

**Before the
COPYRIGHT OFFICE
LIBRARY OF CONGRESS
Washington, D.C.**

**In the Matter of
Cable Compulsory Licensing
Reporting Practices**

Docket No. RM 2005-6

REPLY COMMENTS OF PROGRAM SUPPLIERS

The Motion Picture Association of America, Inc. (“MPAA”), on behalf of its member companies and other producers and/or distributors of movies, series and specials broadcast by television stations (“Program Suppliers”), hereby submits the following reply comments (“Reply Comments”) in response to the Notice of Inquiry (“NOI”) issued by the Copyright Office (“Office”) and published in the Federal Register on August 10, 2006. *See Cable Compulsory License Reporting Practices*, 71 Fed. Reg. 45749 (August 10, 2006). The Office issued the NOI to address the issues raised in Program Suppliers’ Petition for Rulemaking filed on June 7, 2005 (“Petition”). In response to the NOI, Program Suppliers filed their Comments of Program Suppliers on September 25, 2006 (“PS Comments”).

These Reply Comments address the comments of the National Cable & Telecommunications Association (“NCTA”) and American Cable Association (“ACA”).

The Devotional Claimants,¹ the Music Claimants (Broadcast Music, Inc., the American Society of Composers, Authors and Publishers, and SESAC, Inc.) and the Canadian Claimants join in Program Suppliers' Reply Comments. The Joint Sports Claimants ("JSC") also support Program Suppliers' Reply Comments, but will be filing separate reply comments.²

I. Introduction

After more than twenty years without any significant change to the statement of account ("SOA") forms, it is both appropriate and necessary for the Office to update the forms and regulations to keep step with the significant changes in the cable industry. As JSC point out, when the Office promulgated its original regulations and developed the existing SOA forms in the 1970s, it acknowledged that they were subject to reconsideration as circumstances changed and practical experience was obtained. JSC Comments at 2 (citing *Compulsory License for Cable Systems*, 43 Fed. Reg. 958 (Jan. 5, 1978)). Program Suppliers, both in the Petition and their Comments, explain that the numerous changes experienced by the cable industry since that time that require

¹ The Devotional Claimants joining in Program Suppliers' Reply Comments are Liberty Broadcasting Network, Inc., Coral Ridge Ministries Media, Inc., Oral Roberts Evangelistic Association, Crystal Cathedral Ministries, Inc., The Christian Broadcasting Network, Inc., In Touch Ministries, Inc., Family Worship Center Church, Inc., Amazing Facts, Inc., American Religious Town Hall, Inc., Billy Graham Evangelistic Association, Catholic Communications Corporation, Cottonwood Christian Center, Crenshaw Christian Center, Evangelistic Lutheran Church in America, Faith For Today, Inc., It Is Written, Joyce Meyer Ministries, Inc., Rhema Bible Church, Ron Phillips Ministries, Speak The Word Church International, The Potter's House of Dallas, Inc., and Zola Levitt Ministries.

² Program Suppliers support JSC's comments regarding the need for verification that cable operators offer to subscribers the rate that they use to compute their SOA royalty payments. Comments of Joint Sports Claimants ("JSC Comments") at 2-3.

reevaluation and reformation of the antiquated SOA forms to reflect today's industry practices.

NCTA and ACA, the two cable organizations that filed comments in this proceeding, do not dispute that the cable industry has changed significantly since the Office first promulgated the cable royalty regulations and adopted the existing SOAs. Yet, NCTA and ACA, other than supporting one minor change — to require county information on the SOAs — adamantly oppose any modernization of the SOAs. NCTA Comments at 9; ACA Comments at 4.

NCTA's and ACA's desire to keep the SOAs static ignores the Office's demonstrated, substantial interest in aligning its compulsory license operations with current industry practices. *See, e.g., Retransmission of Digital Broadcast Signals Pursuant to the Cable Statutory License*, 71 Fed. Reg. 54948 (Sept. 20, 2006) (requesting comments on proper royalty treatment of digital broadcast signals); *see also Electronic Payment of Royalties*, 71 Fed. Reg. 45749 (Aug. 10, 2006) (updating method for royalty payments). Moreover, they ignore the Office's plans to overhaul many of its processes, including the filing of SOA forms. *See Copyright Office Strategic Plan 2004-2008*, Introduction and p. 26 (noting plans to eliminate paper-based operations, to be replaced by new electronic SOAs in 2007-2008).

The switch to electronic billing and payment practices in the cable industry negates NCTA's and ACA's efforts to overstate the burden that would purportedly inure to cable operators should Program Suppliers' proposals be adopted. *See* NCTA

Comments at 6 (contending that supplying rate and subscriber information for multiple dwelling units (“MDUs”) would be “enormously difficult”); ACA Comments 2 (stating that Program Suppliers’ proposed changes “would add thousands and thousands of hours each year to compliance burdens”). To the contrary, most of the requested changes would require no more than transfer of information already collected and maintained electronically to another electronic file.

Further, NCTA’s and ACA’s contentions fail to acknowledge that much of the proposed additional SOA information is either (1) currently required by the Office’s regulations or by FCC regulations, or (2) already maintained electronically by cable operators in their regular course of business. *See* Comments of Program Suppliers (“PS Comments”) at 12-14. When the SOAs were created, cable operators had far less sophisticated (if any) computer operations than they do now. Information about subscribers and rates, the meat of the additional information being requested, can be readily updated and compiled from existing electronic files. The Office should not allow NCTA’s and ACA’s unsupported exaggerations regarding reporting burdens to dissuade it from updating the more than twenty-year-old SOAs. Indeed, it is far more likely that the burden on all parties, including cable operators, of finding and correcting errors would be alleviated if information provided on the SOAs are easier to understand as Program Suppliers have proposed.

NCTA and ACA fail to acknowledge that, unlike other compulsory licenses, the cable compulsory license does not afford either the Office or copyright owners with a

right to audit. Petition at 2. Absent that right, it is extremely difficult to ascertain compliance based upon a mere review of the SOAs as they currently exist, particularly given that cable operators often stonewall attempts to obtain relevant information that would supplement SOA information. *See text infra*, at 16-17.

Program Suppliers' proposals do not contemplate substantive regulatory changes, but, rather, are little more than requests for clarification of the Office's existing rules. As explained below, Program Suppliers' proposed modifications and clarifications are consistent with the language of Section 111, the Office's regulations, and prior Office Orders, and do not impose any legal obligation outside of the current law. Therefore, Program Suppliers' proposed changes are warranted, and should be adopted by the Office.

II. Program Suppliers' Proposed Changes to the SOAs are Consistent with the Office's Rules and Orders, and Necessary in Light of Cable Industry Changes.

The Petition proposed many changes to the SOAs that are designed to adapt current filing practices to the substantial changes that have taken place in the cable industry since the current SOAs were developed in the 1970s. Program Suppliers' proposed changes allow the SOAs to better match current industry conditions while closely tracking the Office's existing regulations.

A. The Office Has Acknowledged that Reported Gross Receipts and Subscriber and Rate Information Should be Comparable.

The Office has been clear that the subscriber and rate information in Space E of the SOAs was intended to provide a means to roughly approximate the gross receipts

reported in Space K. *See* PS Comments at 6; Petition at 4. NCTA agrees as to this intent, and neither disputes the variances between the data reported in these two sections nor the significance of the variances. NCTA Comments at 5. Instead, NCTA conjures up, without any record support, reasons why variances might occur. Even accepting such conjectures as possible reasons, NCTA presents no evidence that those reasons would remotely explain the size of the variances. ACA claims three reasons for denying Program Suppliers' request: no legal basis, no showing that smaller systems have similar variances in the data reported in Space E and Space K, and that a process is already in place to obtain necessary information. ACA Comments at 5-6. As with NCTA's unsupported assertions, ACA's contentions are equally invalid.

1. The Wide Variation that Exists Between Space E and Space K Data Warrants a Change in the SOA Forms.

Initially, ACA's contention that "there is no basis in law" for Program Suppliers' proposed changes to Space E and Space K, ACA Comments at 5, should be dispatched. All SOAs are required to be verified to the effect that all statements of facts reported in the particular statement are true, correct, and complete and made in good faith. In signing that verification, cable operators are subject to criminal sanctions, as well as copyright infringement liability, for any false, incorrect, incomplete statements or for statements not made in good faith. *See* 37 C.F.R. § 201.17(e)(14); Forms SA1-2 and SA3, Space O, and General Instructions at p.i; *see also* 18 U.S.C. § 1001. Program Suppliers have highlighted a problem that implicates the validity of that verification because on the face of the SOAs, and using only information supplied by cable operators,

a wide variance exists between Space E and Space K information. As the Office has a duty to assure that the information reported (and the basis on which royalties are paid) is true, correct, complete, and made in good faith, it has the authority to promulgate regulations and adjust the SOAs in a manner that will better serve that goal than the current system. *See* 17 U.S.C. § 111(d)(1)(a); NCTA Comments at 3.

Contrary to ACA's assertions, ACA Comments at 6, Program Suppliers have already presented considerable evidence on the record to support their request. Nonetheless, in response to ACA's assertions, Program Suppliers undertook an expanded analysis of the variance between Space E and Space K gross receipts information to include analyses of the top seventy-five systems separately for Form SA1, Form SA2, and Form SA3 systems for the accounting periods 2001-1 through 2004-2.³ The results of these analyses confirm that the variances are large across all types of systems and strongly suggest a pattern of underreporting in Space K with the result that royalty payments are markedly lower than would be required by use of reported Space E information. It is worth noting that neither NCTA nor ACA provide even a sliver of evidence to support their unsubstantiated claims that no problem exists, despite the fact that the data which Program Suppliers used is readily available.

³ For the expanded analysis, *see* Exhibit A, attached hereto. Form SA1 systems were selected based on subscribership and Form SA2 and SA3 systems were selected on the basis of royalties paid. The selected Form SA1 systems represented 1.62% of the total Form SA1 systems and 70.85% of the total Form SA1 subscribers for the eight accounting periods. The selected Form SA2 systems represented 4.21% of the total Form SA2 systems for the period studied, but they accounted for 11.33% of the total Form SA2 royalties for that period. Finally, the selected Form SA3 systems represented 4.34% of the total Form SA3 systems, but they accounted for 31.84% of the total Form SA3 royalties for that period. *See* Exhibit B, attached hereto.

As an initial matter, for the accounting periods that Program Suppliers examined, the average number of systems per accounting period with Space E versus Space K variance (positive or negative) of greater than 10% was as follows: Form SA1 systems-38 (51%); Form SA2 systems-31 (41%); and Form SA3 systems-44 (59%). See Exhibit A. As more fully discussed below, in most cases, the variances were negative, meaning reported (Space K) gross receipts were less than calculated (Space E) gross receipts.

Form SA1. The variance between reported gross receipts (Space K) and calculated gross receipts (Space E) for the top seventy-five Form SA1 systems, on an aggregated basis, ranged from a low of 49% in 2003-2 to a high of 109% in 2004-2 with an overall average of 71% for the eight accounting periods, as shown on the attached exhibit. See Exhibit C, attached hereto. In other words, if the Space E information were correct, gross receipts would have been at least one half more than what was actually reported in all eight accounting periods, and in one period, more than double what was reported.

As the effect of gross receipts on Form SA1 systems is muted by the flat fee paid (\$37 during the periods studied) by Form SA1 systems, Program Suppliers also examined how often the calculated gross receipts were above \$98,600, the cut-off for Form SA1 systems at that time. Out of 600 (seventy-five Form SA1 systems multiplied by eight accounting periods) individual filings analyzed, 239 filings, or 40% of the total, showed calculated (Space E) gross receipts above \$98,600, which, if used in place of the reported (Space K) gross receipts, would have required that the systems file either as Form SA2 or

Form SA3 systems with higher royalty fee payments. Such lost royalties adversely affect both Program Suppliers and other copyright owners.

Form SA2. The same pattern of aggregate reported (Space K) gross receipts being lower than aggregate calculated (Space E) gross receipts holds true for the top seventy-five Form SA2 systems over the eight accounting periods. The percentage differences ranged from a low of 4% to a high of 33%, with an overall average of 19% for the eight accounting periods.

In those accounting periods, the minimum gross receipts for Form SA3 systems was \$379,600. The calculated (Space E) gross receipts exceeded \$379,600 in 270 of the 600 individual Form SA2 filings studied, which amounts to 45% of the Form SA2 filings studied. The other side of this coin is how many of the Form SA2 filers studied were close to meeting the Form SA3 gross receipts minimum: Program Suppliers' analysis showed that 212, or 35%, of the 600 Form SA2 filers studied showed reported (Space K) gross receipts between \$370,000 and \$379,600. This suggests that for many Form SA2 systems even a relatively small difference between reported and calculated gross receipts will be enough to avoid Form SA3 royalty liability.

Form SA3. The expanded Form SA3 analysis is consistent with Program Suppliers' earlier more limited study, as well with the Form SA1 and Form SA2 analyses discussed above. The percentage difference between aggregated reported and calculated gross receipts ranged from a low of 17% in 2001-1 to a high of 49% in 2003-1, with an overall average across the eight accounting periods of 31%. The size of the percentage

differentials (along with the dollar differentials, ranging from \$249 million to \$764 million) between calculated and reported gross receipts in any accounting period belies NCTA's unsupported conjectures that somehow these differences can be explained by intra-period shifts in tier rates or subscriber counts. *See* NCTA Comments at 4-6.

To provide some idea of the potential impact on the royalty pool that these differences could have, Program Suppliers determined the ratio of royalties paid by the seventy-five Form SA3 systems to their reported (Space K) gross receipts for each accounting period studied. The overall average for the eight accounting periods studied was 1.29%, with a range of 1.23% to 1.31% for individual accounting periods. Program Suppliers then multiplied the resulting percentage for each accounting period by the calculated (Space E) gross receipts for the same period as a surrogate royalty fee payment total for the seventy-five Form SA3 systems. In total, using the calculated gross receipts yields a number of about \$50 million in estimated royalty fee payments over and above what was paid by the studied systems.

These analyses provide substantial evidence that calculated (Space E) gross receipts do not roughly approximate the reported (Space K) gross receipts, as the Office intended. Rather, reported gross receipts are substantially lower than calculated gross receipts across all types of cable systems and over several accounting periods. This pattern is not only well-ingrained, but also appears to be the result, particularly among Form SA1 and SA2 systems, of an effort to take advantage of lower, subsidized royalty fees. Neither NCTA nor ACA has offered any evidence to explain why such wide

variance between reported and calculated gross receipts exists. The clear effect of underreported gross receipts is lower royalty payments, which harms copyright owners, including Program Suppliers.

Program Suppliers' proposal does not require that cable systems change what they currently file as reported and calculated gross receipts but rather, asks that unless the two are roughly approximate (Program Suppliers have suggested that a variance of 10% could meet this standard), cable operators must provide some credible explanation for the variance. Contrary to ACA's assertion that the present system provides an adequate means for obtaining the needed information to reconcile two very different gross receipts pictures that appear on the face of many SOAs, ACA Comments at 6, the Office and copyright owners face substantial obstacles from cable operators who are unwilling to provide such information. *See, e.g.*, PS Comments at 18-19 (citing examples where the Licensing Division sent multiple requests for information from cable systems without success). As explained, the current system creates perverse incentives for cable operators to underreport, knowing that no audit powers exist, and the only means to obtain needed information is expensive and time-consuming copyright infringement litigation. As the legislative history of Section 111 makes clear, Congress did not intend the process for obtaining information to be so difficult. *See* PS Comments at 3. Accordingly, the Office should adopt Program Suppliers' proposed changes.

2. Program Suppliers' Requests for Clarification Regarding the Reporting of MDUs on the SOAs are Warranted.

Contrary to both NCTA and ACA's assertions, Program Suppliers have not requested that the Office impose a new requirement regarding MDU reporting. Rather, Program Suppliers seek to have cable operators comply with existing requirements to report specific subscriber and rate information for the MDUs that they serve in Space E. *See* Forms SA3 and SA1-2, Space E (providing blanks for subscriber information for "Motel, Hotel" and "Commercial" and relevant rate information); 37 C.F.R. § 201.17(e)(6)(iii)(B) (noting that cable operators must report "the charge or charges made per subscriber in each subscriber category" and noting that "[e]ach entity (for example, the owner of a private home, the resident of an apartment, the owner of a motel, or the owner of an apartment house) which is charged by the cable system for the basic service of providing secondary transmissions shall be considered one subscriber"). Program Suppliers simply seek to clarify that the subscriber and rate information included in Space E reflect whatever rate arrangement(s) cable operators hold with MDUs, and that cable operators be instructed not to leave areas blank, but rather to indicate with a zero or the designation "N/A" if a particular question does not apply to their system(s). *See* Petition at 6-8. This clarification is consistent with the Office's existing regulatory requirements, and therefore will not impose any new substantive reporting obligation on cable operators.

NCTA's and ACA's assertion that this clarification will impose a significant burden on cable operators, NCTA Comments at 6 (claiming compliance "would be

