UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

Before the
Copyright Office, Library of Congress
Washington, D. C.

In re)
Eligibility for the)
Cable Compulsory License)
Docket No. 96-2

COMMENTS OF THE STAFF OF THE FEDERAL TRADE COMMISSION(1)

The staff of the Federal Trade Commission is pleased to respond to the Notice of Inquiry ("NOI") issued by the Copyright Office of the Library of Congress.(2) The NOI solicits comments on whether, and to what extent, open video systems ("OVSs") are eligible to use the cable compulsory license. OVS is a new distribution technology for multichannel video programming,(3) which combines features of common carriers with those of cable systems.(4) The cable compulsory license provides the legal framework through which cable systems distribute broadcast signals.(5)

The Federal Trade Commission is responsible for maintaining competition and safeguarding the interests of consumers. The staff of the FTC has wide experience in reviewing competition issues in the area of telecommunications.(6) Our purpose in responding to the NOI is to identify the policy considerations that we believe the Copyright Office should carefully consider. We express no view on the technical issues of statutory construction raised by the NOI.

The cable compulsory license applies now to traditional cable systems, private cable systems, and wireless distribution technologies, including MMDS and LMDS.(7) A separate satellite compulsory license applies to home satellite dishes and direct broadcast satellite technologies.(8) Together, these two compulsory licenses provide the legal framework under which all currently existing multichannel video programming distribution technologies carry local and distant broadcast channels. OVS clearly does not qualify for the satellite compulsory license; this NOI addresses whether it qualifies for the cable compulsory license.

One criticism directed at the cable compulsory license has been that it, like other prices that are set administratively rather than by market forces, may allocate resources inefficiently.(9) Because the legal framework governing the distribution of broadcast signals includes provisions in the communications statutes, FCC regulations, and the copyright statutes, this comment's scope is limited to how consumer welfare can be maximized through alternatives the Copyright Office has raised in the NOI. We do not comment here on the larger policy issues raised by the existence of the compulsory license.

We believe that applying the cable compulsory license to OVS could benefit consumers, because it would lead to an allocation of resources that better reflected the relative costs of different video distribution methods. It is likely that extending compulsory licensing to OVS would reduce OVS's costs of acquiring programming and make its acquisition costs comparable to that of other distribution technologies. Absent such an extension, the OVS would have to negotiate a separate copyright license for each program on a broadcast channel. The transaction costs of acquiring broadcast programming for OVS distribution would thus likely be higher than for the other, established distribution technologies.(10) This means that in some circumstances in which OVS is a superior distribution technology, a rival technology may have lower apparent costs because of its low-priced access to programming. In such a circumstance, consumers would face higher prices than if programming were available to all technologies under a compulsory license. Conversely, if compulsory licensing were extended to OVS, differences in price among distribution technologies would accurately reflect the relative costs of providing service by alternative means.

If the Copyright Office does conclude that the compulsory license applies to OVS, the question remains as to precisely where copyright liability under the compulsory license should rest. Unlike a cable operator that programs its entire system itself, the OVS operator will be only one of the programmers on its system.(11) In fact, a purpose of the law is to foster competition among programmers on a single OVS.(12) We recommend that the OVS operator should not be liable for the copyright costs for local and distant broadcast channels carried on the system by independent programmers. In a competitive market, resources are allocated efficiently when each firm internalizes the costs of its inputs. Here, as with cable systems, that would be accomplished by requiring the entity that selects the programming to bear the program acquisition costs, including copyright obligations. The FCC recognizes this principle in its determination that each OVS programmer, not the OVS operator, is responsible for obtaining retransmission consent for local broadcast stations it chooses to carry.

In theory, assigning responsibility for obtaining consent to the OVS operator might also reach an efficient result, if the OVS operator could then, by contract, allocate all copyright costs back to the programmers. But the statutory language of the compulsory license, as it has been interpreted and applied, would make that allocation by contract difficult, because the language precludes correlating the fee with the program source. A party's liability under the compulsory license is based on the total revenue derived from all services that include any broadcast signals covered by the license; it cannot be based only on revenue from subscribers who actually receive the programming for which the fee is charged.(13) Assigning all copyright liability to the OVS operator could permit an independent OVS programmer to obtain what is in effect a subsidy for its programming. For example, the independent programmer might provide several distant broadcast signals with relatively high license fees, making the OVS operator liable for a compulsory license fee based on the fiction that every subscriber to any programmer on the operator's system receives those expensive distant signals. This mismatch would produce inefficient outcomes in programming decisions. Assigning copyright liability under the compulsory license to the OVS programmer, rather than the OVS operator, avoids this potential for distortion.

Accordingly, we recommend that the Copyright Office extend the cable compulsory license to OVS, and that copyright liability rest with the firm providing the programming on the OVS.

1. This comment represents the views of the staff of the Federal Trade Commission, and does not necessarily reflect the views of the Federal Trade Commission or any individual Commissioner. Inquiries regarding this comment should be directed to John Wiegand (415-356-5270) of the FTC's San Francisco Regional Office or David Reiffen (202-326-2027) of the Bureau of Economics.

2. 61 Fed. Reg. 20197 (1996).

3. 47 U.S.C. 571-73.

4. In re Open Video Systems, ___ FCC Rcd. ___, 1-3 (1996)(Second Report & Order).

5. 17 U.S.C. 111.

6. *See*, e.g., Comment of the Staff of the FTC and Antitrust Division of the Department of Justice, Open Video Systems, FCC CS Dkt. 96-46 (1996); Comment of Staff of the FTC, Carriage of Television Broadcast Signals by Cable Television Systems, FCC MM Dkt. 90-4 (1991); Comment of the Staff of the FTC, Reexamination of the Effective Competition Standard for Regulation of Cable, FCC MM Dkt. 90-4 (1991); Comment of the Staff of the FTC, Competition, Rate Deregulation and the Commission's Policy Relating to the Provision of Cable Television Service,

FCC MM Dkt. 89-600 (1990); Comment of the Staff of the FTC, Definition of Cable Systems, Copyright Office Dkt. 86-7 (1986).

7. 17 U.S.C. 111 (f).

8. 17 U.S.C. 119.

9. Some have suggested that the license be repealed, so that cable operators and third party program packagers would negotiate for copyright licenses to retransmit broadcast signals. *See, e.g.*, Benson, Manning & Mitchell, *Copyright Liability for Cable Television: Compulsory Licensing and the Coase Theorem*, 21 J.L. & Econ. 67 (1978); Compulsory Copyright License for Cable Retransmission, 4 FCC Rcd. 6711, 6719-21 (1989) (Report). Others, citing high transaction costs associated with both third party program packagers and the cable compulsory license, have urged that the property rights in broadcast signals be reassigned to the receivers of the signals, restoring the conditions that existed prior to 1976. See Teleprompter Corp. v. CBS, 415 U.S. 394 (1974) (finding no copyright liability for cable operators carrying distant broadcast signals); Cablevision Systems Development Co. v. MPAA, 836 F.2d 599, 605 n.9 (D.C. Cir. 1988)(noting that viewership ratings that reflect the full distribution of broadcast signals make the compulsory license "superfluous"); John Wiegand, *Competitive Effects of Cable Copyright Law*, 41 Antitrust Bull. 61, 75-77 (1996).

10. A market for brokerage service might arise to negotiate universal licenses with programmers. These brokers would enable OVSs to realize the benefits of the scale economies in negotiating broadcast licenses. Such brokerage would reduce an OVS's acquisition cost relative to individual negotiation, but would likely still result in higher transactions costs of acquiring programming than would exist under compulsory licensing. However, a brokerage service market may not arise, since stand-alone demand for broadcast programming by OVSs may not be sufficient to support the development of efficient, competitive programming brokers.

11. *See* 47 U.S.C. 573(b)(1).

12. Open Video Systems, ___ FCC Rcd.___ at 2 (CS Dkt. 94-46) (1996) (Second Report & Order).

13. *See* Cablevision Systems, 836 F.2d at 599; Cable Compulsory License: Merger of Cable Systems & Individual Pricing of Broadcast Signals, 60 Fed. Reg. 2365 (1995) (Notice of Inquiry) (discussing requirement that copyright fee be based on all subscribers to a system, not merely those subscribers who receive the programming for which the charge is made).