yield. We classify our marketable securities as available-for-sale securities. Available-for-sale securities are carried at fair market value. Unrealized gains and losses are included in accumulated other comprehensive (loss) income as a separate component of stockholders' equity. Realized gains and losses, dividends and interest income, including amortization of the premium and discount arising at purchase, are included in interest and investment income. The specific-identification method is used to determine the cost of all securities and the basis by which amounts are reclassified from accumulated comprehensive (loss) income into earnings. While the underlying securities of auction rate securities have contractual maturities of more than 20 years, the interest rates on such securities reset at intervals of 28 or 35 days. Auction rate securities are priced and subsequently trade as short-term investments because of such interest rate reset feature.

We received proceeds from the sale or maturity of marketable securities of \$201,340 and \$9,935 for the nine months ended September 30, 2006 and 2005, respectively. There were no unrealized holding gains or losses on marketable securities as of September 30, 2006 and December 31, 2005.

Restricted Investments

As of September 30, 2006 and December 31, 2005, short-term restricted investments of \$25,000 and \$25,165, respectively, primarily included certificates of deposit placed in escrow for the benefit of a third party pursuant to a programming agreement.

As of September 30, 2006 and December 31, 2005, long-term restricted investments of \$58,300 and \$82,450, respectively, primarily included certificates of deposit and money market funds deposited in escrow for the benefit of third parties pursuant to programming agreements and certificates of deposit placed in escrow to secure our reimbursement obligations under letters of credit issued for the benefit of lessors of office space.

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Property and Equipment

Property and equipment is stated at cost and depreciated on a straight-line basis over the estimated useful lives of the related assets, which range from 2 to 30 years. Our satellite system is depreciated on a straight-line basis over the respective remaining useful lives of our satellites from the date we launched our service in February 2002, or, in the case of our spare satellite, from the date it was delivered to ground storage in April 2002. Leasehold improvements and equipment under capital leases is depreciated using the straight-line method over the lesser of the lease term or the estimated useful life. We capitalize a portion of the interest on funds borrowed to finance the construction and launch of our satellites. Capitalized interest is recorded as part of the asset's cost and depreciated over the satellite's useful life. Capitalized interest costs for the three and nine months ended September 30, 2006 were \$1,134 and \$2,532, respectively. We had no capitalized interest for the three and nine months ended September 30, 2005.

The expected useful lives of our three in-orbit satellites were originally 15 years from the date they were placed into orbit. In June 2006, we entered into an agreement with Space Systems/Loral to design and construct a new satellite. In connection with this agreement, we adjusted the useful lives of two of our in-orbit satellites to 13 years to reflect the way we intend to operate the constellation. We continue to expect our spare satellite to operate effectively for 15 years from the date of launch.

Our satellites have experienced circuit failures on their solar arrays. We continue to monitor the operating condition of our satellites. If events or circumstances indicate that the useful lives of our satellites have changed we will modify the depreciable life accordingly.

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we review our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset is not recoverable. At the time an impairment in value of a long-lived asset is identified, the impairment is measured as the amount by which the carrying amount of a long-lived asset exceeds its fair value. To determine fair value, we employ an expected present value technique, which utilizes multiple cash flow scenarios that reflect the range of possible outcomes and an appropriate discount rate.

In connection with our new satellite agreement, in June 2006 we wrote-off \$10,917 for the net book value of certain satellite long-lead time parts purchased in 1999 that we will no longer need.

Reclassifications

Certain amounts in the prior period unaudited consolidated financial statements have been reclassified to conform to the current period presentation, including the reclassification of equity granted to third parties and employees from a separate line item disclosure to being included in other operating expense line items in order to comply with the requirements of SFAS No. 123R.

Recent Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value and expands the related disclosure requirements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and for interim periods within those years. We do not believe the adoption of SFAS No. 157 will have a material impact on our consolidated results of operations or financial position.

In September 2006, the EITF issued EITF No. 06-1, *Accounting for Consideration Given by a Service Provider to Manufacturers or Resellers of Equipment Necessary for an End-Customer to Receive Service from the Service Provider*. The EITF concluded that if consideration given by a service provider to a third-party manufacturer or a reseller that is not the service provider's customer can be linked contractually to the benefit received by the service provider's customer, a service provider should account for the consideration in accordance with EITF No. 01-9, *Accounting for Consideration Given by a Vendor to a Customer*. EITF No. 06-1 is effective for annual reporting periods beginning after June 15, 2007. We are currently evaluating the effects that EITF No. 06-1 will have on our consolidated results of operations and financial position.

In June 2006, the EITF issued EITF No. 06-3, *How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation)*, to clarify diversity in practice on the presentation of different types of taxes in the financial statements. The EITF concluded that for taxes within the scope of the issue, a company may include charges to customers for taxes within revenues and the charge for the taxes from the taxing authority within cost of sales, or, alternatively, it may net the charge to the customer and the charge from the taxing authority. If taxes subject to EITF No. 06-3 are significant, a

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company is required to disclose its accounting policy for presenting taxes and the amounts of such taxes that are recognized on a gross basis. EITF No. 06-3 is effective for the first interim reporting period beginning after December 15, 2006. We will adopt EITF No. 06-3 effective January 1, 2007. We do not believe the adoption of EITF No. 06-3 will have a material impact on our consolidated results of operations or financial position.

In June 2006, the FASB issued FIN No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109, which prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return, as well as criteria on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN No. 48 is effective for fiscal years beginning after December 15, 2006. We will adopt FIN No. 48 effective January 1, 2007. We do not believe the adoption of FIN No. 48 will have a material impact on our consolidated results of operations or financial position.

4. Subscriber Revenue

Subscriber revenue consists of subscription fees, non-refundable activation fees and the effects of mail-in rebates. Revenues received from automakers for prepaid subscriptions included in the sale or lease price of a new vehicle are also included in subscriber revenue over the service period.

Subscriber revenue consists of the following:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2006	2005	2006	2005
Subscription fees	\$ 153,192	\$ 63,920	\$ 407,203	\$ 154,575
Activation fees	3,955	1,858	11,326	4,742
Effect of mail-in rebates	(1,810)	(1,505)	(10,375)	(3,518)
Total subscriber revenue	<u>\$ 155,337</u>	<u>\$ 64,273</u>	<u>\$ 408,154</u>	<u>\$ 155,799</u>

5. Interest Costs

During the three and nine months ended September 30, 2006, we capitalized a portion of the interest on funds borrowed to finance the construction and launch of our new satellite. The following is a summary of our interest cost:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2006	2005	2006	2005
Interest costs charged to expense	\$ 15,921	\$ 13,693	\$ 48,705	\$ 28,219
Interest costs capitalized	1,134		2,532	
Total interest costs incurred	<u>\$ 17,055</u>	<u>\$ 13,693</u>	<u>\$ 51,237</u>	<u>\$ 28,219</u>

6. Long-Term Debt

Long-term debt consists of the following:

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	Conversion Price (per share)	As of	
		September 30, 2006	December 31, 2005
9 ⁵ / ₈ % Senior Notes due 2013	N/A	\$ 500,000	\$ 500,000
3 ¹ / ₄ % Convertible Notes due 2011	\$ 5.30	230,000	230,000
2 ¹ / ₂ % Convertible Notes due 2009	4.41	300,000	300,000
3 ¹ / ₂ % Convertible Notes due 2008	1.38	52,185	52,693
8 ³ / ₄ % Convertible Subordinated Notes due 2009	28.4625	1,744	1,744
Total long-term debt		\$ 1,083,929	\$ 1,084,437

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9⁵/₈% Senior Notes due 2013

In August 2005, we issued \$500,000 in aggregate principal amount of our 9⁵/₈% Senior Notes due 2013 resulting in net proceeds of \$493,005. Our 9⁵/₈% Senior Notes due 2013 mature on August 1, 2013 and interest is payable semi-annually on February 1 and August 1 of each year. The obligations under our 9⁵/₈% Senior Notes due 2013 are not secured by any of our assets.

In September 2005, we used proceeds from the issuance of our 9⁵/₈% Senior Notes due 2013 to redeem our outstanding 15% Senior Secured Discount Notes due 2007 and our 14¹/₂% Senior Secured Notes due 2009, including accrued interest. The obligations under our 15% Senior Secured Discount Notes due 2007 and 14¹/₂% Senior Secured Notes due 2009 were secured by liens on certain of our assets. These liens were released in connection with the redemption of the notes.

3¹/₄% Convertible Notes due 2011

In October 2004, we issued \$230,000 in aggregate principal amount of our 3¹/₄% Convertible Notes due 2011 resulting in net proceeds of \$224,813. These notes are convertible, at the option of the holder, into shares of our common stock at any time at a conversion rate of 188.6792 shares of common stock for each \$1,000.00 principal amount, or \$5.30 per share of common stock, subject to certain adjustments. Our 3¹/₄% Convertible Notes due 2011 mature on October 15, 2011 and interest is payable semi-annually on April 15 and October 15 of each year. The obligations under our 3¹/₄% Convertible Notes due 2011 are not secured by any of our assets.

2¹/₂% Convertible Notes due 2009

In February 2004, we issued \$250,000 in aggregate principal amount of our 2¹/₂% Convertible Notes due 2009 resulting in net proceeds of \$244,625. In March 2004, we issued an additional \$50,000 in aggregate principal amount of our 2¹/₂% Convertible Notes due 2009 pursuant to an option granted in connection with the initial offering of the notes, resulting in net proceeds of \$48,975. These notes are convertible, at the option of the holder, into shares of our common stock at any time at a conversion rate of 226.7574 shares of common stock for each \$1,000.00 principal amount, or \$4.41 per share of common stock, subject to certain adjustments. Our 2¹/₂% Convertible Notes due 2009 mature on February 15, 2009 and interest is payable semi-annually on February 15 and August 15 of each year. The obligations under our 2¹/₂% Convertible Notes due 2009 are not secured by any of our assets.

3¹/₂% Convertible Notes due 2008

In May 2003, we issued \$201,250 in aggregate principal amount of our 3¹/₂% Convertible Notes due 2008 resulting in net proceeds of \$194,224. These notes are convertible, at the option of the holder, into shares of our common stock at any time at a conversion rate of 724.6377 shares of common stock for each \$1,000.00 principal amount, or \$1.38 per share of common stock, subject to certain adjustments. Our 3¹/₂% Convertible Notes due 2008 mature on June 1, 2008 and interest is payable semi-annually on June 1 and December 1 of each year. The obligations under our 3¹/₂% Convertible Notes due 2008 are not secured by any of our assets.

During the nine months ended September 30, 2006, holders of \$508 in aggregate principal amount of our 3¹/₂% Convertible Notes due 2008 presented such notes for conversion in accordance with the terms of the indenture. We issued 368,115 shares of our common stock upon conversion of these notes.

Space Systems/Loral Credit Agreement

In June 2006, we entered into a Credit Agreement with Space Systems/Loral. Under the Credit Agreement, Space Systems/Loral has agreed to make loans to us in an aggregate principal amount of up to \$100,000 to finance the purchase of our new satellite. Loans made under the Credit Agreement will be secured by our rights under the Satellite Purchase Agreement with Space Systems/Loral, including our rights to the new satellite. The loans are also entitled to the benefits of a subsidiary guarantee from Satellite CD Radio, Inc., our subsidiary that holds our FCC license, and any future material subsidiary that may be formed by us. The maturity date of the loans is the earliest to occur of (i) April 6, 2009, (ii) 90 days after the new satellite becomes available for shipment and (iii) 30 days prior to the scheduled launch of the new satellite. Any loans made under the Credit Agreement generally will bear interest at a variable rate equal to three-month LIBOR plus 4.75%. The Credit Agreement permits us to prepay all or a portion of the loans outstanding without penalty. We have no current plans to draw under this Credit Agreement.

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Covenants and Restrictions

Our 9⁵/₈% Senior Notes due 2013 and the Credit Agreement require us to comply with certain covenants that restrict our ability to, among other things, (i) incur additional indebtedness, (ii) incur liens, (iii) pay dividends or make certain other restricted payments, investments or acquisitions, (iv) enter into certain transactions with affiliates, (v) merge or consolidate with another person, (vi) sell, assign, lease or otherwise dispose of all or substantially all of our assets, and (vii) make voluntary prepayments of certain debt, in each case subject to exceptions as provided in the 9⁵/₈% Senior Notes due 2013 indenture and the Credit Agreement. If we fail to comply with these covenants, our 9⁵/₈% Senior Notes due 2013 and any loans outstanding under the Credit Agreement could become immediately payable and the Credit Agreement could be terminated. At September 30, 2006, we were in compliance with all such covenants.

7. Stockholders Equity

Common Stock, par value \$0.001 per share

We are authorized to issue 2,500,000,000 shares of our common stock as of September 30, 2006. As of September 30, 2006, approximately 457,896,000 shares of our common stock were reserved for issuance in connection with outstanding convertible debt, warrants, incentive stock plans and common stock to be granted to third parties upon satisfaction of performance targets. During the nine months ended September 30, 2006, employees exercised 2,764,476 stock options at exercise prices ranging from \$0.47 to \$3.93 per share, resulting in proceeds to us of \$3,788. Of this amount, \$3,747 was collected as of September 30, 2006. We also collected \$283 in 2006 related to stock option exercises that occurred in 2005.

In January 2006, Howard Stern and his agent were granted an aggregate of 34,375,000 shares of our common stock as a result of certain performance targets that were satisfied in January 2006. We recognized expense associated with these shares of \$224,813 during the nine months ended September 30, 2006.

In January 2004, we signed a seven-year agreement with the NFL. We delivered to the NFL 15,173,070 shares of our common stock valued at \$40,967 upon execution of this agreement. These shares of common stock are subject to transfer restrictions which lapse over time. We recognized expense associated with these shares of \$1,641 during each of the three months ended September 30, 2006 and 2005, and \$3,501 during each of the nine months ended September 30, 2006 and 2005. Of the remaining \$27,328 in common stock value, \$5,852 and \$21,476 are included in other current assets and other long-term assets, respectively, on our accompanying unaudited consolidated balance sheet as of September 30, 2006.

Warrants

We have issued warrants to purchase shares of our common stock in connection with distribution and programming agreements and certain debt issuances. As of September 30, 2006, warrants to acquire 129,405,589 shares of our common stock with an average exercise price of \$3.10 were outstanding. These warrants vest over time or upon the achievement of milestones and expire at various times through June 2014. For the three months ended September 30, 2006 and 2005, we recognized expense of \$4,584 and \$22,763, respectively, and \$45,553 and \$68,787 for the nine months ended September 30, 2006 and 2005, respectively, in connection with warrants.

8. Benefit Plans

Stock-Based Awards

In January 2003, our board of directors adopted the Sirius Satellite Radio 2003 Long-Term Stock Incentive Plan (the 2003 Plan), and on March 4, 2003 our stockholders approved this plan. On May 25, 2004, our stockholders approved an amendment to the 2003 Plan to include members of our board of directors as eligible participants. Employees, consultants and members of our board of directors are eligible to receive awards under the 2003 Plan. The 2003 Plan provides for the grant of stock options, restricted stock, restricted stock units and other stock-based awards that the compensation committee of our board of directors may deem appropriate.

Vesting and other terms of stock-based awards are set forth in the agreements with the individuals receiving the awards. Stock-based awards granted under the 2003 Plan are generally subject to a vesting requirement that includes one or all of the following: (1) over time, generally three to five years from the date of grant; (2) on a specific date in future periods, with acceleration to earlier periods if performance criteria are satisfied; or (3) as certain performance targets set at the time of grant are achieved. Stock-based awards generally expire ten years

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the date of grant. Each restricted stock unit entitles the holder to receive one share of our common stock upon vesting.

As of September 30, 2006, approximately 92,900,000 stock options, shares of restricted stock and restricted stock units were outstanding. As of September 30, 2006, approximately 86,134,000 shares of our common stock were available for grant under the 2003 Plan.

The following table summarizes stock option activity under our stock incentive plans for the nine months ended September 30, 2006 (shares in thousands):

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Intrinsic Value
Outstanding at beginning of period	87,024	\$ 4.61		
Granted	5,179	5.68		
Exercised	(2,764)	1.37		
Cancelled or expired	(812)	4.65		
Outstanding at end of period	88,627	4.78	6.02	\$ 72,552
Exercisable at end of period	50,213	4.75	4.41	68,174

The weighted average grant date fair value of options granted during the nine months ended September 30, 2006 and 2005 was \$3.11 and \$5.16, respectively. The total intrinsic value of stock options exercised during the nine months ended September 30, 2006 and 2005 was \$9,264 and \$39,332, respectively.

As of December 31, 2005, we had \$2,073 of deferred compensation in connection with stock options granted to employees and members of our board of directors. Such deferred compensation was reversed to additional paid-in capital in connection with the adoption of SFAS No. 123R. We recognized stock compensation expense associated with stock options of \$10,812 and \$2,589 for the three months ended September 30, 2006 and 2005, respectively, and \$38,514 and \$11,297 for the nine months ended September 30, 2006 and 2005, respectively. Stock compensation expense associated with stock options for the nine months ended September 30, 2005 included a charge of \$479 for an employee that was deemed to benefit from the modification of a stock-based award resulting in a new measurement date.

The following table summarizes the non-vested restricted stock unit activity under our stock incentive plans for the nine months ended September 30, 2006 (shares in thousands):

	Shares	Weighted Average Grant Date Fair Value
Outstanding at beginning of period	21,977	\$ 2.36
Granted	1,503	5.57
Vested	(19,184)	2.09
Cancelled or expired	(23)	5.71
Outstanding at end of period	4,273	4.68

The weighted average grant date fair value of restricted stock units granted during the nine months ended September 30, 2005 was \$6.23. The total intrinsic value of restricted stock units that vested during the nine months ended September 30, 2006 and 2005 was \$97,423 and

\$11,625, respectively.

As of December 31, 2005, we had \$24,621 of deferred compensation associated with restricted stock and restricted stock units granted to employees and members of our board of directors. Such deferred compensation was reversed to additional paid-in capital in connection with the adoption of SFAS No. 123R. We recognized stock compensation expense associated with restricted stock units and shares of restricted stock of \$3,095 and \$7,862 for the three months ended September 30, 2006 and 2005, respectively, and \$13,272 and \$26,958 for the nine months ended September 30, 2006 and 2005, respectively.

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For the three and nine months ended September 30, 2006, we also recognized stock compensation expense of \$21,838 and \$65,183, respectively, for restricted stock units and common stock expected to be granted for services performed in 2006 or upon the satisfaction of 2006 performance targets. For the three and nine months ended September 30, 2005, we recognized stock compensation expense of \$811 and \$2,422, respectively, for restricted stock units granted in 2006 for services performed in 2005.

401(k) Savings Plan

We sponsor the Sirius Satellite Radio 401(k) Savings Plan (the Plan) for eligible employees. The Plan allows eligible employees to voluntarily contribute from 1% to 50% of their pre-tax salary subject to certain defined limits. Currently we match 50% of employee voluntary contributions, up to 6% of an employee's pre-tax salary, in the form of shares of our common stock. Our matching contribution vests at a rate of 33 $\frac{1}{3}$ % for each year of employment and is fully vested after three years of employment. Expense resulting from our matching contribution to the Plan was \$227 and \$162 for the three months ended September 30, 2006 and 2005, respectively, and \$977 and \$710 for the nine months ended September 30, 2006 and 2005, respectively.

We may also elect to contribute to the profit sharing portion of the Plan based upon the total compensation of all participants eligible to receive an allocation. These additional contributions, referred to as profit-sharing contributions, are determined by the compensation committee of our board of directors. Employees are only eligible to receive profit-sharing contributions during any year in which they are employed on the last day of the year. Profit-sharing contribution expense was \$1,221 and \$1,118 for the three months ended September 30, 2006 and 2005, respectively, and \$3,480 and \$3,207 for the nine months ended September 30, 2006 and 2005, respectively.

9. Income Taxes

We recorded income tax expense of \$578 and \$560 for the three months ended September 30, 2006 and 2005, respectively, and \$1,909 and \$1,680 for the nine months ended September 30, 2006 and 2005, respectively. Such expense represents the recognition of a deferred tax liability related to the difference in accounting for our FCC license, which is amortized over 15 years for tax purposes but not amortized for book purposes.

10. Commitments and Contingencies

The following table summarizes our expected contractual cash commitments as of September 30, 2006:

	Remaining 2006	2007	2008	2009	2010	Thereafter	Total
Long-term debt obligations	\$	\$	\$ 52,185	\$ 301,744	\$	\$ 730,000	\$ 1,083,929
Cash interest payments	4,776	65,578	64,665	59,856	55,600	152,878	403,353
Lease obligations	2,369	8,630	8,375	8,331	8,115	28,097	63,917
Satellite and transmission	932	27,755	79,165	39,869	2,010	8,337	158,068
Programming and content	31,081	120,092	122,499	145,964	147,642	66,327	633,605
Customer service and billing	135	3,492	45				3,672
Marketing and distribution	37,571	53,236	31,415	22,608	25,979	23,577	194,386
Chip set development and production	1,752	5,209					6,961
Other	3,484	5,495	11,088				20,067
Total contractual cash commitments	\$ 82,100	\$ 289,487	\$ 369,437	\$ 578,372	\$ 239,346	\$ 1,009,216	\$ 2,567,958

Long-Term Debt Obligations. Long-term debt obligations include principal payments on our outstanding debt.

Cash Interest Payments. Cash interest payments include interest due on our outstanding debt through maturity.

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Lease Obligations. We have entered into operating leases related to our studios, office space, terrestrial repeaters and equipment.

Satellite and Transmission. We have entered into agreements with third parties to operate and maintain our off-site satellite telemetry, tracking and control facilities and certain components of our terrestrial repeater network. We have also entered into an agreement with Space Systems/Loral to design and construct a new satellite.

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Construction of this satellite is expected to be completed in the fourth quarter of 2008. We plan to launch this satellite on a Proton rocket under our contract with International Launch Services.

Programming and Content. We have entered into agreements with licensors of programming and other content providers and, in certain instances, are obligated to pay license fees and guarantee minimum advertising revenue share. In addition, we have agreements with various rights organizations pursuant to which we pay royalties for public performances of music.

Customer Service and Billing. We have entered into agreements with third parties to provide billing and subscriber management services.

Marketing and Distribution. We have entered into various marketing, sponsorship and distribution agreements to promote our brand and are obligated to make payments to sponsors, retailers, automakers and radio manufacturers under these agreements. In addition, certain programming and content agreements require us to purchase advertising on properties owned or controlled by the licensors. We also reimburse automakers for certain engineering and development costs associated with the incorporation of SIRIUS radios into vehicles they manufacture.

Chip Set Development and Production. We have entered into agreements with third parties to develop, produce and supply chip sets; to develop products; and in certain instances to license intellectual property related to chip sets.

Other. We have entered into an agreement with Canadian Broadcasting Corporation and Standard Broadcasting Corporation to fund SIRIUS Canada. We have also entered into various agreements with third parties for general operating and strategic purposes. Amounts associated with SIRIUS Canada and these various other agreements are included in the commitments table.

In addition to the contractual cash commitments described above, we have entered into agreements with automakers, radio manufacturers and others that include per-radio, per-subscriber, per-show and other variable cost arrangements. These future costs are dependent upon many factors including our subscriber growth and are difficult to anticipate; however, these costs may be substantial. We may enter into additional programming, distribution, marketing and other agreements that contain similar provisions.

Under the terms of a joint development agreement with XM Radio, the other holder of a FCC satellite radio license, each party is obligated to fund one half of the development cost for a unified standard for satellite radios. The costs related to the joint development agreement are being expensed as incurred to engineering, design and development expense in the accompanying unaudited consolidated statements of operations. We are currently unable to determine the expenditures necessary to complete this process, but we do not expect that these expenditures will be material.

We are required under the terms of certain agreements to provide letters of credit and deposit monies in escrow, which place restrictions on our cash and cash equivalents. As of September 30, 2006 and December 31, 2005, \$83,300 and \$107,615, respectively, were classified as restricted investments as a result of our reimbursement obligations under these letters of credit and escrow deposits.

As of September 30, 2006, we have not entered into any off-balance sheet arrangements or transactions.

Legal Proceedings

FCC Inquiry. In April 2006, we learned that two manufacturers of SIRIUS radios and our principal competitor had received inquiries from the Federal Communications Commission as to whether the FM transmitters in their products complied with the FCC's emissions and frequency rules. We promptly began an internal review of the compliance of the FM transmitters in a number of our radios. On June 20, we received a letter directly from the FCC making similar inquiries. On July 12, we responded to the letter from the FCC in respect of the preliminary results of our review. On August 7, we received a follow-up letter of inquiry from the FCC. We continue to cooperate with the FCC's inquiry.

During our internal review, we determined that certain of our radios with FM transmitters were not compliant with FCC rules. We have taken a series of actions to correct the problem.

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(Dollar amounts in thousands, unless otherwise stated)
(Unaudited)

In connection with our internal review, we discovered that certain SIRIUS personnel requested manufacturers to produce SIRIUS radios that were not consistent with the FCC's rules. As a result of this review, we are taking significant steps to ensure that this situation does not happen again, including the adoption of a comprehensive compliance plan, approved by our board of directors, to ensure that in the future our products comply with all applicable FCC rules.

The FCC is continuing its review of our products as well as products of other companies containing FM transmitters. The FCC's laboratory has tested a number of our products and found them to be compliant with the FCC's rules. We are discussing with the FCC methods to bring devices in retail inventory and in consumers' hands into compliance with the FCC's rules. We believe our radios that are currently in production comply with applicable FCC rules. SIRIUS radios that include compliant FM transmitters may be subject to some transmission noise, which may result in us encouraging professional installation in some cases. We continue to study methods to improve the customer experience for our subscribers using SIRIUS radios that rely on FM transmissions.

No health or safety issues are involved with these SIRIUS radios and radios which are factory-installed in new vehicles are not affected.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (All dollar amounts are in thousands, unless otherwise stated)

Special Note Regarding Forward-Looking Statements

The following cautionary statements identify important factors that could cause our actual results to differ materially from those projected in forward-looking statements made in this Quarterly Report on Form 10-Q and in other reports and documents published by us from time to time. Any statements about our beliefs, plans, objectives, expectations, assumptions, future events or performance are not historical facts and may be forward-looking. These statements are often, but not always, made through the use of words or phrases such as "will likely result," "are expected to," "will continue," "is anticipated," "estimated," "intend," "plan," "projection" and "outlook." Any forward-looking statements are qualified entirely by reference to the factors discussed throughout our Annual Report on Form 10-K for the year ended December 31, 2005 (the "Form 10-K") and in other reports and documents published by us from time to time, particularly the risk factors described under "Business Risk Factors" in Item 1A of the Form 10-K and in Part II, Item 1A of this Quarterly Report on Form 10-Q.

Among the significant factors that could cause our actual results to differ materially from those expressed in the forward-looking statements are:

the useful life of our satellites, which have experienced circuit failures on their solar arrays and other component failures and are not insured;

our dependence upon third parties, including manufacturers of SIRIUS radios, retailers, automakers and programming providers; and

our competitive position versus XM Radio, the other satellite radio service provider in the United States, which may have certain competitive advantages, and versus other forms of audio and video entertainment.

Because the risk factors referred to above could cause actual results or outcomes to differ materially from those expressed in any forward-looking statements made by us or on our behalf, you should not place undue reliance on any of these forward-looking statements. In addition, any forward-looking statement speaks only as of the date on which it is made, and we undertake no obligation to update any forward-looking statement or statements to reflect events or circumstances after the date on which the statement is made, to reflect the occurrence of unanticipated events or otherwise. New factors emerge from time to time, and it is not possible for us to predict which will arise or to assess with any precision the impact of each factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

Executive Summary

Overview:

We are a satellite radio provider in the United States. We currently broadcast 133 channels of programming to listeners across the country. We offer 69 channels of 100% commercial-free music and feature 64 channels of sports, news, talk, entertainment, traffic and weather for a monthly subscription fee of \$12.95.

We broadcast through our proprietary satellite radio system, which currently consists of three orbiting satellites, 139 terrestrial repeaters that receive and retransmit our signal, a satellite uplink facility and our studios. Subscribers receive our service through SIRIUS radios, which are sold by automakers, consumer electronics retailers and mobile audio dealers and through our website. Subscribers can also receive our music channels and certain other channels over the Internet.

Our music channels are available to DISH satellite television subscribers and certain of our music channels are offered to Sprint subscribers over multi-media handsets. We also offer traffic and weather data services for a separate fee. Subscribers to DISH satellite television, Sprint and our traffic and weather data services are not included in our subscriber count.

In 2005, SIRIUS Canada Inc., a Canadian corporation owned by us, Canadian Broadcasting Corporation and Standard Broadcasting Corporation, received a license from the Canadian Radio-television and Telecommunications Commission to offer a satellite radio service in Canada. In December 2005, SIRIUS Canada launched service in Canada with 100 channels of commercial-free music and news, sports, talk and entertainment programming, including 10 channels of Canadian content. Subscribers to the SIRIUS Canada service are not included in our subscriber count.

SIRIUS radios are primarily distributed through retailers; automakers, or OEMs; and through our website. SIRIUS radios can be purchased at major retailers, including Best Buy; Circuit City; Crutchfield; Costco; Target; Wal-Mart; and on an exclusive basis through RadioShack. On September 30, 2006, SIRIUS radios were available at more than 25,000 retail locations. We have exclusive agreements with DaimlerChrysler, Ford, Kia, Mitsubishi, BMW, Rolls-Royce, Volkswagen and Audi to offer SIRIUS radios as factory or dealer-installed equipment. We also have relationships with Nissan, Infiniti, Toyota, Lexus, Scion and Subaru to offer SIRIUS radios as factory or dealer-installed equipment. As of September 30, 2006, SIRIUS radios were available as a factory-installed option in 116 vehicle models and as a dealer-installed option in 16 vehicle models. SIRIUS radios are also offered to renters of Hertz vehicles at airport locations nationwide.

As of September 30, 2006, we had 5,119,308 subscribers compared with 3,316,560 subscribers as of December 31, 2005 and 2,173,920 subscribers as of September 30, 2005. Our subscriber totals include subscribers under our regular pricing plans; subscribers that have prepaid, including payments received from automakers for prepaid subscriptions included in the sale or lease price of a new vehicle; and active SIRIUS radios under our agreement with Hertz.

We expect an increasing proportion of our subscribers will be generated through our relationships with automakers. We believe our ability to attract and retain subscribers depends in large part on creating and sustaining distribution channels for SIRIUS radios and on the quality and entertainment value of our programming. We expect to concentrate our future efforts on enhancing and refining our programming, whether through additional agreements with third parties or our own creative efforts; introducing SIRIUS radios with new features and functions; and expanding the distribution of SIRIUS radios through arrangements with automakers and through additional retail points-of-sale.

Our primary source of revenue is subscription fees, with most of our customers subscribing to SIRIUS on either an annual or a monthly basis. We offer discounts for pre-paid and long-term subscriptions as well as discounts for multiple subscriptions. Currently we receive an average of approximately eight months of prepaid revenue per subscriber upon activation. We also derive revenue from activation fees, the sale of advertising on our non-music channels and the direct sale of SIRIUS radios and accessories.

In certain cases, automakers include a subscription to our radio service in the sale or lease price of vehicles. The length of these prepaid subscriptions varies, but is typically six months to one year. In many cases, we receive subscription payments from automakers in advance of the activation of our service. We also reimburse various automakers for certain costs associated with SIRIUS radios installed in their vehicles.

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Costs associated with acquiring subscribers are generally incurred and expensed in advance of acquiring a subscriber and are recognized as subscriber acquisition costs, or SAC. A large percentage of our annual gross subscriber additions are acquired in the fourth quarter in connection with holiday sales. As a result, our SAC, as adjusted, per gross subscriber addition, a key operating metric for our business, is generally higher in the first three quarters of our fiscal year and declines in the fourth quarter as we experience higher activation rates.

During the nine months ended September 30, 2006, we achieved significant financial and operational milestones, including:

led the satellite radio industry in net subscriber additions, capturing a record 61% share of total satellite radio net additions in the third quarter, and nearly doubled our OEM subscriber base;

entered into new exclusive agreements with Volkswagen, Audi, Kia and Rolls-Royce;

introduced the Stiletto 100, the satellite industry's first portable satellite radio with WiFi capabilities;

added new programming, including Howard Stern, Playboy Radio, Cosmo Radio, Blue Collar Comedy Radio, FOX News Channels, the Catholic Channel, Barbara Walters, Jerry Rice, Tony Stewart, Chelsea Football Club, Metropolitan Opera Radio and Jane Pratt.

In June 2006, we entered into an agreement with Space Systems/Loral to design and construct a new satellite that will be one of the most advanced and powerful communications satellites ever built. Construction of the satellite is expected to be completed in the fourth quarter of 2008. The satellite will be launched on a Proton rocket acquired by us under a previously announced launch contract. The aggregate cost of designing, building and launching the satellite and insuring its launch will be approximately \$260,000.

Results of Operations

Our discussion of our results of operations, along with the selected financial information in the tables that follow, includes the following non-GAAP financial measures: average monthly churn; SAC, as adjusted, per gross subscriber addition; customer service and billing expenses, as adjusted, per average subscriber; average monthly revenue per subscriber, or ARPU; and adjusted loss from operations. We believe these non-GAAP financial measures provide meaningful supplemental information regarding our operating performance and are used for internal management purposes, when publicly providing the business outlook, and as a means to evaluate period-to-period comparisons. Refer to the footnotes following our discussion of results of operations for the definitions and usefulness of such non-GAAP financial measures.

Subscribers and Key Operating Metrics:

The following table contains a breakdown of our subscribers for the past five quarters:

	As of				
	September 30, 2006	June 30, 2006	March 31, 2006	December 31, 2005	September 30, 2005
Beginning subscribers	4,678,207	4,077,747	3,316,560	2,173,920	1,814,626
Net additions	441,101	600,460	761,187	1,142,640	359,294
Ending subscribers	5,119,308	4,678,207	4,077,747	3,316,560	2,173,920
Retail	3,482,514	3,276,615	3,000,321	2,465,363	1,564,718
OEM	1,610,074	1,373,610	1,049,036	823,693	581,988
Hertz	26,720	27,982	28,390	27,504	27,214
Ending subscribers	5,119,308	4,678,207	4,077,747	3,316,560	2,173,920
Retail	205,899	276,294	534,958	900,645	209,920
OEM	236,464	324,574	225,343	241,705	149,000
Hertz	(1,262)	(408)	886	290	374

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	As of				
Net additions	441,101	600,460	761,187	1,142,640	359,294

Subscribers. We ended the third quarter of 2006 with 5,119,308 subscribers, an increase of 54% since December 31, 2005 and 135% from the 2,173,920 subscribers as of September 30, 2005. Since September 30, 2005, we added 1,917,796 net subscribers from our retail channel and 1,028,086 net subscribers from our OEM channel, resulting in a 123% and 177% increase in our retail and OEM subscriber base, respectively. Strong contributions by our exclusive OEM s, DaimlerChrysler and Ford, fueled this growth.

The following table presents our key operating metrics for the past five quarters:

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For the Three Months Ended

	September 30, 2006	June 30, 2006	March 31, 2006	December 31, 2005	September 30, 2005
Gross subscriber additions	732,406	830,571	960,610	1,266,674	465,228
Deactivated subscribers	291,305	230,111	199,423	124,034	105,934
Average monthly churn ⁽¹⁾⁽⁵⁾	2.0%	1.8%	1.8%	1.5%	1.8%
ARPU ⁽²⁾⁽⁵⁾	\$ 11.17	\$ 11.16	\$ 10.80	\$ 9.42	\$ 11.15
SAC, as adjusted, per gross subscriber addition ⁽³⁾⁽⁵⁾	\$ 114	\$ 131	\$ 113	\$ 113	\$ 149
Customer service and billing expenses, as adjusted, per average subscriber ⁽⁴⁾⁽⁵⁾	\$ 1.01	\$ 1.05	\$ 1.40	\$ 2.66	\$ 1.59
Total revenue	\$ 167,113	\$ 150,078	\$ 126,664	\$ 80,004	\$ 66,831
Adjusted loss from operations ⁽⁶⁾	\$ (83,153)	\$ (126,528)	\$ (136,650)	\$ (226,269)	\$ (105,414)
Net loss	\$ (162,898)	\$ (237,828)	\$ (458,544)	\$ (311,389)	\$ (180,450)

ARPU. Total ARPU for the three months ended September 30, 2006 was \$11.17, up from \$11.15 for the three months ended September 30, 2005, driven by higher net advertising revenue; the effects of mail-in rebates resulting from lower take-rates and the timing of the commencement of revenue recognition for prepaid subscriptions; offset by the impact of plan mix. At September 30, 2006, approximately two-thirds of our subscribers were on a one-year or longer subscription plan and approximately 15% were paying \$6.99 per month under a multi-unit subscriber plan.

We expect ARPU to fluctuate based on the growth of our subscriber base, promotions, mail-in rebates offered to subscribers and corresponding take-rates, plan mix, subscription prices and the identification of additional revenue streams from subscribers.

SAC, As Adjusted, Per Gross Subscriber Addition. SAC, as adjusted, per gross subscriber addition was \$114 and \$149 for the three months ended September 30, 2006 and 2005, respectively. The decline was primarily attributable to the reduction in average subsidy rates as we continued to reduce manufacturing and chip set costs.

We expect SAC, as adjusted, per gross subscriber addition to decline as the costs of subsidized components of SIRIUS radios will continue to decrease in the future. If competitive forces require us to increase hardware subsidies or promotions, SAC, as adjusted, per gross subscriber addition could increase. Our SAC, as adjusted, per gross subscriber addition is generally higher in the first three quarters of our fiscal year and declines in the fourth quarter as we experience higher activation rates.

Customer Service and Billing Expenses, As Adjusted, Per Average Subscriber Per Month. Customer service and billing expenses, as adjusted, per average subscriber per month declined 36% to \$1.01 for the third quarter of 2006 compared with \$1.59 for the third quarter of 2005.

We expect our customer care and billing expenses to increase and our costs per subscriber to decrease on an annual basis as our subscriber base grows.

Adjusted Loss from Operations. For the three months ended September 30, 2006 and 2005, adjusted loss from operations was \$83,153 and \$105,414, respectively, a decrease of \$22,261. The decrease was primarily driven by an increase in subscriber revenue of \$91,064 as a result of a 135% increase in our subscriber base. Such increase in subscriber revenue more than offset increases in operating expenses of \$81,044.

Net Loss. For the three months ended September 30, 2006 and 2005, net loss was \$162,898 and \$180,450, respectively, a decrease of \$17,552. The decrease was driven by an increase in subscriber revenue of \$91,064 as a result of a 135% increase in our subscriber base, offset by increases in our operating expenses to support the growth of our business.

Three and Nine Months Ended September 30, 2006 Compared with Three and Nine Months Ended September 30, 2005

Total Revenue

Subscriber Revenue. Subscriber revenue includes subscription fees, activation fees and the effects of mail-in rebates.

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Three Months: For the three months ended September 30, 2006 and 2005, subscriber revenue was \$155,337 and \$64,273, respectively, an increase of 142% or \$91,064. The increase was attributable to the growth of subscribers to our service.

Nine Months: For the nine months ended September 30, 2006 and 2005, subscriber revenue was \$408,154 and \$155,799, respectively, an increase of 162% or \$252,355. The increase was attributable to the growth of subscribers to our service.

The following table contains a breakdown of our subscriber revenue for the periods presented:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2006	2005	2006	2005
Subscription fees	\$ 153,192	\$ 63,920	\$ 407,203	\$ 154,575
Activation fees	3,955	1,858	11,326	4,742
Effects of mail-in rebates	(1,810)	(1,505)	(10,375)	(3,518)
Total subscriber revenue	\$ 155,337	\$ 64,273	\$ 408,154	\$ 155,799

Future subscriber revenue will be dependent upon, among other things, the growth of our subscriber base, promotions, mail-in rebates offered to subscribers and corresponding take-rates, plan mix, subscription prices and the identification of additional revenue streams from subscribers.

Advertising Revenue. Advertising revenue includes the sale of advertising on our non-music channels, net of agency fees. Agency fees are based on a stated percentage per the advertising agreements applied to gross billing revenue.

Three Months: For the three months ended September 30, 2006 and 2005, net advertising revenue was \$7,130 and \$1,508, respectively, an increase of \$5,622. More attractive programming and increased advertiser interest resulted in an increase in spots sold.

Nine Months: For the nine months ended September 30, 2006 and 2005, net advertising revenue was \$22,593 and \$3,094, respectively, an increase of \$19,499. More attractive programming and increased advertiser interest resulted in an increase in spots sold.

We expect advertising revenue to grow as our subscribers increase and we continue to improve brand awareness and content.

Equipment Revenue. Equipment revenue includes revenue from the direct sale of SIRIUS radios and accessories through our direct to consumer distribution channel.

Three Months: For the three months ended September 30, 2006 and 2005, equipment revenue was \$3,579 and \$1,030, respectively, an increase of \$2,549. The increase was the result of higher sales through our direct to consumer distribution channel, offset by the effects of promotional discounts.

Nine Months: For the nine months ended September 30, 2006 and 2005, equipment revenue was \$10,367 and \$3,300, respectively, an increase of \$7,067. The increase was the result of higher sales through our direct to consumer distribution channel, offset by the effects of promotional discounts.

We expect equipment revenue to increase in the future as we continue to introduce new products and as sales through our direct to consumer distribution channel grow.

Operating Expenses

Satellite and Transmission. Satellite and transmission expenses consist of costs associated with the operation and maintenance of our satellites; satellite telemetry, tracking and control system; terrestrial repeater network; satellite uplink facility; and broadcast studios.

Three Months: For the three months ended September 30, 2006 and 2005, satellite and transmission expenses were \$7,580 and \$7,695, respectively, a decrease of \$115. Excluding equity granted to third parties and employees expense of \$490 and \$467 for the three months ended September 30, 2006 and 2005, respectively, satellite and transmission expenses decreased \$138 from \$7,228 to \$7,090. As of September 30, 2006 and 2005, we had 139 and 140 terrestrial repeaters, respectively, in operation.

Nine Months: For the nine months ended September 30, 2006 and 2005, satellite and transmission expenses were \$34,279 and \$22,164, respectively, an increase of \$12,115. Excluding equity granted to third parties and employees expense of \$2,202 and \$1,455 for the nine months ended September 30, 2006 and 2005, respectively, satellite and transmission expenses increased \$11,368 from \$20,709 to \$32,077. This increase of \$11,368 was primarily attributable to an impairment charge associated with certain satellite long-lead time parts we purchased in 1999 that we will no longer need as a result of our new satellite contract.

Future increases in satellite and transmission expenses will primarily be attributable to the launch of new satellites, the addition of new terrestrial repeaters and maintenance costs of existing terrestrial repeaters. We expect to deploy additional terrestrial repeaters in 2007 and 2008. Such expenses may also increase in future periods if we decide to reinstate our in-orbit satellite insurance.

Programming and Content. Programming and content expenses include costs to acquire, create and produce content, on-air talent costs and broadcast and webstreaming royalties. We have entered into various agreements with third parties for music and non-music programming. These agreements require us to pay license fees, share advertising revenue, purchase advertising on media properties owned or controlled by the licensor and pay other guaranteed amounts. Purchased advertising is recorded as a sales and marketing expense in the period the advertising is broadcast.

Three Months: For the three months ended September 30, 2006 and 2005, programming and content expenses were \$79,532 and \$28,397, respectively, an increase of \$51,135. Excluding equity granted to third parties and employees expense of \$23,615 and \$4,855 for the three months ended September 30, 2006 and 2005, respectively, programming and content expenses increased \$32,375 from \$23,542 to \$55,917. This increase of \$32,375 was primarily attributable to consulting and license fees associated with new programming, broadcast and webstreaming royalties as a result of the increase in subscribers and compensation related costs for additions to headcount. Equity granted to third parties and employees expense increased \$18,760 primarily due to expense associated with common stock expected to be earned upon the satisfaction of performance targets.

Nine Months: For the nine months ended September 30, 2006 and 2005, programming and content expenses were \$462,511 and \$78,382, respectively, an increase of \$384,129. Excluding equity granted to third parties and employees expense of \$297,139 and \$14,793 for the nine months ended September 30, 2006 and 2005, respectively, programming and content expenses increased \$101,783 from \$63,589 to \$165,372. This increase of \$101,783 was primarily attributable to consulting and license fees associated with new programming, broadcast and webstreaming royalties as a result of the increase in subscribers and compensation related costs for additions to headcount. Equity granted to third parties and employees expense increased \$282,346 primarily due to \$224,813 associated with 34,375,000 shares of our common stock granted to Howard Stern and his agent in January 2006 and expense associated with common stock expected to be earned upon the satisfaction of performance targets.

Our programming and content expenses, excluding equity granted to third parties and employees expense, will increase as we continue to develop and enhance our channels. Beginning February 2007, our agreement with NASCAR will increase our programming and content expenses. In addition, we expect broadcast and webstreaming royalties to increase as our subscriber base grows. We regularly evaluate programming opportunities and may choose to acquire and develop new content or renew current programming agreements in the future at substantial costs.

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Future expense associated with equity granted to third parties and employees is contingent upon a number of factors, including the number of stock-based awards granted, the price of our common stock, assumptions used in estimating the fair value of stock-based awards, estimates for forfeitures, vesting provisions and the timing as to when certain performance criteria are met, and could materially change.

Customer Service and Billing. Customer service and billing expenses include costs associated with the operation of our customer service centers and subscriber management system.

Three Months: For the three months ended September 30, 2006 and 2005, customer service and billing expenses were \$14,915 and \$9,556, respectively, an increase of \$5,359. Excluding equity granted to third parties and employees expense of \$197 and \$140 for the three months ended September 30, 2006 and 2005, respectively, customer service and billing expenses increased \$5,302 from \$9,416 to \$14,718. This increase of \$5,302 was primarily due to increased call center operating costs necessary to accommodate the increase in our subscriber base and increased transaction fees due to the addition of new subscribers. Customer service and billing expenses, excluding equity granted to third parties and employees expense, increased 56% compared with an increase in our end of period subscribers of 135% year over year.

Nine Months: For the nine months ended September 30, 2006 and 2005, customer service and billing expenses were \$44,863 and \$27,051, respectively, an increase of \$17,812. Excluding equity granted to third parties and employees expense of \$645 and \$405 for the nine months ended September 30, 2006 and 2005, respectively, customer service and billing expenses increased \$17,572 from \$26,646 to \$44,218. This increase of \$17,572 was primarily due to increased call center operating costs necessary to accommodate the increase in our subscriber base and increased transaction fees due to the addition of new subscribers. Customer service and billing expenses, excluding equity granted to third parties and employees expense, increased 66% compared with an increase in our end of period subscribers of 135% year over year.

We expect our customer care and billing expenses, excluding equity granted to third parties and employees expense, to increase and our costs per subscriber to decrease on an annual basis as our subscriber base grows.

Cost of Equipment. Cost of equipment includes costs for SIRIUS radios and accessories sold through our direct to consumer distribution channel.

Three Months: For the three months ended September 30, 2006 and 2005, cost of equipment was \$6,196 and \$1,453, respectively, an increase of \$4,743. The increase was primarily attributable to higher sales volume through our direct to consumer distribution channel.

Nine Months: For the nine months ended September 30, 2006 and 2005, cost of equipment was \$13,128 and \$4,381, respectively, an increase of \$8,747. The increase was primarily attributable to higher sales volume through our direct to consumer distribution channel.

We expect cost of equipment to increase in the future as we introduce new products and as sales through our direct to consumer distribution channel grow.

Sales and Marketing. Sales and marketing expenses include costs for advertising, media and production, including promotional events and sponsorships; residuals; cooperative marketing; revenue share; customer retention and compensation. Residuals are monthly fees paid based upon the number of subscribers using a SIRIUS radio purchased from a retailer. Cooperative marketing costs include fixed and variable payments to reimburse retailers and automakers for the cost of advertising and other product awareness activities.

Three Months: For the three months ended September 30, 2006 and 2005, sales and marketing expenses were \$49,083 and \$47,823, respectively, an increase of \$1,260. Excluding equity granted to third parties and employees expense of \$7,609 and \$9,642 for the three months ended September 30, 2006 and 2005, respectively, sales and marketing expenses increased \$3,293 from \$38,181 to \$41,474. This increase of \$3,293 was primarily due to increased cooperative marketing spend, residuals and OEM revenue share as a result of a 135% increase in our subscriber base year over

year and compensation related costs, offset by a decrease in advertising costs. This 9% increase in sales and marketing expenses, excluding equity granted to third parties and employees expense, compared with a 150% increase in total revenue from \$66,831 for the three months ended September 30, 2005 to \$167,113 for the three months ended September 30, 2006. Equity granted to third parties and employees expense decreased \$2,033 primarily due to the timing of third parties achieving milestones and changes in the fair market value of such awards.

Nine Months: For the nine months ended September 30, 2006 and 2005, sales and marketing expenses were \$152,257 and \$137,891, respectively, an increase of \$14,366. Excluding equity granted to third parties and employees expense of \$14,878 and \$30,348 for the nine months ended September 30, 2006 and 2005, respectively, sales and marketing expenses increased \$29,836 from \$107,543 to \$137,379. This increase of \$29,836 was primarily due to increased residuals and OEM revenue share as a result of the increase in our subscriber base, cooperative marketing spend, advertising costs for our new marketing campaign Best Radio on Radio and compensation related costs. This 28% increase in sales and marketing expenses, excluding equity granted to third parties and employees expense, compared with a 174% increase in total revenue from \$162,241 for the nine months ended September 30, 2005 to \$443,855 for the nine months ended September 30, 2006. Equity granted to third parties and employees expense decreased \$15,470 primarily due to the timing of third parties achieving milestones and changes in the fair market value of such awards.

We expect sales and marketing expenses, excluding equity granted to third parties and employees expense, to increase as we continue to build brand awareness through national advertising and promotional activities and expand the distribution of SIRIUS radios. Beginning in 2007, our agreement with NASCAR will increase our sponsorship costs included in sales and marketing expense.

Future expense associated with equity granted to third parties and employees is contingent upon a number of factors, including the number of stock-based awards granted, the price of our common stock, assumptions used in estimating the fair value of stock-based awards, estimates for forfeitures, vesting provisions and the timing as to when certain performance criteria are met, and could materially change.

Subscriber Acquisition Costs. Subscriber acquisition costs include hardware subsidies paid to radio manufacturers, distributors and automakers, including subsidies paid to automakers who include a SIRIUS radio and a prepaid subscription to our service in the sale or lease price of a new vehicle; subsidies paid to chip set manufacturers; commissions paid to retailers and automakers as incentives to purchase, install and activate SIRIUS radios; and equity-based compensation expense related to distribution partners achievement of various milestones. The majority of subscriber acquisition costs are incurred and expensed in advance of acquiring a subscriber. Subscriber acquisition costs do not include advertising, loyalty payments to distributors and dealers of SIRIUS radios and revenue share payments to automakers and retailers of SIRIUS radios, which are included in sales and marketing expense. Subscriber acquisition costs also do not include amounts capitalized in connection with our agreement with Hertz, as we retain ownership of certain SIRIUS radios used by Hertz.

Three Months: For the three months ended September 30, 2006 and 2005, subscriber acquisition costs were \$79,812 and \$81,029, respectively, a decrease of 2% or \$1,217. Excluding equity granted to third parties and employees expense of (\$1,051) and \$12,354 for the three months ended September 30, 2006 and 2005, respectively, subscriber acquisition costs increased 18%, or \$12,188, from \$68,675 to \$80,863. This increase of \$12,188 was attributable to higher shipments of SIRIUS radios and chip sets to support a 57% increase in gross subscriber additions from 465,228 for the three months ended September 30, 2005 to 732,406 for the three months ended September 30, 2006. This increase was offset by reductions in hardware subsidy rates as we continued to reduce manufacturing and chip set costs. Equity granted to third parties and employees expense decreased \$13,405 primarily due to the timing of third parties achieving milestones and changes in the fair market value of such awards.

Nine Months: For the nine months ended September 30, 2006 and 2005, subscriber acquisition costs were \$329,418 and \$235,576, respectively, an increase of 40% or \$93,842. Excluding equity granted to third parties and employees expense of \$30,748 and \$31,115 for the nine months ended September 30, 2006 and 2005, respectively, subscriber acquisition costs increased 46%, or \$94,209, from \$204,461 to \$298,670. This increase of \$94,209 was attributable to higher

shipments of SIRIUS radios and chip sets to support a 101% increase in gross subscriber additions from 1,252,623 for the nine months ended September 30, 2005 to 2,523,587 for the nine months ended September 30, 2006, offset by reductions in hardware subsidy rates as we continued to reduce manufacturing and chip set costs. Equity granted to third parties and employees expense decreased \$367 primarily due to the timing of third parties achieving milestones and changes in the fair market value of such awards.

We expect total subscriber acquisition costs, excluding equity granted to third parties and employees expense, to increase in the future as our gross subscriber additions increase and we continue to offer subsidies, commissions and other incentives to acquire subscribers.

Future expense associated with equity granted to third parties and employees is contingent upon a number of factors, including the number of stock-based awards granted, the price of our common stock, assumptions used in estimating the fair value of stock-based awards, estimates for forfeitures, vesting provisions and the timing as to when certain performance criteria are met, and could materially change.

General and Administrative. General and administrative expenses include rent and occupancy, finance, legal, human resources, information technology and investor relations costs and bad debt expense.

Three Months: For the three months ended September 30, 2006 and 2005, general and administrative expenses were \$35,053 and \$20,103, respectively, an increase of \$14,950. Excluding equity granted to third parties and employees expense of \$11,536 and \$6,137 for the three months ended September 30, 2006 and 2005, respectively, general and administrative expenses increased \$9,551 from \$13,966 to \$23,517. This increase of \$9,551 was primarily a result of legal fees, employment-related costs, rent and occupancy costs and bad debt expense to support the growth of our business. Equity granted to third parties and employees expense increased \$5,399 primarily as a result of the adoption of Statement of Financial Accounting Standard (SFAS) No. 123 (revised 2004), Share-Based Payment (SFAS No. 123R), offset by a decrease in expense for restricted stock units that vested in the first quarter of 2006.

Nine Months: For the nine months ended September 30, 2006 and 2005, general and administrative expenses were \$103,261 and \$64,664, respectively, an increase of \$38,597. Excluding equity granted to third parties and employees expense of \$38,947 and \$21,746 for the nine months ended September 30, 2006 and 2005, respectively, general and administrative expenses increased \$21,396 from \$42,918 to \$64,314. This increase of \$21,396 was primarily a result of legal fees, employment-related costs, rent and occupancy costs and bad debt expense to support the growth of our business. Equity granted to third parties and employees expense increased \$17,201 primarily as a result of the adoption of SFAS No. 123R, offset by a decrease in expense for restricted stock units that vested in the first quarter of 2006.

We expect our general and administrative expenses, excluding equity granted to third parties and employees expense, to increase in future periods for personnel-related and facility costs to support our growth.

Future expense associated with equity granted to third parties and employees is contingent upon a number of factors, including the number of stock-based awards granted, the price of our common stock, assumptions used in estimating the fair value of stock-based awards, estimates for forfeitures, vesting provisions and the timing as to when certain performance criteria are met, and could materially change.

Engineering, Design and Development. Engineering, design and development expenses include costs to develop our future generation of chip sets and new products and costs associated with the incorporation of SIRIUS radios into vehicles manufactured by automakers.

Three Months: For the three months ended September 30, 2006 and 2005, engineering, design and development expenses were \$21,513 and \$13,135, respectively, an increase of \$8,378. Excluding equity granted to third parties and employees expense of \$1,022 and \$3,351 for the three months ended September 30, 2006 and 2005, respectively, engineering, design and development expenses increased \$10,707 from \$9,784 to \$20,491. This increase of \$10,707 was primarily attributable to OEM tooling and manufacturing upgrades and receiver integration for factory installations of SIRIUS radios, development costs associated with the manufacturing of SIRIUS radios and

additional personnel-related costs to support research and development efforts. Equity granted to third parties and employees expense decreased \$2,329 primarily due to the timing of third parties achieving certain production milestones.

Nine Months: For the nine months ended September 30, 2006 and 2005, engineering, design and development expenses were \$56,679 and \$50,252, respectively, an increase of \$6,427. Excluding equity granted to third parties and employees expense of \$10,734 and \$17,020 for the nine months ended September 30, 2006 and 2005, respectively, engineering, design and development expenses increased \$12,713 from \$33,232 to \$45,945. This increase of \$12,713 was primarily attributable to OEM tooling and manufacturing upgrades and receiver integration for factory installations of SIRIUS radios, development costs associated with the manufacturing of SIRIUS radios and additional personnel-related costs to support research and development efforts. Equity granted to third parties and employees expense decreased \$6,286 primarily due to the timing of third parties achieving certain production milestones.

We expect engineering, design and development expenses, excluding equity granted to third parties and employees expense, to decrease in 2007, as we have been incorporating SIRIUS radios and accessories in a significant number of vehicle models in 2006.

We expect future expense associated with equity granted to third parties and employees to decrease in 2007 as performance milestones pursuant to a certain third party agreement were achieved in 2006.

Other Income (Expense)

Interest and Investment Income. Interest and investment income includes realized gains and losses, dividends and interest income, including amortization of the premium and discount arising at purchase.

Three Months: For the three months ended September 30, 2006 and 2005, interest and investment income was \$7,750 and \$7,645, respectively, an increase of \$105. The increase was attributable to a combination of higher overall interest rates and our decision to invest in financial instruments bearing higher interest rates.

Nine Months: For the nine months ended September 30, 2006 and 2005, interest and investment income was \$26,560 and \$16,922, respectively, an increase of \$9,638. The increase was attributable to a combination of higher overall interest rates and our decision to invest in financial instruments bearing higher interest rates.

Interest Expense. Interest expense includes interest on outstanding debt, offset by interest capitalized in connection with the construction of our new satellite and launch vehicle.

Three Months: For the three months ended September 30, 2006 and 2005, interest expense was \$15,921 and \$13,693, respectively, an increase of \$2,228. The increase was primarily the result of interest expense for our 9⁵/₈% Senior Notes due 2013 issued in August 2005, offset by a decrease in interest expense as a result of the September 2005 redemption of our 15% Senior Secured Discount Notes due 2007 and our 14¹/₂% Senior Secured Notes due 2009 and \$1,134 of interest capitalized for the construction and launch of our new satellite.

Nine Months: For the nine months ended September 30, 2006 and 2005, interest expense was \$48,705 and \$28,219, respectively, an increase of \$20,486. The increase was primarily the result of interest expense for our 9⁵/₈% Senior Notes due 2013 issued in August 2005, offset by a decrease in interest expense as a result of the September 2005 redemption of our 15% Senior Secured Discount Notes due 2007 and our 14¹/₂% Senior Secured Notes due 2009 and \$2,532 of interest capitalized for the construction and launch of our new satellite.

Loss from Redemption of Debt. For the three and nine months ended September 30, 2005, a loss from redemption of debt of \$6,214 was recognized in connection with the redemption of our 15% Senior Secured Discount Notes due 2007 and our 14¹/₂% Senior Secured Notes due 2009, including a redemption premium of \$5,502 and the write-off of unamortized debt issuance costs of \$712.

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Equity in Net Loss of Affiliate. Equity in net loss of affiliate includes our share of SIRIUS Canada's net loss.

Three Months: We recorded \$739 for the three months ended September 30, 2005 for our share of SIRIUS Canada's net loss.

Nine Months: We recorded \$4,445 and \$739 for the nine months ended September 30, 2006 and 2005, respectively, for our share of SIRIUS Canada's net loss.

Income Taxes

Income Tax Expense. Income tax expense represents the recognition of a deferred tax liability related to the difference in accounting for our FCC license, which is amortized over 15 years for tax purposes but not amortized for book purposes in accordance with U.S. generally accepted accounting principles.

Three Months: We recorded income tax expense of \$578 and \$560 for the three months ended September 30, 2006 and 2005, respectively.

Nine Months: We recorded income tax expense of \$1,909 and \$1,680 for the nine months ended September 30, 2006 and 2005, respectively.

Footnotes to Results of Operations

- (1) Average monthly churn represents the number of deactivated subscribers divided by average quarterly subscribers.
- (2) ARPU is derived from total earned subscriber revenue and net advertising revenue divided by the daily weighted average number of subscribers for the period. ARPU is calculated as follows:

	For the Three Months Ended				
	September 30, 2006	June 30, 2006	March 31, 2006	December 31, 2005	September 30, 2005
Subscriber revenue	\$ 155,337	\$ 137,636	\$ 115,181	\$ 67,816	\$ 64,273
Net advertising revenue	7,130	8,125	7,338	3,037	1,508
Total subscriber and net advertising revenue	\$ 162,467	\$ 145,761	\$ 122,519	\$ 70,853	\$ 65,781
Daily weighted average number of subscribers	4,848,293	4,354,447	3,782,543	2,505,580	1,968,643
ARPU	\$ 11.17	\$ 11.16	\$ 10.80	\$ 9.42	\$ 11.15

- (3) SAC, as adjusted, per gross subscriber addition is derived from subscriber acquisition costs, excluding equity granted to third parties and employees, and margins from the direct sale of SIRIUS radios and accessories divided by the number of gross subscriber additions for the period. SAC, as adjusted, per gross subscriber addition is calculated as follows:

	For the Three Months Ended				
	September 30, 2006	June 30, 2006	March 31, 2006	December 31, 2005	September 30, 2005
Subscriber acquisition costs	\$ 79,812	\$ 130,563	\$ 119,043	\$ 163,774	\$ 81,029
Less: equity granted to third parties and employees	1,051	(21,900)	(9,899)	(18,594)	(12,354)
Add: margin from direct sale of SIRIUS radios and accessories	2,617	371	(227)	(1,525)	423
SAC, as adjusted	\$ 83,480	\$ 109,034	\$ 108,917	\$ 143,655	\$ 69,098
Gross subscriber additions	732,406	830,571	960,610	1,266,674	465,228

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SAC, as adjusted, per gross subscriber addition \$ 114 \$ 131 \$ 113 \$ 113 \$ 149

- (4) Customer service and billing expenses, as adjusted, per average subscriber is derived from total customer service and billing expenses, excluding equity granted to third parties and employees, divided by the daily weighted average number of subscribers for the period.
- (5) Average monthly churn; ARPU; SAC, as adjusted, per gross subscriber addition; and customer service and billing expenses, as adjusted, per average subscriber are not measures of financial performance under U.S. generally accepted accounting principles. We believe these non-GAAP financial measures provide meaningful supplemental information regarding our operating performance and are used by us for budgetary and planning purposes; when publicly providing our business outlook; to compare our performance from period to period; and to compare our performance to that of our primary competitor. We believe that investors also use our current and projected metrics to monitor the performance of our business and make investment decisions.

We believe the exclusion of equity granted to third parties and employees expense in our calculations of SAC, as adjusted, per gross subscriber addition and customer service and billing expenses, as adjusted, per average subscriber is useful given the significant

variation in expense that can result from changes in the fair market value of our common stock, the effect of which is unrelated to the operational conditions that give rise to variations in the components of our subscriber acquisition costs and customer service and billing expenses. Specifically, the exclusion of equity granted to third parties and employees expense in our calculation of SAC, as adjusted, per gross subscriber addition is critical in being able to understand the economic impact of the direct costs incurred to acquire a subscriber and the effect over time as economies of scale are reached.

These non-GAAP financial measures are used in addition to and in conjunction with results presented in accordance with GAAP. These non-GAAP financial measures may be susceptible to varying calculations; may not be comparable to other similarly titled measures of other companies; and should not be considered in isolation, as a substitute for, or superior to measures of financial performance prepared in accordance with GAAP.

- (6) We refer to net loss before taxes; other income (expense)-including interest and investment income, interest expense, loss from redemption of debt and equity in net loss of affiliate; depreciation; impairment charges; and equity granted to third parties and employees expense as adjusted loss from operations. Adjusted loss from operations is not a measure of financial performance under generally accepted accounting principles. We believe adjusted loss from operations is a useful measure of our operating performance. We use adjusted loss from operations for budgetary and planning purposes; to assess the relative profitability and on-going performance of our consolidated operations; to compare our performance from period to period; and to compare our performance to that of our primary competitor. We also believe adjusted loss from operations is useful to investors to compare our operating performance to the performance of other communications, entertainment and media companies. We believe that investors use current and projected adjusted loss from operations to estimate our current or prospective enterprise value and make investment decisions.

Because we fund and build-out our satellite radio system through the periodic raising and expenditure of large amounts of capital, our results of operations reflect significant charges for interest and depreciation expense. We believe adjusted loss from operations provides useful information about the operating performance of our business apart from the costs associated with our capital structure and physical plant. The exclusion of interest and depreciation expense is useful given fluctuations in interest rates and significant variation in depreciation expense that can result from the amount and timing of capital expenditures and potential variations in estimated useful lives, all of which can vary widely across different industries or among companies within the same industry. We believe the exclusion of taxes is appropriate for comparability purposes as the tax positions of companies can vary because of their differing abilities to take advantage of tax benefits and because of the tax policies of the various jurisdictions in which they operate. We also believe the exclusion of equity granted to third parties and employees expense is useful given the significant variation in expense that can result from changes in the fair market value of our common stock. Finally, we believe that the exclusion of our equity in net loss of affiliate (SIRIUS Canada Inc.) is useful to assess the performance of our core consolidated operations in the continental United States. To compensate for the exclusion of taxes, other income (expense), depreciation, impairment charges and equity granted to third parties and employees expense, we separately measure and budget for these items.

There are material limitations associated with the use of adjusted loss from operations in evaluating our company compared with net loss, which reflects overall financial performance, including the effects of taxes, other income (expense), depreciation, impairment charges and equity granted to third parties and employees expense. We use adjusted loss from operations to supplement GAAP results to provide a more complete understanding of the factors and trends affecting the business than GAAP results alone. Investors that wish to compare and evaluate our operating results after giving effect for these costs, should refer to net loss as disclosed in our unaudited consolidated statements of operations. Since adjusted loss from operations is a non-GAAP financial measure, our calculation of adjusted loss from operations may be susceptible to varying calculations; may not be comparable to other similarly titled measures of other companies; and should not be considered in isolation, as a substitute for, or superior to measures of financial performance prepared in accordance with GAAP.

Adjusted loss from operations is calculated as follows:

	For the Three Months Ended				
	September 30, 2006	June 30, 2006	March 31, 2006	December 31, 2005	September 30, 2005
Net loss	\$ (162,898)	\$ (237,828)	\$ (458,544)	\$ (311,389)	\$ (180,450)
Impairment loss		10,917			
Depreciation	27,583	25,738	24,933	24,915	24,559
Equity granted to third parties and employees	43,418	67,289	284,586	46,196	36,946
Other income (expense)	8,166	6,778	11,622	13,378	12,971
Income tax expense	578	578	753	631	560
Adjusted loss from operations	<u>\$ (83,153)</u>	<u>\$ (126,528)</u>	<u>\$ (136,650)</u>	<u>\$ (226,269)</u>	<u>\$ (105,414)</u>

Liquidity and Capital Resources

Cash Flows for the Nine Months Ended September 30, 2006 Compared with the Nine Months Ended September 30, 2005

As of September 30, 2006, we had \$317,876 in cash and cash equivalents compared with \$810,333 as of September 30, 2005.

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	For the Nine Months Ended September 30,		
	2006	2005	Variance
Net cash used in operating activities	\$ (456,056)	\$ (258,128)	\$ (197,928)
Net cash provided by (used in) investing activities	7,895	(131,943)	139,838
Net cash provided by financing activities	4,030	446,513	(442,483)
Net (decrease) increase in cash and cash equivalents	(444,131)	56,442	(500,573)
Cash and cash equivalents at beginning of period	762,007	753,891	8,116
Cash and cash equivalents at end of period	\$ 317,876	\$ 810,333	\$ (492,457)

Net cash used in operating activities increased \$197,928 to \$456,056 for the nine months ended September 30, 2006 from \$258,128 for the nine months ended September 30, 2005. Such increase in the net outflows of cash was attributable to the following: the pay down of accruals in 2006 primarily for subscriber acquisition costs due to the 101% increase in gross subscriber activations from 1,252,623 for the nine months ended September 30, 2005 to 2,523,587 for the nine months ended September 30, 2006; new programming and distribution partner arrangements entered into in 2006; and higher purchases of inventory to support production needs of our next generation SIRIUS radios and higher sales volumes through our direct to consumer distribution channel. These negative impacts to cash flow were offset by the effects of a decrease in accounts receivable for the pay down of receivable balances generated for activations in the fourth quarter of 2005, which were paid in the first quarter of 2006.

Net cash provided by investing activities was \$7,895 for the nine months ended September 30, 2006 compared with net cash used in investing activities of \$131,943 for the nine months ended September 30, 2005. The \$139,838 increase was primarily a result of sales of auction rate securities in 2006, offset by an increase in capital expenditures from \$17,949 for the nine months ended September 30, 2005 to \$94,368 for the nine months ended September 30, 2006 primarily as a result of costs associated with our satellite construction and launch vehicle.

We will incur significant capital expenditures to construct and launch our new satellite and to improve our terrestrial repeater network and broadcast and administrative infrastructure. These capital expenditures will support the resiliency of our operations and the growth we are experiencing, as well as support the delivery of new revenue streams in the future.

Net cash provided by financing activities decreased \$442,483 to \$4,030 for the nine months ended September 30, 2006 from \$446,513 for the nine months ended September 30, 2005. The decrease was primarily a result of the offering of \$500,000 in aggregate principal amount of our 9⁵/₈% Senior Notes due 2013 in August 2005 resulting in net proceeds to us of \$493,005.

Financings and Capital Requirements

We have financed our operations principally through the sale of debt and equity securities. In August 2005, we sold \$500,000 in aggregate principal amount of our 9⁵/₈% Senior Notes due 2013 resulting in net proceeds of \$493,005.

Future Liquidity and Capital Resource Requirements

Based upon our current plans, we believe that our cash, cash equivalents and marketable securities will be sufficient to cover our estimated funding needs through cash flow breakeven, the point at which our revenues are sufficient to fund expected operating expenses, capital expenditures, working capital requirements, interest and principal payments and taxes. We expect to generate positive free cash flow for the full year 2007, and our first quarter of positive free cash flow could be reached as early as the fourth quarter of 2006. Our financial projections are based on assumptions, which we believe are reasonable but contain significant uncertainties.

Our business is in its early stages, and we regularly evaluate our plans and strategy. These evaluations often result in changes to our plans and strategy, some of which may be material and significantly change our cash requirements or cause us to achieve cash flow breakeven at a later date. These changes in our plans or strategy may include: the acquisition of unique or compelling programming; the introduction of new features or services; significant new or enhanced distribution arrangements; investments in infrastructure, such as satellites, equipment or radio spectrum; and acquisitions of third parties that own programming, distribution, infrastructure, assets, or any combination of the foregoing.

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In June 2006, we entered into a Credit Agreement with Space Systems/Loral. Under the Credit Agreement, Space Systems/Loral has agreed to make loans to us in an aggregate principal amount of up to \$100,000 to finance the purchase of our new satellite. Loans made under the Credit Agreement will be secured by our rights under the Satellite Purchase Agreement with Space Systems/Loral, including our rights to the new satellite. The loans are also entitled to the benefits of a subsidiary guarantee from Satellite CD Radio, Inc., our subsidiary that holds our FCC license, and any future material subsidiary that may be formed by us. The maturity date of the loans is the earliest to occur of (i) April 6, 2009, (ii) 90 days after the new satellite becomes available for shipment and (iii) 30 days prior to the scheduled launch of the new satellite. Any loans made under the Credit Agreement generally will bear interest at a variable rate equal to three-month LIBOR plus 4.75%. The Credit Agreement permits us to prepay all or a portion of the loans outstanding without penalty. We have no current plans to draw under this Credit Agreement.

To fund incremental cash requirements, or as market opportunities arise, we may choose to raise additional funds through the sale of additional debt securities, equity securities or a combination of debt and equity securities. The incurrence of additional indebtedness would result in increased fiscal obligations and could contain restrictive covenants. The sale of additional equity or convertible debt securities would result in dilution to our stockholders. These additional sources of funds may not be available or, if available, may not be available on terms favorable to us.

2003 Long-Term Stock Incentive Plan

In January 2003, our board of directors adopted the Sirius Satellite Radio 2003 Long-Term Stock Incentive Plan (the 2003 Plan), and on March 4, 2003 our stockholders approved this plan. On May 25, 2004, our stockholders approved an amendment to the 2003 Plan to include members of our board of directors as eligible participants. Employees, consultants and members of our board of directors are eligible to receive awards under the 2003 Plan. The 2003 Plan provides for the grant of stock options, restricted stock, restricted stock units and other stock-based awards that the compensation committee of our board of directors may deem appropriate.

Vesting and other terms of stock-based awards are set forth in the agreements with the individuals receiving the awards. Stock-based awards granted under the 2003 Plan are generally subject to a vesting requirement that includes one or all of the following: (1) over time, generally three to five years from the date of grant; (2) on a specific date in future periods, with acceleration to earlier periods if performance criteria are satisfied; or (3) as certain performance targets set at the time of grant are achieved. Stock-based awards generally expire ten years from date of grant. Each restricted stock unit entitles the holder to receive one share of our common stock upon vesting.

As of September 30, 2006, approximately 92,900,000 stock options, shares of restricted stock and restricted stock units were outstanding. As of September 30, 2006, approximately 86,134,000 shares of our common stock were available for grant under the 2003 Plan. During the nine months ended September 30, 2006, employees exercised 2,764,476 stock options at exercise prices ranging from \$0.47 to \$3.93 per share, resulting in proceeds to us of \$3,788. The exercise of the remaining outstanding, vested options could result in an inflow of cash in future periods.

Contractual Cash Commitments

For a discussion of our Contractual Cash Commitments refer to Note 10 to the unaudited consolidated financial statements, Commitments and Contingencies, of this Form 10-Q.

Critical Accounting Policies

For a description of our Critical Accounting Policies refer to Management's Discussion and Analysis of Financial Condition and Results of Operations within our Annual Report on Form 10-K for the year ended December 31, 2005 and Note 3 to the unaudited consolidated financial statements, Summary of Significant Accounting Policies, of this Form 10-Q. During the nine months ended September 30, 2006, we adopted SFAS No. 123R.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

As of September 30, 2006, we did not have any derivative financial instruments and we do not intend to use derivatives. We do not hold or issue any free-standing derivatives. We hold investments in marketable securities, which consist of certificates of deposit and auction rate securities. We classify our marketable securities as

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available-for-sale. These securities are consistent with the investment objectives contained within our investment policy. The basic objectives of our investment policy are the preservation of capital, maintaining sufficient liquidity to meet operating requirements and maximizing yield. Despite the underlying long-term maturity of auction rate securities, from the investor's perspective, such securities are priced and subsequently traded as short-term investments because of the interest rate reset feature. Interest rates are reset through an auction process at predetermined periods of 28 or 35 days. Failed auctions rarely occur. As of September 30, 2006, we held \$34,225 in auction rate securities.

Our long-term debt includes fixed interest rates and the fair market value of the debt is sensitive to changes in interest rates. Under our current policies, we do not use interest rate derivative instruments to manage our exposure to interest rate fluctuations.

Item 4. Controls and Procedures

As of September 30, 2006, an evaluation was performed under the supervision and with the participation of our management, including Mel Karmazin, our Chief Executive Officer, and David J. Frear, our Executive Vice President and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, our management, including our Chief Executive Officer and our Chief Financial Officer, concluded that our disclosure controls and procedures were effective as of September 30, 2006. There have been no significant changes in our internal control over financial reporting or in other factors that could materially affect, or is reasonably likely to materially affect, our internal control over financial reporting for the three and nine months ended September 30, 2006.

Part II

Other Information

Item 1. Legal Proceedings

FCC Inquiry. In April 2006, we learned that two manufacturers of SIRIUS radios and our principal competitor had received inquiries from the Federal Communications Commission as to whether the FM transmitters in their products complied with the FCC's emissions and frequency rules. We promptly began an internal review of the compliance of the FM transmitters in a number of our radios. On June 20, we received a letter directly from the FCC making similar inquiries. On July 12, we responded to the letter from the FCC in respect of the preliminary results of our review. On August 7, we received a follow-up letter of inquiry from the FCC. We continue to cooperate with the FCC's inquiry.

During our internal review, we determined that certain of our radios with FM transmitters were not compliant with FCC rules. We have taken a series of actions to correct the problem.

In connection with our internal review, we discovered that certain SIRIUS personnel requested manufacturers to produce SIRIUS radios that were not consistent with the FCC's rules. As a result of this review, we are taking significant steps to ensure that this situation does not happen again, including the adoption of a comprehensive compliance plan, approved by our board of directors, to ensure that in the future our products comply with all applicable FCC rules.

The FCC is continuing its review of our products as well as products of other companies containing FM transmitters. The FCC's laboratory has tested a number of our products and found them to be compliant with the FCC's rules. We are discussing with the FCC methods to bring devices in retail inventory and in consumers' hands into compliance with the FCC's rules. We believe our radios that are currently in production comply with applicable FCC's rules. SIRIUS radios that include compliant FM transmitters may be subject to some transmission noise, which may result in us encouraging professional installation in some cases. We continue to study methods to improve the customer experience for our subscribers using SIRIUS radios that rely on FM transmissions.

No health or safety issues are involved with these SIRIUS radios and radios which are factory-installed in new vehicles are not affected. We do not expect the resolution of these issues to have an adverse impact on our previous guidance.

On October 13, 2006, we ceased operating 11 of our terrestrial repeaters which we discovered had been operating at variance to the specifications and applied to the FCC for new authority to resume operating these repeaters.

Copyright Royalty Board Proceeding. We are a party to a proceeding before the Copyright Royalty Board of the Library of Congress to establish the royalty rate and terms for the sound recordings we use on our satellite radio service for the period for 2007 through 2012. On October 30, 2006, we and XM filed our direct case in this proceeding with the Copyright Royalty Board and proposed a royalty rate of 0.88% of our satellite radio subscription revenue.

The Copyright Royalty Board must set a rate that is calculated to achieve four statutory objectives:

to maximize the availability of creative works to the public;

to afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions;

to reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk and contribution to the opening of new markets for creative expression and media for their communication; and

to minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices.

We believe that the fee we proposed achieves these objectives and is consistent in principle with the fee established under the same standard for digital cable audio.

SoundExchange, the organization that collects and distributes royalties from various digital music services on behalf of artists and music labels, simultaneously submitted its direct case in this proceeding and proposed a substantially higher royalty rate than we proposed. This submission of direct cases is the beginning of a twelve to eighteen month process which, absent an agreement among the parties, will result in a determination by the Copyright Royalty Board of an applicable royalty rate.

Item 1A. Risk Factors

Reference is made to the Risk Factors set forth in Part II, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2005. The Risk Factors remain applicable from our Form 10-K with the exception of the following changes:

Failure of our satellites would significantly damage our business.

Our three satellites were launched in 2000. We do not maintain in-orbit insurance policies covering our satellites. We estimate that two of our in-orbit satellites will have a 13 year useful life and our third in-orbit satellite will have a 15 year useful life from the time they were launched. In June 2006, we adjusted the useful lives of two of our in-orbit satellites from 15 years to 13 years to reflect the way we intend to operate the constellation. Our operating results would be materially adversely affected if the useful life of our satellites is significantly shorter than we expect, whether as a result of a satellite failure or technical obsolescence, and we fail to launch replacement satellites in a timely manner.

The useful lives of our satellites will vary and depend on a number of factors, including:

degradation and durability of solar panels;

quality of construction;

random failure of satellite components, which could result in significant damage to or loss of a satellite;

amount of fuel our satellites consume; and

damage or destruction by electrostatic storms or collisions with other objects in space, which occur only in rare cases.

Our satellites have experienced circuit failures on their solar arrays. The circuit failures our satellites have experienced to date do not affect our current operations. Additional circuit failures could reduce the estimated useful life of our existing in-orbit satellites.

In the ordinary course of operation, satellites experience failures of component parts and operational and performance anomalies. Components on our in-orbit satellites have failed, and from time to time we have experienced anomalies in the operation and performance of our satellites. These failures and anomalies are expected to continue in the ordinary course, and it is impossible to predict if any of these future events will have a material adverse effect on our operations or the useful life of our existing in-orbit satellites.

If one of our three satellites fails in orbit, our service would be impaired until such time as we successfully launch and commission our spare satellite, which would take six months or more. If two or more of our satellites fail in orbit in close proximity in time, our service could be suspended for at least 24 months. In such event, our business would be materially impacted and we could default on our commitments.

In June 2006, we entered into an agreement with Space Systems/Loral to design and construct a new satellite. The new satellite is expected to be completed in the fourth quarter of 2008, and launched shortly thereafter. Satellite launches have significant risks, including launch failure, damage or destruction of the satellite

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during launch and failure to achieve a proper orbit or operate as planned. Our agreement with Space Systems/Loral does not protect us against the risks inherent in a satellite launch or in-orbit operations.

Failure to comply with FCC requirements could damage our business.

As the holder of one of two FCC licenses to operate a satellite radio service in the United States, we are subject to FCC rules and regulations. The terms of our license require us to meet certain conditions, including designing a receiver that will permit end users to access XM Radio's system; coordination of our satellite radio service with radio systems operating in the same range of frequencies in neighboring countries; and coordination of our communications links to our satellites with other systems that operate in the same frequency band. Non-compliance by us with these conditions could result in fines, additional license conditions, license revocation or other detrimental FCC actions.

The FCC is reviewing whether the FM transmitters in certain SIRIUS radios comply with the Commission's emissions and frequency rules. We are cooperating with the FCC in its on-going inquiry, and have discovered that certain SIRIUS personnel requested manufacturers to produce SIRIUS radios that were not consistent with these rules. We are taking significant steps to ensure that this situation does not happen again, including the adoption of a comprehensive compliance plan, approved by our board of directors, to ensure that in the future our products comply with all applicable FCC rules. We have directed manufacturers of SIRIUS radios with FM transmitters to suspend manufacture and shipment to retailers of non-compliant devices and to make the necessary changes in production to bring the radios into compliance. We believe our radios that are currently in production comply with applicable FCC rules. SIRIUS radios that include compliant FM transmitters may be subject to some transmission noise, which may result in us encouraging professional installation in some cases. We continue to study methods to improve the customer experience for our subscribers using SIRIUS radios that rely on FM transmissions. The FCC's inquiry may result in fines, additional license conditions or other FCC actions that are detrimental to our business.

The FCC has not yet issued final rules permitting us to operate and deploy terrestrial repeaters to fill gaps in our satellite coverage. We are operating our terrestrial repeaters on a non-interference basis pursuant to a grant of special temporary authority from the FCC. The FCC's final terrestrial repeater rules may require us to reduce the power of our terrestrial repeaters and limit our ability to deploy additional repeaters. If the FCC requires us to reduce significantly the power of our terrestrial repeaters, this would have an adverse effect on the quality of our service in certain markets and/or cause us to alter our terrestrial repeater infrastructure at a substantial cost. If the FCC limits our ability to deploy additional terrestrial repeaters, our ability to improve any deficiencies in our service quality that may be identified in the future would be adversely affected.

On October 13, 2006, we ceased operating 11 of our terrestrial repeaters which we discovered had been operating at variance to the specifications and applied to the FCC for new authority to resume operating these repeaters. Our failure to comply with the initial Special Temporary Authority could result in disciplinary action by the FCC, although we do not believe such action would have a material adverse effect on our business or operations.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

See Exhibit Index attached hereto.

SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SIRIUS SATELLITE RADIO INC.

By: /s/ DAVID J. FREAR

David J. Frear
Executive Vice President and
Chief Financial Officer
(Principal Financial Officer)

November 8, 2006

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EXHIBIT INDEX

<u>Exhibit</u>	<u>Description</u>
3.1	Amended and Restated Certificate of Incorporation dated March 4, 2003 (incorporated by reference to Exhibit 3.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2002).
3.2	Amended and Restated By-Laws (incorporated by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2001).
4.1	Form of certificate for shares of Common Stock (incorporated by reference to Exhibit 4.3 to the Company's Registration Statement on Form S-1 (File No. 33-74782) (the "S-1 Registration Statement")).
4.2	Warrant Agreement, dated as of May 15, 1999, between the Company and United States Trust Company of New York, as warrant agent (incorporated by reference to Exhibit 4.4.4 to the Company's Registration Statement on Form S-4 (File No. 333-82303)).
4.3	Indenture, dated as of September 29, 1999, between the Company and United States Trust Company of Texas, N.A., as trustee, relating to the Company's 8¾% Convertible Subordinated Notes due 2009 (incorporated by reference to Exhibit 4.2 to the Company's Current Report on Form 8-K filed on October 13, 1999).
4.4	First Supplemental Indenture, dated as of September 29, 1999, between the Company and United States Trust Company of Texas, N.A., as trustee, relating to the Company's 8¾% Convertible Subordinated Notes due 2009 (incorporated by reference to Exhibit 4.01 to the Company's Current Report on Form 8-K filed on October 1, 1999).
4.5	Second Supplemental Indenture, dated as of March 4, 2003, among the Company, The Bank of New York (as successor to United States Trust Company of Texas, N.A.), as resigning trustee, and HSBC Bank USA, as successor trustee, relating to the Company's 8¾% Convertible Subordinated Notes due 2009 (incorporated by reference to Exhibit 4.16 to the Company's Annual Report on Form 10-K for the year ended December 31, 2002).
4.6	Third Supplemental Indenture, dated as of March 7, 2003, between the Company and HSBC Bank USA, as trustee, relating to the Company's 8¾% Convertible Subordinated Notes due 2009 (incorporated by reference to Exhibit 4.17 to the Company's Annual Report on Form 10-K for the year ended December 31, 2002).
4.7	Form of 8¾% Convertible Subordinated Note due 2009 (incorporated by reference to Article VII of Exhibit 4.01 to the Company's Current Report on Form 8-K filed on October 1, 1999).
4.8	Indenture, dated as of May 23, 2003, between the Company and The Bank of New York, as trustee (incorporated by reference to Exhibit 99.2 to the Company's Current Report on Form 8-K dated May 30, 2003).
4.9	Supplemental Indenture, dated as of May 23, 2003, between the Company and The Bank of New York, as trustee, relating to the Company's 3½% Convertible Notes due 2008 (incorporated by reference to Exhibit 99.3 to the Company's Current Report on Form 8-K dated May 30, 2003).
4.10	Second Supplemental Indenture, dated as of February 20, 2004, between the Company and The Bank of New York, as trustee, relating to the Company's 2½% Convertible Notes due 2009 (incorporated by reference to Exhibit 4.20 to the Company's Annual Report on Form 10-K for the year ended December 31, 2003).
4.11	Third Supplemental Indenture, dated as of October 13, 2004, between the Company and The Bank of New York, as trustee, relating to the Company's 3¼% Convertible Notes due 2011 (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K dated October 13, 2004).
4.12	Indenture, dated as of August 9, 2005, between the Company and The Bank of New York, as trustee relating to the Company's 9⅝% Senior Notes due 2013 (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on August 12, 2005).
4.13	Common Stock Purchase Warrant granted by the Company to DaimlerChrysler AG dated October 4, 2005 (incorporated by reference to Exhibit 4.13 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2005).

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<u>Exhibit</u>	<u>Description</u>
4.14	Common Stock Purchase Warrant granted by the Company to Ford Motor Company dated October 7, 2002 (incorporated by reference to Exhibit 4.16 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2002).
4.15	Form of Media-Based Incentive Warrant dated February 3, 2004 issued by the Company to NFL Enterprises LLC (incorporated by reference to Exhibit 4.25 to the Company's Annual Report on Form 10-K for the year ended December 31, 2003).
4.16	Bounty-Based Incentive Warrant dated February 3, 2004 issued by the Company to NFL Enterprises LLC (incorporated by reference to Exhibit 4.26 to the Company's Annual Report on Form 10-K for the year ended December 31, 2003).
4.17	Amended and Restated Warrant Agreement, dated as of December 27, 2000, between the Company and United States Trust Company of New York, as warrant agent and escrow agent (incorporated by reference to Exhibit 4.27 to the Company's Registration Statement on Form S-3 (File No. 333-65602)).
4.18	Customer Credit Agreement, dated as of May 31, 2006, between the Company and Space Systems/Loral, Inc. (incorporated by reference to Exhibit 4.18 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006).
10.1.1	Lease Agreement, dated as of March 31, 1998, between Rock-McGraw, Inc. and the Company (incorporated by reference to Exhibit 10.1.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998).
10.1.2	Supplemental Indenture, dated as of March 22, 2000, between Rock-McGraw, Inc. and the Company (incorporated by reference to Exhibit 10.1.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2000).
*10.2	Employment Agreement dated November 18, 2004 between the Company and Mel Karmazin (incorporated by reference to Exhibit 10.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2004).
*10.3	Employment Agreement, dated as of June 3, 2003, between the Company and David J. Frear (incorporated by reference to Exhibit 10.7 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2003).
*10.4	First Amendment, dated as of August 10, 2005, to the Employment Agreement, dated as of June 3, 2003, between the Company and David Frear (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K dated August 12, 2005).
*10.5	Employment Agreement, dated as of May 5, 2004, between the Company and Scott A. Greenstein (incorporated by reference to Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2004).
*10.6	First Amendment, dated as of August 8, 2005, to the Employment Agreement, dated as of May 5, 2004, between the Company and Scott Greenstein (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated August 12, 2005).
*10.7	Amended and Restated Employment Agreement, dated as of March 11, 2005, between the Company and James E. Meyer (incorporated by reference to Exhibit 10.5 to the Company's Annual Report on Form 10-K for the year ended December 31, 2004).
*10.8	First Amendment, dated February 2, 2006, to the Amended and Restated Employment Agreement, dated March 11, 2005, between the Company and James E. Meyer (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated February 1, 2006).
*10.9	Restricted Stock Unit Agreement, dated as of August 9, 2005, between the Company and James E. Meyer (incorporated by reference to Exhibit 10.3 to the Company's Current Report on Form 8-K dated August 12, 2005).
*10.10	Employment Agreement, dated as of November 8, 2004, between the Company and Patrick L. Donnelly (incorporated by reference to Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004).

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<u>Exhibit</u>	<u>Description</u>
*10.11	CD Radio Inc. 401(k) Savings Plan (incorporated by reference to Exhibit 4.4 to the Company's Registration Statement on Form S-8 (File No. 333-65473)).
*10.12	Amended and Restated Sirius Satellite Radio 2003 Long-Term Stock Incentive Plan (incorporated by reference to Exhibit 10.10 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2004).
*10.13	Form of Option Agreement, dated as of December 29, 1997, between the Company and each Optionee (incorporated by reference to Exhibit 10.16.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998).
10.14	Joint Development Agreement, dated as of February 16, 2000, between the Company and XM Satellite Radio Inc. (incorporated by reference to Exhibit 10.28 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2000).
31.1	Certificate of Mel Karmazin, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
31.2	Certificate of David J. Frear, Executive Vice President and Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32.1	Certificate of Mel Karmazin, Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32.2	Certificate of David J. Frear, Executive Vice President and Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).

* This document has been identified as a management contract or compensatory plan or arrangement.

Portions of this exhibit have been omitted pursuant to Applications for Confidential treatment filed by the Company with the Securities and Exchange Commission.
