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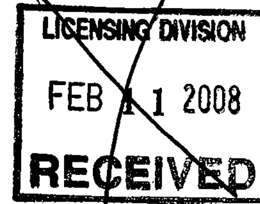

In the Matter of **Definition of Cable System**	)	**Docket No. 2007-11**

COMMENTS OF COPYRIGHT OWNERS

The Office of the Commissioner of Baseball, National Basketball Association, National Football League, National Hockey League, Women's National Basketball Association and The National Collegiate Athletic Association ("Joint Sports Claimants"); Broadcast Music, Inc., American Society of Composers, Authors and Publishers, and SESAC, Inc. ("Music Claimants"); Program Suppliers; National Association of Broadcasters; Devotional Claimants;[1] Public Television Claimants and National Public Radio (collectively "Copyright Owners") submit the following comments in response to the Copyright Office "Notice of Inquiry" published at 72 Fed. Reg. 70529 (December 12, 2007) ("Notice"). The Notice seeks comment on the National Cable & Telecommunications Association's ("NCTA") "Petition for Rulemaking" filed August 17, 2005 ("Petition") to address what NCTA characterizes as the "phantom signal" issue.

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[1] The Devotional Claimants joining in these comments are Amazing Facts, Inc.; American Religious Town Hall Meeting, Inc.; Catholic Communications Corp.; Christian Broadcasting Network; Coral Ridge Ministries Media, Inc.; Cottonwood Christian Center; Crenshaw Christian Center; Crystal Cathedral Ministries; Evangelical Lutheran Church in America; Faith for Today; Family Worship Center Church; In Touch Ministries, Inc.; It Is Written; Joyce Meyer Ministries; Liberty Broadcasting Network; RBC Ministries; Reginald B. Cherry Ministries; Rhema Bible Church; Ron Phillips Ministries; Speak the Word Church International; The Potter's House of Dallas, Inc.; Zola Levitt Ministries, Inc.

INTRODUCTION AND SUMMARY

1. The statutory formula for calculating Section 111 royalties reflects a compromise – a "Form 3" cable system applies minuscule royalty rates (much smaller than Copyright Owners would like) against a "gross receipts" revenue base (much broader than cable operators would like). *See* 17 U.S.C. § 111(d)(1)(B). The cable industry has never been satisfied with minuscule rates alone; it has repeatedly urged the Copyright Office to adopt various theories for narrowing the "gross receipts" component of the statutory formula. *See, e.g.*, *Cablevision Sys. Dev. Corp. v. MPAA*, 836 F.2d 599 (D.C. Cir. 1988), *cert. denied*, 487 U.S. 1235 (1988) (*"Cablevision"*) (rejecting NCTA effort to exclude from "gross receipts" certain subscriber revenue). NCTA's Petition, which recycles a theory first advanced by the cable industry over a quarter-century ago, represents the latest such effort to undo the compromise reflected in the statutory formula.

NCTA characterizes a distant signal that a cable system offers to subscribers in some but not all communities served by that system as a "phantom signal." According to NCTA, it is "inequit[able]," "unreasonable" and "unfair" to require a cable system to calculate its Section 111 royalty based on revenues from system subscribers that do not "actually receive" a particular distant signal. *See* Petition at 3, 4 & 12. To remedy the alleged "inequity," NCTA makes two proposals. It asks the Office to: (1) reduce the instances where two or more facilities are considered a single "cable system" under 17 U.S.C. § 111(f); and (2) allow each Form 3 cable system to calculate its royalty under 17 U.S.C. § 111(d)(1)(B) using multiple "subscriber groups," so that the system may exclude from the statutory formula's revenue component all "gross receipts" paid by system subscribers that did not "actually receive" the distant signal. *See* Notice at 70531. Each of these proposals would require the Office to reverse its longstanding interpretations of Section 111 of the Copyright Act as embodied in existing regulations.

2. More than a decade ago, the Copyright Office correctly concluded that it could not adopt the very same proposals as those set forth in NCTA's Petition because they are inconsistent with Section 111 and thus required Congress to change the Act itself. *See* Copyright Office, *A Review of the Copyright Licensing Regimes Covering Retransmission of Broadcast Signals* at 45-46 (August 1, 1997) ("1997 Report"). Although it has had ample opportunity to do so, Congress has never made those changes. Bills addressing the phantom signal issue have been introduced. *See, e.g.*, H.R. 6164, 98th Cong., 2d Sess. § 202 (1984) (providing that "in the case of any secondary transmissions made to a limited number of subscribers, gross receipts shall be limited to those gross receipts derived from subscribers receiving such secondary transmissions"). However, Congress has not enacted any of those bills into law.

The Office should reaffirm its conclusion that NCTA's phantom signal proposals are inconsistent with existing law and cannot be adopted absent a change in the law. That conclusion is mandated by the plain meaning and legislative history of Section 111 as well as the policies underlying that provision. *See infra* pp. 11-15. Before discussing the proper interpretation of Section 111, Copyright Owners believe it is important to emphasize the following points.

First, Copyright Owners strongly believe that the minuscule rates in the statutory formula are themselves inequitable, even when applied to the broad "gross receipts" revenue base contemplated by law. Those rates produce a total royalty fund that, as the Copyright Office has correctly recognized, falls well short of affording copyright owners fair market value for the use of their works. *See* 1997 Report at vi-vii (Section 111 rates should be amended to reflect fair market value and eliminate undercompensation to authors); *see also id.* at 41-42. Under the statutory formula, the cable industry pays approximately *three-tenths of one percent* of its total

subscriber basic revenues ($33.6 billion in 2007 according to NCTA's website, http://www.ncta.com/Statistic/Statistic/RevenuefromCustomers.aspx (last visited Feb. 8, 2008)) to carry all retransmitted broadcast television signals, which are critical to the success of any cable system.

In fairness, any change to the royalty formula for the Section 111 compulsory license that might be contemplated for the purpose of addressing supposed inequities alleged by NCTA must also be combined with other changes that would produce fair market value for all copyrighted works cable systems exploit pursuant to that license. And any such new royalty formula would need to be geared to a mature cable industry, not to the embryonic collection of "Mom and Pop" systems that existed three decades ago when Congress adopted the original Section 111 formula in the 1976 Act. Besides the legal impediments discussed below, it would be unjust and unreasonable for the Copyright Office to consider altering (or recommend altering) one portion of the Section 111 formula that the cable industry claims to be unfair while the portion that Copyright Owners find unfair remains untouched.

NCTA's proposed scheme of basing royalty payments on receipts from only those subscribers that actually receive a particular signal is, as discussed below, unauthorized by Section 111, and would essentially require starting from scratch and developing an entirely new statutory formula (with compensating changes in the royalty rates) for the Section 111 compulsory license. In the marketplace outside the compulsory license, programmers and cable operators agreeing to such an actual-reception approach often specify different royalty rates depending upon the proportion of subscribers that will receive the programming at issue. For example, it is not uncommon for a programmer and a cable system to agree that the system will pay a license fee of x cents per subscriber per month if the programming is received by at least

90% of the system's subscribers but 2x (or even more than 2x) if it is received by fewer than 50% of the system's subscribers. Such market-negotiated rates result in a total fee that is essentially the same regardless of whether the system offers the programming to all its subscribers or half its subscribers – just as Section 111 requires a cable system to pay the same royalty regardless of whether it offers a distant signal to all its subscribers or some portion of those subscribers.

The terms of the Section 111 compulsory license deprive Copyright Owners of the ability to collect different royalty rates based upon the number of subscribers that actually receive a particular distant signal – in the same way that Section 111 deprives cable systems of the option to limit "gross receipts" to revenues from subscribers that actually receive that signal. If the latter requirement were changed, as NCTA proposes, a corresponding change in the former requirement would be needed, at a minimum, to maintain the balance struck by the compromise that led to the current Section 111 plan.

Second, NCTA leaves the misimpression that, under its subscriber group proposal, two merging Form 3 systems would pay the same royalty post-merger as pre-merger – with NCTA's proposal doing no more than avoiding the payment of "dramatically increased royalties" in those cases. Petition at 3. It should be clear, however, that the effect of adopting NCTA's proposals will actually be to *lessen* the royalty payments that the law now requires many merging systems to pay.

Indeed, as the Office's own examples demonstrate, under NCTA's proposal two Form 3 systems may reduce their Section 111 total royalty obligation post-merger as compared to pre-merger. *See* Notice at 70539-40 (pre-merger, two systems pay $41,401.00 in royalties; post-merger, using the NCTA approach, the combined system pays $35,829.50 in royalties). The

same result generally would follow whenever a Form 3 system with no distant signals merged with a smaller Form 3 system that carried more than one distant signal. The fact that NCTA's subscriber group proposal leads to such a result – which is inconsistent with the very policies underlying Section 111 (*see infra* pp. 14-16) – is itself compelling evidence that the proposal cannot be adopted unless Congress decides to amend Section 111.

Third, NCTA's Petition focuses on the situation where mergers or line extensions result in the combined system offering one or more distant signals in some but not all communities it serves. As the Office has accurately recognized, NCTA's "expansive proposals" are "not limited to those situations;" rather, they would "cover any situation where a cable operator provides a different set of distant signals to different subscriber groups served by the same cable system." Notice at 70531.

NCTA "advocates the creation of 'subscriber groups,' for cable royalty purposes where the operator pays royalties only where distant signals are *actually received* by a particular household." *Id.* (emphasis added). NCTA's concept of "actual reception," if adopted, would permit reduced royalty obligations in a wide variety of situations in addition to those involving phantom signals. For example:

- Switched Video/IPTV. Cable systems are increasingly offering programming on a "switched video" basis – where a subscriber "actually receives" a particular channel only if the subscriber specifically requests that the cable system deliver that channel to his or her set-top box. IPTV technology operates on the same basis. Under NCTA's theory, any cable system that chooses to provide distant signals on a switched video or IPTV basis should be allowed to create subscriber groups based on which subscribers did and did not tune to (and thereby receive) the distant signals offered by the cable system.

Taken to its logical conclusion, NCTA's theory would establish subscriber groups whenever a cable system (regardless of its distribution technology) claimed that some portion of its subscriber base did not view particular distant signals.

- Tiering/A La Carte. NCTA's theory would allow cable operators to use subscriber groups to reduce royalties where a particular distant signal was offered on an expanded basic tier for which only a portion of the system's subscribers paid – or where the signal was offered on an a la carte basis (as FCC Chairman Martin has proposed). In either case, some but not all of the system's subscribers would "actually receive" the distant signal, and different subscriber groups would be created for those that did and did not receive the signal.

- Carriage During a Portion of the Accounting Period. A distant signal offered for only a portion of a six-month accounting period could be considered, under NCTA's theory, to be "actually received" by only those who subscribed to the cable service when the signal was offered. Those who first subscribed to the cable service after the cable system dropped the distant signal or terminated their service before the system commenced carriage of the signal could be considered a separate subscriber group under NCTA's theory since they did not actually receive the signal during the portion of the accounting period when it was carried.

In each of the above examples, NCTA could claim it is unfair to base a Section 111 royalty on gross receipts from subscribers that (a) chose not to request delivery of (and thus do not receive) the distant signal offered as part of a switched video or IPTV service; (b) never viewed the distant signal; (c) did not receive the tier or other service offering with the distant signal; or (d) subscribed only at a time during the six-month accounting period when the distant

signal was not carried. But all these arguments, like NCTA's phantom signal proposals, share the same fallacy – they are predicated upon a concept of actual reception that Congress did not incorporate into the statutory formula. There is no proper basis for the Office to start down the slippery slope on which NCTA's phantom signal proposals are predicated.

Finally, NCTA's phantom signal proposals are simply another variant of the NCTA proposals rejected in *Cablevision.* There, NCTA argued that because Congress intended cable operators to pay Section 111 royalties only for distant non-network programming, "gross receipts" should be limited to revenues paid for that programming alone, *i.e.*, NCTA claimed that cable operators should be able to apportion subscriber fees paid for a tier that contained both distant signals and cable networks between the two types of services and to include in "gross receipts" only the allocated share of revenues supposedly attributable to distant signals. *See Cablevision*, 836 F.2d at 607, 610. In much the same fashion as here, NCTA argued it was unfair and unreasonable to include in "gross receipts" any subscriber fees paid for programming other than distant non-network broadcast programming. *See* Brief for NCTA at 22-26, *Cablevision*, 836 F.2d 599 (D.C. Cir. 1988) (No. 86-5552 and consolidated cases). The Court of Appeals for the D.C. Circuit disagreed, concluding:

> Congress *never* contemplated a precise congruence of the royalties paid and the amount of distant non-network programming actually carried. Instead, Congress picked a *convenient* revenue base . . . .

836 F.2d at 611 (emphasis in original).

As the Court of Appeals in *Cablevision* recognized, Congress never intended to limit "gross receipts" in the statutory formula to revenues attributable solely to the distant non-network programming received by system subscribers. Instead, Congress adopted – as the Court of Appeals recognized – a "convenient revenue base." *Id.* Just as that revenue base includes subscriber revenues attributable to programming other than distant non-network programming, it

also includes fees paid by all of the cable system's subscribers, without regard to whether each distant signal the system carries is actually received by all subscribers (and at all times) during the relevant accounting period. The broader scope of the statutory formula's revenue component is an integral part of the trade-off for royalty rates that amounted to a fraction of one percent in the 1976 Act. *See* Copyright Arbitration Panel, Docket No. 2000-9 CARP DTRA 1 & 2, *Rate Setting for Digital Performance Right in Sound Recordings and Ephemeral Recordings* at 37 (Feb. 20, 2002) (discussing relationship between revenue base and percentage rates in formulas for royalty payments); *see also Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings and Ephemeral Recordings, Final Rule and Order*, Docket No. 2000-9 CARP DTRA 1 & 2, 67 Fed. Reg. 45240, 45249-51 (July 8, 2002); *Digital Performance Right in Sound Recordings and Ephemeral Recordings, Final Rule and Order*, Docket No. 2005-1 CRB DTRA, 72 Fed. Reg. 24084, 24089-90 (May 1, 2007).

3. There is one point on which Copyright Owners and NCTA agree – the need for the Office to act expeditiously on NCTA's Petition. Approximately one-third (or nearly 500) of all Form 3 cable systems are now filing statements of account with subscriber groups; that is a significant increase from the approximately one in ten Form 3 systems in 1983. Source: Cable Data Corporation. As the Copyright Office must be aware, many of these cable systems are abusing the limited right to create subscriber groups for "partially distant signals" (*see infra* pp. 16-18) by routinely calculating royalties as if NCTA's phantom signal proposals were the law, which they clearly are not. Even when the Office warns cable operators that their phantom signal royalty calculations violate Section 111 and existing Office regulations, the cable operators disregard the warnings, often claiming that the issue is undecided because NCTA's Petition is pending. Unless and until the Office takes decisive action to reject that Petition, cable

operators will continue refusing to comply with the law. And Copyright Owners will not receive even the minimal compensation to which they are entitled under Section 111.

NCTA's Petition also underscores the need for the Office to take two additional actions. *First*, in its Section 110 Report dealing with the comparable Section 119 compulsory license, the Office found that

> the lack of an audit provision contributes to the harm inflicted on the copyright owners because it does not allow copyright owners an opportunity to evaluate whether satellite carriers have made full and accurate payments in accordance with the law. Thus, we support the request for an amendment to provide for a negotiated audit right in line with similar provisions in other statutory licenses.

See Copyright Office, *Satellite Home Viewer Extension and Reauthorization Act § 110 Report* at vi-vii (Feb. 2006); *see also id.* at 45-46. The same finding applies with equal force to Section 111. Copyright owners affected by the Section 111 compulsory licenses should have the right to audit cable operators as do copyright owners affected by other compulsory licenses. *See*, *e.g.*, 37 C.F.R. §§ 260.5 and 260.6 (verification of statements of account and royalty payments from pre-existing subscription services); 37 C.F.R. §§ 261.6 and 261.7 (verification of statements of account and royalty payments from certain eligible nonsubscription services); 37 C.F.R. §§ 262.6 and 262.7 (verification of statements of account and royalty payments from certain eligible nonsubscription services and new subscription services).

Absent the right to audit, copyright owners often are unable to determine (without commencing costly and time-consuming litigation) whether cable operators are calculating their Section 111 royalties in accordance with the law. For example, cable operators currently report "gross receipts" of about $6 billion (less than 20% of the industry's $33.6 billion in subscriber basic revenues). Source: Cable Data Corp. and NCTA's Industry Statistics for Revenue from Customers, http://www.ncta.com/Statistic/Statistic/RevenuefromCustomers.aspx (last visited

Feb. 8, 2008). Copyright owners should be entitled to determine whether cable operators are calculating "gross receipts" using the type of theories set forth in NCTA's Petition – particularly where those cable operators refuse even to respond to Office requests to justify particular royalty calculations.

Second, the Office should post on its website an up-to-date list of cable Statements of Account ("SOA") that, based upon Licensing Division review, do not calculate royalties in accordance with Office regulations, including regulations that prohibit the use of subscriber groups for phantom signals. Each year the Licensing Division receives and reviews more than 12,000 SOAs. A principal purpose of that review is to determine whether each cable operator has properly calculated its royalty payment. Copyright owners should not be required to search through the tens of thousands of pages of documents contained in Copyright Office SOA files (that are not always readily available) to locate SOAs that the Licensing Division believes do not comply with Office regulations. By posting the relevant information on its website, the Copyright Office will help ensure that copyright owners receive the benefit of the Licensing Division's efforts (the costs of which are deducted from copyright owner royalties) without incurring additional and unnecessary costs.

DISCUSSION

I. The Copyright Office Should Confirm Its Longstanding Interpretation of the Definition of "Cable System" in Section 111(f) of the Copyright Act of 1976.

1. Section 111(f) defines the term "cable system." The final sentence of that definition states:

> For purposes of determining the royalty fee under subsection (d)(1) [of Section 111], two or more cable systems in contiguous communities under common ownership or control *or* operating from one headend shall be considered one system.

17 U.S.C. § 111(f) (emphasis added). In 1978, shortly after passage of Section 111(f), the Office adopted a regulation making clear that "two or more facilities" would be considered as a single "cable system" if the facilities are either "(A) in contiguous communities under common ownership or control *or* (B) operating from one headend." *Final Regulations in Docket No. RM 77-2*, 43 Fed. Reg. 958, 958 & 961 (1978) ("1978 Regulations") (emphasis added), *adopting* 37 C.F.R. §§ 201.11(a)(3)(ii)(A)-(B), *now codified at* 37 C.F.R. § 201.17(b)(2)(i)-(ii). *See Notice of Inquiry in Docket No. RM 89-2*, 54 Fed. Reg. 38390, 38390 (1989) (noting the regulation "exactly tracks the text of the statute, except that letter designations were inserted in the text to show our understanding of the congressional intent"). As the Office also noted, the regulation "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." *Id.*

NCTA requests the Office substitute the word "and" for the word "or" in Section 111(f) of the Act and Section 201.17(b)(2) of the Office's regulations so that two or more facilities would be considered a single system "only where the facilities were in contiguous communities, under common ownership and control, and operated from one headend." NCTA Petition at 10 (emphasis in original). *See also id.* at 11 ("Under NCTA's proposed rule, cable facilities serving multiple communities would be treated as a single system only when three distinct conditions are satisfied: (i) the facilities are in contiguous communities; (ii) the facilities are under common ownership or control; and (iii) the facilities are operating from the same headend."). As the Office correctly observes in its Notice at 70532, NCTA's proposed rule change "raises significant statutory interpretation issues." In fact, the NCTA proposal requests the Office to turn a blind eye to the plain meaning of the statutory language.

2. Congress used the word "or" in the Section 111(f) definition of "cable system" nine times. NCTA's apparent view is that Congress intended "or" to have a disjunctive meaning the first eight times the term appears in that definition but not the last time. NCTA's view is squarely contrary to well-established canons of statutory construction, as set forth in *In re Espy*, 80 F.3d 501 (D.C. Cir. 1996):

> "Canons of construction ordinarily suggest that terms connected by a disjunctive be given separate meanings," *Reiter v. Sonotone Corp.*, 442 U.S. 330, 339 (1979), and a statute written in the disjunctive is generally construed as "setting out separate and distinct alternatives." *United States v. Behnezhad*, 907 F.2d 896, 898 (9th Cir. 1990). Thus, Congress' use of the disjunctive "or" in this section (twice) indicates it gave the independent counsel a choice between going to the Attorney General or to the court for a referral and that the Attorney General or the court could grant such a referral.

Id. at 505; *accord Chao v. Day*, 436 F.3d 234, 236 (D.C. Cir. 2006) ("We reject Day's interpretation of § 1002(21)(A)(i) because it does violence to the statutory text. The plain language of that text connects the two classes of 'fiduciaries' with the disjunctive 'or' – not the conjunctive 'and.'") (citing *Garcia v. United States*, 469 U.S. 70, 73 (1984) ("Canons of construction indicate that terms connected in the disjunctive in this manner be given separate meanings.")). *See also Nat'l R.R. Passenger Corp. v. United States*, 338 F. Supp. 2d 22, 27-28 (D.D.C. 2004) (striking down agency decision to construe statutory term "and" to mean "or," noting "if the statutory language no longer fits the infrastructure of the industry, the IRS needs to ask for congressional action to bring the statute in line with today's reality. It cannot create an ambiguity that does not exist or misinterpret the plain meaning of statutory language to bend an old law toward a new direction"), *aff'd*, 431 F.3d 374 (D.C. Cir. 2005).

3. This is not one of those "rare" circumstances where courts have construed the term "or" in a statute to mean "and" (*see Nichols v. Bd. of Trs. of Asbestos Workers Local 24*

Pension Plan, 835 F.2d 881, 890 n.79 (D.C. Cir. 1987) (citing *DeSylva v. Ballentine*, 351 U.S. 570, 573 (1956)) – because according the term "or" its disjunctive meaning in this situation would not "be demonstrably at odds with the will of Congress." *Unification Church v. INS*, 762 F.2d 1077, 1084 (D.C. Cir. 1985) (citation omitted); *see also United States v. Moore*, 613 F.2d 1029, 1040 (D.C. Cir. 1979) ("or" means "or" unless such a construction would "frustrate legislative intent"); *Mineral Policy Ctr. v. Norton*, 292 F. Supp. 2d 30, 42 (D.D.C. 2003) ("It is clearly established that '[i]n statutory construction the word 'or' is to be given its normal disjunctive meaning unless such a construction renders the provision in question repugnant to other provisions of the statute,' . . . or 'the context dictates otherwise'") (citation omitted).

As the Office has recognized, the purpose of the statutory language at issue (the last sentence of Section 111(f)) was to avoid the "'artificial fragmentation' of systems (a large system purposefully broken up into smaller systems) and the consequent reduction in royalty payments to copyright owners." Notice at 70530 (citing 1978 Regulations at 958). In fact, Congress added that provision at the specific request of copyright owners, using virtually the identical language that copyright owners proposed (including the term "or" rather than "and"). *See Hearings Before the Senate Subcomm. on Patents, Trademarks and Copyrights on S. 136*, 93d Cong., 1st Sess. 302-03 (1973) ("1973 Senate Hearings") (statement of Jack Valenti).

In its 1997 Report at 45, the Office correctly recognized that its interpretation of the last sentence of Section 111(f) has "worked well to avoid artificial fragmentation," the purpose for which the statutory language at issue was adopted. NCTA never disputes this.[2] To the contrary,

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[2] NCTA argues that the problem instead is that the existing definition "artificially consolidates" systems. Petition at 4, 11. In effect, it suggests that the only issue for congressional concern should be to prevent cable operations already counted as a single system from fragmenting further in an attempt to avoid statutory royalty obligations. But NCTA's argument considers "fragmentation" too narrowly. The statutory definition expressly requires "two or more cable

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NCTA acknowledges that the "purpose of this provision, according to the Act's legislative history, is to avoid the 'artificial fragmentation' of systems (and the consequent reduction in royalty payments)" and that the existing regulation does "inhibit[]" "artificial fragmentation." Petition at 2 & 4. Under these circumstances, the Office's reading of the term "or" to mean "or" is fully consistent with congressional intent.

4. NCTA nonetheless claims, as justification for a rule change, that the existing regulation "inhibit[s]" the "legitimate practice of 'clustering,'" where "multiple system cable operators attempt to obtain management economies by acquiring systems in close proximity to each other." Petition at 4. The facts do not support NCTA's claim – the number and size of clusters actually have risen from 97 in 1994 (with 20.1 million subscribers) to 108 in 2003 (with 53.6 million subscribers). Petition at 8; *see also* Notice at 70530 ("At the end of 2004, there were 118 clusters with approximately 51.5 million subscribers"). The notion that any cable operator would base a decision concerning clustering on its Section 111 royalty payments (which, as noted above, amount to less than one-half of one percent of total subscriber basic revenues) is itself incredible.[3] Certainly NCTA offers no evidence that any cable operator has in fact done so.

In any event, nothing in the legislative history of Section 111 reflects a congressional interest to promote clustering. Thus, even if the existing regulation did "inhibit[]" legitimate

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systems" to be treated as a single system for the purpose of calculating license fees. 17 U.S.C. § 111(f). Congress thus directed that separate systems be combined for royalty calculation purposes, and did not limit its mandate to NCTA's "single technically, managerially, and operationally integrated entity (as reflected by the use of a single headend)." Petition at 11.

[3] Indeed, when cable systems consider whether to merge or to acquire or commence clustered operations, they must weigh the expected economic advantages against all known costs, including the existing legal obligations to pay licensing fees, however small. NCTA's proposal would allow cable systems to capture all the benefits of consolidation while avoiding statutorily mandated license fees.

clustering, as NCTA argues, that fact would not support construing the term "or" to mean "and" because there is no legislative policy reflected in that Act or indeed any other law that favors clustering. Indeed, it is far from clear that the government should take action designed to promote clustering. *Cf.* FCC, *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, Eighth Annual Report*, 17 F.C.C.R. 1244, 1304-05 (Jan. 14, 2002) (summarizing procompetitive and anticompetitive effects of clustering).

Even if the existing regulation results in two merging systems paying more in royalties than if they remained as two smaller systems, that result is fully consistent with the legislative intent to avoid artificial fragmentation. The royalty schedule is based mainly on ability to pay, where larger systems (such as those that enjoy the efficiencies, or to use NCTA's term "management economies," of clustering) are in a position to pay higher royalties than those smaller systems that do not enjoy such efficiencies or "management economies." *See, e.g.*, H. Rep. 94-1476, at 96, *reprinted in* 1976 U.S.C.C.A.N. 5659, 5711 (Section 111 royalty schedule reflects congressional view that "smaller cable systems may be less able to shoulder the burden of copyright payments than larger systems . . .").

II. The Office Should Confirm Its Longstanding Interpretation that Section 111(d)(1)(B) Permits Neither the Creation of Subscriber Groups, Nor the Proration (Allocation) of Gross Receipts, Based on "Phantom Signals."

1. The statutory formula for calculating "Form 3" royalties requires each system to multiply (1) its "gross receipts" from all subscribers in all communities the system serves, by (2) the total "distant signal equivalents" ("DSE") that the system carries by (3) the statutory DSE royalty rates. *See* 17 U.S.C. § 111(d)(1)(B) (reproduced in Appendix A). Section 111 specifies only one situation where a cable system may "prorate" or "allocate" its "gross receipts" (and thereby reduce its royalty) – where the system carries a "partially distant" signal, *i.e.*, a signal

that is distant in some but not all communities served by the cable system. *Id.* In such cases, the cable system may create separate "subscriber groups" and multiply the "gross receipts" from each group by the DSEs for that group. *See* 37 C.F.R. § 201.17(g).

NCTA wants the Office to permit proration (allocation) of "gross receipts" – and the creation of subscriber groups – in additional circumstances beyond the one specified in Section 111. NCTA focuses on possible phantom signal situations where two cable systems (with different distant signal complements) merge and become a single system within the meaning of Section 111(f) – although, as the Notice recognizes, NCTA's theory would apply in a variety of situations beyond merger. NCTA claims it is "inequitable" to require the merged system to calculate its royalties as if the system carried all distant signals in all communities. But the plain language of Section 111(d)(1)(B) requires that a cable system do exactly that – multiply total gross receipts by total DSEs even though the system makes some or all DSEs available to only a portion of the system's subscribers.

The Act does not invest the Copyright Office with authority to create additional exceptions where proration (and thus royalty reduction) would be allowed simply because NCTA claims the existing statutory formula is inequitable. As the Office correctly concluded over twenty years ago:

> The Copyright Office's interpretation of the Copyright Act in these circumstances has been that, unless the signal is partly distant only to some subscribers . . . copyright fees for distant signals carried to any part of a cable system as defined in the Copyright Act . . . must be computed on the basis of total, aggregated gross receipts from all subscribers to the system. This position is based upon the lack of any express provision allowing allocation of gross receipts, except for partially distant-partially local signals.

Interim Regulations in Docket No. RM 83-3, 49 Fed. Reg. 14944, 14948 (1984). *See also* Notice at 70535; Letter dated April 3, 1981 from Copyright Office General Counsel to Counsel for

Service Electric Cable TV, Inc. ("It is clear that the Copyright Act does not simply require royalty payments on the basis of distant signals actually carried to each subscriber of a system. The Act establishes a minimum payment even for systems that carry no distant signals. In calculating the royalty fee for distant signals, there is no provision for applying the DSE to a portion of gross receipts except in the case of partially distant stations."). In short, the Office has consistently and correctly concluded that Congress in the 1976 Act created only one exception to the rule that gross receipts from all system subscribers must be included in the revenue component of the statutory formula – partially-distant signals. It did not create, and the Office has no authority to create, an additional exception for partially-carried distant signals.[4]

2. Traditional canons of statutory construction fully support the Office's refusal to create any additional exception beyond the partially-distant exception included in Section 111 – for phantom (partially-carried) signals or otherwise. As the Supreme Court stated in the analogous case of *TRW Inc. v. Andrews*, 534 U.S. 19 (2001):

> Where Congress explicitly enumerates certain exceptions to a general prohibition, additional exceptions are not to be implied, in the absence of evidence of a contrary legislative intent.

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[4] When Congress created the statutory royalty fee under Section 111(d), it "drew a crucial distinction between local and distant broadcast signals." *Cablevision*, 836 F.2d at 603 (*citing* H.R. Rep. No. 1476, 94th Cong., 2d Sess. 90). Section 111(d)(1)(B)(i), for example, imposes the minimum royalty fee for the privilege of carrying distant signals, and Section 111(d)(3)(A) provides that royalties are to be paid out only to copyright owners of works retransmitted on distant signals. In short, the royalty fees cover distant broadcast signals, not local signals.

In furtherance of this fundamental structure, Congress also created the "partially distant" exception to which NCTA refers. *See* Petition at 13. This exception ensures that cable systems serving subscribers "located partly within and partly without the local service area of a primary transmitter" may calculate gross receipts for royalty purposes only on receipts from subscribers receiving the station on a distant signal basis. 17 U.S.C. § 111(d)(1)(B). It provides no support for NCTA's much broader community-specific proposal, which would apply exclusively to subgroups of subscribers for whom the retransmitted station would be a distant signal.

Id. at 28 (quoting *Andrus v. Glover Constr. Co.*, 446 U.S. 608, 616-617 (1980)). *See also United States v. Brockamp*, 519 U.S. 347, 352 (1997) ("'explicit listing of exceptions' to running of limitations period considered indicative of Congress' intent to preclude 'courts [from] read[ing] other unmentioned, open-ended, 'equitable' exceptions into the statute'") (citation omitted); *Natural Res. Def. Council v. EPA*, 489 F.3d 1364, 1374 (D.C. Cir. 2007) (fact that Congress has "enumerated specific exceptions" in the statute "indicates that Congress has spoken on the question and has not provided" the agency with authority to create additional exceptions); *Natural Res. Def. Council v. EPA*, 489 F.3d 1250, 1259 (D.C. Cir. 2007) (court held that where Congress enumerated four exemptions in the statute, agency had no authority to create a fifth exemption, noting that "there is no reason the usual tools of statutory construction should not apply"); *Schumann v. CIR*, 857 F.2d 808, 811-12 (D.C. Cir. 1988) ("Congress' specific enumeration of certain exceptions indicates that no other exceptions were intended.").

3. The legislative history of the 1976 Act also supports the Office's refusal to create an additional exception for partially-carried (phantom) signals. *First,* Congress explained that its definition of the term "cable system" in Section 111(f) would impact not only the classification of a cable system as Form 1, 2 or 3 but also the royalty fee that the system must calculate:

> Further, the definition [in 17 U.S.C. § 111(f)] provides that, in determining the applicable royalty fee *and* system classification under subsection (d)(2)(B), (C), or (D) cable systems in contiguous communities under common ownership or control or operating from one headend are considered as one system.

H. Rep. 94-1476, at 99, *reprinted in* 1976 U.S.C.C.A.N. 5659, 5714 (emphasis added). As this legislative history indicates, the statutory definition of a single system governs both whether a system must file as Form 1, 2 or 3 and how the royalty fee for that system must be calculated. Under NCTA's subscriber group proposal, however, that definition would apply only to the former and not the latter; a Form 3 system would calculate its royalty as a series of separate

systems rather than as a single system – although NCTA would apply the minimum fee requirement in Section 111(d)(1)(B)(i) only to the entire system and not to each of its component systems. *See* Notice at 70532 (noting that under NCTA's proposal the cable system would use its total gross receipts to determine whether it is a Form 1, 2 or 3 system; however, "the royalties due for the system may be computed on a community-by-community basis . . . .") The legislative history quoted above demonstrates that Congress never intended that result.

Second, the possibility that phantom signals might occur is not a recent phenomenon. Not only long before, but even at the very time Congress was debating Section 111, cable systems were offering distant signals to some but not all of their subscribers. *See, e.g.*, *Telerama, Inc.*, 3 F.C.C. 2d 585 (1966) (FCC refused to allow cable system to carry the same complement of distant signals in all communities served by that system); *Mission Cable TV, Inc.*, 4 F.C.C. 2d 236 (1966) (same). Copyright owners pointed specifically to the cable systems in the *Telerama* and *Mission Cable* cases as examples that would come within the final sentence of Section 111(f), which would treat each as a single system. *See* 1973 Senate Hearings at 302 (Statement of Jack Valenti). Nevertheless, nothing in the legislative history of the 1976 Act suggests that NCTA or any other cable representative urged Congress to create an exemption for partially-carried (phantom) signals comparable to the exemption they sought for partially-distant signals. As the Office observed in an analogous context,

> That Congress *might* have legislated additional exceptions to a full DSE value if cable system operators had argued for additional exceptions cannot be demonstrated now. No support for this argument can be found in the relevant congressional reports. The Copyright Office cannot issue regulations to change a statutory definition based upon mere speculation about congressional reaction to arguments that were never presented to Congress.

Final Regulations in Docket No. RM 79-4, 45 Fed. Reg. 45270, 45272 (1980) (emphasis in original) (concluding that the Office has no authority to create additional exceptions where DSEs may be prorated (allocated) beyond those expressly referenced in Section 111(f) definition of DSE).

4. NCTA says that the Office's current regulations that prohibit the creation of subscriber groups for phantom signals are inconsistent with a "fundamental principle" underlying Section 111 – that a cable system should be required to pay royalties only for "actual signal carriage" and thus "use" of copyrighted works. *See* Petition at 13-14. Citing various provisions of Section 111 and its legislative history, NCTA maintains that the "requirement for actual carriage permeates the Copyright Act." *Id.* at 14.

As the Office has recognized, the legislative history cited by NCTA "does not explicitly support NCTA's suggestions nor is it obvious how this language is relevant to [NCTA's] subscriber group proposal . . . ." Notice at 70532. The same may be said of the statutory provisions that NCTA cites – none of which says anything more than that a cable system must pay royalties where it makes secondary transmissions of broadcast signals. Even more importantly, no one has ever suggested that a Form 3 system should pay royalties for a distant signal that it does not actually carry (except in the case of a system subject to the statutory minimum fee). But NCTA's very definition of phantom signal is that the cable system *does carry* (use) that signal – it simply chooses to make the signal available to only some of its subscribers.

It is uncontroverted that if a Form 3 system chooses to make a distant signal available for only a portion of a six-month accounting period, the system must calculate its royalty as if it carried that signal for all six months – that is, it must include in "gross receipts" subscriber

revenues from all six months. In the same way, if a Form 3 system chooses to make a distant signal available to only a portion of its subscribers, the system must calculate its royalty as if it made that signal available to all subscribers – that is, it must include in "gross receipts" revenues from all subscribers. This result is fully consistent with Section 111. As noted above at page 8, the Court of Appeals in *Cablevision* concluded that "Congress *never* contemplated a precise congruence of the royalties paid and the amount of distant non-network programming actually carried." 836 F.2d at 611 (emphasis in original). *See also* Brief for Copyright Office at 34, *Cablevision*, 836 F.2d 599 (D.C. Cir. 1988) (No. 86-5552 and consolidated cases) ("Congress intended that the calculation of royalty fees under section 111 would be based upon a formula which is only loosely related to the amount of protected programing [sic] actually carried by cable systems to subscribers . . . . When Congress enacted section 111, it effected a trade-off. The royalty schedule was not crafted to reflect actual carriage; on the other hand, the statutory formula provided for the payment of copyright royalties which NCTA itself conceded to be 'minimal.'") (citation omitted).

5. NCTA's proposal, based as it is on cable operators' unfettered discretion to define community groupings for the purpose of reducing royalties, would introduce "[m]ethodological wrangles and monitoring expenses far in excess of those required under the Copyright Office's regulation." *Cablevision*, 836 F.2d at 612. This concern is especially acute because, as noted above, the current statement of account forms fail to require the reporting of critical information that would permit the Office and others adequately to evaluate their compliance with statutory and regulatory requirements. Given the fact that cable operators already generally resort to self-help by underpaying royalties where there is a question as to the applicability of particular royalty calculation requirements, *see* Notice at 70536, changing the rule (or announcing a policy

of not challenging SOAs that prorate royalties across self-defined communities, *see* Notice at 70531) would fundamentally undermine the entire royalty process, and introduce a new wave of uncertainty and disputes.

CONCLUSION

For the reasons stated above, the Copyright Office should expeditiously deny NCTA's phantom signal Petition.

February 11, 2008

Respectfully submitted,

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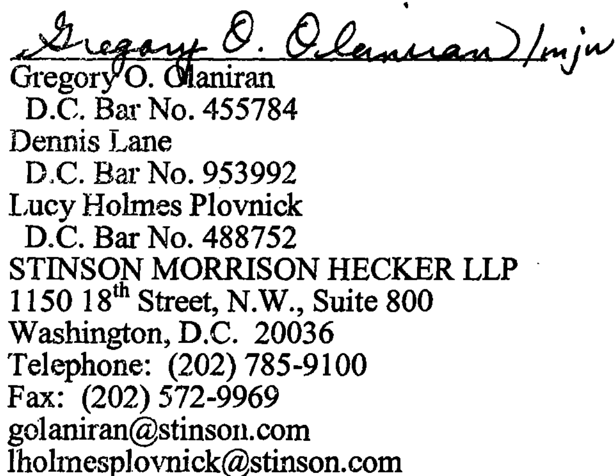

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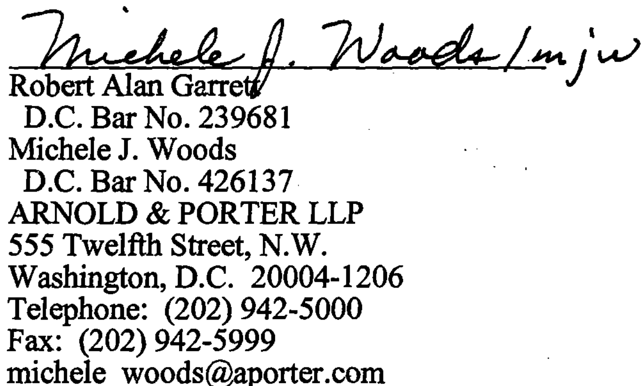

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EXHIBIT A

17 U.S.C. § 111

LIMITATIONS ON EXCLUSIVE RIGHTS: SECONDARY TRANSMISSIONS

. . .

(d) STATUTORY LICENSE FOR SECONDARY TRANSMISSIONS BY CABLE SYSTEMS.--

(1) A cable system whose secondary transmissions have been subject to statutory licensing under subsection (c) shall, on a semiannual basis, deposit with the Register of Copyrights, in accordance with requirements that the Register shall prescribe by regulation--

. . .

(B) except in the case of a cable system whose royalty is specified in subclause (C) or (D), a total royalty fee for the period covered by the statement, computed on the basis of specified percentages of the gross receipts from subscribers to the cable service during said period for the basic service of providing secondary transmissions of primary broadcast transmitters, as follows:

(i) 0.675 of 1 per centum of such gross receipts for the privilege of further transmitting any nonnetwork programming of a primary transmitter in whole or in part beyond the local service area of such primary transmitter, such amount to be applied against the fee, if any, payable pursuant to paragraphs (ii) through (iv);

(ii) 0.675 of 1 per centum of such gross receipts for the first distant signal equivalent;

(iii) 0.425 of 1 per centum of such gross receipts for each of the second, third, and fourth distant signal equivalents;

(iv) 0.2 of 1 per centum of such gross receipts for the fifth distant signal equivalent and each additional distant signal equivalent thereafter; and

in computing the amounts payable under paragraphs (ii) through (iv), above, any fraction of a distant signal equivalent shall be computed at its fractional value and, 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; and

. . .