

A Review of the Copyright
Licensing Regimes Covering
Retransmission of Broadcast Signals

U. S. Copyright Office

August 1, 1997

A Report of the Register of Copyrights

TABLE OF CONTENTS

Executive Summary	i
Introduction	1
I. The Current System of Copyright Licensing for Broadcast Retransmissions	3
A. The Cable Compulsory License	3
B. The Satellite Carrier Compulsory License	8
II. Should the Cable and Satellite Carrier Compulsory Licenses Continue to Exist?	12
A. History	12
The Introduction of Satellite Carrier Retransmissions	14
B. The Comments	16
1. The Cable License	16
2. Other Reasons Offered For Retaining the Cable Compulsory License	18
3. Reasons to Eliminate the Cable License	21
4. Possible Free Market Mechanisms for Clearing Rights to a Broadcast Signal	24
5. Particular Problems Presented by Free Market Negotiation of Broadcast Signals	27
C. The Satellite Carrier Compulsory License	29
1. Reasons Supporting the Existence of the Satellite Carrier License	29
2. Reasons for Elimination of the Satellite Carrier License	31
3. Reasons for Extending the Satellite	

	Carrier License	31
D.	Discussion and Conclusion	32
III.	Should the Cable and Satellite Carrier Licenses Be Harmonized?	34
IV.	Should the Cable Rate Structure be Reformed?	36
A.	Reform Principles	37
1.	The Comments	37
2.	Summary of Reform Principles	40
3.	Copyright Office Recommendation	41
B.	The Small System Subsidy	42
1.	The Comments	43
2.	Copyright Office Discussion and Recommendations	44
C.	The Artificial Fragmentation Problem	45
D.	The Proposed Step-Up Rate	48
V.	How Should the Cable Rate Structure be Reformed?	50
A.	Local versus Distant Signals	50
B.	Models for Rate Reform	52
1.	The Flat, Per Subscriber, Per Signal Fee	52
2.	The Gross Receipts Rate Structure	53
3.	Tariffing	55
C.	Discussion	57
1.	Avoidance of Tiering	58

2.	Subscriber Groups	59
3.	Direct Comparison to Satellite Carriers	59
4.	Changing Signal Lineups	59
D.	Transition to New Rate Structure	60
VI.	Should the Cable Compulsory License Apply to Open Video System Operations?	62
A.	The Telecommunications Act of 1996	62
B.	Prior Copyright Office Consideration Regarding the Status of Open Video Systems	65
C.	Summary of Comments and Testimony	66
1.	The Eligibility Issue	66
2.	The "Nuts and Bolts" of a Compulsory License for Open Video Systems	71
D.	Copyright Office Recommendations	76
VII.	The Passive Carrier Exemption	79
A.	Background Information	79
B.	Summary of Comments and Testimony	84
1.	Open Video Systems Issues	84
2.	Satellite Carrier Issues	87
C.	Copyright Office Recommendations	89
1.	Open Video System Issues	89
2.	Satellite Carrier Issues	91
VIII.	Should the Cable Compulsory License be Extended to the Internet?	92
A.	Summary of the Comments and Testimony	92
B.	Copyright Office Recommendations	98

IX.	Unserved Household Restriction: Discussion and Analysis	101
	A. What is it?	101
	B. History of the Restriction	102
	C. The Issues Presented by the Unserved Household Restriction	107
	1. Eligibility for Satellite Network Service	107
	2. The Local Retransmission Issue	114
	3. The PBS Issue	117
	D. Discussion and Analysis	117
	1. Should the Unserved Household Restriction Remain in the Copyright Law?	118
	2. Local Retransmission: The Best Solution	119
	3. Failure of the Current Unserved Household Restriction	122
	4. The "Red Zone/Green Zone" Approach	125
	5. The PBS National Satellite Service	127
	6. The Picture Quality and Grade B Standards	127
	7. The Surcharge Option	129
	E. Conclusion	131
X.	Additional Issues	133
	A. Treatment of Network Signals	133
	1. Payment for Network Signals	133
	2. Distribution to Networks	134
	B. Payment for Local Signals	135
XI.	Recommendations	137

EXECUTIVE SUMMARY

At the request of Senator Orrin Hatch, Chairman of the United States Senate Committee on the Judiciary, the Copyright Office conducted a review of the copyright licensing regimes governing the retransmission of over-the-air radio and television broadcast signals by cable systems, satellite carriers, and other multichannel video providers. The specific issues addressed in this review include whether the compulsory licenses should continue to exist, whether harmonization of the satellite and cable compulsory licenses is possible and desirable, whether the satellite compulsory license should be extended, whether to extend either of those licenses to new technologies such as open video systems and the Internet, whether the satellite carrier compulsory license should encompass the local retransmission of broadcast signals, how to solve the disputes surrounding the "unserved household" restriction for the retransmission of network television stations that is currently a part of the satellite compulsory license, and whether the satellite compulsory licensing regime should make a special provision for the retransmission of a national satellite feed of the Public Broadcasting Service with a separate royalty rate for such a signal.

I. THE CURRENT SYSTEM OF COPYRIGHT LICENSING FOR BROADCAST RETRANSMISSIONS

There are currently two compulsory licenses in the Copyright Act governing the retransmission of broadcast signals. A compulsory license is a statutory copyright licensing scheme whereby copyright owners are required to license their works to users at a government-fixed price and under government-set terms and conditions. The cable compulsory license allows a cable system to intercept over-the-air television and radio broadcast signals (comprised of copyrighted programming) and to retransmit the signals to its subscribers who pay a fee for such service. The satellite carrier compulsory license permits a satellite carrier to intercept television (but not radio) signals and retransmit the signals to satellite home

dish owners for their private home viewing. The cable compulsory license does not have a sunset provision, but the satellite carrier compulsory license is scheduled to expire on December 31, 1999.

The cable compulsory license originated in the 1976 Copyright Revision Act and was premised on two significant Congressional considerations. The first consideration concerns the difference between cable retransmission of a broadcast signal to the local audience served simultaneously by the broadcaster and its retransmission to a distant audience that would not otherwise be able to receive the signal. In 1976, Congress determined that the carriage of local broadcast signals by a cable operator does not greatly harm the copyright owners of the programming on the signal retransmitted. Based on that consideration, the compulsory license essentially lets cable systems carry local signals for a *de minimis* fee.

To the contrary, Congress found a cable system's retransmission of broadcast signals to subscribers in distant markets does harm copyright owners. To compensate copyright owners for the retransmission of their programming to distant markets, Congress requires cable systems utilizing the cable compulsory license to pay royalties for each signal they carry to distant audiences.

The second consideration concerns a differentiation between large and small cable systems based upon the dollar amount of receipts a cable system receives from subscribers for the carriage of broadcast signals. In 1976, Congress determined that the retransmission of copyrighted works by smaller cable systems whose gross receipts from subscribers were below a certain dollar amount deserved special consideration because of their mostly rural location. Therefore, in effect, the cable compulsory license subsidizes smaller systems and allows them to follow a different, lower-cost royalty computation. Large systems, on the other hand, pay in accordance with a highly complicated and technical formula, principally dependent on how the Federal Communications Commission regulated the cable industry in 1976. The vast majority of royalties paid under the cable compulsory license comes from the large cable systems.

The royalty scheme for the large cable systems employs the statutory device known as the distant signal equivalent (DSE). Whether a signal is distant or local for a particular cable system for purposes of

calculating the system's DSE total is determined in accordance with two sets of FCC regulations on cable systems: the "must-carry" rules for carriage of broadcast stations in effect on April 15, 1976, and each station's television market as currently defined by the Commission. A cable system pays royalties based upon a sliding scale of percentages of its gross receipts depending upon the number of DSEs the station incurs. The greater the number of distant signals a system carries, the greater the percentage the system must apply against its gross receipts and the greater the royalty it will pay under the cable compulsory license.

The statutory rates and percentages applied by cable systems have changed over the years pursuant to rate adjustment proceedings that were held by the now-defunct Copyright Royalty Tribunal and the Copyright Office by authority of the statute. The annual royalty funds collected by the Copyright Office have been distributed to copyright owners pursuant to settlement or distribution proceedings before the same bodies.

The satellite carrier compulsory license was created by the Satellite Home Viewer Act of 1988. The license was due to expire at the end of 1994 but was extended by Congress for an additional five years. The satellite license operates in many respects like the cable license, but with a far simpler royalty calculation method.

The satellite compulsory license allows satellite carriers to retransmit superstation signals to home dish owner subscribers located anywhere in the United States, and to retransmit network signals only to "unserved households." Unserved households are those that cannot receive an over-the-air signal of Grade B intensity of a network station using a conventional rooftop antenna, and that have not received the signal from a cable system within the previous 90 days. After the amendment of the satellite carrier compulsory license in 1994, Congress adopted a "fair market value" standard for adjusting the royalty rates of the satellite license.

II. SHOULD THE CABLE AND SATELLITE CARRIER COMPULSORY LICENSES CONTINUE TO EXIST?

Compulsory licenses are an exception to the copyright principle of exclusive ownership for authors of creative works, and, historically, the Copyright Office has only supported the creation of compulsory licenses when warranted by special circumstances. With respect to the cable and satellite compulsory licenses, those special circumstances were initially seen as the difficulty and expense of clearing all rights on a broadcast signal. However, as early as 1981, the Copyright Office had recommended the elimination of the cable compulsory license and full copyright liability for cable systems' retransmission of distant signals, based on a finding that the cable industry had progressed from an infant industry to a vigorous, economically stable industry which no longer needed the protective support of the compulsory license.

Revisiting the issue, and factoring in the satellite compulsory license, the Copyright Office finds that for licensing the copyrighted works retransmitted by cable systems and satellite carriers, the better solution is through negotiation between collectives representing the owner and user industries, rather than by a government administered compulsory license. However, the comments demonstrate that the cable and satellite licenses have become an integral part of the way broadcast signals are brought to the public, that business arrangements and investments have been made in reliance upon the compulsory licenses, and that the parties advocating elimination of the licenses at this time have not presented a clear path for such elimination at this time. For these reasons, the Copyright Office does not advocate the elimination of the compulsory licenses at the present time. The Copyright Office also believes that the satellite carrier industry should have a compulsory license to retransmit broadcast signals as long as the cable industry has one. Consequently, the Copyright Office would support the removal of the sunset date for the section 119 satellite compulsory license.

However, the Office recommends major revisions for both the cable and satellite compulsory licenses that would make them as simple as possible to administer, would provide the copyright owners with full compensation for the use of their works, and that would treat every multichannel video delivery system the

same, except to the extent that technological differences or differences in the regulatory burdens placed upon the delivery system justify different copyright treatment.

III. SHOULD THE CABLE AND SATELLITE CARRIER LICENSES BE HARMONIZED?

The commenters were nearly unanimous that the cable and satellite carrier compulsory licenses should remain separate because the two signal delivery industries are different in nature and are subject to different communications regulation. For example, the cable technology is terrestrially based and delivers a mix of local and national programming in relatively local markets, while satellite systems deliver mostly national programming on a national basis from satellites whose footprints cover the entire continental United States.

The Copyright Office concludes that merging section 111 and 119 into a single section would not lead toward any practical benefit to the public administration of the licenses and, therefore, the Office agrees that the two sections should not be merged. However, the Office does agree with the rationale behind the idea of harmonization. That is, any existing differences between the copyright treatment of cable retransmissions and of satellite retransmissions should be removed where possible so that the compulsory licenses do not affect the competitive balance between the satellite carrier and cable industries.

IV. SHOULD THE CABLE RATE STRUCTURE BE REFORMED?

The cable compulsory license rate mechanism that was established in 1976 was based upon a Federal Communications Commission (FCC) cable regulatory structure that has not been in existence for a number of years. In addition, the cable royalty system is a three-tiered system with progressively higher rates for larger systems. These factors have resulted in many anomalies in royalty obligations, and many difficulties in royalty calculation that affect copyright owners, cable system operators, and the Copyright Office. The Copyright Office thoroughly examined many ideas for the reform of the royalty rate mechanism, and concluded as follows.

First, the Copyright Office recommends that section 111 be amended to make cable rates as simple as possible and reflect fair market value. This would eliminate many of the administrative costs and uncertainties created by the present royalty mechanism, eliminate undercompensation to authors, and treat cable systems similarly to satellite carriers.

Second, the Office recommends that Congress reconsider the royalty rate subsidy for small cable systems. If Congress does not eliminate the subsidy, the Office would urge Congress to raise the minimal payment paid by small cable systems to an amount that can be considered fair; now the minimal payment does not even meet the amount it costs the Copyright Office to process the payment.

Third, the Copyright Office recommends that Congress amend section 111(f) to define when two cable systems under common ownership or control are, in fact, one system for purposes of section 111 in light of technological advances in headends and in anticipation of open video systems being eligible as cable systems. If a flat, per subscriber fee is not adopted, the same part of section 111(f) should also be amended to calculate cable rates only on those subscriber groups that actually receive a particular broadcast signal, thus addressing the "phantom" signal problem.

To accomplish these goals, the Copyright Office urges Congress to amend section 111(f) to read, "For purposes of determining the royalty fee under subsection (d)(1), two or more cable systems under

common ownership or control that are either (a) in contiguous communities, (b) operating from the same headend, or (c) using the same open video system platform, shall be considered as one system. Once two or more cable systems have been deemed a single larger cable system, the calculation of the rates shall be based on those subscriber groups who receive the secondary transmission as the Register of Copyrights shall by regulation provide."

Fourth, the Copyright Office believes that a rate based on fair market value would obviate the need for a step-up rate such as the 3.75% rate for the retransmission of distant signals that exceeds a certain quota. The Office believes that so long as the marginal costs of each additional signal does not go down, that provides sufficient disincentive for the cable system to import an excessive number of distant signals. Therefore, in keeping with the Office's proposal that differences between the compulsory licenses be eliminated where possible, the Office recommends that the cable distant signal rates should be set at fair market value, with no step-up rate for any class of distant signals, just as the current satellite carrier rates are set.

V. HOW SHOULD THE CABLE RATE STRUCTURE BE REFORMED?

As a preliminary matter to determining the best rate structure model, the Office addressed how to improve the method by which the current section 111 distinguishes which signals are local or distant for a particular cable system. This issue needs to be addressed under any of the three models considered and should be addressed even if the current rate structure is retained.

The Copyright Office strongly urges Congress to eliminate any reference in section 111 to the now-defunct 1976 must-carry rules. Instead, Congress should simply move to the new ADI system of determining a television station's local market. For noncommercial educational stations, which the ADI system does not address, the Office recommends defining the local market of a station as an area encompassing 50 miles from the community of license of the station, including any communities served in whole or in part by the 50 mile

radius. The Copyright Office recommends similar treatment for determining when satellite carriers are retransmitting local or distant signals, as described in Chapter IX.

Having dealt with the issue of when a signal retransmitted by a cable system should be considered a distant signal, the Copyright Office turns to the issue of how to determine the amount of royalties a cable system should pay for its carriage of distant signals. The Office considered three models for reforming the section 111 rate structure to promote simplicity in administration of the license. Each of the models could be adjusted to provide for a marketplace rate. The three models are: (1) a flat, per subscriber, per signal fee similar to that paid by the satellite carriers; (2) a reform of the current gross receipts structure; and (3) a tariffing model proposed by Major League Baseball.

The Copyright Office rejected the tariffing system proposed by Baseball because it would simply replace one complex system with another. The Office then determined that either a reformed gross receipts model or the flat, per subscriber, per signal model would work well to achieve simplicity, certainty, equity, and efficiency.

As between the two models, the Office strongly recommends the flat, per subscriber, per signal fee because: it would eliminate the arbitrary royalty calculations that result when cable systems market channels on different tiers to manipulate their total gross receipts calculations; it would eliminate the time-consuming and complex calculations necessary for reporting subscriber groupings as discussed in Chapter IV; it would provide an easy comparison of the rates paid by cable systems and the rates paid by satellite carriers to facilitate the goal of achieving comparable rates between the two retransmission industries; and it would offer cable systems the flexibility to change their signal lineups monthly without incurring unintended additional royalty fees.

The Copyright Office also recommends that the statute be amended to cause a CARP to be convened to take evidence on what the flat, per subscriber, per signal rates (or the reformed gross receipts model rates) should be, based on the fair market value of the rates, the rates paid by satellite carriers keeping in mind the

regulatory and technological differences between the two industries, and the economic impact of the new rate structure on small cable systems. After the CARP has made its initial determination of cable rates, the Office recommends that all future rate adjustment proceedings be combined into a single cable-satellite rate adjustment proceeding to be conducted every five years so that the cable and satellite carrier industries can be compared by the same CARP panel at the same time.

VI. SHOULD THE CABLE COMPULSORY LICENSE APPLY TO OPEN VIDEO SYSTEM OPERATIONS?

The Telecommunications Act of 1996 creates the open video system as an entirely new framework for entering the video marketplace. In creating this new framework, which allows telephone companies and others to retransmit broadcast signals, Congress and the FCC strove to promote competition, to encourage investment in new technologies, and to maximize the consumers' choice of services. The Telecommunications Act treats open video systems similarly to cable systems by imposing must-carry and other carriage requirements. However, unlike a cable system operator, an open video system operator may act as a programmer itself on no more than one-third of its activated channel capacity, and it must carry programming for other video programmers on a non-discriminatory basis. The structure and appearance of open video systems remain largely unresolved at this time.

Without deciding whether open video systems might qualify as a section 111 cable system under the current statute, the Copyright Office believes that open video systems should be eligible for a cable compulsory license, and that the statute should be amended to facilitate open video systems' inclusion in section 111. The Copyright Office is swayed by the strong resemblance between open video systems and traditional cable systems in both technological and regulatory aspects. The Office agrees with the commenters who argue that it would be patently unfair, and that it would thwart Congress's intent in creating the open video system model, to deny the benefits of compulsory licensing to open video systems when

similar benefits are enjoyed by traditional cable systems, satellite carriers, SMATV systems, and MDS and MMDS operations.

The Copyright Office believes that section 111 should be amended in several ways to facilitate the eligibility of open video systems for the cable compulsory license. First, the definition of a cable system in section 111(f) should be amended to specifically include open video systems as cable systems, and to clarify that each programmer on the open video system is responsible for filing and paying royalties as a cable system. Furthermore, for purposes of identifying which open video system programmers must file together as one system to avoid artificial fragmentation of one larger system into smaller systems, it will be essential for Congress to amend the "contiguous communities" section of the definition of cable system.

Finally, both the complex rate structure in section 111 and the statute's reliance on the former FCC rules for determining local and distant signals should be amended, as discussed in Chapter V, to ensure the smooth administration of the compulsory license with open video systems as cable systems.

VII. THE PASSIVE CARRIER EXEMPTION.

The passive carrier exemption in section 111(a)(3) of the Copyright Act provides an exemption from copyright liability to any carrier who retransmits one or more broadcast signals so long as that carrier has "no direct or indirect control over the content or selection" of the broadcast signal being retransmitted or the recipients of the signal, and so long as its only involvement in the retransmission is to provide the "wires, cables, or other communications channels for the use of others." This provision was intended initially to ensure that telephone companies, whose wires and hardware were used as a conduit for the retransmissions made by cable systems, would not somehow be deemed to be infringers under the new Copyright Act of 1976.

The exemption came into wider use with the rise of superstations in the late-1970's. At that time satellite carriers became involved in the transmission of over-the-air signals to cable systems, and they, too, invoked the passive carrier exemption. Three mid-1980's appellate court decisions defined the scope of the

exemption in the satellite carrier context. When the development of home earth station (satellite dish) technology provided a new market for the retransmission of superstations (i.e., to home dish owners as well as to cable systems), the limits of the passive carrier exemption were explored. In 1986, Register of Copyrights Ralph Oman issued the Copyright Office view that the sale and licensing of descrambling devices to home dish owners by satellite carriers cannot be deemed passive activities within the purview of section 111(a)(3), particularly where the carrier itself encrypts the signal. Thus, for the delivery of superstations to home dish owners, Congress afforded satellite carriers a separate compulsory license, because they did not qualify for the passive carrier exemption in that context.

In this study, the Copyright Office reexamined the passive carrier exemption as it might apply to open video system operators who retransmit broadcast signals for independent programmers. At the same time, the Office considered the views of commenters regarding the entire scope of the exemption.

The Copyright Office concludes that if Congress amends the Copyright Act to clarify that open video systems are eligible for the cable compulsory license, then the passive carrier exemption should be amended to indicate that open video systems qualify for the section 111(a)(3) exemption only in very limited circumstances: when the open video system operator retransmits broadcast signals for an unaffiliated programmer and no stations invoke their must-carry privilege. In such limited circumstances, the open video system would be a truly passive carrier. The Copyright Office believes that providing ancillary services such as marketing, billing, and collecting would not be activities that would disqualify an operator from claiming the exemption. However, the Office takes the position that is consistent with its position regarding satellite carriers, that if an open video system operator for some reason had the need to scramble or otherwise encode its signals and provide decoders to subscribers, it would not qualify for the passive carrier exemption. However, Congress might consider creating a different exemption for open video systems that only retransmit must-carry signals.

The Copyright Office believes it is probable in most, if not all instances, that when open video system operators provide retransmission services for independent programmers, local broadcasters will invoke their must-carry rights against the operators. Then the operators will be required to retransmit the must-carry signal to the subscribers of the independent programmers. It is the Copyright Office's view that in making such carriage of local signals, the open video system operator would be publicly performing the copyrighted works embodied on the signal and must secure a compulsory license to avoid copyright liability. It would not be eligible for the passive carrier exemption. However, Congress might consider creating a different exemption for open video systems that only retransmit must-carry signals.

The Copyright Office also recommends that Congress may wish to reconsider the holding of the United States Court of Appeals for the Eighth Circuit in Hubbard Broadcasting, Inc. v. Southern Satellite Systems, 777 F.2d 393 (8th Cir. 1985), which permits a satellite carrier to invoke the passive carrier exemption even though it carries a signal on which national advertising has been substituted by the broadcaster for the local advertising on the over-the-air signal. The spirit of the law is that the signals should be retransmitted "as is." However, since it is the broadcaster who is making the alterations, not the satellite carrier, the question of who benefits, who's harmed, and whether this is a situation that needs to be remedied is not as clear as if the satellite carrier made the alterations. These issues were not fully briefed before the Office during the comment period, and therefore no conclusion was reached by the Office except that the issue deserves further study.

VIII. SHOULD THE CABLE COMPULSORY LICENSE BE EXTENDED TO THE INTERNET?

The next new multichannel program providers to claim eligibility for compulsory licensing are the Internet broadcasters of audio and some video events. One of these, AudioNet, Inc., described to the Copyright Office the "streaming" technology that, within two or three years, should make it possible for AudioNet to retransmit television broadcast signals to anyone anywhere in the world who has a computer

with audio capability and access to the World Wide Web. The quality of the audiovisual display for such retransmissions should be close to advanced digital television standards. AudioNet argues that Internet retransmitters should be eligible either for a section 111 cable compulsory license or a compulsory license of their own.

The Copyright Office concludes that it would be inappropriate for Congress to grant Internet retransmitters the benefits of compulsory licensing. The primary argument against an Internet compulsory license is the vast technological and regulatory differences between Internet retransmitters and the cable systems and satellite carriers that now enjoy compulsory licensing. The instantaneous worldwide dissemination of broadcast signals via the Internet poses major issues regarding the national and international licensing of the signals that have not been fully addressed by federal and international policymakers, and it would be premature for Congress to legislate a copyright compulsory license to benefit Internet retransmitters.

IX. THE UNSERVED HOUSEHOLD RESTRICTION IN THE SATELLITE CARRIER COMPULSORY LICENSE.

Section 119(a)(2)(B) of the Copyright Act provides that the compulsory license granted under section 119 for the retransmission of television network signals is limited to "persons who reside in unserved households." This provision of section 119 denies the satellite compulsory license to a satellite carrier that retransmits a network signal to a subscriber who already receives the signal of the network's local affiliate from another source. As such, it is a communications provision, modeled after the FCC's network nonduplication rules that apply to cable systems, which has been incorporated in the Copyright Act.

An unserved household, ineligible for receipt of a network signal from a satellite carrier, is defined in section 119(d)(10) as a household that cannot receive an over-the-air signal of Grade B intensity of an affiliate of a particular network, using a conventional rooftop antenna, and that has not subscribed to a cable system that delivers the signal of an affiliate of that network within the last 90 days. The enforcement

mechanism of the unserved household provision has proved problematic. Congress amended section 119 in 1994 to provide a transitional enforcement regime which allowed network affiliates to issue written challenges against subscribers receiving network service which it believed did not reside in unserved households. While the term of that transitional regime has expired, it was highly contentious while it lasted. Now broadcasters who believe they are aggrieved of violations of the unserved household restriction must once again resort to the traditional enforcement action of the Copyright Act, the infringement suit. Several such suits have been brought in the last year.

Another controversial issue that surrounds the unserved household issue is the question whether satellite carriers that retransmit the local network affiliates to subscribers who reside in the affiliates' local markets qualify for the section 119 license. The retransmission of local signals by satellite carriers was never before addressed in section 119 because the technology did not exist to make such local retransmission possible. However, it would appear that such technology is actively being developed and, if satellite carriers could retransmit the signals of local network stations to subscribers, the concern that led to the unserved household provision would theoretically become resolved.

Finally, PBS proposes the creation of a direct feed to satellite carriers of PBS programming (i.e., a national PBS satellite service) that would be exempt from the unserved household restriction.

The Copyright Office suggests that the concept of network program exclusivity protection is not appropriately located in the copyright law. If the section 119 license is extended, the Copyright Office recommends that Congress amend the Communications Act of 1934 to provide, or direct the FCC to adopt, network exclusivity (and for that matter, syndicated exclusivity) protection for satellite retransmissions of broadcast signals. Should Congress decline to do so, the Copyright Office admits that satellite subscriber eligibility for network signals is a problematic issue with few immediate solutions. In an attempt to improve the current unserved household provisions, the Copyright Office makes some further suggestions.

First, the Office notes that a technological solution would be the best solution in the unserved households debate. The problem can be eliminated entirely if technology and business practices advance to enable satellite carriers to retransmit local network affiliates to their subscribers. If the subscribers can purchase the signals of their local network affiliates, they have no need to import distant network signals, and there will be no "unserved households." To clarify the law with respect to such local retransmissions, the Copyright Office recommends that section 119 be amended to allow retransmission of all television broadcast stations, commercial as well as noncommercial educational, within each station's local market. The Office proposes that the local market for commercial stations be the same as defined by the FCC (i.e. ADI, and any modifications thereof), and for noncommercial educational stations all communities in whole or in part within 50 miles of each station's community of license. This definition parallels the definitions suggested by the Copyright Office in Chapter V of this study for local signals in the context of the cable compulsory license. The Office does not at this time take a position as to what royalty rate, if any, should apply to local retransmissions.

Given that local retransmission has yet to be accomplished commercially in the satellite industry, the Office recommends that any extension of the section 119 license must include revision of the unserved household restriction. The Office rejects the substitution of a picture quality standard for the Grade B standard as too subjective, legally insufficient, and administratively unworkable. Likewise, the Office finds the Grade B standard less than precise and cost inefficient when applied to individual household determinations.

If Congress declines to take network program exclusivity protection out of the copyright law and put it into the communications law, the Copyright Office proposes a "red zone/green zone" approach to the problem. The Office recommends that satellite carriers be permitted to retransmit a network signal to all subscribers located outside the local market of an affiliate station of that network (the "green zone"). The satellite carriers would be prohibited from retransmitting the network signal to subscribers located within

the local market area of an affiliate station of that network (the "red zone"). The Office recommends that satellite carriers, and their distributors, be required to disclose to any potential subscribers whether that subscriber resides in a "red zone" or "green zone" with respect to each network signal offered by the satellite carrier.

The Office is highly skeptical that a system can be devised that would accurately and fairly permit the retransmission of network signals to certain "unserved" subscribers within the "red zone" without authorizing some decision-making body to make individual determinations of eligibility. In lieu of creating such a bureaucracy, the Office suggests that Congress consider a transitional solution to the problem until either: (1) satellite carriers implement local retransmission of network signals, or (2) over-the-air digital television becomes a widespread medium and offers a clear standard for determining when a subscriber receives over the air a network signal with good picture quality. For this transitional solution, the Copyright Office would support allowing a satellite carrier to retransmit a network signal to subscribers located in a "red zone" if such subscribers pay a surcharge to the Copyright Office for distribution to the affiliates via the royalty distribution procedures of chapter 8 of the Copyright Act. The rate for such a surcharge would be established by a CARP.

PBS national satellite service would be exempted from the "red zone" provision. In addition, the Copyright Office recommends that Congress eliminate the 90-day waiting period for subscribing to network signals.

X. ADDITIONAL ISSUES

A. TREATMENT OF NETWORK SIGNALS

Under the cable compulsory license, distant network signals count as only one-quarter of a distant signal equivalent (DSE), as opposed to the full DSE accorded a distant independent station. Thus, large cable systems pay four times as much to retransmit an independent station as they pay to retransmit a network station. This ratio was carried over in the satellite carrier compulsory license, where satellite carriers pay 12 cents per subscriber to retransmit a superstation and 3 cents per subscriber to retransmit a network signal. One commenter argues that the rates for network and independent stations should be equalized because subscribers receive valuable programming on network signals, and copyright owners in that programming should be compensated. The Copyright Office agrees that in both the cable and satellite compulsory licenses, the rates paid by the licensees for the retransmission of network signals should be equalized with the rates paid for the retransmission of independent signals (or superstations). The Office, therefore, supports raising the value of network signals to one full DSE for cable systems under the present royalty regime. Furthermore, the Copyright Office recommends that Congress amend section 111(d)(3) to allow owners of network programming to qualify for a distribution of cable royalties, as they qualify for distribution of royalties under the satellite license.

B. PAYMENT FOR LOCAL SIGNALS

Although the Copyright Office has declined to comment as to the royalty compensation due for local retransmission of signals by satellite carriers, the Office does make the following observations about payment for the retransmission of local signals under section 111. Under the current law, every cable system pays a minimum copyright royalty fee, whether or not it carries any distant signals. The Copyright Office believes that the minimum fee is an important aspect of the cable compulsory license and should be retained. The Copyright Office reiterates that retransmissions of broadcast signals, either local or distant, are public

performances within the meaning of the Copyright Act and, therefore, fall within the exclusive rights granted by copyright protection.

XI. RECOMMENDATIONS

In Chapter XI, the Copyright Office summarizes and reiterates the recommendations from Chapters I through X that the Office is sending to Congress.

INTRODUCTION

On February 6, 1997, Senator Orrin Hatch, Chairman of the Committee on the Judiciary, United States Senate, sent a letter to the Register of Copyrights requesting the Copyright Office to conduct a global review of the copyright licensing regimes governing the retransmission of over-the-air radio and television broadcast signals. Senator Hatch asked the Office to report its findings to the Committee and to develop policy options and legislative recommendations by May 1, 1997. The reporting date was extended, at the Office's request, to August 1, 1997.

In making his request, Senator Hatch identified several issues regarding the copyright implications of broadcast retransmissions which warrant consideration. Specifically, these included the advisability of the extension of the compulsory copyright license created by the Satellite Home Viewer Acts of 1988¹ and 1994,² the disputes surrounding the implementation of that compulsory license, and the "unserved household" restriction for the retransmission of network television stations. Additionally, Senator Hatch asked the Office to consider harmonization of the cable and satellite carrier compulsory licenses of the Copyright Act, and whether to extend those licenses to new technologies, such as local retransmission of broadcast signals by satellite, retransmission of broadcast signals over the Internet and by telephone companies, and new markets for public television.

In conducting the fact-finding phase for this report, the Copyright Office scheduled three days of public meetings and solicited comments and reply comments from all interested parties. Comments were filed with the Office before the public meetings and reply comments were filed within one month after the public meetings. This arrangement provided all participants ample time and opportunity to express their views and respond to alternative perspectives.

¹ Satellite Home Viewer Act of 1988, Pub. L. No. 100-667, 102 Stat. 3949-3960 (1988) [hereinafter Pub. L. No. 100-667 (1988)].

² Satellite Home Viewer Act of 1994, Pub. L. No. 103-369, 103 Stat. 3477 (1994) [hereinafter Pub. L. No. 103-369 (1994)].

Forty-three parties filed comments in response to the Notice of Inquiry (NOI), and thirty-five parties filed reply comments. These comments addressed a multitude of questions posed by the Office concerning, for example, the continued need for the licenses, the harmonization of the licensing scheme, and possible amendments to the current licenses. More specifically, the comments addressed the extension of the Satellite Home Viewer Act 1994, disputes surrounding the identification of and service to "unserved households," the adaptation of the current license to the emerging spot beam technology and "open video systems," and the applicability of the licenses to the Internet.

During the three days of public meetings, twenty-four witnesses presented testimony to the Register of Copyrights and her staff on a variety of issues concerning the retransmission of broadcast signals under the cable and satellite compulsory licenses. Representatives from the motion picture industry, cable television, the broadcasting industry, local television, sports associations, Internet audio services, performing rights societies, satellite carriers, small business interests, and the telephone industry each addressed, within the context of a compulsory licensing scheme, topics raised by recent advances in technology and changes in the multichannel video programming market.

These meetings and the comments reflected no consensus among the users or the copyright owners about the future of the licenses. Cable operators found the current cable compulsory licensing adequate and not in need of any major revision, unlike the copyright owners, who preferred abolishing the entire compulsory licensing scheme, or in the alternative, moving toward a marketplace solution through the use of rates based on fair market value in both the satellite and cable compulsory licenses. Similarly, satellite carriers sought comparable rate structures in both licenses, but advocated that the satellite rate structure be adjusted to resemble more closely the cable license rate structure. The satellite carriers also voiced a need for a permanent satellite compulsory license as a means to become more competitive with the cable industry. While it is clear that there are no easy answers to the questions posed by the emergence of new technology (spot beaming, "open video systems," and the Internet), it is essential that the current compulsory licenses

be reevaluated in light of these technological changes and shifts in how the industries conduct their businesses.

I. THE CURRENT SYSTEM OF COPYRIGHT LICENSING FOR BROADCAST RETRANSMISSIONS

There are currently two compulsory licenses in the Copyright Code, 17 U.S.C. § 101 *et. seq.*, governing the retransmission of broadcast signals. A compulsory copyright license is a statutory copyright licensing scheme whereby copyright owners are required to license their works to users at a government fixed price and under government set terms and conditions. The cable compulsory license, 17 U.S.C. § 111, allows a cable system to retransmit both radio and television broadcast programming to its subscribers who pay a fee for such service. The satellite carrier compulsory license, 17 U.S.C. § 119, permits a satellite carrier to retransmit television broadcast programming (but not radio) to satellite home dish owners for their private home viewing. The satellite carrier compulsory license is scheduled to expire on December 31, 1999; the cable compulsory license has no sunset provision.

Senator Hatch requested that the Copyright Office examine and consider revision of these compulsory licenses, as well as the possibility of combining the two into a single license to cover all broadcast retransmissions. In addition, Senator Hatch requested that the Office focus on specific issues related to each of the licenses, as well as to compulsory licensing in general. This report examines and addresses each of these requests.

A. THE CABLE COMPULSORY LICENSE

The cable compulsory license applies to any cable system that carries radio and television broadcast signals in accordance with the rules and regulations of the Federal Communications Commission (FCC). These systems are required to submit royalties for the carriage of their signals on a semiannual basis in accordance with prescribed statutory royalty rates. The royalties are submitted to the Copyright Office, along with a statement of account reflecting the number and identity of the broadcast signals carried, the gross

receipts from subscribers for those signals, and other relevant filing information. The Copyright Office deposits the collected funds with the United States Treasury for later distribution to copyright owners of the broadcast programming through the procedure described in chapter 8 of the Copyright Act.

Creation of the cable compulsory license was premised on two significant congressional considerations: first, the perceived need to differentiate for copyright payment purposes between the impact of local versus distant broadcast signals carried by cable operators; and, second, the need to categorize cable systems by size based upon the dollar amount of receipts a system receives from subscribers for the carriage of broadcast signals. These two considerations played a significant role in deciding what economic effect cable systems had on the value of copyrighted works shown on broadcast television.³ Congress concluded that a cable operator's carriage of local broadcast signals did not affect the value of the works broadcast because the signal was already available to the public for free through over-the-air broadcasting. Therefore, the compulsory license essentially allows cable systems to carry local signals for free.⁴ Congress also determined that distant signals do affect the value of copyrighted programming because local advertisers, who provide the principal remuneration to broadcasters enabling broadcasters to pay for programming, are not willing to pay increased advertising rates for cable viewers in distant markets who cannot be reasonably expected to purchase their goods. Increased viewership of the programming through distant signal importation by cable systems goes uncompensated because advertisers will not pay for it. As a result, broadcasters cannot pay greater sums to copyright owners. The classification of a cable system, by size, based on its income from subscribers, assumes that only the larger systems which import distant signals have any significant economic impact on copyrighted works.

³ See H.R. Rep. No. 1476, 94th Cong., 2d Sess. 90 (1976) [hereinafter H.R. Rep. No. 1476].

⁴ It should be noted, however, that cable systems which carry only local signals and no distant signals (a rarity) are still required to submit a statement of account and pay a basic minimum royalty fee.

Section 111 distinguishes among three sizes of cable systems according to the amount of money a system receives from subscribers for the carriage of broadcast signals. The first two classifications are small to medium-sized cable systems known as Form SA-1's and Form SA-2's, in accordance with the title of the statement of account form which they file with their royalty payments. Form SA-1's pay a flat rate (currently \$28 per half year) for carriage of all signals, while Form SA-2's pay a percentage of gross receipts received from subscribers for carriage of broadcast signals irrespective of the number of distant signals they carry. The large systems, Form SA-3's, pay in accordance with a highly complicated and technical formula, principally dependent on how the FCC regulated the cable industry in 1976. This formula allows the systems to distinguish between carriage of local and distant signals and to pay accordingly. The vast majority of royalties paid under the cable compulsory license come from the large cable systems.

The royalty scheme for the large cable systems employs the statutory device known as the distant signal equivalent (DSE). Distant signals are determined in accordance with two sets of FCC regulations: the "must-carry" rules for broadcast stations in effect on April 15, 1976, and a station's television market as currently defined by the FCC. 17 U.S.C. § 111(f). A signal is distant for a particular cable system when that system would not have been required to carry the station under the FCC's must-carry rules, and the system is not located within the station's television market. 17 U.S.C. § 111(f).

Cable systems pay for carriage of distant signals based upon the number of DSE's they carry. The statute defines a DSE as "the value assigned to the secondary transmission of any nonnetwork television programming carried by a cable system in whole or in part beyond the local service area of a primary transmitter of such programming." 17 U.S.C. § 111(f). A DSE is computed by assigning a value of one to a distant independent broadcast station, and a value of one-quarter to distant noncommercial educational and network stations which do have a certain amount of nonnetwork programming in their broadcast days. A cable system pays royalties based upon a sliding scale of percentages of its gross receipts depending upon

the number of DSE's it carries. The greater the number of DSE's, the higher the total percentage of gross receipts and, consequently, the larger the total royalty payment.

As noted above, operation of the cable compulsory license is intricately linked with how the FCC regulated the cable industry in 1976. 17 U.S.C. 111(b),(c),(f). The FCC regulated cable systems extensively, restricting them in the number of distant signals they could carry (the distant signal carriage rules), and requiring them to black-out programming on a distant signal where the local broadcaster had purchased the exclusive rights to that same programming (the syndicated exclusivity rules). In 1980, however, the FCC took a decidedly deregulatory stance towards the cable industry and eliminated the distant signal carriage rules and the syndicated exclusivity ("syndex") rules.⁵ Cable systems were now free to import as many distant signals as they desired.

Pursuant to its statutory authority, and in reaction to the FCC's action, the Copyright Royalty Tribunal conducted a rate adjustment proceeding for the cable compulsory license to compensate copyright owners for the loss of the distant signal carriage rules and the syndex rules. This rate adjustment proceeding produced two new rates applicable to large cable systems making section 111 royalty payments. 47 Fed. Reg. 52,146 (1982). The first, to compensate for the loss of the distant signal carriage rules, was the adoption of a royalty fee of 3.75% of a cable system's gross receipts for carriage of each distant signal that would not have previously been permitted under the former distant signal carriage rules.

The second rate, adopted by the Copyright Royalty Tribunal to compensate for the loss of the syndex rules, is known as the syndex surcharge. Large cable operators must pay this additional fee when the programming appearing on a distant signal imported by the cable system would have been subject to black-out protection under the FCC's former syndex rules.⁶

⁵ Mahite T.V. v. F.C.C., 652 F. 2d 1140 (2d Cir. 1981), cert. denied sub. nom., National Football League, Inc. v. F.C.C., 454 U.S. 1143 (1982).

⁶ Royalties collected from the syndex surcharge have decreased considerably in recent years because the FCC
(continued...)

Since the Tribunal's action in 1982, the royalties collected from cable systems have been divided into three categories for distribution to copyright owners to reflect their origin: 1) the "Basic Fund," which includes all the royalties collected from SA-1 and SA-2 cable systems, and the royalties collected from large SA-3 systems for the carriage of distant signals that would have been permitted under the FCC's former distant signal carriage rules; 2) the "3.75% Fund," which includes the royalties collected from large cable systems for distant signals whose carriage would not have been permitted under the FCC's former distant signal carriage rules; and 3) the "Syndex Fund," which includes the royalties collected from large cable systems for carriage of distant signals containing programming that would have been subject to black-out protection under the FCC's former syndex rules.

In order to be eligible for a distribution of royalties, a copyright owner of broadcast programming retransmitted by one or more cable systems must submit a written claim to the Copyright Office. Only copyright owners of nonnetwork broadcast programming are eligible for a royalty distribution. 17 U.S.C. § 111(d)(3). Eligible copyright owners must submit their claims in July for royalties collected from cable systems during the previous year. 17 U.S.C. § 111(d)(4)(A). Once the claims have been processed, the Librarian of Congress determines whether there are controversies among the parties filing claims as to the proper division and distribution of royalties. If there are no controversies -- meaning that the claimants have settled among themselves as to the amount of royalties each claimant is due -- then the Librarian distributes the royalties in accordance with the claimants' agreement(s) and the proceeding is concluded. The Librarian must initiate a distribution proceeding in accordance with the provisions of chapter 8 of the Copyright Act for those claimants who do not agree. 17 U.S.C. § 801.

In addition to compulsory licensing under section 111, copyright owners and cable operators are free to enter into private licensing agreements for the retransmission of broadcast programming. Under a private

(...continued)

has reimposed syndicated exclusivity protection in certain circumstances.

licensing agreement, the parties step outside the licensing regime of section 111 and negotiate their own terms and royalty rates for the retransmission of broadcast programming. Private licensing occurs most frequently in the context of particular sporting events, where a cable operator wishes to retransmit a sporting event carried on a distant broadcast station, but does not wish to carry the station on a full-time basis.⁷ The practice of private licensing is not widespread as most cable operators rely exclusively on the cable compulsory license.

B. THE SATELLITE CARRIER COMPULSORY LICENSE

The cable compulsory license was enacted as part of the Copyright Act of 1976 and is indefinite. In the mid-1980s, the home satellite dish industry grew significantly, and satellite carriers had the opportunity to retransmit broadcast programming to home dish owners. In order to facilitate this business, Congress passed the Satellite Home Viewer Act of 1988,⁸ which created the satellite carrier compulsory license found in 17 U.S.C. § 119.

The satellite carrier compulsory license is similar in many respects to the cable license. The license allows satellite carriers to retransmit television broadcast signals (but not radio) to their subscribers upon semiannual submissions of statements of account and royalty fees to the Copyright Office. The calculation of the royalty fees under the satellite carrier license is, however, significantly different from that of the cable compulsory license. Rather than determine royalties based upon a complicated formula of gross receipts and application of outdated FCC rules, royalties under section 119 are calculated on a flat, per subscriber, per signal fee basis. Television signals are divided into two categories -- superstation signals (i.e. commercial independent stations) and network signals (commercial network stations and noncommercial educational stations) -- each with its own attendant royalty rates. Satellite carriers multiply the respective royalty rate

⁷ Under the cable compulsory license, a cable operator that carries any part of a broadcast signal, no matter how momentary, must pay royalties for the signal as if it had been carried for the full six months of the accounting period.

⁸ Pub. L. No. 100-667 (1988).

for each signal they carry by the number of subscribers who receive the signal. This calculation is done for each of the six months of the accounting period, and the total fees yielded equals the semiannual royalty payment.

Satellite carriers may use the satellite carrier compulsory license to retransmit superstation signals to subscribers located anywhere in the United States. The same is not the case, however, for the retransmission of network signals. A satellite carrier may only make use of the satellite compulsory license for the retransmission of network signals to "unserved households." The statute defines an unserved household as one that cannot receive an over-the-air signal of Grade B intensity of a network station using a conventional rooftop antenna and has not received the signal from a cable system within the previous 90 days. 17 U.S.C. § 119(d). Section 119 requires satellite carriers to provide the television networks with subscriber lists to facilitate the determination by broadcasters as to whether subscribers receiving network signals in fact reside in unserved households.

The satellite carrier compulsory license created by the Satellite Home Viewer Act of 1988 was intended to expire at the end of 1994. Instead, in that year, Congress re-authorized the license for an additional 5 years, and made some changes to the license.⁹ The two most significant changes made by the Satellite Home Viewer Act of 1994 involved creation of a temporary mechanism designed to allow broadcasters to target impermissible service of network signals,¹⁰ and adoption of a "fair market value" standard for adjusting the royalty rates of the license.

The purpose of the transitional signal intensity measurement regime was to enable network broadcasters to eliminate service of network signals to subscribers who did not reside in unserved households without incurring the cost of bringing copyright infringement suits. For two years, 1995 and 1996, the statute authorized network affiliate stations to issue written challenges to satellite carriers for any subscribers that

⁹ Pub. L. No. 103-369 (1994).

¹⁰ This procedure, known as the signal intensity measurement procedure, expired on December 31, 1996.

they believed were not entitled to receive network carriage from the carrier. If the subscriber resided in the Grade B contour of the challenging station (generally thought to be the station's over-the-air service area), the satellite carrier, upon receiving the challenge, had the option of either turning off the subscriber's service of that network, or conducting a measurement of the intensity of the signal arriving at the subscriber's rooftop antenna. If that measurement indicated that the subscriber did receive a signal of Grade B intensity, then the carrier would absorb the cost of the test and immediately turn off service of that network signal. If the test revealed that the subscriber did not receive a signal of Grade B intensity, then service could continue and the challenging broadcast station was responsible for reimbursing the satellite carrier for the cost of the measurement. 17 U.S.C. § 119(a)(8).

The transitional signal measurement provisions of the Satellite Home Viewer Act of 1994 were not satisfactory. While many challenges were issued, few if any tests were conducted. Principal reasons given for the lack of testing were that the cost of a test exceeded the revenues received from the subscriber for receipt of network signals, and the failure to reach agreement as to the parameters of an appropriate test. Subscribers lost their network service without a determination as to whether or not they were unserved households and without any means of determining if their service could be restored. Moreover, the transitional signal measurement provisions did not solve the broadcasters' concern about avoiding copyright infringement litigation. Recently, broadcasters filed several lawsuits against one satellite carrier alleging violation of the unserved household provision of section 119.¹¹

The second significant change made by the Satellite Home Viewer Act of 1994 involved a change in the standard used to adjust the royalty rates for superstation and network signals. Under the Satellite Home Viewer Act of 1988, an arbitration panel was directed to adjust the royalty rates in 1991 according to a number of established statutory criteria. These criteria included considering the cost paid by cable operators under the cable compulsory license for the retransmission of broadcast signals, as well as the fees

¹¹ See text at note 117.

paid for retransmission of broadcast signals under any privately negotiated licenses. The 1994 Act replaced these criteria by directing the arbitration panel to adjust the royalty rates to yield royalty fees that reflect the fair market value of the programming contained on the signals. The arbitration proceeding applying this standard is currently underway, and a final determination will be issued in the fall of this year.

Unlike the cable compulsory license, the satellite carrier compulsory license has a statutory sunset, and is scheduled to expire at the end of 1999. Consideration of whether or not to extend the license and, if so, under what conditions, is one of the focal points of this report.

II. SHOULD THE CABLE AND SATELLITE CARRIER COMPULSORY LICENSES CONTINUE TO EXIST?

A. HISTORY

Since its inception, copyright law has been designed to promote the production of creativity by conferring to authors the exclusive right to exploit their works. Compulsory licensing is an exception to the rule of exclusive ownership and, therefore, has been supported by the Copyright Office only when "warranted by special circumstances."¹²

With respect to the cable and satellite carrier licenses, those special circumstances concern the difficulties and costs of clearing all rights on a broadcast signal. In 1976, Congress found "that it would be impractical and unduly burdensome to require every cable system to negotiate with every copyright owner whose work was retransmitted by a cable system."¹³ Congress, therefore, created the cable compulsory license for the secondary transmission of broadcast signals. For those same reasons, the Copyright Office supported the creation of the cable compulsory license at that time.¹⁴

As early as 1981, however, the Copyright Office recommended to Congress that the cable compulsory license be abolished,

The general principle of the copyright law is that copyright owners are entitled to receive fair compensation for the public performance of their works, especially in the case of performances for profit. Cable systems perform copyrighted works for profit when they make secondary transmissions of such works. Copyright owners will be more confidently assured of rightful compensation if that compensation is determined by contract and the market rather than by compulsory license.

¹² *Private Use, Private Property and Public Policy: Home Recording and Reproduction of Protected Works*, David Ladd, Register of Copyrights, p. 44, presented at the VIII Congress of INTERGU, September, 1981.

¹³ H.R. Rep. No. 1476, at 89.

¹⁴ *Copyright Law Revision: Hearings on H.R. 2223 Before the Subcomm. On Courts, Civil Liberties, and the Administration of Justice of the House Comm. on the Judiciary*, 94th Cong., 1st Sess. 976-977 (1975) (letter of Barbara Ringer, Register of Copyrights).

In the last five years, the cable industry has progressed from an infant industry to a vigorous, economically stable industry. Cable no longer needs the protective support of the compulsory license.

A compulsory license mechanism is in derogation of the rights of authors and copyright owners. It should be utilized only if compelling reasons support its existence. Those reasons may have existed in 1976. They no longer do.¹⁵

At the same time that the Copyright Office recommended the elimination of the cable compulsory license and full copyright liability for distant signals, it recommended an exemption from copyright liability for local signals and imported network signals where no local network signal was available.¹⁶

During the 1980s, several bills were introduced to eliminate the cable compulsory license for any cable system serving more than 2,500 subscribers on the ground that larger cable systems had matured to the point where they could negotiate with the copyright owners directly.¹⁷

After the D.C. Circuit Court of Appeals found in 1985 that the FCC's cable must-carry rules,¹⁸ as written and as justified, were unconstitutional, bills were introduced in the late 1980's that would have eliminated the cable compulsory license, but would have continued the compulsory license for those systems that agreed to carry all the television stations in their market.¹⁹

¹⁵ *Copyright/Cable Television: Hearings on H.R. 1805, H.R. 2007, H.R. 2108, H.R. 3528, H.R. 3530, H.R. 3560, H.R. 3940, H.R. 5870, and H.R. 5949 Before the Subcomm. On Courts, Civil Liberties, and the Administration of Justice, Pt. 1, 97th Cong., 1st and 2d Sess. 959-960 (1981) (statement of David Ladd, Register of Copyrights, U.S. Copyright Office).*

¹⁶ *Id.* at 903.

¹⁷ H.R. 3528, 97th Cong., 1st Sess. (1981), H.R. 1388, 98th Cong., 1st Sess. (1983); H.R. 3339, 99th Cong., 1st Sess. (1985).

¹⁸ *Quincy Cable TV, Inc. v. FCC*, 768 F.2d 1434 (D.C. Cir. 1985), *cert. denied sub nom.*, *National Association of Broadcasters v. Quincy Cable TV, Inc.*, 476 U.S. 1169 (1986). *But, see*, *TBS, Inc. v. FCC*, 65 U.S.L.W. 4208 (1997), where the Supreme Court affirmed the 1992 must-carry rules as constitutional.

¹⁹ S. 2529, 100th Cong., 2d Sess. (1988); H.R. 4293, 100th Cong., 2d Sess. (1988); S. 177, 101st Cong., 1st Sess. (1989); H.R. 109, 101st Cong., 1st Sess. (1989).

1. The Introduction of Satellite Carrier Retransmissions.

While Congress was reviewing its approach to cable retransmission during the 1980s, satellite carrier retransmissions created a competing industry. Although the industry began with the unauthorized interception of broadcast signals, Congress amended Section 605 of the Communications Act in 1984 to allow home dish owners to intercept broadcast signals under certain conditions.²⁰ In so acting, Congress only resolved the communications policy aspect. There still remained the question of copyright liability for satellite retransmissions of broadcast signals.

In 1988, the Copyright Office supported the creation of the satellite carrier compulsory license believing that a marketplace structure for the purchase of satellite retransmitted programming was not immediately feasible, but the Office also supported an early sunset to the satellite carrier compulsory license, favoring a marketplace approach for clearing copyrights in place of an indefinite or permanent compulsory license.²¹ Copyright owners also supported the license's creation because they saw the satellite carrier industry as a potentially valuable competitor to cable.²²

Congressional intent, as expressed in the House Judiciary Committee Report on the 1988 bill, stated, "The bill rests on the assumption that Congress should impose a compulsory license only when the marketplace cannot suffice."²³ Similarly, the House Energy and Commerce Committee Report called the

²⁰ *Cable Communications Policy Act* of 1984, Pub. L. No. 98-549, 98th Cong., 2d Sess., § 605(b) (1984).

²¹ *Satellite Home Viewer Copyright Act: Hearings on H.R. 2848 Before the Subcomm. On Courts, Civil Liberties and the Administration of Justice on the House Comm. on the Judiciary*, 100th Cong., 2d Sess. 174 (1988) (statement of Ralph Oman, Register of Copyrights, Copyright Office).

²² "As you know, the leaders in the motion picture industry . . . have been very concerned about competition to the cable industry. The concentration that grows seemingly everyday in the hands of a few large MSOs is of concern to us. . . . [T]here should be competition to the cable industry. Cable . . . enjoys the benefits of compulsory license. This small competitor should enjoy the same benefit." *Id.* at 83. (statement of Timothy A. Boggs, MPAA).

²³ H.R. Rep. No. 887, Part 1, 100th Cong., 2d Sess. 15 (1988).

satellite carrier license "a temporary, transitional statutory license to bridge the gap until the marketplace can function effectively."²⁴

In 1994, the satellite carrier license was extended for another 5 years on the basis that "a marketplace solution for clearing copyrights in broadcast programming retransmitted by satellite carriers is still not available."²⁵

The Copyright Office supported the extension of section 119 for three reasons: (1) it would resolve the litigation that was taking place at that time between the Copyright Office and satellite carriers concerning whether satellite carriers would qualify for a section 111 license in the absence of a section 119 license; (2) it would assure access to broadcast signals, and thus increase the ability of satellite carriers to attract investment capital for the then new DBS services; and, as a result, (3) it would guarantee the satellite carrier's position as a strong and significant competitor of cable.²⁶

Asto any extension of the satellite carrier license beyond 1999, the Senate Judiciary Committee said:

While the committee stresses the importance of a private marketplace solution by the end of 1999, this is not necessarily the final extension of the satellite carrier compulsory license. It would be neither equitable nor good policy to subject the satellite industry, absent negotiated license agreements, to full copyright liability in the year 2000 while satellite's competitor, the larger, well-established cable industry, is allowed to enjoy the benefits of its own compulsory license indefinitely. The limited extension of section 119 permits Congress the opportunity to reconsider the position and relationship of satellite retransmissions in the copyright world 5 years from now and decide whether compulsory licensing is still the correct legislative solution. During its reconsideration the committee must

²⁴ H.R. Rep. No. 887, Part 2, 100th Cong., 2d Sess. 15 (1988).

²⁵ S. Rep. No. 407, 103d Cong., 2d Sess. 8 (1994) [hereinafter S. Rep. No. 407].

²⁶ *Cable and Satellite Carrier Compulsory Licenses: Hearing on H.R. 759 and H.R. 1103 Before the Subcomm. On Intellectual Property and Judicial Administration, 103d Cong., 1st Sess. 18-19 (1993)* (statement of Ralph Oman, Register of Copyrights, Copyright Office).

not overlook the relative position of the cable industry in that same world as well.²⁷

The first question before the Office in this inquiry is whether the time has come when the cable industry and the satellite carrier industries can, by resort to private marketplace mechanisms, overcome the transactional problems that were the original justification for Congress' creation of the licenses.

B. THE COMMENTS

1. The Cable License.

Representatives of the cable industry uniformly testified that the cable license is still needed. The National Cable Television Association (NCTA) asserts that the transactional problems for cable systems are, if anything, greater today than in 1976.²⁸ They cite the near tripling of cable systems (from 3,681 to almost 11,000), and the more than doubling of broadcast stations (from 706 to over 1,500) since 1976. They describe that in the absence of a license, negotiations would be required to obtain clearances for all programs on each station a system would want to carry, typically, nine local stations and three distant stations:

Every cable system in the United States would be forced to anticipate the programming that would be shown, identify the appropriate owner of the copyrighted works, negotiate for the rights to retransmit those works, and acquire the personnel and equipment to black out programming for which rights could not be obtained. And unlike cable networks, which have rights to authorize the nationwide carriage of their networks' programming, broadcasters may not have rights to authorize the retransmission of the works that make up their broadcast day.

NCTA, comment 34, at 6-7.

²⁷ S. Rep. No. 407, at 8.

²⁸ The National Cable Television Association is the principal cable television industry serving over 80% of the national cable customers and 100 cable network programs. National Cable Television Association, comment 34, at 1 [hereinafter NCTA, comment 34].

The Small Cable Business Association (SCBA) describes the costs of clearing the rights as two-fold.²⁹ There is the cost of the time of the employee or employees of the system, and there is the cost of outside assistance to negotiate the agreements. SCBA estimates that small cable operators would likely incur at least \$10,000 in outside counsel fees to clear the rights to an average of five broadcast signals per system. That cost would represent anywhere between \$10 and \$200 per subscriber for the 75% of all cable systems that have 1,000 or fewer subscribers in their system. SCBA, comment 9, at 3-5.

The SCBA also warns that small cable systems have difficulty negotiating equitable rates for programming because of unequal bargaining power, and therefore, in a private marketplace they would end up paying more for their programming than the large operators. Although the small operators have recently formed a buying co-operative, the National Cable Television Co-operative (NCTC), the SCBA reports that several major programmers have refused to deal with the NCTC. Id. at 6-7. The Wireless Cable Association International, Inc. (WCA),³⁰ representing MMDS systems, also claims its wireless cable operators lack any market power to negotiate. WCA, reply comment 4, at 3.

The Cable Telecommunications Association (CATA)³¹ notes that even when a small cable system is owned by a large MSO, it still needs the compulsory license, because, under FCC cable rate regulation, a smaller cable system may not be cross subsidized by its parent organization.³²

²⁹ The Small Business Association represents almost 300 small cable operators, most of whom serve fewer than 1,000 subscribers. Small Cable Business Association, reply comment 33, at 1 [hereinafter SCBA, reply comment 33 or comment 8].

³⁰ The Wireless Cable Association International, Inc. is the principal trade association representing the wireless cable industry. Its membership includes most wireless cable operators in the United States, licensees of many of the Multipoint Distribution Service stations and Instructional Television Fixed Service stations that lease transmission capacity to programming and manufacturers of wireless cable transmission and reception equipment. Wireless Cable Association International, Inc., reply comment 4, at 1 [hereinafter WCA, reply comment 4].

³¹ The Cable Telecommunications Association represents owners and operators of cable television systems serving approximately eighty percent of the nation's cable television subscribers. Cable Telecommunications Association, comment 21, at 1 [hereinafter CATA, comment 21 or reply comment 23].

³² Transcript, *Copyright Office Hearing on Compulsory Licenses*, 408 (May 7, 1997) (testimony of Stephen R. (continued...))

Certain copyright owners also support retention of the cable compulsory license because they fear that their modest incomes from the cable license would be reduced severely by the transaction costs of negotiating in the free marketplace. National Public Radio (NPR)³³ states that it and its member stations currently receive \$200,000-\$300,000 a year in section 111 royalties, but "this income would likely disappear as a result of the increased cost of negotiating individual licenses and discontinued cable carriage of public radio stations." NPR, comment 36, at 6-7.

2. Other Reasons Offered For Retaining the Cable Compulsory License.

While the transaction costs of clearing the rights to the works on broadcast signals was the major reason cited by the commenters who urged that the cable compulsory license should continue to exist, they supported retaining the license for the following other reasons.

a. Heavily regulated arena. Commenters expressed the view that resort to free market negotiations for licenses to retransmit broadcast signals is not appropriate in a context where cable systems are so heavily regulated in every other respect by the FCC.

So long as one of the players, for instance, a broadcaster, gets the transmission medium from the Government for free while another competitor has to pay franchise fees just to build their own transmission medium, and the third competitor, the DBS industry now, has a split system where some of them under Government mandate were allowed to have spectrum for free and others have now had to pay for that spectrum, the Government is intimately involved in every step of telecommunications policy. . . . We are not free, for instance, in the cable industry not to carry local broadcast signals. We're required to carry those signals. That's the must-carry rule. It's not a free market. . . . If you got the government out of all of the aspects of telecommunications, then we might all be free to negotiate on an equal basis. CATA, tr., at 404-405.

See also, NCTA, comment 34, at 7-8.

(...continued)

Effros, President, Cable Telecommunications Association][hereinafter CATA, tr.].

³³ National Public Radio, Inc. is a non-profit membership organization representing 560 full-service public radio stations and managing the Public Radio Satellite Interconnection System. National Public Radio, Inc., comment 36, at 1 [hereinafter NPR, comment 36 or reply comment 14].

b. *Must-carry requirements.* Commenters also note that so long as must-carry obligations are imposed on cable systems, they cannot be required to carry all the local signals, and at the same time, negotiate freely for local signals, because the copyright owners know, in the end, that the cable systems are obliged to take the signal. "We can think of no comparably simple, efficient, and comprehensive way for must-carry to work, absent the local compulsory license."³⁴ NAB, tr., at 32.

c. *Marketplace adjustment.* Commenters observe that after 20 years, the marketplace has fully adjusted to the cable compulsory license. It is a system that generally works for all concerned. Program suppliers who sell to superstations such as WTBS know the programs will be distributed nationwide and charge accordingly. Similarly, sports leagues make private arrangements to compensate for the incursion of out-of-town sporting events into local markets. U.S. West,³⁵ comment 4, at 7-8.

Making a similar argument, The National Association of Broadcasters (NAB),³⁶ states that eliminating the cable license "would require substantial and costly modifications to existing marketplace mechanisms." NAB, comment 39, at 5. The Association of Local Television Stations (ALTV),³⁷ states that "the investment of time and resources necessary to establish a new private licensing scheme would be misplaced." ALTV, comment 30, at 9.

³⁴ *Copyright Office Hearing on Compulsory Licenses*, 32 (May 6, 1997)(testimony of Benjamin F.P. Ivins, Associate General Counsel [for Intellectual Property and International Legal Affairs] National Association of Broadcasters [hereinafter NAB, tr.].

³⁵ U.S. West, Inc. owns the third largest cable television distributor in the United States, Continental Cablevision. It serves about five million domestic cable customers and holds a partnership interest in Time Warner Entertainment as well as an array of video program and other production interests. US West, Inc., comment 4, at 1 [hereinafter US West, comment 4 or reply comment 13].

³⁶ The National Association of Broadcasters is an incorporated association of radio and television stations and broadcast networks, which serves and represents the broadcast industry. The National Association of Broadcasters, comment 39, at 1 [hereinafter NAB, comment 39 or reply comment 30].

³⁷ The Association of Local Television Stations, Inc. is a non-profit association of broadcast television stations unaffiliated with the ABC, CBS, or NBC television networks. The Association of Local Television Stations, Inc., comment 30, at 1 [hereinafter ALTV, comment 30 or reply comment 10].

d. Adequate compensation. Users of the compulsory license assert that the compulsory license system has served well to compensate copyright owners for the use of their works. United Video,³⁸ tr., at 511. The National Cable Television Association observed that the cable industry has paid \$2.3 billion in 20 years for the retransmission of copyrighted works. Currently, the payments amount to about \$170 million a year.³⁹ ALTV states that the record is lacking in establishing that the copyright owners have incurred any harm due to the compulsory license. ALTV, comment 30, at 7-8.

However, the copyright owners who testified in favor of eliminating the cable license assert they are undercompensated by the current compulsory license. MPAA,⁴⁰; NCAA,⁴¹; BMI,⁴² comment 27, at 12. "On average, cable operators pay less than 12 cents [per subscriber per month per signal] — or less than one-third of the market rate."⁴³ Baseball, comment 17, at 14.

e. Small system subsidy. The current cable license permits small cable systems to pay a lower fee for the retransmission of broadcast signals than the larger cable systems. The opposite would occur in a free marketplace where the larger companies would get discounts but the smaller companies would not. CATA, tr., at 423-424.

³⁸ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 511 (May 6, 1997) (testimony of Raymond J. Duffy, Senior Vice President, United Video Satellite Group, Inc. [hereinafter United Video, tr.]).

³⁹ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 58 (May 6, 1997) (testimony of Decker Anstrom, President, the National Cable Television Association [hereinafter NCTA, tr.]).

⁴⁰ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 146 (May 6, 1997) (testimony of Fritz Attaway, Motion Picture Association of America, Inc. [hereinafter MPAA, tr.]).

⁴¹ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 629, 631 (May 6, 1997) (testimony of Ritchie T. Thomas, Esq., representing the National Collegiate Athletic Association [hereinafter NCAA, tr.]).

⁴² Broadcast Music, Inc. is a music performing rights licensing organization which licenses the public performing right in approximately three million musical works. Broadcast Music, Inc., comment 27, at 1 [hereinafter BMI, comment 27 or reply comment 27].

⁴³ The Office of the Commissioner of Baseball represents the thirty clubs engaged in the sport of Major League Baseball. The Office of the Commissioner of Baseball, comment 17, at 1 [hereinafter Baseball, comment 17 or reply comment 20].

f. Public benefits. The Small Cable Business Association (SCBA)⁴⁴ asserts that the cable industry is merely a third party beneficiary of the compulsory license. The primary beneficiary is the public which is able to enjoy the importation of distant signals made possible by the compulsory license. SCBA, tr., at 477.

3. Reasons to Eliminate the Cable License.

On the other hand, most copyright owners took an entirely different view of the feasibility of establishing a free market alternative to the cable and satellite compulsory licenses, and offered the following reasons why the licenses should be abolished.

a. Maturation of cable industry. They assert that the cable industry has matured since 1976 and is fully able to negotiate in the free marketplace. Broadcast Music, Inc. (BMI) argues that the cable license is no longer necessary because the cable industry has grown in the last twenty years to the point where it can negotiate in the free marketplace with no lack of bargaining power. By the end of 1995, 62.1 million households subscribed to cable, and the cable industry's total revenues from all sources were \$25.1 billion. This brought the cable industry to virtual equality with the broadcast industry which had revenues of \$27.9 billion in 1995. BMI, comment 27, at 6-7. In contexts other than the compulsory license, the cable industry has successfully negotiated in the free marketplace for such things as the clearance of basic cable programming services, broadcast retransmission consent, and the music rights in local origination programming. Id. at 7-8. BMI believes that the cable industry could negotiate as well the clearance of programs on broadcast signals.

However, the Wireless Cable Association International, Inc. (WCA) states that MMDS systems, just recently recognized as cable systems for purposes of using the section 111 compulsory license, are in exactly the same position today that the cable and satellite industries were in at the time those licenses were created.

⁴⁴ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 7 (May 7, 1997) (testimony of Matthew Polka, Esq., Eric Breisach, Esq., representing Small Cable Business Association [hereinafter SCBA, tr.]).

WCA describes the wireless cable industry as "fledgling" and "nascent" and asserts that, without the compulsory license, MMDS systems would find "it difficult . . . to enter the market and provide consumers with a choice for video programming services . . . or compete with incumbent cable systems." WCA, reply comment 4, at 3.

b. Programming vitality. Distant signals are no longer the vital source of programming they once were. The Motion Picture Association of America⁴⁵ (MPAA) states that the importance of distant signals to cable systems has diminished considerably since 1976. "There are well over a hundred marketplace satellite-delivered cable and satellite services available to the public" as compared to an average of just three distant signals per cable system, notes MPAA. MPAA, tr., at 46. Therefore, the importance of the government guaranteeing to cable systems access to these signals at a government set price is no longer a matter of "the public interest." Id.

c. Government intervention. Government intervention in the marketplace alters the choices consumers and businesses would make in an otherwise free market. MPAA objects to the "government picking winners and losers." By granting the compulsory license to some delivery systems and not others, or by setting a government price for distant signals but not cable channels, "you end up creating advantages and disadvantages for these various industries in the marketplace," which results in unintended market dislocations. MPAA, tr., at 56, 119.

d. Shifting of costs. The cable license avoids certain transaction costs, but creates other transaction costs. The American Society of Composers, Authors and Publishers (ASCAP) argues that the current system unreasonably shifts much of the transaction costs and burdens onto the copyright owners.⁴⁶

⁴⁵ The Motion Picture Association of America, Inc. is an association that represents copyright owners who syndicate movies, television series and specials to broadcast stations and cable networks.

⁴⁶ The American Society of Composers, Authors and Publishers is the oldest and largest musical performing rights society in the United States with more than 79,000 members comprised of composers, lyricists and publishers of copyrighted musical compositions. The American Society of Composers, Authors and Publishers, comment 6, at 2
(continued...)

While a cable system's only transaction cost, other than the royalty payment itself, is to fill out a government form twice a year, the "copyright owners must negotiate among themselves about how to divide up the royalties. If they are unable to agree, again, copyright owners must engage in costly, time consuming and lengthy arbitrations, first among competing claimant groups to the same royalty pie and then, often, among claimants within the same claimant group." ASCAP, comment 6, at 24. ASCAP finds that these additional arbitrations reduce the amount of royalties ultimately paid to copyright owners, and greatly delay the time when the royalty payments are finally paid to the copyright owners. Id. at 24-25.

e. Inadequate compensation. Copyright owners assert they are inadequately compensated by the current cable license. MPAA offers several analyses to show that the \$170 million in annual royalties the cable industry currently pays is less than what they would pay in a free market. While the \$170 million represents payment for an average of 10 local and distant signals, the cable industry pays the following for a single channel: CNN - \$247.4 million; ESPN - \$485.2 million; TNT - \$360 million; and USA - \$220 million. MPAA, reply comment 3, at 4. MPAA also endeavors to show that Washington area cable systems pay in the range of \$.08 to \$.13 per subscriber, per signal, while the following per subscriber fees obtain for cable channels: CNN - \$0.31; ESPN - \$ 0.63; USA - \$ 0.29; Discovery - \$0.14; and TNT - \$0.46. Id. at 5.

f. Small cable systems would be able to negotiate in a free market. ASCAP expresses confidence that in a free market, there could be reasonable negotiation with the smaller cable systems. "ASCAP negotiates with the radio industry which has 11,000 radio stations, many of whom are tiny radio stations, daytimers, that have very little income, that are virtually automated. . . . We're able to negotiate with them." ASCAP, tr., at 426-427.

(...continued)

[hereinafter ASCAP, comment 6 or reply comment 11].

Major League Baseball (Baseball) also reports good success in concluding free market negotiations with the cable and satellite carrier industries for specific sports programming, including a Sunday and Wednesday night package of baseball games on ESPN that reaches 65 million cable and satellite subscribers; a Monday and Thursday night package of games over the FX and Fox Liberty cable networks; and a package called MLB Extra Innings for satellite subscribers.⁴⁷ "All of these packages are the product of arms length marketplace negotiations. All of these packages provide baseball with fair market compensation and other marketplace rights, without unnecessary administrative costs. These packages demonstrate that compulsory licensing is not necessary and that the marketplace can work if given a chance." *Id.* at 611.

4. Possible Free Market Mechanisms for Clearing Rights to a Broadcast Signal.

In any discussion of the possible elimination of the cable license, the question is what free market mechanisms exist now, or could come into existence, that would work efficiently to replace the current compulsory license. The following mechanisms have been suggested:

a. Require broadcast stations to acquire cable retransmission rights from the program suppliers, and allow the cable system to negotiate with the broadcast station for the entire signal. This mechanism was suggested by the FCC as the means to go to a free marketplace in its 1989 study of the cable license.

Broadcast stations are likely to evolve into retransmission rights packagers, with cable systems operating in a role analogous to "affiliates." Packages of retransmission rights could encompass the entire programming day of the broadcast stations, or only a part of it. This would depend on the range of programming for which the station acquired retransmission rights. . . . This process could work for nationally, regionally, or locally retransmitted stations. In some cases, national superstations might actually evolve into full copyright cable program channels.⁴⁸

⁴⁷ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 610-611 (May 8, 1997) (testimony of Thomas J. Ostertag, General Counsel, Office of the Commissioner of Baseball [hereinafter *Baseball*, tr.]).

⁴⁸ *In the Matter of Compulsory Copyright License for Cable Retransmission*, ¶¶ 12 and 189, 66 Rad. Reg. 2d 1259, 1262, 1295 (1989).

However, U.S. West observes that broadcasters have not shown any interest in this arrangement. "Broadcasters have refused to change their program acquisition practices to place themselves in position to clear their broadcast day." U.S. West, comment 4, at 5. U.S. West believes that until all broadcasters assemble the rights to clear their broadcast days for cable retransmission, there is no private market alternative to the compulsory license. *Id.* at 6.

b. Allow the major copyright owners to form collectives and bargain directly with associations representing cable systems. ASCAP notes that copyright owner collectives have already developed regarding distribution of cable royalties. Under the distribution proceedings that were conducted by the Copyright Royalty Tribunal, and now by the Copyright Arbitration Royalty Panels, claimant groups have coalesced to represent the works that are performed on broadcast signals. They are: the Program Suppliers (movies, re-runs, and specials), the Joint Sports Claimants, the Public Television Claimants (PBS, PTV stations, and producers for PBS), the Broadcast Claimants, the Devotional Claimants, the Canadian Claimants, the Noncommercial Educational Radio Claimants (NPR and NPR-affiliated stations), and the Music Claimants (ASCAP, BMI & SESAC).

Thus, in a free marketplace, cable systems and satellite carriers merely would be expanding their negotiations with the same limited group of collective representatives with whom they now negotiate under the strictures of the voluntary negotiation provisions of Section 111 and 119, in rate adjustment proceedings every five years, in retransmission consent and must-carry matters, and even in certain nonbroadcast rights contexts. ASCAP, comment 6, at 23.

However, the Association of Local Television Stations is pessimistic about the feasibility of collectives, calling them "antitrust time bombs" that would lead to "contention and litigation" over whether the collectives undermine competition, and therefore the transaction costs would be "ongoing and substantial." ALTV, comment 30, at 9. Similarly, NAB conjectures that if collectives are created similar to those now existing in the music industry, to have antitrust oversight would be required in the form of rate

courts; that would be merely a "variation on a theme" from what currently exists, and there would be a "whole lot of pain and suffering to get there for no particular benefit." NAB tr., at 104.

c. *Guaranteed access.* Guarantee program access but have copyright owners and cable operators negotiate the level of payment, similar to AGICOA⁴⁹ in Europe. MPAA supports this as a major improvement to the current compulsory license, but cautions that the difference between the United States and Europe is that in Europe, the many different languages act as a natural barrier to retransmission of distant signals, so the amount of negotiation and clearance is far less. MPAA, tr., at 106, 114.

The Small Cable Business Association (SCBA) cautions that this is the system we have now with the satellite carrier license, and it has not worked. They note that twice, in 1991 and in 1996, the statute called for the owners and the users to negotiate the level of payment, but twice no agreement was reached, and the parties had to resort to a government conducted arbitration. SCBA, tr., at 149.

Consequently, SCBA and NCTA oppose this solution because they take the view that both the access and the price must be set by government to have a meaningful compulsory license. SCBA and NCTA tr., at 115-117.

d. *Development of free market.* Certain commenters urge that the statute need not make any provision for free market mechanisms; they will spring up by themselves. This idea was expressed by MPAA, "Get rid of the compulsory license and the marketplace will work quite nicely." MPAA, tr., at 105, and by American Sky Broadcasting (ASkyB).⁵⁰ When asked whether necessity would be the mother of invention, the General Counsel for ASkyB said, "yes." ASkyB, tr., at 200.

But SBCA asserts that this would not be possible.

⁴⁹ AGICOA is the Association for the International Collective Management of Audiovisual Works (European Community).

⁵⁰ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 168 (May 6, 1997) (testimony of Ellen Agress, General Counsel, American Sky Broadcasting [hereinafter ASkyB, tr.]).

Yes, those pieces might get back to the marketplace through other ways-- sports might be back through another process, the movies might go a different route . . . but you'd no longer be offering what the consumer has been receiving. You'd be offering a hodgepodge of things . . . basically, the consumer's going to lose something that they're getting today.

SBCA, tr., at 141-142.

e. Set certain date for elimination. Some commenters concurred that there is no need to make provision for free market mechanism, advising that Congress make known the cable and satellite licenses will be eliminated on a date certain, and set that period as one to be used for the development of a free market mechanism. However, NCTA cautions about setting "arbitrary dates." NCTA, tr., at 143. NAB was concerned that there would be so much change in the affected industries during the phase out period that it would be very difficult to predict what a proper phase out period should be. NAB, tr., at 142-43.

5. Particular Problems Presented by Free Market Negotiation of Broadcast Signals.

In the absence of a compulsory license that allows use of all the works on a broadcast signal, many believe there could be problems presented by the free market negotiation of broadcast signals. These problems are identified as follows.

a. Advance negotiation. When a cable system retransmits a broadcast signal it cannot know in advance every copyrighted work that will be on it, so how can it negotiate ahead of time?

b. Clearance of all rights. Even when a cable system has negotiated with all the major collectives, how can it be assured that it has cleared all rights? What if there were an individual copyright owner who was not represented by any collective, and he or she decided to sue when his or her work was retransmitted? How can a collective system for negotiation work, if it doesn't represent everyone?

ASCAP offers a solution comparable to a provision in the regulations that govern the section 118 noncommercial educational broadcast compulsory license. There, for any unknown copyright owners who might later claim that his or her work was used without compensation, the noncommercial educational broadcasters pay a fee into an escrow fund. If the owner claims compensation within 3 years, he or she is

compensated from the fund. ASCAP said it would support such an accommodation to take care of those copyright owners not represented by a collective. ASCAP, tr., at 458-459.

c. Possibility of blackout. If the cable systems or the satellite carriers successfully negotiated with most, but not all of the collectives, they could not retransmit the broadcast signal as is. They would have to blackout the portions of the signals where they could not clear the rights, but subscribers have consistently expressed dissatisfaction with blacked out signals. How could this situation be remedied?

The National Collegiate Athletic Association (NCAA)⁵¹ responds that the cable system or satellite carrier could get substitute programming to fill the blacked out parts of the schedule. Because sections 111 and 119 would no longer apply, the cable system or satellite carrier would no longer be restricted from altering the signal. NCAA, tr., at 671.

⁵¹ The National Collegiate Athletic Association is a voluntary association of 902 colleges and universities and allied and affiliated conferences and institutions, whose members conduct numerous intercollegiate athletic events each year. The National Collegiate Athletic Association, comment 26, at 1 [hereinafter NCAA, comment 26].

C. THE SATELLITE CARRIER COMPULSORY LICENSE

1. Reasons Supporting the Existence of the Satellite Carrier License.

While most of the reasons supporting the existence of the compulsory licenses were applicable to both the cable and satellite carrier licenses, comments were filed by the satellite carriers that addressed their particular concerns and their interest in extending the satellite carrier license.

DIRECTV⁵² notes that the satellite license "gives a distributor, particularly a start-up, but any distributor, the ability to in effect do a deal in one place, have certainty with respect to what the programming costs will be and then go about developing investing in the marketing of this package."⁵³ In the absence of a compulsory license, "the satellite carrier theoretically could be forced to negotiate with literally thousands of copyright holders for rights to retransmit copyrighted programming." Id. at 3.

The comments describe that efforts at private negotiations to settle the satellite carrier rates have failed in the past and are likely to always fail. The National Rural Telecommunications Cooperative (NRTC)⁵⁴ notes that "from our experience, it's just been very difficult to bring an entrenched party to the table."⁵⁵ NRTC, tr., at 577. NRTC also notes that certain copyright owners have said there should be no negotiations until the satellite carriers and distributors "clean up their act," in terms of ending service to served households, and NRTC avers that it has done its best. Id. at 588.

⁵² DIRECTV, Inc., a subsidiary of Hughes Electronics Corporation, is a provider of DBS services. DIRECTV, comment 14, at 1 [hereinafter DIRECTV, comment 14 or reply comment 26].

⁵³ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 575 (May 8, 1997) (testimony of James B. Ramo, Executive Vice President, DIRECTV [hereinafter DIRECTV, tr.]).

⁵⁴ The National Rural Telecommunications Cooperative is a not-for-profit cooperative made up of nearly 800 rural electric and telephone utilities and affiliated organizations throughout the United States. The National Rural Telecommunications Cooperative, comment 29, at 1 [hereinafter NRTC, comment 29 or reply comment 31].

⁵⁵ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 577-578 (May 8, 1997) (testimony of B.R. Phillips, III, CEO, National Rural Telecommunications Cooperative [hereinafter NRTC, tr.]).

Primestar Partners⁵⁶ believes that "Congress' hope that the marketplace would provide realistic, feasible alternatives for obtaining rights will not be realized in the foreseeable future," and they recommend that the satellite carrier license "must be viewed as a long-term solution to the clearance of rights for satellite distant signal retransmission rather than simply a transitional mechanism." Primestar, comment 19, at 2.

United Video⁵⁷ sees the issue as black-white; either there is a satellite carrier license or there will be no retransmission of broadcast signals. "You take [section] 119 away, . . . superstations will disappear. There's clearly an initiative by certain entities that want to see superstations go away. This is one of the means to make it happen."⁵⁸ United Video, tr., at 587.

The Satellite Broadcasting and Communications Association of America (SBCA) says the satellite carrier license has worked as "a *de facto* central clearinghouse, thus obviating the need to negotiate thousands of separate license agreements." SBCA, comment 9, at 6. The SBCA believes the copyright owners have been "handsomely rewarded" for their creativity and investment. If the satellite license was unduly inexpensive, there might have been a proliferation of retransmitted broadcast signals, but this "fear . . . has proven to be unfounded" *Id.* at 7. Because the satellite carrier license works well, and private marketplace mechanisms would be onerous, the SBCA urges Congress to recognize this and make the satellite carrier license permanent. "The temporary nature of the satellite compulsory license has put the DTH (direct-to-home) industry at a competitive and political disadvantage. Unlike the other multichannel video program

⁵⁶ Primestar Partners, L.P., an affiliate of General Electric, consists of several cable television multiple system owners and provides DTH service to approximately 1.7 million subscribers located throughout the United States. Primestar Partners, L.P., comment 19, at 1 [hereinafter Primestar, comment 19].

⁵⁷ United Video Satellite Group, Inc. is a satellite carrier program service provider which transmits independent television stations and other programming, via satellite, to cable television and other local distributors, such as SMATV and MMDS operators. United Video Satellite Group, Inc., UVTV and Superstar Satellite Entertainment, comment 31, at 1 [hereinafter United Video, comment 31 or reply comment 12].

⁵⁸ Transcript, *Copyright Office Hearing on Compulsory Licenses*, 587, (May 8, 1997) (testimony of Raymond J. Duffy, United Video Satellite Group [hereinafter United Video, tr.]).

technologies, every few years the DTH industry must divert its focus and resources from building its business to lobbying Congress." Id. at 13.

PrimeTime 24⁵⁹ argues that satellite carriers

provide vital competition to the dominant alternatives — the network/affiliate [broadcast] system, and cable . . . [and] if compulsory licensing for satellite companies is abandoned, we will stand at a devastating competitive disadvantage vis-a-vis the cable companies. Such an action would run contrary to the spirit behind the Telecommunications Act of 1996 . . . wherein Congress intended to achieve lower prices for consumers through more competition for the cable industry, not less.

PrimeTime 24, comment 11, at 12.

2. Reasons for Elimination of the Satellite Carrier License.

The commentators who want the cable license abolished also believe the satellite carrier license should be abolished for the same reasons that were stated above.

However, one commentator, NAB, supports the continuation of the cable license, but opposes an extension of the satellite carrier license. NAB believes that the satellite carrier industry has not lived up to the conditions placed on the satellite carrier license by Congress, namely, to offer network signal retransmissions only to those households that are unserved by a local network station, and therefore, would not support the extension of the satellite carrier license until "the satellite carriers demonstrate their commitment to complying with the conditions of that license." NAB, comment 39, at 6.

3. Reasons for Extending the Satellite Carrier License.

The satellite carrier compulsory license, created by Congress in 1988, and extended by Congress in 1994, is scheduled to expire on December 31, 1999. Having stated in Chapter II that the transactional problems of clearing the retransmission rights to the programs on broadcast signals and the infeasibility at

⁵⁹ PrimeTime24 is the nation's largest and only independent satellite carrier of network television programming to the direct-to-home (DTH) market. PrimeTime 24, comment 11, at 1 [hereinafter PrimeTime 24, comment 11 or reply comment 15].

the present time of moving to a new system justify the continued existence of the cable and satellite carrier licenses, the question remains, should the satellite carrier license be extended, and if so, for how long?

Representatives of the satellite industry argue that the satellite carrier license should be made permanent. SBCA states that its members operate under a competitive disadvantage to cable because the cable industry has a license with no sunset provision: "Rather than spur the development of a marketplace alternative to the compulsory license, the temporary nature of the satellite compulsory license has put the DTH (direct-to-home) industry at a competitive and political disadvantage. . . . SBCA, comment 9, at 13. This uncertainty makes it difficult for DTH providers, many of whom have made substantial start-up investments in their operations, to develop any meaningful long range business plans." Id.

One of the reasons the Office supported the extension of the satellite carrier license in 1994 was because the satellite carrier industry is an important competitor to cable. Competition in the delivery of multichannel video is one of the major goals of the Telecommunications Act of 1996. That competition should be made as fair as possible, and certainly, no law should have the unintended effect of unbalancing that competition.

D. DISCUSSION AND CONCLUSION

As the above history has shown, the Copyright Office has traditionally opposed compulsory licenses because they are a derogation of the author's right to control the use and distribution of his or her work. The current cable and satellite carrier licenses are justified only because of the transactional difficulties of clearing all the rights on a broadcast signal. Other countries have preferred to have the problem of clearing the retransmission rights resolved by private negotiation between collectives representing the owner and user industries, rather than by a government administered compulsory license. Private negotiation has the virtue of recognizing the ownership rights of authors, leaving the decisions in the hands of those who are most affected by them, and avoiding the rigidity of government licenses which require legislation or administrative proceedings to alter or amend them each time market conditions change.

However, the comments show that the cable and satellite licenses have become an integral part of the means of bringing video services to the public, that business arrangements and investments have been made in reliance upon them, that some copyright owners such as NAB, PBS, and NPR favor their continuation, and that, at this time, the parties advocating such elimination have not presented a clear path toward eliminating the licenses. While the Office believes that licensing by private collectives is preferable, the elimination of the licenses does not seem feasible at this time; and in fact, the Office believes that the satellite carrier industry should have a compulsory license to retransmit broadcast signals as long as the cable industry has one. When the time comes when compulsory licensing of the works on broadcast signals has been superseded by market forces, the license should end for both industries together.

Nevertheless, the Office supports major revision for both licenses and believes the following principles should apply: they should provide the author with full compensation for the use of his or her works, they should be as simple as possible to administer, and they should treat every multichannel video delivery system the same, except where the differences in the multichannel video delivery systems justify different treatment, or where differences in the regulatory burdens placed on the multichannel video delivery systems justify different treatment.

III. SHOULD THE CABLE AND SATELLITE CARRIER LICENSES BE HARMONIZED?

If the cable and satellite licenses should continue to exist, and should last for the same length of time, should they be harmonized; that is, should they be made into a single license contained in the same section of the law, with, perhaps, differences spelled out where necessary?

This question was one of the few in the study that received a nearly unanimous response from the commenters, owner and user industry alike. The commenters believed that the cable and satellite carrier license should remain separate. Typical of the responses was NRTC's:

[C]able and satellite are different technologies, providing different services to consumers. For instance, cable systems are terrestrially based and deliver a mix of local and national programming in strictly local markets. Satellite systems deliver programming on a national basis from satellites whose footprints cover the entire continental United States. Satellite systems deliver an expanded, different mix of programming than most cable systems. Two separate copyright licenses are required.

NRTC, comment 29, at 9-10.

Similarly, CATA states:

[T]he point is, of course, that satellite carriers and cable systems represent different "voices," subject to vastly different regulatory and technical constraints. When Section 119 was adopted, it was purposefully not made identical to Section 111 out of recognition of these differences and in an attempt to create a harmonious system of compulsory licensing. Forcing those two different distribution services into a single licensing scheme will produce, begging the Office's indulgence, nothing but a sour note.

CATA, reply comment 23, at 7.

NAB reminds the Office that, "Congress adopted the cable and satellite licenses only after considerable stock-taking on their potential impact on users in varying categories of content providers. The result was a delicate balancing of interests reflected by the differing terms applicable to each communications technology and the differing regulatory and economic attributes of each." A unitary license would allow new technologies to be added into the compulsory license regime without the opportunity to consider and deal with technology-specific characteristics, and thus should be rejected. NAB, tr., at 33.

The Office concludes that merging section 111 and 119 into a single section would not lead to any practical benefit in the public administration of the licenses, and could, as NAB warns, have unintended adverse consequences. Therefore, the Office concurs with the majority of commenters that the two sections should not be merged.

However, the Office does agree with the goal of removing differences between the licenses where possible, so that the compulsory licenses should have the least possible impact on the competitive balance between satellite carriers and cable systems, while, at the same time, retaining differences that are justified by the regulatory and technological contexts of the two industries.

IV. SHOULD THE CABLE RATE STRUCTURE BE REFORMED?

As the Office stated in its Notice of March 20, 1997, the cable royalty rates that were established in 1976 were based upon an FCC cable regulatory structure that has not been in existence for a number of years. As a consequence, the calculation of a cable system's royalties must take into account an understanding of such rules as specialty stations, significantly viewed, grandfathered permitted signals, and signals that would have been permitted under the FCC's former waiver policies, many of which the FCC no longer administers.

In addition, the cable royalty system is a three-tiered system. The smallest systems, those grossing \$75,800 or less per half year pay just \$28 per half year for an unlimited number of distant signals. The medium-sized systems, those grossing more than \$75,800 but less than \$292,000 per half year, pay on a sliding scale from \$28 to \$2190 for an unlimited number of distant signals. However, the larger systems, those grossing \$292,000 or above, pay a percentage of their gross receipts for each distant signal they import; consequently, they pay the bulk of the royalties.⁶⁰

These two factors--the crazy-quilt application of old FCC rules, and the progressively higher rates for the larger systems--have resulted in many anomalies in royalty obligations. Cable systems that are seemingly similarly situated nonetheless pay widely different sums to the Copyright Office because of how much the cable system grossed, or how many signals they would have been permitted to carry under the FCC rules that existed in the 1970s.⁶¹

In its Notice, the Office asked whether the cable royalty rate should be amended to remove reliance on old FCC rules, and whether a flat, per subscriber, per signal charge, such as the one that currently applies in the satellite carrier license, would be preferable to the current three-tiered, progressive rates.

⁶⁰ In 1996, there were 6,465 "small" Form 1 systems, 2,853 "medium" Form 2 systems, and 2,353 "large" Form 3 systems paying cable royalty fees to the Copyright Office.

⁶¹ These anomalies were demonstrated in the comments of St. Croix Cable TV which paid \$61,639 in copyright royalties for the second semiannual accounting period of 1996, but the same system located in Miami or Puerto Rico would have paid only \$16,300. St. Croix, comment 1, at 1.

A. REFORM PRINCIPLES

1. The Comments.

In response to any consideration of royalty rate reform, the following are what some of the commenters listed for the Office as their priorities:

NCTA supports rate reform that ultimately is "revenue-neutral," -- that is, a reform that collects the same amount of royalties overall from the cable systems, not an increase--but warns that "even a revenue-neutral revision of the royalty rates could cause substantial increases in the fees currently paid by small cable systems" and that "Congress recognized the special circumstances faced by small cable systems when it adopted a flat rate approach for them that is not tied to the number of distant signals carried." Ultimately, NCTA believes it is up to the proponents of simplification "to demonstrate that any modification is warranted" and would not upset "the delicate balance of interests reflected in the current law." NCTA, comment 34, at 11-13. NCTA is opposed to any payment for local signals, because "what the cable system is doing is simply ensuring the reception of a signal for which they've [the copyright owners] already received compensation. . . ." NCTA, tr., at 135.

Similarly, CATA states that "the goals of any change in section 111 have to be revenue neutrality and simplicity," but CATA opposes a flat fee because, "the flat fee obliterates the carefully crafted three-tier payment scheme of section 111. This scheme was enacted in recognition of the differing burdens and obligations of smaller cable systems. Smaller systems are predominantly located in sparsely populated areas. They were made to pay lower fees so as to encourage their growth and development in rendering service to an underserved element of our population." CATA, comment 21, at 5.

The SCBA opposes any rate reform, even if it is "revenue-neutral" overall, if it results in higher royalties for the small cable systems. SCBA says it was Congress' intention to allow small cable systems to import distant signals for the benefit of their subscribers. SCBA, tr., at 476-477.

U.S. West opposes any move to a flat per subscriber fee because it sees that as leading inevitably to an increase in fees. "Under no circumstances should the section 111 cable royalty be modified to introduce the artificially high royalties of section 119, or the vague arbitration standards which spawned them." U.S. West, comment 4, at 14.

Similarly, DIRECTV takes issue with the satellite carrier rates which it describes as much higher than the section 111 fees, and subject to adjustments based on a two-step process of negotiation and arbitration which it considers costly and time-consuming. It asks that the satellite carrier fees be comparable to the cable fees, be put into the statute, and be subject to adjustment by a "straightforward, statutorily-imposed formula." DIRECTV, comment 14, at 9. SBCA and NRTC take a similar position, and state that the primary value in rate reform is to have parity between the satellite carrier rates and the cable rates. SBCA, comment 9, at 9-12; NRTC, comment 29, at 7-9.

Baseball wants cable rates determined by marketplace value. Such a determination, it predicts, would increase the cable systems' payments. Baseball also supports putting the payments on a per subscriber/per signal basis to avoid the current complex system which it says, "imposes unnecessary costs and burdens in determining how much cable operators must pay for particular signals . . . [and] is . . . subject to manipulation . . . through accounting methods . . . such as 'tiering.'" Baseball, comment 17, at 19-20. Baseball also wants copyright payments for the cable retransmission of network programs, the cable retransmission of local signals, and the retransmission of signals to the cable systems by satellite carriers that are currently exempted under the passive carrier exemption. Baseball, tr., at 612.

BMI also supports a per subscriber, per signal rate based on marketplace value, and also cites the practice of "tiering" as a means some systems have used to reduce their payments. BMI, comment 27, at 8-9, 12.

The Canadian Claimants support a per subscriber/per signal rate structure for cable not only for its simplicity of payment, but because they believe it will simplify the distribution proceedings, as well. "This

... would be a tremendous aid to the rational distribution of the royalties collected, since only claimant groups with programming on a signal type would then be 'eligible' to seek a share of that royalty fund." CC, comment 32, at 13. They also believe the rates should be the same for cable and satellite, and based on the fair market value. Id. at 18. The Canadian Claimants oppose the three-tiered cable rate structure, because they believe it has led to the same "tiering" practices as a method of rate avoidance mentioned by BMI and Baseball in their comments. Id. at 21-22.

MPAA supports a flat, per subscriber, per signal fee for cable based on marketplace value, but also wants to retain a mechanism, like the current 3.75% rate that inhibits the importation of many distant signals. MPAA would also vary from the flat, per subscriber, per signal fee concept to allow some consideration for small systems. MPAA, comment 35, at 5-7, 12-14; MPAA, tr., at 130, 146. For local signals, MPAA takes the position that when must-carry is invoked by the local broadcaster, the local broadcaster should pay the copyright fee. MPAA, tr., at 133.

For NAB, any change in the cable rate structure should be done in "such a way that it does not produce radical changes in carriage. . . To the extent the equalization of cable and satellite rates included any change in the 3.75% rate that would result in the significant expansion of distant signals being retransmitted into other television markets, such a change would threaten the ability of local stations to serve their local communities to the detriment of important federal policies." NAB, comment 39, at 9. Generally, NAB believes that "modification in pursuit of simplification would likely produce a complicated mess, as myriad carriage situations were reassessed and restructured." Id. at 12. But "if [Congress] were to go to a flat rate system, we would very much support a graduated system of increases [in rates] that would create disincentives to carry an indiscriminate number of additional distant signals." NAB, tr., at 150.

For ALTV, the cable rates should continue as they are, and especially in the way they act to limit the importation of distant signals through the application of the 3.75% rate. In the absence of any limiting factor in the rates, then the number of imported distant signals should be limited by law, and any signals

imported above the limit should be negotiated for in the free marketplace. ALTV, comment 30, at 13-14, ALTV, tr., at 184. ALTV also believes cable retransmission of local signals should be free of copyright obligation. ALTV, tr., at 179.

2. Summary of Reform Principles.

It is clear from a review of the comments that many principles, some of which are conflicting, are being invoked. They may be summarized as follows:

(a) Administration.

- (i) Some commenters believe that while the current rates are administratively complex, things have settled out, the cable systems know what they owe, and no reform is necessary.
- (ii) Other commenters believe that simplification of administration is a reasonable goal but only if the cable systems, as a whole, pay the same amount after reform as they did before reform ("revenue neutral") and the smaller cable systems still pay the same amount as they are paying today.
- (iii) Other commenters believe that simplification of administration is very important, but two features of the current system should be retained: a lower payment by the smaller systems, and a higher, step-up rate for the importation of distant signals that exceeds a certain quota.
- (iv) Other commenters believe in complete simplification of administration, similar to that in place for the satellite carriers, where the price of a signal is the same for all systems regardless of how large the system is, or whether it is the first imported signal or some number above a certain quota.

(b) Equity

- (i) Equity means cable systems pay the same, over all, after reform as they did before reform.
- (ii) Equity means cable systems pay the same rates as satellite carriers pay.
- (iii) Equity means all cable systems pay the same rate, regardless of their gross receipts.
- (iv) Equity means that higher grossing cable systems pay higher rates.
- (v) Equity means cable systems pay the fair market value for the signals.
- (vi) Equity means cable systems pay less than fair market value for the signals.

3. Copyright Office Recommendation.

As already shown, the cable and satellite carrier licenses were justified on the basis of the problems of clearing the retransmission rights to the programs on broadcast signals, not on the basis that the cable and satellite carrier industry required a subsidy. While the Office concurs that problems remain, there is no justification for the amounts paid to authors to be less than the fair market value of their works.

Furthermore, beyond the undercompensation to authors, the administrative complexity of the current cable rates is burdensome, and in many respects, unfair. Many hours are spent by cable systems just to understand how much they owe and how to fill out the forms (which often requires legal advice). In addition, there are the hours spent by the Office in rendering interpretations, and the hours spent by copyright owners in inspecting and challenging filings. These extra efforts might be justified, if there were sound public policy reasons to make the distinctions among cable systems that the current system makes. But, as St. Croix Cable points out, the sum of all these distinctions results in an irrational and unjustified disparity in payments.

The Office is also concerned about how OVS systems or cable systems using OVS platforms would calculate their rates under FCC rules that never applied to them. The Office sees simplification as an important component of making OVS systems eligible for section 111.

Therefore, the Office believes that the cable rates should be as simple as possible and set at fair market rates.

B. THE SMALL SYSTEM SUBSIDY

Complete simplification of the cable rates would mean requiring that each system pay the same rate regardless of its size. There would be no small system subsidy. This is the major impediment to complete simplification, and therefore, an in-depth discussion of the justification of the small system subsidy is warranted.

Currently, the smaller systems pay less than the larger systems in two respects. First, they pay at a lower rate. Second, once they make their payment, they have a right to import an unlimited number of distant signals, whereas the larger systems must pay for every additional distant signal they import.

Congress explained in 1976 why it was affording the smaller cable systems lower rates and unlimited importation of distant signals:

Because many smaller cable systems carry a large number of distant signals, especially those located in areas where over-the-air television service is sparse, and because smaller cable systems may be less able to shoulder the burden of copyright payments than larger systems, the Committee decided to give [smaller cable systems] special consideration.

H.R. Rep. No. 1476, at 96-97.

1. The Comments.

NCTA argues that special consideration for small systems is still required, because there are more small cable systems than ever:

Of the 11,000 cable systems in the United States today, more than 6,200 systems serve less than 1,000 customers each; roughly 2,000 systems serve between 1,000 and 3,500 customers. By comparison, there were fewer than 1,700 systems in 1976

serving fewer than 1,000 customers, and fewer than 1,200 systems that served between 1,000 and 3,500 customers. Therefore, there are more small systems today in rural and smaller markets than when the license was adopted in 1976.

NCTA, reply comments 16, at 5.

NCTA notes that these systems, located as they are in small and rural communities, remain dependent on bringing in distant television stations. While conceding that the number of television stations in the United States has increased since 1976, nonetheless, NCTA finds that "over 26 percent of cable customers live in areas that do not receive a full complement of signals -- three network, one independent, and one educational station -- over the air." NCTA, reply comments 16, at 5-6.

However, MPAA disputes both the need for small systems to get a rate subsidy, and the need for small systems to be able to import an unlimited number of distant signals. MPAA does this by questioning the connection between "small" and "rural":

First, the notions that rural America is served primarily by small systems or that small systems serve primarily rural America are not supported by the facts. [Filing] data . . . show that more than 50% of Form 1 subscribers [the smallest cable systems] are located in Top 100 markets, not in rural America. . . . Thus, most small systems operate in large, not small, markets. Equally compelling, most small markets are served by large systems: Form 3 systems [the largest cable systems] serve over 12 million subscribers in smaller markets or outside of all markets as compared to only about 1.1 million subscribers served by Form 1 systems in these same markets. In short, the assumption that rural America is predominantly served by small systems is unsupported. MPAA, reply comment 3, at 6-7.

MPAA also doubts the special need of rural systems to import distant signals. MPAA notes that in 1976, there were 701 commercial stations, but by 1996, there were 1,174 commercial stations, and that this increase in the number of stations has been mostly felt in the rural areas. "[Filing] data . . . show an average of 5.5 local stations are carried by systems in smaller markets and outside all markets. This suggests that viewers in small markets already have a range of local network and independent stations available without the need to import distant stations to fill out a complement of stations." Id. at 7.

2. Copyright Office Discussion and Recommendations.

The last twenty years have also seen the rise of the MSO, the multiple systems operator. While the filer of the compulsory license fee might ostensibly be a "small" cable system, that same cable system may be a part of an MSO, and as fully capable of paying the same royalty rate as the other systems in the same MSO.⁶² CATA argues that being part of an MSO does not help a small operator because, due to FCC rate regulation, an MSO may not raise basic rates in another, wealthier system to cross-subsidize the basic rate of the smaller system. However, there are numerous other ways being part of an MSO helps the small operator. For instance, the MSO can negotiate better rates for the cable networks the small system is carrying.

It is ultimately a policy question for Congress whether small systems today continue to need a subsidy.⁶³ Industry conditions may very well have changed since 1976. Today, the small system may just as well be an urban system that is part of a large MSO with plenty of available local channels than a stand alone rural system needing to import distant signals. The Copyright Office recognizes, however, that if the royalty rate for small systems were raised to true fair market value, the economic impact on the small systems might be too great. Therefore, the Office recommends that small systems continue to be able to pay less than the large systems.

Having said that, the Office also believes that the current rate that the smallest systems pay is far too low. Systems grossing \$75,800 or less per half year pay only \$28 per half year for the copyright compulsory

⁶² For example, in the second semiannual accounting period of 1995, TCI, the nation's largest MSO, filed copyright fees on behalf of its 1,144 cable systems. 252 of them filed as "small" Form 1 systems, paying just \$28 per half year. Three hundred and seventy-eight of them were "medium" Form 2 systems paying on a sliding scale from \$28 to \$2190 per half year. Only 514, or just 45%, of them were "large" Form 3 systems paying on the basis of each distant signal they imported.

⁶³ In reviewing the small system subsidy, BMI reminds the Office that this is not a matter of small versus big, but, in many cases, small versus small. "It's the songwriter's property that is being used by these entities, the consummate, the ultimate small businessman. Not gargantuan BMI. That's who we represent, the small businessman. Much smaller than a cable operator that has 100 subscribers or 1,000 subscribers or 2,000 subscribers. We should be looking at this end saying how do we protect the small, independent businessman, the small songwriter." BMI, tr., at 464.

licenses, and this can only be described as a nominal payment.⁶⁴ Efforts should be made to raise that minimal payment to an amount that can be considered fair.

C. THE ARTIFICIAL FRAGMENTATION PROBLEM

So long as there is a subsidy in the rates for the smaller cable systems, there will be an incentive for cable systems to structure themselves to qualify as a small system.

This temptation toward artificial fragmentation is avoided under the current system by a provision in Section 111(f) which states, “For the purposes of determining the royalty fee under subsection (d)(1), two or more cable systems in contiguous communities under common ownership or control or operating from one headend shall be considered as one system.” As a result, neighboring cable systems that are commonly owned or controlled, or systems that operate from the same headend, may not claim to be separate cable systems.

However, although this provision has worked well to avoid artificial fragmentation, it has had the result of raising the royalty rates some cable systems pay when they merge. This happens because, if the two systems have different distant signal offerings, then all the signals are being paid for based on the total number of subscribers of the two systems, even if some of those signals are not reaching all the subscribers. This has come to be called the “phantom” signal problem.

To solve the “phantom” signal problem, NCTA has recommended that the cable rates be based only on those subscriber groups that actually receive the signal. NCTA, comment 34, at 8-11. While the Office has previously stated that this solution could not be accomplished administratively because the Office lacked the authority to alter the structure of the cable rates as they are established in Section 111, the purpose of this

⁶⁴ The Office estimates that it costs more to process the \$28 payment than \$28. Since the Office is entitled to subtract its costs before distributing the royalties to the copyright owners, it is safe to conclude that none of the \$28 reaches the copyright owner.

study is to recommend to Congress legislative changes, and the Office endorses this as an appropriate legislative change.

The Office would also recommend another change. At present, cable systems operating from one headend are considered as one system regardless of whether they are in contiguous communities or are under common ownership or control. Changes in the cable industry, and the introduction of OVS, tend to make this emphasis on the headend obsolete. Technological advances in headends make it feasible, as it never has been before, to operate many systems from a single headend. Consequently, operation from the same headend is no longer the hallmark of integrated systems, much less an indicator that an artificial fragmentation is occurring to avoid royalty payments. Furthermore, if one analogizes headends to OVS platforms, the rule quickly becomes that all systems operating from the same OVS platform are considered as one system; such a rule may have an onerous effect on the users of the OVS platform without getting at true artificial fragmentation. The Office recommends that the better rule is that the systems under common ownership or control should be considered as one system only when they are in contiguous communities or use the same headend or OVS platform.

Therefore, the Office recommends that Section 111 be amended to read,

For purposes of determining the royalty fee under subsection (d)(1), two or more cable systems under common ownership or control that are either (a) in contiguous communities, (b) operating from the same headend, or (c) using the same open video system platform, shall be considered as one system. Once two or more cable systems have been deemed a single larger cable system, the calculation of the rates shall be based on those subscriber groups who receive the secondary transmission as the Register of Copyrights shall by regulation provide.⁶⁵

Finally, the Independent Cable and Telecommunications Association (ICTA), the trade association that represents satellite master antenna television (SMATV) systems asks for a change in the interpretation of "contiguous communities" as it applies to SMATV systems. ICTA states:

⁶⁵ The provision for "subscriber groups" would not be necessary if Congress adopts a flat, per subscriber, per signal, fee.

Contiguous communities are presently identified with reference to political boundaries and can include incorporated as well as discrete unincorporated areas. The threshold of contiguity has been developed solely with regard to franchised cable operators. . . . While such an analysis may be logical as applied to franchised cable operators, ICTA strongly believes that it is entirely unworkable in the SMATV context. . . . [SMATV] operators . . . enter into individual contracts to serve discreet, independent buildings or groups of buildings — generally, multiple dwelling units (MDU's). As a result, a [SMATV] operator may have one system serving an MDU in the northern portion of a municipality and another system (with its own separate head-end) serving an MDU in the southern part of an adjacent unincorporated community ICTA strongly believes that to treat these systems as serving one large unitary area is contrary to the intended effect of the contiguous community provision

ICTA, reply comment 7, at 2-3.

ICTA, therefore, seeks a provision that states that SMATV systems are to be treated as serving contiguous communities “only when the MDU's which they serve are adjacent or the systems are served by the same headend.” Id. at 6.

While the Office understands that the nature of SMATV operations is different from that of traditionally franchised cable systems, the Office cannot recommend a different treatment for SMATV systems. That would act against the Office's goal of having the same rule for all video delivery systems wherever possible. However, if the Office's recommendation to allow all § 111 systems to calculate their rates according to subscriber groups is accepted by Congress, the joining together of SMATV systems that are in contiguous communities (even though miles apart as in the above quoted example) will have no greater affect than defining them as a larger cable system rather than a smaller cable system, and, at most, the affected SMATV systems will pay fair market value rates for their license instead of a subsidy rate.

F. THE PROPOSED STEP-UP RATE

Another proposed departure from a simple rate is a step-up rate recommended for imported signals that exceed a certain quota. The current step-up rate, the 3.75% rate, was instituted by the Copyright Royalty Tribunal starting in 1983, and many copyright owners feel it has served the purpose of keeping a flood of distant signals from being imported by the cable systems. The Office believes that may have been true for

the 1980's when distant signals were an important part of the cable system's offerings, but now in the late 1990's, when so many cable networks are seeking space on the cable systems, there is far less incentive for the cable systems to fill up their channel capacity with distant signals. The Office believes that so long as the marginal costs of each additional signal does not go down, that provides sufficient disincentive for the cable system to import an excessive number of distant signals. There is no need for a step-up rate.

Last, the rates for the satellite carrier compulsory license were put on a fair market basis beginning in 1994. In keeping with the Office's above-stated principle that differences between the licenses should be eliminated where possible, especially to avoid tilting the competitive balance in one direction or another, the Office concludes that cable rates should be set at fair market value, just like the current satellite carrier rates currently are.

V. HOW SHOULD THE CABLE RATE STRUCTURE BE REFORMED?

Having concluded in the previous chapter that the cable rates should be made simple to administer and set at fair market value, but with a subsidy rate for the smaller cable systems, the question becomes one of how this new cable rate structure should look.

Three models have been considered by the Copyright Office: (1) a flat, per subscriber, per signal fee similar to that paid by the satellite carriers; (2) a reform of the current gross receipts structure; and (3) a tariffing model proposed by Baseball.

However, before discussing any of these three models, one preliminary issue must be addressed. That is the issue of the method of deciding whether a signal is local or distant, because that determination will have to be made under any of these models, or even if the current system is retained.

A. LOCAL VERSUS DISTANT SIGNALS

Currently, cable systems grossing \$292,000 or more per half year pay on the basis of the number of distant signals they import. No definition of a distant signal is found in section 111. However, local signals are defined. Until the passage of the Satellite Home Viewer Act of 1994, the local service area of the primary transmitter was defined solely as, “the area in which such station is entitled to insist upon its signal being retransmitted by a cable system pursuant to the rules, regulations, and authorizations of the Federal Communications Commission in effect on April 15, 1976. . .” 17 U.S.C. § 111(f). Therefore, a signal is a local signal if the broadcast station had a right under the FCC must-carry rules in effect in 1976 to insist that the cable system carry it. If it did not, the signal is, by definition, a distant signal. Although the must-carry rules in effect in 1976 were declared unconstitutional in 1985,⁶⁶ and new must-carry rules were passed by Congress in 1992, one does not refer to the current must-carry rules to determine if a signal is local or distant but to those must-carry rules in effect in 1976.

⁶⁶ Quincy Cable TV, Inc. v. FCC, 768 F.2d 1434 (D.C. Cir. 1985), cert denied, 476 U.S. 1169 (1986).

One of the features of those old must-carry rules was a concept called “significantly viewed,” which gave a broadcast station a right to be carried by the cable system, even if it were outside of the cable system's area if the broadcast station could show, by certain FCC criteria, that the signal was, nonetheless, “significantly viewed” in the cable system's area. The FCC no longer administers “significantly viewed,” for its determination of its current must-carry rules. Yet, cable systems today must still take this concept into account when filing their royalty fees.

With the passage of the Satellite Home Viewer Act of 1994, the section 111(f) definition of the local service area of the primary transmitter was changed. Cable systems are now given a choice. They can find that a broadcast signal is local if it was entitled to must-carry under the FCC's 1976 rules, or if the cable system is located in the broadcast station's “television market as defined in section 76.55(e) of title 47, Code of Federal Regulations (as in effect on September 18, 1993), or any modifications to such television market made, on or after September 18, 1993, pursuant to section 76.55(e) or 76.59 of title 47 of the Code of Federal Regulations.” 17 U.S.C. § 111(f).

Section 76.55(e) of the FCC's rules shows the new system of defining a television market as one called the Area of Dominant Influence, or ADI. If a cable system in the television station's ADI or could have been required under the 1976 must-carry rules to carry the television station, then the cable system is local to the television station, and the station's signal does not count as an imported distant signal.

The advantage of referencing the television station's ADI to make a local versus distant signal determination is that these are the rules that are currently administered by the FCC, and a quick reference to them could tell any newly started cable system, or any OVS system, whether it is located within the station's ADI. Furthermore, such a method is designed to be flexible because it allows for modification of the ADI at any time by the FCC.

The Office is, therefore, convinced that it is time to eliminate all references to the 1976 must-carry rules, and move to the new ADI system of determining a television station's local market. To achieve parity

with the satellite carrier license, the Office also recommends that the local market of a network station be considered the ADI of the network station, as is further discussed in Chapter IX.

One problem remains, however, with this recommendation. The ADI is for commercial stations. It does not apply to noncommercial educational stations. Dropping reliance on the 1976 must-carry rules would cause a problem for categorizing PBS stations. Rather than attempt artificially to apply ADI to noncommercial educational stations, the Office recommends defining the local market of a noncommercial educational station as an area encompassing 50 miles from the community of license of the station, including any communities served in whole or in part by the 50 mile radius. The Office also recommends this 50 mile radius rule for determining whether a noncommercial educational station is local or distant for satellite carriers. *See* Chapter IX.

B. MODELS FOR RATE REFORM

The Office now proceeds to a discussion of the three possible reform models.

1. The Flat, Per Subscriber, Per Signal Fee.

Currently, satellite carriers pay under section 119 the following rates:

Seventeen and one-half cents per subscriber, per month, for each independent station not subject to syndicated exclusivity blackout demands;

Fourteen cents per subscriber, per month, for each independent station subject to syndicated exclusivity blackout demands; and

Six cents per subscriber, per month, for each network or noncommercial education television station.

These rates were established in 1992 by an arbitration panel applying seven statutory criteria, one of which was "a fair return" to the copyright owner. Congress changed those criteria in 1994. Currently, a Copyright Arbitration Royalty Panel (CARP) is considering adjusting these rates again, endeavoring to establish fees under the new criteria which, among other things, are to be fees that "most clearly represent the fair market value" of the programs on the retransmitted signals.

The virtue of the flat, per subscriber, per signal, rate structure is simplicity. There are no interpretations that need to be made; no ambiguities that need to be resolved; no ongoing rulemakings that need closure; no court cases pending. The Copyright Office's resources that are devoted to the processing of satellite carrier license fees are a fraction of those devoted to the processing of cable license fees. Both the users and the owners save expenses under this system.

The flat, per subscriber, per signal, rate structure also has the virtue of treating all satellite carriers alike. No carrier pays more or less than any other carrier because of any accident of location, or previous treatment by the FCC.

The flat, per subscriber, per signal, rate structure can be set according to whatever criteria Congress deems best, and currently, for satellite carriers, that is the fair market value of the signals.

2. The Gross Receipts Rate Structure.

As described above, the current cable rates are determined with reference to the gross receipts of the cable system. However, it is not gross receipts that makes the current structure so complex. Therefore, it is possible to simplify the cable rate structure and retain the gross receipts concept. Assuming for the purposes of example that the current rate for the first distant signal is retained, the simplest gross receipts rate structure would look like this: "0.893 of 1 per centum of gross receipts for each distant signal equivalent, but in no case less than 0.893 of 1 per centum of such gross receipts."

With such a rate structure, the cable system would pay 0.893% of its gross receipts if it carried no distant signals. If it carried distant signals, the cable system would pay 0.893% of its gross receipts for each distant signal equivalent. Since network and noncommercial educational stations count as just one-quarter of a distant signal equivalent, the rate for retransmitting them would be one-quarter of 0.893%, or 0.22325%.⁶⁷

⁶⁷ However, *see* Chapter XI for discussion of the value of network signals.

If a subsidy for the smaller cable systems is considered desirable, again, using the current rates, a gross receipts based rate structure could look like this:

(A) if the actual gross receipts paid by subscribers to a cable system for the period covered by the statement for the basic service of providing secondary transmission is less than \$292,000, 0.893 of 1 per centum of such gross receipts, regardless of the number of distant signal equivalents, if any; or

(B) if the actual gross receipts paid by subscribers to a cable system for the period covered by the statement for the basic service of providing secondary transmission is \$292,000 or more, 0.893 of 1 per centum of such gross receipts for each distant signal equivalent, but in no case less than 0.893 of 1 per centum of such gross receipts.

With this type of structure, the smaller cable systems would be paying the same rate as the larger cable systems, but they would only pay for 1 DSE regardless of how many signals they imported, whereas the larger cable systems would pay for each DSE.

This system has the virtue of retaining both the gross receipts structure the cable systems are familiar with and the current policy allowing the smaller systems to import as many distant signals as they want without an increase in their fees. It would also bring to an end the nominal payments made by the smallest cable systems, but still keep their payments at a reasonable level. Most importantly, it would end the need to consider any former FCC rule when calculating the rate.

The Copyright Office performed a study to see whether this flat, gross receipts model, using 0.893% as the rate, and the current \$292,000 as the dividing line between the smaller and larger systems would be revenue-neutral with what cable systems are currently paying. Looking at the signal importation choices made by cable systems in the second semiannual accounting period for 1995, and assuming only for the purposes of the study that those same choices would be made after the reform of the cable rates, the Office found that a 0.893% would garner somewhat higher royalties than in 1995, and that revenue-neutrality would probably be reached with a rate of 0.875% instead of 0.893%.

The reason why the flat, gross receipts structure is in approximate balance with the current complex, gross receipts structure is due to counterbalancing changes in the rates. While the rates for the smaller systems, and the larger systems who pay a declining rate after the first DSE, increased, the rates for the systems paying the 3.75% rates decreased.

However, the Office performed a static analysis, assuming that no cable system would change its distant importation choices after cable rate reform. Yet, it is inevitable that as the rate structure changes, the distant signal choices the cable systems make will change. Therefore, while a gross receipts model makes the possibility of achieving revenue-neutrality appear to be feasible, in reality, it is not. Further, the Office believes that the rates, whether based on gross receipts or a flat, per subscriber, per signal fee, should reflect the fair market value of the signals. The Office assumes that this would require raising the rates from their current levels.

3. Tariffing.

As proposed by Baseball, the tariffing system would work as follows: each year the claimant groups that already represent copyright owners under Section 111 and 119⁶⁸ would file tariffs with the Copyright Office. Each tariff would set forth the terms and rates with which the cable systems and satellite carriers would comply to obtain the compulsory licenses. The claimant group could specify a flat fee, a per subscriber/per signal rate, or any other rate calculation. The tariff could also set forth different royalty rates based on factors such as the size of the retransmitter, type of retransmission service, and number of signals carried. A claimant group would also be permitted to specify in each tariff the terms and conditions that the cable operator or satellite carrier must meet to qualify for the compulsory license. Examples of such terms and conditions include blackout provisions that protect exclusivity arrangements with local broadcasters and

⁶⁸ Baseball proposes that a tariff system replace the rate structure and distribution procedures for both the cable and satellite carrier licenses.

a right to a financial audit to ensure proper royalty payments. The system or carrier would pay the royalty set forth in the tariff directly to the entity filing the tariff. Baseball, reply comment 20, at 3-6.

After the tariffs are filed, cable systems and satellite carriers would have a limited period in which they could petition for review of the tariff to determine whether it meets statutory objectives. The review would be conducted by a CARP to determine whether the terms and rates at issue meet the objectives set forth in the Copyright Act. To promote efficiency, all tariff challenges could be consolidated into a single proceeding. In addition, voluntary agreements between each group of copyright owners and the compulsory licensees could be negotiated and would govern retransmission of the applicable programming in lieu of the tariff process. Id. at 4-7.

Baseball states that this tariffing system is similar to the Canadian system but is different in a few significant respects. First, the rate approved by the Canadian Copyright Board for any particular collective permits access to all programming on distant signals in that collective's category, not simply the programming owned by the collective's members. Baseball, on the other hand, is proposing that its tariff only apply to programming owned by the members of the claimant group. The second difference is that the Canadian Copyright Board makes an assessment of the overall share of the royalties that each collective is entitled to (similar to the Phase I allocations made in the United States by a CARP). Baseball is proposing not to adopt this assessment. Third, the Canadian Copyright Board approves only royalty rates and administrative terms and conditions, whereas Baseball's proposed tariff system would permit copyright owners to file substantive terms and conditions for the compulsory license. Id. at 8-10.

Baseball predicts that, similar to the Canadian experience, the need for annual review of the tariffs will wane as the types of rates and terms proposed by the owners and approved by the government settles into a pattern, and Baseball believes that this pattern could eventually lead to private negotiations between the owner and user industries, and provide a segue to installing a free market mechanism. Id. at 10-11.

b. Opposition to a tariffing system. The Canadian Claimants, in their comments, do not believe that the Canadian system is inherently superior to the U.S. system, and therefore, they do not support implementing a tariff system. In particular, they do not like the direct payment between user and owner in a tariff system. The Canadian Claimants remind the Office that there are 13,000 cable systems in the United States and that each system remitting checks to the claimant groups would work a special hardship on the smaller claimant groups to handle. They prefer retaining the Copyright Office or a private party to act as the clearinghouse. CC, reply comment 25, at 8. Further, they would not support a system, such as the one that exists in Canada, where the government sets the overall rate paid by the cable systems and makes the overall allocation among claimant groups, especially if such allocation is done with reference to program ratings. *Id.* at 6-8. They prefer, instead, a flat, per subscriber, per signal rate.

C. DISCUSSION

The Copyright Office does not recommend the tariffing system proposed by Baseball as a useful model for cable rate reform. The tariffing procedure requires yearly proceedings before a government agency, is speculative in that it asks the agency to approve the rates for the prospective use of works, the identity and quantity of which is uncertain, and is likely to be appealed and tied up in court review and possible remands. Baseball seeks such a system because it would give Baseball the ability to set terms that may not exist in the statute, but Baseball has not established the need for additional terms, or stated how it is disadvantaged by the lack of those terms. Foremost, the Office does not see this as a move toward administrative simplicity, but replacing one complex system with another.

Either the gross receipts model or the flat, per subscriber, per signal model would work and would achieve simplicity, certainty, equity, and efficiency. However, the Office recommends the flat, per subscriber, per signal rate as the better model for the following reasons:

1. Avoidance of Tiering.

As mentioned above, copyright owners have all cited the practice of tiering as a method of rate avoidance they would like to see end. This is how tiering works. The Copyright Office has stated that the gross receipts from each tier offering broadcast signals must be added together when cable systems calculate their rate payment. However, if a tier offers no broadcast signals, the revenues from that tier do not become part of the calculation of gross receipts.

As a result, suppose Cable System A is currently offering 35 channels at \$27 a month as part of its basic tier, some of which are broadcast signals. All the gross receipts from the basic tier are counted as part of the calculation of the royalties. Now suppose that Cable System A wants to lower that gross receipts amount. What it does is offer, for example, 18 channels, as Basic Limited for \$18, with all the broadcast signals on Basic Limited. Then it offers Basic Plus which has the rest of the 35 channels that were originally offered for another \$9. While the great majority of subscribers will continue to pay the \$27 as before and receive the same channels as before, they are now subscribing to two tiers instead of one, with all the broadcast signals on the lower tier. This allows the cable system to report only the \$18 per month in gross receipts when it calculates the rates.

So long as the cable rates are based on gross receipts, tiering remains an attractive and legal way to reduce copyright liability. However, the Office does not believe the compensation to the copyright owners should change based solely on how the cable system markets its channel lineup to the subscriber. A change to a flat, per subscriber, per signal rate would end the option of tiering as a means to reduce copyright payments.

2. Subscriber Groups.

As discussed in Chapter IV, section 111(f) requires that cable systems in contiguous communities under common ownership or control or operating from the same headend be considered as one cable system. This is to avoid the temptation of cable systems to artificially fragment to take advantage of the lower rates for small cable systems. The Office recommended a change in section 111(f), where section 111(f) works to combine systems that provide different distant signal complements to different subscriber groups. The proposed amendment would allow those systems to calculate their royalties based on the subscriber groups that actually receive the signals rather than on all the subscribers in the combined systems.

Reporting subscriber groups to the Copyright Office is an additional, but necessary, step in the calculation of rates so long as the rates are based on gross receipts. However, if the rates were based on a flat, per subscriber, per signal rate, the concept of subscriber groups would already be incorporated into the per subscriber rate. There would be no need to make a special provision for their creation in section 111(f), or on the form the cable systems file.

3. Direct Comparison to Satellite Carriers.

The satellite carrier rate is a flat, per subscriber, per signal rate. If the goal is to have comparable rates between the cable and satellite carrier industry, a flat, per subscriber, per signal rate for cable systems would make that comparison possible. On the other hand, a comparison of the gross receipts rates that cable pays with the flat, per subscriber, per signal rates that satellite carriers pay is very problematic, and can only yield general conclusions.

4. Changing Signal Lineups.

The current rule is that if a cable system imports a distant signal for even one day in any given semiannual accounting period, then it must pay for that signal as if it were carried for the entire six month period. As a result, cable systems are careful to add distant signals only on January 1 or July 1 of a year.

To do so at any other time of the year would mean that the cable system would be paying for a period of time when it did not receive the distant signal.

On the other hand, satellite carriers can change their signals every month because they pay on the basis of per subscriber, per signal, per month. If the cable systems paid rates that were per subscriber, per signal, per month, they, too, could make changes by the month rather than by the half year. To afford cable systems that amount of flexibility in a gross receipts model would be more difficult, because the gross receipts are calculated semiannually.

D. TRANSITION TO NEW RATE STRUCTURE

The Copyright Office strongly recommends that Congress adopt the flat, per subscriber, per signal, per month model as the basis for reform. The Office does not recommend any specific rates. Rather, the Office believes that the rates should reflect the true fair market value of those signals. To determine the rates, a full evidentiary record must be developed.

Therefore, the Office recommends that within six months of passage of the reform bill, a CARP should be convened to take evidence on what the flat, per subscriber, per signal rates should be based on the following criteria:

- (a) the fair market value of the rates;
- (b) the rates paid by satellite carriers, and whether any disparity in the rates paid by cable systems and satellite carriers is justified in terms of the regulatory, technological, and economic differences between the two industries;
- (c) the economic impact on small cable systems.

While a CARP is deciding the new rates, the old rates would continue. At the time that the Librarian of Congress adopts the CARP's rates, those rates would take effect, notwithstanding any pending appeal.⁶⁹

⁶⁹ Such a policy follows the current law concerning CARP rates, "The pendency of an appeal under this paragraph (continued...)"

Although the time limit on current CARP proceedings is six months, the Office recommends that Congress allow this particular CARP a longer period to make its determination, if necessary.

Such proceedings should bring the rates to fair market value, narrow the gap between the rates paid by cable systems and satellite carriers to such amounts as can be justified as based on different regulatory, technological or economic contexts, and determine how much the subsidy for the smaller cable systems should be.

After a CARP has made its determination concerning cable rates, the Office recommends that all future rate adjustment proceedings be combined cable-satellite rate adjustment proceedings conducted every five years. This will allow the same CARP to compare the cable and satellite carrier industries at the same time.

It is hoped that by bringing both the cable and satellite carrier rates to full fair market value, the next step toward elimination of the compulsory license will be a small one.

(...continued)

shall not relieve persons obligated to make royalty payments under section 111 . . . to deposit the statement of account and royalty fees specified in those sections." 17 U.S.C. § 802(g).

VI. SHOULD THE CABLE COMPULSORY LICENSE APPLY TO OPEN VIDEO SYSTEM OPERATIONS?

A. THE TELECOMMUNICATIONS ACT OF 1996

Before the passage of the Telecommunications Act of 1996,⁷⁰ telephone companies had been prohibited from entering the cable television business within their own service areas. The Federal Communications Commission did, however, consider the possibility of authorizing telephone companies to lease channel capacity over their phone lines to third parties who would provide video service to phone company subscribers.⁷¹ The system was known as video dialtone, and the FCC issued experimental licenses to a handful of video dialtone operators, several of whom had already begun service to subscribers at the time the Telecommunications Act was passed. These operators provided original and source licensed programming, as well as retransmission of broadcast signals.

When Congress enacted the Telecommunications Act, it repealed the telephone-cable cross-ownership restrictions embodied in prior telecommunications law. This enabled telephone companies to provide video programming directly to subscribers in their telephone service areas.⁷² The Telecommunications Act also repealed the FCC's video dialtone rules and policies (without actually requiring the termination of any video dialtone system that the FCC had already approved) since they were no longer necessary in light of the more expansive business opportunities afforded the telephone companies under the new law.⁷³ Section 651 of the Telecommunications Act lists the following options for telephone companies (as "common carriers") entering the video programming marketplace: (1) provide video programming to

⁷⁰ Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56, (hereinafter referred to as the "Telecommunications Act").

⁷¹ See First Report & Order in Docket No. 87-266, 56 Fed. Reg. 65,464 (1991).

⁷² Id. at § 302(b)(1).

⁷³ Id. at § 302(b)(3).

subscribers through radio communication under Title III of the Communications Act;⁷⁴ (2) provide transmission of video programming on a common carrier basis under Title II of the Communications Act;⁷⁵ (3) provide video programming as a cable system under Title VI of the Communications Act;⁷⁶ or (4) provide video programming by means of an "open video system" under new section 653 of the Communications Act.⁷⁷ Congress also determined that, to the extent permitted by the FCC's regulations, a cable operator or any other person may provide video programming through an open video system.⁷⁸

The FCC characterizes section 653's open video system option as "an entirely new framework for entering the video marketplace."⁷⁹ In creating a regulatory structure around the Telecommunications Act's open video system provisions, the FCC attempted to incorporate the Act's general goal of "accelerat[ing] rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans by opening all telecommunications markets to competition."⁸⁰ More simply put, in creating the new "framework" for entering the video marketplace -- "open video systems" -- Congress and the FCC strove to promote competition, to encourage investment in new technologies, and to maximize a consumer's choice of services. To achieve these goals, the law offers telephone companies and, perhaps, others who choose to enter the field, broad flexibility in determining how to enter the video marketplace.

⁷⁴ Id. at § 651(a)(1).

⁷⁵ Id. at § 651(a)(2).

⁷⁶ Id. at § 651(a)(3).

⁷⁷ Id. at § 651(a)(3)-(4).

⁷⁸ Id. at § 653(a)(1).

⁷⁹ Report and Order and Notice of Proposed Rulemaking in CS Docket No. 96-46 (adopted & released March 11, 1996) 61 Fed.Reg. 10,496 (1996) at ¶ 4.

⁸⁰ Id. at 10,500 n. 3, ¶ 2 (quoting Telecommunications Act of 1996 Conference Report, S. Rep. No. 230 at 113). 104th Cong., 2d Sess. 131 (1996).

Generally, the Telecommunications Act states that an open video system operator: (1) is prohibited from discriminating among video programmers regarding carriage on their systems or among subscribers regarding information the operations provide for the purpose of selecting programming; (2) shall establish rates, terms, and conditions of carriage that are just and reasonable; (3) is prohibited from selecting the video programming (or acting as a programmer itself) on more than one-third of its activated channels if carriage demand exceeds capacity; (4) shall abide by sports exclusivity, network nonduplication and syndicated exclusivity regulations established by the FCC for open video systems; and (5) shall abide by any must-carry rules, and public, educational and governmental (PEG) obligations, and Title III retransmission consent obligations that the FCC establishes for open video systems. The Act also permits the open video system operator to use channel sharing arrangements.

The structure and appearance of open video systems remain largely unresolved at this time. Private industry is still very much in the planning stage, even though the FCC has its open video system rules in place, and telephone companies and other entities interested in building open video systems enjoy reduced regulatory burdens that should maximize their flexibility and reduce the necessity for government oversight of their operations.⁸¹ It would appear likely that one reason that open video systems have not developed a more apparent structure for doing business is the uncertainty the industry faces about how to clear the copyrights in the programming that the open video systems will be retransmitting over the telephone lines.

In the Telecommunications Act, Congress gave little guidance as to an open video system's status under the copyright law. As such, an open video system would arguably be subject to full copyright liability for the public performance of the many copyrighted works embodied in the broadcast signals being retransmitted by the system. This, of course, would not be the case if the open video system were eligible

⁸¹ Some of the Title VI provisions that do not apply to open video systems under subsection 653(c) are: "leased access" obligations under section 612; franchise requirements and fees under sections 621 and 622 (though an open video system operator will be subject to a gross revenue fee at a rate not to exceed the franchise fee paid by the local cable operator under subsection 653(c)(2)(B)); rate regulation under section 623; and consumer protection and customer service requirements under section 632. *Id.* at ¶ 6.

for, and satisfied the requirements of, the Copyright Act's section 111 cable compulsory license. Rather than answering the question whether open video systems are eligible for a section 111 compulsory license, the Telecommunications Act provides in section 653(c)(4) that "[n]othing in this Act precludes a video programming provider making use of an open video system from being treated as an operator of a cable system for purposes of section 111 of title 17, United States Code."

Some commenters in this study have argued that this provision is a congressional affirmation that open video systems do indeed qualify for a section 111 license. The Copyright Office, however, believes that the language merely clears the way for determination of the compulsory license eligibility issue in another forum (i.e. administrative or judicial) or at another time by Congress.⁸²

B. PRIOR COPYRIGHT OFFICE CONSIDERATION REGARDING THE STATUS OF OPEN VIDEO SYSTEMS

For the second accounting period of 1995, the Copyright Office received cable compulsory license statements of account and royalty filings from three systems identifying themselves as video dialtone operators under the rules of the FCC (regulatory precursors to open video systems). The filing parties appeared to be independent program providers leasing access on an open video system created by telephone companies. Faced with these first claims of eligibility under section 111 by open video systems, and expecting additional filings by open video system operators in light of the recent passage of the Telecommunications Act, the Copyright Office opened a Notice of Inquiry to address the eligibility of open video systems for a cable compulsory license under section 111 of the Copyright Act.⁸³

⁸² The Copyright Office noted in its Notice of Inquiry regarding open video systems (Docket No. 96-2) that during the legislative process of the Telecommunications Act, proposals were considered to address specifically telephone company eligibility for section 111 and such amendments were not included in the Telecommunications Act. 61 Fed. Reg. 20,197-20,199 (1996) at n.6.

⁸³ Id.

While the Copyright Office was considering the commenters' arguments as to whether open video systems are eligible for a compulsory license under section 111 of the Copyright Act, the Office received the request from Senator Hatch and the Senate Committee on the Judiciary that prompted this study. Soon thereafter, the Office terminated the Notice of Inquiry regarding open video systems so that it could devote its full energies to addressing the issues raised in the Notice in this study.⁸⁴

C. SUMMARY OF COMMENTS AND TESTIMONY

1. The Eligibility Issue.

The issue posed in this study, whether open video systems should be eligible for some variety of compulsory licensing under the Copyright Act, differs from the issue discussed in the Copyright Office's Notice of Inquiry, whether open video systems are eligible for compulsory licensing under the current section 111, in that the scope of the study can go beyond the words and meaning of section 111 as it now exists. The study, therefore, addresses whether open video systems should be entitled to compulsory licensing under the Copyright Act at all and, if so, what statutory provisions would best provide compulsory licensing for the retransmission of broadcast signals by open video systems considering the legal, technological, and business realities of the telecommunications world today.

In the context of this study, copyright owners, with the exception of PBS and the Canadian Claimants, are adamantly opposed to the application of any compulsory licensing provisions to the retransmission activities of open video systems. Starting with the proposition that the time has come for all compulsory licensing for the retransmission of broadcast signals to cease,⁸⁵ the copyright owners argue that

⁸⁴ Termination of proceeding in Docket No. 96-2A, 62 Fed.Reg. 25,212 (1997). Nothing in this discussion is intended to indicate the Office's disposition of the issues of OVS' eligibility for a compulsory license as a section 111 cable system should Congress decline to act on the Office's legislative recommendations.

⁸⁵ ASkyB, the DBS carrier that intends to offer subscribers the retransmission by satellite of local broadcast stations, would support the elimination of both section 111 and section 119 compulsory licenses. ASkyB, comment 33, at 2.

giving a compulsory license to open video systems (or other new retransmission services) would require copyright owners to subsidize the newcomers. NBA/NHL, comment 22, at 2. They further contend that Congress should afford the marketplace an opportunity to develop licensing mechanisms for open video systems and similar new retransmission technologies. Baseball, comment 17, at 11; NBA/NHL,⁸⁶ comment 22, at 2; NCAA, comment 26, at 2; ASCAP, comment 6, at 28; MPAA, comment 35, at 11. ASCAP argues that "it is a given that inclusion of new technologies in current compulsory licensing schemes or creation of new ones will discourage private negotiation and inhibit the development of marketplace solutions." ASCAP, comment 6, at 23.⁸⁷

The copyright owners are particularly insistent that the rationale for the creation of the section 111 and section 119 licenses, which was to assist the incipient cable and satellite industries whose existence was threatened by a lack of access to programming and financial resources, simply does not exist today, especially with respect to the open video system industry. They contend that "the nature of [the open video system business] requires that all of the entrants into this field have significant resources for start-up costs and program acquisition." *Id.* at 28. There is an underlying view expressed by these commenters that "the telephone companies" are wealthy, powerful entities that do not need the benefits of a compulsory license to make a success of their ventures into the business of retransmitting broadcast signals over open video system platforms. NBA/NHL, comment 22, at 2. These commenters do not address the issue of how an open

⁸⁶ The NBA is a not-for-profit partnership of 27 clubs engaged in the sport of professional basketball. The NHL is a joint venture organized as an unincorporated association, not-for-profit, of 26 clubs engaged in the sport of professional hockey.

⁸⁷ However, another commenter has noted that where a compulsory licensing scheme exists for other industries, an industry left without such a license may be left with no opportunities for licensing at all. In comments submitted in the Copyright Office's Notice of Inquiry regarding open video systems, the Federal Trade Commission noted that were open video systems required to negotiate for retransmission programming in the free market, "a market for brokerage service might arise to negotiate universal licenses with programmers ... [h]owever, a brokerage service market may not arise, since stand-alone demand for broadcast programming by OVS's may not be sufficient to support the development of efficient, competitive programming brokers." Comments of the Staff of the Federal Trade Commission, reply comment 3, in Copyright Office Docket No. 96-2, at 5, n.10.

video system would effectively compete in the "free market" with similarly situated cable systems operating under the section 111 license.

ASCAP contends that new compulsory licensing schemes would place additional burdens and costs on copyright owners to participate in additional ratemaking and distribution proceedings, and would place added administrative and operational burdens on the Copyright Office. ASCAP, comment 6, at 28. However, ASCAP does not specify how this would be the case if section 111 were amended to encompass open video systems in one overall license, since the only additional burden on the copyright owners and the Office would be in tracking additional filings and royalties added to the same basic pool.

The NCAA also argues that extending the cable license in any way would "further break down regional sports broadcast arrangements" as discussed in its arguments in favor of the elimination of all compulsory licenses for the retransmission of broadcast signals. NCAA, comment 26, at 2.

Finally, the copyright owners stress that the nature of the open video system business is still undefined and undeveloped, and it would be unwise at this time to create for the benefit of the industry a compulsory licensing scheme which might not be workable or practical. MPAA, comment 35, at 11; ASCAP, comment 6, at 28; BMI, comment 27, at 14. ASCAP notes that today only one open video system, Bell Atlantic's system in Dover Township, New Jersey, is fully operational. ASCAP, comment 6, at 29.⁸⁸ ASCAP suggests that the telephone companies themselves have put a brake on their plans for rapid expansion of the open video system business because they haven't decided how to develop the industry. Id.

In the context of the Copyright Office Notice of Inquiry, copyright owners argue more specifically that section 111 cannot be read to permit open video systems to qualify as cable systems eligible for a compulsory license, and that only Congress, by specifically amending the copyright law, could make open

⁸⁸ See ASCAP, comment 6, at 8 n.5 (citing FCC, Third Annual Report In the Matter of Annual Assessment of the Status of Competition In the Market for the Delivery of Video Programming, 1997 WL 2451, ¶ 71.)

video systems eligible for a compulsory license.⁸⁹ They contend that it would be inappropriate to "jerryrig a twenty-year old statutory plan created for a different industry." MPAA, comment 1, in Copyright Office Docket No. 96-2, at 2; *see* Music Claimants reply comment 8 in Docket No. 96-2, at 4-5.

To the contrary, all the other commenters in this study addressing the issue, and the others in the Copyright Office administrative inquiry, take the position that open video systems are multichannel video providers that will most likely operate in a fashion so functionally similar to traditional cable systems as to justify the applicability of a compulsory license to them, on terms that account for any technological and regulatory peculiarities of those services. Time Warner,⁹⁰ comment 23, at 7; ALTV, comment 30, at 4; NPR, comment 36, at 11; Canadian Claimants, comment 32, at 5; ABC, comment 20, at 2; PBS, comment 28, at 41; U.S. West, comment 4, at 13; USTA, comment 25, at 16. USTA notes that, in fact, open video systems do not embody a "new" technology at all, but simply a program delivery system established by law and regulatory overlay. *Id.* at 3, n.2. As such, and because open video systems are subject to FCC must-carry, syndicated exclusivity, sports exclusivity, and network nonduplication rules that are almost identical to those applied to traditional cable systems, they can be deemed to comprise an essentially local subscription service featuring as a significant component of its services the local retransmission of local broadcast programming, just like traditional cable. NAB, comment 39, at 8; NPR, comment 36, at 11.

The commenters citing these similarities between traditional cable systems and open video systems conclude that the open video system industry acts as a nascent competitor to cable, and disparate copyright treatment for open video systems would substantially skew the competitive arena and force consumers to pay higher rates for cable service than they otherwise would. NPR, comment 36, at 11. The Federal Trade

⁸⁹ *See, e.g.*, comments in Copyright Office Docket No. 96-2: Joint Sports, reply comment 6, at 4-5; ASCAP, BMI, SESAC, reply comment 8, at 4 [hereinafter Music Claimants, comment 8].

⁹⁰ Time Warner is a diversified media company which acts as a multiple systems operator of cable systems nationwide and is also engaged in the production and distribution of theatrical films, television programs and home videos. Time Warner, comment 23, at 1, [hereinafter Time Warner, comment 23].

Commission makes a similar analysis in its comments in the Copyright Office administrative hearing. FTC, reply comment 3, in Copyright Office Docket No. 96-2, at 5. Even the Canadian Claimants, with a proprietor perspective, find economic advantage to open video systems' potential eligibility for a compulsory license. They state that because the statutory and regulatory structure authorizing the existence of open video systems effectively limits the industry's deployment to large, well-funded companies such as local telephone companies that have an installed communications system (or companies that can afford to install such a system), there will be fewer entrants, a limited number of times a signal will be transmitted, and a higher certainty that the compulsory license royalties will be paid. Canadian Claimants, comment 32, at 5-6.

The USTA offers a detailed discussion of the eligibility of open video systems for compulsory licensing. It forcefully argues that Congress' goals in creating open video systems under the Telecommunications Act will best be met if open video systems are put on an equal copyright footing with respect to other multichannel video providers:

Congress created OVS in order to bring competition to a market dominated by incumbent cable operators. Congress stated that it hoped the OVS approach would "encourage common carriers to deploy open video systems and introduce vigorous competition," also noting that OVS operators "will be 'new' entrants in established markets and deserve lighter regulatory burdens to level the playing field." The availability of the cable compulsory license for OVS operators is an essential and viable means of fair competition with these incumbent cable operators.

USTA, comment 25, at 13 (citing the Telecommunications Act of 1996, § 653(c)(4), H.R. Conf. Rep. No. 458, 104th Cong., 2d Sess., 178 (1996)). The USTA also points out that Congress has taken a technology neutral position on the application of the cable compulsory license for other new retransmission systems such as SMATV, MDS, and MMDS operations, as well as satellite carrier operations; it argues that open video systems should be no exception to this treatment. USTA, comment 25, at 14, 20-21.

The SBCA takes a position that falls outside the debate of eligibility or ineligibility for open video systems under section 111. Arguing parity among providers of broadcast signals, SBCA contends that telephone companies as large and established multichannel video providers should not now enjoy the terms

and advantages of the cable compulsory license because those were not available to DTH carriers when they were new video distribution entrants. The SBCA argues that in fairness, Congress should only make open video systems eligible for the cable compulsory license at such time as it also gives satellite carriers a permanent license and cable-like rates; otherwise, it should devise a section 119 like treatment for open video systems. SBCA, reply comment 22, at 7-8.

2. The "Nuts and Bolts" of a Compulsory License for Open Video Systems.

Only a few commenters have discussed in any detail how a revised cable compulsory license that would encompass open video systems might work. Although MPAA opposes any compulsory licenses for the retransmission of broadcast signals, in the Copyright Office inquiry on open video systems, MPAA suggested a legislative proposal that would offer open video systems a temporary compulsory license to enable its growth as an industry and to ease its transition to the free market. MPAA, comment 1, in Copyright Office Docket No. 96-2, at 1, 16-19. Although the proposal envisioned interim regulations allowing open video systems to utilize the present section 111 which would be replaced by some individualized compulsory license crafted by Congress for a more mature open video system industry, the proposal makes a useful starting point for a discussion on how section 111 might be revised to encompass open video systems on a more permanent basis.

The MPAA proposal assumes that open video systems will operate under section 111 as it exists today. It is instructive to note that all of the following discussion would be rendered moot if Congress were to adopt a flat, per subscriber, per signal rate as recommended by the Office in Chapter V. However, the Office has included the following discussion in the event that the current rate structure is retained.

First, MPAA addresses the issue of which elements of the open video systems (i.e., the telephone company operators or the independent program providers that deliver programming via the system) are eligible for the compulsory license and under what circumstances. MPAA argues that to achieve parity between the royalties paid by open video systems and those of similarly situated cable systems, and to avoid

artificial fragmentation of an open video system from what is really a larger system into a smaller system (the "contiguous communities" problem for traditional cable systems), each open video system operator must determine the gross receipts of the entire open video system operation for purposes of determining the system's filing status (i.e. Form 1/2 or Form 3). The amount of total gross receipts would be the sum of all payments throughout the entire open video system made by program providers or by subscribers that are related to the offering of retransmitted broadcast signals to subscribers. Id. at 17; *see* 11-17. After the open video system operator makes this determination, MPAA would have each program provider, including the open video system operator to the extent that it offers programming, calculate its own gross receipts and DSE values, and file statements of account and make royalty payments based on the entire operation's filing status. These calculations would be analogous to those made by partially distant subgroups of cable systems. Id. at 18.

Other commenters in the administrative inquiry take a similar view on the issue. *See* comments filed in Copyright Office Docket No. 96-2: Comcast comment 6 at 3; NCTA, at 4; ABC, comment 2, at 7-8. Two of those suggest that each open video system facility should generate only one consolidated filing under section 111. Comcast comment 6 in Copyright Office Docket No. 96-2, at 3; ABC comment 2 in Copyright Office Docket No. 96-2, at 8. The open video system commenters, however, contend that any entity that becomes an open video system program provider offering multiple channels, including broadcast signals, to subscribers should be considered the owner of a cable system responsible for section 111 filings with respect to the channels it operates. Bell Atlantic, *et. al.*, comment 7 in Copyright Office Docket No. 96-2, at 26; U.S. West, comment 2, in Docket No. 96-2, at 6.⁹¹ Bell Atlantic suggests that the "contiguous communities" language in the present definition of "cable system," can be applied to open video systems as easily as to

⁹¹ U.S. West argued that if open video system operators were required to include the gross receipts of unaffiliated program providers carried on its system, and the aggregation of receipts resulted in their paying higher royalty rates, they would be entitled under FCC rules to collect administrative fees associated with such filings and to be reimbursed by the programmers for any increased royalties. West argued that this situation would be discriminatory and anti-competitive.

cable systems if lawmakers adopt the legal fiction that for an open video system programmer, the "headend" is deemed to be the "office or site where the video distribution antennae receiving off-air signals (the "primary transmission") interconnects with the OVS wires (the "secondary" transmission)." Bell Atlantic, *et al.*, comment 7 in Docket No. 96-2, at 23. Of course, these issues would not be relevant if Congress were to change the rate structure for section 111 to a flat, per subscriber, per signal fee and to eliminate the lower rates for small cable systems.

In its response to our Notice of Inquiry, MPAA pointed out that where an open video system provides service to multiple markets, under the FCC's must-carry rules, the system may provide all the must-carry signals from each market to all subscribers, or it may configure its facilities so that subscribers only receive the must-carry stations in their own market. If the system chooses the first alternative, it is likely that some part or parts of its must-carry station carriage will be distant for copyright purposes. MPAA would have open video systems determine distant/local status and permitted/non-permitted status on an ADI basis.⁹² To address the situation in which a system serves multiple ADI's and its program providers do not restrict their own service to one ADI, MPAA suggests that the open video system operator would act as arbiter and determine what percentage of the system's total number of subscribers receive each signal as a distant signal. Each program provider would then apply that percentage to its own group of signals, including must-carry signals, to determine the appropriate distant signal equivalent value for its own subscriber group.

Further complicating the issue, the open video system operator has the duty to fulfill the system's must-carry obligation, but often the subscribers will pay the program provider and not the open video system operator for such service, and the operators are not required to use a basic tier for must-carry signals. This situation would make reporting very difficult for an open video system. MPAA, comment 1, in Docket 96-2, at 11-14. To address this difficulty for open video system operators, MPAA would require each program

⁹² The ADI is the Area of Dominant Influence, and is the current way the FCC defines the local market of a television station.

provider to be liable for the minimum royalty fee payment for the must-carry service provided by the cable operator to the program provider's subscribers. Id. at 17-18.

For permitted/non-permitted status, MPAA proposes that each system be governed by the rules that would apply to a cable system located in the largest ADI served by the open video system operator, rather than try to have each program provider determine permitted/non-permitted status on a subscriber-by-subscriber basis. Id. at 18-19. This system, MPAA suggests, would ensure that an open video system not "fragment distant carriage among program providers" and avoid the 3.75% rate liability. Of course, again, these complexities would be avoided if a different rate structure can be devised for section 111.

The telephone companies suggest that to determine local/distant status applying the FCC's must-carry and ADI rules, where there is no established cable system operating in the same service area as an open video system, an open video system could be treated as a new, start-up cable system would be treated. Bell Atlantic, *et. al.* in Docket No. 96-2, comment 7, at 21-22, 26. They contend that in cases where the FCC rules require an open video system to carry broadcast signals, these signals should be treated as local signals for copyright purposes, and that in interpreting permitted/non-permitted carriage, communities and not systems should be granted grandfathered status, so that open video systems get the benefit of paying for signals that are permitted as grandfather signals for similarly situated traditional cable systems at the lower permitted signal rate. Id. On the issue of determining whether signals are local or distant for an open video system whose programmers are located in various places, USTA suggests that each programmer using an open video system designate one point at which they receive programming for retransmission to be designated as the locus of its "facility" and file based on communities served by that point. *See* comments in Copyright Office Docket No. 96-2; USTA, comment 9, at 7, n.5; UVTV, comment 4, at 9-10; Adelphia, comment 12, at 6; Comcast, comment 6, at 1, 6.

Making a similar attempt at creating parity among cable and open video system operators, NCTA suggests that open video system operators be required to pay the 3.75% rate where the total number of distant

signals carried on the system exceeds those that a cable operator in the same market would be permitted to carry at the statutory base rate. NCTA, comment 11, in Docket No. 96-2, at 5. Several parties suggest that whatever regulations govern the application of the cable compulsory license to new cable systems or SMATV systems should be relevant to open video systems. *See* Comments in Docket No. 96-2: NAB, comment 13, at 15-16; ALTV, comment 10, at 19-21.

D. COPYRIGHT OFFICE RECOMMENDATIONS

The Copyright Office is sympathetic to the arguments presented by the majority of copyright owners in this study regarding the desirability of the elimination of compulsory licenses for the retransmission of broadcast signals. Given the premise that the time has come for the elimination of the cable and satellite compulsory licenses, it is difficult to argue that compulsory licensing should apply to more retransmissions made by a new brand of communications channels, the open video system, that was created by both the deregulation and the entrepreneurial zealotry of the telephone companies. Assuming, however, that Congress does not agree with the copyright owners that now is the time to eliminate sections 111 and 119 of the Copyright Act, the Copyright Office agrees with the rest of the commenters that it would be patently unfair, and it would thwart Congress' intent in creating the open video system model, to deny the benefits of compulsory licensing to open video systems when similar benefits are enjoyed by traditional cable systems, satellite carriers, SMATV systems, and MDS and MMDS operations.

The Copyright Office is swayed by the strong resemblance of open video systems to traditional cable systems. Open video systems use the very same "wires, cables [and] other communications channels" that traditional cable systems use to deliver broadcast signals to their subscribers. They will be located in the same geographical areas as traditional cable systems and will potentially serve the same subscribing members of the public as cable systems. Open video systems will be constrained by the same public interest obligations as cable to deliver public, educational and governmental programming, to ensure carriage of local broadcasters and to respect syndicated and sports exclusivity arrangements and protect the network affiliate system by ensuring network nonduplication. In fact, the only discernible differences between open video systems and traditional cable systems are historical. Cable arrived on the scene because of consumer desire for basic programming service, and it fought hard to win a compulsory license that enabled it to become the giant in the video programming industry that it is today. Open video systems were created by Congress because of consumer unrest with cable and a burgeoning telecommunications industry that was anxious to

expand its interests and challenge cable for part of its market share, but has yet to demonstrate how it will try to win a place for open video systems in the program delivery universe. The fact that open video systems will look slightly different from cable systems does not alter the issue of basic fairness confronting the legislators who have created a compulsory licensing structure and doled it out to first one retransmission agent and then another. Should some businesses have the undoubted benefits of a compulsory license, its guaranteed access to programming with its minimal administrative burdens and relatively low cost, but not their direct competitors? The Copyright Office cannot answer that question in the affirmative when the businesses operate in a similar universe and are otherwise subject to analogous regulatory burdens.

While the Copyright Office is, therefore, comfortable with the notion that open video systems should be eligible for compulsory licensing for their retransmission activities, the Office finds it to be vastly preferable for Congress to modify the existing cable compulsory license to clarify how open video systems fit into the licensing scheme rather than trying to suggest that open video systems are already cable systems under section 111. It would seem prudent to include open video systems in section 111 and not try to create a separate compulsory license for them. This is so primarily because open video systems are so inherently similar to cable systems.

The Copyright Office acknowledges the truth in the copyright owners' assertions that the open video system industry is not yet developed enough to enable Congress to create a compulsory license for open video systems that mirrors the intricacies of its business arrangements. However, the Office does not think it will be necessary to know precisely what form or forms the industry will take to draft adequate compulsory licensing provisions. The basic structure of open video systems is clearly established by statute and regulation, and it will certainly be very comparable to the structure of cable systems.

The Copyright Office believes that section 111 should be amended in several ways to facilitate the eligibility of open video systems for the cable compulsory license. First, the definition of cable system in section 111(f) should be amended to specifically include open video systems as cable systems, and to clarify

that each programmer on the open video system is responsible for filing and paying royalties as a cable system. Furthermore, for purposes of identifying which open video system programmers must file together as one system to avoid artificial fragmentation of one larger system into smaller systems, it will be essential for Congress to amend the "contiguous communities" section of the definition of cable system, as described in Chapter IV.

In addition, both the complex rate structure of the current section 111 and the statute's reliance on the former FCC rules for determining local and distant signals must be amended, as discussed in Chapter V, to ensure the smooth administration of the compulsory license with open video systems as cable systems. This could eliminate the need for the various legislative or administrative proposals listed earlier in this chapter that would otherwise be necessary to fit open video systems within section 111. Finally, the passive carrier exemption should be amended as the next chapter describes.

VII. THE PASSIVE CARRIER EXEMPTION

In the course of its open video system inquiry, the Copyright Office had reason to revisit the passive carrier exemption in section 111(a)(3) of the Copyright Act. That section provides an exemption from copyright liability to any carrier who retransmits one or more broadcast signals so long as that carrier has "no direct or indirect control over the content or selection" of the broadcast signal being retransmitted or the recipients of the signal, and so long as its only involvement in the retransmission is to provide the "wires, cables, or other communications channels for the use of others." In comments filed with the Office in Docket 96-2 on open video systems, the parties argued back and forth whether, and to what extent, open video systems qualify as passive carriers eligible for the exemption.

In requesting information for this study, the Copyright Office posed the question whether the passive carrier exemption requires amendment to accommodate open video system and/or Internet retransmitters and, if so, in what fashion. The comments the Office received suggest a number of theories regarding the applicability of the passive carrier exemption to open video systems, and some also offer additional comments regarding the perceived abuse of the exemption by satellite carriers who retransmit broadcast signals to cable systems and the need for a tightening of the exemption.

A. BACKGROUND INFORMATION

The passive carrier exemption originated during the cable television controversy that raged in the 1960's when Congress was attempting a major revision of the Copyright Act of 1909.⁹³ At that time, telephone companies were concerned that because of ambiguity in proposed cable provisions, the retransmission of broadcast signals by cable systems using a telephone company as a common carrier (i.e. to provide lines, equipment, etc.) might be deemed to create copyright liability for the telephone companies.

⁹³ The Copyright Office thoroughly, discussed this controversy and the history of the cable and satellite compulsory licenses in its earlier report. See *Library of Congress, U.S. Copyright Office, Report of the Register of Copyrights, The Cable and Satellite Carrier Compulsory Licenses: An Overview and Analysis* (March 1992).

They proposed language for a specific exemption for passive carriers, and their proposal ultimately became section 111(a)(3).⁹⁴

In the mid-1970's, technological advances enabled satellite carriers to receive broadcast signals (either over-the-air by means of a UHF receiving antenna or by means of a direct microwave connection between the broadcast station and the satellite carrier), then to retransmit the signals to a satellite transponder, and relay the signals by the satellite back to the cable systems' receiving antennae on earth for delivery by the cable systems to their subscribers. This method of retransmitting signals transforms ordinary broadcast stations into "superstations" seen by viewers across the nation. Three mid-1980's appellate court decisions interpreted the section 111(a)(3) exemption as applying to satellite carriers' activities in retransmitting superstations based on a finding that they act as purely passive intermediaries between broadcasters and the cable systems.⁹⁵

In Eastern Microwave, Inc. v. Doubleday Sports, Inc.,⁹⁶ the U.S. Court of Appeals for the Second Circuit held that Eastern Microwave's retransmission of superstation WOR to cable systems fell within the passive carrier exemption even though the court found that technical restrictions forced EMI to make "an initial, one-time determination to retransmit the signals of a particular station." It decided that such a determination does not evidence the "control over the content and selection of the primary transmission intended to be precluded under section 111(a)(3)." Id. at 125, 126.

The court stated that an ordinary common carrier must render its service to all comers, denying it to none on the basis of content, and must not select or choose among those who seek to use its service, on

⁹⁴ See Letter of Professor Walter J. Derenberg, on behalf of American Telephone and Telegraph Company, to Thomas C. Brennan, Chief Counsel, Committee on the Judiciary, U.S. Senate April 25, 1967, (following the introduction of S. 579), reprinted in *Hearings Before the Subcommittee on Patents, Trademarks and Copyrights of the Senate Committee on the Judiciary, Copyright Law Revision*. 90th Cong. 1st Sess. 1143 (1967).

⁹⁵ Eastern Microwave, Inc. v. Doubleday Sports, Inc., 691 F.2d 125 (2d Cir. 1982); WGN Continental Broadcasting Co. v. United Video, 693 F.2d 622 (7th Cir. 1982); Hubbard Broadcasting, Inc. v. Southern Satellite Systems, 777 F.2d 393 (8th Cir. 1985).

⁹⁶ 691 F.2d 125 (2d Cir. 1982).

any basis other than a legitimate business reason. The court then reasoned that when the communication service is technologically limited to one sender, a forced "selection" is inevitable, and such a selection cannot be the type precluded by section 111(a)(c), for to so hold would render the exemption unavailable to "any carrier that did not retransmit every television broadcast of every television station in the country." Id. at 130.

In reaching its holding, the Second Circuit noted that "[u]nlike the activities of older, established common carriers, e.g., the telephone company, . . . the activities [of Eastern Microwave] include carrying the communications desired by receivers rather than those desired by senders" and "unlike older common carriers, EMI is paid by receivers rather than by senders." However, the court noted that "[l]ike those of older common carriers, EMI's activities are paid for as services and involve transmittal of the entire signal without change." Id. at 126. Thus, the court allowed the exemption where the carrier did not look exactly like a telephone company, so long as the carrier did not alter the signal it retransmitted to cable systems.

In WGN Continental Broadcasting Co. v. United Video,⁹⁷ superstation WGN sued a satellite common carrier, United Video, for retransmitting WGN's programming to cable customers stripped of certain teletext information that had been inserted into the "vertical blanking interval" space between the pictures flashed on a television screen. That interval can be used to carry such information as subtitles for the hearing impaired, news bulletins, and weather reports. Id. at 623-24. The Seventh Circuit described the relationship between the cable system and satellite carrier under the passive carrier exemption as follows:

The cable system selects the signals it wants to retransmit, pays the copyright owners for the right to retransmit their programs, and pays the intermediate carrier a fee for getting the signal from the broadcast station to the cable system. The intermediate carrier pays the copyright owners nothing provided it really is passive in relation to what it transmits, like a telephone company. . . . It may not even delete commercials; an important part of the scheme set up in section 111 is the requirement that any cable system that wants to retransmit a broadcast signal without negotiating with

⁹⁷ 693 F.2d 622 (7th Cir. 1982).

the broadcast station or copyright owner transmit intact any commercials it receives from that station.

Id. at 624-25. The court concluded that United Video could not qualify for the passive carrier exemption "because it was not passive -- it did not transmit WGN's signal intact." Id. at 625.

Hubbard Broadcasting, Inc. v. Southern Satellite Systems⁹⁸ examined whether Southern Satellite could still qualify for the passive carrier exemption when it retransmitted superstation WTBS's signal intact from a direct microwave feed supplied by WTBS even though the station itself altered its over-the-air signal by substituting national advertising in the place of local advertising when it prepared the microwave feed. In these circumstances, the United States Court of Appeals for the Eighth Circuit found that the satellite carrier exercised neither direct nor indirect control over the content of the WTBS signal, and the broadcaster's involvement in the commercial substitution process did not implicate any of the concerns raised by Congress in adopting section 111(c)(3) (which prohibits cable systems from engaging in commercial substitution).

Once the business of the retransmission of superstations to cable systems by satellite carriers was firmly entrenched, the passive carrier exemption did not again become an issue until the development of home earth stations (satellite dishes) created another business opportunity for satellite carriers. Initially, broadcast signals (and other signals) delivered by satellite carriers could be intercepted by dish owners who were not part of the copyright owners' intended audience, and dish owners paid no fee to carriers or copyright owners for the signals they received. To control access to the signals, most resale carriers and certain copyright holders decided to encode, or scramble, their satellite delivered signals, and to provide descrambling capacity only to paying subscribers of their service.⁹⁹

⁹⁸ 777 F.2d 393 (8th Cir. 1985).

⁹⁹ See H.R. Rep. No. 887, 100th Cong., 2d Sess., Pt. 1, at 12 (1988).

This brought the status of the satellite carriers' eligibility for the passive carrier exemption into question. By scrambling signals and selling, renting, or licensing descrambling devices to subscribing earth station owners, a carrier arguably exercises direct control over which individual members of the public receive the signals they retransmit, and the carrier engages in more than merely providing "wires, cables, or other communications channels." In March of 1986, the Chairman of the Subcommittee on Telecommunications, Consumer Protection and Finance of the House Committee on Energy and Commerce wrote to the Register of Copyrights to request that the Register issue a "preliminary judgment" on the issue whether a satellite carrier that engages in activities such as scrambling signals and marketing descrambling devices would qualify for section 111(a)(3). The Register set forth his view that the sale and licensing of descrambling devices to satellite earth station owners by satellite carriers falls outside the purview of section 111(a)(3), particularly where the carrier itself encrypts the signal.¹⁰⁰

In response to this controversy, the House Committee concluded that legislation was necessary to meet the concerns of home dish owners and satellite carriers and "to foster the efficient widespread delivery of programming via satellite."¹⁰¹ The "Satellite Home Viewer Copyright Act of 1988"¹⁰² was the result of the controversy. The legislation created a statutory license for satellite carriers to retransmit distant broadcast signals of superstations to dish owners for private home viewing. Thus, under the new legislation, satellite carriers were to be compulsory licensees; they could not be considered passive carriers with respect to their activities pertaining to the retransmission of broadcast signals to home dish owners. However, it should be noted that the new law did provide that satellite carriers can be liable for infringement, if they in

¹⁰⁰ Letter from Register Ralph Oman, Register of Copyrights, to Robert W. Kastenmeier, Chairman of the House Subcommittee on Courts and Intellectual Property (March 17, 1986).

¹⁰¹ H.R. Rep. No. 887, 100th Cong., 2d Sess. Pt. 1, at 14 (1988).

¹⁰² Pub. L. No. 100-667, 102 Stat. 3949 (1988).

any way, willfully alter the content of the programming, commercial advertising, or station announcements embodied in the signals they retransmit. 17 U.S.C. § 119(a)(4).

B. SUMMARY OF COMMENTS AND TESTIMONY

1. Open Video Systems Issues.

As indicated above, the present inquiry regarding the passive carrier exemption was made to determine whether open video systems might sometimes be eligible for the exemption. While the comments occasionally strayed from the open video context, by far the majority of comments on the exemption focused on open video systems.

Generally, copyright owner and cable system commenters expressed the view that open video systems will most likely engage in too many "non-passive" activities regarding their retransmission of broadcast signals to be eligible for the passive carrier exemption. However, several of the commenters who took this position seemed to believe that some of a particular open video system's activities might qualify for the exemption under limited circumstances.

Comcast Cable Communications, Inc. argues that an open video system operator can never be a passive carrier under section 111(a)(3). Comcast, comment 12, Attachment A, at 4. Comcast argues that open video system operators are not regulated as carriers under Title II of the Communications Act, but rather under Title VI which governs cable systems, that they exercise control over the selection of primary transmissions when they exercise their discretion to decide how to divide their channel capacity, decide which duplicated programming services offered by multiple programs will share a single channel on the system, and make other decisions affecting content on the system; and they might provide many non-passive business services, such as scrambling signals carried by the system and selling or leasing descrambling devices to subscribers. Comcast, comment 12, at 5. Comcast argues that when an open video system operator is also a program provider, the chances that it would make "content and channel-based decisions" as the platform provider would be even greater. Id. As such, Comcast concludes that open video system

operators could never meet the requirements of the passive carrier exemption, especially as that provision has been narrowly construed by the Copyright Office.

BMI agrees with Comcast. BMI, reply comment 27, at 11. BMI argues that the telephone industry wants to expand the scope of section 111(a)(3) to "exempt its forays into the high margin television business." Id. at 10. BMI differentiates open video systems' retransmission activities from those at issue in the Eastern Microwave and Hubbard cases because unlike the satellite carriers in those cases, open video systems will themselves be transmitting signals to subscribers over their own lines, providing marketing, billing and collection services, and exercising a certain degree of control over the content customers can see on their systems. Id. at 11.

NCTA states its view that whether and to what extent the passive carrier exemption would apply to open video systems depends on the make up of the individual open video system operation and the role played by the telephone company, which cannot be foreseen in the absence of a concrete open video system plan. NCTA, reply comment 4, in Docket No. 96-2, at 3. BMI adds that, regarding the uncertainty of the open video system industry, the FCC's open video system rules are being challenged in federal court in New Orleans. BMI, reply comment 27, at 11 (citing The Cable-Telco Report, at 1, June 2, 1997).

MPAA argues that only "true" common carriers should be eligible for the passive carrier exemption, and the exemption should be "tightened to avoid expanding this common carrier provision to accommodate these [open video system and other new] services." MPAA, comment 35, at 14. This would appear to mean that open video systems cannot be passive carriers. However, in reply comments, MPAA states that it would not object to allowing a carrier to offer ancillary services that are separate from program carriage services, such as billing, without losing its passive carrier status, so long as those services are not a means for the carrier to select or to control customers of an open video system contrary to the requirements of section 111(a)(3). MPAA, reply comment 3, at 10.

Telephone companies, on the other hand, contend that when an open video system operator merely provides channel capacity to an unaffiliated programmer, and has no control over the programming selected or distributed by that programmer, the open video system operator should be considered a passive carrier exempt from copyright liability under section 111(a)(3). USTA, comment 25, at 8-9. To that end, USTA recommends that section 111(a)(3) be amended to clarify that "wires, cables or other communications channels" include all delivery systems, platforms and technologies where the carrier or distributor provides equipment and services but does not control the selection of the content or information delivered over the system. Id.

USTA also argues that their activities related to any must-carry signals, PEG channels, and other channels that open video system operators are required to carry would not disqualify their eligibility for the passive carrier exemption, although it offers no rationale for this conclusion. Id. at 9-10. U.S. West took this position in the Copyright Office inquiry regarding open video systems. It maintained that if an open video system operator were required to carry must-carry or other such signals to subscribers of unaffiliated programmers, the FCC regulations would allow the operator to charge the programmers for the administrative costs incurred by the operator for such carriage. Since the programmer would then pass the added cost on to its subscribers, without the passive carrier exemption, the copyright owners would be getting a double payment, one reflected in the royalties paid by the open video system operator, and one paid by the programmer. U.S. West, comment 2, in Docket No. 96-2, at 13; U.S. West, reply comments 2, in Docket No. 96-2, at 4-5.

USTA claims the decisions in Eastern Microwave, WGN Broadcasting, and Hubbard would permit an open video system operator, as an exempt "passive carrier," to allow its equipment to be used by other programmers to retransmit broadcast signals simultaneously; would permit an open video system to choose which broadcasts to retransmit, so long as there is no alteration, deletion, or addition to the signals; and would permit an open video system to provide ancillary promotional support (such as marketing, billing, or

collecting fees from particular recipients of retransmissions on behalf of other program providers). Lastly, USTA claims that the existing language in section 111(a)(3) should be clarified to permit a telephone company or other carrier that leases its open video system to a programmer to retain the passive carrier exemption where the carrier technically selects which homes to serve, because the wires and channels are capable of serving such homes. *Id.* at 11. Bell Atlantic/NYNEX supports USTA's arguments in support of a very broad reading of the passive carrier exemption for the benefit of open video system operators. Bell Atlantic/NYNEX joint reply comment 11, at 1-2; *see* Bell Atlantic, *et. al.*, comment 7, in Docket No. 96-2, at 30-31.

NAB strongly rejects the position of USTA and U.S. West that open video carriers can deliver must-carry and PEG programming to the subscribers of their unaffiliated programmers and still maintain their passive carrier status. NAB argues that an open video system operator that retransmits must-carry signals cannot be entitled to the passive carrier exemption for such carriage. NAB and PBS both argue that the very fact that an open video system operator is required to meet must-carry and PEG public access obligations makes it impossible for it to act solely as a passive conduit for material supplied by open video system program providers. NAB, comment 13, in Docket No. 96-2, at 10, n.4; NAB, reply comment 5, in Docket No. 96-2, at 2-3; PBS, reply comment 7, in Docket No. 96-2, at 10, n.4.

2. Satellite Carrier Issues.

Two parties discuss possible amendments to the passive carrier exemption outside the open video system context. Baseball expresses the view that the five satellite carriers that retransmit selected superstations and network stations to cable systems across the country make a separate public performance of the copyrighted works on the retransmitted stations. Baseball argues that these carriers should not qualify for an exemption from copyright liability under section 111(a)(3) because they are making a separate use of copyrighted works and they are commercially profiting by doing so; thus, the carriers should be required to share their profits with the copyright owners whose works they exploit. Baseball, comment 17, at 17-18.

Of course, United Video strongly opposes Baseball's suggestion regarding the passive carrier exemption. United Video responds that the exemption was adopted to simplify the retransmission process and avoid double payment to the copyright owner for the single viewing by the cable subscriber of the broadcast programming. United Video, reply comment 12, at 4. United Video likens satellite carriers' function in retransmitting distant signals to those of "Federal Express delivering video tapes or trucks delivering books" -- they all perform a delivery function for the convenience of the customer who is making use of the copyrighted work. Id. at 8.

Another party, LIN Television Corp., complains that the ability of satellite carriers to substitute alternative advertising in the local signals they retransmit is "wholly inconsistent with the basic concept of a compulsory license given to passive retransmitters of local broadcast signals." LIN, reply comment 1, at 2. LIN notes that, in the context of cable, the Hubbard decision wrongly undercut that basic concept by allowing a satellite carrier to retain its passive carrier exemption when retransmitting an altered signal so long as it is the broadcaster who made the alteration. However, LIN contends that commercial substitution is far more inappropriate in the context of the more limited satellite compulsory license, where it provides a powerful additional incentive for carriers to maximize the number of subscribers and to ignore the law in doing so. Id. at 3.

C. COPYRIGHT OFFICE RECOMMENDATIONS

The Copyright Office believes that in light of the other amendments to the Copyright Act that it is recommending Congress should make some corresponding adjustments to the passive carrier exemption.

1. Open Video System Issues.

If Congress amends the Copyright Act to clarify that open video systems are eligible for the cable compulsory license, then the passive carrier exemption should be amended to indicate that open video systems qualify for the section 111(a)(3) exemption only in very limited circumstances. While it is easy enough to see the logic in USTA's argument that an open video system operator acts in a traditional common carrier capacity when it merely provides the platform for the retransmission of an unaffiliated programmer's broadcast signals, and should therefore be eligible for the passive carrier exemption, the Copyright Office queries when, if ever, an open video system operator will act only in such a capacity. Given the must-carry requirements imposed upon open video system operators by the FCC, NAB posited that open video systems will always be more than just passive carriers, because they will always be called upon to retransmit must-carry signals. The Copyright Office agrees that it seems unlikely that an open video system operator will ever function in a way that is divorced from its must-carry obligations. A traditional cable system certainly cannot do so short of retransmission consent, and open video systems are intended to operate in much the same way as cable systems.

USTA argues that open video system operators should still be considered passive carriers exempt from copyright liability when they retransmit must-carry signals to the subscribers of their unaffiliated programmers. Such a treatment would not comport with the treatment the Copyright Office affords cable systems.

It is the Copyright Office's view, as explained in detail in Chapter X of this study, that any time a cable system retransmits the signal of a broadcast station (even a must-carry station), the system publicly

performs the copyrighted works embodied on the signal and must secure a compulsory license to avoid copyright liability. However, the Office believes that it may be appropriate for Congress to grant an exemption from liability for a cable system's retransmission of local signals under the cable compulsory license because of Congress' historic view that the retransmission of a local signal does not harm the copyright owners. If Congress granted such an exemption, even though a cable system must secure a compulsory license to be free from copyright liability for its retransmission activities, its retransmission of local signals would not garner a significant copyright royalty payment.

In applying this in the open video system context, an open video system operator who retransmits must-carry signals to the subscribers of an unaffiliated programmer would be publicly performing the copyrighted works embodied on the signals and should secure a compulsory license to avoid liability; however, the carriage of must-carry signals would be considered to be the carriage of local signals and, as such, would accrue a *de minimis* royalty obligation for the open video system operator or its unaffiliated programmer. The operator would not need the benefit of the passive carrier exemption to be exempt from a royalty obligation.

In the event that NAB is wrong, however, and an open video system operator might merely carry signals for an unaffiliated programmer when no stations invoke their must-carry privilege, it would be prudent to provide the passive carrier exemption for the operator. In this instance, the open video system operator acts as a truly passive carrier. In such limited circumstances, the Copyright Office takes the position that providing ancillary services such as marketing, billing and collecting would not be activities that would disqualify an operator from claiming the exemption. However, to be consistent with its position regarding satellite carriers, the Copyright Office takes the position that if an open video system operator for some reason had the need to scramble or otherwise encode its signals and provide decoders to subscribers, it would not qualify for the passive carrier exemption.

2. Satellite Carrier Issues.

The Copyright Office does not agree with Baseball that satellite carriers who retransmit broadcast signals to cable systems should be required to pay an additional copyright royalty. So long as the satellite carriers do not engage in unpermitted selection of signals and subscribers, or alter the signals being retransmitted, they should qualify for the passive carrier exemption.

However, the Copyright Office agrees with LIN Broadcasting that Congress may wish to reconsider the method of commercial substitution upheld by the Eighth Circuit in the Hubbard case. Congress crafted sections 111 and 119 to provide cable systems and satellite carriers a compulsory license to retransmit the broadcast signals "as is," and the spirit of those sections is that the signals were not to be altered in anyway. However, since it is the broadcaster who is making the alterations, not the satellite carrier, the questions of who benefits, who is harmed, and whether this is a situation that needs to be remedied are not as clear as when the satellite carrier makes the alterations. These issues were not fully briefed before the Office during the comment period or at the public meetings, and therefore, no conclusion was reached by the Office except that this issue is deserving of further study.

VIII. SHOULD THE CABLE COMPULSORY LICENSE BE EXTENDED TO THE INTERNET?

When the Copyright Office began to consider the eligibility of open video systems for the cable compulsory license, several parties cautioned that once the telephone companies were in the business of retransmitting broadcast signals under the cable compulsory license, someone would want to use the license to put broadcast signals on the Internet. Two commenters in the Office's open video system inquiry, ABC and Joint Sports, urged the Copyright Office, in the event that it decided to recognize open video systems as cable systems, to clarify that customers of a telephone company do not qualify as a "cable system" under section 111 when retransmitting broadcast programming through a computer network. *See* ABC, comment 2, in Docket No. 96-2, at 9-10; Joint Sports, comment 5, in Docket No. 96-2, at 11-12. ABC stressed that allowing retransmissions of broadcast signals over the Internet to qualify for the cable compulsory license would have a devastating effect on the commercial viability of broadcast television. Id.

A. SUMMARY OF THE COMMENTS AND TESTIMONY

When the Copyright Office requested information for this global review of the cable and satellite compulsory licenses, the Office asked the public whether it would be appropriate to include broadcast retransmissions via the Internet in a cable compulsory licensing scheme. Audio Net¹⁰³ is the primary proponent of the eligibility of computer networks for the cable compulsory license."¹⁰⁴

Currently, AudioNet broadcasts audio and some video events in real time via the Internet to anyone anywhere in the world who has a computer with audio capability and access to the World Wide Web. The

¹⁰³ Audio Net, Inc., broadcasts audio and video events in real time and is the largest broadcast network in the Internet. Comment 18, at 1-2, [hereinafter AudioNet, comment 18 or reply comment 29].

¹⁰⁴ Of all the other commenters in this factfinding study, PBS is the only one that supports the extension of the benefit of compulsory licensing to the Internet. PBS argues that Internet retransmitters should be eligible for a compulsory license, and a new compulsory license should be created to fill the special needs of Internet retransmitters; however, PBS would require the Internet compulsory licensees to carry public broadcast stations at their request. PBS, comment 28, at 39-42.

types of audio events broadcast are as follows: network feeds of major league sporting events (e.g., Super Bowl, World Series, NBA Playoffs, Stanley Cup playoffs, etc.); audio of cable television programming (e.g., simulcasting audio of C-SPAN I and II, including Senate and House proceedings); local radio stations carrying talk radio programming, sports events, and music; conferences (e.g., press conferences, governmental hearings, shareholder meetings, etc.); live concert events; Internet radio stations (including original music programming); and the AudioNet Jukebox (more than 1,000 compact disc recordings from more than 30 recording companies). It would appear from AudioNet's written comments that the rights to retransmit most of the listed programming are purchased in the free market; however, the radio stations apparently "sign up" to be retransmitted on AudioNet.¹⁰⁵

Internet broadcasts have been made possible by the development of software known as streaming audio technology. This technology vastly improved the Internet audio experience by permitting the sending of audio files in virtually real time. AudioNet describes the technology as follows:

The software establishes a "buffer" of memory in the user's computer random access memory to which the Internet site downloads a few seconds of audio. As the audio is played from the buffer, the Internet site replaces the played material with the next few seconds of audio. The buffer continually is refreshed in this manner, resulting in a continuous real time playback of audio to the user -- although only a few seconds of audio actually resides on the user's computer at any given time.

AudioNet, comment 18, at 3.

Recently, AudioNet has begun expanding its broadcasts into video programming. Although the technology now permits display on only a small portion of a computer's video screen in less than full motion video, AudioNet estimates that probably within two to three years, the personal computer will be capable of displaying full screen real time television broadcasts with quality exceeding the current television

¹⁰⁵Transcript, *Copyright Office Hearing*, 643 (May 8, 1997) (testimony of Mark Cuban, President, AudioNet, Inc.) [hereinafter AudioNet, tr.]. AudioNet, tr., at 662.

standards and fast approaching advanced digital television standards. AudioNet is thus poised to partake, in the not too distant future, in the market for distribution of television programming via the Internet.

AudioNet asserts that compulsory licensing is necessary to enable access to programming for Internet distribution. Like small cable systems and open video system operators, AudioNet is concerned about the logistical and economic difficulties in negotiating for and obtaining licenses from copyright proprietors. It also fears that, as small, young companies using new technology, Internet broadcasters will face a competitive disadvantage in dealing with the broadcasting industry and large content providers, who might intentionally withhold rights to their programming to preclude the newcomers' entry into the retransmission market. Id. at 6. Finally, AudioNet argues that the establishment of a compulsory licensing scheme for Internet broadcasters should lead to the development of practical means of such licensing, such as a collective administration system (akin to ASCAP and BMI) or a clearinghouse (such as the Copyright Clearance Center). Id. at 7.

AudioNet believes that the Internet should warrant a compulsory license of its own rather than be folded into the cable or satellite licenses, because Internet broadcasting generates income from advertising rather than from subscription fees. It suggests that royalties for Internet compulsory licenses should be either a low flat fee or a small percentage of advertising revenue, and the rate should reflect the "experimental nature" of Internet video broadcasting.¹⁰⁶ Id. at 7, 8.

When questioned at the public meeting regarding the anomaly of a worldwide distribution service attempting to qualify for a compulsory license designed to benefit local retransmission services, AudioNet indicated that, in fact, Internet retransmission of broadcast signals can be controlled to "be a local broadcast medium if the need to distribute in that manner is required." AudioNet, tr., at 687. This would be possible by first pinpointing the location of any particular user of the service through a process known as "geographic

¹⁰⁶ However, in the public meeting held by the Copyright Office on May 8, 1997, Mark Cuban of AudioNet stated that he preferred "to fit [Internet retransmitters] into the existing" section 111 compulsory license, and that he believed that they already do fit under the cable license. AudioNet, tr., at 662.

identification." AudioNet, reply comment 29, at 6-7. With this information, the Internet retransmitter could control the extent to which a broadcast signal is retransmitted by using various encryption or other technology. AudioNet, tr., at 687.

Although it might be possible for AudioNet to operate like a cable system and enforce to some extent must-carry or other requirements or limitations on free carriage of signals, AudioNet takes the position that Internet broadcasters should be exempt from the must-carry rules. AudioNet, comment 18, at 8. Rather, AudioNet claims to promote "localism" by the very act of distributing many local signals to a nationwide or worldwide audience.¹⁰⁷

Regarding the must-carry responsibilities¹⁰⁸ that must be shouldered by traditional cable systems and that are factored into the compulsory licensing equation as discussed in chapter I of this study, AudioNet states that it "would likely be physically and economically impossible for any Internet broadcaster to carry all local channels in every market in which Internet access was available." AudioNet, reply comment 29, at 7. AudioNet is adamant that any statute or regulation that requires implementation of technology such as geographic identification so as to restrict delivery of programming "unnecessarily restrains consumer access to information that otherwise may freely be available to the public, and ultimately thwarts the fundamental opportunity of the Internet as a global communications medium." Id.

Copyright owners, broadcasters, and cable interests alike strongly oppose AudioNet's arguments for the Internet retransmitters' eligibility for any compulsory license. These commenters uniformly decry that the instantaneous worldwide dissemination of broadcast signals via the Internet poses major issues regarding

¹⁰⁷ AudioNet mistakenly assumes that under a compulsory license "local broadcasters will receive a license fee anytime an Internet provider broadcasts a local program," and also argues that local broadcasters will be able to charge more for advertising. It contends that "Every broadcaster has the same opportunity and broad reach (on the Internet) . . . no one station has a distinct advantage over another." Audio Net, reply comment 29, at 4.

¹⁰⁸ Syndicated exclusivity, sports exclusivity, network nonduplication, and PEG requirements are not discussed by AudioNet.

the United States and international licensing of the signals, and that it would be premature for Congress to legislate a copyright compulsory license to benefit Internet retransmitters at this time.

The copyright owners point out that many producers of original programming are beginning to transmit their works over the Internet, and giving Internet retransmission services the advantages of compulsory licensing would put those originators at a competitive disadvantage and possibly thwart the development of free market licensing incentives such as blanket licensing. RIAA, comment 24, at 14; RIAA, reply comment 21, at 8; ASCAP, comment 6, at 20; NPR, comment 36, at 13; Canadian Claimants, comment 32, at 7; BMI, comment 27, at 14.

In response to AudioNet's proposal of a low, flat royalty fee (or, in fact, any compulsory licensing fee), several copyright proprietors retort that copyright owners should not subsidize the costs of a fledgling Internet retransmission service's entry into the communications field, especially before the free market has had an opportunity to operate. Canadian Claimants, comment 32, at 7; RIAA, reply comment 21, at 8; ASCAP, reply comment 11, at 12. The Canadian Claimants argue that the revenues paid by Internet retransmitters under a compulsory license would likely not be high enough to result in any worthwhile additional royalties for copyright owners. Canadian Claimants, comment 32, at 7. They argue that Internet technology allows almost anyone to retransmit copyrighted material, and a compulsory license for Internet retransmitters would cause serious losses to copyright owners. But AudioNet explains that streaming multimedia technology is extremely costly in the same way that it is very costly to retransmit broadcast signals via satellite, and most likely there would not be a great number of licensees utilizing a compulsory license for Internet retransmissions. AudioNet, tr., at 656, 663.

The sports interests are particularly concerned that a compulsory license in favor of Internet retransmissions would displace the sponsoring institutions of telecast sporting events from exploiting international markets for those time-sensitive telecasts. They argue that, to date, cable and satellite compulsory licensing mechanisms have shown themselves incapable of addressing and compensating damage

to the copyright owners for violations of their exclusivity agreements internationally, and that considering the Internet's instantaneous worldwide reach coupled with an Internet user's ability to store, edit and retransmit information, a compulsory license for Internet retransmissions would be bound to create havoc with the licensing mechanisms working in the free market. NCAA, comment 26, at 2; NBA/NHL, comment 22, at 3; Baseball, comment 17, at 8.

The broadcast and cable interests declare that the Internet retransmitters should not qualify for compulsory licensing because they are unregulated in the communications context and they are not a localized retransmission service. They state first that Internet retransmissions would function very differently from the other multichannel video providers that already qualify for a cable compulsory license. ALTV, comment 30, at 4; ABC, comment 20, at 4; Time-Warner, comment 23, at 7; NAB, comment 39, at 8; NBC, reply comment 24, at 2. They argue that Internet retransmitters are not subject to FCC regulations such as must-carry, syndicated and sports exclusivity, network nonduplication, and PEG requirements, and with no such protection to local broadcasters and copyright owners, the compulsory licensing of their services would severely compromise local broadcasters' ability to control the distribution of their signals, would harm syndicated programming and local broadcasting businesses, and would jeopardize the network/affiliate system. Cox, reply comment 17, at 9; ABC, comment 20, at 3-4; NAB, comment 39, at 8; NAB, reply comment 30, at 8; NPR reply comment 14, at 8.

NPR notes that there is no evidence that the communications policy goal of ensuring the availability of broadcast signals to consumers is served by allowing a compulsory license for Internet retransmissions. Rather, there already exists sufficient availability of retransmission service, and an Internet compulsory license would likely undermine, rather than enhance the production and broadcast distribution of locally-oriented programming. NPR argues that the simultaneous Internet retransmission of local broadcast signals to national and international audiences would somehow stifle the production of local programming. *Id.* at 13-14. Thus, NPR concludes that compulsory licensing should not be allowed for Internet retransmissions.

Several commenters also express concern that Internet retransmissions are by nature so widespread, and at this point in time so subject to unauthorized copying, that this factor alone should render them ineligible for compulsory licensing. These commenters express doubt that any current encryption technology would be sufficient to protect Internet retransmissions from unauthorized copying, and contend that compulsory licensing should not be contemplated in the Internet arena until such time as security is a given. MPAA, comment 35, at 13; NAB, reply comment 30, at 8.

Finally, RIAA and Cox note that federal and international policymakers are only beginning to address the telecommunications and copyright policy issues posed by the burgeoning Internet industry, and it would be inappropriate and premature for Congress to adopt a compulsory licensing regime to benefit Internet retransmission of broadcast signals before such time as the policy debate has been fully aired at all governmental and intergovernmental levels. RIAA, comment 24, at 12; Cox, reply comment 17, at 10.

B. COPYRIGHT OFFICE RECOMMENDATIONS

The Copyright Office agrees with the majority of parties expressing views before us on the issue of Internet retransmissions. The Office concurs with the many arguments outlined above regarding the inappropriateness of bestowing the benefits of compulsory licensing on an industry so vastly different from the other retransmission industries now eligible for compulsory licensing under the Copyright Act. Even satellite technology, which allows the retransmission of broadcast signals to a far wider audience geographically than does traditional cable technology, and which remains less regulated than cable at the federal level, allows for the restriction of retransmissions within the United States unless copyright owners consent to international retransmissions. Internet retransmitters, while perhaps technologically capable of restricting their transmissions to a defined area, clearly intend to utilize to the utmost the Internet's ability to disseminate programming "instantaneously worldwide."

Even beyond the many solid arguments made by the copyright owners and other commenters summarized above, the Copyright Office believes it is premature to consider the implications for the

retransmission of broadcast signals via the Internet before it has fully considered the many other copyright issues involved in all aspects of Internet operations. For example, the Copyright Office questions AudioNet's position that retransmitting broadcast signals over the Internet does not actually involve copying in addition to publicly performing the copyrighted works retransmitted. AudioNet, tr., at 656-658. If each user of AudioNet's services actually copies or has the potential to copy retransmitted programming on his or her home computer, the copyright implications go far beyond compulsory licensing.

Furthermore, the Copyright Office notes, as did several other commenters, that at the present time, President Clinton's Information Infrastructure Task Force's Working Group on Intellectual Property Rights takes a decidedly free market view on the issue of licensing copyrighted works used on the Internet. In its "White Paper" the Working Group on Intellectual Property Rights states: "[t]he marketplace should be allowed to develop whatever legal licensing systems may be appropriate for the [National Information Infrastructure]."¹⁰⁹ The Working Group concludes that given the nascent state of the National Information Infrastructure, it is premature to suggest that a comprehensive licensing system could best be devised from a "central planning perspective." NII White Paper, at 199.

The Federal Communications Commission seems to take a similarly wait-and-see, anti-regulatory perspective toward the Internet. In March of this year, the FCC's Office of Plans and Policy issued a working paper entitled *Digital Tornado: The Internet and Telecommunications Policy*. In that paper, the FCC concludes that the government should avoid unnecessary interference with the Internet's development. The FCC notes that the technological shifts associated with the Internet dovetail with the communications industry's transition from regulated monopolies to a world of overlapping competitive firms, and that the greatest contribution that government can make to the development of the Internet is successfully opening

¹⁰⁹ Information Infrastructure Task Force, Intellectual Property and the National Information Infrastructure: The Report of the Working Group on Intellectual Property Rights 53 (Sept. 1995) (hereinafter "NII White Paper").

the communications sector to competition.¹¹⁰ At a time when the Internet as an industry seeks to be free from government regulation in order to permit the free market to maximize its potential development, it would seem unfair to the providers of the content that will ultimately be disseminated via the Internet not to afford them the same opportunities to maximize their potential over the powerful Internet medium.

For these reasons, the Copyright Office recommends that Congress decline to create a compulsory license for the retransmission of broadcast signals on the Internet.

¹¹⁰ FCC Office of Plans and Policy, OPP Working Paper No. 29: Digital Tornado: The Internet and Telecommunications Policy (March 1997).

IX. UNSERVED HOUSEHOLD RESTRICTION: DISCUSSION AND ANALYSIS

A. WHAT IS IT?

Section 119(a)(2)(B) of the Copyright Act provides that the compulsory license granted under section 119 for the retransmission of television network signals is limited to "persons who reside in unserved households." This provision of section 119 is the network territorial limitation of the compulsory license, also known as the "white area" restriction.¹¹¹ What it means is that satellite carriers may not make use of the section 119 license to retransmit a network signal to a subscriber who already receives the signal from another source.¹¹² The restriction is therefore a communications provision, modeled after a regulation of the Federal Communications Commission applicable to the cable industry (the network nonduplication rule), even though it appears in the Copyright Act.

The means of determining when a particular subscriber resides in an unserved household, and is therefore eligible for receipt of a network signal under the satellite license, is found in the definition of an "unserved household" in section 119(d)(10). That provision provides:

The term "unserved household," with respect to a particular television network, means a household that --

(A) cannot receive through the use of a conventional outdoor rooftop receiving antenna, an over-the-air signal of Grade B intensity (as defined by the Federal Communications Commission) of a primary network station affiliated with that network, and

(B) has not, within 90 days before the date on which that household subscribes, either initially or on renewal, to receive secondary

¹¹¹ The term "white area" refers to an area unserved by television signals. Originally, the term meant a geographic area that was not capable of over-the-air reception of any broadcast signals, but the term now means in the context of the satellite license a household which is not capable of receiving an over-the-air signal of a local network affiliate and has not received a network signal from the local cable operator within the previous 90 days. The satellite license for network signals is therefore limited to subscribers who reside in unserved households.

¹¹² However, there is no such restriction concerning the retransmission of superstations.

transmissions by a satellite carrier of a network station affiliated with that network, subscribed to a cable system that provides the signal of a primary network station affiliated with that network.

If the subscriber resides in an unserved household with respect to a particular network, then a satellite carrier may make use of the satellite license to retransmit a network signal to the subscriber. If the subscriber does not reside in an unserved household, then the carrier cannot make use of the license. It is important to note, however, that the copyright law does not prohibit a satellite carrier from providing network service to a subscriber who does not reside in an unserved household. Rather, the satellite carrier simply cannot make use of the compulsory license in this circumstance, and must negotiate privately with the copyright owners of the programming appearing on the network signals being retransmitted. The Copyright Office is not aware, however, of any satellite carriers or copyright owners that have attempted to negotiate such rights.¹¹³

B. HISTORY OF THE RESTRICTION

The genesis of the unserved household restriction was the 1988 Satellite Home Viewer Act. At the time, the satellite industry was in the nascent stage of development, with home satellite dishes still a relative novelty, and digital satellite service (DBS) still years away. As a new industry, satellite carriers were relatively free of regulation. Restrictions and limitations applicable to the cable industry, particularly those addressing the exclusivity of broadcast programming, did not and do not apply to satellite carriers retransmitting broadcast programming. Given this lack of regulatory obligation in the communications context, it was determined that creation of a compulsory license for the satellite industry must be conditioned

¹¹³ The comments submitted by the satellite carriers state that private licensing of broadcast programming as a general matter, is not possible. *See e.g.* SCBA, comment 9, at 3. Copyright owners, however, favor such an approach. *See e.g.* MPAA, comment 35, reply comment 3. None of the commenters offered any discussion of whether private licensing of network signals would be possible for subscribers who were served with network signals from another source. Given the contentious nature of the unserved household issue in the context of the current statutory provisions, it is reasonable to infer that copyright owners would not allow private licensing of network programming to served households.

upon certain communication regulatory concerns. The principal manifestation of these concerns was the unserved household restriction.

The restriction was designed as a surrogate for the network nonduplication rules of the FCC applicable to the cable industry. These rules, found at 47 C.F.R. §§ 76.92-76.97, prevent a cable operator from importing a distant network signal to compete with a local broadcast station carrying that same network. The purpose of these rules is to allow affiliate broadcasters to negotiate network programming exclusivity rights with their respective networks so that the network affiliate stations are the only ones authorized to broadcast network programming in their areas. The area in which a local network affiliate is entitled to nonduplication protection is defined in its programming contract with its network, but in no case can the protection exceed an area more than 35 miles from the broadcast station.¹¹⁴

No similar rule existed for the satellite industry at the time of passage of the Satellite Home Viewer Act in 1988, nor does such a rule exist now. When Congress first considered creating the satellite license, network broadcasters expressed concern that local affiliates would lose viewers to distant network stations imported by satellite carriers because of the lack of nonduplication protection. Unlike cable systems, which carry the signals of the local affiliates (and are now required to do so by the must-carry rules recently upheld by the Supreme Court), satellite carriers do not provide local signals. Thus, for example, a person residing in Washington, D.C. who subscribed to satellite service would not receive the Washington, D.C. NBC affiliate, but would most likely receive the New York City NBC affiliate. The Washington, D.C. affiliate would therefore lose as viewers those subscribing to a satellite service, thereby affecting the viewing ratings of the station and, ultimately, reducing its advertising revenues. Broadcasters insisted that if Congress were to enact a copyright compulsory license for satellite carriers, a restriction must be built into the license to

¹¹⁴ If the station is located in a smaller television market, an additional 20 miles of protection is added, for a total of 55 miles.

afford them nonduplication protection and prevent their loss of viewership to distant network stations. The result was the creation of the section 119(a)(2)(B) unserved household restriction.

The legislative history to the 1988 Satellite Home Viewer Act is replete with Congressional endorsements of the network-affiliate relationship and the need for nonduplication protection. The House Commerce Committee Report states:

Under the bill, satellite carriers are provided a limited interim compulsory license for the sole purpose of facilitating the transmission of each network's programming to "white areas" which are unserved by that network. The Committee believes that this approach will satisfy the public interest in making available network programming in these (typically rural) areas, while also respecting the public interest in protecting the network-affiliate distribution system.

This television network-affiliate distribution system involves a unique combination of national and local elements, which has evolved over a period of decades. The network provides the advantages of program acquisition or production and the sale of advertising on a national scale, as well as the special advantages flowing from the fact that its service covers a wide range of programs throughout the broadcast day, which can be scheduled so as to maximize the attractiveness of the overall product. But while the network is typically the largest single supplier of nationally produced programming for its affiliates, the affiliate also decides which network programs are locally broadcast; produces local news and other programs of special interest to its local audience, and creates an overall program schedule containing network, local and syndicated programming.

The Committee believes that historically and currently the network-affiliate partnership serves the broad public interest. It combines the efficiencies of national production, distribution and selling with a significant decentralization of control over the ultimate service to the public. It also provides a highly effective means whereby the special strengths of national and local program service support each other. This method of reconciling the values served by both centralization and decentralization in television broadcast service has served the country well.

The networks and their affiliates contend that the exclusivity provided an affiliate as the outlet for its network in its own market is an essential element of the overall system. They assert that by enhancing the economic value of the network service to the affiliate, exclusivity increased the affiliate's resources and incentive to support and promote the network in its competition with the other broadcast networks and the other nationally distributed broadcast and nonbroadcast program services.

The Committee intends by this provision to satisfy both aspects of the public interest -- bringing network programming to unserved areas while preserving the exclusivity that is an integral part of today's network-affiliate relationship.¹¹⁵

The sentiments expressed by the 100th Congress extended to the 103d Congress when it passed an extension of the satellite carrier compulsory license in 1994. Not only did the 103d Congress endorse the principle of network nonduplication protection embodied in the license, it strengthened the enforcement provisions. Prior to 1994, a network affiliate (or copyright owner) aggrieved by a satellite carrier's violation of the unserved household restriction had only the copyright infringement suit as a means of redress. Statutory damages were limited (\$5 per subscriber per month in the case of individual violations, and \$250,000 per accounting period for a pattern of violations), and no suits were brought in the initial term of the license. While these limitations remained in place, the 103d Congress clearly delineated that, in an infringement suit, the burden of proof rested with the satellite carrier to demonstrate that it had not violated the unserved household restriction. 17 U.S.C. § 119(a)(5)(D). Further, Congress created a transitional enforcement regime, lasting from 1994-1996, which allowed each network affiliate to issue written challenges against subscribers receiving network service which it believed did not reside in unserved households.

For subscribers residing within the predicted Grade B contour of a network affiliate, upon receipt of a challenge, the satellite carrier servicing that subscriber had two options: 1) turn off immediately the service of that network signal to the subscriber; or 2) conduct a signal intensity measurement at the household of the subscriber to determine if he or she was receiving a signal of Grade B intensity at his or her rooftop antenna. If the satellite carrier conducted the signal intensity measurement and it revealed that the subscriber did not receive a signal of Grade B intensity from the challenging affiliate, then service could continue and the affiliate was required to pay the cost of the measurement. If the measurement revealed that

¹¹⁵ H.R. Rep. No. 887 (Part 2), 100th Cong., 2d Sess. 19-20 (1988). *See also* H.R. Rep. No. 887 (Part 1), 100th Cong., 2d Sess. 18-19 (1988).

the subscriber did receive a signal of Grade B intensity, then the satellite carrier was required to immediately turn off service of that network to the subscriber and absorb the cost of the measurement (i.e. "loser pays").

Affiliates were limited in the number of subscribers that they could require a satellite carrier to conduct a measurement for, not to exceed 5 percent of the subscribers within the affiliate's local market within a calendar year. For those subscribers challenged in excess of 5 percent, the responsibility to conduct the signal intensity measurement fell to the challenging affiliate. Satellite carriers were given 60 days to turn off service when the measurement determined that the subscriber received a Grade B intensity signal, and 30 days after termination to notify the affiliate that such action had been taken. At the same time, the satellite carrier was required to reimburse the affiliate for the cost of the measurement.

For subscribers who resided outside the predicted Grade B contour of the affiliate station, the responsibility of conducting signal intensity measurements fell upon the affiliate, with the same "loser pays" regime applicable to the results. If an affiliate made a reasonable attempt to conduct a survey at the household of a subscriber and was denied access for the purpose of making the measurement, then the satellite carrier was required to terminate service within 60 days of denial of access.¹¹⁶

As noted above, the transitional signal intensity measurement provisions expired on December 31, 1996. Broadcasters currently aggrieved of violations of the unserved household restriction must once again resort to the traditional enforcement action of the Copyright Act -- the infringement suit. To date, broadcasters have brought lawsuits in Texas and Florida for violations of the unserved household restriction, and the defendant in both those cases, PrimeTime 24, has counterclaimed for antitrust violations in New York federal district court.¹¹⁷

¹¹⁶ In addition to adopting the transitional signal intensity measurement, Congress broadened the definition of a network signal covered by the unserved household restriction. *See* 17 U.S.C. § 111(d)(2). Broadcast stations affiliated with Fox, Paramount and Warner Brothers are now considered network signals under section 119, whereas they are not under the cable compulsory license.

¹¹⁷ Carman Communications, Inc. v. PrimeTime 24 Joint Venture, CIV. No. 2-96-CV-086, (N.D. Tex., Amarillo (continued...))

C. THE ISSUES PRESENTED BY THE UNSERVED HOUSEHOLD RESTRICTION

Operation of the unserved household restriction, particularly the transitional signal intensity measurement provisions, has been problematic. Satellite carriers claim that they cannot determine when particular households are, or are not, eligible for network service, and that the current standard of measurement -- Grade B -- is flawed and unworkable. Broadcasters claim that the current standard is fine and superior to any other methods, and that the problem lies with the satellite carriers' (particularly PrimeTime 24) repeated intentional violations of the restriction. Satellite subscribers faced with termination of their network service have raised their concerns with Congress, the Copyright Office, and the FCC; expressing anger and confusion with a law they believe denies them the right to obtain any programming they are willing to pay for. The controversy engendered by the restriction is one of the principal factors motivating this study by the Office.

1. Eligibility for Satellite Network Service.

a. *Complaints of the satellite carriers.* As noted earlier in this study, satellite carriers assert that extension of the satellite license is critical to the continued success of their industry as a competitor of the wired cable industry. To foster further success, the satellite carriers uniformly state in their testimony before the Office that clarification of the unserved household restriction is required so that consumers may be adequately served while, at the same time, satellite carriers will be able to determine their responsibilities and liabilities under the Copyright Act in a cost efficient manner.¹¹⁸

(...continued)

Division); CBS, Inc. v. PrimeTime 24 Joint Venture, CIV-Nesbitt No. 96-3650, (S.D. Fla., Miami Division); PrimeTime 24 Joint Venture v. NBC, Inc., 97 CIV-3951, (S.D.N.Y., filed May 30, 1997).

¹¹⁸ One satellite carrier, Primestar Partners, L.P., states that it is too early for the Copyright Office to propose changes, if any, to the unserved household restriction because certain satellite carriers and broadcasters are attempting to negotiate their differences. Instead, Primestar advocates that Congress should consider adopting any solutions which the parties may privately negotiate. Primestar, comment 19, at 2-3.

Suggestions as to the reform of the unserved household restriction range from its abolition,¹¹⁹ to replacement of the Grade B standard with a picture quality standard for determining subscriber eligibility,¹²⁰ to payment of a surcharge collected from subscribers to network affiliates to compensate for loss of viewership.¹²¹

PrimeTime 24 is the principal advocate of replacing the Grade B signal intensity standard with a test of picture quality. Under the PrimeTime 24 proposal, a first-cut approach would categorize subscribers geographically to determine eligibility. Known as the "red zone/green zone" approach, certain geographic areas would be targeted as automatically eligible for satellite service ("green zone"), while subscribers in the remaining geographic areas ("red zones") would be eligible for network service pending the outcome of a new testing regime. The Grade B signal intensity standard of section 119(d)(10) would be replaced by a picture quality standard, whereby a subscriber would be eligible for service of a particular network if he or she did not receive an adequate over-the-air picture from the local affiliate. The subscriber would also be required to sign an affidavit that he or she did not receive an adequate over-the-air picture, and that such poor picture is not the product of inadequate or faulty receiving equipment. The affidavit would be turned over to the respective affiliate located near the subscriber (i.e. the one that caused the subscriber to be geographically determined to be in a "red zone"), and the affiliate would have the opportunity to challenge the subscriber's receipt of satellite network service. Once a challenge is issued, an objective third party observer, approved by both the satellite carrier and challenging affiliate, would enter the subscriber's home and view his or her over-the-air picture quality of the local affiliate. The third party observer would be supplied with graded images of standard picture quality, ranging from excellent to unacceptable, agreed to by both satellite carriers and affiliates. If the observer determined the over-the-air picture to be inadequate,

¹¹⁹ See DIRECTV, reply comment 26, at 6; Hamilton County Telephone Co-op, reply comment 8, at 1,

¹²⁰ PrimeTime 24, reply comment 15, at 1.

¹²¹ National Rural Telecommunications Commission, comment 34, at 9-10.

the subscriber could receive satellite service of that network, and the challenging affiliate would pay the cost of the test. If the observer determined the picture quality to be adequate, the subscriber would be denied service and the satellite carrier would bear the cost of the test. The observer's determination would be final, and not subject to appeal.

PrimeTime 24 argues that the Grade B signal intensity test must be replaced with a picture quality test because an over-the-air broadcast signal of Grade B intensity does not guarantee receipt of a quality picture. It submits that key provisions of the current definition of an unserved household -- such as "conventional rooftop antenna" and "signal of Grade B intensity" -- are not defined by the FCC. It further notes that the FCC's rules governing the Grade B contour and its determination were fashioned by the FCC more than 40 years ago as predictors of television service, not of the respective quality of the television picture. *See* PrimeTime 24, reply comment 24, at 9 (citing MIT study that showed no correlation between signal strength and picture quality). PrimeTime 24 submits that the ultimate inquiry for the consumer is the quality of his or her picture, not whether he or she is receiving a signal of any particular strength.

As an alternative to a prohibition on certain satellite subscribers receiving network service, several commenters propose that subscribers residing in the "red zone" be charged an additional amount for the privilege of receiving satellite network service. This surcharge would be collected into a fund and distributed to network affiliates in a manner similar to the division of compulsory license fees under section 119. DIRECTV, reply comment 26, at 6; Hamilton County Telephone Co-Op, reply comment 8, at 1. Finally, the satellite carriers submit that whether the unserved household definition is retained or reformed, all existing subscribers of network service should be grandfathered in their receipt of such service during any extension period of the 17 U.S.C. § 119 license.

b. Complaints of the broadcasters. Not surprisingly, broadcasters object to any modifications of the unserved household definition and call for stronger enforcement measures. They assert that the Grade B signal intensity standard is the only truly objective one, and that a picture quality standard

will prove impossible to administer and will result in serious erosion of over-the-air network viewership. Broadcasters also oppose any grandfathering of existing satellite customers, asserting that violations of the current statute should not be rewarded in any extension of the license.

Broadcasters' objections to any changes in the current unserved household restriction are principally championed by the National Association of Broadcasters ("NAB") and the Network Affiliated Station Alliance ("NASA"). NAB begins its challenge by stating that the legislative history demonstrates that section 119 was created to allow satellite carriers an opportunity to provide network service to rural areas of the country, not urban areas, and submit an affidavit of Michael Remington, former majority counsel to the House Subcommittee on Courts, Intellectual Property and the Administration of Justice, who was responsible for drafting the 1988 Satellite Home Viewer Act. NAB, reply comment 30, at Appendix A. NAB submits that section 119 was never created with the intent to allow satellite carriers to enter urban areas of the country, and that satellite carriers' efforts to amend the unserved household restriction are nothing more than an attempt to grab a greater market share of television viewers at the expense of local network broadcasters. Id. at 12.

NAB, NASA, and all other broadcaster commenters,¹²² uniformly attack statutory substitution of a picture quality standard for Grade B. NASA states that Grade B "is an objective tool or proxy developed by the FCC for measuring picture quality," and that in terms of objectivity of a test standard, "[n]othing is a close second" to the Grade B standard. NASA, reply comment 19, at 17, 40. Both NASA and NAB challenge satellite carriers' assertions that there is no relationship between a signal of Grade B intensity and picture quality, asserting that satellite carriers' MIT study demonstrating a lack of such relationship is biased and analytically flawed. Id. at 9-11; NAB, reply comment 30, at 15-16. During the hearings before the Copyright Office and in the comments, NAB and NASA presented evidence to demonstrate that there is a

¹²² See *eg.* NBC, comment 39 and reply comment 24; LIN TV, reply comment 1; *see also* Small Cable Business Administration, comment 8 and reply comment 33.

direct correlation between Grade B signal intensity and picture quality, and that PrimeTime 24 is serving numerous subscribers with network signals who are capable of receiving a good quality picture over-the-air from the local network affiliate.¹²³

Likewise, broadcasters uniformly criticize the picture quality standard put forth by satellite carrier interests as administratively unworkable. Specifically, they attack PrimeTime 24's proposal of a subscriber affidavit followed by a third party observer picture quality test. With respect to the affidavit, NAB asserts that such an affidavit is valueless because subscribers will naturally be biased in the consideration of the over-the-air picture quality, and are already predisposed to satellite service. Id. at 18. NASA questions what is meant by an affidavit, and what penalties would be adopted if the subscriber made false statements. NASA, reply comment 19, at 10-11.

With respect to picture quality, both NAB and NASA submit that, by definition, such a determination is completely subjective, and submit deposition testimony from PrimeTime 24's expert witnesses in the Miami and Amarillo cases confirming the subjectivity. Id. at 13-14. Because of the inherent subjectivity, they question how a third party observer, acting alone, can accurately assess the quality of a picture. Both NAB and NASA cite the International Telecommunications Union's 1995 publication, "Methodology for the Subjective Assessment of the Quality of Television Pictures," which calls for at least fifteen nonexpert observers, viewing the television screen in a controlled lighting environment, to make an accurate picture quality determination. NAB, reply comment 30, at 16-17; NASA, reply comment 19, at 19. Further, even assuming that satellite carriers and broadcasters could agree to some kind of observer test, NASA questions how a subjective picture quality test could be applied by a federal judge and/or jury in determining a copyright infringement suit for violation of the unserved household restriction. Id. at 20.

¹²³ Much, if not all, of this testimony was formulated by the broadcasters for their infringement suits against PrimeTime 24 in Amarillo, TX and Miami, FL.

NASA also criticizes the suggestion of several commenters that, instead of a ban on satellite service in unserved households, subscribers pay a surcharge for satellite network service which would be distributed among local broadcasters. NASA submits that such a proposal "is fundamentally at odds with the principle of a free market and with traditional protection afforded intellectual property." Id. at 23. NBC asserts that such a surcharge would not preserve audience share and would jeopardize the economic viability of local affiliate stations. NBC, reply comment 30, at 7.

Further, if there is an extension of section 119, all broadcasters oppose the grandfathering of existing subscribers who are receiving network service in violation of the current unserved household restriction provision. *See e.g.* NASA, reply comment 19, at 25; NAB, comment 39, at 42-43.

Although broadcasters oppose any changes to the current unserved household restriction, NASA proposes several amendments to enhance its operation and effectiveness. First, NASA recommends that any household passed by cable, whether or not it actually subscribes, be prevented from obtaining satellite network service. NASA submits that such a proposal favors receipt of the local affiliate from cable, and would allow removal of the 90 day waiting period after cable subscription currently present in section 119(d)(10). NASA, reply comment 19, at 31. Second, NASA proposes that all satellite carriers be required to place a disclosure statement in all sales, advertising, promotion, and customer information agreements identifying the provisions of the unserved household restriction and informing customers and potential customers that they might not be eligible for satellite service of network signals. Id. at 33. Third, NASA requests that the limitations on statutory damages in sections 119(a)(5)(A) and (B) be removed so that broadcasters and copyright owners are entitled to full copyright remedies for unserved household restriction violations. Id. at 34.

Fourth, NASA requests that all commercial substitutions performed by satellite carriers in their carriage of network signals be banned. Id. at 35. *See also* LIN TV, reply comment 1, at ii. Fifth, NASA requests that satellite carriers be prevented from providing service of network signals to any subscribers until

notice of such service has been given to the area affiliate and the affiliate has had a reasonable period of time (45 days) to evaluate the subscriber's location and his or her eligibility to receive network service. Id. at 35. Finally, NASA requests that in providing subscriber lists to the networks (which is currently required by section 119(a)(2)(C)), satellite carriers be required to sort their subscriber lists by market and send the list of new subscribers and disconnects to the appropriate local affiliate, with a copy to the network. NASA asserts that such a requirement will reduce the number of inappropriate challenges brought by local affiliates. Id. at 36.

c. The 90 day waiting period. In addition to the Grade B intensity standard, the unserved household definition prohibits a satellite carrier from providing network service to a subscriber that had received cable service, which included the local affiliates, within the previous 90 days. NAB supports retention of this aspect of the unserved household restriction and urges that the waiting period be expanded because Congress should favor local retransmission services, such as cable, over national retransmission services such as satellite. NAB, comment 39, at 40.

Satellite carriers oppose retention of the 90 day waiting period. SBCA argues that the provision is anti-consumer and serves no legitimate copyright function because "one multichannel video service is favored over another and thus [the provision] has inadvertently created a government-sponsored industrial policy." SBCA, reply comment 22, at 5. PrimeTime 24 opposes NASA's suggestion that satellite network service be prohibited to households passed by cable. PrimeTime 24, reply comment 15, at 20-21.

2. The Local Retransmission Issue.

A controversial issue that arose at the initiation of this study is the retransmission by satellite carriers of local network affiliates to subscribers who reside in the affiliates' local markets. Specifically, local retransmission was being aggressively advanced by American Sky Broadcasting (ASkyB), a venture of Rupert Murdoch's News Corporation Limited. Although interest in providing local retransmissions has

recently waned,¹²⁴ the issue is still open for consideration and the testimony of ASkyB and others remain in the record.

ASkyB's proposal, as presented in its written comments and oral testimony, was to launch a DBS service late in 1997 to, among other things, retransmit local broadcast signals to local audiences. The retransmission of local broadcast signals would make ASkyB very much like a local cable operator, in that its subscribers would not have to rely upon distant (particularly network) signals for broadcast programming. Local retransmission would be achieved through a combination of signal compression, so that more signals could be placed on each satellite transponder, and a process known as "spot beaming," whereby retransmission of particular signals would be confined to a narrow geographic area, as opposed to the whole country, thereby allowing multiple use of the same frequency.

In the summer of last year, representatives of ASkyB approached the Copyright Office requesting a declaratory ruling that local retransmission of network signals was permissible under the satellite license and, specifically, the unserved household restriction. After being informed by the Office that it did not issue declaratory rulings in matters of statutory interpretation, ASkyB revised its request to inquire as to whether the Office would accept a statement of account and royalty fees from a satellite carrier that identified retransmission of network signals within the stations' local markets. The Office replied that it would.¹²⁵ Although the Office's response has been variously represented as an affirmation of the Copyright Office that local retransmission of network signals is permissible under the current statute, the Office expressly

¹²⁴ Provision of local network retransmission was supposed to be made a part of a new DBS service known as "Sky," the result of a merger between ASkyB and another satellite carrier, EchoStar. ASkyB, comment 33, at 1, fn. 1. The merger of EchoStar and ASkyB did not, however, take place and ASkyB is currently slated to merge with PrimeStar Partners. There are no announced plans to begin immediate offerings of local network signals, as was the original ASkyB plan.

¹²⁵ See Letter from Marilyn Kretsinger, Acting General Counsel, to William S. Reyner, Jr. (August 15, 1996).

disavowed making such a determination and confined its opinion to articulating its practice for accepting satellite statements of account and royalty fees. Id. at 4-5.

ASkyB now requests that the definition of an unserved household be "reaffirmed and clarified" to ensure that the local retransmission of network signals does not run afoul of the unserved household restriction. ASkyB, comment 33, at 2. In addition, ASkyB requests that the unserved household definition be amended to define what constitutes a "local" retransmission. ASkyB asserts that a network station's local service area should be its Area of Dominant Influence (ADI) as defined by the FCC. Id. at 7. Under this approach, a satellite carrier would be able to retransmit the signal of the Washington, D.C. NBC affiliate within that station's ADI without violating the unserved household restriction. Thus, the Baltimore NBC affiliate could not object to subscribers in the Washington ADI who received an over-the-air signal of Grade B intensity of the Baltimore affiliate. Finally, ASkyB requests that the royalty rate paid by satellite carriers for local retransmission of both network and superstation signals be zero, the same rate applicable to local retransmissions by cable systems carrying local signals. Id. at 8.

Most of the parties presenting testimony in this proceeding favor the concept of local retransmission of broadcast signals; in fact, some welcome it. *See e.g.* NBC, reply comment 24, at 8. Those commenting on the issue, however, urge that satellite carriers retransmitting local signals be required to comply with FCC regulations applicable to local retransmissions by cable systems, particularly the must-carry rules. *See* NASA, reply comment 19, at 30.

3. The PBS Issue.

PBS adds an additional wrinkle to the unserved household restriction: namely an exemption from the restriction for its national satellite service. Rather than rely upon satellite carriage of individual PBS affiliates, PBS proposes creation of a direct feed to satellite carriers of PBS programming, i.e., a national PBS satellite service. PBS asserts that it needs the section 119 license to provide this service and, because it is defined as a network under the license, needs an exemption from the unserved household restriction. PBS, reply comment 28, at 1. Thus, under PBS's proposal, a subscriber residing in Arlington, Virginia, would be eligible for service of PBS from his or her satellite carrier, even though there is a PBS affiliate located in Arlington. PBS asserts that its national service will solve any potential unserved household restriction problems for public television and should be endorsed. Id. at 2.

DIRECTV supports a PBS national service, asserting that it "can and should be an important source of noncommercial educational and informational programming that DBS operators can use to meet their obligations to reserve channel capacity for such programming under section 335 of the Communications Act." DIRECTV, comment 14, at 9-10.

D. DISCUSSION AND ANALYSIS

The unserved household restriction has created considerable turmoil not only between satellite carriers and broadcasters, but between consumers and the federal government. The Copyright Office has received more Congressional inquiries on the eligibility of satellite subscribers for network service than any other matter in its history, and the FCC (as well as the Office) has been bombarded with literally thousands of calls and letters from irate subscribers who, for the most part, believe that federal law prevents them from obtaining network programming that they are willing to pay for and want to see. The question of what to do about the unserved household restriction is a difficult one which admits of no easy answer. Unfortunately, there was nothing close to a consensus among the parties presenting testimony to the Office, and the battle lines between satellite carriers and broadcasters are clear and longstanding. Nevertheless, the Office is

entering the fray in an attempt to resolve consumer confusion caused by the unserved household restriction and to recommend a more efficient and workable compulsory license.

1. Should the Unserved Household Restriction Remain in the Copyright Law?

If section 119 is extended, the threshold question is why retain this restriction at all. The restriction is a copyright substitute for a communications regulation (the network nonduplication rules) and, as such, is arguably better located in communications law. The fact that the unserved household restriction ended up in the copyright law is nothing more than happenstance. Because the FCC did not regulate the carriage of broadcast signals by satellite, network broadcasters could not receive the exclusivity protection they enjoyed in the cable setting and therefore lobbied Congress in 1988 to place such protection in the copyright law. If the section 119 license is extended, the Communications Act of 1934 could be amended to include network exclusivity (and, for that matter, syndicated exclusivity) protection for satellite retransmissions of broadcast signals, or the FCC could be directed to adopt nonduplication rules for the satellite industry. The FCC has considerable experience and expertise in creating and applying nonduplication rules to the cable industry and is capable of extending those rules to satellite. The FCC has applied its network nonduplication rules for a number of years, and the Copyright Office is not aware of any dissatisfaction in either the cable or broadcast industries with the scope of protection and application of these rules. Furthermore, the FCC has the continuing jurisdiction and regulatory mechanisms to make adjustments to its regulations on a case by case basis should any difficulties arise. The Copyright Office, on the other hand, lacks expertise in communications law, and does not enforce the copyright law or have authority to resolve the substantive rights of individual parties. Congress may, therefore, wish to remove the matter of network exclusivity protection from copyright law and place it in communications law where it more appropriately belongs.

Having said this, the Office does understand that there is a fundamental difference between network exclusivity protection in the cable arena and that of satellite, though such difference does not have a bearing upon its removal from copyright law. Cable television is a localized retransmission service, technologically

capable (and required by law) of delivering local broadcast stations to subscribers. Every network affiliate is therefore virtually guaranteed to be on the local cable operator's system. Importation of a distant network affiliate by a cable system would provide a subscriber with a supplement to his or her local affiliate service, not a substitute. The same is not the case with satellite service of network signals. Because satellite remains a nationwide retransmission service, it must select a limited number of network affiliates to provide all its customers across the country. Thus, in areas where a household is receiving its local network affiliate by other means (over-the-air or via cable), subscription to satellite acts as a substitute for local viewing.¹²⁶ Because the satellite industry currently does not provide subscribers with their local network signals, the Copyright Office believes that importation of distant network signals creates a greater potential for harm for broadcasters and copyright owners in the satellite context than it does in the cable context. This distinction explains why there has not been a significant and continuing controversy over the network nonduplication rules and exclusivity protection in cable, and why the tension between network broadcasters and satellite carriers over the unserved household restriction is so great.

2. Local Retransmission: The Best Solution.

In the Copyright Office's view, the best solution to the issue of subscriber eligibility for satellite service of network signals is a technological one. If satellite carriers were to provide subscribers who reside within the local market of a network affiliate the signal of that affiliate, the need for the unserved household restriction with respect to that affiliate would be eliminated. The subscriber would be served with the local network affiliate, and the satellite carrier would no longer be required to import a distant network affiliate in order to provide network service to the subscriber.¹²⁷ The Copyright Office, therefore, recommends that

¹²⁶ This presumes, of course, that subscription to satellite preempts viewing of local signals from other sources.

¹²⁷ If a satellite carrier is providing service of the local affiliate of a network to a subscriber, there remains the possibility that the carrier may still wish to import a distant affiliate of the same network as an additional service. This is precisely the situation that the FCC's network nonduplication rules were adopted to cover, and the rules could be applied to the satellite industry. The Office believes that this could best be accomplished by FCC regulation, as opposed
(continued...)

retransmission of any broadcast station, network or independent, within that station's local market be permissible under section 119.

To implement this recommendation, there are certain issues which require resolution. Any amendment must include a definition of a station's local market, both for commercial and noncommercial educational stations. NASA recommends that the predicted Grade B contour, adopted under the 1994 Satellite Home Viewer Act to define the area wherein a broadcaster could challenge a subscribers receipt of satellite network service, be used to determine the local markets. NASA, reply comment 19, at 30. NRTC favors adoption of a 35 mile zone to define the local market of a network station, while ASkyB favors use of "market determinations made by the FCC that delineate the geographic scope of the cable compulsory license under §111" (i.e., the station's Area of Dominant Influence (ADI)). NRTC, reply comment 31, at 5-6; ASkyB, comment 33, at 7.

Because the Copyright Office is endorsing local retransmission for both network and non-network stations, local markets must be defined for noncommercial educational stations as well as commercial stations. The FCC defines a commercial station's local market as its ADI for purposes of the must-carry rules, and ADI is currently used for determining local markets under the cable compulsory license.¹²⁸ The Office believes that ADI is superior to Grade B contours or 35 miles because ADI's are separated from one another by community lines, unlike Grade B contours or a 35 mile zone which is likely to cross through communities, resulting in a commercial station which is local to one part of a community but not another.

(...continued)

to attempting to include further nonduplication protection in the copyright law.

¹²⁸ It is not, however, the sole method for determining local markets under the cable license. In addition to ADI, cable systems may use the FCC's 1976 must-carry rules, and determinations thereunder, applying whichever one yields the larger geographic area.

Unfortunately, ADI is only applicable to commercial stations. A separate definition is, therefore, required for noncommercial educational stations.¹²⁹ Rather than attempt artificially to apply ADIs to noncommercial educational stations, the Office recommends defining the local market of a noncommercial educational station as an area encompassing 50 miles from the community of license of the station, including any communities served in whole or in part by the 50 mile radius. This area is broad enough to resemble the local market for cable carriage of noncommercial educational stations, and to encompass must-carry obligations that the FCC might someday impose on local retransmissions by satellite carriers.

In addition to defining the local market, a decision must be made as to what royalty rate, if any, satellite carriers retransmitting local stations must pay to copyright owners. ASkyB states, that under the cable compulsory license, large cable systems that carry at least one distant signal (which is the vast majority of such systems) are not required to pay a royalty fee for local signals.¹³⁰ ASkyB then asserts that the rate should be zero to place satellite in parity with cable. ASkyB, comment 33, at 2. The Office notes that a proceeding under chapter 8 of the Copyright Act to adjust the satellite license rates is currently underway, and ASkyB has presented testimony to the Copyright Arbitration Royalty Panel (CARP) proposing that it adopt a zero rate for local retransmissions. Because the Copyright Office is obligated under the statute to review the CARP's determination on this matter, the Office believes that it would be premature to suggest or comment as to the appropriate royalty rate, if any, to be applied to local retransmissions by satellite. The Office, therefore, refrains from making any recommendation at this time.

3. Failure of the Current Unserved Household Restriction.

Local retransmission of network affiliates is the best solution for resolving the problem of satellite subscriber eligibility for network signals. The Copyright Office recognizes, however, that the technology

¹²⁹ This would exclude PBS if its national satellite service preempts carriage of all PBS affiliates.

¹³⁰ Small and medium sized systems pay a fixed fee regardless of the number of broadcast signals, local or distant, that they retransmit.

for retransmitting local signals via satellite is not widely available and that even ASkyB, its chief proponent, may be backing away from offering such a service. The satellite industry remains a nationwide retransmission service, capable of providing a limited number of broadcast signals on a national basis. The problems associated with the unserved household restriction that existed in 1988, and were revisited in 1994, persist and the stakes have been raised by the increase in size of the satellite industry and the diminution of the networks' viewing share to other video sources. If there is another extension of the section 119 license, the question is whether the problems with the unserved household restriction identified in the above sections may be corrected, or at least ameliorated.

The section 119 license has now been in existence for almost 10 years. In its first term, the issues surrounding the unserved household restriction were of private concern between copyright owners, broadcasters and satellite carriers. These issues were brought into the public eye in 1994 with the adoption of the transitional signal measurement provisions and the resulting termination of network satellite service for thousands of satellite subscribers. As noted above, termination of service has led to a barrage of public complaints with the Copyright Office, the FCC, and the Congress. The consumer ill-will created by the 1994 amendments can be traced to several sources.

First, from a public policy standpoint, the Office believes that the transitional signal measurement provisions had problems inherent in their conception that doomed them to failure. The putative purpose of the provisions was to enable broadcasters, through the issuance of challenges to subscribers, to weed out ineligible subscribers through the mechanism of signal intensity measurements conducted at the subscribers' households. Although the terms and conditions for conducting the measurements were not put in the statute, both broadcasters and satellite carriers promised Congress at the time of passage of the 1994 Satellite Home Viewer Act that they would privately negotiate the terms and conditions. They never did. Even if they had, it is unlikely that satellite carriers would have conducted many, if any, measurements because the cost would

far exceed the revenues received from the subscribers for delivery of network signals.¹³¹ The result of this impasse was that virtually no measurements of any sort were conducted, regardless of their legal sufficiency. Instead, the common practice of the satellite carriers was, upon receipt of an affiliate challenge, to simply turn off network service to the subscriber. Although the satellite carriers did not offer any testimony as to the total number of disconnects, PrimeTime 24 claims to have terminated 300,000 subscribers' network service as a result of challenges. PrimeTime 24, comment 11, at 1. It is, consequently, no surprise that there has been a significant consumer uproar. Because the 1994 signal measurement provisions did not establish a well defined, cost efficient testing regime, they could not operate as intended.

Responding to the complaints of its subscribers, the satellite carriers and their distributors often informed customers that they could continue to receive service of a network signal if they contacted their local affiliate and convinced the affiliate to withdraw its challenge. This practice is commonly referred to as obtaining a "waiver" from the local broadcaster.¹³² Through its numerous contacts with satellite customers, the Copyright Office is aware that many network affiliates have agreed to withdraw their challenges. Many have not, however, and some affiliates have not had any mechanism in place to respond to subscriber inquiries. Because there are no standards and requirements for this practice, its operation has been uneven and has contributed to consumer confusion and anger.

Another practice of the satellite carriers was to inform subscribers whose network signal receipt had been challenged to pay for and conduct their own signal intensity measurement. A corollary to this practice

¹³¹ Even though the statute provides that the "loser pays" the cost of the measurement, there are still the upfront costs associated with conducting the test. For challenges to subscribers located within the predicted Grade B contours of local affiliates, satellite carriers were required to incur the actual cost of the measurement, in the hopes of recovering such cost at a later date. With broadcasters issuing tens of thousands of challenges, it was unreasonable to expect that satellite carriers would absorb the initial cost of conducting measurements at each of these subscribers' household, even with the 5% limit on the number of households subject to testing. See 17 U.S.C. § 119(a)(8)(C).

¹³² The term "waiver" is actually a misnomer, because the broadcaster is not waiving any provision of the law or its rights. Instead, withdrawing the challenge is more along the lines of a covenant not to sue, whereby the local affiliate agrees that it will not challenge a subscriber's receipt of satellite service of a network station as violative of the unserved household restriction.

was an offer from the satellite carrier to conduct the test, but at the subscriber's expense. A significant problem with this approach is that because there are no agreed upon standards for conducting a measurement, the legal sufficiency of a measurement conducted by a subscriber is in serious doubt. A subscriber could therefore pay an engineer or other party to conduct a measurement, discover that he or she resides in an unserved household, but still have network service terminated because the local affiliate and/or satellite carrier would not accept the results of the measurement.

Another failure of the signal measurement provisions particularly, and the unserved household restriction generally, is the confusion it has created among consumers. Subscribers who do not understand the law and are faced with termination commonly complain that federal law prevents them from receiving the television signals they are willing to pay for, or that the Copyright Office or the FCC has ruled that they cannot receive network service. Satellite carriers, and particularly their distributors, have directly contributed to this confusion, especially after they have signed up a potential customer for satellite network service. Much of this confusion could have been avoided if satellite carriers were required to disclose the provisions of the unserved household restriction before they provided a subscriber with satellite service.

The Copyright Office has also received numerous complaints regarding the 90 day waiting period from termination of cable service. Consumers do not understand, in circumstances where they cannot receive a signal of Grade B intensity and have discontinued their cable service, why they have to do without any network service for three months. Clearly, the purpose of the 90 day waiting period is to discourage cable subscribers from terminating their service, thereby making satellite service less attractive. The provision is anti-competitive by favoring one type of video retransmission provider over another. The Copyright Office cannot see any sound public policy reasons as to why consumers who do not subscribe to cable are immediately eligible for satellite network service (provided, of course, that they do not receive the over-the-

air signal), and those who have subscribed to cable in the past must endure 90 days without any network service. The Office recommends that the 90 day waiting period be eliminated.¹³³

4. The "Red Zone/Green Zone" Approach.

In sum, the signal measurement provisions have not provided a workable standard. If the section 119 license is extended, and the unserved household restriction remains in the copyright law, what can be done to better determine a subscriber's eligibility for network service? The Copyright Office believes that the only clear-cut solution to the problem of determining eligibility is to establish well defined geographic areas wherein satellite service of a particular network is permitted and to exclude provision of service in all other areas. This is the "red zone/green zone" approach described above in the discussion of the comments. Under this approach, the local markets of a network affiliate would be defined, and satellite carriers would be denied the compulsory license for a network signal for any subscriber who resides within the local market of an affiliate of that same network (i.e., the "red zone"). Subscribers who reside outside the local market of a network affiliate could receive satellite service of that affiliate (i.e., the "green zone"). Because Grade B is not delineated along community lines and is consequently too imprecise to clearly define "red zones" and "green zones," the Copyright Office recommends that reference to Grade B, for purposes of defining the local market, be dropped and replaced by the same definitions of local markets for local retransmissions described above.

In addition, the Copyright Office recommends that satellite carriers, and their distributors, be required by statute to disclose to subscribers before they receive satellite service whether or not the subscriber resides in a "red zone" or a "green zone" for receipt of each network signal offered by the satellite carrier. Such disclosure statements should substantially reduce consumer confusion by informing a potential subscriber, up front, whether he or she is eligible to receive service of a particular network signal.

¹³³ The Office also opposes, for the same reasons, NASA's suggestion that the unserved household definition be amended to prevent any household that is passed by cable, but does not subscribe, from receiving satellite network service, if it is otherwise eligible.

The commenters are divided on the issue of whether subscribers currently receiving satellite network service, either legitimately or illegitimately, should be grandfathered under any extension of section 119. The Office is proposing a new standard for determining subscriber eligibility, which will change the eligibility of many households. Some subscribers now eligible for a network signal will not be eligible for it under the "red zone/green zone" approach, while subscribers not now eligible will become so under the new approach.

The Office is troubled by the idea of grandfathering subscribers who are not currently eligible for network service, yet receive it anyway, and who would also not be eligible under the "red zone/green zone" approach. The commenters did not address the issue of grandfathering in the context of the "red zone/green zone" approach and the intricacies it presents. The Office believes that there is, therefore, an insufficient record on which to base a recommendation on grandfathering at this time and refrains from doing so.

The Copyright Office believes that the "red zone/green zone" approach is the only way the unserved household restriction can be reformed so as to provide clear statutory guidelines and a system that will guarantee the program exclusivity of network affiliates. Implementation of the "red zone/green zone" approach will effectively end satellite service of network stations in urban areas and confine it to predominantly rural areas of the country, which was the espoused purpose of adopting the satellite compulsory license in 1988.

5. The PBS National Satellite Service.

If the "red zone/green zone" approach is adopted, PBS will seek an exemption for its national satellite service. PBS has represented to the Copyright Office that its affiliates have agreed to a national feed of PBS programming, and there appears to be no reason to apply the "red zone/green zone approach" to satellite carriage of the PBS national service. The Office, therefore, favors a statutory exemption for this service.

6. The Picture Quality and Grade B Standards.

While the Office recommends the "red zone/green zone" approach as the best statutory solution, it recognizes that there will be households located in a "red zone" that do not receive an adequate over-the-air signal from the local affiliate, and do not, or cannot, receive the local affiliate from a cable operator or other multichannel video programming provider. The Office also understands that Congress is desirous of providing cable with active competition, particularly in urban areas, and that satellite represents the potential for such competition. The Office does not believe, however, that section 119 can be so finely crafted as to permit workable determinations as to the eligibility of individual households for satellite receipt of specific networks, short of creating a bureaucracy to make such determinations.

The Office has examined and considered the approach offered by PrimeTime 24 to replace the Grade B signal intensity standard with a picture quality standard. The attractive asset of a picture quality standard is that, in theory, it allows households that have previously not received acceptable network service to obtain a network picture of high quality. The Office agrees with broadcasters, however, that a picture quality test for eligibility of satellite service is far too subjective and inherently biased, and will increase consumer confusion and conflict between satellite carriers and broadcasters. The Office questions the ability of satellite carriers and broadcasters to agree to a third party observer to make picture quality determinations, or a group of such individuals, when the parties could not agree to the far more objective Grade B signal intensity measurement in 1994. Furthermore, the Office does not believe that picture quality is a legally sufficient standard on which to base a determination of copyright liability. Because of the subjective nature of picture quality, federal judges and juries are likely to arrive at very different conclusions as to what constitutes an acceptable over-the-air picture, thereby muddying the infringement standard. The Office, therefore, concludes that adoption of a picture quality standard would be unsound copyright policy.

At the same time, the Office acknowledges that the current Grade B standard is not without its problems. While Grade B is certainly more objective than picture quality, over-the-air delivery of a signal of Grade B intensity does not guarantee a quality picture. Even if Grade B is retained, none of the parties

have offered any solution as to how to conduct meaningful intensity measurements that are cost efficient for satellite carriers. As long as the cost of measurement exceeds the revenues of service,¹³⁴ there is no economic incentive to conduct the measurement. If the cost of the measurement is placed upon the subscriber desiring service, with perhaps the opportunity to recover the cost from the challenging network affiliate, clear engineering standards must be adopted so as to guarantee uniformity in testing and to assure that the subscriber will receive network service if the measurement reveals that he or she does indeed reside in an unserved household. Because it lacks engineering expertise, the Copyright Office cannot recommend what the measurement standards should be. The only suggestion that can be made is that if the standards are left to the parties to negotiate, they be forced to go to arbitration after a period of time to resolve the matter so as to avoid recurrence of the impasse of 1994.

In short, the Office seriously questions whether section 119 can be drafted so as to permit workable, individual determinations of subscriber eligibility for network service. Individual determination typically requires examination of individual facts, and a determination as to whether a particular household receives adequate network coverage requires consideration of topographical features, weather conditions, availability, location and sufficiency of the household's receiving equipment, access to other program providers, and other special circumstances. These determinations cannot be made in a statutory provision.¹³⁵

7. The Surcharge Option.

Nevertheless, the Office recognizes the consumer issue, and the competition issue, of allowing satellite carriers to offer network service to those subscribers who reside in "red zones" that legitimately cannot receive an over-the-air signal. The answer is retransmission of local network affiliates by satellite carriers. Because the technology to accomplish this is not readily available, the Office has considered other

¹³⁴ Some satellite carriers apparently offer network service for as little as \$20 a year.

¹³⁵ While particularized determinations can be made by a government agency, the Copyright Office is not suggesting that Congress create such an agency, or authorize an existing one, to determine which U.S. households can or cannot receive what network signals from their satellite carrier.

options. Satellite carriers have proposed imposing a surcharge on these subscribers, and submitting the surcharge to the Copyright Office for distribution to affiliates via the royalty distribution procedures of chapter 8 of the Copyright Act. Broadcasters oppose the concept of a surcharge. The Office agrees that, over the long term, a surcharge may not adequately compensate local affiliates for the loss of viewers, and accompanying decline in revenues, resulting from increased satellite network service in red zones. A surcharge, however, appears to be the only statutory mechanism for allowing subscribers in the "red zone" an opportunity to receive satellite network service.¹³⁶ It is not possible to craft a statutory test or standard that will yield individual determinations of adequate network service (if, in fact, one can define what adequate service is) or provide the economic incentives to make such determinations. A surcharge eliminates the need for determining individual subscriber eligibility by allowing any subscriber in a "red zone" for a particular network signal, if he or she wishes to incur the additional cost, to receive satellite service of that network.

The Office does not offer any suggestion as to what would be an appropriate surcharge to level on satellite carriage of network signals to "red zone" subscribers because the Office does not have any means at its disposal for determining what amount of money would adequately compensate local network affiliates for the loss of viewers to their signal. The rate could be established by Congress in the statute, or by a CARP convened under chapter 8 of the Copyright Act.

Because of the long term harm to local affiliate viewership, the Office recommends that any surcharge adopted be temporary. A temporary surcharge would allow the satellite industry additional time

¹³⁶ A surcharge is also a means of addressing the unique situation of owners of mobile homes and recreational vehicles who desire satellite network service. Currently, satellite carriers are unable to sell satellite network service to these consumers because such homes/vehicles may move into areas where they can receive over-the-air signals of network affiliates, even if on a temporary basis. A satellite carrier that can provide network service to a mobile home or recreational vehicle on one day, because that home/vehicle is an unserved household, can be liable for copyright infringement the next day, because the home/vehicle has moved into a served area. A surcharge would alleviate this problem by allowing satellite network service for these home/vehicles, albeit at a higher price than would presumably be charged by a satellite carrier if the home/vehicle were a permanent structure located in an unserved area.

to develop and implement local retransmissions. If the satellite industry fails to implement this technology by the expiration of the surcharge, then it would be consigned to providing network service to only those subscribers in "green zones."

In suggesting a temporary surcharge, the Office is guided by the fact that implementation of over-the-air digital broadcasting in the next several years is likely to change the complexion as to what constitutes an unserved household.¹³⁷ The parties represented to the Office that over-the-air receipt of a digital television signal is on an all or nothing basis. Either the household receives a digital quality picture, or it receives no signal at all. This presents the possibility that a "picture receipt" standard may someday be implemented to target individual households within the "red zone." It is premature, however, to recommend a solution to the unserved household restriction for digital television. Even if broadcasters commence transmissions in digital in a few years time, they will continue to simulcast a corresponding analog signal for a period of time. Depending upon how well digital broadcast television is accepted by the public will determine how long broadcasters continue analog transmissions. The FCC has targeted a ten year transition period, but this certainly could be extended. Until such time as a majority of households choose to receive digital signals through their television set, digital broadcasting will not offer any real solution to the unserved household restriction. The Office, therefore, recommends that Congress reexamine the issue of satellite network service to "red zone" subscribers once digital broadcasting is established and a firm timetable for elimination of analog transmissions is adopted.

E. CONCLUSION

Satellite subscriber eligibility of network signals is a problematic issue without a clear-cut solution. Technological limitations created the need for the unserved household restriction, and technological advancements can eliminate it by enabling satellite carriers to retransmit local network affiliates to their

¹³⁷ See Fourth Report and Order, Docket No. 87-268, 11 FCC Rcd 17,771 (1996); Fifth Report and Order, Docket No. 87-268, 62 FR 26966 (May 16, 1997); Sixth Report and Order, Docket No. 87-268, 62 FR 26684 (May 14, 1997).

subscribers. If the section 119 license is extended, the Copyright Office strongly recommends that it be clarified to allow retransmission of all television broadcast stations, commercial as well as noncommercial educational, within each station's local market. The Office proposes that the local market for commercial stations be the same as defined by the FCC (i.e. ADI, and any modifications thereof), and for noncommercial educational stations all communities in whole or in part within 50 miles of each station's community of license. The Office does not take a position as to what royalty rate, if any, should apply to local retransmissions.

Given that local retransmission has yet to be accomplished commercially in the satellite industry, the Office recommends that any extension of the section 119 license should include revision of the unserved household restriction. The Office found the transitional signal measurement provisions adopted in the 1994 Satellite Home Viewer Act to be a failure. The Office opposes the substitution of a picture quality standard for the Grade B standard because it is too subjective, legally insufficient, and administratively unworkable. Likewise, the Office finds the Grade B standard less than precise and costly when applied to individual household determinations.

If network program exclusivity protection remains in the copyright law, (and the Office suggests that it be moved to the communications law and regulation), the Office proposes adoption of a "red zone/green zone" approach, based on local markets rather than Grade B, which would clearly delineate geographically those subscribers who are eligible for network service and those that are not. The "red zone/green zone" approach would apply to all network signals, except the PBS national satellite service. In addition, the Office recommends that satellite carriers, and their distributors, be required to disclose to their potential subscribers whether they reside in a "red zone" or "green zone" with respect to each network signal offered by the satellite carrier. The Office takes no position as to whether subscribers should be grandfathered under the "red zone/green zone" approach.

If Congress wishes to allow certain subscribers within the "red zone" to receive network service, the Office has concerns that this can be accomplished statutorily without authorizing some decision making body to make individual determinations of eligibility. In lieu of creating such a bureaucracy, the Office suggests that Congress consider a transitional solution, such as a surcharge, until such time as satellite carriers implement local retransmission of network signals and/or over-the-air digital television becomes a widespread medium.

X. ADDITIONAL ISSUES

A. TREATMENT OF NETWORK SIGNALS

There are two issues involving retransmission of network signals by cable systems that have not been addressed at this point: DSE value accorded to network signals, and distribution of royalties to network program copyright owners.

1. Payment for Network Signals.

As discussed above, distant network signals under the cable compulsory license are paid for in a different manner than independent commercial stations. Congress made the determination in 1976 that network programs were bought and paid for on a nationwide basis, and that importation of distant network signals by cable operators did not harm copyright owners.¹³⁸ Network signals, therefore, count as only one-quarter of a distant signal equivalent (DSE), as opposed to the full DSE accorded distant independent station. The one-quarter value accounts for the nonnetwork programming (local news, weather, specials) that appears on network signals during the course of the typical broadcast day.

The rationale for the difference in value accorded network versus independent signals was carried over into the satellite carrier compulsory license. The original satellite rates for payment of superstation (i.e. independent station) and network signals was 12 cents per subscriber and 3 cents per subscriber, respectively, which represents the four-to-one ratio established in the cable license. One of the commenters, ABC, Inc., asserts that the value of network and independent signals should be equalized under both licenses. ABC, comment 20, at 3. ABC states that the theory that network programming is adequately compensated by national advertising revenues is no longer valid because cable system and satellite carrier subscribers receive valuable programming which should be compensated. Further, ABC notes that superstations such as WGN

¹³⁸ H.R. Rep. No. 1476, 94th Cong., 2d Sess. 90 (1976).

and WTBS receive national advertising revenues, yet their programming receives full value under the compulsory licenses. Id.

The Copyright Office testified in 1992 in favor of equalizing the rates for the satellite carrier license.¹³⁹ The Office noted that because networks were entitled to a royalty distribution under the section 119 license, as opposed to the section 111 license, it no longer made sense to value a network signal at one-quarter the value of a superstation signal. The proposal was not adopted in the 1994 Satellite Home Viewer Act.

The Copyright Office maintains its point of view that the rates for network and superstation signals should be equalized under the section 119 license. Furthermore, the Office supports equalization of the DSE value of network and independent stations under the cable license. The Office can determine little discernible difference between the manner in which programs and national advertising are bought and sold on network stations and the large independent stations, such as WTBS. Although cable systems undoubtedly would oppose raising the DSE value of network signals (none addressed the issue), the Office believes that network programming is of significant value to cable systems and should be compensated. The Office, therefore, supports raising the value of network signals to one full DSE.

2. Distribution to Networks.

A related issue to the DSE value of network signals under the cable license is entitlement of network programming for royalty distributions. As noted above, network programming is entitled to distribution of royalties under the satellite license, but not the cable license. ABC advocates that the distinction be eliminated, and that networks be allowed to share in cable royalties.

As with equalization of DSE values, the Office supports removal of the restriction entitling only owners of nonnetwork programming to a distribution of cable royalties. 17 U.S.C. § 111(d)(3). Network

¹³⁹ *Copyright Broadcast Retransmission Licensing Act of 1992: Hearings on H.R. 4511 Before the Subcomm. on Intellectual Property and Judicial Administration of the House Comm. on the Judiciary, 102d Cong., 2d Sess. (1992).*

programming is of significant value to cable systems, and network program copyright owners should be entitled to compensation for that value. Further, as a policy matter, it makes little sense to allow networks royalty distributions under the satellite license, but deny them that right under the cable license. Increasing the DSE value of a network signal from one-quarter to one should result in a corresponding inclusion of networks in the royalty distribution.

B. PAYMENT FOR LOCAL SIGNALS

Although the Copyright Office has declined to comment as to the royalty compensation due local retransmission of signals by satellite carriers, the Office does have several observations about payment of local signals under section 111.

It is a common belief that carriage of local signals by cable systems is on a royalty-free basis. This is a fiction, however, for the statute does provide for a minimum copyright royalty fee to be paid by every cable system, whether or not it carries any distant signals. 17 U.S.C. § 111(d)(1)(B), (C) and (D). Small and medium sized cable systems (Form SA1-2) pay a flat fee even if they retransmit only local signals, and large cable systems (Form SA-3) also pay a fee, based upon a percentage of their gross receipts, even if they retransmit only local signals. Curiously, a large cable system that carries one distant signal, in addition to local signals, pays the same royalty fee as a cable system which carries only local signals.

Copyright treatment of local retransmissions was significantly debated during the passage of the 1976 Copyright Act, particularly after the Supreme Court held that local retransmissions under the 1909 Copyright Act were not public performances, and hence not subject to copyright liability. Fortnightly Corp. v. United Artists Television, Inc., 392 U.S. 390, reh'g denied, 393 U.S. 902 (1968). While Congress chose to impose copyright liability on all broadcast retransmissions by cable systems, it found that copyright owners were only harmed by retransmission of distant signals, and created a compulsory license regime that

sought to compensate copyright owners principally for retransmissions of distant signals.¹⁴⁰ Nevertheless, cable systems are required to submit a minimum fee for retransmission of only local signals.

The Office believes that the minimum fee is an important aspect of the cable compulsory license and should be retained. In reaching this decision, the Office considered placing a zero rate on the retransmission of local signals. If this were done, some systems would not owe any royalties. However, if such systems were required to file a statement reflecting the signals that they carried, an administrative filing fee to cover processing costs would be required. The Office rejected such an approach because it believes that local systems have value even though there may be no economic harm to copyright owners. The Office also believes that all cable systems should be required to pay at least a minimum amount for the ability to retransmit broadcast signals.

¹⁴⁰ H.R. Rep. No. 1476, 94th Cong., 2d Sess. 90 (1976).

XI. RECOMMENDATIONS

1. Existence of the Cable and Satellite Carrier Licenses.

- While the Copyright Office prefers marketplace mechanisms for the use and payment of copyrighted works, the Office recommends that the cable and satellite carrier licenses not be eliminated at this time.

2. Extension of the Satellite Carrier License.

- The Copyright Office recommends that the satellite carrier license should be in place as long as the cable license is in place. Therefore, the Office recommends that the satellite carrier license be extended with no sunset provision.

3. Harmonization of the Cable and Satellite Carrier Licenses.

- The Copyright Office recommends that the cable and satellite carrier licenses remain separate licenses.
- The Copyright Office recommends that differences between the two licenses be removed where possible on the principle that the compulsory licenses should not unduly affect the competitive balance between the cable and satellite industries.

4. Application of Section 111 to Open Video Systems.

- The Copyright Office recommends that section 111 be amended to make the cable compulsory license available to open video systems.
- The Office recommends that section 111 be amended in the following areas:
 - (a) definition of a cable system;
 - (b) passive carrier exemption;
 - (c) cable rate structure;
 - (d) contiguous communities provision.

5. Application of Section 111 to Internet.

- The Copyright Office recommends against extending the cable compulsory license to Internet service providers or creating a new compulsory license for Internet service providers.

6. Passive Carrier Exemption.

- The Copyright Office recommends that the passive carrier exemption be amended to provide that open video systems may provide such ancillary services as marketing, billing, and collecting.
- The Copyright Office recommends that the passive carrier exemption not extend to open video systems that scramble or encode their signals.
- The Copyright Office recommends that the passive carrier exemption not be extended to open video systems that retransmit local signals under their must-carry obligations, but the Office recommends that Congress might consider creating a different exemption for open video systems that only retransmit must-carry signals.

7. Cable Rate Reform.

- The Copyright Office recommends that Congress adopt a flat, per subscriber, per signal fee, similar to the fee structure already in place for satellite carriers.
- As an alternative to the flat, per subscriber, per signal rate, the Copyright Office recommends a simplified gross receipts fee structure.
- The Office recommends against any step-up rate to inhibit the importation of distant signals.
- The Office recommends that network programs be fully compensated, and that network signals be paid for as a full distant signal.
- The Copyright Office recommends that the cable rate structure be reformed so that it is simple to administer and compensates authors at fair market value.
- The Copyright Office recommends that Congress reconsider the existence of its current policy to subsidize small systems. The Office recommends that Congress at least raise the payments made by small systems from their current nominal level. However, at present, the Office recommends the continuation of a differential rate for small systems and large systems.

8. The Unserved Household Restriction.

- The Copyright Office recommends that the satellite carrier compulsory license be clarified to permit the retransmission of a network affiliate to subscribers located within that affiliate's local market.
- The Office recommends that a commercial network station's local market be defined as its Area of Dominant Influence, and a noncommercial educational network station's local market be defined as the communities that, in whole or in part, are located within 50 miles of the station's community of license.

- The Copyright Office recommends that the unserved household restriction be removed from the copyright law and placed in the communications law.
- In the alternative, if the unserved household restriction remains in the copyright law, the Office recommends adoption of a "red zone/green zone" approach to determining subscriber eligibility for network signals. The Office also recommends that satellite carriers, and their distributors, be required to disclose to their potential subscribers whether they reside in a "red zone" or "green zone" with respect to each network signal offered by the satellite carrier.
- The Copyright Office also supports a temporary surcharge to subscribers located in a "red zone" who nonetheless desire network service, with the monies collected distributed to local network affiliates.
- The Office supports this surcharge as a temporary solution and recommends that Congress revisit the unserved household restriction in the future when technological developments present better solutions to network service in the "red zone."
- The Copyright Office recommends that Congress eliminate the 90-day waiting period for subscribing to network signals.