# ANNOUNCEMENT

from the Copyright Office, Library of Congress, Washington, D.C. 20559

NOTICE OF INQUIRY

COMPULSORY LICENSE FOR AND MERGER OF CABLE SYSTEMS

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**LIBRARY OF CONGRESS**

**Copyright Office**

**37 CFR Part 201**

**[Docket No. RM 89-2]**

**Compulsory License for and Merger of Cable Systems; Notice of Inquiry**

**AGENCY:** Library of Congress, Copyright Office.

**ACTION:** Notice of inquiry.

**SUMMARY:** The Copyright Office of the Library of Congress issues this notice of inquiry to inform the public that it is examining the issues of merger and acquisition of cable systems and their impact on the computation of royalties under the cable compulsory license of the Copyright Act, section 111, title 17 U.S.C. The Office also seeks public comments and proposals as to the proper reporting and royalty calculation procedures for cable systems under common ownership in contiguous communities, whether as a result of merger of systems or expansion of a single system.

**DATE:** Initial comments should be received by December 1, 1989. Reply comments should be received by December 29, 1989.

**ADDRESS:** Interested persons should submit ten copies of their written comments as follows:

If sent by mail: United States Copyright Office, Library of Congress, Department 17, Washington, DC 20540.

If delivered by hand: Office of the Register of Copyrights, Copyright Office, James Madison Memorial Building, Room 407, First and Independence Avenue, SE., Washington, DC.

**FOR ADDITIONAL INFORMATION CONTACT:** Dorothy Schrader, General Counsel, Copyright Office, Library of Congress, Department 17, Washington, DC 20540. Telephone: (202) 707-8380.

**SUPPLEMENTARY INFORMATION:**

**1. Background**

Section 111(c) of the Copyright Act of 1976, title 17 of the United States Code, establishes a compulsory licensing system under which cable systems may make secondary transmissions of copyrighted works embodied in broadcast signals. The compulsory license is subject, among other conditions, to requirements that the cable system report its signal carriage in statements of account twice yearly and remit royalties to the Copyright Office, in accordance with a statutory formula, for later distribution to copyright owners. The royalty is calculated by applying the number of distant signal equivalents ("DSE's") and the royalty rate against the gross amounts paid to the cable system by its subscribers for the basic service of providing secondary transmissions.

The Copyright Act also provides, as part of the section 111(f) definition of a cable system, that "[f]or 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 head-end shall be considered as one system."

On December 1, 1977, in one of our first proceedings under the cable compulsory license, the Office published proposed rules in the Federal Register (42 FR 61051) to establish the basic reporting and royalty payment filing procedures for cable systems. Among other issues, we considered the meaning of the above-quoted final sentence of the definition of cable system. We noted that the "legislative history of the Act indicates that the purpose of this sentence is to avoid the artificial fragmentation of cable systems," since Congress fixed lower rates for smaller cable systems.

In final regulations published January 5, 1978 (43 FR 958), we adopted an interpretation of the last sentence of the statutory definition of cable system that exactly tracks the text of the statute, except that letter designations were inserted in the text to show our understanding of the congressional intent. This regulation, § 201.17(b)(2), remains in effect. The National Cable Television Association (NCTA) has several times requested that the Copyright Office re-open the matter of the correct interpretation of the final sentence of the statutory definition of cable system. We have not revisited this issue since 1978 because the regulation in question was adopted after a careful review of the legislative history of the Copyright Act by those Copyright Office officials who were active participants in the copyright revision process that led to enactment of the 1976 Act.

By this Notice, however, the Copyright Office re-opens the matter of the interpretation of the final sentence of the definition of cable system in 17 U.S.C. 111(f) (hereafter the "contiguous communities" provision). We do so because, in addition to the requests of the NCTA for reconsideration of this

issue, the Copyright Office has received several letters from representatives of cable systems asking us to provide guidance on the reporting and filing procedures where one system acquires or merges with another. Mergers of systems present a number of problems in computing the royalty fees, including the problem that the merger frequently involves "adjoining" systems, and therefore raises questions about the contiguous communities provision.

Under the existing regulation, two or more cable facilities are classified as one individual cable system if the facilities are either in contiguous[1] communities under common ownership or control or are operating from one[2] common headend. A single statement of account must be filed in these cases and the "combined" DSE's must be applied against the gross receipts for secondary transmissions for the "combined" system. The growing expansion of cable system coverage and recent trends toward economic concentration in the industry create several difficulties with respect to the determination of the proper royalty sums due under the cable compulsory license. In an effort to resolve these difficulties, the Office is conducting this inquiry into the matter of the merger and acquisition of cable systems and their impact on the computation of royalties under the cable compulsory license.

In defining a cable system for purposes of the cable compulsory license, § 201.17(b)(2) of 37 CFR, provides that "two or more cable facilities are considered as one cable system if the facilities are either: (A) In contiguous communities under common ownership or control or (B) operating from one headend." Thus, if two or more cable systems satisfy this aspect of the definition of "cable system," they must submit a single Statement of Account as one system and calculate the royalty fee accordingly. However, given the current climate of cable system expansion, corporate mergers and acquisitions present real problems in calculating the royalty payment due from the system.

For example, assume a situation where there are two completely independent but contiguous cable systems. System A carries two non-permitted (3.75% rate) independent station signals and System B, assigned a different television market, carries the same two independent station signals but on a permitted (base rate) basis, plus a superstation signal on a non-permitted (3.75% rate) basis. Systems A and B are purchased by the same parent company and apparently become a single cable system for purposes of the compulsory license. The purchase raises several problematic issues as to the calculation of the proper royalty fee. Should the independent stations be paid for at the 3.75% rate or the non-3.75% rate system-wide, or should the rates be allocated among subscribers within the system and, if so, on what basis? Furthermore, if allocation is the answer, what rate can be attributed to new subscribers to the merged system? Finally, there is the question of the superstation signal which is only carried by former cable System B. At the time of acquisition, should the superstation be attributed throughout the entire system, even though many subscribers do not receive the signal (a so-called "phantom" signal)? And which system's market quota (A's or B's) should be used for the entire statement? Innumerable variations and combinations of signal carriage, permitted versus non-permitted signals, and television market quotas are possible. These vexing questions present a serious problem for a newly contiguous, merged system in calculating the proper royalty fee.

Under another regulation, 37 CFR 201.17(h), cable systems may pay the[3] non-3.75% rate in some cases where "expanded geographic carriage" of certain signals occurs. This regulation is specifically limited, however, to the situation in which a signal was actually carried in only part of a system due to the pre-June 25, 1981 Federal Communications Commission (FCC) carriage restrictions. In adopting this regulation as part of the implementation of the Copyright Royalty Tribunal's (CRT) 1982 rate adjustment, we reasoned that the "expanded geographic carriage" which results directly from the FCC's 1980 deregulation order does not represent any "additional DSE" because before deregulation the system had to pay royalties system-wide for FCC restricted signals. (49 FR 14944, April 16, 1984 and 49 FR 26722, June 29, 1984). At that time, we addressed issues relating to the CRT's 1982 rate adjustment, and we did not have before us any evidence or comment regarding merger or acquisition of cable systems. This regulation therefore only applies to the expansion of signal coverage within a system resulting from the FCC 1980 deregulation. It does not cover situations where expanded carriage of a signal results from the creation of a new system through merger or acquisition, which operates in contiguous communities.

**2. Filing Procedures and Policies for Merged Cable Systems**

In view of the many problems created by mergers, acquisitions and expansion, the Copyright Office, in order to develop a coherent policy to deal with these matters, invites public comment on the general problem and on the following questions.

(1) In the hypothetical case posited above, where contiguous Systems A & B carry the same two independent station signals (and System B carries an additional signal) but, before the merger, System A must pay the 3.75% rate for the independent signals, and the two systems are subsequently purchased by the same entity, how should the proper royalty fee determination be made and should the Copyright Office continue to require Systems A & B to file a single statement of account?

(2) Should the merged system be required to pay the 3.75% rate for the two independent station signals for all the subscribers to the system (subscribers to both A & B), or should the two signals be treated as permitted (non-3.75% rate) signals for the entire system, and, if so, why? Or, should the system be allowed to allocate the rates among the former subscribers to System A and B, resulting in the cable system paying for the right to secondarily transmit the same independent station signals at different royalty rates?

(3) If allocation between two different royalty rates for the same two independent station signals is desirable, on what basis should it be allowed? Should the former boundries separating Systems A & B be followed for purposes of determining the allocation? What happens if the system expands and adds new subscribers? How should they be treated for purposes of allocating the rate among the same two signals?

(4) In the hypothetical case, System B also carried a superstation signal at the 3.75% rate. At the time of the acquisition, the superstation signals would still only be received by the former subscribers of System B. How should this signal be paid for by the new system? (a) Should the superstation signal be attributed to the entire subscriber base, even though many subscribers do not actually receive the signal (a so-called "phantom" signal)? or (b) If allocation of the signal is desirable, on what basis should it be allowed? Should the sums paid by only those subscribers who actually receive the signal be included in the gross receipts for that signal?

(5) In considering the impact of mergers and acquisitions of the computation of the royalty fee, should the method by which the combined system was developed affect the policies relating to computation of royalties? (That is, should it make any difference whether the new system comes about through merger of two systems to form a third new one, or if one system acquires another and the second system disappears, or if both systems remain largerly intact from an operational viewpoint but are now under common ownership?)

[1] Error; line should read:
"facilities are *either* in contiguous"

[2] Error; line should read:
"or control *or* are operating from one"

[3] Error; line should read:
"§ 201.17(h), cable systems may pay the"

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(6) If the systems were franchised by different local authorities, may the new system allocate the gross receipts to account for disparate local franchising conditions that require maintenance of certain secondary transmission service, which will not be system wide in the new cable system?

(7) The preliminary assessment of the Copyright Office is that, except for the definition of cable system in section 111(f) of the Copyright Act, the issues posed by merger and acquisition of systems are primarily matters of administrative and regulatory policy. To the extent that neither the statute nor the legislative history of the Act give guidance, the Copyright Office could probably provide guidance based on its responsibility for the fair and effective administration of the compulsory license. We request comment, however, whether the Copyright Office should attempt to provide guidance on these matters, which were largely uncontemplated by the Congress in establishing the compulsory license.

Dated: August 29, 1989.

Ralph Oman,

*Register of Copyrights.*

Approved by: James H. Billington,
Librarian of Congress.

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