Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
Expanding Consumers' Video Navigation Choices	)	MB Docket No. 16-42
Commercial Availability of Navigation Devices	)	CS Docket No. 97-80

REPLY COMMENTS OF

THE FREE STATE FOUNDATION[*]

I. Introduction and Summary

These reply comments are submitted in response to comments submitted in this proceeding that offer unjustified calls for harmful, stringent regulation of video devices and apps. In particular, these reply comments respond to pro-regulation comments that fail to address the significant legal and policy problems raised by the Commission's proposed rulemaking. The Commission should *not* impose the video device and app regulations proposed in its Notice.

The principal points raised in these reply comments are: (1) the Commission lacks statutory authority for its proposed video device and app regulations; (2) the proposed standards body poses improper sub-delegation, an unworkable timeline, and patent litigation concerns; (3) the lack of cost-benefit analysis is a strong indicator of arbitrary policymaking, offering illusory benefits and likely harms that would distort a video market the Commission already has recognized as effectively competitive; (4) banning MVPDs from subsidizing the video devices they offer would harm consumers by depriving them of options for avoiding up-front costs for

[*] These reply comments express the views of Randolph J. May, President of the Free State Foundation, and Seth L. Cooper, Senior Fellow. The views expressed do not necessarily represent the views of others associated with the Free State Foundation. The Free State Foundation is an independent, nonpartisan free market-oriented think tank.

devices; (5) the proposed regulations raise serious copyright concerns that comments supporting regulation do not take seriously; and (6) the proposed regulations pose free speech problems under the First Amendment, despite the unconvincing arguments of pro-regulatory comments to the contrary.

Regulations proposed in the Notice go far beyond the Commission's authority under Section 629 of the Communications Act. That Section is directed toward ensuring commercial availability of "equipment" for accessing MVPD service, not a wide-ranging mandate to regulate "information flows" or video apps. Both the Commission and comments supporting its regulation misguidedly urge that software or apps be "read into" the term "equipment." But such a reading is not within the ordinary meaning of "equipment" and nothing in the statutory context alters the ordinary meaning. Further, legal precedent does not permit the expansive reading of Section 629 offered by the Commission and by comments supporting the proposed technical mandates. The U.S. Court of Appeals for the District of Columbia Circuit decision in *EchoStar v. FCC* (2013), for instance, "refuse[d] to interpret ancillary authority as a proxy for omnibus powers limited only by the FCC's creativity in linking its regulatory actions to the goal of commercial availability of navigation devices."

Unfortunately, the Notice appears premised on the erroneous idea that numerous unresolved issues regarding technical mandates and rule implementation can be circumvented by passing the buck to a proposed external "Open Standards Body." But the Commission's overreliance on an external standards body would constitute an improper delegation of agency authority. Mandating a set of technical standards for making "information flows" available to third parties necessarily involves substantial regulatory decision-making power. Legal precedent, including the U.S. Court of Appeals decision in *U.S. Telecom Association v. FCC* (2004),

disfavors sub-delegations of authority such as the Notice's proposed conferral of authority on the standards body. Courts will not read such authority into Section 629, which lacks a clear statement authorizing the kind of sub-delegation proposed in the Notice.

Further, the Commission has given the standards body an unrealistic and unworkable 2-year timeline for establishing new standards to comply with the Notice's technical mandates. For that matter, standards bodies typically include members that have voluntarily, even if reluctantly, come to the table to participate in the development process. The membership dynamic will not hasten the contemplated standards body's completion of its proposed assignment. Needless to say, the Commission's proposal to develop its own technical standards as a backstop will likewise hamper the standards body's progress. Members that favor the Commission's backdrop would have little to no incentive to compromise.

Given the magnitude of the proposed rulemaking's impact on the technology, business model, and economic arrangements of the video services and device markets, the absence of any cost-benefit analysis of the proposed regulations by the Commission constitutes strong evidence that its proposal is arbitrary and capricious. When markets are demonstrably competitive and innovative, it is unwise to distort them by overriding existing trends benefiting consumers with government mandates whose cost-benefit calculus is unknown or unknowable. In its *Effective Competition Order* (2015), the Commission recognized the competitiveness of the video services market. Data collected in the *Seventeenth Video Competition Report* confirms that competitive conclusion. The Commission's lack of any estimate of the costs and benefits of its proposed regulation surely weighs against imposing technical mandates on video devices, information flows, and apps in the competitive environment now known to exist.

Nor should the Commission ban MVPD providers from subsidizing the costs of video

devices they make available to their subscribers. Cross-subsidies might be a concern if market power existed and facilitated higher rate charges to provide subsidies. But no market power problem has been shown to exist. It is anti-consumer to ban MVPDs from offering subscribers the ability to avoid paying up-front costs for equipment for accessing video services. A ban would also impose burdens on MVPDs that third-party device manufacturers would avoid. And such a ban would impose special burdens on DBS providers that would have no choice but to charge subscribers up front the costs for video devices. DBS services require set-top box devices for interfacing with dishes. Unlike other MVPDs, DBS providers could not work around such a ban by an exclusively apps-based model for content delivery.

Initial comments that we filed in this proceeding explained that the proposed regulations would undermine the exclusive rights of video programmers in copyrighted content. Some comments filed in this proceeding have confirmed these concerns by their insistence that third-party device makers should not be subjected to licensing terms regarding the display of copyrighted video content because they are not contracting parties with the video programmers. Other comments all but ignored or downplayed this serious concern. Yet the concern is real. Simply put, the Commission proposes to force MVPDs to make their information flows available to third-party device makers, leaving MVPDs without the means to enforce their contracts and intellectual property rights. The proposed regulations would benefit third-party device makers that choose to use video programming content in ways inconsistent with licensing terms accepted by MVPDs as a condition of carriage and inconsistent with copyrights.

Pro-regulatory comments in this proceeding do not articulate a reasoned defense of the Commission's proposed rulemaking on free speech grounds. But the Commission's proposal should, at minimum, be subject to intermediate scrutiny under the Supreme Court's First

Amendment jurisprudence. Given the state of competition in the video market, the Commission cannot establish a substantial government interest to support its proposed regulations. And it is highly doubtful the Commission can justify its rejection of careful tailoring in its proposal, which sweeps so broadly with intrusive technical mandates.

The Commission should jettison its proposed regulations and allow market entrepreneurs and innovators to lead us into an apps-centric future for viewing MVPD and other video services. Consumers will be better served by the availability of new choices for video viewing under a policy favoring continued operation of the innovative and competitive forces.

II. The Commission Lacks Authority to Impose Its Proposed Technical Mandates on Video Devices, Delivery of MVPD Services, and Video Apps

The Commission lacks statutory authority under Sections 629 for much of its proposed technical mandates.[1] The text of Section 629 addresses "Commercial consumer availability of equipment used to access services provided by multichannel video programming distributors."[2] The Commission was not charged by Section 629 to regulate "information flows" or video apps. Nor was the Commission authorized to alter the MVPD services being accessed by consumers using MVPD-provided or third party-provided equipment. Section 629(f) puts an exclamation mark behind the narrow scope of Commission authority: "Nothing in [Section 629] shall be construed as expanding or limiting any authority that the Commission may have had under law in effect" prior to the law going into effect.[3]

Legal precedents do not offer the Commission a way to work around the clear limits on agency authority contained in law. Indeed, the U.S. Court of Appeals for the District of Columbia Circuit decision in *EchoStar v. FCC* (2013) rejected previous claims of exaggerated

[1] *See, e.g.*, Comments of ACA, at 60-74; Comments of NCTA – Appendix A, at 12-29.
[2] 47 U.S.C. § 549(a).
[3] 47 U.S.C. § 549(f).

authority to regulate video devices pursuant to Sections 629 and 624A.[4] In its decision striking down encoding regulations, the D.C. Circuit addressed the Commission's claims of authority based on Section 629 and concluded "the statute's language is not as capacious as the agency suggests."[5] In the Section 629 context, the D.C. Circuit declined to defer to a broad agency interpretation of the Commission's ancillary power: "[W]e refuse to interpret ancillary authority as a proxy for omnibus powers limited only by the FCC's creativity in linking its regulatory actions to the goal of commercial availability of navigation devices."[6] The D.C. Circuit similarly declined to defer to agency claims of authority over MVPDs other than cable operators based on Section 624A. It reasoned that "[t]he FCC is powerless to wield its ancillary jurisdiction, however, where 'there are strong indications that agency flexibility was to be sharply delimited.'"[7] And it added: "Section 624A's textual delegation of authority to regulate cable systems, as opposed to all MVPDs, is precisely such an indication."[8]

Comments supporting the Commission's proposed regulations do not comport with the *EchoStar* decision and its underlying reasoning. They focus on language authorizing the Commission to "adopt regulations" and other terms that are beside the over-arching point that Section 629 is directed toward equipment, not video services.[9] And the term "equipment" simply does not admit an interpretation to allow it to mean or include "app." Those comments read into the text a meaning it does not contain in its natural sense or in its context.

Nor does the STELAR Act of 2014 expand the Commission's authority under Section 629

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[4] 704 F.3d 992 (D.C. Cir. 2013). *See also* Seth L. Cooper, "A Recent Appeals Court Ruling on Ancillary Power Limits Could Curb Regulatory Overreach," *Perspectives from FSF Scholars*, Vol. 8, No. 5 (February 12, 2013), available at: http://www.freestatefoundation.org/images/A_Recent_Appeals_Court_Ruling_on_Ancillary_Power_Limits_Could_Curb_Regulatory_Overreach_021113.pdf

[5] 704 F.3d, at 997.

[6] 704 F.3d, at 999.

[7] 704 F.3d, at 999.

[8] 704 F.3d, at 999.

[9] Comments of Public Knowledge, at 6 (citing Notice, at 21-22).

as claimed in comments.[10] STELAR's mandate was narrowly targeted. The Commission was directed to establish a working group to recommend "a not unduly burdensome, uniform, and technology- and platform-neutral software-based downloadable security system in furtherance of section 629."[11] This targeted provision coincided with Congress's repeal of the Commission's misguided integration ban that prohibited single devices from containing both conditional access and security functions. The Commission's ban actually prohibited devices from downloading security functions from the Internet. Here, the Commission cannot be said to be merely proposing not unduly burdensome downloadable security standards obtained in consultation with a working group. The Notice reaches far beyond downloadable security, sweeping in content, apps, and more. For that matter, the proposed technical mandates *are* unduly burdensome.

III. The Commission's Delegation of Authority to an Outside Body Is Improper and Poses Process and Policy Problems

The Notice appears premised on the erroneous idea that numerous unresolved issues regarding technical mandates and rule implementation can be circumvented by passing the buck to a proposed external "Open Standards Body."[12] This is problematic in several respects.

First, the Commission's overreliance on an external standards body constitutes an improper delegation of agency authority. Comments filed in this proceeding have persuasively analyzed the nature of this improper delegation.[13] The work that the Notice proposes to task the standards body to do involves regulatory decision-making. This includes determining specifications for making so-called "information flows" to third-party device makers and a variety of other decisions necessary to flesh out myriad technical aspects of the Commission's new definitions

[10] Comments of Public Knowledge, at 7.
[11] Pub. L. No. 113-200, 128 Stat. 2059 § 106.
[12] In the Matter of Expanding Consumers' Video Navigation Choices, Notice of Proposed Rulemaking (Notice), MB Docket No. 16-64, CS Docket No. 97-80, at § 41 (released February 18, 2016).
[13] *See, e.g.*, Comments of American Cable Association (ACA), at 74-84; Comments of AT&T, at 102-103; Comments of the National Cable & Telecommunications Association (NCTA) – Appendix A, at 66-69.

for "service discovery," "entitlements," and "content delivery." Substantial discretionary authority is certainly required to make those determinations. Yet such an external standards body and such a wide-ranging task in the Notice are nowhere authorized by Congress. Its members are not public officials who have sworn oaths to uphold and defend the Constitution and laws of the United States in a recognized official capacity. Legal precedents cited by comments in this proceeding, including the U.S. Court of Appeals decision in *U.S. Telecom Association v. FCC* (2004), disfavor sub-delegations of authority such as the Notice's proposed conferral of authority on the standards body.[14] Courts will not read such authority into that statute where a clear statement is lacking, as is the case with Section 629.[15] Even assuming for the sake of argument that Congress delegated the Commission authority to regulate MVPD-provided information flows, video apps, and the like, the Commission cannot rightfully transfer its governing authority to private parties.

Second, the Commission has given the standards body an unrealistic and unworkable timeline for establishing new standards to comply with the Notice's technical mandates. The Commission's mere reliance on a one-year estimate by certain pro-regulatory market participants is unreasonable.[16] The reality is that technical standards typically take much longer to develop. In this instance, the Commission has underestimated the time necessary for responsible development of standards by at least 50%.[17] A critical factor overlooked by the Commission in this respect is standards body membership dynamics. Standards bodies typically include members that have voluntarily, even if reluctantly, come to the table to participate in the development process. However, the member composition contemplated by the Notice is different

[14] 359 U.S. 554, 566 (D.C. Cir. 2004) (cited in Comments by Comments by AT&T, at 102-103; Comments of NCTA – Appendix A., at 67-68.
[15] *See* 359 U.S. at 565-568.
[16] *See* Notice, at § 43.
[17] *See* Notice, at 43 (proposing MVPDs be required to comply with new rules two years after adoption).

in this critical respect: several of its members will be effectively forced by the Commission to participate. It is a matter of common sense that forced participation is not conducive to consensus decision-making. Further, the Commission's proposal to develop its own technical standards as a backstop will further hamper the environment in which the standards body would have to work.[18] Standards body members that favor the Commission's backdrop would have little to no incentive to compromise with members of the standards body with whom they disagree.

Third, the Commission's reliance on open standards to be produced by the external standards body risks spawning patent litigation. Once imposed, the Commission's proposed regulations would displace existing marketplace providers' reliance upon proprietary rights and intellectual property in favor of standardization. All things being equal, patent litigation is not a bad thing; it is necessary for enforcement of intellectual property rights. However, when unwise government regulation spawns patent litigation, such litigation is a consequence of government's wrongful disturbance of the ascertainability and security of IP rights, which also undermines the value of IP. Comments have astutely pointed out that a mandated standardization process can result in an entire industry being locked in to a particular standard for which one or a few key patent owners could gain market power over the rest of industry and extract above-market royalty rents.[19] Also, Section 1498(a)'s exclusive remedy provision for patent infringements occurring "for the government" and "with the authorization or consent of the Government" would be triggered by the Commission's proposed rules requiring MVPD compliance with its mandated technical standards for making information flows available.[20] The Commission's proposal to impose standardization in the video space will likely result in market participants diverting resources from continuing innovation to vindicating their IP rights from regulatory

[18] *See* Notice, at § 43.
[19] Comment of NCTA – Appendix A, at 60.
[20] Comment of NCTA – Appendix A, at 61-62 (citing 28 U.S.C. § 1498(a)).

arbitrage. Diversion of resources and extra costs will not benefit consumers. If anything, providers will recover those increased costs from consumers through higher prices.

IV. The Commission's Failure to Undertake a Cost-Benefit Analysis Is Legally Problematic and Symptomatic of Arbitrary Policymaking

The Commission's failure to undertake any serious cost-benefit analysis of its proposed regulations or to even express genuine interest in the costs is another profoundly troubling aspect of the Notice. First, the Commission's lack of consideration of the costs is surely inconsistent with the spirit, if not the letter of the STELAR Act's requirement that a working group recommend a "not unduly burdensome" downloadable security standard.[21] Given the magnitude of the proposed rulemaking's impact on the technology, business model, and economic arrangements of the video services and device markets, the absence of careful attention to the reasonably foreseeable costs of its proposed regulations constitutes strong evidence that the Commission's proposal is arbitrary and capricious.

When markets are demonstrably competitive and innovative, it is unwise to distort such markets and override existing trends benefiting consumers with government mandates whose cost-benefit calculus is unknown or unknowable. The Commission has recognized that the video services market is characterized by effective competition. Data collected in the *Seventeenth Video Competition Report* doubles down on that competitive conclusion.[22] Indeed, there is also ample evidence of innovation and choice in video devices and video apps for viewing content. (*See* Appendix A.) The Commission's lack of any estimate of the costs and benefits of its

[21] *See, e.g.*, Comment of AT&A, at 100.

[22] In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, *Seventeenth Report*, MB Docket No. 15-158 (Media Bureau) (released May 6, 2016), available at http://transition.fcc.gov/Daily_Releases/Daily_Business/2016/db0509/DA-16-510A1.pdf. For a summary of how the data contained in the report does not support the technical mandates proposed in the Notice, *see* Seth L. Cooper, "Video Report Data Undermine the FCC's Rationale for New Device Regulations," *Perspectives from FSF Scholars*, Vol. 11, No. 16 (May 20, 2016), available at: http://www.freestatefoundation.org/images/Video_Report_Data_Undermine_FCC_s_Rationale_for_New_Device_Regulation_052016.pdf. The paper is attached to this reply comment as Appendix A.

proposed regulation surely weighs against imposing those regulations on the innovative and competitive environment now known to exist. So, too, the Commission's track record of imposing video device regulations that have imposed unforeseen costs on industry and consumers with unrealized benefits – including the FireWire mandate, the integration ban, and the CableCARD regime as a whole – warrants rejection of intrusive and wide-ranging regulations that are completely unsupported by cost-benefit analysis.

In failing to undertake a cost-benefit analysis of its proposed video device and app regulations, the Commission overlooks the likely regulatory costs to smaller MVPDs. They are less likely to absorb such costs than their larger competitors. The Commission's proposed regulations are thus likely to put smaller MVPDs at a distinct competitive disadvantage and harm consumer welfare by artificially reducing the supply of available choices for video services.

V. Banning MVPD From Subsidizing Video Devices Would Harm Consumers and Put DBS Providers at Competitive Disadvantage

Nor should the Commission ban subsidies by MVPD providers for video devices made available to their subscribers.[23] Cross-subsidies may be a valid concern where market power conditions allow a monopolist to pay for those subsidies through higher rate charges. But there is no identifiable market power problem requiring such a heavy-handed restriction. The *Effective Competition Order* (2015) bolsters the Commission's decision *not* to impose such a ban in its *First Report and Order* (1998). Reversing that precedent in 2016 would make no sense. It is anti-consumer to ban MVPDs from offering their subscribers or potential subscribers the ability to avoid paying up-front costs for equipment necessary for accessing video services. A ban on MVPDs subsidizing the costs of video devices offered to their subscribers is also anti-competitive. In essence, it is a form of price control. And it would impose burdens on MVPDs

[23] Notice at §§ 85, 86.

that third-party device manufacturers would avoid. More so, such a ban would impose special burdens on DBS providers. Whereas cable and other MVPD services have the potential to eventually transition away from physical set-top boxes altogether and deliver their services entirely through apps, DBS services require physical set-top box devices for interfacing with dishes and providing access to subscribers. Non-DBS MVPDs would eventually be able to work around such ban by advancing to an exclusively apps-based model for delivery of video services. DBS, however, would be at a competitive disadvantage in attracting new subscribers who would have no choice but to pay the up-front costs for a video device.

Comments supportive of the ban fail to take seriously the effectively competitive state of the market and ignore the consumer benefit of avoiding up-front costs for MVPD-provided video devices.[24] To impose restrictions on MVPDs in an effectively competitive market in order to prop up market rivals is misguided competitor welfare policy, not consumer welfare policy.

VI. Contrary to Claims Made in Supporting Comments, the Proposed Regulations Pose Serious Copyright Problems

Comments supporting the Commission's proposed regulations fail to take seriously or address the serious copyright concerns involved. As initial comments filed by the Free State Foundation explain,[25] the Commission's proposal would undermine the exclusive rights of video programmers to control the reproduction, distribution, and public performance of copyrighted video content by making such content available to third-party device makers that have not obtained licenses. Pro-regulation comments have confirmed these concerns by insisting that third-party device makers should not be subjected to licensing terms regarding the display of

[24] *See* Comments of Public Knowledge, at 52-52; Comments of TiVo, at 30-32; Comments of the Consumer Video Choice Coalition (CVCC), at 46-48.
[25] Comments of the Free State Foundation (FSF), at 13-14, available at: http://apps.fcc.gov/ecfs/document/view?id=60001688291.

copyrighted video content because they are not contracting parties with the video programmers.[26] Other comments in this proceeding all but ignored or downplayed this serious concern.[27] Yet the concern is real, based not only on the Commission's proposal to force MVPDs to make all of their information flows available to third-party device makers, but the lack of enforceability when parties benefitting by such regulations choose not to use copyrighted content consistent with the licensing terms upon which MVPDs secured program carriage rights.

The claim made in comments that the Commission has authority to impose the regulations proposed in the Notice because the Congress passed both the Copyright Act and the Communications Act puts the cart before the horse.[28] Such a claim essentially assumes the Commission was delegated authority under Sections 629 and 624A to impose the regulations proposed in the Notice. That profoundly mistaken assumption is the key issue to be decided. However broad the Commission's authority under those Sections, they provide no specific bases or clear statement for any new regulatory exceptions to copyright protections provided in the Copyright Act. For the Commission to conclude otherwise would be contrary to widely acknowledged canons of statutory construction, including the general rule that statutes are to be read in harmony with each other and the presumption against implied repeals of statutes.

The proposed regulations' interference with intellectual property rights likely extends beyond impairment of the exclusive rights under the Copyright Act. The proposed regulations appear to give cover to commercial misappropriation of copyrighted content by video programmers. MVPD rights obtained under licensing agreements and other proprietary rights in their channel lineup, tier placements, advertising arrangements, and branding are also potentially subject to commercial misappropriation facilitated by the proposed regulations.

[26] *See*, e.g., Comments of TiVo, at iii.
[27] *See*, *e.g.*, Comments of Google, at 4; Comments of Public Knowledge, at 45-47.
[28] *See* Comments of Public Knowledge, at 10-11.

VII. Contrary to Claims Made in Supporting Comments, the Proposed Regulations Pose Significant Free Speech Problems

Finally, comments supporting the Commission's proposed regulations fail to adequately address the serious First Amendment free speech problems posed by the Notice. As explained in initial comments filed by the Free State Foundation,[29] the Commission's proposal should at minimum be subject to intermediate scrutiny under the Supreme Court's First Amendment jurisprudence. Given the state of competition in the video market, it is doubtful the Commission can establish a substantial government interest behind its proposed regulations. And it is highly doubtful the Commission can justify its rejection of careful tailoring in its proposal, which sweeps so broadly with intrusive technical mandates.

To the extent pro-regulatory comments in this proceeding even address First Amendment issues, they do not articulate a reasoned defense of the proposed regulations on free speech grounds. One comment offering an empty one-line defense on First Amendment grounds cites to an irrelevant Supreme Court case addressing the originality requirement in copyright law.[30] Another comment turns the First Amendment upside down by treating it as an affirmative grant of power to promote speech through government regulation.[31] But the First Amendment is a restriction on government power over the speech by private actors. Hence the opening lines of the First Amendment "Congress shall make no law... abridging the freedom of speech."

[29] Comments of FSF, at 15-16.
[30] Comments of CVCC, at 34 (citing *Feist Publications, Inc. v. Rural Telephone Services Co*., 499 U.S. 340, 347-348 (1991)).
[31] Comments of Public Knowledge, at 13-14.

VIII. Conclusion

For the foregoing reasons, the Commission should act in accordance with the views expressed herein.

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