ANNOUNCEMENT

from the Copyright Office, Library of Congress, Washington, D.C. 20559-6000

EXTENSION OF COMMENT PERIOD

NEW

CABLE COMPULSORY LICENSE; NOTICE OF INQUIRY REGARDING MERGER OF CABLE SYSTEMS AND INDIVIDUAL PRICING OF BROADCAST SIGNALS

The following excerpt is taken from Volume 60, Number 5 of the Federal Register for Monday, January 9, 1995 (pp. 2365-2367)

LIBRARY OF CONGRESS

Copyright Office

37 CFR Part 201

[Docket No. 89–2A]

Cable Compulsory License; Notice of Inquiry Regarding Merger of Cable Systems and Individual Pricing of Broadcast Signals

AGENCY: Copyright Office, Library of Congress.

ACTION: Extension of comment period.

SUMMARY: The Copyright Office is reopening the comment period in Docket RM 89–2 (Merger of Cable Systems) to broaden the scope of this proceeding. Specifically, the Office seeks comment as to 1) the copyright royalty implications of *a la carte* offerings of broadcast signals by cable operators and 2) the permissibility of allocating gross receipts among subscriber groups for *a la carte* signals in computing royalties due under the cable compulsory license of the Copyright Act.

DATES: Initial comments should be received by February 23, 1995. Reply comments should be received by February 8, 1995.

ADDRESSES: Interested persons should submit fifteen copies of their written comments, if delivered by mail, to: Copyright GC/I&R, P. O. Box 70400, Southwest Station, Washington, D.C. 20024. If delivered by hand, fifteen copies should be brought to: Office of the General Counsel, James Madison Memorial Building, Room LM-407, 101 Independence Avenue, S.E., Washington, D.C. 20540.

FOR FURTHER INFORMATION CONTACT: Marilyn J. Kretsinger, Acting General Counsel, Copyright GC/I&R, P. O. Box 70400, Southwest Station, Washington, D.C. 20024. Telephone (202) 707-8380. Telefax: (202) 707-8366.

SUPPLEMENTARY INFORMATION:

I. Background

On September 18, 1989, the Copyright Office published a Notice of Inquiry (NOI) in Docket No. RM 89-2 to inform the public that it was examining the issues of merger and acquisition of cable systems and their impact on the computation and reporting of royalties under the cable compulsory license, 17 U.S.C. 111. 54 FR 38390 (1989). At the heart of the 1989 NOI were the royalty filing questions raised by the application of the "contiguous communities" provision of the §111(f) definition of a cable system. That provision provides that two or more cable facilities are considered as one cable system if the facilities are either in contiguous communities under common ownership or control or operating from one headend. *See also* 37 CFR 201.17(b)(2).

The Office highlighted some of the difficulties created by cable systems in contiguous communities becoming a single system through either merger or acquisition by a common owner:

> 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?
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> 54 FR at 38391

Based on the above scenario, the Office also formally posed a set of further questions —many of which addressed the creation of subscriber groups for attributing signals and royalty rates. Among these questions were whether cable operators should be allowed to attribute distant signals among their subscribers in accordance with the conditions that existed prior to the merger or acquisition, and whether cable operators should only be required to include in gross receipts the revenues generated from subscribers who actually received a broadcast signal. *Id.* at 38391–92.

Several parties, who commented on the 1989 NOI, proposed a possible "solution" to the above described scenario.[1] Their proposal is a two step approach:

[1] Although the Copyright Office has reviewed the comments, it has not reached any conclusions or decisions with regard to the suggestions proposed by the various commentators.

aggregation, and then allocation of gross receipts. Cable systems would first aggregate the gross receipts of all of their subscribers to determine which Copyright Office form (and hence royalty rates) to use; then cable systems would report carriage of distant signals according to subscriber groups. Thus, in the above example provided by the Office in the 1989 NOI, Systems A and B would aggregate their gross receipts to determine which form to use (either SA 1-2 or SA-3) and the corresponding royalty rates, and then continue to file separately (i.e. as they were filing prior to the merger/acquisition). Thus, if System A and B"s aggregated gross receipts total was in excess of $292,000, both systems would file a separate form SA-3 with the corresponding royalty rates. System A would file an SA-3 and report two non-permitted independent signals at the 3.75% rate, based only on the gross receipts of the subscribers in the communities System A serves. System B would also file an SA-3 and report both the non-permitted 3.75% superstation signal and those same two independent signals on a permitted basis, based on the gross receipts of the subscribers in the communities System B serves. See comments of American Television and Communications Corp. at 10; comments of Baraff, Koerner, Olender & Hochberg, P.C. at 2-3; comments of Adelphia Communication Corp *et. al.* at 10; comments of National Cable Television Association at 13; comments of Program Suppliers at 7-9. But see comments of Joint Sports Claimants at 3. The referenced commentators argue that this approach is consistent with the "contiguous communities" provision of §111(f) since that provision speaks only to how systems are to be classified, not how they are to report carriage, and sustains the purpose of the provision to prevent fragmentation of cable systems.[2]

The referenced commentators' proposal advocates the creation of "subscriber groups" within a single cable system, requiring allocation of gross receipts to specific groups of subscribers and application of varying royalty rates to those groups. Until now, the Copyright Office has looked with disfavor on allocation of gross receipts based on subscriber groups, since allocation among different subscribers, with one exception, is not specifically recognized by §111 and creates problems in applying the royalty rates.[3] The only express allowance for allocation in §111 is the partially local/partially distant provision of §111(d)(1)(B). That section provides that "in the case of any cable system located partly within and partly without the local service area of a primary transmitter, gross receipts shall be limited to those gross receipts derived from subscribers located without the local service area of such primary transmitter." There are now other "subscriber group" and gross receipts allocation issues beyond those of §111(d)(1)(B) and those presented by the merger and acquisition of cable systems.

II. The 1992 Cable Act

In 1992 Congress passed the "Cable Television Consumer Protection and Competition Act of 1992" (1992 Cable Act) which, among other things, regulates the rates that cable operators may charge their subscribers for cable programming services. Although the 1992 Cable Act is telecommunications legislation, and not copyright, its passage has created additional issues related to creation of subscriber groups and allocation of gross receipts to those addressed in our 1989 NOI.

The 1992 Cable Act permits the Federal Communications Commission, and in some cases local franchising authorities, to regulate the rates charged by cable operators for both broadcast and nonbroadcast programming services. While packages or "tiers" of programming services are subject to rate regulation, Congress excluded per-channel service offerings from such regulation. These per-channel offerings are known as *a la carte* signals because, to be exempt from rate regulation, subscribers must have a "realistic choice" in deciding whether to receive the signal. Report and Order and Further Notice of Proposed Rulemaking in MM Docket 92-266, 8 FCC Rcd. 5631 ¶¶327-328 & n. 808.

The exemption from rate regulation for *a la carte* signals encourages cable operators to offer some, if not all of their services (beyond the basic tier required by the 1992 Cable Act to be provided to all subscribers), on a subscriber choice basis. Thus, for example, a cable operator might offer subscribers three distant superstation signals (WTBS, WWOR, WGN, etc.) at $3 a month per signal. A subscriber could choose any combination of these signals, or none at all, and pay only the per signal charges for those signals selected. The result is a number of distant signal offerings by the cable operator, with varying numbers of subscribers within the system selecting, receiving, and paying separately for each signal.

With the increasing ability of cable operators to offer subscribers essentially "one signal tiers" of broadcast stations, issues arise as to the proper calculation and reporting of royalty fees under the section 111 cable compulsory license. If every distant signal offering is allocated to the entire subscriber base of the cable system, "one signal tiers" that are purchased by just a few of the cable system's subscribers could result in costing the cable system more in royalties than the income it gets from the few subscribers. As noted above, the Copyright Office has had a long-standing policy against creation of subscriber groups and allocation of gross receipts, except as provided for in §111(d)(1)(B). By extending the comment period in this proceeding, the Office is now re-examining this policy in both the context of merger and acquisition of cable systems and *a la carte* broadcast signals.

III. Extension of Comment Period

Because the royalty issues presented by *a la carte* broadcast signals resemble many of those presented by the merger and acquisition of cable systems, the Copyright Office is reopening this proceeding to receive comment on how compulsory license royalty payments should be made for *a la carte* offerings of broadcast signals by cable operators. Specifically, the Office seeks comment on the following inquiries:

(a) As described in the "System A and System B" example in the 1989 NOI to this proceeding, a "phantom" signal problem occurs when the superstation carried by System B is attributed to all subscribers throughout the merged systems, even though the subscribers in former System A do not actually receive the signal. In the case of *a la carte* broadcast signals, should carriage of each distant broadcast signal be attributed throughout the entire subscription base, even if many subscribers do not actually receive the signal. The Copyright Office has historically required such attribution, based upon its interpretation that the Copyright Act permits only allocation of gross receipts among subscriber groups for partially local/partially distant signals. Does the 1992 Cable Act, or other circumstances, warrant a change in this interpretation? If so, on what basis?

(b) It has been suggested by some that the Copyright Office should permit creation of subscriber groups for *a la carte* broadcast signals, and allow cable operators to allocate gross receipts only to those subscribers who select and receive a particular signal. Thus, for example, if a cable system has 1000 subscribers and only 500 of them choose to receive superstation X, the distant signal equivalent (DSE) value generated by superstation X would only be applied against the gross receipts generated from the 500 subscribers who took the superstation, as opposed to

[2] "Fragmentation" is the practice whereby a cable system separates or "fragments" its system into a series of smaller systems filing separate forms, usually the SA 1-2, and corresponding lower royalty rates. The purpose of fragmentation is to reduce the operator's overall gross receipts and thereby create a substantially lower royalty payment under the cable license.

[3] The royalty rate problems include identifying the signals to which the 3.75% rate applies and in the case of permitted signals, what is the order of the DSE (first, second, third).

applying it against the system's total gross receipts.[4]

One concern with allowing that would be that it would offer the cable system an incentive to pull its distant signals from its basic tier offering, and offer them only as *a la carte* signals, thus reducing the subscriber base from which the royalty is calculated.

The Cable Act of 1992 has made it more difficult for cable systems to restructure their distant signal offerings because it states that, for a basic tier subject to rate regulation, "such basic service tier shall, at a minimum, consist of * * * (iii) any signal of any television broadcast station that is provided by the cable operator to any subscriber, except a signal which is secondarily transmitted by a satellite carrier beyond the local service area of such station." 47 USC 543 (b) (7) (iii).

Therefore, for distant signals that are imported by means other than satellite carrier, if the cable system offers it to one subscriber, it must offer it to all on the basic tier. In 1989, 48.2% of all instances of distant signal carriage on a Form 3 cable system were by means other than satellite carrier. 1989 Cable Royalty Distribution Proceeding, 57 FR 15286, 15294 (1992).

However, 51.8% of distant signal carriage in 1989 was by means of satellite carrier, and those signals could be pulled from the basic tier without violating the 1992 Cable Act. In addition, cable systems that are not subject to basic tier rate regulation because there is effective competition in the system's franchise area, are also free to restructure.

What would be the statutory basis for allowing *a la carte* allocation, and what effect would it have on the total amount of royalties paid?

(c) If the Copyright Office allowed the type of gross receipts allocation described in question (b), what is the proper royalty rate to assess against the gross receipts of each subscriber group? For example, if a cable system carried two distant signals on an *a la carte* basis, one a permitted signal and the other a non-permitted signal at the 3.75% rate, how can it be determined which subscriber group is receiving the less expensive base rate permitted signal, and which group is receiving the more expensive 3.75% rate non-permitted signal? Obviously, there is a powerful incentive for the cable operator to assign the 3.75% rate to the signal with the fewest subscribers, and hence the lowest amount of gross receipts. A similar problem occurs in applying the decreasing rates for permitted signals. Are there any fixed factors which the Copyright Office could apply to prevent the repeated occurrence of applying the lower rate against the higher gross receipts? What effect would that have on the total royalty pool generated by §111?

The Copyright Office requests comment on the questions raised in this extended comment period, as well as any other issues related to compulsory license royalty payments for *a la carte* offerings of broadcast signals.

Dated: December 29, 1994.

Marybeth Peters
Register of Copyrights.

Approved by:

James H. Billington
The Librarian of Congress.

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[4] This example assumes the cable system is an SA-3 form system, and therefore makes royalty payments based on the number of DSE's carried.