TESTIMONY
OF FRITZ ATTAWAY
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AND
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MOTION PICTURE ASSOCIATION OF AMERICA

BEFORE THE
COMMITTEE ON THE JUDICIARY
U.S. HOUSE OF REPRESENTATIVES

"Copyright Licensing in a Digital Age: Competition, Compensation and the Need to Update the Cable and Satellite TV Licenses"

FEBRUARY 25, 2009

Chairman Conyers, ranking member Smith, members of the Committee, thank you for this opportunity to present the views of the creators and distributors of movies, series, specials and other prerecorded entertainment programming that constitute the largest category of television programming retransmitted by satellite carriers and cable operators under the statutory compulsory licenses in sections 111, 119 and 122 of the Copyright Act.[1]

With due respect to the satellite carriers and cable operators who ever more efficiently deliver programming to the homes of consumers, it is not headends, or satellites, or fiber-optic cables that consumers crave and are willing to pay for. It is entertaining and informative programming that consumers desire. As the Committee begins its re-examination of the Satellite Home Viewer Act, I want to stress that our goal is to provide consumers the highest possible quantity and selection of television programming. To do that, the men and women who invest

[1] Motion Picture Association of America, Inc. ("MPAA") is a trade association representing six of the world's largest producers and distributors of motion pictures and other audiovisual entertainment material for viewing in theaters, on prerecorded media, over broadcast TV, cable and satellite services, and on the Internet. MPAA members include Paramount Pictures Corporation, Sony Pictures Entertainment Inc., Twentieth Century Fox Film Corporation, Universal City Studios LLLP, Walt Disney Studios Motion Pictures, and Warner Bros. Entertainment, Inc. MPAA also represents some 200 non-member program producer and syndicator claimants to cable and satellite compulsory license royalties with respect to the distribution of such royalties.

their talent and capital to create that programming must be fairly and adequately compensated.

With that in mind, my message today is simple and straightforward:

1. The cable and satellite compulsory licenses are historical anachronisms that are no longer justified in today's television program marketplace;
2. Tinkering with the existing compensation schemes for the sake of "harmonization" or any other seemingly attractive catch phrase will create some short term winners and losers, but will not advance the interests of consumers in abundant and affordable television programming;
3. If the compulsory licenses are retained, their scope should not be broadened, program owners should be fairly compensated and direct, marketplace program licensing should be encouraged.

Because the impending sunset of the satellite compulsory license gives particular urgency to the subject of this hearing, I will start with a short history of the satellite license and then move on to some of the issues that are sure to be raised during the course of this discussion.

HISTORY OF THE SATELLITE COMPULSORY LICENSE

The Satellite Home Viewers Act ("SHVA") of 1988 created in Section 119 of the Copyright Act a five-year "compulsory license" that allows

direct-to-home satellite program distributors (such as Dish Network and DirecTV) to retransmit broadcast television programming from distant markets without the permission of the copyright owners of that programming. This satellite compulsory license, like the cable compulsory license enacted more than a decade earlier, limits the rights of copyright owners and forces them to make their creative works available for retransmission without their consent and without any ability to negotiate a fair, marketplace price.

The SHVA was extended for five-year periods in 1994, 1999 and 2004. The 1994 renewal provided for a royalty rate adjustment procedure aimed at providing copyright owners with market value compensation for the use of their programming by satellite companies. This procedure resulted in the establishment of market based royalty rates in 1998 by a panel of independent arbitrators appointed by the Copyright Office.[2] However, these market based rates were short lived.

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[2] "The Panel specifically endorsed the approach taken by PBS, and its principal witness, Ms. Linda McLaughlin. Using data supplied by an industry survey group, Ms. McLaughlin examined the license fees paid by multichannel video programming distributors ('MVPDs') to license the viewing rights to 12 popular basic cable networks. These networks are A&E, CNN, Headline News, Discovery, ESPN, the Family Channel, Lifetime, MTV, Nickelodeon, TNN, TNT, and USA. Ms. McLaughlin testified that these basic cable networks represented the closest alternative programming to broadcast programming for satellite homes, and that studies indicated that consumers value networks and superstations as least as highly as popular basic cable networks. Direct Testimony of Linda McLaughlin at 2-5. She then calculated a 'bench-mark' rate for these networks to be used by the Panel as representative of the fair market value of broadcast signals retransmitted by satellite carriers:* * * 'I have calculated a basic cable network benchmark price and used it to estimate a minimum compulsory license fee for satellite-retransmitted broadcast stations. The average license fee of the 12 popular basic cable networks was 18 cents in 1992--when the maximum satellite compulsory rate was 17.5 cents--and has risen to 24 cents in 1995, an annual increase of ten

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Although satellite companies pay market-based license fees for scores of non-broadcast program services that they sell to their subscribers, they strongly objected to paying market based royalty rates for any retransmitted broadcast programming. They successfully petitioned Congress to impose a substantial discount on the market based rates, essentially creating a subsidy for satellite television services borne not by the government but by the creators of broadcast programming. These discounts – 30 percent for "superstation" programming and 45 percent for network and PBS programming – went into effect in July of 1999.

After the reduction of satellite royalty rates in 1999, Congress in the 2004 reauthorization provided for an adjustment of the rates under the supervision of the Librarian of Congress. Voluntary negotiations between the two major satellite carriers and the major program owner groups resulted in a marginal rate increase and an annual inflation adjustment. The current royalty rate paid by satellite carriers under Section 119 remains, almost ten years later, less than the market rate established in 1999, notwithstanding substantial increases in programming costs since that time.

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percent per year. The license fees for these 12 basic cable networks are forecast to increase to an average of 26 cents in 1997, 27 cents in 1998 and 28 cents in 1999. This suggests that the compulsory rate for satellite retransmitted stations should increase at least correspondingly with the average prices for basic cable networks, to an average at least 27 cents for the 1997-99 period.'" *Rate Adjustment for the Satellite*

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NEITHER THE SATELLITE NOR THE CABLE COMPULSORY LICENSE IS JUSTIFIED IN TODAY'S MARKETPLACE

The market conditions that gave rise to the cable compulsory license in 1976, and the satellite compulsory license in 1988, have long since disappeared. In 1976, distant and local television broadcast signals were the only programming cable operators could sell to their subscribers. By 1988, the emerging direct-to-home satellite industry offered some of the so-called "cable" networks like USA Network and ESPN, but distant television broadcast signals were critical to the ability of then-nascent satellite television services to compete with more established cable services. In both instances, the prevailing opinion was that the "transaction cost" of negotiating retransmission rights for the television broadcast programming that was so essential to these still emerging services justified a government imposed, below market compulsory license rate to insure the viability of these services given the state of the relevant markets at the time.

Today, out-of-market ("distant") television broadcast signals remain an important part of cable and satellite program packages, but account for a minuscule amount of the programming sold by satellite carriers and cable systems to their subscribers. For instance, in Arlington County,

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Carrier Compulsory License, 62 Fed. Reg. 55742 at 55648 (Oct. 28, 1997), *aff'd SBCA v.*
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Virginia, Comcast offers 297 channels of programming, only one of which is a distant TV station retransmitted under the Section 111 compulsory license. DirecTV offers the citizens of Arlington 568 channels, only one of which is a distant TV station retransmitted under the Section 119 compulsory license.[3]

Despite being a small portion of the programming packages offered by cable and satellite companies, distant broadcast station programming is still highly valuable. If it were not, we would not be here. But, in thinking about whether compulsory licensing can be justified today, it is important to recognize that each one of the tens of thousands of hours of non-broadcast programming sold by cable and satellite systems to their subscribers is licensed on marketplace terms and conditions. Only the relatively small amount of retransmitted, distant broadcast programming is subject to a government imposed compulsory copyright license.[4]

The fact that the overwhelming majority of television programming offered by cable and satellite companies is licensed in marketplace transactions suggests that there is no longer any justification for

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Librarian of Congress, 172 F.3d 921 (D.C.Cir. 1999)(unpublished).

[3] See http://www.comcast.com/Customers/Clu/ChannelLineup.ashx?area=0 and http://www.directv.com/see/pdf/chnllineup.pdf; http://www.directv.com/DTVAPP/global/contentPageIFnorail.jsp?assetId=P4880022#h:759.628

[4] Local station programming is also retransmitted under the compulsory licenses. However copyright owners receive no compensation for the retransmission of local broadcast programming and consent must be obtained from the local stations whose signals are retransmitted. See 47 U.S.C §325(b)(1).

retaining the historical relics that are the cable and satellite compulsory licenses. As recently reported by the Register of Copyrights:

> The cable and satellite industries are no longer nascent entities in need of government subsidies through a statutory licensing system. They have substantial market power and are able to negotiate private agreements with copyright owners for programming carried on distant broadcast signals. The Office finds that the Internet video marketplace is robust and is functioning well without a statutory license. The Office concludes that the distant signal programming marketplace is less important in an age when consumers have many more choices for programming from a variety of distribution outlets.[5]

THE SATELLITE AND CABLE COMPULSORY LICENSES WERE SEPARATELY DESIGNED FOR VERY DIFFERENT SERVICES, EACH WITH ITS OWN DISTINCT NEEDS AND BUSINESS MODELS

Although the programming services offered by cable systems and satellite carriers are largely indistinguishable today, they were very different when the satellite license was first imposed in 1988. Cable systems from the outset offered subscribers a collection of local and distant broadcast signals. In many instances, the primary appeal of cable service was that it provided better reception of local signals while eliminating the need for roof-top antennas. And cable was largely an

[5] Satellite Home Viewer Extension and Reauthorization Act, Section 109 Report, *A Report of the Register of Copyrights, June 2008*, at page 219.

urban and suburban service because of the high cost of stringing cable wires in sparsely populated, rural areas.

When direct-to-home satellite services came on the scene, they provided no local stations and only a few distant signals because of bandwidth limitations. They catered to rural customers who had available few, if any, over-the-air local stations and in areas where satellite service had an infrastructure cost advantage over cable.

Because of these significant differences between the two services, the cable and satellite compulsory licenses were drafted quite differently. When the cable compulsory license was drafted in 1976, Congress adopted a royalty formula based on a percentage of cable subscriber receipts and intended to produce a certain sum in royalty payments.[6] This formula did not directly link the royalty fee to the number of TV signals carried. Rather, the fee is based on "distant signal equivalents" which reflect the amount of distant, non-network programming on different types of retransmitted TV signals, starting with zero. That is, even if a cable system carries no distant signals, a minimum royalty fee is required "for the privilege of retransmitting distant non-network programming."[7] Moreover, the royalty calculation designed by Congress for cable systems requires distant signal equivalents to be applied to all gross subscriber receipts for any program services that include

[6] H.R. Rep. No. 1476, 94th Cong., 2d Sess. at page 91.
[7] Id. at page 96.

retransmitted broadcast signals, even if the cable operator chooses to deliver certain signals to only a portion of its subscribers.[8]

And, significantly, the cable royalty calculation results in a lower fee for the second and subsequent distant signals carried, until the number of distant signals equals the number of distant signals that could be carried under Federal Communications Commission rules then in effect, at which point the fee for additional signals not allowed by those rules increases dramatically. In effect, the rate structure creates a "cap" on the number of distant signals that cable systems carry under the cable compulsory license.

The cable compulsory license formula was clearly a "rough justice" approach, requiring concessions from all sides. Copyright owners were forced to forego their exclusive right to authorize the retransmission of their works and to accept less than market value under a government-run compulsory licensing system, and cable operators were required to pay a minimum royalty whether or not they retransmit any distant signals.

In 1988, direct-to-home satellite companies provided a very different service as compared to the service offered by cable companies. As a result, Congress chose a very different royalty formula in the

[8] "We [the Copyright Office] believe Section 111 is clear. As long as a cable operator subjects itself to the statutory license, and publicly performs the non-network

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satellite compulsory license. Instead of a royalty calculation based on a percentage of gross revenues and only indirectly related to the number of distant broadcast stations carried, Congress determined that the satellite royalty should be a fee based on the number of subscribers per month that receive each retransmitted distant broadcast station. In contrast to the more complicated cable compulsory license royalty calculation based on a percentage of subscriber revenues, in the satellite license Congress chose to directly link the fee to "the total number of subscribers that received such retransmissions."[9] Also, in contrast to the cable license, the satellite license monthly per subscriber fee does not change depending upon the number of distant signals carried, and thus does not impose an effective cap on the number of distant signals carried. A standard, flat fee per subscriber per month is required, regardless of the number of signals carried.

One thing that both the satellite and cable royalty payment plans have in common is that payment of royalties is basically left to the honor system. That is, satellite and cable companies pay royalties based on self-reported subscriber, revenue and signal carriage data in statements of account filed with the Copyright Office, without any means for the Copyright Office or copyright owners to substantiate independently that

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programming carried by a distant signal, it must pay royalties for such use no matter if some subscribers are unable to receive it." *Definition of Cable System*, 73 Fed. Reg. 25627, 25632 (May 7, 2008).

the information is valid. If these licenses are retained, Congress should provide an audit mechanism whereby copyright owners who are supposed to be compensated for the use of their works by satellite and cable companies can verify that the statutory compensation required by the licenses is, in fact, being paid.

"HARMONIZATION" OF THE SATELLITE AND CABLE LICENSES WOULD PERPETUATE THE FUNDAMENTAL UNFAIRNESS OF THE CURRENT SYSTEM WITH NO CORRESPONDING PUBLIC INTEREST BENEFIT

It has been suggested that the cable and satellite compulsory licenses be "harmonized" based on the current satellite license payment model, with the result that both cable and satellite companies would pay a flat monthly per subscriber fee for each distant signal carried. While such harmonization may have surface appeal, it would result in a very substantial adjustment in the royalty fees paid by individual cable systems, with some paying more in royalties, and others less, than they do under the current formula.

MPAA's analysis of statements of account filed with the Copyright Office shows that if large ("Form 3") cable operators were required to pay compulsory license royalties on the same basis and at the same level as now paid by satellite carriers, roughly 34% of Form 3 cable systems

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[9] 17 U.S.C. Section 119(b)(1)(A).

would pay lower royalty fees than they do under the current cable royalty calculation. The remaining 66% of Form 3 cable systems would pay higher royalty fees than they pay under the current system. Thus, harmonization would redistribute somewhat copyright owners' forced subsidy of the cable and satellite industry, but would not eliminate the unnecessary government suspension of the program marketplace for retransmitted broadcast programming, and it would have no impact on consumers.

There is no evidence that either cable or satellite royalty payments have any impact on subscriber rates. When the satellite royalty rates were reduced by 30 to 45% in 1999, there was no corresponding reduction in the rates charged by satellite carriers to their subscribers. In fact, there is evidence that satellite program rates actually increased after Congress reduced compulsory license royalty rates.[10] This evidence strongly suggests that providing fair, marketplace compensation to program owners will not harm cable and satellite subscribers. Thus, if Congress does not eliminate the compulsory licenses as recommended by the Copyright Office, because they are historical relics with no justification in the program marketplace of today, Congress should at least insure that copyright owners are fairly compensated. This could be accomplished by directing the Copyright Royalty Judges at the Copyright

[10] Testimony of Fritz Attaway before the Committee on the Judiciary, U.S. Senate, "The Satellite Home Viewer Extension Act," May 12, 2004.

Office to establish market rates to be paid by both cable and satellite companies. However, if Congress is not disposed to take either of these courses, then it should leave the satellite and cable royalty formulae in place, with the appropriate inflationary adjustments, for the period of any extension of the satellite license. Harmonization of the royalty rate formulae without a fundamental change from a government imposed subsidy of the cable and satellite industries to a market based scheme where program owners are fairly compensated, would be equivalent to rearranging the deck chairs on the Titanic. It would alter the amount of subsidy received by individual recipients, but would do nothing to benefit consumers and nothing to change the fundamental inequity of the present system.[11]

COMPULSORY LICENSE ROYALTIES PAID BY CABLE AND SATELLITE COMPANIES HAVE NEGLIGBLE IMPACT ON CONSUMERS

For the most recent semi-annual accounting period, January through June, 2008, cable systems paid royalties totaling $79,820,643,

[11] The vast disparity between the compulsory license royalty payments for television programming and marketplace payments for the exact same programming is illustrated by Turner Broadcasting Service's conversion of its program package from a distant signal, WTBS in Atlanta, to the TBS cable network in 1998. Providing basically the same programming, other than news and other local programs, as a cable network that it had as a distant broadcast signal, TBS was able to obtain direct license fees that by 2000 were almost equal to the combined cable and satellite royalty funds ($188 million for TBS vs. $186 million cable+satellite royalty fund), and by 2004 had grown to substantially more than the combined royalty fund ($287 million vs. $204 million cable+satellite royalty fund). Kagan, Economics of Basic Cable Networks (5th Ed. 2005).

and satellite carriers paid royalties totaling $46,926,370, for a grand total of $126,747,013.[12] This is a substantial amount of money. However, when placed in the context of the cable and satellite financial picture, it is a negligible portion of the cost of their operations for which subscribers pay.

The National Cable & Telecommunications Association ("NCTA") reports that 2008 estimated cable revenue was $81.35 Billion.[13] Compulsory cable royalties are less than 0.1% of these revenues. DirecTV reported revenues of $5.3 Billion for the fourth quarter, 2008, or $21.2 Billion on an annualized basis, and advised subscribers that it would raise rates, effective March 4, by an average of 4%.[14] The other major satellite carrier, Dish Network, reported revenues of $2.89 Billion for the fourth quarter of 2008,[15] or $11.56 Billion on an annual basis. Royalty fees paid under the satellite compulsory license will amount to some 0.14% of these revenues.

NCTA reports 64.7 million cable subscribers as of June, 2008.[16] DirecTV and Dish Network subscribers totaled 17.6 million[17] and 13.78

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[12] Report of receipts provided by the Copyright Office on February 6, 2009.

[13] See http://www.ncta.com/Statistic/Statistic/Statistics.aspx

[14] Multichannel News, *DirecTV Loads Up 301,000 Subs In 4Q, Satellite Operator Posts Best Sub Growth in Three Years as Revenue Increases 9%*, Todd Spangler, February 10, 2009.

[15] The Wall Street Journal Digital Network, *Dish Network 4th-quarter net up 14%, revenue up 12%*, by Robert Daniel, February 26, 2008.

[16] Ibid, Note 10.

million,[18] respectively, at the end of 2008. If each cable and satellite subscriber is sent a monthly bill through the U.S. Postal Service at the current rate of 42 cents, the annual cost of sending these bills would be more than $480 million, or almost four times as great as the combined compulsory license royalties paid by cable and satellite companies.

IF THE COMPULSORY LICENSES ARE RETAINED, COMPENSATION TO PROGRAM OWNERS SHOULD NOT BE REDUCED AND THE LICENSES SHOULD NOT BE EXPANDED OR LIMIT MARKETPLACE LICENSING ALTERNATIVES

The evidence is overwhelming that the program marketplace can and, for the vast majority of cable and satellite programming, does work without the need for compulsory licensing. Certainly there is no justification for lowering the present level of compulsory license royalty compensation to program owners, or for further expanding the current licenses beyond the entities now eligible or to cover retransmission of distant programming not currently permitted. In particular, because both the cable and satellite licenses are inextricably bound to regulations of the Federal Communications Commission ("FCC"), such as those governing network program non-duplication and syndicated exclusivity,

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[17] Ibid, Note 11.

[18] Ibid, Note 12.

any entity not subject to those regulations should be excluded from the scope of the existing compulsory licenses.

Even if Congress decides to continue to allow cable and satellite companies to use broadcast programs at below market rates, Congress should not further impede the ability of program owners to obtain the full economic value of their creations through exclusive licenses with broadcast stations and networks, or diminish the value of such licenses once they are entered into. Respect for freely negotiated program licenses with stations and networks, written into the existing compulsory licenses by incorporating the aforementioned FCC network non-duplication and syndicated exclusivity rules, should be maintained and where necessary, strengthened where broadcast stations and program owners have bargained for exclusive rights. [19] Rather than expanding the scope of the compulsory licenses, Congress should encourage marketplace transactions which strike a fair bargain between rights owners and program users.

[19] There is one disparity between the cable and satellite licenses that should be harmonized. The cable license requires cable operators to provide exclusivity for syndicated programming on both independent and network distant stations retransmitted in local markets ("Syndicated Exclusivity" or "Syndex Protection"). That is, if a local station has exclusive rights to broadcast a particular syndicated program, the cable operator upon request from the local station must not violate the local station's exclusive rights by retransmiting that same program from a distant station. The satellite license provides syndicated exclusivity with respect to distant independent stations, but not distant network stations. This disparity should be corrected by amending the satellite license to afford the same syndicated exclusivity rights as the cable license.

The existing licenses are "compulsory" only for program owners. They allow cable and satellite companies to enter the marketplace and license programs directly from owners even when the compulsory licenses might apply.[20] Such direct licensing should be encouraged. Whatever Congress does in this area it should ensure that these licenses in no way discourage such direct licensing and preserve the option to engage in direct, marketplace licensing rather than taking advantage of the mechanism of the compulsory licenses.

[20] For instance, a cable system located in a DMA that encompasses areas in adjacent states and carrying "local" signals from another state could negotiate with distant in-state stations for retransmission rights to the news and public affairs programming owned by those in-state stations separate and apart from the cable compulsory license.