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MUSIC LICENSING REFORM

HEARING

BEFORE THE

SUBCOMMITTEE ON INTELLECTUAL PROPERTY

OF THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

ONE HUNDRED NINTH CONGRESS

FIRST SESSION

JULY 12, 2005

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MUSIC LICENSING REFORM

TUESDAY, JULY 12, 2005

UNITED STATES SENATE,
SUBCOMMITTEE ON INTELLECTUAL PROPERTY,
COMMITTEE ON THE JUDICIARY,
Washington, D.C.

The Subcommittee met, pursuant to notice, at 2:38 p.m., in room SD–226, Dirksen Senate Office Building, Hon. Orrin G. Hatch, Chairman of the Subcommittee, presiding.

Present: Senators Hatch and Leahy.

OPENING STATEMENT OF HON. ORRIN G. HATCH, A U.S. SENATOR FROM THE STATE OF UTAH

Chairman HATCH. We will begin this hearing. Senator Leahy is here. He is on the phone, but he said it is fine if I move on ahead.

Good afternoon. I welcome you all to today's hearing on music licensing reform. This is the first of what will likely be a series of hearings on whether changes to current copyright law are needed to encourage rapid deployment of legal online music services, while ensuring the equitable compensation of creators and copyright holders.

Now that some of the fundamental liability issues involved in the Grokster case have been resolved, our focus turns in part to a variety of difficulties that hinder the ability of legal online services to compete effectively against illegal download and file-sharing services. At this hearing, I hope we can begin to identify some of the perceived problems faced by a number of companies and businesses in the area of music licensing. Although the discussion will center principally on Section 115 and the mechanical compulsory license, I hope today's hearing will also help us gain a better understanding of some of the emerging business models and any impediments to their development.

Section 115 of the Copyright Act governs the compulsory license that allows a licensee to make and distribute a mechanical reproduction of a non-dramatic musical work without the consent of the copyright owner. The compulsory license appears to have been enacted in response to concerns about the potential for a monopoly in the market for player piano rolls.

In spite of various amendments and occasional suggestions that it be repealed, Section 115 and the mechanical compulsory license have survived enormous changes in the music industry and are still with us almost a century later. And despite attempts by Congress and the Copyright Office to alter the terms and application of the license in response to new business models, it is reported

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that use of the compulsory license has steadily declined to the point that it may be the exception rather than the rule.

Currently, there appears to be near consensus that Section 115 is outdated and, particularly in the online world, does not adequately serve the purposes for which it was intended. Some argue that changing the marketplace for music products and the evolution of online music services has made Section 115 obsolete.

In sum, we appear to be at a point where there is widespread agreement that the current compulsory license simply does not work. However, from my perspective, there appears to be little or no agreement among experts, academics and industry participants regarding what can or ought to be done about these problems.

Some of the difficulties identified involve the application of a system in which two sets of distinct mechanisms, organizations and practices have evolved for the licensing of different rights in the same musical work—one for the public performance rights and the other for the reproduction and distribution rights.

Especially when dealing with new types of services and uses that do not fit easily into familiar categories and concepts, it is often unclear precisely which rights are implicated. Understandably, some argue that many new uses, especially those involving digital transmission and storage, implicate both sets of rights and thus may require separate licensing by two different entities for the same song on behalf of the same copyright owner.

It is claimed by some that this scheme of licensing imposes inefficiencies and burdens that unreasonably delay or prevent deployment of some new services and limit the potential success of others. Today, I expect that we will hear different opinions about both the scope and seriousness of the difficulties caused by the uncertainty as to which rights are implicated by new services and online activities, as well as what, if any, changes to copyright law are necessary to address this set of problems.

Like the Register of Copyrights and others, I would like to see a solution that focuses on two goals that are inherent in copyright policy: ensuring that creators are compensated fairly and facilitating consumer access to good music.

A second set of concerns involving the burdens and inefficiency of the specific terms and operation of the compulsory license itself also appears to figure prominently in the debate on music licensing reform. Some argue the license is sufficiently burdensome to severely limit its usefulness both in the physical and virtual marketplace. Again, I anticipate that there will be some disagreement as to the nature and scope of the problems posed by some of the specific provisions of Section 115, as well as what should be done to address these provisions.

A wide variety of remedies to problems identified by the stakeholders and others have been proposed to date. They range from incremental reforms to wholesale repeal of Section 115. In addition to helping us identify and define these problems, I hope that our witnesses today will help the Subcommittee understand the range of possible solutions that have been proposed and the implications, both positive and negative, of such solutions for various segments of the music industry.

On our first panel, we are pleased to have the U.S. Register of Copyrights, Marybeth Peters. We are always happy to have you testify and we appreciate your expertise and the work that you do and the help that you give this Committee from time to time, you and your dedicated staff.

Our second panel includes a diverse group of industry participants. First, we will hear from one of the pioneers and leading voices in the legal distribution of content over the Internet, Rob Glaser, the founder and CEO of RealNetworks.

After that, we will hear from Rick Carnes, who is a very talented working songwriter down in Nashville, as well as President of the Songwriters' Guild of America, and Glen Barros, President of the Concord Music Group, which is an independent record label and music publisher.

After that, Ismael Cuebas, the Director of Merchandising Operations at Trans World Entertainment Corporation, who is testifying on behalf of the National Association of Recording Merchandisers, will give us his views on the licensing difficulties faced by music retailers.

Then we will hear from Del Bryant, the President and CEO of BMI, Inc., one of the largest and best-known performing rights organizations in the business which represents more than 300,000 songwriters, composers and music publishers in all genres of music. I understand that Del was born into the music business and came up through the ranks at BMI. His views are informed by more than three decades at BMI, and we are lucky to have the benefit of his expertise and perspective. I would also like to thank Del for being willing to testify here on short notice, despite scheduling difficulties for him and his organization.

Last not but least, we welcome David Israelite, who is the President and CEO of the National Music Publishers' Association, a man who is well known to this Committee and well respected by all of us.

First, we will turn to Senator Leahy for his opening remarks. I appreciate the privilege of working with Senator Leahy on these issues. We work together well on these issues, and hopefully we can find some ways of solving some of these problems. But, today, we want to learn all we can about them and see where we go from there.

Senator Leahy.

STATEMENT OF HON. PATRICK J. LEAHY, A U.S. SENATOR FROM THE STATE OF VERMONT

Senator LEAHY. Well, thank you, Mr. Chairman, and I will be brief because we want to get on to the witnesses. As some know, we have had another matter that has been somewhat distracting today and may take me out of here for a while.

First off, to state the obvious, digital music is here. I was leaving on a trip to Europe back a few years ago—actually, Europe and Africa. My daughter explained to me that I probably couldn't bring the old victrola—that went right over everybody's head; there is nobody here to remember what a victrola is—on the plane, and that it was time now to download some music that you could listen to digitally. I loved the idea. I ended up with several days' worth of

music, ranging from Puccini to the Grateful Dead and just about everything else in between.

Chairman HATCH. There is everything else in between.

[Laughter.]

Senator LEAHY. You don't like Puccini?

Chairman HATCH. I like them all. You got me to like the Grateful Dead.

Senator LEAHY. You never got to go to a concert with me.

Chairman HATCH. You never invited me.

[Laughter.]

Senator LEAHY. Too late now.

[Laughter.]

Senator LEAHY. I do recall one time being on stage at one of the Grateful Dead concerts. Sting was warming up the crowd. The phone backstage rang and it was the White House and they were looking for me. I got on the phone and the Secretary of State started talking and he said, Pat, could you turn that radio down? Of course, they had no idea where they reached me. I said, well, that is Sting. Dead silence. I said Sting, the rock star. Still dead silence.

I said I am on stage—and by now the sweat is pouring down my face—

Chairman HATCH. Was that the Clinton administration?

[Laughter.]

Senator LEAHY. I am not going to tell you.

I am on stage at a Grateful Dead concert and Sting is warming up the crowd. There was a sigh and he said, well, that is fine, but do you have time to speak with me and the President?

[Laughter.]

Senator LEAHY. It is exciting for companies that are seeing business potential in new platforms and formats. I mention my daughter Alicia because we looked at a number of the different ways of downloading and I thought if I was going to be doing this, I would like to find out more about it. It is exciting, the variety that is out there.

What I find exciting is musicians who see greater avenues for their artistic expression, not only people like my friends in U2, but people that might have a niche area that would not be heard of otherwise, but now have a way of reaching not only nationwide, but worldwide distribution. What is most exciting is for consumers. Those who have very eclectic tastes like I do can pick up the music in various different ways and can listen to it anywhere.

We are going to hear today about some outdated laws that were never intended to address digital music. As legislators, you try to pass laws that stand the test of time. For the most part, our intellectual property laws have accomplished that goal. In fact, Section 115 of the Copyright Act at the center of today's discussion, as Senator Hatch already said, had its roots in piano rolls at the turn of the last century. So we have to ask if these laws for piano rolls are ready to go digital today.

There are problems with the current licensing system. I would like to thank Marybeth Peters for her hard work and her patience. Over the years, she has shown both for this Committee as we try to work through these problems.

Everybody agrees the present system is not working as efficiently as it might. Potential licensees aren't sure which licensing rights apply to certain activities. They may have difficulty even tracking down the appropriate person from whom to obtain those rights. This means that building a comprehensive online catalog of music available to consumers can sometimes be slow or ultimately impossible.

Just as it may be the case that outdated laws have contributed to this problem, it may well be the case that the market offers a solution, either by forcing the parties to adjust to the new environment or by encouraging the stakeholders to back consensus legislation. It is in the interest of all of us to reach an agreement, and we don't want to pass a law that is going to make it more difficult for you. There is nobody in this room that can tell me what will be the furthest advance in digital devices five years from now. None of us can do that.

As Ms. Peters has noted, making legal copies of musical works available online is essential to combatting online piracy. It is a simple thing for me. I want technology not to be hampered and technology to expand however it might. I want as large markets available as possible and let people compete at the market. But, thirdly, those who produce the music in whatever form—the writers, the performers, whoever else—have a right to be compensated. It should not be stolen.

Now, if we can protect all of that, the marketplace can do a great deal. So let us protect the interests of the songwriters and serve the interests of consumers. I think it is possible to do both.

So, Mr. Chairman, I thank you for having this hearing. I think it is well worthwhile.

[The prepared statement of Senator Leahy appears as a submission for the record.]

Chairman HATCH. Well, thank you, Senator. We appreciate it.

We will turn to Ms. Marybeth Peters, who is certainly an expert in this area, and we look forward to taking your testimony.

STATEMENT OF MARYBETH PETERS, REGISTER OF COPYRIGHTS, LIBRARY OF CONGRESS, U.S. COPYRIGHT OFFICE, WASHINGTON, D.C.

Ms. PETERS. Mr. Chairman, Senator Leahy, just two weeks ago in *MGM* v. *Grokster*, the Supreme Court gave a boost to copyright owners in their battle against massive peer-to-peer infringement on the Internet. Nobody has suffered peer-to-peer infringement more than copyright owners of music, and the Grokster decision represents an opportunity for music publishers, the record industry and authorized online music services to take action to stop illegal services that assist and encourage infringement, and to offer attractive alternatives to consumers who have been tempted by illegal services in the past.

But as much as we can rejoice in the Grokster decision, it is too early to declare victory in the battle against the culture of infringement that has led so many to demonstrate a lack of respect for copyright law and for the authors who are supposed to benefit from that law.

While the Grokster decision may make it more difficult for peer-to-peer services to encourage large-scale infringement, it does not necessarily mean that all of those users of peer-to-peer services will flock back to legitimate services.

Mr. Chairman, you and Senator Leahy have long made it clear to the music industry that it cannot simply rely on strong copyright laws to stop online infringement. The music industry has to offer consumers what they want, and what they want is easy and affordable access to all the music they desire, preferably through one-stop shopping from a single online music service such as Rhapsody, iTunes and other legitimate services.

Now, when there is reason to hope that the illegal services may be stopped or at least slowed down, and before the next generation of infringement-enabling services captures the attention of the Grokster generation, now is the time to enable legitimate services to meet that demand.

In order to give consumers one-stop shopping, digital music services need something similar to one-stop shopping. Just as the consumer wants to get all of his or her music in one place, a digital music service wants and needs an efficient way to clear all rights to all of the music it wishes to offer.

But, sadly, a digital music service today must seek a separate license for each musical work it wishes to offer for downloading. And for each musical work, it is faced with the demands for payment from two different middlemen who represent the same copyright owner and the same songwriters.

Much of the blame for our unworkable system can be laid at the feet of the antiquated Section 115 compulsory license. But much of the blame is due to the division of the world of music into two separate realms—one for public performance and one for reproduction and distribution. In the age of the Internet, that division makes no sense, when so many digital transmissions of music can be said to involve both public performance and reproduction.

These two sets of rights are licensed in very different ways. Songwriters and music publishers license music performance through three performing rights organizations, or PROs, and virtually every song anyone could wish to license is in the repertoire in one of these three PROs, which offer blanket licenses for public performances of all the songs in their repertoires.

In contrast, a record company or digital music service that wishes to license to reproduce and distribute phonorecords of a musical work must obtain a separate license for each musical work it wishes to license, must track down the music publisher for each song it wishes to license. And while Harry Fox represents a large number of music publishers, he can license only a fraction of the works that are, in fact, licensed by the PROs.

Unlike the public performance right, reproduction and distribution rights are subject to Section 115's compulsory license. But as a practical matter, that license simply sets a ceiling on the rates that can be charged for the making and distribution of phonorecords and for licenses that are actually obtained through the music publisher or the Harry Fox Agency.

The second major hindrance to music licensing for digital transmission is that almost any kind of digital transmission of music,

when it occurs today, the PROs will assert a right to license and receive royalties for the performance right and Harry Fox and the music publishers will assert a right to license and receive royalties for reproduction and distribution, even though in many cases the justification for requiring both licenses is tenuous.

But it seems inefficient and unfair to require a licensee to seek out two separate licenses from two separate sources in order to compensate the same copyright owner and the same songwriters for the right to engage in a single transmission of a single work.

In my written testimony, I outline some of the possible solutions to these problems. One solution is to convert the Section 115 license to a blanket license along the lines of Section 114 for digital public performances of sound recordings. Such a reformed statutory license ideally would include all reproduction, distribution and performance rights necessary for digital transmissions. Another solution would be to repeal Section 115 and establish a system of collective licensing that builds on the strengths of the existing PROs. My written testimony elaborates on these and other possible solutions.

I and my staff stand ready to work with you and the affected industries to find effective and efficient solutions to improve the licensing of musical works for the benefit of our songwriters and composers, as well as consumers.

Thank you.

[The prepared statement of Ms. Peters appears as a submission for the record.]

Chairman HATCH. Thank you. Now, let me just ask one simple question. What types of music licensing systems are used in other countries of the world? How do they work and, in your opinion, how efficient are they?

Ms. PETERS. I think that with respect to performing rights, our performing rights societies are as good as any in the world. One of the differences is that, of course, they are limited to performance rights, and in a number of countries of the world a single PRO does, in fact, license both the public performance right and the reproduction and distribution right. That is very prevalent in Europe and in Eastern Europe.

While you get the one-stop shopping for the rights, there are some issues with the fact that there are many societies and their reporting rights are different. So, actually, I am not sure one is better than the other. But at least with regard to obtaining the rights, there is one-stop shopping in other countries.

Chairman HATCH. So do collective licensing systems in other countries tend to provide for blanket licensing of all musical works on a percentage royalty?

Ms. PETERS. That is a prevalent model.

Chairman HATCH. Well, what are some of the tradeoffs involved in this type of an approach?

Ms. PETERS. We have heard in the Copyright Office that with respect to digital transmissions many people who participate in the process would prefer a percentage royalty rather than a penny rate. I don't think there is anything inherent in our existing license to restrict that, but we have never had a percentage rate.

Certainly, we know today that with respect to the mechanical reproduction right, people do not use the compulsory license and it is impossible to clear the bulk of the rights in the vast number of works that music services want. So in our case, there is an inability to clear the rights. At least with respect to some of the foreign societies, you can get the right. There are, as I said, some other efficiency issues with those societies.

Chairman HATCH. Someone recently described music licensing negotiations as being similar to blind men playing poker. Not only do the players not see everyone else's cards, they don't even know what cards are in their own hand. They don't see their cards and they don't know what is in their own hand, and as a result each of them keeps upping the ante hoping that others will fold. Perhaps this is also a question for the second panel, but is this something where Congress has sufficient sight to referee the game?

Ms. PETERS. If you believe that something should be done right now and that the situation needs to be improved right now, I originally had suggested a different model that actually would take a longer time to put into place. You actually could use the Section 114 compulsory license as a model, which provides a blanket license for the right to use all sound recordings. You could put that model in place, and if you enacted it this year, almost overnight you could, in fact, enable the licensing of all musical compositions that have been distributed to the public in the form of phonorecords.

Chairman HATCH. If a blanket statutory license system were adopted, how do you think the online marketplace would change from what we currently see today?

Ms. PETERS. Well, I think the second panel will tell you, but I think that to the extent that they are unable to license certain musical compositions and either they use them without permission from the music publisher or they don't use them at all, I think you create a much more secure environment for those businessmen and I think you create the availability of a much larger repertoire that can, in fact, compete much more effectively with the illegitimate services.

Chairman HATCH. Thank you.

Senator Leahy.

Senator LEAHY. Thank you.

Ms. Peters, if I understand both from your testimony and what you have said before, it is often unclear which licensing rights apply to a particular technology. I am wondering, are there lines that can be drawn? When is a download a performance distribution, some sort of hybrid? What about the different varieties of streaming? Can you make those distinctions clearer or do we need legislation to do that?

Ms. PETERS. We are struggling with the issue of limited downloads and on-demand streams at the moment. I would say that for a vast number of the services that are made available, whether it is on-demand streaming or limited downloads or a different combination, there is, in fact, a public performance right that is implicated and there are reproduction and distribution rights that are implicated. So for the bulk of the online services,

whether or not there should be compensation is a separate question, but the rights are, in fact, implicated.

Senator LEAHY. You and a whole lot of others have told me that we have got to make improvements to the way music is currently licensed if we are going to fight illegal downloading. Of course, there are hundreds of millions of dollars at stake here, but we can't seem to get consensus legislation.

Why can't the parties get together, when there is so much at stake? We all know that we are going to have online music. In effect, you open a store in everybody's home all over the world, and if you are going to sell music, you want to have that store. Why can't we get some kind of consensus agreement? I say that as one who would sing the Alleluia Chorus if we did because it would make our job a lot easier up here.

Ms. PETERS. There are some areas where there is some agreement. It is not broad enough to craft a complete solution, so actually what I am going to say to you and to Senator Hatch is you need to take some leadership to try to get it accomplished.

I think that when we held negotiations with most of the parties last summer, there was agreement on a blanket licensing approach. Maybe that was as far as there was total agreement. There are huge issues with regard to what the rate would be, how the rate would be set, who would oversee the rate.

I actually think that if the parties were told that we need to do it and we need to do it now and it has to be broad enough so that it doesn't only answer the issues of today which seem to focus on subscription services, but I think would be much broader in a year or two, I actually would be hopeful that it could be accomplished this year. Nobody has held people's feet to the fire and said we are going to change this law; it doesn't work. I would like to assist in trying to get that done.

Senator LEAHY. What do you do to reach the next point? You might have comparable services, but entirely different technologies. Mr. Glaser's written testimony, if I read it correctly, expresses concern that satellite radio is able to offer services RealNetworks cannot, such as the capacity to record content and play it back later on. Is this appropriate? How do you figure out how to treat different technologies that are offering similar products?

Ms. PETERS. Mr. Glaser has a point. He says that the Internet now is actually competing with radio, cable, satellite, and that they should be looked at similarly. I think each one seems to have its own niche and have its own rules that grew up around it. Certainly, cable has a statutory license that is different than the satellite compulsory license, and now we are talking about a music Internet license.

I am not sure at this point in time that you really could from a policy perspective put it all together so that you were comfortable that the policies went across the board. But I do think that with respect to Internet music, you could start there and maybe when some agreement was reached with that, you could look at other models and see if, in fact, maybe there was consensus on how to get them closer together.

Certainly, Mr. Glaser and others are correct in saying that they pay royalties for webcasting and that broadcasters are not going to pay royalties for digital broadcasting, and they say that is not fair.

Senator LEAHY. If I might, Mr. Chairman, just one more question.

Chairman HATCH. Sure.

Senator LEAHY. You offer two approaches to legislative reform of Section 115. One is to take 115 and change it something along the lines of Section 114, the blanket license. The second approach—and that was in the Copyright Office's draft legislation—would replace Section 115 with a system of collective licensing. Many refer to it as the ASCAP–BMI system.

But you state that, in principle, you support just a simple repeal of Section 115. What if we just simply repealed it? What is going to happen in terms of cost of online services and availability?

Ms. PETERS. In my idealistic view, we basically oppose compulsory licenses. We believe in exclusive rights and in people controlling those exclusive rights. So I would, in principle, always support eliminating a compulsory license, and I would still suggest doing that, though you may have to put it off if you want to solve the problem very quickly.

The problem with eliminating it right now is we have a dysfunctional way of licensing the reproduction and distribution of the mechanical right, and I don't know how you fix that overnight if you just eliminate it. So although I favor it in principle, if our goal is to have efficient licensing of the broadest musical repertoire possible for online services, I think we have to go another route in the interim.

Senator LEAHY. Thank you, Mr. Chairman.

Chairman HATCH. Thank you, Senator.

Well, thank you, Ms. Peters.

Ms. PETERS. Thank you.

Chairman HATCH. We appreciate having your advice. We hope you will continue to think about these matters and let us have the best advice you can give us.

Ms. PETERS. Thank you very much.

Chairman HATCH. We will move to panel two, with Rob Glaser. We are honored to have you here, Rob. We appreciate all that you have been able to do in your business.

Rick Carnes is an old friend who is a great songwriter, the President of the Songwriters' Guild of America. We will turn to you next, Rick, afterwards. And then we have Ish Cuebas, Director of Merchandising Operations for Trans World Entertainment and Co-Chairman of the Media On Demand Task Force Corporate Circle, National Association of Recording Merchandisers, from Albany, and then Glen Barros, President and CEO of Concord Music Group, from Beverly Hills, California; Del Bryant, President and CEO of BMI, in New York; and David Israelite, who is President and CEO of the National Music Publishers' Association right here in Washington, D.C.

So we will start with you, Mr. Glaser. We welcome you back to the Committee. You are no stranger to this Committee and we appreciate you taking the time and putting forth the effort to be here with us. We look forward to what you have to say.

STATEMENT OF ROB GLASER, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, REALNETWORKS, INC., SEATTLE, WASHINGTON

Mr. GLASER. Well, thank you, Mr. Chairman. Senator Leahy, thank you as well. It is a privilege to testify here today on behalf of RealNetworks and the Digital Media Association, which represents all of the leading companies in our industry.

Rhapsody, our award-winning music subscription service, enables consumers to play over a million songs on demand and to download the music to their PC or portable device for unlimited listening. Today, we have over 1 million music subscribers, and in each case we pay a piece of our revenue to rights-holders, both the performers and composers.

All along, our biggest competitor has not been another legitimate service, but piracy. Frankly, outdated and broken laws have made it much harder than it should have been to build compelling legitimate services such as Rhapsody. In the process, the global recorded music industry shrank from about $40 billion to about $30 billion in annual revenue.

Today, I urge the Subcommittee to modernize archaic music licensing laws and stabilize the foundation for lawful online services. Updating our laws will enable the industry to channel resources into building great legal music services that can win consumers away from the pirate networks.

Specifically, I urge the Congress to take the following four steps: first, modernize Section 115 to provide a one-stop-shop blanket license for mechanical rights; second, clarify that no mechanical license is necessary for streaming services, including the incidental and server copies required to deliver a performance; third, end the statutory bias that provides satellite and cable radio providers with a more favorable royalty standard and more flexible technology requirements than Internet radio providers like us; and, fourth, enable us to innovate with compelling radio features so our royalty-paying radio creates more paying customers and generates more royalties for artists. These are our simple steps, but let me take a few minutes to elaborate.

First, the blanket license. As recognized by the Copyright Office, and I believe everyone sitting here today, the song-by-song, pencil-and-paper compulsory mechanical licensing process that dates back to 1909 in some cases just doesn't work and must be updated to help Rhapsody and other Internet services compete more effectively against piracy.

While we have spent millions of dollars setting up our licensing systems, we simply don't have the resources to procure the millions of individual song licenses the current system requires. Meanwhile, illegal services like Grokster give away all the music for free, don't pay artists anything and have millions of songs.

A recent article stated that illegal P2P networks have up to 25 million unique song files. We have about 1 million. Online services, music publishers, songwriters, recording artists, recording companies and retailers all support a single statutory blanket license that provides online music services, all necessary publishing rights, without legal confusion or administrative delay. There are solvable disagreements about how broad the scope of the blanket license

should be and whether the royalty rates should be set by Congress or by industry negotiation. We strongly favor negotiated royalties, with arbitration as a last resort.

Second, we face the significant uncertainty of not knowing when online music triggers the performance right, when it triggers the mechanical reproduction right, or when it triggers both. We agree with the Copyright Office that a stream is a performance that should only require a public performance license and a song that is downloaded for on-demand access should only require a mechanical license.

Like in the physical world, we don't believe there is any case in which both a mechanical and a performance royalty should be paid for the same digital distribution. To be clear, we absolutely want to pay creators for using their music, but they should be paid fairly and fully, and only once. A double-dip royalty simply isn't fair.

Third, we ask the Subcommittee to address the basic unfairness caused by application of more favorable royalty ratings to satellite and cable providers who compete directly with online companies such as RealNetworks. The result is that Internet services are subject to sound recording performance rates that are 50 percent higher than our competitors in satellite and cable radio.

The Copyright Office has said on several occasions that competitive services such as satellite and cable television should be governed by equivalent royalty standards and royalty rates. Today, we ask the Subcommittee to pick one standard for all digital radio competitors and let the market, rather than Congress, determine the winners in the business.

Fourth and finally, to re-ignite Internet radio innovation and promote renewed growth in sound recording performance royalties, RealNetworks and DiMA, joined today by the Recording Artists Coalition, urge a broader, clarified and objective definition of non-interactive services.

Today, it is often difficult to ascertain whether an online radio service is a, quote, "non-interactive service" and therefore eligible for the statutory sound recording performance rights or a, quote, "interactive service" that is ineligible for the statutory license. We would much rather innovate than litigate, and there have already been several lawsuits on this topic. Consumer-influenced radio specifically should be deemed non-interactive as long as the songs are not played on demand and the radio station complies with the existing rules governing the frequency with which a radio station can play a given artist or album.

In closing, let me emphasize the current system is broken, but you can fix it. Give us a chance to compete fairly and both consumers and content owners will benefit from the technological innovations we will unleash.

Thank you very much.

[The prepared statement of Mr. Glaser appears as a submission for the record.]

Chairman HATCH. Well, thank you, Mr. Glaser.

Mr. Carnes, we will turn to you.

STATEMENT OF RICK CARNES, PRESIDENT, SONGWRITERS' GUILD OF AMERICA, NASHVILLE, TENNESSEE

Mr. CARNES. Chairman Hatch, Senator Leahy and members of the Subcommittee, thank you for allowing the Songwriters' Guild of America the opportunity to testify today on proposals for reform of the music licensing system.

My name is Rick Carnes and I am President of the SGA, the Nation's oldest and largest organization run exclusively by and for songwriters. I have been a professional songwriter for 27 years. It is a job that pays practically nothing, has no benefits, no health insurance, no pension and no job security at all. In a way, it is a crazy way to make a living, but I love it anyway because, you see, songwriters don't write songs just to make money. We make money just so we can keep writing songs.

In the last decade, over half of America's professional songwriters have been forced to abandon their careers. Songwriters are not in a recess; we are in a deep, deep depression. Between deregulation of radio, corporate mergers throughout the music industry and rampant Internet piracy, we are being wiped out. So how can the reform of Section 115 improve the lot of songwriters?

To start with, please give us a raise. For 69 years—

Chairman HATCH. Marybeth, you had better pay attention to this.

[Laughter.]

Mr. CARNES. For 69 years, from 1909 to 1978, royalty rates were fixed at two cents. From 1978 on, we have only gotten cost of living increases on our 1909-level wages. So today's songwriters are literally being paid piano roll rates for digital downloads.

The compulsory license isn't even a minimum wage for us; it is a maximum wage. At the eight-and-a-half-cent penny rate, that means that the most I can make on a million-selling album is $85,000. I have to split that with my music publisher, so I get $42,500. Then I split that with my co-writer, the recording artist, and that leaves me only $21,250.

And then there is that catch-22, the controlled compositions clause. This is a clause placed in every new recording artist's contract that basically forces the artist to have to write or co-write all the songs they record so the record labels can get away with paying a three-quarters royalty rate. That cut rate leaves me with less than $16,000 for a million sales. For a platinum album, the very pinnacle of success in the music business, all I get is $16,000, while the middlemen make millions. Register of Copyrights Marybeth Peters recently stated that in determining public policy and legislative change, it is the author, not the middleman, whose interests should be protected.

Section 115 needs to be streamlined to make music licensing much easier for all, especially the music subscription services that have a legitimate complaint that they don't know who to pay, nor how much. But if the subscription services insist on making 50 percent of the revenues and the record labels demand 50 percent of the revenues for their master recordings, then there is nothing left on the table for the songwriters. And in these negotiations so far, they have been demanding up to 95 percent of the money. There is nothing left for the songwriters.

A form that makes the licensing process fast and efficient would be a good thing. But if it starves the songwriters in the process, the whole enterprise is going to fail. These Internet companies are new to the music business, but they need to understand something. We are not manufacturing widgets here. The best way to make great music is not by driving the cost of production down. The way is to pay great songwriters a livable wage and make great music, which will drive the profits up for everybody.

To that end, the SGA and our colleagues in the National Songwriters' Association, the NMPA, ASCAP and BMI have all put forward a unilicense proposal that we believe best achieves music licensing reform while simultaneously providing essential marketplace protection for songwriters. Our proposal seeks a reasonable rate of 16 2/3 percent of Internet subscription service revenues, with a minimum flat dollar fee as a floor. A single designated super agency will collect the blended mechanical and performance royalties under a blanket license, thereby creating one-stop music licensing.

America's first professional songwriter, Stephen Foster, died in poverty with 38 cents in his pocket at the age of 37. He left behind a legacy of songs that have moved the entire Nation and enriched a horde of middlemen, but he never earned enough money to sustain him or his family. The story of American songwriters is far too often a rags-to-rags tale. It is my sincere hope that in reform of the music licensing process, we will begin and end with a focus on helping today's American songwriters and artists survive in a very difficult present and thrive in a much better future.

Thank you.

[The prepared statement of Mr. Carnes appears as a submission for the record.]

Chairman HATCH. Well, thank you.

Mr. Cuebas, we will take your testimony.

STATEMENT OF ISMAEL CUEBAS, DIRECTOR OF MERCHANDISING OPERATIONS, TRANS WORLD ENTERTAINMENT CORPORATION, ALBANY, NEW YORK, ON BEHALF OF THE NATIONAL ASSOCIATION OF RECORDING MERCHANDISERS

Mr. CUEBAS. Good afternoon, Chairman Hatch, Ranking Member Leahy. Thank you for inviting me to testify about the state of the music industry and the challenges in music licensing. We hope Congress can help our industry to remain healthy and vibrant.

I am Ish Cuebas, Director of Merchandising Operations at Trans World Entertainment in Albany, New York. Trans World is a member of the National Association of Recording Merchandisers, an industry trade group that serves the music retailing community. Trans World is one of the largest entertainment retailers in the United States, with 800 stores in 46 States, the District of Columbia, Puerto Rico and the U.S. Virgin Islands.

Trans World operates four e-commerce sites and the FYE Download Zone, a digital music subscription and download service. Trans World is currently designing and developing the next generation of our listening and viewing stations, called LVS 3. These stations will allow our customers to search, find and explore music. These stations are designed and built to support the growing busi-

ness of digital media distribution, allowing consumers to burn full albums onto a CD or create their own compilations. It will allow them to download a full album or compilation or a song they have just heard on the radio onto a portable device. It will allow them to buy download at the store and send them to a home or office PC.

Music retailers continue to face significant business challenges. Sales of digital tracks continue to post big increases year over year, but has not slowed illegal downloading on peer-to-peer networks. We know one of the best ways to prevent pirated downloads is to provide consumers with legal alternatives. This is no small challenge and time is definitely not on our side.

A lot of music is still unlicensed largely because of the extremely burdensome process that is required. Our record label partners are trying to ramp up to handle the licensing process, but that takes time we simply do not have. In order to support these initiatives, we need to modernize the Section 115 mechanical license. The license is outdated and doesn't fit with today's new digital technologies.

In March 2004, NARM formed a Media On Demand Task Force comprised of various member segments to seek solutions to the challenges of the new business models. NARM, RIAA and the Recording Artists Coalition have strongly advocated a broad blanket license that would cover all products in the marketplace and speed up the process.

The current unilicense proposal is too narrow in its scope, applying only to subscription services which account for less than 1 percent of all music sales. The Copyright Office's proposal would offer broader blanket licensing for the distribution of music, but the administrative process resulting from eliminating the compulsory license would likely make things worse instead of better for music retailers.

These proposals do not address dual discs. The music industry needs a vehicle to attract consumers by offering an exciting value proposition. We believe that the dual disc serves this purpose. Under the current system, for example, it would take more than 100 separate licenses to clear one dual disc, which is hindering a more robust release schedule.

What our retailer members have told us loud and clear is that they need an opportunity to experiment with various digital distribution models over the next few years. Legal digital download services represent a significant anti-piracy initiative. It is a great opportunity for songwriters, publishers, record labels, retailers and digital service providers to sell more music and generate excitement and enthusiasm among consumers. This opportunity will be missed if retailers can't easily experiment with the whole range of models for providing music on demand.

We are committed to moving forward with both one-to-one and group negotiations and look forward to working with you and your staff to help resolve these important issues.

Thank you.

[The prepared statement of Mr. Cuebas appears as a submission for the record.]

Chairman HATCH. Thank you so much.

Mr. Barros, we will take your testimony.

STATEMENT OF GLEN BARROS, PRESIDENT AND CHIEF EXECUTIVE OFFICER, CONCORD MUSIC GROUP, BEVERLY HILLS, CALIFORNIA

Mr. BARROS. Thank you, Chairman Hatch, Ranking Member Leahy and all the other members of the Subcommittee for inviting me today to participate in this hearing. I am grateful for the opportunity to share some practical thoughts on how the inefficient system of licensing musical compositions is contributing to the contraction of the music industry by preventing companies from offering consumers exciting and competitive products that I think are necessary if we are to thrive and maybe even survive as an industry.

A little background on the Concord Music Group. Concord Records is a 32-year-old independent record label that focused on jazz and traditional pop for most of its history, expanding into adult contemporary pop recently. Last year, we acquired a company called Fantasy, Inc., which is a treasure chest and one of the greatest catalogs on the planet of recordings and also musical compositions, focusing on jazz, R&B, blues and rock. Our catalog encompasses artists such as Miles David, John Coltrane, Rosemary Clooney, Ella Fitzgerald, all the way to Little Richard, Isaac Hayes and Credence Clearwater Revival.

We also invest millions of dollars each year in new recordings and in trying to develop new artists. Current recordings are Chick Corea, Sonny Rollins, Carole King, Michael Feinstein, Peter Cincotti. And most recently we have enjoyed great success this past year with the final recording of Ray Charles. In all, we are one of the largest independent record companies in the world, with over 10,000 recordings ranging from 1940 until today. Also, an important distinction is that we own music publishing rights. So we are here today really as a music publisher and a record company, and have a broad perspective on the issue being discussed here in this hearing.

Our position is that the current system for licensing musical compositions is not serving anyone as it really should. This is a challenging time in the music business. Piracy, radio consolidation and exciting entertainment options have caused the market to contract. At the same time, we have new technologies that can help add value and bring exciting new products to the consumer.

We have talked a lot about digital alternatives which are very important, but also there are physical alternatives which bring value—dual disc, SACD. All of these things add significant value and can help expand the market. Unfortunately, we have struggled with music licensing issues raised by these new technologies, and I would like to focus on one example of a physical product where the licensing system impedes our ability to make it work.

There is a product called Super Audio CD where there are two layers on a disc. The first layer is a standard two-channel CD where the consumer has the normal experience. The other is a surround sound product where the consumer can hear it like you would a video where you can sit in the center of a six-channel mix. Because it is multi-layer, many publishers have taken the position that, in fact, there are two music files on that disc and that you should be compensated twice. Yet, the disc sells at exactly the

same price and is really designed to offer the consumer an alternative.

Intuitively, I know this shouldn't be the case, and legally I am told it probably isn't. But there really is no way to solve this dispute. It costs thousands of dollars to issue every single SACD and it is a speculative proposition. We don't know if the market will take hold. Yet, here we are investing, and at the same time having to face the possibility of arguing with our colleagues in the music publishing community. That just doesn't make practical business sense.

The same applies when we want to add video content to a CD. Again, we have to approach dozens of publishers. The response time is difficult. Often, it involves duplicate costs, and once again it is just not practical. The end result is we usually just don't do it. We can't devote scarce human resources to a process that has low probability and usually ends up in us paying more for it. What this means is that everybody is hurt by a system that is an impediment to giving consumers more value and getting them to buy more music.

I would like to be clear that I believe writers and publishers should absolutely receive their fair share of music industry revenues, especially since we are publishers, too. But this mechanical licensing process that we have today is a true impediment to seeing that happen.

My suggestions for reform are as follows: Adopt an efficient blanket licensing system like every other compulsory license. Two, provide a percentage royalty. Writers and publishers should share in the upside when consumers are willing to pay a premium price. When it is necessary to provide extra value to win back business from the pirates or economic realities of new technologies and business models demand, the mechanical royalties should reflect that.

Three, avoid potential for disputes. A simplified percentage royalty would be a big step. We should also give consideration to process changes, such as the possibility of an expedited proceeding in the Copyright Office to put to rest questions like whether or not we have to pay twice on an SACD.

Four, consider whether licensing for uses not currently covered by Section 115 can be facilitated. There are uses like lyrics or bonus audio-visual material where the transaction costs of work-by-work clearance are very high relative to the returns that the market will bear.

I want to reiterate this is not an issue of trying to undercut royalties or shift divisions in how the pie is cut up. It is really an effort to grow that pie for all of us, and I believe if we do that and create the flexibility that we need to compete, it will make a huge difference in enhancing the availability of music, the investment in new artists and new songs, and will grow the music industry for everyone.

Thank you.

[The prepared statement of Mr. Barros appears as a submission for the record.]

Chairman HATCH. Thank you, Mr. Barros.

Mr. Bryant.

STATEMENT OF DEL R. BRYANT, PRESIDENT AND CHIEF EXECUTIVE OFFICER, BROADCAST MUSIC, INC., NEW YORK, NEW YORK

Mr. BRYANT. Chairman Hatch, thank you for the opportunity to testify today. My name is Del Bryant and I am the President and CEO of BMI. BMI is proud to represent the public performing rights of over, as you mentioned, 300,000 songwriters, composers and music publishers. With a catalog of more than 6.5 million works, and growing, the BMI family includes icons of American music today and yesterday—the icons Hank Williams, Sr., Billie Holiday, Charles Ives, Miles Mingus Monk, Chuck Berry and the Eagles, to Toby Keith, Mariah Carey, Three Doors Down, Norah Jones and John Williams, and that simply scratches the surface.

My background gives me special insight on the issues that we are discussing today. My late parents, Boudleaux and Felice Bryant, were the first full-time professional songwriters in Nashville, Tennessee. And like most songwriters, you wouldn't know their names, but you would know some of their works—"Bye, Bye Love," "Wake Up Little Susie," "All I Have to Do Is Dream," and the Tennessee State song, "Rocky Top."

As a son of songwriters, I know firsthand what it means to rely on the income that comes from performing rights through BMI and the money which comes to the publisher in the form of mechanicals. I know how precious these royalties are to the creators, and especially to their families. In more than three decades at BMI, I have learned how precious dollars going out as licensing fees are to the broadcasters and the other users who use America's music.

Because we were founded by leaders of the broadcast industry to create competition in licensing, BMI has always had a special appreciation for the business models and programming needs of the hundreds of thousands of enterprises which bring our music to the public. Many groups with whom we negotiate, including DiMA members, have acknowledged that BMI does a good job in establishing a fair market value for music. Our operations are efficient, fair, transparent, and our royalty distributions are accurate, timely and competitive.

American performing rights organizations operate in a healthy competitive atmosphere which provides benefits to the creators and music users alike. It is a win-win for the American free enterprise system. BMI has been recognized as a global leader in digital initiatives for more than a decade. We are among the absolute very first in the music industry with a website, the first to license music for performance on the Web, and the first to post our entire catalog on the Internet.

In calendar year 2004, BMI tracked more than 2.4 billion performances of music on over 3,500 licensed digital services. As those numbers grow exponentially, we have developed a robust infrastructure to handle the volume. Over the past several months, BMI has had participation in industry discussions in an attempt to facilitate the licensing of digital music services. We are not part of the problem, but we are willing to be part of the solution.

BMI, along with the NMPA, FHA and ASCAP, has made a proposal to provide one-stop shopping for both the mechanical and the

performing right for digital subscription music services described in more detail in my written statement.

The two key components, in BMI's view, for the Committee to consider are, first, an antitrust exemption; second, a statutory rate set by Congress. I also address the recent proposal by Register of Copyrights Marybeth Peters and what BMI feels are its benefits and probable shortcomings.

The current conversations among creators, music providers, licensees and members of Congress will, we believe and hope, deliver an equitable marketplace solution to the issues being examined by this Committee today. Whether it be our proposal or another, we believe Congress should not lose sight of the more modest attempts to address digital music services problems. We look forward to being a supportive and, if necessary, proactive participant in these ongoing discussions under the Chairman's leadership.

Mr. Chairman, we are grateful to the Committee and Congress for the effectiveness of the Copyright Act, which has permitted BMI to develop a highly successful business, allowing songwriters, composers and publishers to be fairly compensated for their creative endeavors.

Thank you, and I would be glad to answer any questions.

[The prepared statement of Mr. Bryant appears as a submission for the record.]

Chairman HATCH. Well, thank you, Mr. Bryant.

Mr. Israelite, we will turn to you.

STATEMENT OF DAVID ISRAELITE, PRESIDENT AND CHIEF EXECUTIVE OFFICER, NATIONAL MUSIC PUBLISHERS' ASSOCIATION, WASHINGTON, D.C.

Mr. ISRAELITE. Thank you, Chairman Hatch, Senator Leahy. I am David Israelite, the President and CEO of the National Music Publishers' Association. I thank you for allowing me to testify today about music licensing reform, and I thank you for allowing Irwin Robinson, the Chairman and CEO of Famous Music and the chairman of my board, to submit written testimony for the record.

For more than 80 years, NMPA has been the principal trade association representing the interests of music publishers and their songwriter partners in the United States. A music publisher is a company or individual that represents songwriters by promoting songs, licensing the use of songs and protecting the property rights of the songwriter. Put simply, the role of the music publisher is to represent the interests of the songwriter and the song.

While this is a hearing about music licensing, I must thank you, Mr. Chairman, and you, Senator Leahy, and the members of this Committee for all that you have done to help music through your efforts to protect intellectual property. You have long recognized that the property rights in intellectual property deserve no less protection than physical property. It is an important value and one that is relevant to this hearing.

Mr. Chairman, I know that you and several other members of Congress are concerned about the recent Supreme Court decision in *Kelo* v. *The City of New London* regarding the rights of private property owners. A taking of property for the public good must be balanced very carefully against the importance of private property

rights, which are the cornerstone of our constitutional freedoms. While we can all agree that it is in everyone's best interest to develop the digital music industry and make it successful, it must not be done in a way that is disrespectful of the private property rights of creators.

Many people would be surprised to learn that in every recorded song there exist two separate and distinct copyrights. When a songwriter writes the words and notes of a song, that musical composition contains a copyright. When an artist records that song, that particular version of the songwriter's song or that sound recording also has a copyright. Both copyrights contain property rights, and the songwriter and the artist both deserve compensation for the use and sale of that property. What would surprise people even more is to learn that while the value of an artist's sound recording is governed by a free market, the value of a songwriter's musical composition is controlled and regulated by the Government.

Further complicating the music business is the emergence of digital technology. While digital technology provides an exciting new medium for distribution of music, it also presents new challenges to the licensing of music. A digital media company wishing to sell music must obtain both copyrights. It must obtain the sound recording copyright from the recording industry at a price negotiated in a free market and it must obtain the musical composition copyright from the publishing industry at a price largely controlled by the Government through Section 115 of the Copyright Act.

Songwriters and music publishers are excited about the emergence of digital technologies, but it always must be remembered that the purpose of a digital music company is to sell the private property of others. With that in mind, we recognize that there are challenges to the licensing of this private property.

NMPA, through its wholly-owned subsidiary, the Harry Fox Agency and its publisher clients, have issued nearly 3 million licenses to at least 385 different licensees for digital delivery of musical works. There are several digital media companies offering millions of songs to the public today. The system has allowed these companies to launch successfully, but the system can work better.

NMPA, along with ASCAP, BMI, the Songwriters' Guild and the National Songwriters' Association, have proposed a solution which respects property rights, protects creators and addresses the needs of licensing reform for the digital age. Our proposal, called the unilicense, would create a one-stop shop where online subscription services could obtain a blanket license covering both performance and mechanical rights through a licensing agent.

Our proposal would minimize disruption of the industry by maintaining existing licensing structures, thus eliminating any additional administrative expenses. It is a proposal that has been embraced by both songwriters and publishers, and is the subject of continuing negotiation with the Digital Media Association.

There are other proposals that suggest more radical changes to the music business. While songwriters and music publishers are ready and willing to help facilitate the efficient licensing of musical compositions of their property, we would be opposed to any proposal that will impose more Government control, be less respectful

of private property rights, or create an even more unlevel playing field in the music business for the songwriter.

I thank you again for this opportunity to testify and I look forward to answering any questions you may have.

[The prepared statement of Mr. Robinson appears as a submission for the record.]

Chairman HATCH. Well, thank you so much. This has been an interesting panel to me. Of course, you are citing the various interests and the various problems that exist.

Let me start with you, Mr. Israelite. I am intrigued by the unilicense concept that you have mentioned in your remarks and that has been advanced by some folks. Now, how would such a system work, if implemented? Let me just a couple follow-on questions on that.

Would the license cover all rights to all musical works, and if so, would it be implemented by adding performance rights to Section 115? Also, what mechanism would allow for adjustments to the royalty rate over time?

Mr. ISRAELITE. We have offered the unilicense proposal because we have identified these digital subscription services as the area most in need of reform. There are several problems today. Number one, it is a unique type of service that blends both a performance right and a mechanical right. Yet, the digital company is troubled by the fact that it must pay both or doesn't know exactly what it should pay. Secondly, there isn't a rate today for a mechanical license in a subscription service.

What our proposal would do is create a one-stop agency that would license all music. It would license both the performance and mechanical rights for one price. That agency would then distribute the money through existing distribution mechanisms, so that the user or the license would never have to choose between a performance or a mechanical, would not have to pay twice, and would get blanket licensing for all works, for all rights. But yet it would leave the current system in place so that the current mechanisms to use for performance and mechanical licensing could continue to exist and work as they work today.

We think it is a proposal that solves the problem today. It is one that has been embraced by, I think, most, if not all of the songwriting and publishing organizations, and it has been the subject of intense negotiation. We continue to negotiate. Obviously, money has been a large part of that negotiation, but in terms of implementation I think that we have worked out most of the issues about how it would work.

Chairman HATCH. Would there be any way for publishers to opt out? If so, wouldn't that raise the same concern that has been voiced by many about both the current system and the proposals to move to a system of multiple collective rights organizations or music rights organizations, MROs, if you will, namely the inefficiency of having to license from numerous rights-holders, agents or MROs?

Mr. ISRAELITE. One of the advantages of the unilicense is the concept of being able to go a single place to get all of the rights. The issue of the opt-out is one that we continue to negotiate in our private negotiations. Obviously, there are some that would prefer

to be able to license directly, as they do today in the current marketplace.

Some of the other proposals that have been put on the table potentially could create even more places to have to go for licenses. For example, the idea of creating MROs, or multiple rights organizations, that have both, but yet not limiting the number of them could create a situation where you would have thousands and thousands.

I think we can work that out. I think we can make it so that—I am not sure that one-stop shopping is necessarily what is required, but as long as it is manageable. And I don't think that the digital media companies would mind as long as they have a manageable number of places to go to get the rights, much like they do in the performance rights area today where they go to three different ones to get their rights for performances.

Chairman HATCH. I am not against having any of you who care to make any comments about these things interrupt and make them.

Mr. GLASER. What I would say, Senator Hatch, on that point is since Mr. Israelite mentioned the services, from our company's perspective and DiMA, we have a significant preference for Register of Copyright's proposal. It may be that if there is further clarification on the unilicense, some of the issues would be addressed. But, specifically, of the ones we know about, the notion of opt-outs defeats the purpose of a blanket license and would be probably worse than the status quo.

In terms of the royalty rate, we have a process that has worked most recently in our arbitration with the Copyright Office over the rate for radio stations. Like all of these things, it was a negotiation. The negotiation didn't conclude successfully, and then there was an arbitration that resulted in an outcome that we as an industry can live with. I think that process is far superior to the Congress trying to set a price or a price mechanism.

One other element is having prices where you have to have a fixed minimum per subscriber would limit innovation in a very specific way. For instance, we have a service called Rhapsody 25 that we introduced in April. It is one of the best mechanisms that we think we have come up with in the industry to combat piracy where a consumer can listen to up to 25 on-demand streams a month without being a paying subscriber. And on the 26th, they say, hey, you are done.

We got all of the major record companies to agree to that, which was a fair amount of work, but they were all ultimately interested in combatting piracy. And having a free on-ramp to legitimacy seemed like a good way to go. If we had had a per-subscriber minimum rate, we could have never have done that. So you have got to be very careful when setting prices to avoid doing it in a way that limits innovation.

Chairman HATCH. I have some other questions, but I will turn to Senator Leahy and then I will ask my other questions.

Senator LEAHY. Well, I was just curious. The NMPA and the Songwriters' Guild have put forth a proposal that would provide them with 16 2/3 percent of gross Internet subscription service revenues. Am I correct on that?

Mr. GLASER. Yes, Senator.

Senator LEAHY. I understand that other countries use some different formulations.

I will start with Mr. Glaser and ask each one of you the same question. What is the appropriate amount of compensation for songwriters, and do you favor an approach that guarantees a percentage of revenues or some other kind of determination?

Mr. GLASER. Well, I would say that it is a little bit hard to answer the question in the absolute because from our standpoint we care about the cumulative cost; in other words, what we are paying all of the rights-holders, in general. Today, it has been widely reported that that rate is about 50 percent, plus or minus, and if it ended up going from 50 percent to 67 percent, that would have a significantly deleterious effect.

Senator LEAHY. I am talking about the amount to songwriters.

Mr. GLASER. Well, that is what I am saying. It is a little bit hard to answer in the abstract. I will tell you that internationally where there have been negotiations, like in the UK, France and Australia, the online services are paying 8 percent or less of revenue. So that has been marketplace negotiations. Now, certainly, some of the rights-holders have gone in looking for more, but that is kind of what we are seeing in the marketplace today, which is principally internationally what is going on.

Senator LEAHY. Mr. Carnes.

Mr. CARNES. Well, to add to that, first of all we don't know exactly what they are paying for. Their subscription services may be covering who knows what. I know the one 8-percent rate that I know of was a start-up rate. It was a rate in the UK, where they gave them the opportunity to start at 8, but it is supposed to go to 12, and then I don't know where it goes from there.

I can tell you this: If you ask somebody on the street, how much do you think the songwriter is getting for this one-dollar song, they will tell you probably 50 cents.

Mr. GLASER. And how much are you getting on the pirate networks, Mr. Carnes?

Mr. CARNES. Well, now, you know, if we are going to try to compete with free, then we are going to have to drop the rate all the way down to what they are talking about—nothing. I think this is a property rights thing, just like David was saying. It is about what my property is worth and how I can make a living creating it.

Senator LEAHY. Mr. Cuebas.

Mr. CUEBAS. Well, our interest primarily is in retail and getting this to the consumer. We do want the songwriters to get paid. We want everybody to get paid here. We just want it to be easy to get these licenses so we can offer it to our consumers. If we are going to compete with these online services who are offering 4 million-or-so tracks and the best I can offer them is 1 million, then I can't compete.

Senator LEAHY. But you don't have a feeling on the 16 2/3 percent of gross Internet subscription service revenues?

Mr. CUEBAS. Not on the percentage, no.

Senator LEAHY. Thank you.

Mr. Barros.

Mr. BARROS. On the subscription service, I think the matter needs to be studied. I don't know if 16 2/3 is right or not, but I would certainly be willing to roll up my sleeves and figure it out and help figure it out. But I do think that the 16 2/3 concept is too specific. We are only talking about subscription services here and I think the issue is really broader than this.

For example, when we get to the physical world, I think the same issue applies. A percentage royalty has to be brought to bear, and what is that correct percentage royalty? My proposal would be that we look at it in such a way that right now we try to create that right economic division without disrupting the economics of the business.

One thing you have to clearly remember is that somebody is also investing a lot of money. Record companies spend millions of dollars trying to promote artists, and therein promote songs, too. So there is a significant investment that goes into it and there is the right division of the profits from that and payment for costs and supplies, and I think we would need to just study that and come up with the right number.

Senator LEAHY. Mr. Bryant and Mr. Israelite, you believe in the 16 2/3?

Mr. BRYANT. Well, I think there are several benchmarks you can look at for the 16 2/3. Ring tones in the last few years have sold over a quarter of a billion units that have been paid for, and the approximate share for a publisher is 10 percent. And between BMI, ASCAP and SESAC, it is somewhere between 5 and 6 cents. So you have in the marketplace that has been negotiated freely approximately 16 cents that is working in the digital area.

Also, in the home recording digital situation with DART, there was a two-to-one ratio—the artist, record company twice that of the underlying work, the writer and the publisher share. What is being suggested here is a three-to-one, which is certainly far more reasonable.

I would suspect, in light of what Rick said, that it is very reasonable, and that indeed when you are measuring it up to what the record company is getting for their share and what someone may have to pay for the record company share, it may not work into the model that Mr. Glaser is speaking of. But that really shouldn't be cut out of the hides of songwriters and publishers. That is an examination of the model, I would suspect, but there are several very good examples in the marketplace that work.

Senator LEAHY. Mr. Israelite.

Mr. ISRAELITE. Thank you, Senator. Two things. First of all, I think it is important to recognize that since 2001 we have not had a rate for these subscription services and that publishers and songwriters have voluntarily licensed the entire catalog that we represent without knowing what our rate is. And we haven't distributed one penny in those last four years to allow these new services to get off the ground. It is something that we have done to help them.

Secondly, the reason why the market doesn't work today is because if you are a DiMA company and you have to go out and get both copyrights, one of the copyrights represented by the record la-

bels has a complete free market. They can charge whatever they want and if you don't like it, they can say no.

On our side of the equation, with our copyright, we are controlled, and as a result the DiMA companies know that they can get our copyright without having to pay a rate that is negotiated in the free market. What has happened as a result of that is that these subscription services today have cut deals with the record companies where I think they are paying roughly 50 percent of revenue and they haven not been able to cut a deal with us because they know ultimately they can get our licenses and we don't have a free market to say no. That has created quite a problem.

We have put the number of 16 2/3 on the table. We anticipated that as part of a negotiation, we could work all this out. We haven't gotten there yet, but we are still hopeful. We still think that we can work the economics out to make this work.

Senator LEAHY. Well, Mr. Chairman, not only is my time up, but I have to go to another matter. These are very good things. We have a number of technical questions, including one very real one here: What do I have to do if I want to get the necessary licenses if we set up the Hatch-Leahy Music Store, either bricks and mortar or online? I wasn't quite sure how you get through that thicket. It would be an eclectic problem.

If I might, I would like to submit some of these questions for the record, but I do want to thank the Chairman for holding this hearing.

Chairman HATCH. Well, thank you, Senator Leahy.

If I could just ask a couple more questions, because this is an extremely interesting hearing to me. I want the system to work, I want everybody to come out of it whole.

I know, Rob, if we don't compensate writers, we are not going to have the creativity. If we compensate them too much so you can't be in business, we won't have the dissemination, just to cite the two of you. We have also been confronted with piracy that has been robbing us blind in this industry, and a belief by our young people, at least, in many respects that anything that is on the Internet is free and therefore they can take whatever they want to, regardless of whether they are robbing Mr. Carnes or not, which, of course, they are, and you and all of you.

Let me just say, according to the NMPA testimony, the Harry Fox Agency has, quote, "issued almost 3 million licenses to at least 385 different licensees for digital delivery of musical works," unquote, that, quote, "represent the vast majority of musical works for which there is any meaningful level of consumer demand," unquote. But you indicate that RealNetworks still, quote, "cannot obtain licenses for the broad category of songs it needs to compete with pirate services," and that you "do not know the final licensing royalty costs," unquote.

Now, can you comment for the benefit of the Committee on this difference in perspective and explain what type of works you cannot license and why, so that we will understand that?

Mr. GLASER. Well, there are two issues. One has to do with whether we can get a license at all, and the second has to do with whether or not we can get a license for all of the modes of use of a service, and I will explain by way of example.

One of our new capabilities is something called portable subscriptions. That means you pay a larger fee—$15 a month is our general fee for that—and you download music onto an MP3 player, kind of like an iPod, and you move that around. And as long as you every month check back in and we get a reporting of what songs were played so we can pay the artists, and we verify that you have a subscription that is active, you can keep doing that for paying $15. It is sort of a rental model for music.

We have a lot of songs that we have the right to stream directly, but we don't have the right either for publishing reasons or for performance reasons or for recording reasons to play. So it makes these portable subscription services much more confusing for a consumer, because we have a catalog of 1 million, but we may only have 600,000 where you can take them on the go. So do we sort of have to explain to consumers, hey, we have got this footnote out here for a third of our library? It is a difficult thing and it is one of the things that has impeded that kind of service.

In turn, if you compare it to something like the illegal services like Grokster, they let you download and move it onto a portable device with no limitation at all. So that is a very specific thing where we have invented a lot of technology to make a better competitor against the pirate services and this specific licensing issue is getting in the way.

I could go on, but I hope that that gives you a flavor of how this undercuts our ability to compete, not in a black-and-white way, but in a cumulative way that is quite significant.

Chairman HATCH. Well, some claim that online music services will pay, as you have said, about half their revenues in music royalties, but that current arrangements funnel most of these royalties to the recording companies, leaving almost nothing for the songwriters.

Do you agree with that, Mr. Carnes?

Mr. CARNES. Well, as the negotiations stand right now, I mean I think that I am going to go back to the 16 2/3 percent. I thought that was entirely reasonable because the songwriter's share of that is only 8 1/3, which leaves more than 90 percent for everybody else. I mean, I feel like that is reasonable. We are taking a real leap of faith here by going with a percentage rate instead of a penny rate.

Chairman HATCH. Well, let me ask you this, Mr. Glaser. What proportion of the overall royalty payment goes to the record labels for the sound recording and what proportion is expected to go to songwriters and publishers, if you know?

Mr. GLASER. Well, in terms of expected, it is very hard to say. We are reserving money; in fact, we have already booked it as expenses and every quarter our accountants and our lawyers write down what they think is the rate to reserve. I don't actually know what the rate is. I know, cumulatively, we have set aside probably millions of dollars at this point, and we would love to pay Mr. Carnes and his colleagues through the agencies here as soon as we have a rate established.

So this isn't a case where we are going to have to change our economics if there is a fair rate. We have set that money aside. So when we say 50 percent, that is based on including what we pay

the recording companies today, both the majors and the independents, and what we expect we will pay.

Now, just to be clear, that is only for on-demand services. For things like radio services, there already are rates established either through the licensing regimes or through negotiations that we have done directly with ASCAP and BMI. And those rates, I believe—and I will get corrected—are in sort of the 3- to 5-percent range for radio play.

And that is a final point. We are the only kind of service that is paying both performers and songwriters for radio play. So our industry offers a better deal, and I believe a fairer deal to artists than traditional radio, because traditional radio only pays publishing and it doesn't pay recording. So I think our service, if you looked it sort of thoroughly, is the most artist-friendly kind of service out there. And we are willing to pay fair rates; we just don't want the rates to accumulate up to where it makes the economics of our business unsustainable or where we are disadvantaged relative to other broadcast methods, be it either radio-style or full sort of on-demand services.

Chairman HATCH. Well, as you know, I admire you and the pioneer work that you have done in this industry and how you have tried to at least help us move along the lines of winning over the pirates out there. I have a lot of respect for that.

Mr. GLASER. Thank you, Mr. Chairman.

Chairman HATCH. We still have a lot of questions, but we appreciate what you are trying to do.

Mr. Bryant, let me turn to you for a second. What are the potential concerns for creating an exemption for incidental reproductions or incidental performances so online services, depending on the type of service, would have to get a mechanical license or a performance license, but not both? Is there a practical solution of making our current system of exclusive rights which developed in a world of sheet music and live public performances fit in the online world a little bit better? Can you help me with that?

Mr. BRYANT. I am not sure, Mr. Chairman, of the scope of your question. I heard it, but I am not sure I understood that.

Chairman HATCH. Well, basically, what I am saying is if we create an exemption for incidental reproductions or incidental performances so online services, depending on the type of service, would have to get a mechanical license or a performance license, but not both—

Mr. BRYANT. You are talking about ephemeral rights, I believe.

Chairman HATCH. Yes, I think so.

Mr. BRYANT. I am sure that the Copyright Act as it stands now implicates, certainly, a performing right with each transmission.

Chairman HATCH. Right.

Mr. BRYANT. And I believe that creators are certainly entitled in this new space to every opportunity to make income, and I believe it was stipulated in the Copyright Act; I am sure it was.

Are all of the situations that we have discussed here today at each end of the spectrum the best way to fairly handle this? I am not sure, but as David said, there seems to be at this point a little bit of reluctance to start talking about some of these issues when there are propositions on the table. We have writers and publishers

who are literally waiting for some decisions and we are in the process of trying to come up with some of those solutions on a real workable scale.

Of course, BMI, of itself, licenses every situation. You can get a BMI license, as I am sure Mr. Glaser knows, by simply asking for one. It is an automatic situation. It certainly doesn't take anybody out of a going into business model because you can take us to rate court and come with a fair rate at some point if we can't agree to one.

In some of the other situations which don't have the rate proceedings, I think it comes down to negotiating and working in the marketplace. Even though BMI has a rate proceeding, we have rarely used it because we certainly negotiate and we work out situations. So I think once again, as David said, there are some solutions out there on the table and we are ready to negotiate.

Chairman HATCH. Mr. Cuebas, let me ask you a question. How important is it to music retailers to get a more robust stream of releases in new physical formats like your dual disc format, and how much of a difference would that make to purchasing behavior?

Mr. CUEBAS. Well, recently with dual discs, we have seen increased sales. We are offering the customer additional value. The value of CDs has been decreased tremendously and dual disc gives the consumer the value they are looking for.

Chairman HATCH. Let me just say this. You are all interrelated. The problem is the system isn't working well, and part of it is because of piracy, but part of it is the way the system has built upon bygone years. We are in a digital world now, we are in an online world now.

Naturally, every one of you has to make money, starting with the music writers. I have known Mr. Carnes for a long time and he is a marvelous songwriter, no question about it, one of the best in the business. And he is good-natured about it, too, but not when it comes to representing his group. He feels like they are getting screwed.

I think that is a fair comment. Don't you?

Mr. CARNES. Yes.

Chairman HATCH. Yes, okay, and I can personally testify to that in the sense that I know some wonderful writers who are as good as anybody in the business who just can't make it anymore and have had to get out of the business and work in fast-food restaurants, and so forth. Generally, they have to anyway just to be able to sustain themselves while they are writing.

What percentage of writers would be able to live off what they make from writing music?

Mr. CARNES. I hesitate to make a guess. You know, it has got to be less than 1 percent, though.

Chairman HATCH. I can't help but remember about seven or eight years ago I spoke to one of the national groups, and I had just received my first royalty check for writing songs and it was, I think, $57 or something like that, which is a big, big check for me. There were about 1,000 people there, all music writers, and I got up and I said I just got my first royalty check, and the place went crazy. They stood on chairs and yelled and screamed, and so forth.

One of the leaders of the industry leaned over to me and she said, Senator, the reason they are so excited is, as good as everybody is in this room, very few of them will ever receive a royalty check at all. So, naturally, I have tried to help the creators because, Mr. Glaser, without them—of course, there have been enough creators in the past and maybe we can just live off that, but I don't think so. We have got to continue to innovate and continue to come up with ways of solving these problems.

Mr. GLASER. Absolutely.

Chairman HATCH. But I generally try to help the creators because they are at the bottom of this totem pole, and unless they are performers who write their own music, there is very little chance for them to really be able to self-sustain themselves. I know some of the best in the business who can't do it. As Rick said, we try to earn money so that we can continue doing what we love, and that is what these songwriters tell me.

One of the reasons why I started writing music was so I could understand this. And, boy, have I gotten so that I understand it. It is just terrible, and I empathize greatly with Mr. Carnes. Now, I also empathize with Rob Glaser. I have seen what he has had to do to create Rhapsody and to create this business. He has had to take on a lot of big-time people and go through an awful lot of fighting and screaming and litigation and everything else to create what really is a remarkably efficient and good system for delivering music. Knowing him, I know that he wants to pay what the market will bear, and I hope that continues to be true.

You retailers, if you don't have the music, you can't sell it, and we all know that. What BMI and ASCAP and SESAC do is extremely important. The question is should we go to one single, unitary system whereby all of these special deliverers of services are kind of pushed out into just one great big agency that does it.

I see a lot of different problems here that have to be solved, and I don't know that we in the Congress are capable of solving them. Maybe we are, with your help, but this hearing is really a beginning hearing for trying to understand and sort this out to see if there is some way that we can be fair to everybody concerned. But I would like to start with the songwriters because without them, all of this is a house of cards. So I am very concerned about it. And as you know, we are going to just turn to Marybeth here and she is going to solve all these problems for us. It is only fair that you have to live up to your earth-shaking reputation.

Let me leave just a final thought here and that is that we are open here, Senator Leahy and I and the other members of this Committee, too good ideas. We don't have any desire to hurt anybody. We don't have any desire to pick one side over the other. When I say that I naturally have a lot of affinity for songwriters, I do because they create this stuff, and without them everything else falls.

A few years ago, worrying about piracy, I tongue-in-cheek said that there is technology that could destroy individual PCs. My gosh, you would have thought the whole world was coming to an end. I was just kidding, just kidding, but trying to make the point that this is a terrible problem and that we have to do something

about it. And I challenged the industry to help us. Mr. Glaser is doing something about that, and so are all of you.

I guess I am so serious most of the time, they don't catch my humor when I actually tell—and they are still complaining about that. I had so many vicious e-mails that you would have thought—it was actually a lot of fun, between you and me.

But I want some help here, and I know Senator Leahy does. If you guys can help us to know how to do this system better, we want to do it better. I am not sure that legislation is the answer, but we are certainly willing to look at if we could help everybody in the process. I do believe that ASCAP, BMI and SESAC—I didn't mean to put them in any particular order, but I believe they do a tremendous service. I also believe that the publishers can do a tremendous service, too. Naturally, without retail we can't do it. Without delivery systems, we can't do it, and the wholesalers. I mean, it all is a system that has worked to a degree in the past, but it is not working well today and we need to come up with some ideas that will work here.

The whole purpose of this Subcommittee is to try to help resolve some of these issues. And we don't want to pick any sides. We want to get these resolved as best we can, and we would appreciate the best ideas you have.

Does anybody have any other comments they would care to make?

Rick, I am amazed that you are not willing to make some more comments. I have been around you enough that you have never lacked a comment.

Mr. CARNES. I have always just been an opening act. I am not a closer.

[Laughter.]

Chairman HATCH. That is great, that is great.

Well, I am grateful to all of you. This has been helpful to us. We are going to continue to hold these hearings and hopefully we can get to the bottom of this in the future. Thanks so much.

[Whereupon, at 4:12 p.m., the Subcommittee was adjourned.]

[Submissions for the record follow.]

SUBMISSIONS FOR THE RECORD

COMMENTS OF THE AMERICAN SOCIETY OF COMPOSERS, AUTHORS AND PUBLISHERS

Before the

SUBCOMMITTEE ON INTELLECTUAL PROPERTY OF THE
SENATE COMMITTEE ON THE JUDICIARY
109th Congress, 1st Session

July 19, 2005

SUMMARY

The American Society of Composers, Authors and Publishers (ASCAP) submits these comments on music licensing reform further to the hearing held by the Subcommittee on July 12, 2005. ASCAP applauds the efforts of the Subcommittee, the Chairman and Ranking Member, in addressing issues vital to the well-being of songwriters and music publishers. ASCAP also applauds the goals of the Copyright Office, as stated by the Register in her testimony and in her testimony and draft legislation submitted to the House Subcommittee on Courts, the Internet and Intellectual Property on June 21, 2005. Unfortunately, the legislative proposal offered by the Copyright Office with the best of intentions does not further these laudable goals. The Copyright Office proposal, well-intentioned though it is, is fatally flawed throughout and will likely harm, rather than help, songwriters and music publishers. Our unilicense proposal, however, achieves the same goals as the Copyright Office proposal, without any of the attendant dislocations and concerns.

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COMMENTS

As the Subcommittee is familiar with ASCAP, we simply attach a brief description of the Society and its operations for the record. ASCAP applauds the efforts of the Subcommittee, the Chairman and Ranking Member, in addressing issues vital to the well-being of songwriters and music publishers.

OUR UNILICENSE PROPOSAL

The reform that all parties advocate concerns the rights of reproduction and distribution – the "mechanical" license of section 115 – and not performing rights licensing, which is the only licensing area in which ASCAP operates. Nevertheless, in an effort to assist the music community not only of the songwriters and music publishers who are our members, but also the music users who need our members' rights, we joined in an effort to achieve that reform.

As a result of discussions with interested user parties last year, it became apparent that the real difficulty they faced was in the licensing of subscription services. As DiMA's representatives have repeatedly stated publicly, in testimony and elsewhere, ASCAP's and BMI's performing right licensing system works well for them. But DiMA's members needed more to effectuate their subscription service business – they needed a "one-stop shop" that encompassed both performing and mechanical rights. We therefore joined with the NMPA/HFA and BMI, supported by the SGA and NSAI, and proposed a "unilicense" which would achieve that end.

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The unilicense would be available to services which met two criteria: 1) they operated on a subscription basis (whether via payment for time or on some other basis), and either 2) they offered downloads limited in some fashion or 3) they offered on-demand streaming. The single, unitary license would be issued by a "Super Agency," which would collect the single license fee. The fee, set by statute, would be 16-2/3% of the revenues of the subscription service. (There are many reasons why that fee is fair – one was noted by the Register in her testimony: "it was clear that digital transmissions were substantially superior to, and therefore more desirable than, analog transmissions." Written test. p. 7.) That fee would then be divided, by private agreement, among the performing rights and mechanical rights interests. An antitrust exemption would allow us to establish the necessary administrative structures and undertake the unitary licensing and division of license fees, all without governmental involvement or interference.

Our unilicense proposal would realize the goals for music licensing reform which are advocated by the Copyright Office and many, if not all, interested parties.

WE SHARE THE GOALS ADVOCATED BY THE COPYRIGHT OFFICE AND OTHER INTERESTED PARTIES

ASCAP shares and applauds the goals advocated by the Register in her testimony before this Subcommittee and, previously, before the House Subcommittee. The Register made several points in her testimony, which were echoed in the testimony of various parties on all sides of the issue, which bear repeating, and which we fully endorse:

1) The Register advocated a solution to the pending issues that comports with the Copyright Office's longstanding policy preference against statutory licensing for

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copyrighted works and for a system of licensing determined in the marketplace where copyright owners exercise their exclusive rights. We agree.

2) The Register said that the time had come to phase out the mechanical compulsory license and allow for truly free market negotiations. We agree.

3) The Register and others said that Section 115 should be modernized to deal with licensing of copyrighted works in the digital age. We agree.

4) The Register and others advocated collective administration as a means of achieving that end. We agree.

5) The Register recognized that separate rights in copyrighted musical compositions – the mechanical right and the performing right – were involved in digital uses. We agree.

6) The Register and others advocated enabling a single licensing regime, which would encompass both rights, and thus benefit users administratively. We agree.

7) The Register and others noted that facilitating legal uses, for which creators and copyright owners were paid, was necessary to combat piracy. We agree.

8) The Register noted that our model of licensing the performing right "appear[s] to function quite successfully." (Written test., 29.) Rob Glaser, testifying for RealNetworks and DiMA, referred to our "smoothly-operating . . . licensing processes." (Written test., p.8.) We, of course, agree.

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9) Most importantly, the Chairman, the Ranking Member and the Register all said that the primary focus should be on the songwriter, who should be fairly compensated for all non-privileged uses of his or her work. In determining public policy and legislative change, it is the author – the songwriter – whose interests should be protected. We would only add that the role of the music publisher is also vital, as the music publisher's function is to protect the interests of the songwriter. As a membership association owned and run by and for composers, authors and music publishers – in which the interests of songwriters and music publishers coincide fully – we agree.

Unfortunately, the legislative proposal offered by the Copyright Office with the best of intentions does not further these laudable goals. Here are some reasons why:

The Copyright Office's proposal to unify mechanical and performing rights licensing in Music Licensing Organizations (MROs) would defeat the very purpose it ostensibly seeks to achieve.

First, instead of the "one-stop shop" advocated by the Register, the proposal would result in a proliferation of MROs. Instead of dealing with one, or even three, licensing organizations, digital users would have to deal with far more than they now do.

Second, that fragmentation of the market would severely harm, rather than help, authors. The efficiency of collective licensing through the existing performing rights organizations (ASCAP, BMI and SESAC), which was so lauded by the Register, would be destroyed, and the unequal bargaining power the PROs now face in dealing with huge user entities would be exacerbated. The result could be the destruction of the PROs'

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efficiency. And those fragmented MROs might not be run by and for songwriters in partnership with their music publishers, as ASCAP is.

Third, ASCAP and BMI, transformed into MROs, would still be subject to the strictures of the consent decrees, which, for example, make their rates subject to court determination. While we have lived comfortably under the consent decree in the licensing of performing rights for over fifty years, the Copyright Office proposal is unfair for several reasons: It would impose court rate determination on mechanical rights, where it has never been before. It flies in the face of the stated goal of freeing mechanical rights from compulsory licensing and allowing the free marketplace to work, and would reduce the bargaining power that songwriters and their publishers have. And, if MROs other than ASCAP and BMI arise (which we believe is a virtual certainty), there would be an unequal playing field – they would not be subject to <u>any</u> rate determination mechanism, while our writer and publisher members and BMI's affiliates would be for <u>both</u> performing and mechanical rights. That is patently unfair.

Fourth, ASCAP and BMI do not have any administrative structure in place to deal with mechanical rights. The proposal thus would penalize songwriters and publishers, who would have to pay the costs of creating and administering such a structure.

Fifth, our experience has shown that when the rights of reproduction, distribution and performance are combined on a compulsory basis – which would be the case with the Copyright Office's proposal – the license fees received by songwriters, composers and their publishers go down, and not just because administrative cost savings (if any) are passed along to users. Such was the result when, fifty years ago, the synchronization and

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performing rights were compulsorily "merged" for theatrical exhibitions of motion pictures in the United States – our writers and publishers receive far less than do their colleagues in other countries where those rights are not compulsorily merged.

Sixth, there are many concerns regarding both digital and physical goods mechanical licensing. ASCAP does not license and has never licensed these rights – indeed, our consent decree forbids us from doing so – and hence defers to the expertise of the National Music Publishers Association and the Harry Fox Agency on these matters.

In sum, the Copyright Office proposal, well-intentioned though it is, is fatally flawed throughout.

But, in the Register's and others' testimony before this Subcommittee, we find the outlines of a solution, one based on our unilicense proposal, for our unilicense proposal achieves the same goals advocated by the Register and others, without any of the attendant dislocations and concerns which would result from the Copyright Office's legislative proposal.

The Register testified as follows:

> Should the concept of free marketplace negotiations for reproduction and distribution rights for nondramatic musical works appear to be desirable, then a variation on [the Copyright Office's proposal] might also be worthwhile to explore. One might ask whether it would further benefit the industry as a whole simply to repeal, yet not replace, the section 115 compulsory license. Then reproduction and distribution rights would truly be left to marketplace negotiations. A sunset period of several years would likely be prudent to permit the industry to develop a smooth transition. My prediction would be that music publishers would voluntarily coalesce into music rights organizations, or perhaps would create a single online clearinghouse (or a handful of such clearinghouses) which would permit one-stop shopping while nevertheless permitting each publisher to set its own rates. ***It might be wise to couple repeal of section 115***

> ***with incentives designed to promote one of these alternatives that would result in one-stop shopping or something close to it.***
>
> ***In principle, I favor this approach.***

(Written test., 34-35, emphasis added.) **We suggest that our unilicense proposal is exactly what the Register was advocating – repeal of section 115 with incentives designed to result in one-stop shopping.**

Our unilicense proposal works because: 1) it provides digital users with a true "one-stop shop" where they can get all the rights in musical compositions that they need; 2) it keeps existing licensing structures, thus eliminating any additional administrative expenses of any significance, while reaping the benefits of many decades of licensing experience and expertise; 3) it prevents the utter chaos in the music industry that would result from the Copyright Office proposal; and 4) it does not impose any compulsory licensing regime, and allows the marketplace to function without governmental interference.

We greatly appreciate the leadership shown by the Chairman and Ranking Member in dealing with this issue, and also commend the Register for the laudable goals she set forth in her testimony. We pledge our full efforts to achieve a workable solution, which is beneficial for songwriters, for the music publishers who invest in and facilitate their creativity for the benefit of the public, and for the users of music as well.

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ABOUT ASCAP

The American Society of Composers, Authors and Publishers is the United States' oldest and largest performing rights licensing organization. ASCAP was founded in 1914 by songwriters including Victor Herbert and John Phillip Sousa, for the purpose of licensing the right of nondramatic public performance in the copyrighted musical works they created.

ASCAP is the only true American performing rights *society* – it is an unincorporated membership association, whose members (now numbering over 210,000 active writers and publishers) are exclusively composers, lyricists and music publishers. ASCAP is run by a 24-person Board of Directors consisting of 12 writers and 12 publishers; the writer Directors are elected by the writer members of ASCAP and the publisher Directors by the publisher members. The current Chairman of the Board is the noted, multiple award-winning lyricist Marilyn Bergman.

The ASCAP repertory consists of millions upon millions of musical works in all genres and types – pop, rock, alternative, country, R&B, rap, hip-hop, Latin, film and television music, folk, roots, blues, jazz, reggae, gospel, contemporary Christian, new age, theater, cabaret, dance, electronic, symphonic, chamber, choral, band, concert, educational and children's music – the entire musical spectrum.

ASCAP is home to the greatest names in American music, past and present, as well as thousands of writers in the early stages of their careers. ASCAP members include Cole Porter, Aaron Copland, Stevie Wonder, Bruce Springsteen, Leonard Bernstein, Madonna, Wynton Marsalis, Stephen Sondheim, Dr. Dre, Mary J. Blige, Duke Ellington, Rogers and Hammerstein, Garth Brooks, Tito Puente, Dave Matthews, Destiny's Child, and Henry Mancini, just to name a few. In addition, through affiliation agreements with foreign performing rights societies, ASCAP licenses the music of hundreds of thousands of their members in the USA.

ASCAP's licenses allow music users to perform any and every work in the ASCAP repertory, upon payment of one license fee. ASCAP's hundreds of thousands of

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licensees include Internet sites and wireless services, restaurants, nightclubs, hotels and motels, cable and television networks, radio and television stations, conventions and expositions, background/foreground music services, shopping malls, dance schools, concert promoters, and retail businesses. Those who perform music find ASCAP's licensing model highly efficient, for, with one transaction, they are able to perform whatever they want in the enormous ASCAP repertory.

ASCAP deducts only its operating expenses from the licensing fees it receives (in 2004, operating expenses were 13.5% – lower than any other American performing rights organization, and among the lowest in the world). The remainder is split 50-50 between writers and publishers. Each member's royalty distribution is based on a survey of what is actually performed in the various licensed media. ASCAP royalty distributions make up the largest single source of income for songwriters, enabling them to make a living, pay their rent and feed their families. ASCAP thus fulfills the Constitutional purpose of copyright, allowing songwriters – who are the smallest of small businessmen and women – to earn a fair return on the use of their property and so use their creativity to enrich America's culture.

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Statement of Glen Barros,
President & CEO
Concord Music Group

Before the Subcommittee on Intellectual Property
Senate Committee on the Judiciary

Music Licensing Issues

July 12, 2005

Mr. Chairman, Ranking Minority Member Leahy and other distinguished members of the Subcommittee, good afternoon and thank you for inviting me to participate in this hearing. As the President of the Concord Music Group, an independent record label and music publisher, I recognize and appreciate the leadership this Committee has provided in the past on many issues affecting my business. I am not a lawyer, so I am not going to dwell on the technical details of mechanical licensing. However, I am grateful for the opportunity to share some practical thoughts with you today on how the existing inefficient system of licensing musical compositions is contributing to the contraction of the music industry by preventing companies of all sizes from offering consumers the exciting and competitive products that are necessary if we are to thrive, and maybe even survive, as an industry.

Background

By way of introduction, the Concord Music Group is committed to offering inspiring, innovative and high quality recordings of great artistic merit. Originally formed as an offshoot of the Concord Jazz Festival, Concord Records has been considered a leader in the jazz and traditional pop fields for over 30 years. Last year, Concord acquired and merged with Fantasy, Inc., home to one of the world's most prestigious catalogs of jazz, blues, R&B and rock music, to

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create the Concord Music Group. Today, the Concord Music Group is one of the largest independent record companies in the world and keeper of an extraordinary rich, and, in many cases, historically significant, catalog of recordings from some of the most admired and enduring names in music. Concord is also the holder of a prominent catalog of music publishing rights, including many of the best known songs written by John Fogerty while he was a member of Creedence Clearwater Revival. Over the years, such legendary artists as Tony Bennett, Rosemary Clooney, Count Basie, John Coltrane, Creedence Clearwater Revival, Miles Davis, Duke Ellington, Bill Evans, Ella Fitzgerald, Vince Guaraldi, Isaac Hayes, Thelonious Monk, Tito Puente, Mel Torme, Little Richard, and Otis Redding have recorded for Concord or Fantasy labels. The record company's current recordings and releases include such world-class artists as Peter Cincotti, Chick Corea, Michael Feinstein, Carole King, LaToya London, Marian McPartland, Barry Manilow, Sergio Mendes, Ozomatli, Eddie Palmieri, Sonny Rollins and many more. In all, our catalog contains over 10,000 recordings, ranging from the 1940s through today.

You may be familiar with one of our recent releases, "Genius Loves Company," the final recording by the legendary Ray Charles. This historic CD was completed last year just prior to Ray's death and, in addition to being a multi-platinum seller, received eight Grammy awards, including Album and Record of the Year.

The Concord Music Group currently employs approximately 100 people based in Los Angeles and Berkeley, California. In addition, we provide significant income and revenue to hundreds of others in the production and marketing of our recordings. We currently have nearly 3,500 albums in print and will issue over one hundred new releases this year.

Concord has a broad perspective on the issues being addressed this afternoon. In addition to being a record company, it is important to note that Concord owns significant music

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publishing assets. Accordingly, we see these issues both as an owner and as a user of musical compositions.

The Current System for Licensing Musical Compositions is Not Serving Anyone As It Should

This is a challenging time in the music business. Piracy, other demands on consumers' time and money, radio consolidation, and reduced and less varied inventories at retail have made it much more difficult to market both new and existing recordings, let alone build an audience for a new artist. This has all led to declining sales. But this is also a revolutionary time in the music business. New technologies give us opportunities to offer consumers new and innovative ways to enjoy music. Particularly in the case of genres like jazz, the Internet is a very encouraging means of extending our distribution. In addition, new formats like Super Audio CD ("SACD") and CD/DVD DualDisc offer great promise for giving consumers the exciting products and extra value they want, and that we hope will let us compete successfully for their limited time and money.

Unfortunately, while our business always requires us to balance the concerns of art and commerce, we have particularly struggled with the music licensing issues raised by new technologies and their effects on our investment decisions. Our experience with SACD is illustrative. An SACD is a form of multilayer disc that lets us include music in both a standard stereo format as well as a "surround-sound" format so that the consumer can enjoy an enhanced listening experience with the proper playback equipment but can still listen to it on a standard CD player. It is very exciting to be able to offer some of our jazz masterpieces in the higher fidelity formats possible on an SACD. But introduction of any new kind of offering requires investment and risk. We've invested in releasing some 30 titles in SACD, and are considering

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the investment in more. But it is expensive to remix an album for this new format, and an uphill battle to sell it into limited retail markets. Nonetheless, we believe that the format could expand the overall industry if it were to gain traction and are, therefore, willing to invest toward that end.

After launching our SACD lines, we were informed that many music publishers think that, simply as a result of the music being technically encoded two times on the disc, they are entitled to get paid twice as much for an SACD release of a song as for a regular CD release, even though they sell at generally the same price point. Our counsel tells me that we shouldn't have to pay twice – and as a business proposition I know that to be true. It just doesn't make business sense, however, to invest in promoting a speculative new format while at the same time having to spend time and money arguing with our colleagues in the music publishing community. We'd certainly like to clarify this issue, but there doesn't seem to be any practical way to resolve the dispute.

Another example, of lost business opportunity pertains to adding video content to our musical offerings. On many occasions our marketing and production personnel have asked to provide bonus video material with one of our recordings (for which the consumer is not charged any more), only to be rejected because the licensing process would be administratively prohibitive and the publishing costs would likely be duplicative.

In addition, while the problems in the current system for licensing musical compositions critically impair our ability to pursue new forms of products, those problems are not limited to new technologies or applications. Every day we grapple with musical composition licensing issues. Even in the "easy" case of licensing musical compositions at the statutory rate for a front-line release in the traditional CD format, the process is too slow, too inefficient and too paperwork-intensive. Tackling the licensing for anything out of the ordinary is really daunting.

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You see, every song has at least one publisher and a high percentage have multiple publishers. Given that a CD typically has between ten and twenty tracks, it is common that we must deal with dozens of copyright owners to clear a single album's release. And while many licensing transactions are straightforward, there are tens of thousands of music publishers and countless individuals, such as heirs of writers of older repertoire, who lack either the wherewithal or desire to respond to license requests on a timely basis. Too often we have been burned by committing months of scarce staff time to a clearance effort, only to find late in the process that a project just won't be viable. This frequently and regretfully causes us to conclude at the outset that we can't pursue potential projects because securing all the necessary licenses at an acceptable price is just too difficult and uncertain to warrant investment in the clearance effort. As a relatively small business, we simply need to allocate our staff to completing projects that we know can be licensed on a quick and cost efficient basis.

As a result of examples such as these, consumers are getting less value and are, therefore, buying less. This means that artists are getting less exposure, and writers, publishers and record companies are all making less money than if we could deliver greater value and generate excitement with the consumer. I would like to experiment with many new products and see our music in all types of services. However, on top of the significant investment, risk and downward market forces, it's just not practical for businesses like ours to contend with the licensing issues necessary to make that happen.

It is very important to remember that Concord is a music publisher as well. As such, I certainly want to see writers and publishers receive their fair share of music industry revenues. In fact, given that music publishing rights are typically afforded much higher valuation multiples than recordings, the owner of both types of copyrights has a clear interest in seeing a bigger

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piece of the pie go to the publishing rights. However, as someone who is in the trenches trying to enhance the value of all our rights by producing new music, developing artists and giving consumers what they want, I can tell you that the inefficient process for licensing musical compositions is a substantial impediment to expanding the music industry revenues in which writers and publishers share. It is my steadfast belief that the entire industry, including publishers and songwriters, will see greater income if we had a simpler, more transparent licensing system with lower transaction costs, a percentage rate royalty, and less opportunity for disputes. Writers, publishers and record companies have spent too much time and effort fighting over the division of a shrinking pie. And that will continue so long as that the system for licensing musical compositions prevents companies like Concord from pursuing good projects to meet consumer demand, because consumers will acquire their music from illegal peer-to-peer services or spend their money on other entertainment products. It's time to work together to increase the size of the pie for all of us. If we want to reverse the last few years' trend of shrinking revenues, we need a licensing system fit for the 21st century.

Suggestions for Reform

I'd like to conclude with a few specific suggestions for reform of the current system for licensing musical compositions.

First, we should have a more efficient system for administration of mechanical licensing. The Section 115 license is the only compulsory license that it is not a blanket license. For example, an Internet webcaster can perform all commercial sound recordings by filing a single notice of intention and paying a single Section 114 royalty to the "designated agent." There is no reason we should not have a similar system for Section 115.

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Second, we should have a system with more royalty rate flexibility. The current per-unit, cent-rate royalty often does not reflect the economic realities of new technologies and business models and the resulting changes in the traditional business models. If consumers are prepared to pay a premium price for a DVD-Audio product, a download to a cell phone or a ringtone, songwriters and publishers should get their fair share. Conversely, when it is necessary to provide consumers extra value to win business back from the pirates, or a subscription service presents a different consumer value proposition than the sale of traditional products, the mechanical royalty should reflect that. A percentage royalty – like that which has long been in place in Europe and many other countries – is the only approach that makes sense for the 21st century.

Third, we should have a system with more certain application, and less room for disputes, when licensees are considering investment in new technologies. That could be achieved in part through changes in license terms. For example, a license with fewer intricate requirements and a percentage royalty would not lend itself to disputes the way the current one does. Another part of the solution should be procedural. A small business could never afford litigation over any of these issues, but an expedited proceeding in the Copyright Office might provide a practical way of putting to rest questions like whether we have to pay twice to release an SACD.

Finally, we should consider whether there is anything that should be done to facilitate licensing for uses not currently covered by Section 115. I think there probably are uses like lyrics or limited audiovisual material on DualDiscs where the transaction costs of work-by-work clearance are so high relative to the royalties that the market would bear that we would all benefit from some means to reduce the substantial impediments to these uses.

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I truly believe that making these changes would make a huge difference in enhancing the availability of music through legitimate product and service offerings and grow music industry revenues to the benefit of everyone.

Thank you for your time; I would welcome your questions.

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STATEMENT OF DEL R. BRYANT
PRESIDENT AND CHIEF EXECUTIVE OFFICER
BROADCAST MUSIC, INC.
BEFORE THE
SENATE COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON INTELLECTUAL PROPERTY
ON "MUSIC LICENSING REFORM"

July 12, 2005

Chairman Hatch, Senator Leahy, and Members of the Subcommittee, thank you for the opportunity to testify concerning the important subject of "Music Licensing Reform".

My name is Del R. Bryant. I am President and Chief Executive Officer of BMI, one of the world's leading performing right organizations ("PROs"). America's copyright laws have provided a firm foundation to support a vibrant creative community of songwriters and composers whose works fuel a robust and growing entertainment industry. BMI is proud to represent the public performing rights of over 300,000 songwriters, composers and music publishers, more than any other performing right licensing organization. BMI oversees a repertoire of more than 6.5 million musical works. BMI's repertoire includes outstanding creators in every style of musical composition: from pop songwriters to film and television composers; from country music to gospel; from classical composers to commercial jingle writers; from library music to musical theatre composers; from jazz to hip hop; from metal to meringue; classical to soul; rock to reggae; and all categories in between. BMI also represents the performing rights in the musical works of thousands of foreign composers and songwriters when those works are publicly performed in the United States.

Since BMI's doors opened in 1940, our core competency is licensing the public performing rights of these musical creators and copyright owners. To be successful in this

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mission, BMI developed an understanding of and appreciation for the business models and programming needs of the hundreds of thousands of businesses across our nation that bring our creators' music to the public. We are a trusted bridge between the musical creator and copyright owner on the one hand and the businesses using music on the other. We maintain a sensitivity to the creative process, identifying and supporting musical creation in all its varieties. At the same time, we reach out to our licensees by listening to their needs, and where possible, offering licensing solutions that permit them to focus on their businesses. Our operations are efficient, fair and transparent, and our royalty distributions are accurate and timely. Competition among the American PROs (BMI, ASCAP and SESAC) provides benefits to creators and music users alike. . . a win-win success story for the American enterprise system.

Specifically, BMI's role is to license one of the six exclusive copyright rights, the right to perform publicly musical works. Public performances of musical works occur on radio, television, cable, satellite and the Internet as well as at concerts, sports venues, restaurants, hotels, retail stores and universities, to name a few of the many categories of BMI licensees. BMI licenses its music literally wherever music is communicated to the public. As you know, BMI operates on a non-profit making basis, distributing all income (less overhead and reasonable reserves) to our affiliated songwriters and publishers. The PRO model has proven over the decades to be highly beneficial to the songwriting community as well as to the businesses that require timely and efficient clearance of music copyrights. In her recent testimony before the House Intellectual Property Subcommittee, Register of Copyrights Marybeth Peters highlighted the success of the PRO model. Many groups with whom we negotiate, including DiMA, have acknowledged that BMI does a good job in establishing a fair market value for music.

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The emergence of a viable business in the digital distribution of music in recent years has focused the attention of the industry and members of Congress on issues having to do with licensing of the mechanical right when music is digitally delivered. Some digital music services have complained that the current compulsory license for mechanical rights codified in Section 115 of the Copyright Act is cumbersome and requires reform. While the issue of mechanical licenses has not historically impacted BMI, the digital transmission of music often involves both the mechanical right and the public performing right. Consequently, BMI has attempted to meet our licensees' needs to provide licensing solutions where both rights are required. Over its entire history, BMI has actively represented the public performing right interests of our affiliated songwriters, composers and music publishers in the marketplace as well as in Washington, DC, to protect the performing right which is vital to songwriters' and publishers' livelihoods.[1] We have fought against legislative and regulatory efforts that would unfairly eliminate or truncate the public performing right as it applies to digital transmissions.

In an attempt to resolve the claimed problem that digital music services are unable to secure the necessary mechanical rights and performing rights, I would like to point out that BMI believes that the proposal made by NMPA-HFA, BMI and ASCAP for a "Unilicense" continues to be a preferable solution to the problems at hand. The "Unilicense" proposal does not involve a repeal of the Section 115 compulsory license, which for decades has set the backdrop for licensing of mechanical rights in physical CDs (and LPs and cassettes). Also, it does not create an upheaval in existing music industry licensing institutions with unsettling marketplace repercussions. Rather, it entails an antitrust exemption that would permit the existing PROs and HFA, to offer a one stop shop to obtain a license for the reproduction/distribution and performing

[1] For example, in October 2001 BMI joined ASCAP and the National Music Publishers' Association ("NMPA") in a Joint Statement addressing these Internet licensing issues to meet licensees' needs.

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rights to subscription interactive digital music services. A key component of the proposal is that Congress would establish a fixed license rate as a percent of subscription music services' gross revenues (with minimum fees as appropriate). This rate would provide reasonable compensation to the songwriters and music publishers for the use of their musical works. In this regard, it is noteworthy that the record industry, which has no regulation of its licensing of interactive digital music services, have negotiated substantial rates from these same users for the copyright rights in sound recordings.

There have been complaints by some internet music services' about "double-dipping" by copyright owners of musical works under the current copyright law. These complaints are unfounded. At bottom, they are simply complaints about the separate administration of the public performing and mechanical rights in the U.S. As you know, BMI and ASCAP for decades have licensed public performing rights only, while music publishers have customarily licensed reproduction and distribution rights either directly to record labels or else through the Harry Fox Agency. In Europe, by contrast, both performing rights and mechanical (i.e. reproduction/distribution) rights may be jointly administered. Despite the separate structure of the licensing organizations in the U.S., many businesses have successfully licensed both performance and reproduction rights over the past decades.[2] BMI has long licensed subscription digital music services like Music Choice and DMX, and has licensed video on demand and other cable and satellite television services. Why should performance royalties not be available to

[2] Background music services like Muzak for example have long held performance right licenses from BMI and ASCAP while they also obtain the necessary reproduction licenses from both music publishers and the record labels. Most music appearing in television and film is licensed both for public performance and for "synchronization" (i.e. reproduction) with the program. Internet webcasters pay sound recording rights owners separate fees for public performance and ephemeral reproduction rights under sections 114 and 112 of the Copyright Act.

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songwriters for Rhapsody and other services, when the obvious intent of the subscriber who is enjoying conditional downloads is to *listen* to *performances* of the music?

While DiMA and the Local Radio Internet Coalition ("LRIC") have praised the collective blanket licensing model for licensing Internet music services, in their very next breath they will argue that the performing right should not apply to subscription downloading services.[3] What these services seek is not only ease of licensing the copyright rights they need, but also a bargain basement license fee, all at the expense of the songwriters whose works provide the very foundation of their businesses. As mentioned above, in 2001, BMI and ASCAP publicly stated that they would not seek license fees for pure, unconditional downloads. This should satisfy the needs of "e-tailers" who are selling music digitally with no restrictions. Under these types of new subscription digital music services, however, the consumer's ability to listen to her subscription music (however delivered) stops the minute her subscription expires. The fact is that many of the new online music services also offer a wide variety of limited or conditional downloading services for a monthly subscription fee. It is these services that the PROs seek to license, and that are the focus of the "unilicense" proposal.

In Europe, where societies jointly administer the public performing right and mechanical rights, both the performing rights and mechanical rights are being paid for. The Joint NMPA-HFA/ASCAP/BMI unilicense proposal would accomplish something similar by providing for the necessary exemption from antitrust laws to create a joint licensing "super agency" for this purpose. The unilicense proposal achieves the goal of one stop shopping

[3] DiMA and the LRIC state that the Register of Copyrights agrees that performance rights are not associated with downloads. This is a distortion of the Register's Section 104 report and testimony. The Register's report addressed pure downloads only, and very briefly at that. The report recognized that downloads are public performances under the law. In her subsequent testimony last year the Register advised Congress not to act in this area, and recently has proposed the creation of MROs to permit PROs to license all kinds of downloads.

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without the need for government oversight. It permits a private business issue to be resolved by the private businesses. It achieves this goal with a minimum amount of legislation and regulation. The royalty rate would be set by Congress. There would be no need for the parties to submit to expensive adjudication by Copyright Royalty Judges. The allocation of the royalties collected would be an internal business decision not requiring government intervention or oversight.

I believe that the "Unilicense" proposal directly targets the two types of digital audio transmissions currently being offered by digital music services, namely conditional downloads and interactive streams, for which DiMA and others have claimed that they are unable to obtain the necessary performing right and mechanical licenses. That is why we proposed a targeted solution that is narrowly tailored to fit the problem. Although we question whether or not the digital music services have adequately demonstrated that they cannot obtain the necessary licenses for these services in the market, BMI has nevertheless joined ASCAP and NMPA-HFA to offer a compromise "Unilicense" solution that has a suitably narrow scope and would involve as little disruption to the music industry as possible.

The plain fact is that many of the innovative and exciting new services represented by DiMA offer combinations of streaming and downloading capabilities to their subscribers As the industry's discussions proceed, our primary objective will be to safeguard the *full* value of our affiliated songwriters' and publishers' copyrights and create an efficient and fair licensing system for digital music services. We echo the sentiments of the Register of Copyrights Marybeth Peters when she testified at a recent hearing held by the House Judiciary Committee's Subcommittee on Courts, the Internet and Intellectual Property that the development of

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competitive *licensed* digital music services can help ease the piracy epidemic that is currently sweeping the country (and the world) through unauthorized peer to peer file sharing.

In her testimony, Ms. Peters, proposed legislation entitled "The 21st Century Music Licensing Reform Act," which would repeal the current mechanical compulsory license provision of the Copyright Act (Section 115), in favor of an entirely new structure. Her proposal would redefine the current PROs as "music rights organizations" (or "MROs"). According to the proposal, an "MRO would be authorized, and required with respect to digital audio transmissions, to license the reproduction and distribution rights of any non-dramatic musical work for which it was authorized to license the public performance right."

As we understand it, the Copyright Office's proposal would require MROs to offer a blanket license to audio digital music services that combines both the public performing right and the mechanical rights needed for making the various kinds of digital audio transmissions of music to consumers. Her proposal would facilitate this by automatically amending every public performing right grant to a PRO to include mechanical rights. The licensing contemplated by her proposal addresses all digital audio transmissions,

Although her proposal provides for an unlimited number of MROs, Ms. Peters testified that she anticipates few MROs will actually be created, and that MROs will function similarly to how the three PROs operate in the U.S. today. However, there is concern that many MROs will come into existence since the Copyright Office definition of MRO appears to enable any copyright owner or aggregator to become an MRO. We do not believe that creating a world of dozens (or hundreds) of MROs would be an improvement over the current landscape. In fact, if this were to happen, the proposed cure would actually become no cure at all. The digital music services would be put in a position of having to deal with many more licensing entities than they

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do today. The result would be a very cumbersome licensing process that would serve to benefit pirates who would continue to operate without any authorization while the legitimate digital services would be hampered in their attempts to secure appropriate licensing.

I testified at a recent "PRO oversight hearing" before the House Intellectual Property Subcommittee that the PRO business model of blanket licensing and marketplace negotiations works for licensees and creators alike and should not require legislative intervention. While the Copyright Office proposal to essentially adopt the PRO model for mechanical rights licensing in digital audio transmissions is a strong endorsement of the way we do business, the proposal represents a far-reaching change in the way music publishing rights are licensed in the United States that transcends the immediate issues at hand. At this time, while we appreciate Ms. Peters' attempt to offer a comprehensive overhaul of the mechanical licensing system, BMI believes that there are significant areas of concern and therefore supports the unilicense proposal.

As Ms. Peters' testimony reflects, we are not a part of the problem. We are willing to be part of the solution, however. Whether the solution be our "unilicense" proposal or another, we believe Congress should not lose sight of more modest attempts to address the digital music services' problems.

BMI has been recognized as a global leader in digital initiatives for more than a decade. We were the first music company with a website, the first to license music for performance on the web, and the first to post data on our entire catalog, now more than 6.5 million musical works, on the Internet. We recognized the potential for licensing digital transmissions before Internet streaming was a reality. In calendar year 2004 alone, BMI processed 2.4 billion performances of music from more than 3,500 different digital licensees, and as those numbers grow exponentially, we have the robust infrastructure to track their growing volume, too. We

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provided the core technology for FastTrack, an international alliance of copyright organizations who share a network of performance and mechanical rights data on more than 20 million copyrights.

We look forward to continued conversations with you and your staff and other members of the Subcommittee, and will under the Chairman's leadership continue to work closely with all sectors of the music industry in order to develop music licensing solutions. Mr. Chairman and Mr. Ranking Minority Member, we are grateful to you for the effectiveness of the Copyright Act, which permits BMI to function, and songwriters, composers and publishers to be compensated. Thank you for your many years of strong leadership on these issues which affect the livelihoods of the hundreds of thousands of individuals we represent.

July 12, 2005

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STATEMENT OF RICK CARNES, PRESIDENT
THE SONGWRITERS' GUILD OF AMERICA
ON MUSIC LICENSING REFORM

Intellectual Properties Subcommittee,
Senate Committee on the Judiciary

July 12, 2005

Chairman Hatch, Senator Leahy, and Members of the Subcommittee, thank you for allowing The Songwriters Guild of America the opportunity to testify today on proposals for reform of the music licensing system.

My name is Rick Carnes and I am President of SGA, the nation's oldest and largest organization run exclusively by and for songwriters. I am a working songwriter and have lived in Nashville since 1978. While I have been fortunate to have had a modicum of success in my career-- including co-writing number one songs for Reba McEntire ("I Can't Even Get the Blues") and Garth Brooks ("Longneck Bottle") along with songs for Steve Wariner, Alabama, Pam Tillis, Conway Twitty, and Dean Martin among others-- I am reminded constantly of the perilous existence that all of us who have chosen songwriting as a profession labor under daily.

I am sure the members of this Subcommittee are familiar with the current economic plight of the American songwriter. Over the last decade, more than half of America's professional songwriters have been forced to abandon their careers due to income declines stemming from, among other things, the de-regulation of radio, corporate mergers throughout the music industry, and rampant Internet piracy. The average annual royalty income earned by American songwriters is today well below the national poverty level.

Let me give you the painful facts. When I was a young songwriter, like every aspiring music creator I dreamed of having one of my songs on a million selling album. That, I imagined, would be the very pinnacle of success, assuring my financial security. A closer look at the real numbers illustrates just how naïve I was to place my faith in the current system.

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Under the present compulsory licensing provisions, a songwriter is to receive 8.5 cents per song on any CD ("phonorecord") manufactured and distributed, or legally downloaded, in the United States. So, if one of my songs appears on a million selling album, I am theoretically due $85,000 by statute. However, I split that money half and half with my music publisher by contract. That leaves me $42,500. Then I must spilt that in half again with the recording artist who co-wrote the song with me, leaving me with $21,250. Practically every artist now co-writes every song on his or her album with the primary songwriter, because the record labels have included a controlled composition clause in every new artist's contract that makes it financially ruinous for the artist to record more than one or two tracks that he or she did not co-write. The reason the record companies do this is so they can pay the artist, and his or her co-writer, 75% of the statutory mechanical royalty rate. Because of the controlled composition clause, and with transaction costs deducted, my royalty income is reduced by thousands more dollars.

Thus, after all is said and done, I end up making less than $16,000 for having a song on a million selling CD. Of course, given that the retail charge to consumers for a CD may be as high as $18, a million sales will generate up to $18 million for someone....

Let me put that figure in even starker perspective. Perhaps some of you remember the famous film "The Glenn Miller Story," in which actor James Stewart --playing the great trombonist and American war hero-- explained to his skeptical father that being a songwriter wasn't such a bad way to make a living in 1936. "Pop," he said excitedly, "I get 2 cents for every record sold!" Well, that amounted to $20,000 per million units distributed in the middle of the Great Depression. And that amount, sadly, is in practice more than I get today.

As Register of Copyrights Marybeth Peters recently put it, the current system of compensating authors under Section 115 is "antiquated". No songwriter could possibly argue with such a conclusion other than to insist it was an understatement.

How did American songwriters reach this economic nadir? The most obvious reason is the astonishing fact that the U.S. statutory mechanical royalty rate was not raised from the 2 cent level for 69 years from 1909 to 1978. And for the last 27 years, modest increases to 8.5 cents have not addressed that longstanding, bedrock inequity. The reason I am making less than $16,000 on a million sales is that I am getting 1936 wages in 2005! That truly *is* "antiquated" compensation. More and more songwriters simply can no longer afford to continue to expend the time and energy required to practice their craft, while attempting to support their families. And as we suffer personally, American musical culture --long a source of enormous national pride, international prestige, and positive trade balance-- is endangered along with us.

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Sometime between the enactment of the compulsory license in the early Twentieth Century and the evolution of today's modern music industry, the authors who are granted "exclusive" rights to their respective writings under the Constitution and the United States Copyright Act have lost virtually every ability --due to marketplace inequities-- to effectively influence how their works are licensed and how much they are paid for such licensed uses. As Congress considers reforms to Section 115, songwriters hope that changes will give power back to the creators, starting with a mechanism to raise the mechanical royalty rate to a more reasonable level.

It is not only mechanical royalty rates, however, that need to be changed (although that would certainly represent a good start). Register Peters was also correct when she stated in House testimony last month, "At its inception, the [Section 115] compulsory license facilitated the availability of music to the listening public. However, the evolution of technology and business practices has eroded the effectiveness of this provision." Critically, Register Peters emphasized, "...in determining public policy and legislative change, it is the author--and *not* the middlemen--whose interests should be protected." SGA agrees wholeheartedly.

Songwriters support the digital music revolution. The success of legitimate online services is vital to any chance we have of improving our dire economic situation. We recognize how valuable it may be to streamline the music licensing system in ways that favor getting more music to the market quickly in new creative new formats that consumers desire, like music subscription services. But these services require entirely new licensing solutions because they implicate both mechanical and performance rights.

Thus we were pleased to join recently with our colleagues in the Nashville Songwriters' Association (NSAI) and with our friends in the music publishing industry in taking a substantial leap of faith by allowing subscription-style Internet music services to operate while the parties tried to determine a fair split of the total music revenues generated. With royalty rates and payments for the licenses issued by songwriters and music publishers being held in abeyance, record companies proceeded to negotiate licenses for the sound recordings unilaterally with the subscription services, taking for themselves up to 50% of the services' revenues. With the service providers apparently wanting to pay at most 50% of their revenues to license the music and the record companies already taking 50% that leaves nothing on the table for the creators of the music.

In response to this situation, the songwriter and music publisher community (including SGA, NSAI, The National Music Publishers Association, and the performing rights societies) have put forth a "Uni-license" proposal that we believe best achieves licensing reform while simultaneously providing greater essential marketplace protections for songwriters. Our proposal seeks a reasonable rate of 16 2/3 % of gross Internet subscription service revenues, with a minimum flat dollar fee per as a floor. The songwriters will, in the end, receive roughly half of this percentage-based income, with the publishers sharing in the other half. There can be no public policy justification for giving the creators of the songs--on whose labors the entire music industry depends--anything less than this figure while the record company and service provider 'middlemen'

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take the giant share of the money.

Throughout the Section 115 reform process, the stated goals have included protecting creators, simplifying the licensing process, and achieving "one-stop licensing" for digital subscription services. Our Uni-license proposal would meet these goals, and can also be instituted quickly and with minimal overhead costs. The super agency contemplated by our proposal would allow Internet subscription services to obtain a blanket license for all performing and mechanical rights in exchange for payment of a reasonable percentage of the companies' gross revenues to the agency. The designated mechanical and performance rights agents would then distribute the royalties to the appropriate writers and publishers. Perhaps most importantly, our proposal will get legitimate, on-line subscription services into the marketplace quickly, helping to curtail piracy.

I would mention two points of special concern to songwriters in our proposal to reform the licensing process. The first relates to transparency and songwriter participation. One of the most critical issues for songwriters and recording artists is transparency in the payment process. Songwriters must receive unlimited access to any payment data. To assure this and to guarantee fairness in the process generally, songwriters want a major role in the governing structure of any super agency. The second point relates to transaction costs. The costs of 'sorting out' these blanket distributions should not be shifted onto the creators since we are not the direct beneficiaries of the new 'efficiency' in the licensing process. In fact, distribution costs under a blanket license will be significantly higher for creators than the old mechanical license where a sale could be directly tied to a songwriter.

The songwriter community recognizes that a key goal of Section 115 reform should be to counteract music piracy. The more legitimate music is offered online, the more illegal file sharers will have a viable alternative to piracy. The simplified licensing system described above is intended to facilitate use of music by legitimate on-line services, and thus represents a key means to combat piracy. The songwriter community also recognizes that the inability to secure a compulsory license for a sound recording may be an impediment to offering all music on-line. Songwriters and music publishers have questioned the equity of a compulsory license for musical compositions without establishing a compulsory license for the sound recording as well. Songwriters recognize and respect the arguments made by recording artists and record labels wanting to maintain and control rights to their sound recordings online. They have legitimate reasons for concluding that a compulsory license for sound recordings is a bad idea. However, songwriters believe a delicate balance must be sought to compensate for the marketplace inequities created by this system. We believe the Uni-license proposal of a 16 2/3% royalty rate for the musical composition would help to restore such a balance.

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As alluded to above, another area of drastically needed reform concerns the longstanding record company practice of applying so-called "controlled composition" rate reductions and caps to mechanically licensed musical works. When Congress finally completed reform of American copyright law and enacted the 1976 Copyright Act, which nominally raised the mechanical royalty rate in 1978 and provided a mechanism for future increases, record companies immediately used their market leverage to coerce recording artists into including mechanical royalty reductions and other royalty caps in their recording contracts. The result has been devastating to the songwriter community, as the gains that Congress sought to bestow on us after seven decades of frozen rates were immediately and severely diminished by contract. This inequitable dealing now threatens to infect Internet transactions as well, with certain recording companies seeking to apply controlled rates to on-line sales of recordings. The songwriter community respectfully asks this Committee to examine controlled composition practices, and to assist us in eliminating these clauses once and for all.

During these past few months of freewheeling negotiations among parties in the music industry, there have even been discussions about eliminating the compulsory mechanical license altogether. While we are not philosophically opposed to this idea, pragmatically we feel that keeping the current compulsory license on physical product and adding the new Uni-license for subscription services would be an easier solution for all to administer and create less risk for songwriters. But if the percentage rate for subscription services is going to be set at a level too low for songwriters to make a living; if we can get no relief in an equitable royalty setting procedure; if we are to be perpetually beset with "antiquated" compensation that favors only the 'middlemen'; then we might favor lifting the compulsory and taking our chances in the marketplace. Better a few songwriters survive than none at all. But when lambs and wolves are pitted against one another in "free and open competition," the lambs rarely fare as well as we might hope.

SGA has always believed that at the end of the day what matters most is the music. Songwriters don't write songs just to make money; we make money just so we can keep writing songs. But the story of American songwriters is all too often a "rags to rags" tale. Stephen Foster, America's first professional songwriter, died in poverty with 38 cents in his pocket at the age of 37. He left behind a legacy of songs that moved the entire nation, and that enriched a horde of 'middlemen', but which never earned enough to sustain him or his family. It is my sincerest hope that any reform of the music licensing process will begin and end with a focus on what will help American songwriters and artists survive a very difficult present, and thrive in a much better future.

On behalf of our songwriter-members and all those who create the greatest music in the world, SGA wishes to thank the Subcommittee for the opportunity to share our views on these vital issues.

Thank you.

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Testimony of Ismael Cuebas

Director of Merchandising Operations

Trans World Entertainment Corporation

on behalf of the

National Association of Recording Merchandisers (NARM)

Before the Subcommittee on Intellectual Property

U.S. Senate Committee on the Judiciary

"Music Licensing Reform"

Tuesday, July 12, 2005

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Good morning, Chairman Hatch, Ranking Member Leahy and members of the Subcommittee. Thank you for inviting me to testify today about the current and future profile of music retailing, the related challenges in music licensing and how Congress can help our industry now so it can remain healthy and vibrant. I am Ismael Cuebas, Director of Merchandising Operations for Trans World Entertainment Corporation in Albany, New York. I have held this position since 2001. Prior to that, I was a music buyer for Trans World, a position I assumed in 1994. I currently serve as a liaison between my company's Merchandising, Marketing and MIS Departments. My individual affiliations with NARM include serving on NARM's Media-On-Demand Task Force and Retailers Advisory Council.

Trans World is a member of the National Association of Recording Merchandisers (NARM). Founded in 1958, NARM is an industry trade group that serves the music retailing community. NARM's diverse membership includes brick-and-mortar, "click-and-mortar" and online retailers, wholesalers, distributors, content suppliers (primarily major and independent music labels, but also video and video game suppliers); suppliers of related products and services; artist managers; and consultants, marketers, and educators in the music business field. The Association's retail/wholesale membership alone represents about 25,000 stores and 500,000 employees.

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NARM represents about 85 percent of the music and entertainment retailing marketplace, from Anderson Merchandisers and Handleman Company (Wal-Mart and Kmart wholesalers), Best Buy, Borders, Circuit City, Musicland, Newbury Comics, Target, Tower, and Virgin to "tastemaker" independent retail coalitions and smaller individual specialty stores. Our members also include online retailers like Amazon.com, eBay and Apple Computer's iTunes Music Store, as well as new players in the industry such as Starbucks.

Trans World is one of the largest entertainment retailers in the United States. Founded in 1972, the company currently operates over 800 stores in 46 states, the District of Columbia, Puerto Rico and the U.S. Virgin Islands. Trans World operates e-commerce sites including fye.com, wherehouse.com, coconuts.com and secondspin.com.

Trans World's mall locations operate primarily under the FYE—For Your Entertainment brand. The Company also operates freestanding locations under the names Coconuts Music and Movies, Strawberries Music, Wherehouse Entertainment, CD World, Spec's, and Planet Music.

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Trans World launched the FYE Download Zone—a subscription based digital music subscription and download service—in October 2004. The FYE Download Zone increases the functionality and catalog available for our customers to sample and purchase the music they want. Over 1 million tracks can be accessed via permanent downloads, portable subscriptions or tethered subscriptions and streaming.

Trans World is also designing and developing the next generation of our innovative listening and viewing stations (LVS) called LVS 3. This is a next generation of technology for our customers, which will enhance their overall in-store experience and expand our sales opportunities through new product information displays and full catalog search capabilities.

LVS 3 is more than a device and an improved set of information; it's a whole new technology platform being designed and built to support the growing business of digital media whether burning a CD, delivering digital music to the home, or filling a portable player in the store. Available later this year, LVS 3 will be a destination within a destination—a place in our stores where customers can view promotions, search and browse our full product catalog, place special orders for product not in the store and select digital music in the manner of their choosing.

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As the digital media industry grows, our LVS 3 system will grow with it. We are building a new system for the needs of today and laying the foundation for the needs of tomorrow. For Trans World and its retail contemporaries, tomorrow is here. If this business model is to progress as we all hope it will—and feel there is certainly the strong potential to develop—Trans World will want to have the licensing process be expedited and as seamless as possible. I will explain later in this testimony the obstacles we face in accomplishing this objective.

Music retailers continue to face significant business challenges. A year ago this month, CD sales were ahead of 2003 by about 9 percent. By the end of 2004, that lead had dropped to about 2 percent, but still provided the first positive numbers since 2000. So far this year, however, it has been a decidedly different story. At mid-year, CD album sales have fallen behind 2004 by approximately 7 percent, which is cause for some concern. But historically, the fourth quarter presents some of the year's highest profile artists and album releases, and accounts for a big portion of annual sales.

On the other hand, sales of digital tracks continue to post huge increases year-over-year and offer promise for bright prospects for the entire industry. Consumer demand is clearly there for digital music delivery, fueling increasing interest among music retailers to explore ways they can sell more music to more people in their stores using various new digital delivery models.

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We know that one of the best ways to reduce the demand for pirated digital downloads is to provide consumers with the opportunity to avail themselves of a broad range of exciting, legal alternative products and services—both in retail stores and online. We want to help the industry sell more music to more people.

This is no small challenge and time is definitely not on our side. With this in mind, NARM has been working with its content distributor, kiosk and related technology vendor members, as well as the Recording Industry Association of America (RIAA), to develop in-store options to serve music consumers and add more excitement to the music shopping experience.

Retailers are excited about the prospect of introducing these new offerings in their stores to meet the demands of consumers. Options may include downloading full albums onto a burned CD or portable device; compiling multiple songs onto a custom burned CD or portable device; downloading songs on demand to a portable device; or even downloading songs in the store and sending them to a home or office computer.

Some of the other ideas being talked about include having "just in time" delivery of a sound recording so that a store is always "stocked" and retailers don't lose sales opportunities; and offering out of print recordings or recordings that appeal to niche audiences that stores don't carry because there isn't sufficient space to support demand. Even more exciting is the opportunity to provide consumers with one-of-a-kind, special products like limited distribution of a live concert within days of the performance.

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NARM is uniquely positioned to help advance the industry's efforts to explore the commercial viability of this new technology because its constituents come not just from the retail/wholesale segment, but also from the record label and kiosk/technology communities. NARM is trying to balance the interests of each.

In March 2004, NARM formed a Media-On-Demand Task Force comprised of prominent retailers conducting beta testing of in-store CD burning kiosks. The Task Force spent months sharing experiences and gathering information from retailers, record labels and CD burning technology companies. In February 2005, the Task Force gathered almost 50 representatives from the technology, computer hardware, content and retail communities.

This first meeting was noteworthy because it exemplified a willingness of competitors and trading partners to exchange issues and concerns about how to make this new technology suitable for retailers. The successful meeting concluded with a shared commitment by all participants to get actively and quickly engaged in seeking solutions to shared challenges.

After careful analysis and exchanging specific concerns with the content and technology companies, the Task Force held their second meeting in June 2005 to explore further how retailers can compete with "free" by creating a compelling value proposition for consumers.

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Buoyed by business opportunities to increase special order sales, Task Force members are nevertheless concerned with the slow progress being made in the amount of content available for burning. Whether it's full-length albums or single tracks, the quantity of music that retailers currently have to offer their customers for lawful burning is discouraging.

A significant amount of music is still unlicensed, largely because of the extraordinarily burdensome process that is required. While we are actively working through a myriad of other key issues that need to be addressed as well, clearly the burdens of the music licensing process have surfaced time and time again as an impediment to advancing these business models. Our record label partners are trying to ramp up to handle the convoluted licensing process, but that takes time—time we simply do not have.

In order to support these digital delivery initiatives, we need to modernize the Section 115 license. The Section 115 mechanical license was created at a time and for a technology that doesn't fit with today's new digital technologies.

The license also requires that a royalty be paid on any copy of a sound recording, however many "copies" are made in the process of producing digital downloads or in streaming. These copies are not actually publicly performed in the traditional sense. The statute makes no distinction between ephemeral copies and other copies.

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Additionally, the development of new technologies to deliver music to consumers has raised questions about whether some new products and services implicate purely mechanical licenses, performance licenses or some combination of the two. Attempts to resolve these matters through private negotiations is a time-consuming process ill-suited to the pace of the technological progress in the music industry and has made it virtually impossible for retailers to keep up with consumer demand for legal alternatives to file sharing services.

As this Subcommittee is probably aware, a number of proposals have been offered in the past few months by the various parties involved in the debate over modernization of the Section 115 license. I will take a few moments to comment on these proposals from the NARM perspective.

NARM, together with RIAA and the Recording Artists Coalition (RAC) have strongly advocated a broad blanket license that would cover all technologies and speed up the licensing process. In our view, retailers have a brief window of opportunity in which to launch digital services and capitalize on the growing acceptance and demand for music in a variety of digital formats.

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NARM has applauded various proposals for a new blanket license to facilitate easier clearance of copyrights and has pledged to work with everyone involved in the music industry to find an acceptable compromise. While the parties have worked hard to reach a compromise and we have found much common ground, the principal issue for retailers is that Section 115 be modernized to ease the burden of licensing and that it cover all products in the marketplace.

The current Unilicense proposal being suggested by the performing rights organizations, music publishers and songwriters, does not meet our test as it is too narrow in its scope. The NMPA/PRO/Songwriters proposal applies only to "time-based subscription fee" services. While some retailers may choose to offer subscription services, others are considering alternative digital distribution configurations that will not be subscription-based. Some may do both.

The Copyright Office's proposal would offer broader blanket licensing for the distribution of phonorecords, but unfortunately, the administrative process resulting from eliminating the compulsory license altogether would likely create more uncertainty, and add new levels of complexity, that could actually make things worse instead of better for music retailers.

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These proposals also do not address the new generation of physical products like DualDiscs, that have been embraced by consumers and present an encouraging beacon of hope for the bottom line of "brick-and-mortar" music retailing. This new product is a single disc that includes a CD on one side and an enhanced audio version of that CD, plus video content on the other side.

The music industry needs a vehicle to attract the consumer by offering an exciting value proposition. NARM believes that this is DualDisc. Under the current system, for example, it could take more than 100 separate licenses to clear one DualDisc, which is hindering a more robust release schedule.

Conclusion

NARM supports converting the existing Section 115 license into a blanket license that will cover all products in the marketplace. Based on the what we've learned from our Media-On-Demand Task Force, we believe it's the only way to get licenses cleared quickly and not be embroiled in protracted negotiations. What our retailer members have told us loud and clear is that they need the opportunity to experiment with various digital distribution models over the next few years. Experimentation is critical because it is the key to identifying what kinds of products consumers will want.

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Legal digital download services represent a significant anti-piracy initiative and are a great opportunity for songwriters, publishers, record labels, retailers, and digital service providers to sell more music and generate excitement and enthusiasm among music consumers — a goal everyone in the music industry shares. This opportunity will be missed if retailers can't easily experiment with the whole range of models for providing music on demand.

NARM continues to advocate for a legislative solution that will provide for a broad blanket license with a simplified administrative process so our members may get even with, or ahead of the curve instead of remaining behind it. We are committed to moving forward with both one-to-one and group negotiations, and look forward to working with you and your staff to help resolve these important issues.

I thank the Committee for this opportunity and ask that my written testimony be made part of the record.

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United States Senate
Subcommittee on Intellectual Property
Committee on the Judiciary

Hearing on "Music Licensing Reform"
July 12, 2005

TESTIMONY OF ROB GLASER
Chairman and CEO, RealNetworks, Inc.

Chairman Hatch, Senator Leahy and Members of the Subcommittee,

On behalf of RealNetworks and the Digital Media Association, thank you for inviting me to testify today regarding one of the most significant issues facing legitimate royalty-paying online music services today: outdated music licensing laws that are creating significant legal and business uncertainty and complexity, and inhibiting our ability to innovate and win consumers away from pirate networks. Simply put, it is time to move our 1909-era licensing system into the digital age to help legal services compete effectively with illegal services.

Thanks to the U.S. Supreme Court's Grokster decision, all Americans enjoy greater clarity regarding the boundaries of lawful and unlawful behavior. At the same time, anti-piracy enforcement and education efforts have recently been enhanced by stronger laws, larger budgets, and focused attention.

Following those successes, it is timely and necessary for this Subcommittee to turn its attention to a last important component of a comprehensive anti-piracy legislative effort – modernizing our outdated and ineffective music licensing statutes. By clarifying and simplifying the compulsory composition mechanical license and the statutory sound recording performance license, this Subcommittee and the Congress will provide RealNetworks and the entire online music industry with business and legal certainty and dramatically reduced complexity. Modernizing these statutes will significantly enhance our ability to offer exciting royalty-paying online music services that will win even more consumers away from pirate networks.

RealNetworks pioneered Internet media when we released the first streaming media software in 1995. Since then we have developed technology and services that offer creators and consumers opportunities to connect with high quality digital sound and video as never before – over the Internet, in real-time or on-demand, in secure formats or with the ability to make copies according to the copyright holder's wishes. RealNetworks provides online music and video subscription services to millions of Americans. Our music offerings include Internet radio (both non-interactive webcasting and on-demand streaming, digital download sales, and music subscription services that allow users to rent music and even take it with them on portable devices. Our fellow members in DiMA

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provide similar services to millions more Americans. Collectively we represent the future of legal digital media.

Why am I testifying today about arcane music licensing laws? Because these laws, some enacted as early as 1909, are so outdated and broken that they are backfiring – rather than helping innovators grow the music business and grow artists' revenue, the laws are inhibiting innovative new services as we try to work with our creative partners to defeat piracy. That cannot be what Congress intended, so today I ask the Subcommittee to repair and modernize the Copyright Act's music licensing provisions – Section 115 which concerns music distribution and Section 114 which concerns Internet radio – to help royalty-paying online music services gain legal certainty and cut down on wasteful Kafka-esque paperwork, and thereby to grow faster, and win even more consumers away from pirate networks.

Specifically, there are four concrete measures Congress can take to supercharge the online music industry, dramatically reduce piracy, and substantially enhance songwriters' and recording artists' income, as well as music publisher and recording industry revenue:

1) Replace the dysfunctional Section 115 compulsory mechanical song-by-song license with a simple, comprehensive statutory blanket license that can be administered digitally and triggered on one notice, just like the blanket composition performance rights licenses that are administered by ASCAP and BMI, and just like the blanket sound recording performance rights licenses administered by SoundExchange. Not surprisingly, rules written in the analog world of 1909 simply do not work for licensing the millions of compositions needed to compete today.

2) Confirm that songwriters and music publishers' deserve full-value payment for online services' use of their creative works, but that the payment due when a composition is streamed is entirely in the form of *performance* royalties, and the payment due when a composition is *distributed* as a download is entirely in the form of mechanical royalties. RealNetworks should not be required to pay *double* publishing royalties for our Rhapsody Internet radio and digital download offerings while our broadcast radio and CD retail competitors pay only one royalty.

3) End years of confusion and litigation by clarifying that the definition of "interactive service" in Section 114, with regard to sound recording performance rights, ensures that Internet radio programming based on user preferences falls squarely within the statutory license so long as the service complies with the generally applicable programming restrictions for the statutory license and so long as users are not permitted to control how much a particular artist is heard or when a particular song is played.

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4) Equalize sound recording performance royalty standards so that all radio competitors – broadcast, cable, satellite and Internet – pay the same royalty to artists and recording companies.

RealNetworks' Rhapsody and other DiMA members' online music services compete every day against free music available on illegal pirate networks. We also compete every day with terrestrial, cable and satellite music services. To compete effectively we must offer a comprehensive music catalog and be user-friendly, feature-rich and fairly priced on a level playing field that does not discriminate against the Internet. The amendments I suggest today will accomplish these goals, and in doing so will promote certainty, reduce litigation and risk, and ensure more royalties to creators.

I. Section 115 of the Copyright Act is an Enormous Roadblock to Online Music Services' Success and Our Ability to Defeat Piracy in the Marketplace.

Congress established the Section 115 compulsory "mechanical" reproduction license in 1909 to facilitate the licensing of musical works. Congress's goal at that time, and during the nearly 100 years since, has been to promote the development of new music markets by making copyrighted compositions widely available, while also ensuring that copyright owners get paid for the use of their works.

Fast-forward almost 100 years and the underlying goals and principles remain the same. Royalty-paying online services are precisely the type of new music market that Congress intends to promote; and the Section 115 compulsory mechanical license should play an important role by facilitating online music services' efforts to license broad catalogs of music that are needed to compete with online black markets. Unfortunately, Section 115 as currently written is not very useful to online services, because (i) the licensing process is unworkable for digital music services; and (ii) its ambiguous scope causes uncertainty and risk, which results in excessive double-dip royalty payments.

The §115 licensing *process* is dysfunctional because:

(a) it imposes outdated paper-based and traditional mailing requirements that hinder prospective licensees' ability to efficiently identify copyright owners, license their works and pay royalties. Today's law requires each music service to separately identify the publisher of each of the millions of songs it wants to make available on a service, which is nearly impossible as no comprehensive database exists with such information. Services must then locate and notify by certified mail each publisher, and regularly inform each publisher of every individual work that is deployed on the service. While this process was acceptable for licensing a dozen works at a time for piano rolls and compact discs, it cannot support an online music service that requires more than a million songs to be viable. We need a system that recognizes the advent of computers and the Internet;

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(b) its procedural requirements are based upon antiquated modes of doing business. The statute does not permit adequate modernization to be accomplished by regulation and the penalties for noncompliance are draconian: infringement liability plus disqualification from ever obtaining a compulsory license for that work. Please do not underestimate the chill in the online music industry created by the Copyright Act's combination of a strict liability standard with extraordinarily high statutory penalties. Though intended to protect copyright owners and punish thieves, this combination of strict liability and high monetary damages when combined with outdated procedural requirements is creating massive and wasteful complexity which promotes fear and uncertainty rather than innovation and development of new markets.

There are also significant disagreements about the *scope* of §115's application to legal, royalty-paying digital music services, the impact of which is exacerbated by the threat of strict liability and statutory damages:

(a) there is disagreement about whether on-demand Internet radio services which merely perform music require mechanical reproduction licenses, even though such services do not provide users with copies that the users can control and use as they see fit. DiMA and the Register of Copyrights believe that on-demand performances may justify a higher performance royalty than pre-programmed radio services (and ASCAP and BMI charge almost a 50 percent surcharge for on-demand performances), however, the server-based and ephemeral incidental reproductions that are technically required to render performances should be either royalty-free fair use or should be exempted from royalties under the ephemeral recording exemption that is provided to terrestrial broadcasters in §112 of the Copyright Act;
(b) there is disagreement about whether the §115 license extends to so-called "tethered" downloads made as part of subscription services for which consumers pay a monthly fee, in contrast to permanent downloads, for which consumers generally pay a per-song fee;
(c) there is disagreement about whether the §115 license extends to all the incidental reproductions that are technically required to be made in the course of the distribution of one song to one purchaser (e.g., by a download store), or whether the incidental network and transient reproductions and server copies require an additional license and payment;
(d) there is disagreement about whether the delivery to one purchaser of the same download (i) in two different audio formats, or (ii) to two different locations (e.g. to a work and a home computer) triggers more than one mechanical royalty; and whether the delivery of fully encrypted "locked content" that can not be heard by anyone triggers the payment of a mechanical royalty before it is decrypted and "unlocked" and becomes accessible to the user. For all practical purposes, without the key there is no music, just a jumble of ones and zeroes.

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Though the law and its shortcomings are complex, the result of this antiquated system is simple: legal services are critically handicapped and we are forced to incur significant administrative expenses that should be completely unnecessary in our modern, computerized world. We can not obtain licenses for the broad catalog of songs we need to compete with pirate services and we do not know the final licensing royalty costs of providing our own services. The compulsory, guaranteed-to-be-available publishing license that Congress intended to be a meaningful alternative to negotiating direct licenses with tens of thousands of music publishers is instead so administratively burdensome and of such uncertain scope that it is shackling legal services and undermining rather than promoting innovation and new royalty-paying markets. Meanwhile, illegal services continue to serve their "customers" at light speed across the Internet.

II. A modernized Section 115 will provide necessary clarification for digital services and benefit songwriters and music publishers.

A modern, efficient composition license would provide innovative online music services a practical and efficient means to offer consumers all the music that has been previously recorded and distributed. It would also ensure full-value royalty payments to songwriters and publishers. In testimony and in industry discussions that have occurred under the auspices of the House Judiciary Committee, one solution has been proposed that would meet these goals: a statutory blanket license.

1. The Preferred Solution: A Statutory Blanket Mechanical License Coupled With Clarification On The Scope Of Such License.

The most effective legislative reform would create a statutory blanket license that would provide digital music services the ability to obtain easily the publishing rights they require. Music services would be required to report music usage and pay royalties to an agent designated by rightsholders, who would in turn distribute royalties to songwriters and publishers.

Section 115 currently makes available licenses on a song-by-song basis, because in 1909 when the license was developed, and in 1976 when it was modified, licensees typically required only a handful of compositions to produce a piano roll, composition book or record album. Today, however, online services such as RealNetworks' Rhapsody require more than a million licenses simultaneously, as we seek to offer consumers the most comprehensive music selection possible.

- Only a blanket license can offer modern music services non-infringing access to all available music for purposes of lawful commercial distribution, which was precisely Congress's goal when creating the original compulsory mechanical license.

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- Only a blanket license can eliminate legitimate services' unreasonable legal risk, which would permit us to unleash additional resources for marketing, customer service, and improving systems to deliver royalties electronically.
- Only a blanket license will result in the development of one comprehensive database of all copyright ownership information so services can accurately, electronically and efficiently report all music usage and songwriters can accurately, electronically and efficiently be paid.

Imagine a modern marketplace where we can provide songwriters instant access from any computer to information regarding how their songs were used and how much they will paid. A modernized system will dramatically improve transparency for the artists, remove administrative overhead costs, and with electronic payment systems, will result in much faster payment.

A statutory blanket license does not mean that royalties are discounted, nor that music services are free of reporting obligations. Instead the blanket license would be similar to those provided today by SoundExchange, ASCAP and BMI – the collective agent grants licenses on a non-discriminatory basis for the use of all copyrighted compositions. Royalty rates for the blanket mechanical license would be determined just as mechanical royalty rates have been determined since the 1976 Copyright Act – by industry-to-industry negotiation with an arbitration process available if the parties fail to reach agreement. And music services would be required to pay full-value mechanical royalties and to submit usage reports detailing which compositions have been used and how they have been used, so as to assist the process of ensuring that songwriters and publishers are paid accurately.

Confirm Legal Authority to Set Percentage-of-Revenue Royalties. As music offerings today are much broader than traditional "mechanical" products, royalty structures must also broaden to accommodate industry development. For example, time-based subscription services such as Rhapsody that permit unlimited downloads of songs within a given month, do not lend themselves to traditional cents-per-song royalties. Some rightsholders, however, claim that Section 115 does not permit mechanical royalty rates to be set as a percentage of music service revenue, but rather must be set on a cents-per-reproduction basis.

RealNetworks and DiMA disagree that percentage of revenue royalties are prohibited by current law, but we urge Congress to resolve the confusion around this issue and confirm that percentage-of-revenue royalties are permissible under a modern 115 license. Some rightsholders are concerned that percentage royalties will underpay them as services give music away or as the value of music becomes increasingly lower. But percentage royalty structures have worked well for U.S. performance royalties and for European publishers for several decades.

Clarify that §115 Does Not Apply to Digital *Performances*, and That it Does Apply to *Limited Download* Subscription Services. As discussed earlier, ambiguities regarding the scope of Section 115 have put online music services in the unprecedented situation of being asked for multiple publishing royalties when services appear to not require them.

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Music publishers assert that online music services need mechanical licenses for on-demand performances or "streams" even though we have already obtained performance licenses from ASCAP, BMI and SESAC. They seek mechanical licenses for the server copies and ephemeral "buffer" copies that technically are required to be made solely in order to facilitate the delivery of the performance to the user; but these copies are not controlled by, and have no economic value to, the user. The Copyright Office concludes that on-demand performances should require only performance royalties, and has recommended that Congress confirm this conclusion with clarifying legislation. We urge the Committee to act on this recommendation, and similarly to clarify that digital downloads, whether permanently sold or rented by subscription, do not implicate performance rights unless the download is rendered as music and is audible simultaneous to its transmission.

2. An Interesting Alternative: The "Unilicense" Proposed by the Songwriter/Publisher Community.

In recent months, songwriters, music publishers and their collective licensing agents have recognized that online music services face unique challenges, and that it is in the music community's greater interest to help online services compete against pirate networks. This has resulted in a legislative proposal for a new statutory blanket license that would bundle all performance, reproduction and distribution rights that online services need in order to offer innovative services such as Rhapsody and those of our DiMA colleagues. Though still a conceptual proposal at this point, the proposed "unilicense" has important qualities that RealNetworks and DiMA support:

1) It covers the entire repertoire of U.S. copyrighted music, thus ensuring that online services can offer consumers the most complete repertoire available and thereby compete against pirate networks.

2) It creates a central clearinghouse enabling music services to pay all publishing royalties for all songs in one place and enabling music publishers to collect all digital royalties owed to them from one place. The collective designated agent would also create a mechanism for publishers to identify the compositions they own in one system which is available and transparent to all parties involved. This significantly reduces the transaction costs for both publishers and music services.

3) It limits online services to a single license obligation for each offering, even if the rightsholders and services disagree regarding the scope or value of those rights. This would eliminate double-dip licensing and focus attention instead where it belongs: on determining the value of the music use without regard to how the "rights" are characterized.

4) It recognizes that percentage-of-revenue royalties are an important alternative for modern royalty rate negotiations.

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There are, however, continuing disagreements regarding certain aspects of the Unilicense. Some publishers desire the right to opt out of the unilicense, which would essentially make the license voluntary and completely destroy its value. For any blanket license to work it must be comprehensive, encompassing all music that has otherwise been available through the traditional Section 115 license. Additionally, industries disagree as to whether Congress should legislate a royalty rate. Songwriters and publishers have asked Congress to set a rate 2 – 3 times higher than rates currently being paid by Internet radio services and digital download stores. DiMA prefers that prices not be set by Congress, and that instead we maintain the traditional rate-setting process of statutory and compulsory licenses: industry-to-industry negotiations followed by arbitration if the parties cannot agree.

Additionally, DiMA supports music publisher and songwriter legislative proposals that would recognize that new consumer music offerings that merge digital and physical attributes should not implicate traditional reproduction rights and royalties. Specifically,

- Technologically protected "locked content" that is delivered to consumers in ways they cannot access, e.g., without any key present, should not trigger a royalty until a consumer affirmatively accesses the music;
- Anti-piracy protected multi-session CDs that enable consumers to play the music on multiple devices but which limit their ability to upload the music to the Internet, should only trigger a single mechanical royalty per musical work rather than one royalty for each copy or "session."

3. Eliminating Section 115 will create turbulence and risk, and hinder royalty-paying services' growth.

As Register Peters testified today, the Copyright Office agrees with DiMA that the current Section 115 compulsory license does not work. In past testimony she has recommended that Congress either repair the compulsory mechanical license or discard it entirely. Most recently, however, she has testified in favor of eliminating the compulsory license entirely, and instead requiring that each musical work's digital performance, distribution and reproduction rights be administered in a bundle; and that songwriters and publishers have unlimited choice regarding third-party administration of those bundled rights.

RealNetworks and DiMA disagree strenuously with the Copyright Office recommendation because eliminating the compulsory license would dramatically increase the administrative burden on Internet music services. We believe that the Copyright Office's proposal is certain to impede, rather than assist, our ability to license the broad catalog of musical works necessary to compete with pirate services

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We are deeply concerned that the proposed Music Rights Organizations would not likely develop as the Copyright Office suggests, as the uncertainties associated with the Copyright Office proposal are extraordinary. Experience teaches us that each MRO is likely to impose different and inconsistent royalty and reporting structures – this is exactly what is happening in Europe and it has slowed the roll-out of legal music in Europe. In addition, the proposal does not ensure that the smoothly-operating ASCAP and BMI licensing processes would extend to reproduction and distribution rights. Though it is of course possible that the PROs would voluntarily extend to distribution and reproduction rights their existing operational procedures (i.e., blanket licensing on request and then negotiating price), it seems unlikely that publishers and songwriters would approve this practice. It seems more likely to us that the mere possibility of blanket licensing on request would incentivize publishers and songwriters to create many more MROs than the Copyright Office predicts. Absent the rate court backstop discussed above, nothing would inhibit the PROs (or any newly formed MRO) from preventing legitimate online services' access to blanket licenses that are necessary to build a music service that is competitive against black market networks. Moreover, the federal district "rate courts" which today oversee PROs' performance rights licensing and act as a backstop against anticompetitive conduct, would have no jurisdiction over the PROs' management of reproduction and distribution rights. Waiting for years, possibly decades, of antitrust enforcement activity to work out these issues will be too little, too late to make a difference for today's on-line music industry.

As a result of the unlimited number of new MROs, the Copyright Office proposal would not resolve online services' administrative burden associated with current Section 115, but instead would substitute new, and likely much greater burdens. There is nothing in the proposal to fix today's administrative impossibility – song-by-song licensing combined with the multi-million dollar burden of determining who owns each song in a multi-million song library. Nothing in the proposal prevents MROs from licensing all works on a song-by-song, format-by-format basis as the Harry Fox Agency and the 115 license require today. Moreover, the Copyright Office proposal could spawn hundreds of Music Rights Organizations, and DiMA members would have to obtain licenses from each and every one. And perhaps worst, DiMA services would be forced to match composition licenses obtained from a myriad of publishers and MROs in different data formats and structures with sound recording licenses obtained from record companies in order to ensure that each individual work's license is complete, an extraordinarily complex requirement that has not been successfully accomplished to date by any one, not even by the Harry Fox Agency which has been at this for years.

Rather than destroying the compulsory license altogether, DiMA urges the Subcommittee to fix it – to simplify and modernize the license so that all stakeholders benefit and none are harmed in the process. The statutory blanket license structure has been embraced by all stakeholders in this discussion – including songwriters and music publishers and their representatives, recording companies, online services, and retailers. This Subcommittee should not permit disputes about details to overwhelm the much broader consensus in support of structural reform rather than wholesale destruction.

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III. Clarify and Simplify Internet Radio Laws to Level The Playing Field, Promote Service Growth and Increase Royalties to Record Companies and Artists.

Since the Internet radio sound recording performance license was enacted in 1998 as part of the Digital Millennium Copyright Act, Internet radio services have paid several millions of dollars in royalties to recording companies and recording artists. These payments evidence widespread consumer adoption of Internet radio, but also underscore how the law discriminates against RealNetworks and our DiMA colleagues in the Internet radio business based solely on our choice to deliver music to consumers via the Internet, rather than broadcast, cable or satellite radio technologies.

Today, we ask the Subcommittee to fix the Section 114 statutory sound recording Internet radio license in two significant respects:

1) Clarify when an online radio service's consumer-influence features fall within the scope of the Section 114 statutory sound recording license and when a service is "interactive" and thereby outside of, and not eligible for, the statutory license. This issue has spawned several court cases and a Copyright Office proceeding, and has dramatically reduced innovation in online radio offerings. The Subcommittee can end this legal quagmire and fix the definition of "interactive" service so that it reflects Congress' intention to promote rather than inhibit innovative royalty-paying Internet radio services.

2) Level the playing field among competing radio providers, or at least among digital radio providers. Internet radio, broadcast radio, cable radio and satellite radio compete directly against one another for a limited universe of listeners and advertisers. Unfortunately, as discussed below, Internet radio services are subject to higher royalty rates and a less favorable royalty rate-setting standard than our satellite, cable and broadcast competitors, and we are also limited by more programming and functionality limitations.

1. Confusion Over the Definition of "Interactive Service" Hampers Growth of Services and Royalties.

RealNetworks and DiMA urge the Subcommittee to clarify the definition of "Interactive" Internet radio service so we know when services are eligible for the statutory license and when they are not, without spending millions of dollars in litigation and without risking millions more in damages.

Whether a particular Internet radio service qualifies for the statutory license is dependent on several statutory factors -- most notably the radio service must:

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- comply with programming restrictions known as the "sound recording performance complement", e.g., that limits the number of songs of a single artist or album that can be played in a 3-hour period, and
- not be an "interactive service" as defined in the statute.

The 1995 Digital Performance Right in Sound Recordings Act defined an "interactive" service as "one that enables a member of the public to receive, on request, a transmission of a particular sound recording chosen by or on behalf of the recipient." This definition was clear, and there was never any question (or litigation regarding) whether a service was or was not interactive. In 1998 Congress amended the definition of "interactive" service, changing it from a fairly straightforward and objective test to one requiring a complex subjective analysis. Nevertheless, in both 1995 and 1998 Congress also specified that services may permit some consumer influence in their statutory license programming.

Relying on this safe harbor and their interpretation of the "interactive" restrictions, several companies developed Internet radio services in 1999 and 2000 that permitted varying levels of consumer influence. These services' features included permitting consumers to rate songs, artists and albums, and to request that specific songs or artists' recordings be performed (but not at a specific time or in any specific order). Recording companies complained that these services did not qualify for the DMCA license and threatened to sue. Seeking clarification, DiMA petitioned the U.S. Copyright Office for regulations interpreting the definition, but the Copyright Office declined to propose regulations or to delineate specific features that individually or in combination would disqualify programming from the statutory license. The Copyright Office did, however, affirm unequivocally that services can incorporate consumer influence in their programming without making the service "interactive."

In May, 2001, several recording companies filed a copyright infringement suit against Listen.com, Inc. (now owned by RealNetworks), Launch Media (now Yahoo!), and several additional DiMA companies, seeking to disqualify consumer-influenced radio from the statutory Internet radio license. A few DiMA companies settled by agreeing to pay extraordinarily high royalties and maintain some consumer influence features; others agreed to eliminate all consumer influence features; still others went out of business.

The "interactivity" dispute creates a very straightforward business and competitive problem that should be recognized by the entire music community. Internet radio pays millions of dollars in royalties every year to artists and the recording industry. Broadcast radio – even digital broadcast radio – pays zero. If Internet radio is saddled by rules forcing our programming to be exactly like broadcast radio, or forcing direct label-by-label negotiations regarding royalties that our broadcast competitors are not even required to pay at all, then how are we to compete, succeed, and generate even more royalties for sound recording companies and artists?

Today RealNetworks and many DiMA companies have developed compelling and innovative consumer-influenced radio offerings that we have chosen not to introduce

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because the risk of litigation is too great. This harms the entire music industry community, because the goal of these services is to win consumers away from black market networks, to generate royalties and introduce them to new music, thereby promoting music purchases and subscriptions that grow royalty revenue even more. These services do NOT substitute for on-demand services. They simply enable music lovers to find stations tuned to their desires rather than programmed by a monolithic radio station holding company.

To compete against broadcast radio – which is subject to no royalties – and cable and satellite radio – which are subject to lower royalty rates, Internet radio must be free to create, introduce and promote innovative consumer-influenced offerings using the power of our technology. And let's not forget the artists. The statutory license requires that 50% of royalties paid by statutory license Internet radio services be paid directly to recording artists. The recording companies' efforts to restrict the scope of the statutory license by defining all innovative services as "interactive" directly decreases the amount of royalties paid to artists by Internet radio services.

Instead of holding back the royalty-paying medium, we urge the recording industry, and Members of Congress who believe that sound recording and artists companies should be paid, to unshackle Internet radio's programming restrictions and promote the medium that pays. In furtherance of fully-licensed litigation-free royalty-paying online music, DiMA urges the Subcommittee to amend the "interactive service" definition to ensure that programming based on user preferences falls squarely within the statutory license, so long as the generally applicable programming restrictions for the statutory license are not violated and so long as users are not permitted to control when a particular song might be played. RealNetworks and other DiMA companies want to focus our energy on developing exciting royalty-paying products and services that combat piracy, rather than on lawyers and litigation.

2. All Radio Services, or At Least all Digital Radio Services, Should Pay the Same Royalties and Play by the Same Rules.

   i. Sound Recording Performance Royalty Should be Equalized.

On behalf of the Internet radio industry, RealNetworks today renews a longstanding request: that the Committee equalize the sound recording royalty rates paid by radio services, and particularly by digital radio services. This includes, of course, equalizing the legal rate-setting standard used by CARPs when determining the royalty rates of various types of digital radio services. Setting aside the legalese and the history of how we got to today's disparity, let's focus today on fairness – fairness to competing services, fairness to artists and fairness to recording companies. We note that Register of Copyrights Marybeth Peters also has suggested that the Congress reconsider the rate-setting standards that apply to essentially competitive digital radio services.

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All competitors deserve a level playing field, particularly when an obligation is structured by government. As technologies and new competitive services develop, government should not favor or disfavor a single technology or distribution medium absent compelling circumstances, which do not exist in the radio programming market. The Committee is familiar with cable and satellite television programming royalties and the basis for equity in that marketplace. The same is true in radio – broadcast, cable, satellite and Internet radio.

At minimum, RealNetworks and DiMA implore the Committee to reconsider why Internet radio services are saddled with a royalty rate-setting standard that differs from cable and satellite radio, and that resulted in arbitrators setting our percentage of revenue royalty rates more than 50% higher than our competitors' royalty rates. Putting aside which of the many possible standards should prevail – and whether the right choice already exists in current law or whether a new standard should be developed – basic fairness requires that competitors pay the same royalties to the same providers of the same content. Similarly, fairness to consumers compels a level playing field to ensure fair, robust competition that in the long run favors the most innovative and efficient radio services wins, rather than the services most favored by Congress. Consumer choice free of legal bias, and not Congress, should determine which services thrive and which do not.

ii. The Inequity is Multiplied by the "Aberrant" Ephemeral Sound Recording Reproduction Royalty.

As the Copyright Office noted in a 2001 Report to Congress, there is an imbalance between the legal and financial treatment of so-called ephemeral copies of compositions in the broadcast radio context, and similar copies of sound recordings utilized by Internet radio.

Since 1976 broadcast radio has enjoyed a statutory exemption to make reproductions of compositions so long as the reproduction remains within the radio station's possession and is used solely to facilitate licensed performances of the same music. Internet radio services also require ephemeral recordings to enable their webcasts, but while broadcast radio typically requires a single ephemeral copy, webcasters require several copies to accommodate competing consumer technologies (e.g., RealNetworks or Windows Media formats) and services (e.g., dial-up or broadband Internet access). Each of a webcaster's ephemeral recordings functions precisely like the copy exempted for radio broadcasts, but Internet radio is saddled with having to license these copies, rather than enjoying the benefit of an exemption. In the first Internet radio CARP, the recording industry was awarded nearly a 9 percent bonus on top of the performance royalty for the making of these ephemeral copies which add no independent value. They are simply a by-product of modern technology.

In its Section 104 Report to Congress, the Copyright Office stated that the compulsory license for sound recording ephemerals, found in Section 112(e) of the Copyright Act, "can best be viewed as an aberration" and that there is not "any justification for imposition of a royalty obligation under a statutory license to make copies that . . . are

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made solely to enable another use that is permitted under a separate compulsory license." *Section 104 Report, p. 144, fn. 434.* The Copyright Office urged repeal of this compulsory license; DiMA asks the Subcommittee to act on this request.

iii. Competing Radio Services Should Not Be Subject To Different Programming and Functionality Rules Based Only On Their Different Technologies.

As the Subcommittee may recall, the Section 114 sound recording performance license imposes several rules that apply to Internet radio but not to our satellite, cable or broadcast competitors. Since technologies have evolved and converged and our competitors' radio services now have become available over the Internet or other flexible digital formats, it seems reasonable to amend the sound recording performance complement and other rules that needlessly differ among competitive technologies and services. One example is the restriction that prohibits Internet radio providers from engineering features that facilitate the recording of their radio programming, which prohibition is not similarly applied to cable and satellite radio providers. The result is that the satellite radio provider XM Radio markets an innovative MyFi device that records up to five hours of programming for consumers' portable enjoyment outside the reach of a satellite signal, but Internet radio companies arguably may not offer a similar recording feature and fall within the statutory license. This is blatantly anticompetitive and unfair.

Additionally, the basic programming restrictions that were put in place to reduce the substitutional impact of Internet radio on music sales should be relaxed, as digital broadcasters whose programming is available over the Internet present the same substitutional risk, but are not saddled with these programming restrictions, and of course do not even pay sound recording royalties.

* * * *

Internet music services are at a crossroads today. Legal on-line music services are poised to be the music industry's most powerful weapon against piracy. But we need Congress to modernize the Copyright Act, enabling us to efficiently license, report and pay royalties for the music we sell. The paper and pencil system of the last century simply does not work in the new millennium. A modernized statute will reduce unnecessary administrative overhead, improve transparency for artists and allow us to focus our resources on creating great products and services that beat the pirate services. In this way, Congress can promote innovation, protect copyright, and grow the economic pie for all stakeholders in the music industry.

Thank you for the opportunity to represent RealNetworks, DiMA and the legitimate, royalty-paying online music industry at today's hearing.

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Statement of Senator Patrick Leahy
Intellectual Property Subcommittee of the Committee on the Judiciary
"Music Licensing Reform"
July 12, 2005

Digital music is here – and it is exciting. It is exciting for companies that see business potential in new platforms and formats. It is exciting for musicians who see greater avenues for their artistic expression. Most of all, it is exciting for consumers, who are able to enjoy more music, with more variety, in more ways. Yet, there are obstacles, and we will hear today about outdated laws that were never intended to address digital music.

As legislators, we try to pass laws that stand the test of time. And for the most part, our intellectual property laws accomplish that goal. In fact, Section 115 of the Copyright Act, which will be at the center of today's discussions, has its roots in piano rolls at the turn of the last century. Today we will ask if the same laws that were intended to address player pianos are ready to "go digital."

It does appear that there are problems with the current licensing system, and I would like to thank the Register of Copyrights, Marybeth Peters, for her hard work – and her patience – in helping to work through these problems. Everyone agrees that the present system is not working as efficiently as it might. Potential licensees are unsure of which licensing rights apply to certain activities, and they may have difficulty in even tracking down the appropriate person from whom to obtain those rights. This means that building a comprehensive online catalog of music available to consumers can be a slow, and ultimately impossible, process.

Just as it may be the case that outdated laws have contributed to this problem, it may well be the case that the market offers a solution, either by forcing the parties to adjust to the new environment or by encouraging the stakeholders to back consensus legislation. After all, it is certainly in the interest of everyone to reach an agreement. As Ms. Peters has noted, making legal copies of musical works available online is essential to combating online piracy.

As we look for solutions, our ultimate goal should be clear: to protect the interests of songwriters and serve the interests of consumers.

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Statement of the Local Radio Internet Coalition
Hearing on Music Licensing Reform
Before the Subcommittee on Intellectual Property
Judiciary Committee
United States Senate
Hearing Date July 12, 2005

The Local Radio Internet Coalition appreciates this opportunity to submit its views on the important issues that are interfering with the development of a vibrant market for music on the Internet. The Coalition comprises major radio broadcasting companies that have a vital interest in the development of the Internet as a means to serve their local audiences with convenient access to their broadcast programming and with innovative new programming alternatives.[1] These efforts have been hindered significantly by unreasonable licensing requirements and an antiquated legal framework.

The July 12 Hearing focused primarily on section 115, the mechanical compulsory license. However, that is not the only provision of the Copyright Act that is broken and must be fixed in order to foster legitimate music services on the Internet. The Copyright Office has, in the past, identified problems with the ephemeral recording exemption of section 112. Moreover, defects in the sound recording performance statutory license in section 114 are keeping thousands of radio stations off of the Internet and depriving radio audiences, and the audio market as a whole, of a new, more convenient and more creative way to hear their favorite radio stations. Any legislative effort to address the problems of music on the Internet should address these problems as well as those that exist with section 115.

The Coalition commends the Copyright Office for its recognition that section 115 is broken and that legislation is necessary to fix it and "other problems that hinder the licensing of nondramatic musical works."[2] We also commend the Copyright Office for its effort to unify musical work performance and reproduction rights to eliminate "inefficient" and "questionable" demands for multiple payments for the same transmission of the same work.[3] We view the effort as a positive step, albeit one that does not go far enough. The questionable demands of copyright owners recognized by the Copyright Office are, in fact, a form of double-dipping based entirely on the artificial separation of rights rather than on meaningful economic value.

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[1] The members of the Coalition are Bonneville International Corp., Clear Channel Communications Inc., Cox Radio, Inc., Entercom Communications Corp., Salem Communications Corp., and Susquehanna Radio Corp.

[2] Music Licensing Reform, Statement of Marybeth Peters, Register of Copyrights, before the Subcommittee on Courts, the Internet, and Intellectual Property, Committee on the Judiciary United States House of Representatives 13, June 21, 2005 ("Peters June 21 House Written Testimony"); Written Statement of Marybeth Peters, Register of Copyrights, before the Subcommittee on Intellectual Property, Committee on the Judiciary, United States Senate 12, July 12, 2005 ("Peters July 12 Senate Written Testimony") ("[S]ection 115 is not up to the task of meeting the licensing needs of the 21st century.").

[3] Peters June 21 House Written Testimony 11, 14; *accord* Peters July 12 Senate Written Testimony 25-26 ("it is difficult to understand how [the practice of double licensing] serves the legitimate interest of copyright owners . . . the license of the predominant right should automatically be accompanied by, in effect, a royalty-free license of the incidental right").

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The Coalition supports the Copyright Office's proposal to create a one-stop blanket compulsory license "that will provide a workable solution not just for immediate concerns, but for the foreseeable future."[4] The Coalition also agrees with the Digital Media Association that the fee should be set by arbitration absent negotiated agreement.[5]

The Coalition also is intrigued by the Copyright Office's proposal to create a system of "Music Rights Organizations" and believes that approach might also hold promise if certain key premises are recognized. In particular, the Coalition has substantial concerns that the Copyright Office's reliance for this approach on the model of performance rights licensing fails to recognize the critical importance of the consent decrees to that model. Absent the decrees, the performance rights market would fall under the weight of the performance rights organizations' (PROs') market power resulting from the aggregation of rights and the manner in which those rights are defined. Indeed, many of the characteristics of the performance rights market cited by the Copyright Office in its House testimony, particularly the PROs' licensing of all comers and the success of industry negotiations, depend entirely upon the existence of the consent decrees. Collective administration of copyright rights without appropriate oversight and limitations concentrates market power and distorts the market. The Subcommittee need look no further than the publishers' jointly authored proposal for a "unilicense" costing 16.67% of revenue for evidence of this effect. That amount far exceeds license fees adopted for musical work performance rights under negotiations disciplined by a consent decree. Any legislation that provides for collective administration of licenses should include a provision for judicial or arbitral oversight of fees and terms and additional provisions to ensure the availability of reasonable licenses to all users.

The Coalition stands ready to devote its resources and experience to assist the Subcommittee to develop legislation that can make the Internet the home of diverse, exciting, consumer-friendly legitimate music offerings that provide fair compensation to copyright owners, fair returns to music services, and fair value to the public. The issues are complex but not insoluble. We would appreciate the opportunity to participate fully in any process that follows.

I. Congress Should Resolve Problems Affecting Other Internet Music Services, Including Simulcast Streaming, at the Same Time It Addresses Section 115.

Section 115 is only part of the problem. The patchwork of more recent amendments to a law written for 1976 technology simply will not foster the growth of competitive Internet music services. Among other issues, the ephemeral recording exemption of section 112 should be modernized to accommodate today's realities and the sound recording performance statutory license contained in section 114 needs substantial reform to foster the performance of music on the Internet and to allow consumers to have access to the radio broadcasts that they want to hear when they are away from a radio or in an area with poor reception.

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[4] Peters July 12 Senate Written Testimony 23.

[5] Written Testimony of Rob Glaser, before the Subcommittee on Intellectual Property, Committee on the Judiciary, United States Senate 6, July 12, 2005

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The Coalition is particularly concerned about the difficulties presented by the law to radio broadcasters interested in streaming their broadcast programming over the Internet ("simulcast streaming"). Although the Internet was once believed to offer an important new means by which radio stations could reach their listening audience and serve the public, the medium is vastly underused; its promise wasted.

Radio simulcasting has unique needs that must be accommodated in the law if the public is to have access to this service. Unfortunately, the rules in section 114 largely were developed by the record companies and Internet-only webcasters to meet programming and business models that differ dramatically from those of radio.

The Coalition's concerns relate to four distinct sets of issues—(i) the sound recording performance fee for Internet streaming, including the amount of the fee, the fact that it is imposed on broadcasters for listeners who are within the broadcaster's local service area, and the standard by which that fee is determined, (ii) the conditions under which the necessary statutory licenses are available, (iii) the law governing the making of copies used solely to facilitate lawful performances, and (iv) the threat of impossible and unnecessary reporting and recordkeeping requirements.

A. Simulcast Streaming to Listeners Within a Station's Local Service Area Should Be Exempt.

Congress should make clear that Internet streaming of a radio broadcast to members of a radio station's local over-the-air audience is not subject to the sound recording performance right, just as the over-the-air performance is not. Internet transmissions to those local audiences are indistinguishable from over-the-air performances. They are provided as a service to the public that is ancillary to the over-the-air transmission, to facilitate access. Transmissions to these local audiences provide the same public service benefits to the community as over the air transmissions.

Further, the enormous promotional benefit provided by radio airplay to record companies and recording artists is beyond dispute. Congress has long recognized the value and importance of that promotion to record companies and performing artists. Internet transmissions to a radio station's local audience provide the same benefits to the record companies as the station's over-the-air broadcasts. As the 2002 CARP Panel concluded, "[t]o the extent that internet simulcasting of over-the-air broadcasts reaches the same local audience with the same songs and the same DJ support, there is no record basis to conclude that the promotional impact is any less."[6] RIAA's own CARP witness agreed that "[p]er capita per listener minute, the promotional benefit to Sony of someone listening to a radio signal over-the-air and someone in the same geographical area listening to the same signal over their computer is going to be very similar."[7]

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[6] Final Report of the Copyright Arbitration Royalty Panel in Docket No. 2000-9 CARP DTRA 1 & 2 (February 20, 2002) (hereinafter "Panel Report") at 75.

[7] Transcript of CARP Proceedings at 12861-62 (McDermott).

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The Copyright Act recognizes that transmissions within a radio station's local service area are special, and specifically exempts from the sound recording performance right retransmissions of radio broadcasts that remain within a 150-mile radius of the transmitter.[8] This exemption is not available if the broadcast is "willfully or repeatedly retransmitted more than a radius of 150 miles."[9] The Copyright Office has held that this exemption does not apply to Internet retransmissions, as Internet transmissions are not so limited.

Of course, in 1995, when this exemption was enacted, Congress was not focused on the fact that Internet retransmissions could not be limited to 150 miles. There is no reason to limit this exemption to retransmission services that prevent retransmissions beyond the station's local service area. Transmissions beyond 150 miles may be subject to the right and charged a fee. Transmissions to local listeners should not be, regardless of the fact that other listeners may be outside the local service area.

B. The Sound Recording Performance Fee, and the Standard By Which it Is Set, Should Be Reformed.

The DMCA gave rise to a profound change in the standard by which the sound recording performance fee is set. In 1995, after a fully inclusive process, Congress determined that the fee should be based on a consideration of four policy factors that previously governed rate-setting, which are set forth in section 801(b) of the Copyright Act. These factors include affording the copyright owner a fair return and the user a fair income, recognizing the contribution of both the copyright owner and the service, including the contribution in opening new media for communication, and minimizing the disruptive impact on the structure of the industries involved and on generally prevailing industry practices.

The closed 1998 negotiations gave rise to a new standard—"the rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller,"[10] a standard that has given rise to a presumption in favor of agreements negotiated by the cartel of record companies, acting under the antitrust exemption contained in the Copyright Act.[11] The standard, and RIAA's use of that standard, led to an unreasonably high fee in the 2002 CARP proceeding that set sound recording fees.

In the 1998-2002 proceeding, RIAA relied on 26 agreements that its "Negotiating Committee" had reached with webcasters that had specific needs and a willingness to pay a fee far above the fee that would prevail in a competitive free market. As the arbitration panel found:

> [b]efore negotiating its first agreement, RIAA developed a strategy to negotiate deals for the purpose of establishing a high benchmark

[8] § 114(d)(1)(B).

[9] § 114(d)(1)(B)(i).

[10] § 114(f)(2)(B).

[11] § 114(e)(1).

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> for later use as precedent, in the event a CARP proceeding were necessary. The RIAA Negotiating Committee reached a determination as to what it viewed as the "sweet spot" for the Section 114(f)(2) royalty. It then proceeded to close only those deals (with the exception of Yahoo!) that would be in substantial conformity with that "sweet spot."[12]

The "sweet spot" was not based on any calculation of a reasonable rate of return or any economic study, but "simply reflected on the Negotiating Committee's instinct of what price the marketplace would bear." Panel Report 48 n. 28. The Panel found a "consistent RIAA strategy" to develop evidence to present to the CARP.[13]

The RIAA Committee adopted a "take-it-or leave-it" approach, entering into agreements with services willing to agree to its terms for numerous reasons that did not reflect the value of the sound recording performance right.[14] *In fact, not a single radio broadcaster was willing to pay the fees sought by RIAA.* For this, and a host of other reasons—including the fact that many of RIAA's licensees never paid any fees under their agreements, or never commenced operations—the Panel concluded that 25 of the agreements "do not establish a reliable benchmark."[15] The Librarian confirmed the Panel's rejection of these agreements.

Nevertheless, the Panel ultimately relied entirely on the twenty-sixth agreement—the agreement between the RIAA Negotiating Committee and Yahoo—despite the fact that this agreement resulted from the same common plan by the Committee to create CARP evidence.

Incredibly, the Panel had before it Yahoo's own testimony that it made the deal not because it believed the sound recording fee was competitive, but because it wanted to avoid the cost of participating in the CARP, estimated to exceed $2,000,000. Not by coincidence, this amount was approximately the total amount Yahoo paid under its agreement. In short, the deal did not reflect the value of the sound recording performance right; it reflected the cost of avoiding participation in the CARP litigation.

Yahoo also testified that it could not pass along to broadcasters even the .05 cent per performance fee set forth in its agreement for radio retransmissions. Yahoo's representative told the panel:

> [W]e've not passed any of these fees along to the radio stations because we have every interest in keeping those stations signed up with us. So we've made the business decision that it made more

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[12] Panel Report at 48.

[13] *Id.* at 49. The Panel found that RIAA's denials "lack[ed] credibility" in light of extensive record evidence. *Id.* 49-51.

[14] *Id.* at 51.

[15] *Id.* at 51-60.

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> sense for us to actually stomach these fees than to try to pass them on to our radio station partners because we're afraid that if we tried to do that, they would terminate their agreements with us.[16]
>
> Upon further questioning, Yahoo's representative confirmed that "Yahoo!'s judgment is that if it passed along to the radio stations the radio station retransmission rate that it has negotiated, a lot of those stations would just pull the plug."[17]

Moreover, Yahoo terminated the deal at the end of 2001, before the Panel issued its report recommending a fee. Then, within one week after the Librarian announced his decision affirming the Panel's proposed fee, Yahoo announced that it was shutting down its radio retransmission business.

Later, after the Librarian's decision was rendered, other evidence emerged, further confirming just how unreliable the Yahoo deal was as an indicator of a competitive fair market fee. Mark Cuban, the founder and President of Broadcast.com, the company that became Yahoo's broadcast retransmission business, wrote in June 2002 to the industry newsletter "Radio and Internet News" to say that "the deal with RIAA was designed with rates that would drive others out of the business so there would be less competition."

Why did the arbitration panel rely on this agreement under these circumstances? Simply put, the Panel concluded that an effort "to derive rates which would have been negotiated in the hypothetical willing buyer/willing seller marketplace is best based on a review of actual marketplace agreements."[18] In short, the Panel essentially created a presumption in favor of the RIAA agreements, despite the overwhelming evidence that those agreements did not represent the relevant, hypothetical, competitive free market.

The radio industry, of course, believes that this decision was grossly incorrect. The D.C. Circuit declared the question to be "a close one" but affirmed because of the "extremely deferential" standard of review that existed under the law at the time.[19] In the meantime, we now face the need to litigate the matter all over again, under the same misguided willing buyer/willing seller standard.

The sound recording performance fees adopted by the CARP under the current standard are exorbitant. The same standard should not be allowed to govern fees for 2006-2010. Rather, Congress should return to the four-factor standard of section 801(b).

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[16] Transcript of CARP Proceedings at 11,429 (Mandelbrot).

[17] *Id.* at 11,430.

[18] Panel Report at 43.

[19] *Beethoven.com LLC v. Librarian*, 394 F.3d 939, 953 (D.C. Cir. 2005). This standard of review was abolished by the Copyright Royalty and Distribution Reform Act of 2004.

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C. The Statutory Performance License Conditions Must Be Reformed To Accommodate Longstanding Industry Practice.

The statutory performance license applicable to Internet streaming contains several conditions that are incompatible with the traditional way radio stations are programmed and administered. These conditions impose untenable choices on radio broadcasters which must either (i) change their basic programming and business practices to permit an ancillary Internet service; (ii) obtain direct licenses from each and every record company whose music they play (an absurd concept, considering the impracticability and Congress' longstanding desire to keep record companies and radio broadcasters from direct dealings over what gets played on the radio); (iii) not stream; or (iv) face the prospect of having to defend uncertain and hugely costly copyright infringement litigation if any claims are made that the statutory license is not available.

The statutory sound recording performance license for streaming contains nine eligibility conditions. Three of these conditions are so inconsistent with longstanding broadcasting practices that the parties who negotiated the DMCA conditions recognized that they could not be complied with. Thus, while the statute exempts third parties that retransmit radio broadcasts from these conditions, it requires broadcasters who want to stream their own programming to comply with them.[20] The situation is unfair, unstable, not in the public interest, and must be changed.

The specific conditions that cause problems for broadcasters are:

- Condition (i), which prohibits the play of sound recordings that exceed the so-called "sound recording performance complement" during any 3-hour period, of 3 selections from any one album (no more than 2 consecutively), 4 selections by any one artist (no more than 3 consecutively), or 4 selections from a boxed set of albums (no more than 3 consecutively);[21]

- Condition (ii), which calls into question the ability of a disc jockey to announce the songs that will be played in advance;[22] and

- Condition (ix), which requires the transmitting entity to use a player that displays in textual data the name of the sound recording, the featured artist and the name of the source phonorecords as it is being performed.[23]

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[20] *See, e.g.*, 17 U.S.C. § 114(d)(2)(C)(i), (ii) and (ix).

[21] *Id.* § 114(d)(2)(C)(i).

[22] *Id.* § 114(d)(2)(C)(ii).

[23] *Id.* § 114(d)(2)(C)(ix).

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1. The Sound Recording Performance Complement Is Discriminatory and Inconsistent with Broadcasting Practice.

Radio stations often play blocks of recordings by the same artist or play entire album sides. These features, such as Breakfast with the Beatles, or Seven Sides at Seven, are popular among listeners and remind audiences of great music that is available to buy. Tribute shows (or entire tribute days) are also common on the death of an artist, an artist's birthday, or the anniversary of a major event in music. Thus, many radio stations played numerous George Harrison songs throughout the day after he died. Radio stations similarly played many Beatles songs on the fortieth anniversary of the group's first arrival in New York. All of these practices could be deemed to violate the statutory license if the station were streaming.

2. The Prohibition on Pre-Announcements Is Discriminatory and Inconsistent with Broadcasting Practice.

Condition (ii) prohibits "prior announcement" of "the specific sound recordings to be transmitted" or, even, "the names of featured performing artists" other than "for illustrative purposes." This could be interpreted to mean that every time a DJ says "Next up, the latest hit by Beyoncé," or even, "in the next half hour, more Led Zeppelin," the DJ is violating the license and putting the station at risk for being sued for copyright infringement.

These, and the naming of songs to be played in the near future, are all common broadcasting practices. Ironically, record companies have often encouraged radio stations to make such announcements, as they help keep the listener tuned in and waiting to hear the latest song. Identifying songs should not trigger copyright liability.

3. The Obligation To Provide the Internet Player with a Simultaneous Display of Title, Artist and Album Information Is Discriminatory and Beyond the Capabilities of Many Radio Stations.

Condition (ix) requires broadcasters to transmit a visual statement of the title, artist, and album of the current song playing. This requirement simply does not recognize the realities of the radio business, which has developed over the years to meet the needs of its over-the-air business model. For example, the condition requires a transmitting entity to have a digital automation system to control its broadcasts and to have title, artist and phonorecord information loaded into that system. Many stations do use such a system. But many smaller radio stations, and some of the largest, still run their broadcasts the old-fashioned way – a production employee places a CD manually into the player, hits the play button, and turns dials to fade out one song and start the next.

Further, the great majority of recordings played by radio stations are received directly from the record companies, in the form of advance promotional singles and albums, or from third-party services. Although these discs often include a phonorecord title, many do not. Moreover, radio stations often do not load that title into their music information databases, because it is not relevant to their primary over-the-air activity. These stations should not be disqualified from Internet streaming.

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It makes no sense, and serves no one's interests, to require radio stations to alter their programming practices, which have served both them and the record industry well for decades. Nor is it fair or practical to require broadcasters to incur substantial costs to change the way they do business in order to stream their broadcasts over the Internet. This would be worse than the tail wagging the dog, as Internet streaming today isn't even a hair on the tail compared to radio's core business. There has never been a showing that these three conditions offer any benefit to anyone. They should be eliminated.

D. Congress Should Provide an Exemption for Reproductions of Sound Recordings and Underlying Musical Works Used Solely To Facilitate Licensed or Exempt Performances, and Should Ensure That the Conditions Applicable to Those Exemptions Are Consistent with Modern Technology.

Section 112 of the Copyright Act provides the right to make certain royalty-free temporary copies of musical works and sound recordings from which transmissions are made and that have no purpose other than to facilitate licensed or exempt public performances. These provisions need to be expanded and adapted to accommodate modern realities.

The ephemeral recording exemption of Section 112(a) of the Copyright Act allows an entity entitled to make a public performance of a work to make one copy of the material it is performing in order to facilitate the transmission of that performance, subject to certain restrictions. This exemption is based in large measure on the premise that if a transmitting entity had paid for the right to perform the work, it would be unreasonable (and a form of double dipping) to make the entity pay a second time for the right to make a copy that had no other role than facilitating that performance.[24] The exemption was created during the 1976 revision of the Copyright Act and was crafted to reflect the technology of the time, namely, the use of program tapes by radio and television stations to facilitate their performances.[25]

Of course, program tapes are no longer the staple of broadcasters. Now, radio stations often use digital compact discs and digital music servers to make their performances. However, stations still have the practical need to make recordings in order to make licensed performances. In fact, broadcasters may need to create multiple copies in order to engage in Internet streaming, and the transmission technology itself may cause additional copies to be made.

The DMCA recognized this practical reality when it created the statutory license in section 112(e) for multiple ephemeral recordings of sound recordings performed under the new sound recording performance license. However, by creating a statutory license instead of expanding the section 112(a) exemption, the law created an artificial opportunity for record companies to double dip and earn added fees based on the technology used by the transmitting entity rather than on the economic value of the sound recording.

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[24] Likewise, if public policy interests decreed that the performance should be exempt, there was no rationale for charging a fee to make a copy used solely to facilitate the exempt performance.

[25] *See* H.R. Rep. No. 94-1476, at 101 (1976) (noting that "the need for a limited exemption [for ephemeral recordings] because of the practical exigencies of broadcasting has been generally recognized").

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The Copyright Office opposed this statutory license in 1998 and has recently restated its opposition and its belief that an exemption should be enacted. In the report ordered under Section 104 of the DMCA, the Copyright Office commented that the Section 112(e) ephemeral recording license "can best be viewed as an aberration."[26] The Office went on to say that it did not "see any justification for the imposition of a royalty obligation under a statutory license to make copies that have no independent economic value and are made solely to enable another use that is permitted under a separate compulsory license. . . . Our views have not changed in the interim, and we would favor repeal of section 112(e) and the adoption of an appropriately-crafted ephemeral recording exemption."[27]

Further, the DMCA left a significant gap in the law that has created further risk and uncertainty for all transmitting organizations, even those paying the double-dip ephemeral recording royalty to the record companies. The Section 112(e) statutory license applies to the sound recording, but does not apply to the musical or other works embodied in those sound recordings. It makes no sense to differentiate between the sound recording and the underlying work that is the subject of the recording. Such copies should be exempt for the same reason that multiple ephemeral recordings of sound recordings made solely to facilitate a licensed performance should be exempt.[28]

Moreover, three conditions applicable to the existing ephemeral recording exemption (two of which also apply to the Section 112(e) statutory license) discriminate against broadcasters and ignore the realities of today's technology. First, the exemption in Section 112(a) applies only to copies made to facilitate performances made in the transmitting organization's "local service area." The legislative history of the DMCA made clear that, where the Internet was involved, the "local service area" was congruent with the reach of the Internet.[29] However, in its December 11, 2000 rulemaking holding radio subject to the sound recording performance right, the Copyright Office attempted to support its conclusion by taking the position that broadcasters, but not Internet-only webcasters, were subject to a narrower "local service area" (their primary broadcasting area) and that the Section 112(a) exemption was not available when broadcasters streamed their programs on the Internet.[30] Unfortunately, in making these comments, the Copyright Office was focused on sound recordings, which are subject to the Section 112(e) statutory license; it failed to consider the impact of its position with respect to musical works, which are not covered by Section 112(e). Radio broadcasters do not believe that the Copyright Office's dictum is correct; if it were, radio stations that stream their broadcasts

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[26] *See* U.S. Copyright Office, DMCA Section 104 Report at 144 n.434 (Aug. 2001).

[27] *Id.*

[28] Further, there is no known licensing mechanism available to license the ephemeral recording of all works embodied in performed sound recordings.

[29] *See Digital Millennium Copyright Act*, H.R. Conf. Rep. No. 105-796, at 80 (Oct. 8, 1998) (clarifying that Section 114(f)-licensed "webcasters," whose local service area is the Internet, "are entitled to the benefits of section 112(a)").

[30] *See* 65 Fed. Reg. at 77,300.

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would face uncertainty and risk with respect to ephemeral recordings of the musical works they broadcast. Congress could not have intended this result. Any ephemeral recording exemption should extend beyond transmissions within a "local service area."

Second, the exemption provides that "no further copies or phonorecords" may be made from the exempt or licensed ephemeral recording. While that limitation worked for program tapes, it does not work with today's transmission technologies. The Internet operates by making intermediate copies. Cache and other intermediate copies are essential to any transmission.[31] Digital receivers also typically make partial buffer copies of the works being performed. The "no further copies" condition should be amended so that it does not apply to copies or phonorecords made solely to facilitate the transmission of a performance.[32]

Third, music users more and more are using digital music servers to make licensed performances. Music from compact discs may now be loaded onto computers, from which the performances are transmitted. These server copies have no use other than to facilitate the performance. It serves no purpose, and creates a dead-weight economic loss, to require transmitting organizations to purge these servers every six months.

The ephemeral recording exemption is designed to ensure that transmitting entities that are providing performances to the public can operate efficiently and without uncertainty and risk. These performances are already fully compensated or have been deemed exempt from copyright liability. There should be no further payment needed to make copies used only to facilitate the permitted performance.

E. Congress Should Ensure that Reporting Requirements Do Not Preclude Broadcasters from Engaging in Simulcast Streaming.

The Copyright Act directs the Copyright Office to "establish requirements by which copyright owners may receive reasonable notice of the use of their sound recordings" under the statutory license and "under which records of use shall be kept."[33] The Copyright Royalty and Distribution Reform Act of 2004 has transferred this duty to the Copyright Royalty Judges. The Office has, on an interim basis, required these reports for two weeks each calendar quarter.

To the Copyright Office's credit, the interim regulation is far more manageable than that sought by SoundExchange. That wish list sought census reporting of a multitude of data points

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[31] *See* H.R. Rep. No. 105-551, Part 2, at 50-51 (July 22, 1998).

[32] For the same reason, the law should deal clearly with those cache and buffer copies, which may or may not qualify within the scope of the existing Section 112(e) license. The Copyright Office, in its Section 104 Report, supports this recommendation; after extensive study of the issue, the Copyright Office recommended "that Congress enact legislation amending the Copyright Act to preclude any liability arising from the assertion of a copyright owner's reproduction right with respect to temporary buffer copies that are incidental to a licensed digital transmission of a public performance of a sound recording and any underlying musical work." *See* DMCA Section 104 Report at 142-43.

[33] 17 U.S.C. § 114(f)(4)(A).

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for each and every performance, and would have eliminated virtually all broadcasters from the Internet.

Unfortunately, the interim regulation is still inconsistent with the way many broadcasters—particularly smaller stations—do business. Thus, it all but assures that many stations will be kept from streaming their programming on the Internet. Moreover, the threat of added burdens in the future weighs heavily on the decision to stream or not.

It is important to keep in mind that broadcasters have developed their internal systems to run their primary over-the-air business, not an ancillary Internet service that generates few listeners. Sound recordings played by radio stations often are provided to those stations by the record companies themselves. These sound recordings often are provided on special promotional discs, not the retail album sold to consumers. The precise nature of these promotional recordings varies. In some cases, they are in slickly produced special promotional singles. At other times, the recordings are on "homemade" CD-Recordables, or "CD-Rs," not unlike the discs consumers would burn using their home computers, that contain one or more songs and are identified by nothing more than a handwritten or typed label. Some stations get their music by direct electronic download into the broadcast group's servers, or are sent MP3 files. Smaller labels provide music with even less formality. There is only one constant—*the music provided by the record labels to radio broadcasters commonly does not contain all of the information required even by the interim rule, much less the information that would be required by the rules sought by SoundExchange.* For example, record companies routinely send radio stations songs with only title and artist information.

In addition, almost all radio stations broadcast third-party content at some point during their broadcast day. These syndicated and other third-party programs, provided for over-the-air use, are often accompanied by little, if any, information about the music they include. Nevertheless, the Copyright Office has concluded that it does not have "authority" in the Act to exempt such programs from any reporting obligation, despite the fact that the Act required only "reasonable" notice and recordkeeping.[34]

The type of census reporting sought by SoundExchange is not necessary in order to permit reasonable accuracy in royalty payments. Indeed, the large music PROs, ASCAP and BMI, use sampling for their distribution and require a smaller sample than the Copyright Office has included in its interim rules—typically one or two weeks per year. The PROs even shoulder most of the burden of gathering data themselves by listening to radio stations and are able to identify performances using title and artist information alone.

Congress should either clarify the law or make clear that the "reasonable" reporting obligation it imposed contemplates reasonable sample periods, permits the exclusion of information a station lacks, and would be satisfied by the reporting of sound recording title and artist name.

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[34] 69 Fed. Reg. at 11,521.

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II. Congress Should Eliminate the Double-Dip Licensing that Results from Artificial Bifurcation of Rights Related to a Single Transaction.

The Copyright Office has correctly determined that multiple demands from multiple licensors for multiple rights are interfering with the ability of services to provide innovative lawful music offerings on the Internet.[35] Moreover, despite the Office's hesitancy to name these demands double-dipping, that is precisely what they are. Such demands make neither economic nor legal sense. Any legislative solution to the problems of music on the Internet should establish a system under which a single transaction requires only one license from a given copyright owner or owners.

In its Report under section 104 of the DMCA, the Copyright Office made clear that neither (i) temporary copies incidental to a licensed performance or (ii) public performances incidental to licensed downloads should require separate license.[36] The Office recommended legislation to clarify the former and has said that "it does not endorse the proposition that a digital download constitutes a public performance even when no contemporaneous performance takes place." *Id.* at xxvii. Nevertheless the licensors of reproduction rights continue to assert claims over transactions in the nature of performances and the licensors of performance rights continue to assert claims over transactions in the nature of downloads. These claims are unreasonable.

The copyright rights contained in section 106 were created in 1976 to approximate discrete means by which a work is exploited in light of then-existing technology. Each different type of exploitation (performance, reproduction, distribution) typically implicated a different right, leading to one and only one payment for that transaction. Where multiple rights were implicated (e.g., publication by the reproduction and distribution of copies), there was no history of discrete exploitation and multiple licensing. Nor did Congress envision digital transmissions implicating different rights licensed by different licensors. The law has simply failed to keep pace with technology.

As the Copyright Office recognized in the Section 104 Report, discussing copies incidental to a real-time performance: "this is not a case where an additional use is being made of a work beyond the use that has been compensated. The making of buffer copies is part of the same use. It is integral to the performance and would not take place but for the performance."[37] Conversely, the Office recognized that, even if a download can be considered a public performance, "the performance is merely a by-product of the transmission process that has no value separate from the value of the download."[38]

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[35] Peters June 21 House Written Testimony 11; Peters July 12 Senate Written Testimony 12-13, 25-26.

[36] DMCA Section 104 Report at 142-148; Peters July 12 Senate Written Testimony 25-26.

[37] DMCA Section 104 Report at 145.

[38] *Id.* at 147.

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Del Bryant, in his testimony on behalf of BMI, attempts to justify this double dipping, claiming that the users' concerns "are simply complaints about the separate administration of the public performing and mechanical rights in the U.S."[39] The explanation is baffling—we agree that the unique approach of the music industry of using separate administration for different rights has led to overreaching and aggressive claims by the different licensing bodies. That does not justify those unreasonable demands. Mr. Bryant then argues that because performance royalties are payable for streaming, they should be payable for downloads, because, in Mr. Bryant's words, "the obvious intent of the subscriber who is enjoying conditional downloads is to listen to performances of the music."[40] But the Copyright Act does not give copyright owners the right to license *performances*; it provides only the right to license *public performances*. Indeed, Mr. Bryant's theory proves too much. The purchaser of a CD or of an unconditional download also makes that purchase with the "obvious intent" of "listen[ing] to performances of the music." In such a transaction, the copyright owner receives only one payment—for the copy. He or she does not receive a second payment for the "performance" made when the buyer uses that copy. The one-payment rule should apply with respect to downloads—conditional, unconditional, limited or unlimited—and public performances.

Congress should amend the Act to make clear that such double-dip licensing is not permitted. The law should be clear about which activities implicate the public performance right and which implicate the reproduction right. Only one license should be needed from a copyright owner for a given activity.

III. Any Reliance on the PRO Model To Fix Section 115 Must Take Account of the Critical Importance of the Consent Decrees in Reducing the Market Power Created by Collective Administration.

One option for reform proposed by the Copyright Office (at pages 27-34 of the Register Peters' Written Testimony) is repeal of the section 115 compulsory license in favor of collective licensing. In the House Testimony introducing this approach, the Office credited the collective administration of performing rights model as one "that works very well."[41] In response to questions, the Register cited the fact that the PROs offer licenses to any user that wants them and the fact that the PROs have been able to negotiate successfully with users.

In fact, the very characteristics that the Register cites to justify reliance on the collective administration model owe their existence to the consent decrees that govern ASCAP and BMI. The decrees require ASCAP and BMI to grant licenses, automatically, to all users, subject to later determination of the applicable fee.[42] They also provide significant discipline over rates by establishing recourse to the respective Rate Courts if the parties are not able to negotiate a

[39] Written Statement of Del R. Bryant, Broadcast Music, Inc., before the Subcommittee on Intellectual Property, Committee on the Judiciary, United States Senate 4, July 12, 2005.

[40] *Id.* at 4-5.

[41] Peters June 21 House Written Testimony 14.

[42] ASCAP Decree, section 9. BMI Decree section 14.

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satisfactory agreement. These protections, and others contained in the consent decrees,[43] are critical to protect users from the extraordinary market power that is created by the aggregation of rights and horizontal power to fix prices established by collective administration, and the fact that the rights regime is skewed to require users to clear each work individually, regardless of the administrative burdens that might impose.[44] In other words, the Copyright Office's reliance on the PRO model confirms the importance of protections equivalent to those provided by the ASCAP and BMI consent decrees. The Copyright Office acknowledges that the issue "warrants further consideration."[45]

Collective administration without any means to discipline license fees and terms and without suitable use-based licensing such as the per-program license creates a substantial threat to the market. A licensing collective without a consent decree or the equivalent of a consent decree functions as a monopolist, with whom all radio stations must deal and is capable of extracting supra-competitive fees, far in excess of the relative value of its repertory. Radio stations simply are not able to control the selection of all of the music played during the broadcast day. Many programs and all commercials are created by third parties. The entire value of the program and the commercial should not be held hostage to the claims of the owner of a single composition contained in the program or commercial.

Any legislation to reform music licensing must include legislative protections against such abuse. Congress cannot rely on the possibility that existing decrees will be amended or new decrees with be entered. Entry of a consent decree first requires a decision to bring an antitrust suit by the Justice Department, an Executive Branch agency with extensive demands upon its limited resources. Moreover, a consent decree—even the modification of a consent decree—requires the *consent* of the party subject to the decree. If the party does not consent, the Justice Department must be committed to pursuing a costly and burdensome action against that party. Reliance on such a process for each of the potentially many MROs that could be created would place an unreasonable burden upon the Justice Department, the parties and the courts, all to accomplish the result desired by the Copyright Office and easily established by legislation.

Conclusion

We appreciate the Subcommittee's interest in these matters of great concern for radio broadcasters. Congress should act promptly to repair the law applicable to ephemeral recordings, Internet simulcast streaming and other uses of music on the Internet. Among other

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[43] For example, per program or per segment licenses that permit users to have access to the entire repertory but pay on the basis of use, provide additional protection against anticompetitive conduct by creating the possibility of competition from other license sources. Per program and per segment licenses are also critical to foster equity for users whose programming contains limited amounts of copyrighted music. Such users should not pay the same fee as those that provide music intensive programming.

[44] The ability to save these administrative burdens is sometimes confused with the value of the underlying works and the underlying rights. It should not be. It is an artifact of the legislative regime.

[45] Peters July 12 Senate Written Testimony 32.

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things, Congress should address excessive sound recording performance fees and the methodology for setting those fees.

Excessive rights fees, double-dip royalty claims and legal uncertainties are keeping legitimate music services off of the Internet, hampering those legitimate services that do offer Internet music, and fostering the demand for unlawful downloads. The webcasting provisions of the DMCA were not written with radio broadcasters in mind. The Subcommittee should act promptly and decisively to begin the process of fixing the law in a manner that properly accounts for longstanding radio programming and business practices and recognizes the ancillary nature of Internet streaming to radio broadcasters.

The current state of affairs harms both radio broadcasters and the listening public, who often are unable to listen to their favorite stations in places where over-the-air reception is hampered. It also harms the copyright owners of musical works, who are deprived of their public performance revenues, and performing artists, who are deprived of this additional avenue of exposure and promotion for their music by an industry that for decades has worked hand-in-hand with the recording industry to create demand for those sound recordings through the airplay they receive through radio.

The Coalition stands ready to work with the Subcommittee to reform the system so that radio broadcasters will not continue to be inhibited from placing their programming on the Internet by excessive fees and unrealistic and overly burdensome statutory license conditions and reporting requirements.

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STATEMENT OF MARYBETH PETERS
REGISTER OF COPYRIGHTS
Library of Congress
United States Copyright Office
101 Independence Avenue, S.E.
Washington, D.C.
(202) 707-8350

Before the

U.S. SENATE COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON INTELLECTUAL PROPERTY

109th Congress, 1st Session
July 12, 2005

Senator Hatch, Senator Leahy, and distinguished members of the Subcommittee, I appreciate the opportunity to appear before you to testify on the need to reform section 115 of the Copyright Act and possible ways to accomplish it. Section 115 governs the compulsory licensing of the reproduction and distribution rights for nondramatic musical works by means of physical phonorecords and digital phonorecord deliveries. This compulsory license has been in effect for 96 years. However, the means to provide music to the public have changed radically in the last decade, necessitating changes in the law to protect the rights of copyright owners while at the same time meeting the needs of the users in a digital world. The present language of section 115 is outdated, particularly as applied to the online environment. Reform is necessary not only to promote the availability of a wide variety of music to the listening public, but also to assist in the music industry's continuing fight against piracy.

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This written statement contains three parts. The first chronicles the evolution of the compulsory mechanical license. The second discusses why a need for reform exists, and the final section sets forth some of the suggestions the Copyright Office and interested parties have proposed to accomplish the reform.

Evolution of the Compulsory Mechanical License

1. *Mechanical Licensing under the 1909 Copyright Act*

Starting in 1905, copyright owners began seeking legislative changes which would grant them the exclusive right to authorize the mechanical reproduction of their works. The impetus for this movement was the emergence of the player piano and the ambiguity surrounding the extent of copyright owners' right to control the making of copies of their works on piano rolls. Then, in 1908, the Supreme Court held in White-Smith Publishing Co. v. Apollo Co.[1] that perforated piano rolls were not "copies" under the copyright statute in force at that time, but rather parts of devices which performed the work. This decision spurred Congress to take action and, in 1909, Congress granted copyright owners' wish in part by adding to the Copyright Act the right, but not an exclusive right, for copyright owners to make and distribute, or authorize others to

[1] 209 U.S. 1 (1908).

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make and distribute, mechanical reproductions (known today as phonorecords) of their nondramatic musical works.[2]

However, due to concerns about potential monopolistic behavior, Congress also created a compulsory license to allow anyone to make and distribute a mechanical reproduction of a nondramatic musical work without the consent of the copyright owner provided that the person adhered to the provisions of the license, most notably paying a statutorily established royalty to the copyright owner. Section 1(e) of the 1909 Act allowed any person to make "similar use" of the nondramatic musical work upon payment of a royalty of two cents for "each such part manufactured." However, no one could take advantage of the compulsory license until the copyright owner had authorized the first mechanical reproduction of the work. Moreover, the original license placed notice requirements on both the copyright owners and the licensees. Section 101(e). The copyright owner had to file a notice of use with the Copyright Office – indicating that the musical work had been mechanically reproduced – in order to preserve his rights under the law, whereas the person who wished to use the license

[2] The music industry construed the reference in Section 1(e) of the 1909 Act as referring only to a nondramatic musical work as opposed to music contained in dramatico-musical works. *See,* Melville B. Nimmer, NIMMER ON COPYRIGHT § 16.4 (1976). Congress expressly incorporated this interpretation into the law with the adoption of the 1976 Act. 17 U.S.C. § 115(a)(1). It is important to keep in mind that a "musical work" refers to a composition (e.g., the specification of notes and lyrics, such as written on a page of sheet music) while a "sound recording" refers to the fixation of a particular performance of a composition such as on an audio compact disc. However, to reproduce a recorded song, one needs to obtain licenses both as to the musical work as well as to the sound recording.

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had to serve the copyright owner with a notice of intention to use the license and file a copy of that notice with the Copyright Office. The license had the effect of capping the amount of money a composer could receive for the mechanical reproduction of his work. The two cent rate set in 1909 remained in effect until January 1, 1978, and acted as a ceiling for the rate in privately negotiated licenses.

Such stringent requirements for use of the compulsory license did not foster wide use of the license. It is my understanding that the "mechanical" license as structured under the 1909 Copyright Act was infrequently used until the era of tape piracy in the late 1960s. During this period, the "pirates" inundated the Copyright Office with notices of intention to utilize the compulsory license, many of which contained hundreds of song titles. The music publishers refused to accept such notices and any proffered royalty payments since they did not believe that reproduction and duplication of an existing sound recording fell within the scope of the compulsory license. After this flood of filings passed, the use of the license appears to have again became almost non-existent; up to this day, the Copyright Office receives very few notices of intention.

2. *The Mechanical License under the 1976 Copyright Act*

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The music industry adapted to the compulsory license in the intervening years and, by and large, sought its retention, opposing the position of the Register of Copyrights in 1961 to sunset the license one year after enactment of the omnibus revision of the copyright law. Music publishers and composers had grown accustomed to the license and were concerned that the elimination of the license would cause unnecessary disruptions in the music industry. Consequently, the argument shifted over time away from the question of whether to retain the license and, instead, the debate focused on reducing the burdens on copyright owners, clarifying ambiguous provisions and setting an appropriate rate. The House Judiciary Committee's approach reflected this trend and in its 1976 report on the bill revising the Copyright Act, it reiterated its earlier position "that a compulsory licensing system is still warranted as a condition for the rights of reproducing and distributing phonorecords of copyrighted music," but "that the present system is unfair and unnecessarily burdensome on copyright owners, and that the present statutory rate is too low."[3]

To address these concerns, Congress adopted a number of new conditions and clarifications in section 115 of the Copyright Act of 1976, including:

- making the license available only after a phonorecord has been distributed to the public in the United States with the authority of the copyright owner and only to someone whose primary intent is to distribute phonorecords to the public for private use (§ 115(a)(1));
- disallowing the duplication of a sound recording embodying the nondramatic musical work without the authorization of the copyright owner of the sound recording (§ 115(a)(1));
- allowing for the rearrangement of a nondramatic musical work "to the extent necessary to conform it to the style or manner of the interpretation

[3] H. Rep. No. 94-1476, at 107 (1976), citing H. Rep. No. 83, at 66-67 (1967).

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of the performance involved," provided that the rearrangement "does not change the basic melody or fundamental character of the work" (§ 115(a)(2));

- allowing a licensee to file its notice of intention with the Copyright Office in the case where the public records of the Copyright Office do not identify the copyright owner and include an address (§ 115(b)(1));

- requiring service of the notice of intention on the copyright owner "before or within thirty days after making, and before distributing any phonorecords of the work" (§ 115(b)(1));
- requiring payment only on those phonorecords made[4] and distributed[5] after the copyright owner is identified in the registration or other public records of the Copyright Office (§ 115(c)(1));[6]

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[4] Congress intended the term "made" "to be broader than 'manufactured' and to include within its scope every possible manufacturing or other process capable of reproducing a sound recording in phonorecords." H. Rep. No. 1476, at 110 (1976). Although originally enacted to address the reproduction of musical compositions on perforated player piano rolls, the compulsory license has for most of the past century been used primarily for the making and distribution of phonorecords and, more recently, for the digital delivery of music online.

[5] For purposes of section 115, "the concept of 'distribution' comprises any act by which the person exercising the compulsory license voluntarily relinquishes possession of a phonorecord (considered as a fungible unit), regardless of whether the distribution is to the public, passes title, constitutes a gift, or is sold, rented, leased, or loaned, unless it is actually returned and the transaction cancelled." *Id.*

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- establishment of an independent rate setting body to adjust the rates;[7] and

- allowing for termination of the license for failure to pay monthly royalties if a user fails to make payment within thirty days of the receipt of a written notice from the copyright owner advising the user of the default (§ 115(c)(6)).

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[6] This provision replaced the earlier requirement in the 1909 law that a copyright owner must file a notice of use with the Copyright Office in order to be eligible to receive royalties generated under the compulsory license.

[7] In 1993, Congress passed the Copyright Royalty Tribunal Reform Act of 1993, Pub. L. 103-198, 107 Stat. 2304, which eliminated the Copyright Royalty Tribunal and replaced it with a system of *ad hoc* Copyright Arbitration Royalty Panels (CARPs) administered by the Librarian of Congress. Late last year, Congress passed the Copyright Royalty and Distribution Reform Act of 2004, Pub. L. 108-419, 118 Stat. 2341,which replaced the CARP system with three full-time Copyright Royalty Judges appointed by the Librarian of Congress.

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This revised compulsory license worked reasonably well for the next two decades, but the use of new digital technology to deliver music to the public required a second look at the license to determine whether it continued to meet the needs of the music industry. During the 1990s, it became apparent that music services could offer options for the enjoyment of music in digital formats either by providing the public an opportunity to hear any sound recording it wanted on-demand or by delivering a digital version of the work directly to a consumer's computer. In either case, the possibility existed that the new offerings would reduce and perhaps even eventually replace the need for mechanical reproductions in the forms heretofore used to distribute nondramatic musical works and sound recordings in a physical format, e.g., vinyl records, cassette tapes and most recently audio compact discs. Moreover, it was clear that digital transmissions were substantially superior to, and therefore more desirable than, analog transmissions. In an early study conducted by the Copyright Office, the Office noted two significant improvements associated with digital transmissions: a superior sound quality and a decreased susceptibility to interference from physical structures such as tall buildings or tunnels.[8]

3. *The Digital Performance Right in Sound Recordings Act of 1995*

[8] *See,* Register of Copyrights, U.S. Copyright Office, Copyright Implications of Digital Audio Transmission Services (1991).

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By 1995, Congress recognized that "digital transmission of sound recordings [was] likely to become a very important outlet for the performance of recorded music."[9] Moreover, it realized that "[t]hese new technologies also may lead to new systems for the electronic distribution of phonorecords with the authorization of the affected copyright owners."[10] For these reasons, Congress made further changes to section 115 to meet the challenges of providing music in a digital format when it enacted the Digital Performance Right in Sound Recordings Act of 1995 ("DPRA"), Pub. L. 104-39, 109 Stat. 336.[11] The amendments to section 115 clarified the reproduction and distribution rights of copyright owners of musical works as well as clarifying the role of producers and distributors of sound recordings, especially with respect to what the amended section 115 termed "digital phonorecord deliveries." Specifically, Congress wanted to reaffirm the mechanical rights of songwriters and music publishers in the new world of digital technology.

To accomplish this goal, Congress expanded the scope of the compulsory license to include the making and distribution by means of digital transmissions of phonorecords and, in doing so, adopted a new term of art, the "digital phonorecord delivery" ("DPD"), to describe the delivery to a consumer of a phonorecord by means of a digital transmission, which requires the payment of a statutory royalty under section 115. The precise definition of this new term reads as follows:

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[9] S. Rep. No. 104-128, at 14 (1995).

[10] *Id.*

[11] The DRPA also granted copyright owners of sound recordings an exclusive right to perform their works publicly by means of a digital audio transmission, 17 U.S.C. § 106(6), subject to certain limitations. *See*, 17 U.S.C. § 114.

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> A "digital phonorecord delivery" is each individual delivery of a phonorecord by digital transmission of a sound recording which results in a specifically identifiable reproduction by or for any transmission recipient of a phonorecord of that sound recording, regardless of whether the digital transmission is also a public performance of the sound recording or any nondramatic musical work embodied therein. A digital phonorecord delivery does not result from a real-time, nonintegrated subscription transmission of a sound recording where no reproduction of the sound recording or the musical work embodied therein is made from the inception of the transmission through to its receipt by the transmission recipient in order to make the sound recording audible.

17 U.S.C. § 115(d). What is noteworthy about the definition is that it includes elements related to the right of public performance and the rights of reproduction and distribution with respect to both the musical work and the sound recording. The statutory license, however, covers only the making and distribution of the phonorecord, and only with respect to the musical work. The definition merely acknowledges that the public performance right and the reproduction and distribution rights may be implicated in the same act of transmission, and that the public performance does not in and of itself implicate the reproduction and distribution rights associated with either the musical work or the sound recording. In fact, Congress included a provision to clarify that "nothing in this Section annuls or limits the exclusive right to publicly perform a sound recording or the musical work embodied therein, including by means of a digital transmission." 17 U.S.C. § 115(c)(3)(K).

The DPRA also clarified that the statutory license for digital phonorecord deliveries permits reproduction and transmission by means of a digital phonorecord delivery of a musical composition embodied in a sound recording owned by a third party, provided that the licensee obtains authorization from the copyright owner of the sound recording to deliver the DPD. Thus, the license provides for more than the reproduction and distribution of one's own version of a

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performance of a musical composition by means of a DPD. Under the expanded license, a service providing DPDs can in effect become a virtual record store if it is able to clear the rights to the sound recordings. More importantly, the DPRA allows a copyright owner of a sound recording to license the right to make DPDs of both the sound recording and the underlying musical work to third parties if it has obtained the right to make DPDs from the copyright owner of the musical work.[12]

Apart from the extension of the compulsory license to cover the making of DPDs, Congress also addressed the common industry practice of incorporating controlled composition clauses into a songwriter/performer's recording contract, whereby a recording artist agrees to reduce the mechanical royalty rate payable when the record company makes and distributes phonorecords including songs written by the performer. In general, the DPRA provides that privately negotiated contracts entered into after June 22, 1995, between a recording company and a recording artist who is the author of the musical work cannot include a rate for the making and distribution of the musical work below that established for the compulsory license. There is one notable exception to this general rule. A recording artist-author who effectively is acting as her own music publisher may accept a royalty rate below the statutory rate if the contract is entered into after the sound recording has been fixed in a tangible medium of expression in a form intended for commercial release. 17 U.S.C. § 115(c)(3)(E).

The amended compulsory license also extended to DPDs the already-existing process for establishing rates for the mechanical license. Under the statutory structure, rates for the DPDs

[12] *See*, 17 U.S.C. § 115(c)(3)(I), S. Rep. No. 104-128, at 43 (1995).

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can be decided either through voluntary negotiations among the affected parties or, in the case where these parties are unable to agree upon a statutory rate, by a Copyright Arbitration Royalty Panel ("CARP") – or now by the Copyright Royalty Judges ("CRJs"). Pursuant to section 115(c)(3)(D), the CRJs must establish rates and terms that "distinguish between (i) digital phonorecord deliveries where the reproduction or distribution of a phonorecord is incidental to the transmission which constitutes the digital phonorecord delivery, and (ii) digital phonorecord deliveries in general." The difficult issue, however, is identifying those reproductions that are subject to compensation under the statutory license.

The Need for Reform

At its inception, the compulsory license facilitated the availability of music to the listening public. However, the evolution of technology and business practices has eroded the effectiveness of this provision. Despite several attempts to amend the compulsory license and the Copyright Office's corresponding regulations[13] in order to keep pace with advancements in the music industry and in technology, the use of the section 115 compulsory license, other than as a de facto ceiling on privately negotiated rates, has remained at an almost non-existent level.

There is no debate that section 115 needs to be reformed to ensure that the United States' vibrant music industry can continue to flourish in the digital age. As evident from the numerous proposals for change recently submitted to the Chairman of the House of Representatives' Subcommittee on Courts, the Internet, and Intellectual Property ("House Subcommittee") by

[13] *See,* Notice and Recordkeeping for Making and Distributing Phonorecords, 64 Fed. Reg. 41286 (1999); Mechanical and Digital Phonorecord Delivery Compulsory License, 66 Fed. Reg. 14099 (2001); Compulsory License for Making and Distributing Phonorecords, Including Digital Phonorecord Deliveries, 66 Fed. Reg. 45241 (2001); Compulsory License for Making and Distributing Phonorecords, Including Digital Phonorecord Deliveries, 69 Fed. Reg. 34578 (2004).

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entities representing all aspects of the music industry, the operative question is not whether to reform section 115, but how to do so. Prior attempts to tinker with section 115's language to include online transactions have been useful band-aids, but Congress has had to continue to revisit the same issues as technology and business realities have changed the context. It is now time to modernize section 115 holistically not only to address immediate needs, but also to establish a functional licensing structure for the future.

Because section 115 and its predecessor have rarely been used as functioning compulsory licenses and have served simply as a ceiling on the royalty rate in privately negotiated licenses, it has placed artificial limits on the free marketplace. Until the digital revolution in the mid-1990s, the system worked well enough. As long as the function of section 115 was simply to set the rates for licenses between music publishers and record companies that wished to make and distribute sound recordings and to provide a rarely-used backup procedure for obtaining licenses, there was no compelling need to change the system. But with the rise of digital music services that seek to acquire the right to make vast numbers of already-recorded phonorecords available to consumers, section 115 is not up to the task of meeting the licensing needs of the 21st Century. A new mechanism is needed to make it possible quickly and efficiently to clear the necessary exclusive rights for large numbers of works.

For various reasons that made sense at one time, the domestic music licensing structure for nondramatic musical works has evolved as a two-track system, one for licensing public performance rights and the other for licensing the reproduction and distribution rights. This worked reasonably well when the two sets of rights rarely intersected. But the reality of digital transmissions is that in many situations today it is difficult to determine which rights are

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implicated and therefore whom a licensee must pay in order to secure the necessary rights. Faced with demands for payment from multiple representatives of the same copyright owner, each purporting to license a different right that is alleged to be involved in the same transmission, licensees end up paying twice for the right to make a digital transmission of a single work. Some have called this "double-dipping." I would not characterize it that way; I recognize that separate rights are involved – or at least alleged to be involved – and that copyright owners employ separate licensors for each of those rights. I also recognize that in at least some of these cases, there are reasonable arguments that the ability to license each of these rights has real value to the licensee. But whether or not two or more separate rights are truly implicated and deserving of compensation, it seems inefficient to require a licensee to seek out two separate licenses from two separate sources in order to compensate the same copyright owners for the right to engage in a single transmission of a single work. That is not the case with respect to sound recordings, where the artificial division of the licensing regimes for performances and for reproductions and distribution does not exist, and where licensees can obtain all necessary rights to a work from a single licensor. I have recommended, and continue to recommend, that the law clarify the scope of the various rights, or at the very least provide some mechanism so that copyright owners who merely seek to be paid what they believe they are owed do not face charges of double-dipping.

The increased transactional costs (e.g., arguably duplicative demands for royalties and the delays necessitated by negotiating with multiple licensors) also inhibit the music industry's ability to combat piracy. Legal music services can combat piracy only if they can offer what the "pirates" offer. I believe that the majority of consumers who have engaged in illegal peer-to-peer "file-sharing" of music would choose to use a legal service if it could offer a comparable product.

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Right now, illegitimate services clearly offer something that consumers want: lots of music at little or no cost. They can do this because they offer people a means to obtain any music they please without obtaining the appropriate licenses. However, under the complex licensing scheme engendered by the present section 115, legal music services must engage in numerous negotiations with publishers and record companies which result in time delays and increased transaction costs. In cases where they cannot succeed in obtaining all of the rights they need in order to make a musical composition available, the legal music services simply do not offer that selection, thereby making them less attractive to the listening public than the pirates. The recent Supreme Court decision in Metro-Goldwyn-Mayer Studios v. Grokster[14] affords legitimate music services an opportunity to make great strides in further penetrating the market, but it is an opportunity that will necessarily be squandered if Congress does not modernize the section 115 licensing regime so that legitimate music services take advantage of the blow the Court has struck against illegitimate offerings, before other illegal sources arise. Reforming section 115 to provide a streamlined process by which legal music services can clear the rights they need to make music available to consumers will enable these services to compete with, and I believe effectively combat, piracy.

Interested parties expressed the need for reform during a hearing on March 11, 2004 before the House Subcommittee. A number of witnesses testified about the difficulties they have encountered in licensing the use of nondramatic musical works under this antiquated statutory

[14] No. 04-480, slip. op. (U.S. June 27, 2005), *available at* www.supremecourtus.gov/opinions/04pdf/ 04-480.pdf.

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scheme. Among other things, complaints were voiced about the difficulties in locating copyright owners to obtain licenses to reproduce and distribute nondramatic musical works; the procedural requirements for obtaining a compulsory license; the lack of clarity over what activities are covered by the compulsory license; difficulties in licensing the use of nondramatic musical works for sound recordings in new configurations; and problems created by the per-unit penny-rate royalty established by section 115.

Two of the issues highlighted at that hearing – issues that we at the Copyright Office have been hearing about for several years – involve problems arising when online music services wish to license activities that involve both reproduction and public performance, leading to demands for payment to two separate agents for the same copyright owner (i.e., the "double-dipping" concern); and the contrast between the relatively efficient licensing process for performance rights and the unsatisfactory process for licensing reproduction and distribution rights. While the three performing rights societies – the American Society of Composers, Authors and Publishers ("ASCAP"), Broadcast Music, Inc. ("BMI") and SESAC, Inc. – collectively are able to license public performances of virtually all nondramatic musical works, a significant percentage of nondramatic musical works cannot be licensed from the main licensing agent for the reproduction and distribution rights – the Harry Fox Agency, Inc. ("HFA"). For this and other reasons, some of which I will address below, online music services that wish to obtain licenses to make available as many nondramatic musical works as possible find it impossible to obtain the necessary reproduction and distribution rights.

Because of the problems identified at the March 2004 hearing, the House Judiciary Committee ("House Committee") asked me last July to bring interested parties together to

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address the modernization of section 115.[15] The House Committee asked that I survey areas of concern, identify areas of agreement, and identify the positions of various parties on areas where there was no agreement. I was asked to report on the results of these efforts in September.

Discussions involving the National Music Publishers' Association, Inc. ("NMPA") and its subsidiary The Harry Fox Agency, Inc. ("HFA"), the Digital Media Association ("DiMA") and the Recording Industry Association of America, Inc. ("RIAA") began on July 16, 2004, and continued throughout the summer. At the start of these discussions, there was general agreement within the group that any change to section 115 should be structured along the lines of the section 114 license,[16] including the use of a blanket license and a designated agent to collect and distribute the royalty fees. The group then focused on several key areas, including the scope of a statutory license, collection and distribution of the royalty fees, controlled composition clauses, sublicensing, and rate setting options. In general, the parties reached no consensus on any particular issue, stating instead that their position on any particular issue would depend on how a proposal handled other key concerns.

Nevertheless, the parties discussed a number of options for the scope of a section 115 blanket license, ranging from the broadest possible coverage, including traditional product and musical works in all digital transmissions and new product offerings, to a slight modification of

[15] Letter from Representatives E. James Sensenbrenner, Jr., Lamar Smith, John Conyers and Howard Berman to Register of Copyrights Marybeth Peters of July 7, 2004.

[16] The section 114 statutory license covers the public performance of sound recordings by means of a digital audio transmission. 17 U.S.C. § 114.

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the current license to extend coverage only to online subscription services offering "tethered" downloads and/or on-demand streams. User groups favored the broader approach, seeing it as a way to streamline the licensing process and move new product offerings and media formats into the marketplace with the expectation that they will be a viable option to piracy. NMPA, on the other hand, favored a modest change in the current law, noting its fear that even limited change will harm publishers and traditional business practice. Thus, it supported a blanket license but only to the extent that such a license be administered by a single designated agent and not include physical product.

Besides the scope of a blanket license, other controversial issues involved the administrative aspects associated with collecting and distributing the royalty fees, the process for selecting a designated agent, and the extent to which the designated agent could use the funds for its own licensing practices or lobbying efforts. All participants agreed that a single entity should assume the responsibility for collecting and distributing the royalty fees, but they could not agree on how that entity should be selected or whether or to what it extent it should shoulder the costs of creating a new database for fulfilling its responsibility. To address the later problem, NMPA suggested that the statute provide a means for the designated agent to recover its start-up costs. It also expressed concern over a perceived free-rider problem and suggested that opt-outs not be allowed as a solution to this problem. Participants, however, were unwilling to endorse any proposal on these issues without additional knowledge about the scope of the license, e.g., whether it would be sufficiently broad to generate adequate funds to cover the set-up costs of the program, or a decision on the availability of the information in the database to others.

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Two other issues hotly debated among the participants were the abolition of the controlled composition discount and the right to sublicense. Not surprisingly, NMPA favored nullification of the controlled composition clause in recording contracts with respect to any activities covered by blanket licenses, whereas the record companies, who by virtue of the controlled composition clauses in recording contracts are able to pay the songwriters and publishers less than the statutory rate, opposed any such change. The recording companies contended that the elimination of controlled composition clauses would seriously diminish their flexibility in licensing which, in turn, would have a negative effect on their ability to conduct business and invest in new talent.

Users and copyright owners likewise differed on the sublicensing question. Publishers sought a restriction on the right of a recording company to sublicense use of a musical work covered by a blanket license and stated a preference that services deal directly with the designated agent or music publishers when making digital deliveries under a blanket license. Not surprisingly, the recording companies opposed this position. Their preference was to retain the option of offering services an opportunity to sublicense through them rather than have the service seek out and deal with yet another licensor. They maintained that it would be extremely difficult to market a new product if they could not provide all licenses for use of the product.

One other key issue discussed during these talks concerned the rates and the process to set them. Users wanted a statutory change to clarify that the rate setting body could establish a rate based on percentage-of-revenue. They also wanted clarification as to whether a service must pay for server copies and intermediate reproductions under the law or whether one type of reproduction or both were exempt. This last issue was of particular interest to certain user

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groups who would potentially have to participate in more than one ratesetting proceeding to set rates applicable to a single activity, i.e., webcasting.

Formal discussions concluded in early September and, on September 17, I reported my observations to Representatives Sensenbrenner, Conyers, Smith and Berman, noting that these parties were willing to explore legislation to establish a blanket licensing scheme in section 115 to facilitate the licensing of copyrighted nondramatic musical works even though significant differences remained among the parties regarding the appropriate scope of such a license and regarding operational and economic issues.[17] My letter also noted that the parties were willing to continue discussions among themselves and with the Copyright Office in an effort to arrive at consensus legislation. The outgrowth of these discussions were a number of different proposals on how to reform section 115 submitted to Representative Smith in recent months by various organizations representing publishers, songwriters, performing rights societies, record companies, online music services, and record retailers. In general, those proposals appear to reflect the same disparity of views that I reported on last September. The only consensus appears to be that the interested parties would be amenable to a blanket license with one designated agent and the filing of only one notice to use any number of works. In light of the facts that the interested parties agree that section 115 does not adequately meet the current and future needs of the music industry, that the parties are unable to agree upon a solution, and that prior amendments to the Copyright Act and the Copyright Office's regulations have not fully remedied

[17] Letter from Register of Copyrights Marybeth Peters to Representatives E. James Sensenbrenner, Jr., Lamar Smith, John Conyers and Howard Berman of September 17, 2004.

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the problems, the time has now come to revise section 115 holistically. And, as noted above, the recent decision in MGM v. Grokster provides the music industry with an opportunity to capitalize on the Court's unanimous condemnation of illegitimate services that set out to exploit the market for mass infringement. It can do so by offering consumers easily available and affordable access to the music that consumers want. Removing the impediments to the licensing of legitimate online services is a necessary step in making that marketplace work.

Proposed Legislative Solutions

Any solution to the crisis in music licensing must make it easy for licensees to obtain, from a single source or at least a manageable number of sources, all the necessary rights for all the musical compositions licensees wish to offer to the public. Such "one-stop shopping" is essentially available today with respect to performance rights.[18] However, nothing approaching "one-stop shopping" exists with respect to reproduction and distribution rights. And as noted above, a music service must obtain separate licenses for (1) the performance and (2) the reproduction and distribution of the same musical works, even when the performance, reproduction and distribution all take place in the course of a single transmission. True "one-stop shopping" would involve (1) all the musical compositions one wishes to license, and (2) all necessary rights one wishes to license.

[18] In actuality, the performing rights societies – ASCAP, BMI and SESAC – offer "three-stop shopping": A music service that wishes to license the rights to all nondramatic musical compositions must obtain a license from each of the three societies. But that has not proved to be a significant burden with respect to the licensing of performance rights.

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As I see it, there are two ways to accomplish such "one-stop shopping." First, a solution along the lines of our discussions last year, transforming the section 115 compulsory license into a section 114-style blanket license with royalty payments funneled through a single designated agent could simplify the licensing process. Alternatively, the section 115 compulsory license could be abandoned – at least with respect to digital phonorecord deliveries – and replaced with a system of collective licensing similar to systems in place in many other countries. Each option has its pros and cons, as well as a host of controversial issues and logistical concerns. Regardless of whichever option is selected, further discussion with interested parties will necessarily be required in order to minimize disruption to the industry. Because our discussions last year centered on a blanket statutory license, I will first address that alternative.

1. *Expansion of the Section 115 Compulsory License*

a. *A Blanket Compulsory License*

Section 114 of the Copyright Act may provide a useful model for licensing of reproduction and distribution of nondramatic musical works. Under section 114, an eligible music service may obtain a license to transmit certain kinds of performances of all sound recordings by filing a single notice of intent to use the statutory license with the Copyright Office. Royalty rates and terms of payments are established by the Copyright Royalty Judges through the mechanism set forth in Chapter 8 of the Copyright Act. The royalty payments are made to a designated agent of copyright owners and performers (currently SoundExchange, which is controlled equally by record companies and performers), which distributes the royalties to the copyright owners and performers.

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A similar mechanism under section 115 would permit a digital music service to obtain a license to make digital phonorecord deliveries of any musical composition (or at least of any musical composition that has been distributed to the public in the United States under the authority of the copyright owner; *see,* 17 U.S.C. § 115(a)(1)) simply by serving or filing a notice of intent to use the statutory license. Royalty payments would be made to a single entity which would then redistribute those royalties to the copyright owners, and the royalty rates and terms of payment would be established under the Copyright Royalty Judge system.

Last year I tried without success to guide the interested parties to consensus on such a proposal, and I have not given up hope that agreement may ultimately be reached. However, the interested parties thus far have not been able to resolve their differences, and I suspect that in order for such a solution to be accomplished, it may be necessary for Congress to make some important decisions notwithstanding the lack of consensus among all the affected parties.

My 2004 testimony before the House Subcommittee[19] addressed such an approach, among others. Interested parties have also recently submitted to the House Subcommittee various proposals for further amendment. The two points of agreement among the interested parties seem to be a desire to have a blanket licensing scheme with one designated agent and a single notice procedure regardless of the number of

[19] *See,* Statement of Marybeth Peters, the Register of Copyrights, before the Subcommittee on Courts, the Internet, and Intellectual Property of the House Committee on the Judiciary, *Section 115 Compulsory License, available at* http://www.copyright.gov/docs/regstat031104.html.

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musical works to be utilized pursuant to the statutory license. I agree with the consensus on these two fundamental points.

One of the main points of contention, however, is the envisioned scope of the compulsory license. As explained in my recounting of last summer's multiparty discussions, the music publishers in general seem to favor a narrow expansion to address only the most critical issues (online subscription services offering limited downloads and on-demand streams), while the record companies and user groups seem to favor a more holistic approach to encompass all issues such as audiovisual works, server and other intermediate copies, ringtones and promotional uses. Although I am not yet prepared to take a position on all of these specific issues, I do in general favor an approach that will provide a workable solution not just for immediate concerns, but for the foreseeable future. I do, therefore, believe that at a minimum the compulsory license should be clarified to expressly include within its scope all intermediate reproductions of a nondramatic musical work made within the course of any digital phonorecord delivery, including buffer, cache and server copies.[20]

[20] Technically, these are phonorecords rather than copies, *see* 17 U.S.C. § 101 (definitions of "copies" and "phonorecords"), but terms such as "buffer copy" and "server copy" have entered common parlance.

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Similarly, consideration should be given to amending the section 115 license to provide that reproductions of nondramatic musical works made in the course of a licensed public performance are either exempt from liability or subject to the statutory license. When a webcaster transmits a public performance of a sound recording of a musical composition, the webcaster must obtain a license from the copyright owner for the public performance of the musical work, typically obtained from a performing rights organization such as ASCAP, BMI or SESAC. At the same time, webcasters find themselves subject to demands from music publishers or their representatives for separate compensation for the reproductions of the musical work that are made in order to enable the transmission of the performance. I have already expressed the view that there should be no liability for the making of buffer copies in the course of streaming a licensed public performance of a musical work.[21] On the other hand, RIAA and the Harry Fox Agency have reached an agreement that buffer copies and server copies made for purposes of or in the course of the streaming of performances are included within the scope of the section 115 compulsory license. But perhaps more important than the decision whether to provide an exemption for such copies or to include them within the section 115 license is the need to clarify the status of such copies one way or another. Any reform of section 115 should definitively resolve that issue.

Another issue to consider is the administration of an expanded section 115 license. It is not clear to me whether all the affected parties subscribe to the notion that

[21] *See*, U.S. Copyright Office, DMCA Section 104 Report 142-146 (2001), *available at* http://www.copyright.gov/reports/studies/dmca/sec-104-report-vol-1.pdf. Statement of Marybeth Peters, The Register of Copyrights, before the Subcommittee on Courts, the Internet, and Intellectual Property of the House Committee on the Judiciary, *Oversight Hearing on the Digital Millennium Copyright Act Section*

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a blanket section 115 license should be available to any qualified service that files or serves a notice of intent to use that license, or whether a service wishing to use the license must somehow obtain the license from the copyright owner or its representative. Within a statutory licensing scheme, I see no reason why prospective licensees should have to do anything to obtain the license other than serve notice of their intent to use the license and comply with all the requirements of that license.

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104 Report, available at http://www.copyright.gov/docs/regstat121201.html.

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In any event, how to set up the entity that would collect the royalties and disburse them to copyright owners is a key issue. One model is the section 114 model, in which a new entity representing and controlled by copyright owners would be created to serve this function. Existing entities (e.g., The Harry Fox Agency or one of the performing rights societies) might also be able to play this role. Another, more established model is found in sections 111 and 119 of the Copyright Act and in the Audio Home Recording Act:[22] royalties are paid to the Copyright Office, which disburses them to eligible copyright owners. Distributions are made either when all eligible copyright owners agree on the division of royalties or, failing that, in a distribution proceeding conducted by the Copyright Royalty Judges. This is a function that the Copyright Office could easily perform.

b. *Extending Section 115 to Include Certain Performances*

While enacting a section 114-style license for the reproduction and distribution of phonorecords would resolve one of the two key issues – i.e., the desirability of giving licensees a single source from which to obtain such licenses for all musical works – it would do nothing to address the problems created by the competing claims of performing rights societies and The Harry Fox Agency (and/or music publishers) that online transmissions of music require separate licenses for the performance right and for the reproduction and distribution rights. As I have already suggested, although it is easy to see how this practice serves the purposes of the two groups of licensing

[22] 17 U.S.C. Ch. 10.

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agents, it is difficult to understand how it serves the legitimate interests of copyright owners.

To the extent that a particular form of digital transmission involves both the performance right and the reproduction and distribution rights, the copyright owner should be entitled to reap the actual value of both sets of rights. As I have already indicated, there will be occasions where one of the rights is technically implicated, but where there is no legitimate reason to require that compensation be paid for the exercise of that right. An online music service that engages in streaming under a license of the performance right should not be required to pay as well for the right to make the buffer and cache copies that are incidental to the performance that is being streamed. An online service that offers downloads under a license of the reproduction and distribution rights should not also be required to pay for what may also technically constitute a public performance even though the recipient of the download does not contemporaneously cause the downloaded work to be performed.

In those cases, the license of the predominant right should automatically be accompanied by, in effect, a royalty-free license of the incidental right. But even when both rights are legitimately involved and the licensee is simultaneously obtaining economic value from both the performance and reproduction of a musical work by means of the same transmission, there is no justification for requiring the licensee to obtain two separate licenses from two different middlemen acting on behalf of the same copyright owner. The licensee should be able to obtain a single license for all the necessary rights, and to pay the full value of the license in a single payment to a single

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entity, which will then see to it that the copyright owner receives the compensation to which he or she is due.

In the context of an expanded section 115 statutory license, it makes most sense to provide that for any digital transmission of music in which not only the reproduction and distribution rights, but also the performance right are involved, the section 115 statutory license will cover (and obtain appropriate compensation to the copyright owner for) all the necessary rights. It should be left to the collecting agent – whether that be an entity established by the copyright owners or whether it be the Copyright Office acting in accordance with rate-setting and distribution orders of the Copyright Royalty Judges – to see to it that the royalties reach the copyright owners to whom they are due.

Another approach – but a more difficult one to administer in light of constantly changing technology – would be to determine by statute (or by administrative regulation) for each kind of digital audio transmission whether the transmission should be considered a performance or a reproduction, but never to characterize any particular kind of transmission as requiring compensation for both types of rights. But in addition to the administrative difficulties in making such determinations and keeping them up to date, such a resolution would overlook the likelihood that there will be occasions when both types of rights are implicated and where the copyright owner deserves to be compensated for the exercise of both types of rights. For that reason, I believe it makes more sense to give the copyright owner the full value of the rights that are exercised, but to do so in a single payment that eliminates at least one of the

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middlemen. Again, the key concern should be with compensating the copyright owner, not with ensuring the continued viability of any particular intermediary's business plan.

2. *Repeal of the Section 115 Compulsory License*

a. *Collective Licensing*

Another option to consider is eliminating the section 115 compulsory license and perhaps replacing it with a collective licensing structure. When I met several weeks ago with the Chairman of the House Subcommittee to discuss the various proposals made by interested parties, I suggested that such an approach might be preferable. The Chairman requested that I explore this concept further by preparing initial model legislative language. He then requested that I testify as to the benefits of this concept, which I did on June 21.[23]

This collective licensing structure does have a certain amount of appeal because a fundamental principle of copyright law is that the author should have the exclusive right to exploit the market for his work, except where doing so would conflict with the public interest. The Copyright Office has long taken the position that statutory licenses should be enacted only in exceptional cases, when the marketplace is incapable of working. One could argue that it is difficult to say that the marketplace is incapable of working with respect to reproduction and distribution of nondramatic musical works when the marketplace has never been given a chance to succeed. The moment the copyright owner's right to control mechanical reproductions of a nondramatic musical

[23] For a copy of this legislative language, a section-by-section analysis and other exploratory information, please see my written statement as submitted to the House Subcommittee, available at http://www.copyright.gov/docs/regstat062105.html.

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work in the form of phonorecords was created, it was accompanied by the compulsory license.

Our compulsory license in the United States is also an anomaly. Virtually all other countries that at one time provided for this compulsory license have eliminated it in favor of private negotiations and collective licensing administration. Many countries permit these organizations to license both the public performance right and the reproduction and distribution rights for a musical composition, thereby creating "one-stop shopping" for music licensees and streamlined royalty processing for copyright owners.[24]

The United States also has collective licensing organizations, such as ASCAP, BMI and SESAC, which appear to function quite successfully. These performing rights organizations license the public performance of musical works – for which there is no statutory license – providing users with a means to obtain and pay for the necessary

[24] *See*, David Sinacore-Guinn, COLLECTIVE ADMINISTRATION OF COPYRIGHTS AND NEIGHBORING RIGHTS: INTERNATIONAL PRACTICES, PROCEDURES, AND ORGANIZATIONS § 17.9.3 (1993) (citing 45 countries which permit collective licensing organizations to license both rights, including Argentina, Brazil, Chile, France, Germany, Greece, Hong Kong, India, Israel, Italy, Japan, Mexico, South Korea and Spain). The European Union has recently recognized that there may be value in one-stop shopping in the form of EU-wide licensing of online music. *See,* Huw Jones, *EU Weighs Plan to Help Online Music Marketsource*, Reuters (June 30, 2005), *available at* http://today.reuters.co.uk/news/newsArticle.aspx?type=internetNews&storyID=005-6-30T04025Z 01_MOR038309_RTRIDST_0_OUKIN-MEDIA-EU-COPYRIGHT.XML, visited July 8, 2005.

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rights without difficulty. It seems reasonable to ask whether a similar model would work for licensing of the rights of reproduction and distribution.

The discussion draft that I presented to the House Subcommittee attempted to strike the appropriate balance between the rights of copyright owners and the needs of the users in a digital world. Its overarching purpose was to remove the barriers which inhibit the music industry's ability to clear rights in order to open the licensing structure to free market competition.

The discussion draft set forth rights and obligations for newly-defined music rights organizations ("MRO"). An MRO would be authorized, and required with respect to digital audio transmissions which the Copyright Office has been told present the greatest need for licensing reform, to license the reproduction and distribution rights of any nondramatic musical work for which it was also authorized to license the public performance right. In essence, this would mean that MROs would be authorized to license downloads and other reproductions (e.g., server, cache and buffer copies) made in the course of digital audio transmissions, even when there is no public performance involved or where the proportion of the public performance right implicated in relation to the reproduction or distribution rights is questionable. This should lead to "one-stop shopping" for any online music service seeking to license rights to a work.[25] This structure would create an efficient mechanism for copyright owners to license and for potential licensees to obtain all of the necessary rights to make nondramatic musical

[25] It would be "one-stop" shopping with respect to all of the necessary rights for all works in an MRO's repertoire. Of course, it would not be "one-stop" for a licensee wishing to obtain rights to all nondramatic musical works. That licensee would need to obtain a blanket license from each of the MROs. But that simply reflects the current state of affairs with respect to public performance rights, and

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works available to the listening public, particularly in the context of the Internet and other digital transmission media. It would also leave evolving business terms to the flexibility of marketplace negotiations. The discussion draft continued to recognize the rights of copyright owners, who would appropriately retain the right to license their works themselves whether or not they chose to engage an MRO. It also would provide incentives for effective notice of an MRO's repertory of works available for licensing.

Substituting the MRO structure for the section 115 compulsory license would address the two themes that I have already identified as central to the current crisis: the conflicting demands made by copyright owners' agents for the licensing of performance rights and by their agents for the licensing of reproduction and distribution rights, and the contrast between the ability of performing rights societies collectively to license performance rights for virtually all nondramatic musical works and the inability of any organization or combination of organizations to do the same with respect to reproduction and distribution rights.

The model legislation has generated a sizable response. The majority of the feedback has praised its goals, namely to increase efficiency and promote the free market, but many interested parties have expressed concern as to its actual implementation.

One concern that has been raised is the potential proliferation of an unmanageable number of MROs. Although I recognize that this would theoretically be possible, I do not believe that it would be likely. The current performing rights society

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that state of affairs appears to be satisfactory.

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market has been open to any number of entities for the better part of a century, yet only three actually exist. Similarly, only one major mechanical rights licensing entity exists even though nothing in the law prohibits more. I assume that the same market forces that prompted the formation of these existing collective organizations and inhibited more from arising – namely administrative efficiency, substantial start-up costs and the songwriters' and publishers' recognition that they have more bargaining power as a unified group – would likely discourage excessive fractionalization of the MRO marketplace. Meanwhile, even if a few more MROs were to exist than the current number of collective entities, I consider it unlikely that this would be an unmanageable number and it would still provide "one-stop shopping" for any user needing to clear all of the rights to a particular musical composition. Additional MROs might even provide a competitive environment in favor of the individual songwriter in choosing which intermediary would be best in administering the rights in her musical works. However, the responses from the performing rights societies and others have certainly raised a genuine prospect that there might be a multiplicity of MROs and that some or many music publishers might withdraw from the existing performing rights societies under the system described in the discussion draft. It would be prudent to investigate this further before deciding whether such a course of action would be desirable.

Another concern related to antitrust issues is whether the existing antitrust decrees governing ASCAP and BMI might be expanded to take into account the new functions of ASCAP and BMI as music rights organizations and/or to apply to other MROs. I have taken no position on whether the existing consent decrees *should* be extended, for example, to subject the royalty rates offered by an MRO for a

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reproduction and distribution license to review by a rate court. I recognize that antitrust concerns are integral to this or any other legislative concept, and have begun consulting with the Antitrust Division of the Department of Justice.

Regardless of whether formal consent decrees would apply to MROs, many parties have expressed a desire for the MROs' rate to be subject to some sort of oversight, be it by arbitration, a rate court, the Copyright Royalty Board or otherwise. I think this provision definitely warrants further consideration, although I note that greater Government-dictated oversight diminishes the ability of the free market to function. On the other hand, I recognize that the more market power that an MRO would have, the greater would be the justification for supervision by a rate court or other governmental entity. And it is my understanding that collective administration organizations abroad are usually subject to some form of government oversight.

I have also heard criticism expressing concern that the MRO proposal would create uncertainty. Obviously, it would be necessary to work with all interested parties to minimize the negative ramifications, while realizing that *any* change would necessarily have some negative consequences for some party or parties. For example, I have heard the argument that without the statutory license in place, more popular songwriters would receive greater payments than less popular ones. While this could well be true, it is also the very essence of the free market. The more desired an item is, the higher price it can command. I have also heard the argument that some licensing agents could lose market share if large copyright owners chose to license their works directly, an option which I point out happens to be currently available as well.

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The bottom line is that if the section 115 license were to be eliminated, some current music industry participants may have to adjust their business practices to maintain their current levels of profitability without the artificial rate ceiling afforded by the statutory license. Not meaning to minimize this practical reality, I wish to emphasize that the overriding goal of any licensing scheme should be to compensate copyright owners properly and provide an efficient and effective means by which licensees can obtain rights to make nondramatic musical works available to the listening public. Ancillary support organizations are important to the process, and in any new licensing regime they will necessarily continue to serve their roles, albeit perhaps with modifications induced by the increased competition present in a free market. As always, my focus is primarily on the author. The author should be fairly compensated for all non-privileged uses of his work. Intermediaries who assist the author in licensing the use of the work serve a useful function. But in determining public policy and legislative change, it is the author – and not the middlemen – whose interests should be protected.

I recognize that the licensing scheme in my discussion draft was a radical departure from the current structure. However, given the problems that seem to inevitably arise every few years with the section 115 compulsory license and the interested parties' apparent inability to reach consensus on the majority of issues regarding how best to further revise section 115 to meet the industry's needs, I believe that such an approach has considerable merit. In any event, at the very least this proposal and the feedback we have received will assist in reaching a clearer understanding of how best to modify the system that is already in place.

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I also recognize that the discussion draft did not address some of the issues raised in the proposals that music industry representatives recently submitted to the House Subcommittee. Some of those issues relate to ringtunes, promotional uses, multi-format discs, percentage royalty rates, lyric displays, licensing of music for audiovisual works, locked content and accounting logistics. I consider these to be business or economic issues which are best resolved in the free marketplace.[26] Eliminating the section 115 compulsory license creates this marketplace, and the case can be made that there is no need for Government to legislate what the parties can negotiate themselves.

b. *Simple Repeal of the Compulsory License*

Should the concept of free marketplace negotiations for reproduction and distribution rights for nondramatic musical works appear to be desirable, then a variation on this legislative concept might also be worthwhile to explore. One might ask whether it would further benefit the industry as a whole simply to repeal, yet not replace, the section 115 compulsory license. Then reproduction and distribution rights would truly be left to marketplace negotiations. A sunset period of several years would likely be prudent to permit the industry to develop a smooth transition. My prediction would be that music publishers would voluntarily coalesce into music rights organizations, or perhaps would create a single online clearinghouse (or a handful of such clearinghouses) which would permit one-stop shopping while nevertheless permitting each publisher to set its own rates. It might be wise to couple repeal of section 115 with incentives

[26] Some of them may also easily be addressed under existing law.

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designed to promote one of these alternatives that would result in one-stop shopping or something close to it.

In principle, I favor this approach. After all, the Constitution speaks of authors' "exclusive rights to their Writings," and in general authors should be free to determine whether, under what conditions and at what price they will license the use of their works. But for the past few years, the music industry has been in a state of crisis, as unauthorized mass infringement has become all too easy and, unfortunately, all too tempting to engage in. Consumers, used to being able to obtain any musical work they want at little or no cost, will demand no less from the legitimate marketplace. The Supreme Court's decision two weeks ago may offer some breathing room to the music industry, but that breathing room should not be squandered. Rather, it offers at best a limited opportunity to reform the system of music licensing in a way that will meet the demands of a public that knows how to get what it wants one way or another. A laissez-faire approach that gives each musical copyright owner the complete freedom to decide whether and how to license his or her works may be too risky in the current environment.

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3. *Other Issues*

Other questions and proposed remedies have been raised that address more technical or business-related issues, but these are matters more appropriately addressed once an overall approach has been selected. They include whether and under what terms to permit controlled composition clauses, whether percentage versus penny rates should apply, and notice and accounting procedures. Some interested parties' proposals have also raised tangential issues such as defining the term interactive in Section 114 or creating a public performance right for analog transmission of sound recordings. While such issues may well deserve attention, I understand that today's hearing is to evaluate the defects of section 115, not all topics relating to music licensing in general.

Conclusion

I commend you, Mr. Chairman, for convening this hearing to discuss the problems associated with the use of the section 115 license in a digital environment. I look forward to working with you, members of the Subcommittee, and the industries represented at this table to find effective and efficient solutions to make improvements in the licensing of musical works that will better enable consumers to enjoy the music that our songwriters and composers create and that will compensate our songwriters and composers in a way that continues to provide them with ample incentives to continue to create and make available the music that we all enjoy.

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Testimony
United States Senate Committee on the Judiciary
Music Licensing Reform
July 12, 2005

David Israelite / Irwin Z. Robinson
President & CEO , National Music Publishers' Association / Famous Music Publishing

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Testimony of
Irwin Z. Robinson
Chairman and Chief Executive Officer
Famous Music Publishing
Before the Senate Judiciary Committee
Subcommittee on Intellectual Property

July 12, 2005

Good afternoon, Chairman Hatch, Senator Leahy and Members of the Subcommittee. I am Irwin Robinson, Chairman and Chief Executive Officer of Famous Music Publishing. I thank you for allowing me to submit written testimony about music licensing reform.
I also serve as Chairman of the Board of the National Music Publishers' Association ("NMPA"), the principal trade association representing the interests of music publishers and their songwriter partners in the United States. For more than eighty years, NMPA has served as the leading voice of the American music publishing industry — from large publishing businesses to self-published songwriters — before Congress, the administration and in the courts. The approximately 600 music publisher members of NMPA, along with their subsidiaries and affiliates, own or administer the great majority of the musical compositions licensed for manufacture and distribution as phonorecords in the United States. It is important to distinguish the copyright in these musical compositions, which form the foundation of today's music industry, from the copyright in the sound recording of an artist's rendering of those compositions. Both ingredients — the "musical work" and the "sound recording" — are essential to make music available as the public knows it.

The Role of Music Publishers in the Music Industry
A music publisher is a company or, in many instances, an individual, that represents the interests of songwriters by promoting their songs and by licensing the use of their songs for reproduction and distribution in CD's, on the Internet, through public performances, and exercising the other rights available under the copyright law. The role of the music publisher is to represent the interests of the songwriter.
Music publishers play an integral role in both the business and creative side of the music industry. Music publishers are often involved at the very beginning of a writer's career. After signing songwriters to a publishing deal, publishers will do everything from helping writers find co-writers to securing artists to record writers' songs. Often when a songwriter retains a publisher, the publisher will advance desperately needed money to the songwriter to help him or her survive so that the writer can focus on what he or she does best – write music.
Primarily, music publishers administer copyrights, license songs to record companies, digital media companies, television companies, and any other users, and collect royalties on behalf of the songwriter. These administrative duties are made easier by the Harry Fox Agency ("HFA"). Founded in 1927, HFA, a wholly owned subsidiary of the NMPA, provides an information source, clearinghouse and monitoring service for licensing musical copyrights, and acts as licensing agent for more than 27,000 music publishers, which in turn represent the interests of more than 160,000 songwriters. Since its founding, HFA has provided efficient and convenient services for publishers,

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licensees, and a broad spectrum of music users. With its current level of publisher representation, HFA licenses the largest percentage of the mechanical and digital uses of music in the United States on CD's, digital services, records, tapes, and imported phonorecords.

Online Music Licensing Reform

I thank the Subcommittee for holding a hearing on online music licensing reform. Music publishers have taken great strides in helping digital media companies launch new services to compete with illegal file sharing companies, and we will continue to facilitate the legal sale of music in the digital world. NMPA has been in negotiations regarding the licensing by online subscription services of on demand streams and limited downloads in an effort to formulate solutions that will ensure the availability of all songs for licensing by subscription services and guarantee a level playing field for the determination of rates. Recently, the Copyright Office drafted a legislative proposal, which would abolish the mechanical compulsory license of Section 115 of the Copyright Act and create new Music Rights Organizations ("MROs") to license collectively performance and mechanical rights. As a music publisher, I am very concerned with the Copyright Office proposal and believe it is fatally flawed. Conversely, NMPA, the American Society of Composers, Authors, and Publishers ("ASCAP"), and Broadcast Music, Inc. ("BMI") have proposed a solution, which better respects property rights, protects creators, and addresses the needs of licensing reform for the digital age. Our proposal, called a "unilicense" would truly create one stop shopping where online subscription services could obtain a blanket license covering performing and mechanical rights through a Super Agency administered by NMPA and the Performing Rights Organizations ("PROs"). Songwriters and music publishers believe the unilicense proposal is a superior proposal that would appropriately balance the needs of the marketplace with the interests of copyright owners. The unilicense proposal also enjoys the support of Nashville Songwriters Association International ("NSAI") and the Songwriters Guild of America ("SGA").

Today the emergence of new technologies is set to change the music industry forever. Through my work in the music publishing industry for nearly 48 years, I have experienced first hand the evolution of the music industry into the digital world. Although illegal "peer-to-peer" services continue to dominate Internet delivery of music, the success of several lawful online music services has finally begun to fulfill the promise that the Internet offers as a legitimate marketplace for music. Additionally, I am hopeful that the Supreme Court ruling in the MGM v. Grokster decision will be the boost that legal online music services need to triumph over illegal music services.

Nearly four years ago, in order to combat the theft of music and ensure the lawful availability of musical works online, through NMPA/HFA, publishers, including my company Famous Music Publishing, made the historical decision to empower legitimate subscription services by entering into a "use now, pay later" licensing system. In the fall of 2001, NMPA and HFA entered into an agreement with the Recording Industry Association of America ("RIAA") to assist the launch of new subscription services by creating a framework for mechanical licensing of such services to offer limited, or tethered, downloads and on-demand streams despite the fact that agreement had yet to be reached as to the applicable royalty rates. In that agreement, the parties agreed to make licenses available immediately on a bulk basis with the understanding that licensees will pay royalties at a future date when rates are determined, either by agreement or arbitration. The parties further agreed to clarify the scope of rights licensed in order to avoid disputes — and potential litigation — in favor of jump-starting new businesses. All parties to the agreement stipulated that on-demand streams and limited downloads involve a mechanical right, and that pure "radio-style" streaming does not involve a mechanical right. In the wake of that historic agreement, HFA on behalf of publishers entered into similar agreements with independent subscription services on essentially the same terms. These agreements paved the way for the launch of a wide array of subscription services offering a broad repertoire of music to online subscribers.

Indeed, music publishers have every economic incentive to issue as many licenses to new, legitimate Internet music services as possible. It is only through such license agreements that music publishers

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and songwriters are compensated. For this reason, the songwriting and music publishing communities have consistently worked with new businesses to promote broad public access to their works on fair and reasonable terms. Time and again, when called upon to help jump-start new distribution channels for their music, songwriters and music publishers have risen to the challenge.

While the influx of new online music companies that want to offer immediately every song ever written has put an enormous strain on the music publishing industry in licensing mechanical rights, music owners have made a Herculean effort to satisfy that demand. As of today, HFA's publisher clients have issued almost 3 million licenses to at least 385 different licensees for digital delivery of musical works. These licenses represent the vast majority of musical works for which there is any meaningful level of consumer demand.

Despite the continued assistance music publishers have provided to online music distribution, I recognize the need to reform Section 115 of the Copyright Act. NMPA has been engaged in ongoing discussions with the Digital Media Association ("DiMA"), the RIAA, the Recording Artists' Coalition ("RAC"), National Association of Recording Merchandisers ("NARM"), NSAI, SGA, ASCAP, BMI, SESAC, Inc. and the U.S. Copyright Office for several months trying to find a solution that would ensure the availability of all songs for licensing by subscription services and guarantee a level playing field for the determination of rates.

On June 21, 2005, the Register of Copyrights presented a legislative proposal to the House Judiciary Subcommittee on Courts, the Internet, and Intellectual Property. As The Copyright Office proposal would repeal the current mechanical compulsory license provision of the Copyright Act (Section 115), and replace it with an entirely new structure. This proposal would mandate that current PROs become MROs, which would be required to license both performance and mechanical rights. The new MROs would offer blanket licenses to digital music services that combine both the public performing right and the mechanical rights needed for making the various kinds of digital audio transmissions of music to consumers.

As I stated before, I find the Copyright Office proposal severely flawed. First, I believe the Copyright Office proposal would impose more government control over the music industry and would not result in a free marketplace system. By mandating that PROs become MROs and tasking these new MROs with administering both performance and mechanical rights, the Copyright Office proposal may subject mechanical rights to the same rate courts under consent decrees, which govern some PROs. The Copyright Office proposal does not clearly address whether the rate courts that currently govern some performing rights organizations would apply to mechanical rates. More than likely, mechanical rate negotiations would be subjected to these same rate courts, resulting in more government control over negotiations rather than less. Merging mechanical and performance rights into one rate proceeding would also reduce the small amount of bargaining power that songwriters have. Record companies currently do not have a rate court imposed on them, so they are free to negotiate in a free market without government regulation. This proposal does nothing to level the playing field.

Second, the Copyright Office proposal would have severe economic ramifications and would be very harmful to the music publishers and songwriters. The Copyright Office proposal would put the Harry Fox Agency, the primary mechanical licensing agency, at a severe competitive disadvantage since it would take away a substantial section of its business, administering mechanical royalties in the digital world, and forcibly give it to PROs by statute. The most likely result of the Copyright Office proposal is that HFA will be left with only licensing mechanical rights in the physical world, threatening its viability all together. Additionally, the Copyright Office proposal would force PROs to build a mechanical rights licensing, collection and distribution infrastructure, which would involve a large capital cost and additional operational overhead, thereby reducing royalty payments to writers and publishers. There are many other complications, such as splits that can differ between performance and mechanical royalties. The proposal also devalues mechanical rights by combining them with performance rights, thereby reducing royalty payments to writers and publishers.

Third, the Copyright Office proposal would create more confusion than the current system. It was the

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Copyright Office's intent to create one (or three) stop shopping for the digital media companies who sell the property of songwriters and artists. However, it is entirely conceivable that several MROs could emerge and complicate things even more. The publishers, especially large multinational publishers, may decide it is more economical to create their own MROs and license directly.

I believe our unilicense proposal is a superior solution to the Copyright Office proposal. The unilicense would balance the needs of the marketplace with the interests of copyright owners. The goal sought by the Copyright Office -- to have one place to obtain the performance and mechanical rights needed for a single price – is achieved in the unilicense proposal. The unilicense would create a Super Agency, which would issue to digital subscription companies a blanket license covering both performing and mechanical rights in exchange for a percentage of the digital media company's revenue. Under the uniliense proposal, a designated mechanical agent and designated performance agents would administer royalties and distribute them to the appropriate writers/publishers. The unilicense proposal addresses the areas of most critical need raised by digital media providers – access. It maintains existing licensing structures, thus eliminating any additional administrative expenses, while reaping the benefits of many decades of licensing experience and expertise.

I am hopeful that the market place can address many of these concerns without government intervention, and there has been much progress in recent months. However if Congress chooses to make changes to the music licensing process, I believe any Congressional action should move toward a free market and respect property rights. In that vein, NMPA supports eliminating Section 115 of the Copyright Act and truly allowing the marketplace to govern the music industry. NMPA also supports eliminating the government's control over rates at which songwriters are compensated. If Congress acts, I respectfully request it act consistently with free market principles and deference to property rights.

Again, I appreciate the opportunity to submit testimony to the Subcommittee. I believe a level playing field is essential in order to ensure the availability of all songs for licensing by subscription services, and to guarantee that songwriters and music publishers obtain fair rates for their creative works.

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STATEMENT OF SESAC, INC.

HEARING BEFORE THE U.S. SENATE COMMITTEE ON THE JUDICIARY SUBCOMMITTEE ON INTELLECTUAL PROPERTY JULY 12, 2005

SESAC appreciates the opportunity to submit this statement in light of the oral and written testimony presented at the July 12, 2005 hearing on Music Licensing Reform.

SESAC is one of three domestic musical performing rights organizations. It was organized in 1930, and is the country's second oldest PRO. It literally started as a mom and pop operation, and was family owned for its first 62 years.

SESAC, like other PROs, represents songwriters and music publishers and grants licenses to music users authorizing the public performance of musical compositions, for which SESAC functions as a non-exclusive licensing agent. SESAC is relatively small compared to its two competitors, ASCAP and BMI, who together share approximately 95% of all performing rights revenues.

SESAC supports efforts to increase efficiencies in music licensing that will benefit legitimate music users, but not at the expense of music creators and copyright owners. In reviewing the various proposals that have been presented, SESAC cannot support legislation that either mandates that it change its business model to include additional functions such as increased mechanical licensing or imposes new regulations upon SESAC, especially those based upon Department of Justice orders that regulate the conduct of ASCAP and BMI (such as mandatory rate court proceedings, or so-called "automatic" licensing without the parties having first come to terms). SESAC cannot support the establishment of any superagency that would place SESAC at the mercy of its

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two giant competitors as would occur in the proposal put forth by its competitors, ASCAP, BMI, and the NMPA.

THE PERCEIVED "PROBLEM" WITH MUSIC LICENSING

As SESAC understands it, music users, particularly DiMA and the RIAA, have complained that the mechanical licensing system generally, and Section 115 specifically, are not working, particularly in the internet space, in terms of efficiency and protection from potential infringement liability.

To the extent that other interested parties want to open discussions concerning Section 112 ephemeral recordings or the Section 114 public performance right in sound recordings by digital audio transmission, SESAC does not presently take a position on those topics. However, to the extent that any legislative proposals implicate the public performance right in musical compositions and/or the operation of the PROs, SESAC has a strong interest in the outcome and is pleased to share its thoughts.

A FIRST POSSIBLE SOLUTION - REVISING SECTION 115 STATUTORY COMPULSORY LICENSE PROVISIONS ONLY

The recent discussions concerning possible revisions to the methods of music licensing – and the statutory provisions underlying them – have ranged from minimal corrections in the compulsory licensing of mechanical rights under Section 115, to a wholesale revamping of business models by the creation of new types of licensing entities. Upon reflection, after having participated in and attended numerous recent hearing and meetings on the topic, SESAC believes that the more prudent course would

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be a narrowly tailored response to specific problems perceived by music owners and music users.

The interested parties, including the music users, point to performing rights licensing through the PROs as the model of efficiency. In particular, by obtaining blanket licenses from the three PROs, a music user can obtain the right to publically perform virtually the entire U.S. popular repertory.

If the main problem in music licensing is difficulty in obtaining timely and complete mechanical rights through the Harry Fox Agency ("HFA"), the perceived problem can be solved without tampering with performing rights licensing. SESAC believes that the problem could be "fixed" by simply revising Section 115 to replace the compulsory license and statutory rate with a blanket license model, as successfully employed for performing rights by the PROs. This alternative would be an effective "surgical" alternative to the broad statutory revisions proposed to address the specific problem.

Although a compulsory blanket license along the lines of the Section 114 sound recording performance license arguably would be more efficient for music users because mechanical rights in virtually the entire U.S. repertory would be made statutorily available, SESAC in principle does not support compulsory licensing (especially if no "opt out" is permitted). Even without compulsory licensing, however, blanket licensing of mechanical rights would provide substantially more efficiency than the present system, but not at the expense of the music owners' rights to choose when and how to license their intellectual property. SESAC would expect that a new blanket licensing system for mechanical rights under Section 115, employing the efficiencies that are enjoyed in

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performing rights licensing, might encourage HFA and/or one or more other new entities to increase the percentage of collective representation of mechanical rights in the U.S. repertory.

SESAC believes that the second "problem" voiced by music users, the purported uncertainty concerning which rights are implicated in a given exploitation, and the perceived potential infringement liability in "guessing" incorrectly, is largely illusory. SESAC takes the position that all digital music transmissions implicate the public performance right, regardless of what other rights might be implicated. See U.S.C. § 101 (defining what it means to "perform" a work "publicly" and to "transmit" a performance); see also U.S.C. § 115(d) (defining "digital phonorecord delivery"). In any event, SESAC believes that the issue of the existence and valuation of rights in the context of a given digital transmission can be satisfactorily addressed in the context of marketplace negotiations between music users and music owners, as apparently is the case in numerous other countries, without the necessity for statutory revisions to address every possible scenario or, more problematically, statutorily permitting rights that are characterized as merely "ancillary" and noncompensable. The issue, however interesting, can find a practical resolution in the marketplace. Any suggestion of purported "double-dipping" in the licensing of musical rights for digital transmissions incorrectly assumes that music users are overpaying for musical rights in various contexts, suggesting a lack of confidence in the marketplace's ability to properly value the rights claimed to be implicated in a given method of exploitation. This certainly has not been SESAC's experience in negotiating license agreements with various digital music users.

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In this regard, SESAC respectfully disagrees with the Register of Copyrights' testimony that " it seems inefficient to require a licensee to seek out two separate licenses from two separate sources in order to compensate the same copyright owners for their right to engage in a single transmission of a single work." If music users are able to obtain blanket licenses for all necessary performing and mechanical rights from a small number of entities (presently three PROs and HFA), the additional incremental efficiencies perceived in creating new layers of administration through a "unilicense/superagency" or MROs are not readily apparent. In short, SESAC does not believe that the blanket licensing of mechanical rights under Section 115 necessarily must be accomplished by a single designated agent; blanket licensing itself sufficiently simplifies the licensing process, as with the blanket licensing of performing rights which is conducted by three PROs.

If music users could obtain blanket licenses for both performance rights and mechanical rights in the U.S. repertory through a handful of agencies (the three PROs and one or more mechanical licensing agencies such as HFA), the goal of efficiency and protection from potential liability (whether a given transmission implicated performance rights, mechanical rights, or both) could be narrowly and successfully addressed.

A SECOND POSSIBLE SOLUTION – A ONE-STOP "UNILICENSE"

If it is determined that broader reform is absolutely needed, SESAC is generally in favor of the concept of a one-stop unilicense, limited to internet music subscription services only, through which such internet subscription services could obtain all necessary performance and mechanical rights through one agency. Under SESAC's

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proposal, fees would be based upon a percentage of service revenues to be negotiated, or arbitrated in the Copyright Office, and the unilicense would be administered by the Copyright Office along the lines of cable (Section 111) and satellite (Section 119) compulsory licensing.

Alternatively, SESAC is not entirely opposed to the concept of a new superagency administering this unilicense, along the lines of Soundexchange. Significantly, however, SESAC cannot endorse the specific superagency/unilicense proposal put forward by ASCAP, BMI, and the National Music Publishers' Association (the "NMPA") because, conspicuously, their proposal would require SESAC to make its repertory available through such a superagency, while specifically excluding SESAC from having an equal say in its operation. Instead, under the exclusionary proposal of ASCAP and BMI, they alone would oversee performance rights (with HFA, a wholly-owned subsidiary of the NMPA, overseeing mechanical rights) in their superagency, effectively leaving SESAC at the mercy of its competitors. Such a proposal raises a host of difficult antitrust issues, including the exclusion of SESAC, which illustrate that this suggested solution is not as simple as it might appear at first glance but, rather, unnecessarily creates complications that SESAC's suggested solution does not.

If, as ASCAP and BMI suggest, the superagency would be merely a "lockbox" operation, they should have no objection to SESAC's equal participation in its administration. If, on the other hand, their proposed superagency will be making substantive decisions directly affecting SESAC's licensing operation and fee collections, SESAC should have the right to equal participation, at the least. In fact, given SESAC's marketplace efficiencies and innovations, as well as its private industry perspective which

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drives it to reduce overhead and streamline operations, perhaps a compelling argument can be made for SESAC to be the designated PRO representative in their proposed superagency. Should SESAC be excluded from equal representation and management of such a superagency, it should not be forced, through legislation or other methods, to include its repertory in a plan in which it had no input.

A THIRD POSSIBLE SOLUTION – MUSICAL RIGHTS ORGANIZATIONS

Although SESAC generally finds the Register of Copyrights' proposal interesting and worthy of discussion, it has substantial reservations. Most importantly, SESAC cannot support legislation that requires it to undertake a substantial business function (mechanical licensing) that it might choose to forgo. Although SESAC historically has engaged in a limited amount of mechanical licensing as an accommodation to some of its affiliates, SESAC has not decided at this time whether it wants to engage more extensively in that marketplace.

Procedures such as rate court proceedings are not free marketplace mechanisms. In any proposed legislative reworking of the musical rights licensing marketplace, including the Register's proposal concerning the establishment of Music Rights Organizations ("MROs"), SESAC strongly believes that such remedial or punitive measures, which are derived from the judicial orders to which ASCAP and BMI are subject, should not be foisted legislatively upon any other MROs whose marketplace conduct does not otherwise require them.

Moreover, SESAC cannot support the Register's proposal that MROs, including SESAC, be required to automatically issue licenses subject to subsequent

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agreement between the parties concerning the license fee, whether by third-party dispute resolution or otherwise. Like rate courts, such "automatic" licensing is based upon the provisions of the ASCAP and BMI judgments to remedy past anticompetitive conduct, and should not be imposed upon SESAC or any other new MRO. There has been no showing that a marketplace in which MROs would compete to issue music licenses would perform anticompetitively or inefficiently.

As pointed out by the other interested parties (both the music users and the music owners), the Register's proposed legislation appears likely to lead to a proliferation of MROs, creating less, not more, efficiency in the music licensing marketplace. Additionally, this proposal would require, on a massive and onerous scale, the renegotiation of existing contracts, including those between the present licensing agencies and their affiliates, as well as those among the present PROs and their foreign counterparts, with which they have reciprocal agreements.

In any event, in the case of so-called "split copyrights" (split copyrights are common in the music industry and occur when co-writers are represented by different performing rights organizations; each writer having given his authorization to his respective performing rights organization to license his share of the public performance of the work), true "one stop" licensing for a given musical work simply would not be possible under this proposal because more than one MRO would be licensing the right to use that work.

CONCLUSION

SESAC believes that, in light of the various proposals that have been presented and discussed in detail, the conversation should return to a relatively modest

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but effective suggestion: revision of Section 115 to provide for blanket licensing of mechanicals rights without revising performing rights licensing. The interested parties acknowledge that performing rights licensing isn't "broken;" therefore, it does not need to be "fixed."

Any legislative reworking of the music licensing system that implicates public performance rights and/or the PROs - through the creation of MROs, a unilicense, a superagency, or otherwise - should recognize SESAC's unique and beneficial role in the marketplace; SESAC cannot support any proposal that it determines would lead (in the course of correcting problems in licensing other rights) to the imposition of punitive, remedial, or exclusionary restraints upon it or force SESAC to expand its minor mechanical music licensing operation.

That being said, SESAC stands ready to work with all interested parties in exploring any legislative initiative to improve the efficiency and effectiveness of music licensing, so long as the interests of fairness to all parties are preserved.

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