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**Cutting the Cord: Leveling the Playing Field for Virtual Cable Companies**

Camille M. Johnson<sup>1</sup>

**Introduction**

The oligopolistic playground of today's cable companies is being threatened by the increasing popularity of television accessed by millions via the Internet. The outdated frameworks of cable and satellite companies, also known as multichannel video programming distributors ("MVPDs"), are waning in comparison to the reach and convenience of the Internet.

Naturally, the Internet is the expanding frontier in the television distribution industry and has grown to be the preferred method of viewing programming content. Anticompetitive behavior on the part of the MVPDs, however, has served to stifle new Internet television providers, particularly virtual cable companies. Restrictive agreements between content programmers and the MVPDs prevent content creators from striking the most economically sound distribution deals, the fallout of which negatively impacts the consumer.

Internet television providers have been at the mercy of the leverage and bargaining power of the MVPDs, driven by cable, satellite and fiber optics companies such as Comcast, Time Warner Cable, Dish, Direct TV, Verizon and AT&T. These MVPDs not only control the distribution of programming content but they also control and are primary distributors of Internet broadband connection, often bundling packages and manipulating prices to discourage MVPD subscribers from canceling their cable subscriptions. Government intervention is necessary to

allow for the entrance of virtual cable companies into the multi-channel video programming industry. Expansion of the compulsory licensing scheme under the Copyright Act would be most effective in achieving this goal.

This paper addresses the issues surrounding the anticompetitive behavior of MVPDs and possible solutions in favor of the Internet television providers in four parts. Part I addresses the beginnings of cable television and the establishment of the pay-TV distribution network. Part II explores the increasing popularity of Internet television today and the difficulties faced in gaining traction in the MVPD dominated marketplace. Part III addresses MVPD content lockouts other anticompetitive tactics in response to a growth in popularity of online television. Part IV recommends legislative reform and policy solutions that will enable Internet television companies to participate on a level playing field with the existing MVPDs.

## **I. The Establishment of the MVPD Framework**

Cable television was developed in response to a need to broadcast to households located outside of the reach of the broadcast signals.<sup>2</sup> Cable companies were established to retransmit the broadcasters' signals by way of cable line, which were in essence "performances" of copyrighted works. Technically as performances of copyrighted works, a cable company would be required to negotiate licenses for each retransmission.<sup>3</sup>

### **A. Copyright Act Exemption for MVPDs**

Within the Copyright Act enacted in 1976, an exemption was made for cable companies, in that they need not have to negotiate individual licenses for retransmission and could simply

pay a fee set by the government for compulsory licensing of the content to be rebroadcast to cable subscribers.<sup>4</sup>

Specifically, Section 111 of the Copyright Act provides:

Secondary transmissions to the public by a cable system of a performance or display of a work embodied in a primary transmission made by a broadcast station licensed by the Federal Communications Commission... shall be subject to statutory licensing upon compliance with the requirements of subsection (d) where the carriage of the signals comprising the secondary transmission is permissible under the rules, regulations, or authorizations of the Federal Communications Commission.<sup>5</sup>

Subsequently, satellite companies were added to cable companies in qualifying for the exemption under the Copyright Act by way of the Satellite Home Viewer Act of 1988, Title II, Pub. L. No. 100-667.<sup>6</sup> This Act allowed satellite companies to enter the market and compete in the content distribution market along with the existing cable companies.<sup>7</sup> Satellite companies such as Dish and DirecTV control approximately 25% of the market.<sup>8</sup> Telephone companies are the most recent entrant to this content distribution scheme and have been added to the compulsory licensing scheme.<sup>9</sup> Telephone companies such as AT&T utilize fiber optics technology and control approximately 11% of the market.<sup>10</sup>

## B. Broadcast vs. Non-Broadcast Programmers

MVPDs distribute both broadcast and non-broadcast content. Broadcast content is developed by the major content programmers, such as ABC, NBC, Fox and CBS. These companies are available to the public for free over the airwaves by antennae and are distributed by the MVPDs under the compulsory licensing exemption scheme. However, MVPDs are

required to obtain Retransmission Consent from broadcast programmers as part of a 1992 compromise within the Cable Television and Consumer Protection Act, in order to rebroadcast the signal which is separate in theory from rebroadcasting copyrightable content. In order to extract additional fees from the MVPDs, broadcast programmers bundle their own smaller non-broadcast companies to be distributed through MVPDs under separate negotiated licensing agreements.<sup>11</sup>

Non-broadcast companies develop content that can only be accessed through an MVPD subscription. These non-broadcast companies include Time Warner, which owns CNN, TNT and TBS, and then Viacom owns MTV, VH1, Spike, Comedy Central, BET and others.<sup>12</sup> Distributors in some cases own their content creators, a prime example being Time Warner Cable's parent-subsidiary relationship with its programmers and Comcast who owns NBCUniversal. This relationship is referred to as vertical integration, which serves as a basis for the centralization of bargaining power within the MVPD landscape.<sup>13</sup>

The MVPDs negotiate with non-broadcast programmers for carriage on their networks. Smaller cable programmers on the outside of the vertical integration scheme are often integrated by being forced into unfavorable agreements with the MVPDs. In order to be distributed by the MVPDs, smaller content creators are often obligated to sell significant shares of stock to the MVPD and as a result become part of the vertical integration scheme.<sup>14</sup>

This sort of vertical integration allows MVPDs direct control over the content of their subsidiaries and the subsidiaries' ability to negotiate web-based streaming deals.<sup>15</sup> Contract terms weigh heavily in favor of the MVPDs, which include "most favored nation" clauses which "grant the distributors the benefit of any contract negotiated with a rival distributor." This is done to ensure Internet television companies cannot fairly compete with MVPDs. A resistance

to this sort of scheme by the smaller cable programmers may result in being “blackballed” by other distributors.<sup>16</sup>

### C. MVPD Usage Trends

The most recent data on usage shows that MVPD subscribers constitute 83 percent of American households, a decrease from 92 percent just five years prior.<sup>17</sup> The shifting consumer behavior is fully apparent in the numbers. According to Bloomberg’s Ian King, “The impact on the \$80 billion pay-TV industry is already being felt, with 2013 on pace to be the first year ever that total U.S. pay-TV subscriptions will decline, falling to 100.8 million from 100.9 million last year. And while 3.2 million new U.S. households were set up in the last three years, the paid-TV industry only added 250,000 subscriptions in that same period.”<sup>18</sup> Although the growth of MVPDs has slowed, they continue to dominate the content distribution marketplace. The lack of competition in this industry has resulted in inflated subscription rates, even in light of the abysmal customer satisfaction ratings.<sup>19</sup> Programmers only receive about a third of what the MVPDs collect from subscribers and make up the rest of their revenues through advertising fees.<sup>20</sup>

With their broadband Internet distribution capabilities, MVPDs bundle their cable subscription services with their broadband services offered to consumers making it difficult for consumers to transition to Internet only. This forced dynamic increases rates on broadband if the customer decides to cancel their cable subscription. “Today, cable operators make between fifty percent and sixty percent of their revenues from their MVPD service, while the balance comes from Internet access and phone services. They would make less money, all else equal, if consumers paid them only for Internet access.”<sup>21</sup>

The rates on bundled services have increased steadily year to year. A report released by the FCC noted that “under the current bundling regime, cable prices have increased by an average of 4.6% per year and in excess of 7% per year for the expanded basic program tier over the past five years, pointing to the industry’s practice of making most networks as available as part of a bundle tier-- as a potential reason for the rise in rates.”<sup>22</sup>

Entry costs to establishing a cable or satellite company are very high, creating barriers of entry for MVPDs who wish to enter the market by a more traditional route utilizing physical equipment. Beside the cost of the physical equipment needed to deliver content, this year alone MPVDs “will spend \$45 billion to secure the most attractive programming. That compares to a projected \$2.4 billion to be spent by Netflix, which accounts for the majority of online services purchasing content.”<sup>23</sup> MPVDs are at risk to lose a substantial portion of market share if Internet television providers are able to gain real footing in the industry. As the threat of cord cutting rises, so do the defense mechanisms and anticompetitive tactics of the MPVDs in their attempt to maintain status quo.<sup>24</sup>

## **II. The Rise of Internet Television**

Viewing television content has grown exponentially in popularity since broadband capabilities made it easy to view video over the home Internet connection. Companies operating in the online television setting are available in a variety of business models, including “subscription, per-episode fees, advertiser supported, or some combination.”<sup>25</sup>

More generally, the current Internet television industry can be divided into two categories: the online content distributors and the companies that produce online content streaming devices. Although there are many online content distributors, there are no existing

virtual cable companies. Virtual cable companies would in effect operate as direct competitors to existing MVPDs. However, because of the inability of virtual cable companies providers to carry television stations (in most part at the hands of the MVPDs) virtual cable companies will not be able to enter the market as a viable channel viewing product.

#### A. The Leading Online Content Distributors:

1. Netflix: This online distributor was established in 1999 as a mail order DVD movie service, although founders had their sights on an Internet content streaming service (hence the name Netflix as opposed to Postflix!<sup>26</sup>) In 2007, Netflix implemented its Watch Instantly service which soon became the primary section of growth and revenue for the company consisting of both movies and television shows. As of the third financial quarter 2013, Netflix served 40.3 million subscribers with earnings of \$32 million. Currently, the subscription fee for consumers is \$7.99. Recent growth has been attributed to the release of Netflix original programming such as jailhouse drama “Orange is the New Black” and political clincher “House of Cards”.<sup>27</sup>
2. Hulu: Established in 2008, Hulu is the primary online distributor of broadcast television programming. This online content company distributes programming owned by the joint venturers: Comcast, 21<sup>st</sup> Century Fox Corporation and The Walt Disney Company.<sup>28</sup> In 2010 Hulu created a premium service, Hulu Plus, for \$7.99 per month. Hulu currently has approximately 4 million subscribers and



generated \$695 million in revenue in 2012 between subscriptions and advertisers.<sup>29</sup>

3. YouTube: This content provider has become the primary source for user-generated video on the Internet. Established in 2005, Google purchased YouTube in 2006 for \$1.65 billion. Although most of the content is user generated, corporations such as CBS and BBC participate in a corporate partnership program with YouTube. Through these partnerships, viewers can watch content.<sup>30</sup>

#### B. Leading Internet Television Streaming Devices:

1. Apple TV: This is a device that enables the consumer to watch content from online distributors on a conventional television. Consumers can watch content and also purchase new programming straight from the iTunes store. The Airplay component of the device differentiates it from similar online content to television devices in that it pushes content from other Apple products such as the iPhone and iPad and screen mirroring capability with Mountain Lion enabled laptops. The Apple TV currently retails for \$99.<sup>31</sup>
2. Roku: Similar to the Apple TV, Roku is also a content streaming device. Since its joining with Netflix in 2008, Roku has climbed to use in 37 percent of streaming households compared with 24 percent using Apple TV. The device ranges from \$50 to \$100. Roku, “which generates revenue through hardware

sales, advertising, and channel subscription fees, made over \$100 million in sales last year.”<sup>32</sup>

3. Vudu: Acquired by Walmart in 2010, Vudu is a content delivery system, which is delivered through an add-on device form and through subscription. It operates an “online library of HD movies,” and “enables users to stream movies and watch on Sony PlayStation3, Blu-ray players, HDTV’s, PC’s or Macs, TVs, and home theatres.”<sup>33</sup>
4. Chromecast: This is the most recent device to appear on the market with its debut on July 24, 2013. The Chromecast is a media-streaming adapter in the form of a dongle. A dongle is a small device that plugs into a computer or high definition television and serves as an adapter to enable the streaming of content to high definition enabled televisions. Chromecast enables Google Play Music, Google Play Movies & TV, YouTube and Netflix. Most recently Hulu Plus and Pandora Radio have been enabled on the device.<sup>34</sup>

### C. The Growth of the Cord Cutters and Cord Nevers in Response to Internet TV

“Cord cutters” and “cord nevers” are currently the biggest threat to the current MVPD model, relying entirely on the content that they are able to stream by way of their Internet access and specialty streaming devices. Cord nevers are of particular concern to cable companies. Consisting mostly of tech savvy “20-somethings”, cord nevers have never subscribed to a traditional MVPD service, but rather choose to stream content over Internet

connection. “It’s hard not to be concerned that there’s a growing population growing up not using pay-TV. Alternatives are growing by the day,” as quoted by media research analyst Rich Greenfield of BTIG Research.<sup>35</sup>

Cord cutters are “customers that once bought traditional cable or satellite TV subscriptions, yet have since cut the cord, as it were, and now rely mainly on the programming they can access by way of the Internet.”<sup>36</sup> “Both groups affect the cable industry, which is unlikely to return to the growth in customer numbers it once enjoyed,” as quoted by analyst Ian Olgeirson of SNL Kagan.<sup>37</sup>

“According to the Consumer Electronics Association’s (CEA) latest “U.S. Household Television Usage” report, the number of U.S. households that receive cable TV programming through cable, satellite, and fiber connections has fallen to 83%- down from 88% in 2010. The CEA cited non-TV devices such as computers, tablets, and smartphones, as well as streaming services as a major factor in the drop in cable subscribed households.”<sup>38</sup> Cord cutters and cord nevers today stand at 19 percent of the population, approximately 11 percent claim to be cord cutters while the other 8 percent claim to be cord nevers.<sup>39</sup>

#### D. Virtual Cable Television- A More Efficient Business Model

Virtual cable companies would be able to offer consumers something that MVPDs cannot, which is meaningful choice in the movies and television series consumers choose to watch at a much lower cost. Virtual cable companies would have the luxury of avoiding exorbitant costs of entry and infrastructure building, keeping costs of subscriptions low. Traditional MPVDs, in turn, would have to lower their subscription fees in order to compete with virtual cable companies.

Virtual cable companies would also allow smaller programmers to compete and garner the best deals without being forced to sign over their equity interest to the MVPDs. “Programmers could go directly to consumers without cutting a deal with the MVPD. As a result, programmers would have greater leverage in negotiating with the MVPD, as programmers could reach an audience without being wholly dependent on a few powerful distributors.”<sup>40</sup> A robust online market would allow broadcasters and non-broadcasters alike better distribution options.

### **III. Anti-Competition- Cable’s Stronghold on Distribution**

A great deal of gatekeeping and anti-competitive behavior on the part of the MVPDs has kept virtual cable companies from flourishing in the marketplace. Content lock-outs and crafty agreements have been blamed for online television’s current state. Lock-out strategies are simply one aspect of a long history of anti-competitive behavior in the industry. “Historically, incumbent dominant distributors of any content, for any medium, have tried to stifle emerging competitors by denying them content, almost invariably requiring government action to protect competition.”<sup>41</sup>

#### **A. The History of Anticompetitive Practices Within the Industry**

When cable television entered the market, broadcasters attempted to suppress its operations by denying the cable companies the ability to retransmit programming. Government intervention, in the form of the Copyright Act, was necessary to enable cable companies to compete freely in the marketplace.

The same form of suppression was a reality for satellite companies when they entered the market in the 1980's. At that time it was the cable companies, that were locked out by broadcasters, who were now seeking to block satellite companies from the market. Once again, the government intervened adding to the legislation the exemption of satellite companies as well as cable companies under compulsory licensing schemes.<sup>42</sup> History repeated itself once again with the arrival of phone companies entering the market as distributors, and once again the government had to intervene.

#### B. Internet Distribution Restrictions and the Suppression of Intel's Virtual Cable Service

“Just as the broadcasters attempted to lock out cable operators, and as cable operators attempted to lock out both satellite operators and phone carriers, all three incumbent MVPD industries seek to lock out internet enabled competition.”<sup>43</sup> The MVPDs are now actively trying to suppress the creation of a virtual cable company in development by Intel. The service that Intel is preparing to distribute is one that streams dozens of channels that can be found on MVPD services, over the existing broadband Internet infrastructure.

This model is unlike any Internet streaming service already in existence in that there is no current MVPD type service available over the Internet. The prospect presents the most ominous threat to the existing MVPD stronghold. Although there has been no announcement as to what programmers have signed up to be distributed through Intel, Intel has made it clear that they would be willing to pay more than other distributors for the acquisition of channels for its service. “The distributors are using a variety of methods to pressure the owners of cable channels, which whom they have lucrative long-term contracts, not to sign contracts with upstarts like Intel, that way preserving the status quo.”<sup>44</sup>

MVPDs have been a significant factor in the programmers' apprehension and it comes down to the distribution contracts signed with the MVPDs, "Some contracts include clauses that expressly prohibit the channels to be sold to an Internet distributor like Intel, while other contracts merely discourage such competition by including financial incentives or penalties. So-called most favored nations clauses, which are common, exist to ensure that if another distributor receives a cheaper rate for a channel later, that rate applies across the board." Intel needs a substantial number of channels to break loose from these anticompetitive restraints and sign on to the burgeoning virtual cable company, before they can move forward as a viable service.<sup>45</sup>

The second largest cable company, Time Warner Cable ("TWC"), has been held to be the most aggressive when it comes to content blocking. Time Warner's stance is simply that exclusivity is not anticompetitive as was articulated by a TWC spokeswoman, "Exclusivities and windows are extremely common in the entertainment industry. It's absurd to suggest that in today's highly competitive video marketplace, obtaining some level of exclusivity is anticompetitive."<sup>46</sup>

Richard Greenfield of BTIG Research rejects such an assertion, "They are not paying for exclusivity. They are saying you can sell to X, to Y, and Z, but you are forbidden from selling to this new class called A."<sup>47</sup> Time Warner regularly pays off programmer to prevent web-based streaming.<sup>48</sup> "Incentives to lock-out content providers from streaming their properties online include monetary bonuses and threats to drop programming."<sup>49</sup>

Even without the lock-out strategies looming over Intel, Verizon has shown interest in buying the project out. It is not clear whether Verizon intends to continue to develop the concept of virtual cable television, or is simply attempting to quash a possible competitor. According to Peter Kafka and Arik Hesseldahl, "If Intel seemed like an odd place for a Web TV project,

Verizon makes plenty of sense, at least on paper: It has relationships and reach that Intel never had. Verizon already serves up conventional pay TV to more than five million subscribers via its FiOs unit, and sells broadband access to nearly six million subscribers.”<sup>50</sup>

This move by Verizon may turn out to be a step in the right direction toward a supporting a viable virtual cable television model, or it may be the end of Intel’s effort toward launching a successful product.

### C. Government Oversight and the Justice Department’s Antitrust Probe

All of the aforementioned anticompetitive behavior, in addition to a number of other practices on the part of the MVPDs has drawn the attention of the Justice Department, who began a broad investigation into the restrictive practices of the MVPD industry. The focus of the investigation is possible antitrust issues associated with such anticompetitive practices and the exploration of the possibility that MVPDs are “acting improperly to quash nascent competition from online video.”<sup>51</sup>

One year prior to the commencement of the Justice Department’s probe into the MVPD industry, consumers of Time Warner Cable brought suit against the company for what they perceived to be antitrust violations. *In re Set Top Television Box Anti-Trust Litigation* plaintiff customers of Time Warner Cable company filed suit against Time Warner Cable for an unlawful “tying” arrangement which requires customers to rent cable boxes at exorbitant rates, in order to access “Premium Cable Services” provided by Time Warner.<sup>52</sup>

“A tying arrangement is an agreement by a party to sell one product but only on the condition that the buyer also purchases a different or tied product, or at least agrees that he will not purchase that product from any other supplier.”<sup>53</sup> The court cited that, “The essential

characteristic of an invalid tying arrangement lies in the seller's exploitation of its control over the tying product to force the buyer into the purchase of the tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms.”<sup>54</sup>

Plaintiffs in this case allege Sherman Act antitrust violations with regard to the bundling of products, tying the cable service to the expensive rental of the set-top box which a customer can just as easily buy directly from the set-top box manufacturers.<sup>55</sup> They make the argument that Time Warner Cable uses the boxes to force customers into unnecessary fees and is in essence a restrictive practice.

The court in response to the complaint enters an analysis exploring the tying claims and applying the relevant standard: “Plaintiffs asserting an illegal tying arrangement must plausibly allege first, a tying and a tied product; second, evidence of actual coercion by a seller that forced the buyer to accept the tied product.”<sup>56</sup> The court focuses its analysis on the third factor being, “sufficient economic power in the tying product market to coerce purchaser acceptance of the tied product.” The last two factors taken into consideration are, “anticompetitive effects in the tied market: and fifth, the involvement of a ‘not substantial’ amount of interstate commerce in the tied market.”<sup>57</sup>

The court accepts the argument that Time Warner Cable is participating in product tying in order to coerce customers into paying for multiple products in order to receive one.<sup>58</sup> The court here however takes issue with the satisfaction of the third factor. In order to prove that Time Warner cable was acting in a way to be in violation of the Sherman Act, the plaintiffs had to show that Time Warner by itself had sufficient economic power in the tying product market to coerce purchaser acceptance of the tied product.<sup>59</sup>



In this case, the court cites that the plaintiffs had failed to meet their burden of proving that Time Warner Cable by itself garnered the competitive power and market strength to affect the market with their tying tactics.<sup>60</sup> The court found that plaintiffs' assertions of Time Warner Cable's market power were in the aggregate, and insufficient to support a claim of violation of the Sherman Act.<sup>61</sup> Although the plaintiffs did not prevail against Time Warner Cable in this case, it does serve as a precursor to the current Justice Department probe that is exploring the restrictive practices of the entire MVPD industry.

The Justice Department probe has directed its investigation to a number of concerning areas. Investigators are scrutinizing the use of data-caps that a number of MPVDs have implemented to limit the streaming capabilities of its subscribers. There are concerns that this practice is aimed at discouraging subscribers from discontinuing their cable service in favor of cord cutting.<sup>62</sup>

In particular, Comcast has come under fire for its data-cap policy over its broadband Internet connection, because it made an exception for its own video viewing application on the Xbox which it did not subject to data-caps. This action appears to have been in violation of an agreement made with the Justice Department in securing antitrust approval of its takeover of NBCUniversal. "Under the terms of the settlement, Comcast agreed it would not 'unreasonably discriminate' against other companies transmitting data over its pipes, or treat its own content differently."<sup>63</sup>

The Justice Department is also investigating whether cable, and fiber optics companies are "acting anticompetitively by making viewers have a cable subscription before being able to access certain online programming."<sup>64</sup> This is a very common practice in the industry today, with many cable companies taking it even a step further by requiring subscribers to be within the

reach of the Internet access they receive in their bundled package in order to stream online programming provided by the MVPD.<sup>65</sup> This practice falls under the tying practices found in the *In re Set-Top Cable Television Antitrust* case.

Most importantly, the Justice Department is investigating the legality of the contracts forged between the MVPDs and the programmers, in order for programmers to gain distribution. The Justice Department cites most favored nations clauses, roping programmers into offering the MVPDs the best deal available, as problematic. “The Justice Department is questioning whether there are legitimate business reasons for such terms or whether they are intended to stop programmers from experimenting with other forms of online distribution.”<sup>66</sup>

Although the report on the Justice Department’s investigation into the practices of the MVPD industry has not yet been released, mere existence of an investigation by the Justice Department into the MVPDs unwieldy business practices is indicative of some level of wrong doing on the part of the MVPDs. Whether they surface from this investigation with clean hands is something yet to be seen; however, if the Justice Department takes all of the MVPD anticompetitive tactics into consideration, it will be clear that the MVPDs are using their unbridled power to suffocate any flicker of virtual cable competition.

#### **IV. Compulsory Licensing, Retransmissions, and the Need for Legislative Reform**

Extension of the compulsory licensing exemption under the Copyright Act to virtual cable providers may be the solution to creating a more equitable MVPD marketplace.

Compulsory licensing would provide a nascent industry, such as virtual cable companies, the opportunity to compete and vie for programmers and content on the same level as established MVPDs. The most recent and relevant case with respect to compulsory licensing and Internet

television providers is *WPIX, Inc. v. ivi Inc.* Here, the court had the opportunity to declare Internet broadcast television as a legitimate source of viewing live television, however the courts took a very narrow and outdated view of legislative language relating to compulsory licensing.

#### A. Current Litigation in Internet Television

##### *1. WPIX, Inc. v. ivi Inc.*

In *WPIX*, defendant *ivi*, an online content service, was streaming live broadcasts over the Internet of approximately 30 New York and Seattle based broadcast television stations. Plaintiff companies who brought suit were: ABC, Disney Enterprises, CBS, The CW Television Stations, Inc., Universal Network Television, Telemundo, NBC, and Fox. A preliminary injunction had been issued on *ivi* to prevent them from streaming the content. The principal issue the court addressed, that was raised as an argument by *ivi*, was whether *ivi*'s Internet streaming service constituted a cable system under the compulsory licensing exemption of the Copyright Act.<sup>67</sup>

Section 111(c)(1) of the Copyright Act reads in pertinent part:

“Secondary transmissions to the public by a *cable system* of a performance or display of a work embodied in a primary transmission made by a broadcast station licensed by the Federal Communications Commission... shall be subject to statutory licensing upon compliance with the requirements of subsection (d) where the carriage of the signals comprising the secondary transmission is permissible under the rules, regulations, or authorizations of the Federal Communications Commission.”<sup>68</sup>

The definition of “cable system” held special relevance in this case. As it is defined in the statute, a “cable system” is defined as:

“a facility, located in any State, territory, trust territory, or possession of United States, that in whole or in part receives signals transmitted or programs broadcast by one or more television broadcast stations licensed by the Federal Communications Commission, and makes secondary transmissions of such signals or programs by wires, cables, microwave, or other communications channels to subscribing members of the public who pay for such service. For purposes of determining the royalty fee under subsection (d)(1), two or more cable systems in contiguous communities under common ownership or control or operating from on headend shall be considered as one system.”<sup>69</sup>

The court explores the literal meaning of the term cable systems and concludes that the definition is ambiguous with respect to Internet television providers, claiming that it is unclear whether transmissions over the Internet “is or utilizes the facility, that receives and transmits signals, through wire, cables, microwave, or other communication channels.” The court here focuses too narrowly on the literal meaning and glazes over what would stand to be the most relevant part of the definition of a “cable system” --the clause referring to “other communications channels.” The legislative inclusion of such language would indicate to any reader that the legislature intended to include future conceptions of communication channels, not conceived at the time the Act went into effect.

In its discussion of legislative history the court cites that “compulsory licensing not only protects the commercial value of copyrighted works but also enhances the ability of cable systems to retransmit such programs... thereby allowing the public to benefit by the wider dissemination of works carried on television broadcast signals.” If this is the purpose of compulsory licensing in the context of cable systems, then why would it make sense that the

understanding of compulsory licensing should not be extended to Internet TV providers? What would logically follow in a progressive society is that new developments and technologies within similar communication channels be afforded the same rights and privileges as what is afforded to existing technologies.

The court ultimately decided that ivi. was not a cable system<sup>70</sup> and as such was not entitled to a compulsory license for their over the Internet broadcasts. ivi was enjoined from further retransmissions. This outcome is indicative of a refusal by the judiciary to view the Internet as a viable and legitimate mode for broadcasts. Ultimately, the only way to allow virtual cable companies a fair chance to enter the market place is for Congress to extend the current meaning of the compulsory license exemption.

## *2. Aereo & BarryDriller-- Circuit Split*

A recently decided Second Circuit case, *WNET, Thirteen v. Aereo*, marks the champion of Internet television broadcasters. However, it has simultaneously created a circuit split with the Ninth Circuit by way of *Fox Television Stations, Inc. v. BarryDriller Content Systems*. Both address online redistribution of broadcast network television programs. *Aereo* survived judicial review, while *Fox* did not.

In *Aereo*, founders of the Internet streaming company developed a new way to transmit broadcasts over the Internet to be received by an individual digital antennae device that is personal to each subscriber. The device functions in a way that each digital antennae has its own transmitter at the central hub of Aereo. Subscribers have access to both live and recorded broadcasts for which they paid a monthly fee. A number of broadcast companies, including Fox,

Univision and the Public Broadcasting Service, brought suit against Aereo for infringing the exclusive right of the copyright owners “to perform the copyrighted work publicly.”<sup>71</sup>

In pertinent part 17 U.S.C. §106(4) provides that performing work publicly means:

(1) To perform or display it at a place open to the public or at any place where a substantial number of person outside of a normal circle of a family and its social acquaintances is gathered; or

(2) To transmit or otherwise communicate a performance or display of the work to a place specified by clause (1) or to the public, by means of any device or process, whether the members of the public capable of receiving the performances or display receive it in the same place or in separate places and at the same time or different times.”<sup>72</sup>

The court concluded that, “because each subscriber has access to a single copy of a broadcast through that single antenna, and no other subscribers can receive a transmission from that copy, the Second Circuit held that the transmission did not constitute a public performance.”<sup>73</sup> In effect, Aereo has used the Internet and a device that sends signals personal to the subscriber to get around the question of public performance in broadcast, which would require the ability to purchase a compulsory license, as was denied to *ivi* in the previous case resulting in a permanent injunction.

There were similar facts, yet an opposite outcome in *Fox Television Stations, Inc. v. BarryDriller Content Systems*. Broadcast television networks brought suit against the BarryDriller Content Systems streaming company for infringing their copyrights by retransmitting broadcasts using Internet connection. BarryDriller had a similar personal digital receiver set-up as the devices at Aereo. The Ninth Circuit rejected the reasoning in Aereo and “enjoined a ‘technologically analogous’ broadcast system.”<sup>74</sup>

The outcomes of these cases have left a split in authority between the Second and Ninth Circuits. Unless there is a restoration of harmony among the circuits, the split may make a good case for Supreme Court review. Allowing for Internet television companies to be eligible for compulsory licensing would bypass this circuit split and make way for a more fair and competitive MVPD marketplace.

#### B. A Recommendation for Industry-Wide Compulsory Licensing

When taking into consideration Internet television companies' severe lack of bargaining power, legislation enacted in favor of the existing MVPD industry and a judiciary confused about the influence of Internet television and its far reaching impact on the lives of today's consumers, it is clear that Internet television providers and virtual cable start-ups deserve adequate protection once afforded to nascent cable, satellite, and fiber optics companies many years ago. Compulsory licensing for both broadcast and non-broadcast programmers should be available industry-wide to level the playing field for virtual cable company start-ups.

On the opposite end of the pro-compulsory licensing position, there is a pro-MVPD contingent that believes that all compulsory licensing as it relates to cable, satellite and telephone companies, should be repealed. Preston Padden, former president of ABC and former executive vice-president of The Walt Disney Company testified before the Subcommittee on Courts, IP and the Internet advocating for the repeal of the compulsory license for MVPDs.<sup>75</sup>

His reasoning is as follows: "Subject to a brief transition period, Congress should repeal the cable and satellite compulsory licenses in 17 U.S.C. Sections 111, 119 and 122. At the same time Congress should repeal the retransmission consent provision in 47 U.S.C. Section 325 (b)(1)(A) and legislatively repeal the FCC's regulations governing network non-duplication,

syndicated exclusivity and blackouts.”<sup>76</sup> He insists that, “The end result would be to put cable and satellite distribution of broadcast television programs under the same legal regime as the distribution of non-broadcast programs- namely, simple free market copyright negotiations.”<sup>77</sup>

Mr. Padden makes the claim that repealing the compulsory licensing scheme would in fact create a level playing field for any company that seeks to enter the MVPD marketplace.<sup>78</sup> The claims made during Mr. Padden’s testimony are simply out of context with the realities of the marketplace today. With the ever-growing pressure of the MVPDs to maintain status quo and effectively shut out any viable competitors such as the virtual cable companies, by way of their anticompetitive tactics, there can never be any meaningful freedom of competition without some sort of government intervention. Here, we have a marketplace that is being manipulated by the MVPDs and the intervention of the government by imposing a compulsory licensing scheme is the only way to rectify such bad acts.

Congress must reform the current laws and extend compulsory licensing beyond its current meaning. Throughout history, compulsory licensing has been used to rectify failing markets, today the MVPD industry is a failing market in that its sole purpose is to constrict competition. Compulsory licensing in this sense must be extended to Internet television companies, specifically virtual cable providers for both broadcast and non-broadcast programming. This shift would allow for Internet television companies to compete in the marketplace at designated agreed upon licensing fees set across the board by industry leaders. Compulsory licensing in this form would dissipate the ability of the MVPDs to manipulate distribution agreements and pricing to lock out virtual cable television competitors.



### C. Recommended Statutory Language

The proposed language would read as follows:

*Compulsory Licensing Reform Act: Limitations on Exclusive Rights- Secondary Transmissions of Broadcast and Non-Broadcast Programming by a Multi-Channel Video Programming Distributor*

Secondary transmissions to the public by a multi-channel video programming distributor, of a performance or display of a work embodied in a primary transmission made by a broadcast or non-broadcast station licensed by the Federal Communications Commission shall be subject to statutory licensing set by industry, upon compliance with the requirements of subsection where the carriage of the signals comprising the secondary transmission are permissible under the rules, regulations, or authorizations of the Federal Communications Commission.

A “multi-channel video programming distributor” should be construed broadly and is defined as: “an entity, whether physical or virtual, based in any State, territory, trust territory, or possession of United States, that in whole or in part receives signals transmitted by one or more television broadcast and non-broadcast stations licensed by the Federal Communications Commission, and makes secondary transmissions of such signals or programs by wires, cables, Internet, or other communications channels to subscribing members of the public who pay for such service.

## **VI. Conclusion**

Consumers deserve a marketplace that is free from collusion and anticompetitive practices. When government permits such actions to persist, the consumers are the ones who bear the burden of the greed perpetuated by today's MVPDs. The most efficient actor, virtual cable companies must be given a chance to thrive. The government should intervene with an appropriate compulsory licensing scheme to rectify the wrongs of the MVPD industry.

In the future Internet television providers, particularly virtual cable companies will mostly likely render MVPDs obsolete. Until then, the MVPD industry will fight to maintain dominance over the field, whatever the cost may be.

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