Before the

UNITED STATES COPYRIGHT OFFICE

Library of Congress
Washington, D.C.

In The Matter of		**Docket No. 2000-9**
Digital Performance Right	:	**CARP DTRA 1&2**
in Sound Recordings and	:	
Ephemeral Recordings		

Rebuttal Testimony of ADAM B. JAFFE

I. INTRODUCTION AND OVERVIEW

I have been asked to review the arguments put forward by RIAA and its witnesses in its direct case, and to respond to a number of issues that were raised by the Panel or in cross-examination during my own direct testimony. I have structured this rebuttal testimony as follows. I begin in Section II by restating the conceptual economic argument as to why the market value of performance rights for sound recordings is likely to be no greater than the market value of performance rights for musical works, and addressing certain issues relative to this analysis that arose during the direct case. I then proceed in Section III to analyze a large new dataset that I have obtained that shows exactly how much is paid for musical work and sound recording rights when they are licensed at the same time, for the same use, in actual competitive markets.

In Section IV, I restate and update the fee model that I have introduced, and discuss certain sensitivity issues that arose during the direct case. After the discussion of my fee model, Section V examines the overall evidence in the proceeding on the relative magnitudes of promotional value and displacement from internet streaming of sound recordings. Section VI examines the evidence as to the reasonableness of the agreements put forward by RIAA as benchmarks. Section VII discusses the testimony of Dr. Nagle, and Section VIII considers the relevance of the information in the business projections produced by webcasters. Section IX addresses the economic consequences of the fee proposal put forward by RIAA. Section X concludes with consideration of a few issues related to the licensing of ephemeral copies.

The main conclusions of this rebuttal testimony are:

- Economic analysis of the incentives underlying the willing buyer/willing seller negotiation tells us that the value of the sound recording performance right is unlikely to be greater than that of the musical work performance right.
- Analysis of data relating to the use of previously existing sound recordings and musical works in movies and TV programs, based on over 700 songs and over $20 million in royalty payments, demonstrates conclusively that competitive markets value sound recordings no more highly than musical works.
- I restate my fee model to facilitate direct comparison to the RIAA fee proposal. Updated data do not change the conclusion that the over-the-air musical work fee per performance is $.00020. Conservatively adjusting this fee for the promotional value differential between sound recordings and musical works

produces a fee per performance for webcasters of $.00014. Multiplying this per-performance fee by 15 songs per hour for webcasting yields a webcaster fee per listener hour of $.0021.

- For simulcasts/rebroadcasts, the likely influence on willing buyer/willing seller negotiations of the zero royalty rate for the same programs over-the-air, combined with the lower likelihood of displacement, suggests a lower rate. I had previously concluded that the range of reasonable rates was from 40% to 70% of the over-the-air musical works rate. I propose that the Panel use the lower end of this range (40% of over-the-air) for simulcasts/rebroadcasts, producing a per-performance fee of $.00008. Multiplying by the average of 12 songs per hour on over-the-air music station yields a fee per listener hour of $.0010.

- Examination of licenses for performance of musical works on the internet confirms the validity of my reliance on over-the-air performance royalties. Although less information is available, what information there is indicates that musical work rates on the internet may be slightly higher than, or much lower than, musical work rates for over-the-air radio.

- There is good evidence of significant promotional value for sound recordings on over-the-air radio, and this value is greater for sound recordings than for musical works. The available data indicate that promotional value also exists on the internet, and is larger than the effect of displacement of CD sales by internet performances. RIAA's evidence on displacement consists entirely of fears about the future and unsystematic, unquantifiable anecdotes.

- The evidence indicates that the 26 agreements put forward as benchmarks by RIAA do not reflect willing buyer/willing seller valuations, but rather the market power of RIAA in the presence of incomplete information, licensees' concerns about time pressure and uncertainty, bundling of the statutory rights with other valuable considerations, and willingness to pay above-reasonable rates to avoid large legal fees associated with securing uncertain rates through the CARP.

- Most of the 26 licenses are of trivial economic significance, and these licensees are not comparable to those seeking the statutory license in this proceeding.

- Even putting aside issues of reasonableness and comparability, the RIAA benchmarks do not support their fee proposal. The proffered benchmarks show no significant economic activity corresponding to 15% of revenue. The vast majority of royalties collected on a per-performance basis are based on a royalty rate one-eighth as great as that proposed by RIAA in this proceeding.
- The superficial flexibility offered by the RIAA fee model is illusory. Their per-performance model is 20 to 100 times as expensive as their percent-of-revenue model.
- A recent report by the Copyright Office confirms the validity of my analysis of the relationship between fees for ephemeral copies and fees for performances.

11. EQUIVALENCE OF MUSICAL WORK AND SOUND RECORDING DIGITAL PERFORMANCE RIGHT MARKET VALUES

A. Implications of the willing buyer/willing seller test

To understand whether the willing buyer/ willing seller outcome for sound recordings would be the same as that for musical works, we must analyze how both buyers and sellers would approach a negotiation over blanket licenses for non-subscription digital performance rights. In both cases, we can analyze how the "willing buyer" (potential licensee) and the "willing seller" (potential licensor) would approach these negotiations. If both the buyers and the sellers would be approaching these negotiations from economic positions that are similar with respect to musical works and sound recordings, then there is no economic basis for concluding that the market values for the two rights would differ.

1. The buyer side of the negotiation

The value that buyers put on the right of public performance of both musical works and sound recordings is derived from the value that they expect to realize by making public performances of music. In order for the buyers' valuations of the two rights to differ, it would have to be the case that there is some distinction in the manner or extent to which each right facilitates such performances. But no such differences exist. Buyers need both the sound recording and the musical work performance rights in order to make public performances. This means that each right is worthless to the buyers unless they also procure the other right. Conversely, once both sets of rights are procured, they each contribute symmetrically to the generation of the value through public performance. Because of this symmetry and mutual necessity, the buyers' "willingness to pay" for each right will be derived in the same way from the value that the buyers expect to derive from making performances. Hence, there is no difference in the buyers' "willingness to pay" for the musical work performance right and the sound recording performance right. Going into negotiations over either right, the buyers will be in the same position.

Note that it is important for this analysis that we are analyzing, in each case, blanket licenses for substantial portions of the repertoire.[1]

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[1] As discussed in my direct testimony, the appropriate economic interpretation of the willing buyer/willing seller test is that of a hypothetical competitive market. We can think of this market as being one in which competing non-exclusive licensors each

For some *specific* sound recording or musical work the user may value one more than the other. If licensing were done on a performance-by-performance basis, and I want to broadcast Frank Sinatra singing "As Time Goes By," it could be that what I really want is a Sinatra performance, or it could be that what I really want is that particular song. Depending on my preference, if the owner of Hoagie Carmichael's copyrights refused to give me the musical work performance right, I may well decide to play some other Sinatra sound recording. On the other hand, if the owner of the sound recording right refused, I might use some other recording of the song. *So* for this particular sound recording/musical work combination, I might value the musical work more, or I might value the sound recording more.

At the ***blanket-license*** level, however, I do not have the choice to substitute a different sound recording or a different musical work. Whatever I broadcast, it must contain both a musical work and a sound recording.[2] As long as I am negotiating for blanket rights to each, they are both essential and I would value them equally.

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offer essentially the entire repertoire, or, alternatively, one in which competing licensors each offer blanket licenses for substantial portions of the repertoire.

2 This statement is not strictly true, because there are some musical works and some sound recordings for which permission is not needed. On the musical work side, I could try to find Sinatra singing a song that has fallen into the public domain. Conversely, Sinatra's pre-1972 sound recordings do not carry the right to control public performances. But as long as many of the performances that I wish to make require both rights, I will need a blanket license covering both musical works and sound recordings.

2. The seller side of the negotiation

The sellers of each right are not the same, but each comes to the hypothetical table from a similar position. In each case, the costs of producing the underlying intellectual property are sunk. Further, in each case, these costs (including compensation for the risks incurred) are covered by revenues earned in other markets. In the case of sound recording rights holders, these costs are covered by CD sales.3 In the case of musical work rights holders, the costs are covered by the combination of mechanical royalties and over-the-air performance royalties. The digital performance royalty is incremental to this substantial revenue base in both cases. Finally, and most important, there is no incremental cost imposed on either the musical work or sound recording licensor by virtue of making the underlying intellectual property available for digital performance.[4],[5] In such a situation,

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3 Altschul, Transcript at 872-873; Katz, Transcript at 1051.

4 There is evidence, discussed further below, that allowing digital performances actually *increases* the licensor's revenue in other markets, via promotional value. This would imply that the incremental cost is actually negative, and the licensor's minimally acceptable outcome would be a negative royalty, i.e., a payment from the licensor to the licensee. Alternatively, if it were believed that digital performances displace sales of CDs, this could be thought of as an incremental cost of the digital performance license, which would result in a minimum acceptable royalty greater than zero. As explained further below, the possibilities of promotion and displacement may lead to adjustments that have to be made to the otherwise equivalent values of sound recordings and musical works. Thus the argument in this section should be understood as establishing equivalence in the value of musical works and sound recordings before any consideration is given to either promotion or displacement.

5 Altschul discussed Warner Bros. Record's expenses at length in both his written and his oral direct testimony. None of the costs he mentions, however, pertain to webcasting. (Altschul, Transcript at 805-821, and Direct Written Testimony of David Altschul at 14-21). Additionally, Katz and Himelfarb were both unable to identify

economics tells us that both the sound recording and musical work rights holders would approach this hypothetical negotiation for the performance right in the same way: they would recognize that there is no incremental cost to supply this market, and would simply hold out for as much of the user's overall performance value as they can get.[6]

Note that this analysis does not in any way suggest that the zero-incremental-cost of the right being transferred would lead to a zero royalty. Quite the contrary, intellectual property with zero incremental cost is routinely licensed at positive royalty rates. With respect to both musical works and sound recordings, we have a buyer (potential licensee) with some maximum willingness to pay which is derived from the value to the buyer of the performances, and we have a seller with a minimum willingness to accept equal to the zero incremental cost. The economics of bargaining, as well as common sense, suggests that the parties will reach agreement at some point in between. Economics cannot really tell us *where* in the interval between the buyer's maximum royalty and the seller's minimum royalty the parties will come out. It will depend on the stubbornness, negotiating skills, and perhaps bladder

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additional costs specifically associated with webcasting under the statutory license. (Katz,Transcript at 1045-1046; Himelfarb, Transcript at 2868).

6 It is possible that at some future date it will cease to be the case that the cost of making sound recordings is covered by CD sales, and that digital performance royalties are no longer incremental. But there is no evidence in this proceeding that anyone anticipates such a dramatic transformation of the marketplace during the time period at issue here. (Katz, Transcript at 1034-1035, 1104). Griffin actually states that there is a possibility of an increase in sales in the short run for less well known artists. (Griffin,Transcript at 1588-1589).

control of the parties. These factors combine with the going-in valuations of the parties to determine the outcome. And because these going-in valuations on both the buyer's and seller's sides are the same with respect to musical works and sound recordings, there is no reason to expect that the outcomes would be higher for one or the other.

Because the minimum acceptable royalty for the licensors of both the musical work and the sound recording is zero, and the likely result of bargaining is an agreement somewhere between this zero valuation and the buyer's valuation driven by the value of performances, the outcome of the hypothetical negotiation depends, in effect, only on (1)the value to the buyer of the right to perform publicly, and (2)the fraction of that value that ends up, through negotiation, passing to the musical work and sound recording licensors. Again, unless there is some systematic difference between the negotiation skills of the respective licensors, there is no reason to believe that one or the other of these will constitute a larger share of the overall performance right.

The notion that parties that jointly create value will split that value equally is also confirmed by the very statute under which this proceeding occurs. The joint interest of the record label and the recording artist in the sound recording itself is analogous to the joint contribution of the sound recording and the musical work to a public performance. Further, there is no evidence that the magnitude of their original contributions to the underlying CD are the same. Yet Congress deemed that the labels and artists should split the sound recording digital performance royalty equally, i.e., that the value of the artist's contribution should be deemed equal to the value of the record label's contribution, just as I have suggested that the value of the sound recording and the musical work are similar.

B. Other issues pertaining to the relationship between sound recording and musical work valuations

1. Dr. Nagle's approach to valuation confirms the equivalence of sound recording and musical work

The view that the value of the sound recording performance right is driven *entirely* by the value to the buyer of making performances provides the foundation for the analysis undertaken by Dr. Nagle. As explained further below, I believe that Dr. Nagle's analysis is not informative as to the value of the sound recording performance right under the willing buyer/willing seller test. But I find it interesting, nonetheless, that in attempting to determine the value of the sound recording performance right, Dr. Nagle adopted a framework that is predicated on the assumption that the licensor of sound recording performance rights would approach this licensing on the basis of zero incremental cost, so that the value of the right is driven entirely by the valuation of the potential licensee.7 That is, Dr. Nagle's analysis made no reference to, and drew no inferences from, the costs or risks incurred by

[7] See Nagle, Transcript at 2561.

the record labels in creating sound recordings. He looked only at what the right of public performance might be worth to the licensees.

There is nothing about this analysis that would be in any way different if the question were the value of the musical work performance right.[8] Thus, if Dr. Nagle's analysis is at all relevant to the question of valuing the sound recording performing right, it follows as a matter of simple logic that (1)the costs and risks incurred by the producers of sound recordings are irrelevant to the valuation (since they did not enter in any way into Dr. Nagle's analysis), and (2)the market valuations of sound recordings and musical works are likely to be similar (since Dr. Nagle's analysis would apply just as well to musical works as it does to sound recordings).

2. The irrelevance of the "relevant market" test

Professor Wildman's observation that sound recordings and musical works compete in different markets is true, but does not undercut this analysis.[9] Indeed, in the sense used by Wildman (markets defined for the purpose of antitrust analysis), there are *four* distinct markets that have been discussed in relation to the value of sound recordings and musical works. These are: (1)the market for sound

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[8] Nagle, Transcript at 2659-2661. As explained above, the available alternatives for the two licenses are no different – both licenses are necessary.

[9] Direct Written Testimony of Steven S. Wildman at 10-11; Wildman, Transcript at 3336-3337. Although Wildman states that musical works and sound recordings "trade in different markets," he recognizes that "You can't produce a sound recording by taking more work and less performance or less recording or vice versa. They both have to be there."

recordings embodied in CDs; (2)the market for the musical work mechanical rights necessary to reproduce and sell the CDs; *(3)*the market for the right of public performance of sound recordings by digital means; and (4)the right of public performance of musical works by digital means. It is certainly true that *(3)*and (4)are distinct markets, in the sense that the right of public performance of the sound recording is not a substitute for the right of public performance of the musical work, or vice versa. Indeed, as I have emphasized, you need both. At the same time, (1)and *(3)*are also not the same market. Having the CD, or even the right to copy the CD, is not a substitute for the right of public performance, or vice versa. They are distinct markets, and must be analyzed as such.

Similarly, my conclusion above that the sellers of musical works and sound recordings come to the hypothetical negotiations with the same economic position does not depend on their being in the same market. They are not, but I have analyzed the conditions underlying each of these two distinct markets and shown that these conditions are the same.

3. Relative valuation of sound recordings and musical works in other countries

In my direct testimony, I noted that the value of sound recording performing rights, in those countries that recognize such rights, is generally no greater than the value of musical work performing rights in those same countries. The Rebuttal Testimony of Professor William Fisher further analyzes the treatment of sound recording and musical work performing rights in other countries, in order to determine whether the relationship between the valuations of the sound recordings and musical works might be due to different legal regimes governing the valuation of the two different rights. His analysis confirms the general conclusion that, in those countries where the legal regimes covering the two rights are equivalent, sound recording performances are generally valued at or below the level of the musical work performances.

4. Artist versus composer

There has been some discussion in this proceeding of how potential listeners typically search for the music they want to hear and how the services identify the music the user is listening to.[10] While it appears that search engines typically do not provide the ability to search for particular composers (and the composer is typically not identified along with the rest of the information provided to the user while listening), this does not in any way imply that listeners do not value the musical work.[11] The typical service *does* identify and allow one to search for a particular *song* by name.[12] The song embodies the musical work,

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[10] McIntyre, Transcript at 5032-5034; Roy, Transcript at 7297-7298; Moore, Transcript at 7488; Juris, Transcript at 7098-7099.

[11] The rebuttal testimony of Michael Fine supports the conclusion that music consumers value musical works at least as much as they value the artists who perform them.

[12] Wise, Transcript at 4182-4183; Pakman, Transcript at 4376; Juris, Transcript at 7098-7099.

and is in fact what is covered by the musical work copyright. The fact that people do not typically search by composer is no more relevant than the fact that they do not typically search by record label. The song is the musical work, just as the artist represents the sound recording. Hence the prevalence of both the ability to search by song title, and the ability to search by artist name, in fact reflects the underlying symmetry of contribution of the sound recording and the musical work.

C. What can we learn about the relative value of sound recordings and musical works from the markets for CDs and mechanical royalties?

RIAA argues that making CDs is a costly and risky business, and that their costs and risks are greater than those incurred by composers and publishers.[13] As explained above, this proposition, even if true, is irrelevant to the hypothetical negotiation in a different market over the digital performance rights, because: the costs and risks in that different market are all sunk; they are incurred with the expectation of being recovered in the CD market; and, in any event, there is no incremental cost to the sound recording rights holders associated with making the sound recordings available for digital performance.[14] For this reason, even if it were true that it costs more or is riskier to make sound

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[13] Direct Written Testimony of Charles Ciongoli at 2; Ciongoli, Transcript at 1150-1156; Katz, Transcript at 998-1001; Direct Written Testimony of Steven S. Wildman at 12-13; Wildman, Transcript at 3363-3368.

[14] Altschul, Transcript at 805-821, and Direct Written Testimony of David Altschul at 14-21; Katz, Transcript at 1046; Himelfarb, Transcript at 2868.

recordings than to make musical works, it would not change the proposition, recognized by Nagle, that these costs and risks do not affect the market price for the digital sound recording performance right.[15]

But even if the costs and risks in the CD market were somehow relevant, the evidence in this proceeding does not support the proposition that the costs and risks are greater on the sound recording side.

As for risk, the conceptually appropriate question is not whether any given album is a risky proposition, but rather whether the overall business of making albums is risky. Record companies have a portfolio of artists and albums, and their cash flow and profits depend on the sales from that portfolio. The fact that most albums do not make money is no more informative than the fact that most songs written by composers do not make significant money. RIAA has presented no evidence that the profits of recording labels are any more volatile or uncertain than those of music publishers.[16]

With respect to the magnitude of the investments made, RIAA has not made a case that the investment in creating sound recordings

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[15] Nagle, Transcript at 2672-2673.

[16] [[In fact, Altschul testified to the fact that in general, Warner Bros. Records is profitable and that the three years presented in his direct written testimony and in RIAA Exhibit No. 002 DR are unrepresentative, and that Warner Bros. Records realized profits of approximately $20 million in 2000. (Altschul, Transcript at 829, 843-844). Additionally, Altschul stated that even in the years presented in his exhibit when Warner Bros. Records was unprofitable, Warner Music Group was profitable. (Altschul, Transcript at 829-830).]]

exceeds the investment in creating musical works. The main input into the creation of musical works is the composers' time, which is very difficult to value for a given composer, and even more difficult to aggregate across the body of composers. The particular cost figures put forward by RIAA may seem substantial, but they do not establish an investment greater than that necessary to create musical works.[17]

There has also been evidence in the proceeding regarding the average profits earned by a record company on the sale of CDs, relative to the mechanical royalties earned by composers and publishers on CDs.[18] This comparison is somewhat difficult to interpret, because the mechanical royalty is limited by statute. But even in the absence of this statutory constraint, the larger compensation for record companies relative to composers and publishers from the sale of CDs does not demonstrate that their costs are greater, or that the value of the sound recording exceeds that of the musical work.

As discussed in my direct testimony, composers and publishers earn substantial royalties – approximately $340 million per year – from

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[17] RIAA purports to establish that record labels' investments exceed those of music publishers. (Direct Written Testimony of Charles Ciongoli at 2; Ciongoli, Transcript at 1150-1156; Katz, Transcript at 998-1001; Wildman, Transcript at 3363-3368; Direct Written Testimony of Steven S. Wildman at 12-13). But publishers represent only part of the investment that creates musical works. There is no evidence in the proceeding regarding the value of composers' contributions to the creation of musical works, and the royalty-sharing rules between composers and publishers do not demonstrate their relative contributions any more than the 50/50 split of royalties decreed by Congress between record labels and artists represents their relative value contributions to the creation of sound recordings.

[18] Katz, Transcript at 1059.

over-the-air performances.[19] The royalties from over-the-air blanket licenses are distributed to individual composers and publishers in proportion to the frequency with which their musical works are, in fact, played on the radio. And a song is not played on the radio to any significant extent until it appears on a CD. This means that when a composer agrees to have her song on a CD, she generates the possibility of a significant future royalty stream. Conversely, a publisher who holds out for a high mechanical royalty on a particular CD risks not being on the CD, and hence losing a significant future revenue stream.[20] In effect, because incorporation into the CD is a necessary condition for access to the large pool of over-the-air royalties, owners of musical work mechanical rights are likely to agree to transfer those rights at rates well below their underlying value. For this reason, the overall average relationship between record company profits and mechanical royalties cannot be used to infer the relative magnitude of investment in each, or the relative value of musical works and sound recordings.

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19 Direct Written Testimony of Adam Jaffe at 45-46.

20 Katz, Transcript at 1005: "A music publisher's main source of income derives from a recording by an artist. Once that recording is done, they can get income from different streams and performance or reproduction. But if you are a music publisher, you have got to get your song recorded, otherwise it doesn't actually have much worth."

111. MARKET EVIDENCE ON THE RELATIVE VALUE OF MUSICAL WORK AND SOUND RECORDING RIGHTS

The previous section summarized the strong conceptual argument why the competitive market value of sound recordings should be comparable to that of musical works in incremental licensing markets. In this section I show that this prediction is overwhelmingly verified by empirical data on the competitive market prices at which license rights covering sound recordings and musical works are purchased.

A. The competitive market for the rights to reproduce sound recordings and musical works in movies and television

The U.S. does not generally recognize a right of public performance in sound recordings, so it is not possible to make a direct comparison of musical work and sound recording performance royalties in a competitive market. There are, however, circumstances in which the market does value rights related to sound recordings and musical works, where the right at issue is not a performance right, but is an incremental right in the sense discussed above. In particular, when a pre-existing sound recording is incorporated into a motion picture or television program, the producer must secure the right to reproduce both the sound recording itself and the underlying musical work for this purpose.

The economic incentives underlying the determination of these royalties correspond to those described above, namely that the buyer needs both the musical work and sound recording rights, and the licensors of both the sound recording and musical work rights face zero incremental cost in conveying the right in question. Further, the markets in which these rights are purchased are competitive, because payments for each song are negotiated separately, and producers have access to multiple sound recordings and multiple musical works. Therefore, these markets provide a strong empirical test of my conclusion that the valuation of sound recording and musical work performance rights should be similar.

The right that is necessary in order to use an existing sound recording in a motion picture or television episode is generally called a "master use right," while in the case of the musical work, this right is referred to as the synchronization, or "synch" right (because the audio musical work is "synchronized" with the video). Economic analysis of the incentives underlying the bargaining for the acquisition of these rights is exactly the same as the analysis above regarding performance rights, except that the negotiation occurs on a song-by-song basis rather than a blanket basis. The movie producer will have some maximum willingness to pay to use the song; she needs permission from both the sound recording copyright holder and the musical work copyright holder. Each of the two copyright owners, meanwhile, faces no incremental cost in allowing the sound recording or musical work to be incorporated into the movie.[21]

In the case of any specific song, the producer may care about getting a particular performer, or may care about getting a particular song, so that for any single song the payment for the sound recording may be greater than that for the musical work, or vice versa. On average, however, if my analysis of the underlying economics applies, the two should be approximately equal.[22]

There are not, to my knowledge, any public data sources that report fees paid by movie and television producers for master use and synch rights. I have been able to obtain, from three of the five largest major Hollywood studios, data on the fees paid for these rights in a substantial number of recent productions of these studios. These data

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[21] When the movie is shown in theaters, a public performance also occurs. There is no right to control the public performance of the sound recording. With respect to the musical work, there is a right to control public performance, but the ASCAP and BMI consent decrees (following antitrust litigation in the 1940s) prohibit the performing rights organizations from charging a separate fee for the right to perform the musical work in United States movie theaters. Consequently, a synch license for a theatrical movie typically also conveys a right to perform the song in U.S. movie theaters. From an economic perspective, the synch right and the master use right are equivalent in terms of the economic activity they allow to occur: they are both necessary and sufficient in order to make the movie and show the movie in theaters.

[22] With respect to both the synch right and the master use right, there are issues of values derived from other markets that could conceivably affect the royalties. In the case of the sound recording, incorporation in a hit movie could stimulate CD sales. In the case of the musical work, successful movies may eventually be shown on television, which would generate additional performance royalties. In both cases, these additional revenues would be highly uncertain, because few movies are successful enough to generate significant impacts of this sort, and in terms of the comparisons above these two effects offset each other. On balance, there is no reason to believe that these potential effects would have a major impact on the conclusion that the sound recording and musical work rights have similar values.

were derived from the accounting records of the companies. In order to ensure that reported fees represent competitive market conditions, I have excluded transactions that were not "arm's length," where other services or rights were bundled with those of interest, or where the sound recording and musical works right were owned by the same party, and songs that were written or rerecorded for the production in question.[23]

Figure 1 displays the results for motion pictures from the three studios. For competitive/confidentiality reasons and concerns of the studios, the three studios are referred to as Studio A, Studio B, and Studio C. After the exclusions described above, I have data for 423 songs in 30 different movies, representing licenses issued by of publishers and of record labels, and comprising total payments for these rights of about million. As expected, for any given song, or even for any given movie, there is some variation, with the royalties for the sound recording right sometimes being greater and the royalty for the musical work right sometimes being greater. For example, the "master" of Stevie Ray Vaughn's performance of Texas Flood was licensed at while the synch right was licensed for On the other hand, the publisher of the song Anticipation received a synch license fee of , while the master recording (by Gefkens)

[23] Inclusion of these transactions in the analysis would not change the conclusion that the sound recording is valued, on average, at slightly less than the musical work.

was licensed at The data nonetheless reflect that the synch and master use fees, in the vast majority of instances, are *identical.*

Interestingly, in some cases the holder of the musical work copyright agrees to a fee, but insists on a "most favored nation" ("MFN") provision that ensures that, if the studio agrees to pay more for the corresponding master use right, the synch right payment will be increased to make them equal. Conversely, sometimes the sound recording copyright owner insists on MFN treatment vis-a-vis the corresponding synch right. Such insistence on parity, in both directions, obviously suggests that copyright holders believe that the two rights should be valued equally.

Indeed, equality is what the data show. On average, the payments for the sound recording are slightly less than those for the musical work, with the sound recording payments equal to of the musical work payments for Studio A, for Studio B, and for Studio C. But the overall tendency towards approximate equality is unmistakable.[24]

Figure 2 displays the data for television. I have data for 7 television series/films produced by Studio A and Studio B during a recent production season.[25] The episodes in these series contained 288

[24] Although the phenomenon of MFN clauses in one direction or the other is not uncommon, it is not necessary to the result. The same finding of approximate equality holds if the songs with MFN clauses in either direction are excluded.

[25] The situation with respect to performance rights for television shows is slightly different than for movies. Again, the sound recording does not carry a right to

songs (after excluding those with possibly non-competitive market rates, as explained above) for which a little over in royalties was 2 paid. Again, the conclusion is crystal clear: the sound recording is worth, if anything, slightly less than the musical work.

These data confirm the validity of my conceptual analysis of the economic incentives underlying bargaining for sound recording and musical work rights licensing with a lack of ambiguity that is rare in economics. There is simply no room for debate. Whatever one may believe about the relative cost or profitability of making CDs or writing songs, when the sound recordings embodied in those CDs are licensed for later use, the evidence is overwhelming that the value of the sound recording right is no greater than the value of the musical work right.

B. Summary of discussion of fundamental symmetry of sound recording and musical work performance right valuations

If the concept of value to be applied is the willing buyer/willing seller test, the evidence is overwhelming that the overall value (i.e., before any consideration of the impact of either promotional value or

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control public performances, while the musical work does. In this case, the performing rights collectives do collect the royalties for public performances, in a manner analogous to the royalties for over-the-air radio performances that I have discussed previously. The fact that the incorporation of a song into a TV show creates an opportunity for a musical work performance royalty, but no opportunity for a sound recording performance royalty, might lead one to expect that the competitive price for the "synch right would be reduced. There is, however, no evidence of such a tendency in these data. The performance royalties for musical works depend on the number of performances, Since these musical works are single songs used in a single episode of a TV program, the number of performances may not be large. Of course, the possibility of such additional payments for the musical work (but not the sound recording) only strengthens the conclusion that the overall value of the sound recording is no greater than that of the musical work.

displacement of CD sales) of digital sound recording performance rights

is no greater than the value of musical work performance rights:

- Economic analysis of the willing buyer/ willing seller negotiation tells us:

  (1)that the licensor's costs would be irrelevant, and that the outcome would be a royalty equal to some fraction of the buyer's valuation;

  (2)that the buyer's valuations of the sound recording and musical work performance rights would be identical;

  *(3)*that there is no economic or legal reason why the *fraction* of that value conveyed in the royalty to the licensor would differ as between sound recordings and musical works; and, therefore

  (4) the outcomes of the two negotiations are likely to be similar.

- Dr. Nagle's analysis of the value of the sound recording performance right is predicated on the principles listed in the previous bullet, and hence confirms the equivalence of the sound recording and musical work performance right values.

- No arbitration panel or similar body that has explicitly examined the question of the relative value of sound recording and musical work performance rights has ever concluded that the sound recording should be valued at a greater rate. In contrast, the digital-cable CARP in the U.S. and the Copyright Board in Canada explicitly considered this question and determined that the values should be the same.[26]

- There is no evidence in this proceeding of any market in which sound recording and musical work rights are valued in a situation incremental to their original creation, in which the sound recording is valued more highly than the musical work, let alone valued at a rate some 5 to 20 times that of the musical work.

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[26] See Jaffe Rebuttal Exhibit 4, Report of the Copyright Arbitration Royalty Panel, Docket No. 96-5 CARP DSTRA, at ¶ 169 (November 28, 1997); Jaffe Rebuttal Exhibit 5, Decision of the Copyright Board of Canada, Public Performance of Sound Recordings 1998-2002, August 13, 1999, at 32. In other countries, the relevant authorities *implicitly* came to the same conclusion (or the stronger conclusion that the sound recording is worth *less* than the musical work) by assigning equal or lower values to the sound recording than were assigned to the musical work.

- Data from hundreds of songs, in dozens of movies and television programs, representing licenses issued by hundreds of publishers and record companies and involving tens of millions of dollars of royalties, prove conclusively that competitive markets value rights derived from sound recordings no more highly than the analogous rights derived from musical works.

IV. THE FEE MODEL

A. Structure of the fee model

In my direct testimony, I explained that the best way to develop the reasonable royalty fee is on the basis of the extent to which performances are actually made. I used one hour of broadcast heard by one person (a "listener hour") as a basic unit of the extent of performances made. I also derived a model based on one person hearing a single song (a "listener song") that I suggested should be available as an alternative for those streamers whose programming contained significant amounts of time with no sound recordings for which performance royalties are owed.

In its fee proposal, RIAA has proposed that one fee option be based on the number of "performances," defined to be equivalent to the concept that I had labeled the "listener song." In order to avoid confusion, and to focus the debate on the issues on which we differ rather than on potentially distracting issues of nomenclature, in this report I will accept the RIAA designation of the "performance" as the basic fee unit, and recast my fee model based on that concept of performance. This restatement of my approach is conceptually equivalent to the analysis that I had previously performed, but will, I believe, assist the Panel in understanding the similarities and differences between my approach and that of RIAA.

In my previous analysis, I calculated the average fee paid by over-the-air broadcasters per listener hour, and used that listener-hour fee as the basis for a proposed fee for internet streamers. I also calculated the average fee paid by over-the-air broadcasters per listener song, and suggested that this be an alternative model available to some streamers. To emphasize the point at which my approach can be looked at in parallel with that of RIAA, I can reverse this order of derivation, starting first with the fee per performance (listener song) on over-the-air radio, and then constructing the fee per listener hour from the per-performance fee.

As explained in my direct testimony, there is considerable benefit in terms of calculational ease to using data on Aggregate Tuning Hours ("ATH"). The number of annual ATH can be readily calculated going forward for most streamers. This number corresponds to annual listener hours, which is why I had based my previous model on that concept. Although I now propose to derive the basic fee benchmark on a per-performance basis, the availability of ATH information makes it highly desirable to formulate the performance-based model so that it can be calculated on the basis of ATH. This greatly reduces the data-collection burden, with the added benefit that the royalty is based on widely used numbers that are collected for other purposes.

To derive fees based on ATH from the fee per performance, I propose allowing streamers who choose to do so to base their royalty payments on ATH, combined with an estimate of the average number of songs per hour that corresponds to their category of streaming activity. For broadcast streamers with music formats, the ATH fee would be the fee per performance, times 12 songs per hour, the approximate average for music stations in my over-the-air database.27 For webcasters, the ATH fee would be the per-performance fee times 15 songs per hour, which appears to be a typical number for webcasting.[28] Stations who choose not to utilize these typical or average songs-per-hour figures (e.g., news/ talk/ sport stations, mixed-format stations, or religious talk stations with limited music) would base their license payments on some reasonably reliable method for estimating the actual number of songs per hour in their streaming.

In my direct testimony, I suggested that the option of paying based on performances (listener song) rather than on the basis of listener hours be limited to those streamers with fewer than 7 songs per hour. This was to prevent creating incentives for streamers with between 7 and 12 songs per hour choosing the listener-song model, and thereby undermining the validity of the average. The experience of attempting to

[27] This is a conservative assumption. The sample of stations in the fee model averaged slightly greater than 11 song detects per hour.

[28] Wise, Transcript at 4240.

estimate actual songs per hour for some stations, combined with the proposal by RIAA of a per-performance fee, has convinced me that such a limitation is unnecessary. I believe that the cost and difficulty of constructing an actual estimate makes it unlikely that any station in the 7-12 songs-per-hour range would bother to try to estimate its actual songs per hour.[29]

In essence, what I have done is to reproduce the previous model, but to derive the fee per hour from the fee per song, rather than vice versa. I believe that this simplifies the model, and makes it more directly comparable to the RIAA proposal. Substantively, the results are approximately the same as before for any licensee that chooses to count the actual number of performances and for broadcast music channels using the ATH model (because multiplying the per-performance fee by 12 songs per hour approximately reproduces the previous listener-hour result). For webcasters on the ATH model, the new approach leads to slightly higher fees than before. This is because the previous approach assumed that a webcast *hour* was equivalent to an over-the-air music *hour*, even though the webcast hour typically contains more songs. The new approach would recognize that, at the present time, the evidence

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[29] My direct testimony also proposed a third option, the "segmented listener hour" model. On reflection, I have concluded that this is an unnecessary complication, because stations such as Comedy Central Radio that have programming portions free of sound recordings for which performance rights must be obtained can calculate the appropriate fee using the per-performance (listener-song) model, incorporating the extent of programming without feeable performances into their reasonable estimate of songs per hour.

indicates that the average number of songs per hour in webcasting exceeds the average in over-the-air broadcasting, and would increase the webcasting fee proportionately.[30]

B. Recalculation of the fee model

At the time of my direct testimony, the most current data available to me on over-the-air broadcasters musical work royalty payments came from payments made by the broadcasters for the year 2000 on an estimated basis. As I explained then, there was no reason to believe that the final numbers would differ systematically from the payments based on estimates. Since the filing of my first report, the final reports for 2000 for ASCAP and BMI, and final numbers for SESAC for most stations, have become available. I have recalculated the fees incorporating this final information, to check my initial assumption that the estimated payments would be accurate on average. I also utilized some additional information that became available to refine my estimates of the number of songs per hour in various formats.[31] The results of the revised calculations are summarized in Figure *3*.

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[30] There is nothing intrinsic to webcasting that makes the number of songs per hour necessarily greater. If this same model were to be utilized for some future time period, it would be appropriate to adjust the webcasting songs-per-hour figure to reflect actual practice at that time.

[31] I updated the Broadcast Data Systems (BDS) songs-per-hour calculation based on data provided by Mr. Fine as part of discovery in this proceeding. In the average detects-per-hour data from the spring, each unique station in the dataset was treated as being tracked by the BDS for the entire year. However, some stations were not tracked by BDS for the entire year. I recalculated average detects per hour based on the actual number of weeks each station was tracked by BDS. In addition, I excluded Mexican and Canadian stations. These adjustments had a small effect on

I requested from the radio station groups updated data that reflected the fees owed by station based on 2000 year-end revenues.[32] As expected, for some stations, fees increased as compared to the fees reported to me in the spring, and for some stations, fees decreased. But in aggregate, the year-end fees paid to ASCAP, BMI, and SESAC were very close to the figures that were reported to me in the spring. In addition to updating the payments made by stations in my calculation, I have also included additional stations for which I now have complete data. If I did not have complete performing rights organization fee data as part of the most recent data production, I used the best available information on the stations' fees, that is, the data on fees that they reported to me in the spring of 2001.[33]

In total, I relied on data from 872 radio stations representing over $143 million in fees paid to ASCAP, BMI, and SESAC.[34] The fee per

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the figures that I utilized for songs per hour for different formats, slightly increasing the average songs per hour.

[32] The timing of my last report made it impossible for me to use data based on year-end revenue. Radio stations make payments throughout the year to ASCAP and BMI based on revenues earned in the prior year plus an inflation adjustment. In April of the following year, stations file an "annual report," summarizing year-end revenues, and calculate a fee based on that revenue. Stations compare this fee with payments made, and "true up" their accounts. If the estimated payments were greater than the fee owed, the station gets a refund. If the estimated payments were less than the fee owed, the stations make an additional payment. These "true-up" payments were not reflected in the data I used in the spring.

[33] For 74 stations representing less than $7.5 million that were included in the 898 stations used in my calculations in the spring, I was missing final data on payments to one of the performing rights organizations, usually SESAC.

[34] As discussed in my direct testimony, stations were excluded from the per-performance calculation if I did not have data on the average number of songs per hour for stations of that format.

performance and the fee per listener hour for over-the-air radio stations are \$.00020 and \$.0022, respectively, as summarized in Figure *3* These numbers represent the average fee per listener paid by stations that represent a significant portion of the total fees paid to the performance rights organizations for the copyright obligation incurred for performances of the musical work on over-the-air radio.

C. Minimum fee

Within a per-performance model, payments to copyright holders are proportional to the performances of music, and this fee structure guarantees the copyright owner is compensated for music used. As discussed in my direct testimony, this eliminates the concern, expressed in the legislative history and echoed by Mr. Marks in his direct testimony,

*[35] Under our model, they will be paid for every performance made. The only circumstance in which the resulting royalties will be small is where there are very few performances. I have not seen any argument as to why, when very few performances are being made, it is necessary that significant royalties be paid. Indeed, based on this

[35] Marks, Transcript at 9389-9390

* Subsequent to the filing of the restricted version of Professor Jaffe's rebuttal testimony, RIAA requested that additional information herein be designated as "Restricted" under the Protective Order entered in this proceeding. The relevant information has been bracketed and marked with an asterisk in this document. In accordance with the Protective Order, the Services reserve the right to challenge RIAA's claimed "Restricted" designations.

concern alone, it would be appropriate to have no minimum fee, so that a licensee who made no performances would not have to pay any royalties.

Given that the per-performance model protects the copyright owners from the rights' being used without appropriate compensation being paid, the only remaining economic argument for a minimum fee is that one is necessary to protect the administrator of the fee collection system from having to service a licensee who costs more to have in the system than the revenue that it generates. In this context, what is relevant is not the overall cost of operating the licensing system, but rather the *incremental* cost of adding another licensee to that system. The revenues that are collected by the per-performance model will cover the overall costs of operating the licensing system. The per-performance model is, after all, derived from the over-the-air musical works licenses, which are administered by ASCAP, BMI, and SESAC. Those entities provide a marketplace benchmark for what it costs to run such a system. Each of them must process payments, keep track of data, make distributions – perform all of the functions that Mr. Marks testified SoundExchange will have to perform.[36] These costs are covered by the payments that are made by licensees who make significant performances, and indeed each licensee will bear those costs in proportion to the number of performances made.

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[36] Marks, Transcript at 9390-9391.

To see the relevance of the minimum fee, imagine that, for some reason, I would like a sound recording performance license, but I actually do not intend to make more than a tiny number of performances. Now, since I am making a tiny number of performances, I should cover practically none of the overall costs of operating the licensing system; those costs are borne in proportion to the number of performances, and hence will be covered by the fees paid by others. But by virtue of my taking a license, the operator of the licensing system will bear certain costs that they would not bear if I had not signed up. They will have to add me to their accounting system; they may have to send me periodic invoices; they will have to receive, process and deposit my checks. And if I am making very few performances, the revenue that I generate under the per-performance model may not even cover these costs, let alone contribute to the overall system. Hence it is appropriate that every licensee pay at least enough to cover these incremental costs, regardless of how many performances they make.

RIAA itself has agreed to a license with a minimum fee of On its face, this calls into question the legitimacy of the proposed $5000 minimum fee. Conceptually, it is hard to see why RIAA would agree to a deal with a minimum if the incremental cost of handling one more licensee were greater than

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Just as with the performance fee itself, ASCAP, BMI, and SESAC provide market evidence of what this kind of minimum fee looks like.[38] ASCAP's internet license annual minimum fee is $264; BMI's is $259; and SESAC's is $150.[39] Clearly, my proposed annual minimum fee of $250 is in the same range as these fees.

In calculating fees per performance, I totaled the fees paid to each organization, in order to compare total fees to total performances. With respect to the minimum fee issue, however, what is relevant is the minimum charged by any *one* organization, because *each* of these organizations has exactly the same kind of incremental costs associated with an additional licensee. Each of them must do the accounting, send the invoices, and process the checks. These costs are not related to the portion of the overall repertoire that the organization handles, because they are related to processing the licensee end of the operation, not the distribution end. In effect, this duplication of processing costs is a minor inefficiency associated with having multiple collecting organizations. Thus, using these fees as benchmarks, it is clear that a minimum on the order of $250 per year represents marketplace experience.

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[38] I have noted that it is difficult to use the musical work internet licenses to determine the appropriate fee per performance, because we have so little experience with stations operating under these licenses that we cannot measure the fees on a per-performance basis with any accuracy. This difficulty does not apply to the minimum fees, which can simply be read off of the license forms offered by each society.

[39] See Jaffe Rebuttal Exhibits 1A, 1B, and 1C.

D. Sensitivity of the fee model

Confirmation based on internet musical worksfees. In my original report, I looked at the fee per listener hour of over-the-air radio stations rather than on the internet. The standard over-the-air radio license is based on a percent of revenue. Because it is desirable to have royalty payments based on performances, I converted the percent of revenue into a payment per performance.[40] As explained in my direct testimony, I believe that the over-the-air radio royalty is more reliable than a royalty rate that might be derived from the limited experience with musical works licensing on the internet.[41] In order to explore, however, whether there is any indication that rates would be much higher if one looked at musical works licensing on the internet, I have undertaken some analysis of the internet musical works licensing experience.

The standard-form internet license offered by BMI and ASCAP is a percent-of-revenue model. Although there are some alternative formulas, the primary formula amounts to 1.615% of revenue for ASCAP and 1.75% of revenue for BMI. The standard internet license offered by SESAC is based on page requests, not revenue. As noted previously, however, SESAC accounts for a small share of the overall royalty

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[41] Direct Written Testimony of Adam Jaffe at 17-18.

picture.[42] Hence the overall musical works royalty is approximately 3.5%of revenue. In over-the-air radio, the royalties paid to the three licensing organizations for musical works comprise approximately *3%* of revenue. Because the definitions of revenue subject to fee are not precisely the same, these percentages may not be directly comparable.[43] It is clear, however, even with allowance for the inexact match in revenue definitions, that the internet royalty rates as a percentage of revenue are, at most, only slightly higher than the over-the-air radio rates and much lower than the 15% of revenue proposed by RIAA.

Since the internet is new, there is limited experience with licenses in this medium. However, one webcaster in this proceeding -- has signed licenses with ASCAP, BMI, and SESAC. Because we have performance-related data, we can convert the fees to equivalent per-performance rates.

[42] Most radio station groups have a license with SESAC that does not use the percent-of-revenue formula. Examination of the data provided to us suggests that ASCAP and BMI fees account for greater than 98% of fees paid by over-the-air radio stations.

[43] The ambiguity regarding the percent of revenue that goes to musical work performance rights in over-the-air radio derives from the fact that the licenses are specified in terms of a "net revenue" concept that is calculated solely for the purpose of the license agreements. The estimate of 3% to 3.5% is derived as follows. BMI apparently collects 1.35% of gross revenue. See Jaffe Rebuttal Exhibit 3, United States of America v. BMI, In the Matter of the Application of Music Choice, et al., for the Determination of Reasonable License Fees; Memorandum and Order, 64 Civ 3787 (LLS),July 20, 2001, at 12. Assuming that ASCAP's share is comparable, and SESAC has a small share, this would correspond to 3% of gross revenue. The stated net revenue percentages are 1.615% for BMI and 1.605% for ASCAP, suggesting that the total as a percent of net revenue would be about 3.5%.

Simultaneous listeners. The issue was raised during my oral direct testimony that data on aggregate tuning hours measure computers using streams and not the number of listeners to those streams.[44] I am aware of no data indicating the frequency with which multiple listeners utilize a single internet stream. I do not have any reason to believe that the possibility of multiple listeners necessitates any meaningful adjustment to the fee model.

AQH. It was suggested during my cross examination that my listener-hour fee is not appropriate for the internet because it is derived from Arbitron AQH, which counts people who listen for 5 or more minutes during a 15-minute period as having listened for the entire 15 minutes.[45] As best as I can determine, Arbitron does not have data on the frequency with which people listen for more than 5 minutes but less than 15 minutes. As a threshold matter, in terms of aggregate listener hours, this effect would be offset by those listeners who listen to one or more stations during a 15 minute period, but do not listen to any one

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44 Jaffe, Transcript at 6687.

45 Jaffe, Transcript at 6678.

station for at least five minutes and therefore are not counted for having listened at all. Given this, and the fact that ratings based on AQH are the standard measure of listening audience throughout the radio industry, I do not think it is appropriate or necessary to make any adjustment for this issue. It certainly would not be appropriate to apply a three-fold adjustment based on the ratio of 15 minutes to 5 minutes. This would be right only if ***every*** listener stopped listening after 5 minutes (and no listeners ever tuned in for less than 5), which is clearly not correct.

E. Timing issues

We are not attempting to set fees for all time, just for specific two-year periods. The statute specifies that rates shall be adjusted every two years.[46] During that two-year time period, the contemporaneous musical work fee is a reasonable benchmark for the sound recording rate at that time. The fact that the formula underlying the musical works rate was first established in the past does not undermine its validity as an indicator of the market rate today. Markets must continually deal with the evolution of prices over time, and there is no reason to believe that current prices are distorted because of past prices.

[46] Congress recognized that the "two-year intervals are based on upon...recognition that the types of transmission services in existence and the media in which they are delivered can change significantly in short periods of time." House Conference Report No. 105-796 at 86.

Thus, the fee paid for musical works in 2000 is clearly a valid benchmark for fees to be paid for sound recordings in 2000. As was pointed out in cross examination, in 2000, the fees that the over-the-air radio stations paid to BMI were for interim and not final fees.[47] The interim fees are set at the same level as the last final fees, which were subject to negotiations. There is an ongoing rate court proceeding to determine BMI final fees at which the radio stations have asked for a lower fee and BMI has asked for a higher fee. The final fees paid to BMI could be higher or lower than the current rate of 1.605% of revenue, so there is no reason to believe that there is a bias associated with using the interim fees.[48] Even if BMI fees were increased the full amount that BMI has requested - which is surely higher than what the final rate will be – this would change our result by only a small amount.[49,50]

47 Stephen Fisher, Transcript at 7707.

48 In fact, in the BMI rate recently decided in a rate dispute between Music Choice and BMI, the final rate for the cable and satellite services was 1.75% of revenue, below the *3%* of revenue interim fee. See United States of America v. BMI, In the Matter of the Application of Music Choice, et al., for the Determination of Reasonable License Fees; Memorandum and Order, 64 Civ 3787 (LLS), July 20, 2001.

49 BMI payments account for approximately 49% of total performing rights organization fees. So if BMI's final fees were equal to its request, this would imply an upward adjustment of less than 6% to our fees.

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The 2000 fee is clearly conservative when applied to 1999, because revenues have been rising faster than have audiences.[51] Hence the 2000 fee provides a ceiling on the rate for the 1999-2000 time period.

With respect to 2001-2002, numbers on payments that are to be made in the future are simply not available. An appropriate approach would be to use the 2000 rate per performance as the crossover point for the sound recording, and then adjust that rate going forward (i.e., 2001-02) on the basis of forecasts of the CPI inflation index.[52] Mechanically, I propose an increase to the fee of *3%* in 2001 and *3%* in 2002.

F. Different fees for different types of streamers

The Panel requested evidence regarding fees for different types of streamers. Any such distinctions should be made on the basis of a conclusion that the competitive market value of the sound recording is different in these different contexts. The mere observation that differences exist, or that some uses appear to be more valuable to the users than others, does not demonstrate that the value of the sound recording itself is different in the different contexts. By analogy, a car with leather seats and power windows may be more desirable and sell for more than the same car with vinyl seats and window cranks. But that

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[51] Total radio industry market revenue grew 10% from 1999 to 2000 (Duncan's American Radio). Audience size remained approximately constant over the same time period. (Arbitron Radio Listening Trends).

[52] The Congressional Budget Office estimated an increase of 3% in 2001 and 2.7% in 2002. (Congressional Budget Office, August 2001, Table 2.2).

does not mean that the engine in the more expensive car is worth more than the engine in the second car.

It is clear that the value of an internet streaming services is derived from much more than just the sound recordings themselves. Indeed, if all one needed to derive value from internet streaming were sound recordings, it would be hard to understand why no one has managed to make any money in this business, since the sound recordings themselves have been available to anyone who filed for the statutory license. Thus the starting presumption should be that the various service offerings that are being considered differ with respect to the overall package of services that they offer users, but do not differ with respect to the value of the sound recordings themselves.

Consumer influence. Except to the extent that consumer influence affects the likelihood of displacement, it is not grounds, as a matter of economics, for a higher fee. People who have fancy stereos do not pay more for CDs; by the same token, the enhanced value associated with consumer influence is due to the technology of the webcaster. It does not increase the value of the underlying sound recording. Further, it is possible that consumer influence could increase promotional value; by allowing consumers to hear music more within a range of their musical preferences, they may be more likely to hear new music that they like enough to buy.[53]

Further, defining what constitutes "consumer influence" creates a hornets' nest of problems. The ingenuity of entrepreneurs will always outstrip our ability to make distinctions and draw lines. And any lines that are drawn will end up being arbitrary. For these reasons, I do not think that it is necessary or appropriate to attempt to set different rates for streamers based on the extent of consumer influence.

The observation that fees distinguished on the basis of consumer influence are likely to be more trouble than they are worth is reinforced by the relatively small premia that have been negotiated in voluntary licenses involving the consumer-influenced services participating in this proceeding which the RIAA contends are "interactive."

It does not

53 Direct Written Testimony of Quincy McCoy at 5

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make sense to create a potentially complicated set of arbitrary distinctions in order to implement such small differences, particularly in the absence of any evidence that significant displacement is occurring.

Syndicators. RIAA proposes a higher fee for syndicators. Within a per-performance model, there is simply no logical or economic justification for this higher rate. The performance is the performance, its value is what it is, and that value does not change if the fee is paid by a party who is packaging the performances for someone else's website. For example, one of the agreements proffered by RIAA itself as a benchmark for its proposal does not impose any premium for performances that occur in the context of syndication.[56]

Simulcast/rebroadcast of ouer-the-air signals. In the willing buyer/ willing seller negotiation, the fact that the sound recording performance right is free over the air would likely have a significant impact when parties negotiated the rate for performance of the same sound recordings over the internet. Although there is not a one-to-one correspondence between performances that are heard by people who would otherwise listen over the air and performances within 150 miles, it does seem likely that Congress's decision to exempt rebroadcasts within 150 miles was driven by a related perception that the value of a sound recording rebroadcast on the internet cannot be totally divorced from the

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zero value that the same sound recording performance earns over the air.[57]

Further, any concern about greater displacement of CD sales from internet performances vis-a-vis over-the-air performances does not seem to apply to simulcast/rebroadcast.[58] For these reasons, there is a strong case that the royalty rates should be lower for broadcast streamers than for webcasters.

I do not believe that it is possible to quantify these effects in a rigorous way so as to derive a discount off the webcaster rate that should be applied to the streaming of over-the-air broadcasting. In my direct testimony, I concluded that a sound recording performance royalty in the range of 40% to 70% of the musical works rate would be reasonable, given the greater value to sound recordings of promotion, the market power of the musical works owners, the conservatism of the calculations that I undertook, the evidence from other countries, and the statutory factors.[59] I then proposed a fee model based on the absolute upper limit of this range. This led to a proposed per-performance rate of $.00014, or 70% of the over-the-air rate of $.00020.

Given the factors discussed above, I believe it would be reasonable for the rebroadcaster rate, instead of being at the upper end of the 40%

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57 1976 Copyright Act, 17 U.S.C. § 114(d)(1)(B)(i) (1998).

58 Katz, Transcript at 1112-1113.

59 Direct Written Testimony of Adam Jaffe at 48.

to 70% range, to fall at the lower end of the range. This would justify a rate of 40% of the over-the-air rate of $.00020, or $.00008 per performance. Although motivated in part by the same considerations underlying the exemption for listeners within 150 miles, this approach would not be based directly on any evidence regarding listenership within 150 miles, and no further discount based on any such information would be appropriate.

Figure 4 combines these figures with the fee-per-hour figures and shows a summary of the services' proposed fees.

G. Services' proposed royalty payments

The Panel requested, in its order of September 7, 2001, that each side provide a chart, based on evidence in the record, showing the royalty payments that each service would pay for October 28, 1998-December 2000 and for January 2001-December 2002. Figure 5 summarizes those calculations for services that have provided ATH data. ATH is a measure that is widely used on the internet and is, in effect, the average number of listeners times the number of hours streamed. For purposes of these calculations, I have used for the number of performances: 15 per hour for webcasters; 12 per hour for music-intensive broadcasters; and 1 per hour for news/ talk/ sports broadcasters.[60] When a licensee, instead,

[60] The evidence that I have reviewed suggests that 1 song per hour is likely to overstate *significantly* the use of music on news, sports, and talk stations. Many stations play little or no feature music. For example, WABC is one of the few ABC stations that has music programming. WABC reports to ASCAP and BMI that about 5% of its weighted *hours* contain music. Most of these hours must not be full hours of music,

calculates its fees, it will have the option to base its calculation on the industry average or on a reasonably reliable estimate, specific to that licensee, of songs per hour times tuning hours.

Webcasters. In this proceeding, the webcasting services have provided historic tuning hours for the October 28, 1998-December 2000 time period, and they have provided estimates of tuning hours for the period January 2001-December 2002. In general, a webcaster's fee is calculated by multiplying tuning hours times 15 performances per hour times the fee of $.00014 per performance, subject to a minimum fee for years that the licensee was in operation. For example, a service that has been in operation since October 28, 1998 (or before) would pay a fee in the first time period that is the greater of tuning hours times 15 times $.00014 per performance, or $542 ($42 for October 28-December 1998, $250 for 1999, and $250 for 2000). For the 2001-2002 time period, the fee per performance is adjusted by the projected increase in the CPI, which, as discussed above, is estimated to be *3%* per year. For purposes of these calculations, I have assumed that the fee per performance is $.00015 ($.00014 times 1.06).[61] Again, the fee is calculated as the

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since WABC's only all-music programming is a three-hour Sinatra program on a weekend night.

[61] This is a simplifying assumption for convenience. I suggested above that the rate be increased 3% in 2001 and 2.7% more in 2002. The data provided to me by the webcasters are estimates for the two-year period 2001-2002. By applying the 6% increase to this total for both years, I slightly overestimate the payments that would result if separate numbers were available for the two years.

greater of the minimum fee ($250 per year for 2 years, or $500) or $.000 15 per performance times 15 performances times ATH.

Webcasters that: (1) have significant non-music programming; (2) have programming that does not incur a sound recording copyright obligation (because the sound recordings are from before 1972 or because the service owns the copyright); or *(3)* have otherwise licensed a significant fraction of their music programming directly from the individual owners of the performance right are likely to estimate fewer than 15 performances per hour. The only webcaster to which I have made an adjustment for purposes of calculating the fees is Comedy Central Radio. According to Joe Lyons, 50% of the sound recordings used on Comedy Central Radio are owned by Comedy Central.[62] The tuning hours listed in Figure 5 have been adjusted to account for the fact that only 50% of the tuning hours are for sound recordings that are part of the RIAA repertoire.

Broadcasters. On a going-forward basis, the broadcasting stations that are simulcasting their programming on the internet will be able to track tuning hours either through server logs or through third party ratings services. However, the broadcasting services generally do not have historical data available covering the time period October 28, 1998-December 2000. I used data that I collected from the broadcasters

[62] Direct Written Testimony of Joe Lyons at 4.

in the spring of 2001 about streaming activity at the beginning of 2001 to make a conservative estimate of the fees owed by these stations for the time period October 28, 1998-December 2000.[63] The fees displayed in Figure 5 are illustrative only. In some cases, the radio stations have contractual arrangements with the streaming provider to pay the licensing fees for sound recording performances.[64] For Clear Channel, the data that I have available is for 87 stations out of the 300 that were streaming at the time that the direct cases were filed.

To estimate fees, I assume that tuning hours in 2000 were equal to the level observed at the beginning of 200 1. This is clearly a generous assumption since listening was growing over this time period. I assume that tuning hours in 1999 were half of the 2000 level.[65] For the two months in 1998, I assume that fees are at the same level as 1999 for the one-sixth of the year (e.g., two months).

For stations with music programming, the fee is the greater of $250 per year or $.00008 per performance times 12 performances per hour times tuning hours. Stations that are generally recognized to be sports/news/talk stations do not play significant music. For purposes of my fee calculations, I have assumed that the fee for sports/news/talk

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63 The data is summarized in XJAF 00538a, 00539-0054 1.

64 Juris, Transcript at 7072-7073.

65 According to the survey done by Mazis, over 50% of respondents had listened to internet streaming within the last 12 months. See Direct Written Testimony of Michael Mazis at 7.

stations is 1 sound recording per hour at a rate of $.00008 per song times tuning hours, subject to the minimum fee.

V. PROMOTIONAL VALUE VERSUS DISPLACEMENT

As discussed in my direct testimony, the likely equivalence in value of the sound recording performance right and the musical work performance right holds before adjustment for any differences in promotional value.[66] For either right, expected promotional value would tend to induce the seller to reduce the royalty rate that would otherwise prevail. Under competition, the royalty rates would be reduced by the value of any promotion created by performances. This means that if the promotional value of sound recordings exceeds that of musical works, the competitive royalty for sound recordings would be lower than that for musical works.

There has been much discussion in the testimony in this proceeding about whether digital performances of sound recordings will promote the sale of CDs, or reduce the sales of CDs through "displacement." This is not an "either/or" proposition. Most likely, both will occur to varying extents for different listeners. What matters is the *net* incremental impact on CD sales due to digital performances; i.e., the increases (if any) due to promotion minus the decreases (if any) due to displacement.

[66] Direct Written Testimony of Adam Jaffe at 36-37.

The fee model discussed above and in my direct testimony is derived from the overall equivalence of the sound recording and musical work market values, with an adjustment for the differential value of promotion to the sound recording and musical work in over-the-air radio. The validity of this model is not dependent on the assumption that no displacement occurs. It depends only on the assumption that the net promotional value due to internet broadcasts (the promotional effect minus losses due to displacement) is comparable to the estimated promotional value effect from over-the-air broadcasts. Furthermore, since the fee model is predicated on a 30% reduction from the over-the-air rate, while the conservative promotional value calculation I carried out would have supported a deduction of almost 50%, there is already some leeway for increased displacement, so long as that increase is not too large.[67]

This leads to the question of the state of evidence in this proceeding regarding the net effect of promotion and displacement from internet broadcasts. Much of this evidence consists of fears of what might happen in the future, rather than any testimony about displacement that is occurring today.[68] Given the time period-specific

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[67] The value to sound recording rights holders comes in the form of record company profits and recording artist royalties from the sale of CDs. I excluded artist royalties from my promotional value calculation in my direct testimony, which clearly leads me to understate the value of promotion to rights holders in sound recordings. (Direct Written Testimony of Adam Jaffe at 47; Jaffe, Transcript at 6528-6529).

[68] Katz, Transcript at 1034-1035, 1104-1105, 1120.

nature of the task before this Panel, it is simply unnecessary to try to determine how great displacement may be at some future date when internet streaming is better developed. This hypothetical future level of displacement, no matter how certain, is simply not relevant to fees for time periods ending in 2002.

Another form of evidence that has been presented is anecdotal impressions based on conversations with a few internet users.[69] No social scientist would base conclusions on evidence of this type, and it would be similarly inappropriate for the Panel to do *so*.

Putting aside anecdotal evidence and testimony about what might happen in the future, the facts in evidence regarding promotional and displacement effects are the following:

- Promotional value of over-the-air performances is large. This is confirmed by the SoundData survey data, as well as the millions of dollars spent every year by record labels to try to direct the promotional effect towards their own labels.[70]

- The survey conducted by Professor Mazis indicates that there is also observable promotional impact among existing listeners to internet streaming, and that this effect is larger than any displacement effect for these listeners.[71]

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[69] Katz, Transcript at 1097-1099, 1128; Griffin, Transcript at 1589-1591; Himelfarb, Transcript at 2886-2887.

[70] Direct Written Testimony of Michael Fine at 5-14; Rosen, Transcript at 532-533; McLaughlin, Transcript at 705-709; Altschul, Transcript at 937-952; Katz, Transcript at 1001; Griffin, Transcript at 1565-1566; Wilcox, Transcript at 1783-1785; Kenswil, Transcript at 24 12.

[71] Direct Written Testimony of Michael Mazis at 18-20.

- There is no quantitative evidence that has been presented showing that significant displacement is occurring now, or is likely to occur through 2002.[72]

- There is no evidence that displacement was a significant concern cited by RIAA in its negotiations with its "benchmark" licensees as a factor justifying the rates it was requesting.

- Royalty rates for internet performance of musical works proffered by ASCAP and BMI do not appear to be significantly higher than the musical work performance royalties on over-the-air radio. Although the value of promotion to the musical works is less than to the sound recordings, it is still significant. If net promotion were known to be much less on the internet, the owners of rights in the musical works would be demanding higher rates.[73]

- There are attributes of streaming from which it is logical to infer that displacement *might* be larger on the internet than over-the-air.

- There are also attributes of streaming from which it is logical to infer that promotional value *might* be larger on the internet than over-the-air. These include:

  (1) the availability of track-identifying information;

  (2) the availability of other information about albums and performers in conjunction with the streamed music;

  (3) the presence in many cases of "buy buttons" or links to sites where purchases can be made[74];

  (4)

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[72] Katz, Transcript at 1082; Griffin, Transcript at 1531; Wilcox, Transcript at 1800-1801; Pipitone, Transcript at 2301-2302. In fact, Wilcox stated that he does not believe there is a set formula that can be used to quantify the displacement caused by a given service. (Wilcox, Transcript at 1806).

[73] See Rebuttal Testimony of Adam Jaffe, Exhibit 2A (ASCAP) and Exhibit 2B (BMI).

[74] For example the NetRadio "buy button" produced $750,000 in record sales in 2000. Of course, listeners buy albums from other vendors in addition to ordering through "buy buttons." See discussion about NetRadio, Wise, Transcript at 4156-4158.

[75] Wilcox, Transcript at 1955-1959.

Taken together, this evidence simply does not support a conclusion that net promotion on the internet is likely to be less than on over-the-air radio, let alone enough less to require a rate even higher than that produced by the conservative discount that I have applied to existing over-the-air rates.

VI. THE RIAA BENCHMARKS

A. Framework for consideration of the R I M benchmarks

RIAA has put forward as indicia of willing buyer/willing seller contracts the agreements that it entered into with various parties prior to this CARP proceeding. The Panel must determine whether these proffered benchmarks provide reliable information that indicates that the rates and terms requested by RIAA are consistent with the willing buyer/willing seller test, i.e., reflective of competitive market rates and terms for the statutory license. As a threshold matter, I have demonstrated that the RIAA proposed rates are 5 to 20 times the corresponding rate for musical works, whereas in the extensive, well-developed market for sound recording and musical work rights in movies and television the sound recording earns no more than the musical work. This is strong evidence that the RIAA benchmark agreements do not represent competitive market rates. Nonetheless, in this section I analyze the proffered benchmark agreements on their own terms.

In determining whether and to what extent to rely on these proffered benchmarks, there are three categories of issues to consider:

- Did buyers have good information about and access to a statutory license that was a good substitute for the RIAA-offered agreement, so that we can presume that they were "willing" buyers in the appropriate sense?

- How much real information about competitive market conditions does a given agreement convey, i.e., is it an economically significant transaction that should be given significant weight?

- Is the situation in which the agreement was reached such that it is comparable to the situation facing other statutory licensees?

If the first of these questions cannot be answered in the affirmative, then we cannot conclude that the contract at issue represents reasonable rates and terms, even in its own context. Buyers who did not have good information about their alternatives cannot be considered "willing" buyers in the sense of replicating competitive market outcomes. Buyers for whom the statutory license was not a good substitute for the voluntary deal being offered by RIAA did not have significant protection against the market power of RIAA, which was, of course, the only party offering the voluntary license. In other words, the statutory license is the conceptual "immunization" against the likelihood that the contracts negotiated by RIAA reflect its market power. If the statutory license was not a good substitute for the RIAA deal from the licensee's perspective, then this immunization was ineffective, and the deal represents monopoly rates and terms rather than reasonable rates and terms.

Even if the license is not unreasonable as a benchmark for the above reasons, if it is not economically significant, it should be given little weight in determining overall market rates and terms. Any real market always contains aberrations. When there is little at stake economically, the buyer does not have a significant incentive to learn what true market conditions are. A buyer in such circumstances may well agree to terms that no rational buyer would accept if they were applied proportionately to a situation where the economic stakes were higher, simply because, in these circumstances, the unreasonable terms impose costs that are too small to make it worthwhile to search, negotiate, or litigate for more reasonable terms.

Finally, we still need to determine whether the buyers in these deals were similarly situated, from an economic and business perspective, to the licensees who are requesting the statutory rates and terms. Otherwise, the proffered agreements are not good "comparables." To use them in the current setting (if at all fair to do *so)* would require adjustment for the different economic and business circumstances that apply.

I will first discuss conceptually the kind of circumstances that appear to have arisen requiring negative answers to each of these three key questions, with examples from the documentary record as to where they apply. I conclude this section with an overall assessment of the proffered benchmarks, and conclude that they do not support the fee proposal that RIAA has made.

B. Was the licensee a willing buyer in the appropriate sense?

RIAA puts forward these 26 agreements as evidence of what terms and conditions would be agreed to between willing buyers and willing sellers. As I have discussed before, I believe that the willing buyer/willing seller test should be interpreted as rates and terms that would prevail in a competitive market. As a general observation, it is worth noting that all of the 26 agreements contain confidentiality provisions that prohibit the licensees from discussing the agreements with others. If these agreements represent competitive rates and terms, there would be no economic logic to the inclusion of such confidentiality provisions. When my grocer sells me oranges, he has no reason or inclination to limit my ability to discuss that transaction with others. Indeed, open and freely-flowing information is one of the hallmarks of a competitive market. That RIAA chose to impose strict confidentiality on its licensees suggests that it did not, indeed, perceive the deals it was making as competitive market transactions, and/or it did not wish the market to function competitively via widely available information.76

[76] It is, of course, not uncommon for contracts to contain confidentiality provisions. Often the reason for such provisions is that the contracts are highly tailored to the specific circumstances of the individual buyer, and the seller does not want other buyers to know about these tailored terms. But RIAA has not suggested that these contracts were based on special deals tailored to each licensee. To the contrary, they

Information problems. Reasonable information about the alternatives available is a necessary condition for a well-functioning market. Thus a willing buyer, in the sense of one who engages in a transaction that reflects what would transpire in a competitive market, must be reasonably well-informed about the available alternatives. With respect to transactions with RIAA, an important dimension of information is understanding how the statutory license works, and understanding how the availability of the statutory license makes it unnecessary for streamers to execute a voluntary deal with RIAA in order to engage in activities covered by the statutory license. If a licensee does not appear to have this understanding, then there can be no presumption that the availability of the statutory license disciplined the monopoly power of RIAA, and hence no reason to believe that the agreement reflects anything other than monopoly rates desired by RIAA.

There is considerable evidence that some licensees did not, in fact, understand the alternatives available to them.[77] Further, in some cases, it appears the licensees who seemed to believe that they needed a voluntary RIAA license to begin streaming were not disabused of that notion by RIAA.]was a potential licensee who

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have put forward these agreements as evidence of general market conditions, and as appropriate as benchmarks for the generic statutory license.

77 I am aware that the RIAA website contained information about the availability of the statutory license. But the website information is fairly general, and it is clear from the evidence that some licensees did not understand what the statutory license did for them, even after consulting the website.

contacted RIAA evidencing significant misunderstanding of how the statutory license works. Their correspondence with RIAA started with an email reading:

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It would seem that RIAA could have responded with the information that the filing of the intent letter was all that was necessary to be "totally compliant with the laws." Instead, Mr. Marks responded:

This examples is only illustrative of incorrect and incomplete information that was held by numerous licensees.78

Concerns about timing and uncertainty. As noted, without the statutory license available as a reasonable substitute, the rates and terms in the RIAA deals must be construed as monopoly rates and terms, not reasonable rates and terms. To the extent that the delay and uncertainty associated with the ultimate outcome of this proceeding was a significant problem for a potential licensee, the reliance on the

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78 See, for example, [[

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statutory license and the outcome of this proceeding would not have been a good substitute, meaning that the licensee may well have agreed to an above-competitive rate for the (available)voluntary deal.

Examples of impatience and concerns about the uncertain CARP outcome fall into several broad categories, and are evidenced in the record. Several licensees demonstrated a sense of urgency because of a variety of other business matters that were affected by the RIAA negotiations, including the need on the licensee's part to secure an RIAA license as a predicate to concluding a webcast radio syndication agreement with a third party or, in some cases, to secure investors.[79] For example:

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[79] For other examples of timing concerns, see, for example, [[

.]]*[81] Again, these examples illustrate the ways in which delay and uncertainty made reliance on the CARP a poor substitute for the deal being offered by RIAA.

"Bundling" of other considerations with rights conveyed by the statutory license. It is elementary logic that the rates in the deals made by RIAA are indicative of reasonable rates for the statutory right only if what was conveyed to the licensees by RIAA in those deals was limited to the statutory right. There is considerable evidence that this was not the case. On the contrary, many of the licensees made it clear that a significant reason they were doing deals with RIAA was to get

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[80] On the uncertainty of arbitration, see, for example, [[ ]]

[81] On the uncertainty of coverage issue, see [[

something *other* than the simple right to make streaming performances.[82]

For example, as Mr. Marks discussed in his oral testimony,

[82] For examples of additional other considerations, see, for example,

[83]

Cost of litigation. The value of a CARP-determined statutory license as a substitute for a voluntary deal is inherently limited by the legal costs that parties expect would accompany that option. Put simply, the cost of relying on the statutory license would be the expected reasonable rate *plus* litigation costs. Thus, if the RIAA-proposed voluntary deal exceeded a reasonable rate, but exceeded it by less than the expected litigation costs, licensees would still agree to the proposed unreasonable rate.

Many licensees knew that their streaming activities might be limited during the arbitration period, and it was often true that even rates significantly above a reasonable level would still be cheaper than litigating in this proceeding. Examples of such concerns in the record are as follows:

[87] See, for example,

[88] See, for example,

Mr. Marks of RIAA actually utilized such anticipated litigation costs in negotiation]

This message implies that, even if believed that the reasonable rate was zero, they would still be better off accepting RIAA's "proposed numbers," because litigating to get the reasonable rate would cost even more.

C. Adjustment of the RIAA benchmark to derive a reasonable royalty

As I discussed in my direct testimony, it is very difficult to start from an unreasonable benchmark, and then adjust it to produce a reasonable rate, because the magnitude of "unreasonableness" will typically be unknown.

When an agreement is reached, and the

alternative to that agreement is a reasonable fee procured through large legal expenses, the only economically reasonable inference is that the agreed rate is no higher than the reasonable rate *plus* the expected legal fees. This implies that one could adjust the agreed-to rate by subtracting the expected legal fees to yield the reasonable rate. But if Mr. Marks is correct that the legal fees would exceed the payments under the agreement, such an adjustment would produce zero as the reasonable rate. More generally, it is not going to be possible to make such adjustments in a logically consistent manner.

D. Economic significance or "weight"

In the previous section, I discussed numerous reasons why many of the license deals put forward by RIAA as benchmarks cannot be presumed to represent reasonable royalty rates. In addition, most of the agreements are with streamers who have never streamed, have already ceased streaming, or are operating at levels such that the payments they are making to RIAA are economically insignificant (often at the minimum fee rate rather than any per-performance or revenue-based formula). Such agreements do not convey significant information about market conditions even if they could be presumed to be reasonable.

the amount represented by the sound recording rights in my music and television data (which demonstrated equality with musical work valuations), and about one-seventieth as large as the over-the-air royalties that were used in my promotional value calculation and that establish my per-performance rate.

Half of the agreements are with parties who have either ceased operations [[ ]] or have not yet launched streaming [[(iJockey.com(NRJ Media); GaliMusica.com; She]] For most of the licensees, RIAA has either not reported amounts paid under the licenses, or reported very small amounts, as low as [[ ]]

Thus, in the aggregate, there is much, much less here than meets the eye. Contrary to the impression created by the oft-repeated reference

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89 Direct Written Testimony of Steven M. Marks.

90 Direct Written Testimony of Steven M. Marks;

91 Direct Written Testimony of Steven M Marks;

92 Also, see

to 26 benchmark agreements, RIAA has not presented the Panel with broad evidence regarding marketplace transactions. On the contrary, the vast majority of the proffered benchmarks convey little or no information about market conditions. Even RIAA's own expert Dr. Nagle agreed that rates for webcasting should be based on economically significant webcasters (and should not be based, for example, on agreements with companies that have proven not to be viable). Of the 26 statutory licensees, Dr. Nagle believes that only 'is economically significant.[93]

[93] Nagle, Transcript at 2562-2563, 2642-2643, 2648.

Thus while RIAA *claims* that its fee proposal is supported by the benchmarks it has put forward, if weighted by economic significance, these purported benchmarks present little support for the percent-of-revenue / expense formula, and support a per-performance fee only of the fee they propose.

E. Comparability

Finally, many of the purported RIAA benchmarks are not appropriate for this proceeding because the licensees and the economic and business circumstances in which they operate are different from the licensees seeking the statutory license in this proceeding. At the most basic level, many of the licensees are not primarily in the business of

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streaming; they sought the streaming license as a means to the end of other, non-statutory licenses, or they paid little attention to the terms of the streaming license because it was unimportant to their business.[96]

As discussed above, many licensees were primarily interested in interactive licenses or other deals that they thought would be facilitated by having an RIAA agreement. [[

]]* The only entity among the 26 purported benchmark licensees whose sole business is internet streaming, and is currently operating, is

[96] See, for example.

[97] See [[ ).]]

[98] See :

with a single channel of streaming audio; and appears to have made only trivial royalty payments under its agreements. Thus, even putting aside issues of reasonableness and significance, RIAA simply has not put forward a benchmark that is comparable to the licensees before the Panel.

F. Overall assessment

Considering the information about RIAA's proffered agreements as a whole, I find that RIAA has failed totally to provide benchmarks that justify its fee proposal as consistent with the willing buyer/willing seller standard. In many cases – and in all cases where economically significant royalties have actually been paid – there are significant indications that the transaction does not represent competitive market conditions, because the licensee did not have good information, could not wait for the alternative of the CARP, was primarily interested in getting things other than the statutory rights, or viewed the legal cost of getting the reasonable statutory rate as too high to be worthwhile. Thus while these transactions were "voluntary" in some sense, they do not meet the willing buyer/willing seller standard of the statute.

Even putting aside, however, the evidence that the transactions do not represent reasonable fees, the experience under these agreements simply does not provide justification for the fee proposal that RIAA has actually put forward in this proceeding. That proposal has three components that interact in a complex way. The three components are: 15% of revenue, 5% of operating expense, and $.004 per performance. I consider in turn whether there is economically meaningful support for each of these elements that actually appears in the RIAA benchmarks.

There is no economically significant support in these agreements for royalties based on 15% of revenue, or indeed for any royalty based on revenue. No licensee has paid non-trivial royalties derived as a percentage of revenue. Given the nascent stage of the industry and the status of these licensees, there is no evidence that any of the voluntary licensees ever expected to pay royalties based on revenue. The appearance of the words "15% of revenue" in the contracts is of no economic significance if the parties knew that royalties would not be paid under this formula (because of an alternative minimum fee, for example). The proffered agreements do not provide any evidence that any of the voluntary licensees actually believed that a royalty equal to 15% of revenue is a reasonable royalty. Thus the revenue-based royalty component of the RIAA proposal stands without any evidence that buyers were ever willing to pay it.

It appears that there may be one licensee who paid a non-trivial royalty on the basis of 5% of expenses , . But RIAA itself puts forward the expense-based royalty only as a backup to the revenue royalty to ensure that the royalties will be reasonable even if the licensee has little or no revenue. That objective is achieved automatically by a reasonable performance-based fee. Thus if the fee model contains a reasonable performance-based fee, the royalty based on expenses serves no economic function.

Non-trivial royalties have been paid on a per-performance basis. As noted above, however, the royalties that have been paid do *not* support the per-performance fee that RIAA has actually proposed. The overwhelming bulk of the royalties actually paid on a per-performance basis were paid on the basis of per performance, not $.004.

Finally, non-trivial royalties have apparently been paid on essentially a lump-sum basis

But, again, there is no connection between these royalty amounts and the RIAA proposal in this proceeding. There is no basis for an inference that the payment of these amounts somehow demonstrates the reasonableness of 15% of revenue or $.004 per song, since the payments were not made on those bases.

I began this section with the suggestion that the fact that the RIAA's proposed rate is inconsistent with competitive market evidence creates a strong presumption that the agreements it has proffered are the result of market power rather than competition. Analysis of the circumstances surrounding the agreements provides ample support for that proposition.

There is certainly an intuitive attraction to using market transactions for the right in question as a benchmark for the statutory rates and terms. But even putting aside the evidence of market power, it is striking the extent to which the rates and terms proposed by RIAA for statutory licensees are not, in fact, the rates and terms supported by its own benchmark. The RIAA proposal bears cosmetic similarity to some of the agreements that have been reached. But the core elements of that proposal are not, in fact, supported by the economic activity that has occurred in connection with those agreements.

VII. IRRELEVANCE OF THE TESTIMONY OF DR. NAGLE TO WILLING BUYER/WILLING SELLER VALUATION

Dr. Nagle presents an analysis in which he purports to estimate the maximum amount that a "viable"webcaster would be willing to pay for the right of public performance of sound recordings on the internet. As explained below, he makes serious errors in these calculations. But even putting these errors aside, the exercise of estimating the buyers' maximum willingness to pay for the right has only limited relevance to the willing buyer/willing seller value. By definition, the *maximum* willingness to pay of the buyer would be extracted only by a *monopolist* seller. That is, in real market transactions, the only way, conceptually, that a licensor could achieve a royalty at the level calculated by Dr. Nagle would be if that licensor had a monopoly on the right in question.

For the reasons explained in my direct testimony, and as supported by the one of RIAA's experts, the economically appropriate interpretation of the willing buyer/willing seller test is that it corresponds to a *competitive* market rate, not the rate that would be extracted by a monopolist.99 The monopolist rate will always be higher than the competitive rate. Further; the monopoly rate will be much higher than the competitive rate if the demand for the good in question is highly "inelastic." Because most streamers have no alternative to securing a blanket license for the sound recording performing right, their demand is highly inelastic, and the monopoly rate is likely to be far in excess of the competitive rate.[100]

The maximum willingness to pay of the buyer does have some relevance to the competitive, willing buyer/willing seller rate: it is the starting point or "upper bound" rate with which the buyer would enter the negotiations. This bears on the willing buyer/willing seller test only insofar as it establishes, in principle, the reservation or walk-away rate for the licensees. We know only that the willing buyer/willing seller rate could never exceed this level. As discussed above, a similar analysis can

99 Wildman, Transcript at 3474-3475.

100 Dr. Nagle notes that a premise of his model is that webcasters do not have an economically viable alternative to an RIAA license. Nagle, Transcript at 2608.

be done for the seller, and the zero incremental cost tells us that the lower bound for the rate is zero. Dr. Nagle's analysis is totally unhelpful in determining where, in the range between these two points, a willing buyer and a (competitive)willing seller would end up.

Although Dr. Nagle's analysis does not tell us where in the range between the seller's walk-away point (zero)and the buyer's walk-away point (the maximal value calculated by Dr. Nagle) the two parties would come to agreement, his analysis is useful for illustrating that the costs of the seller do not enter in any way into this analysis. It is only the buyer's valuation, and the give-and-take of negotiation, that determine the share of that value passed to the seller, which affects the outcome. This is why the willing buyer/willing seller valuation for the sound recording ought to be similar to that of the musical work: they are both nothing more than some negotiated fraction of the value to the buyer of making public performances.[101]

Even on its own terms, Dr. Nagle's analysis is conceptually flawed. In particular, while Dr. Nagle states that many – if not most – streamers will fail, he does not consider this highly risky environment when selecting the rate of return that the successful streamers will expect to earn.[102] Economics tells us that the *expected* or average return for an

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[101] As discussed above and in my direct testimony, this approximate equality holds only before adjustment for promotion and displacement. After adjustment, the sound recording performance right is worth less than the musical work right because of greater promotional value for the sound recording.

[102] Nagle, Transcript at 2706, 2765-2766.

uncertain venture must be as great as the market return on capital.[103] If everyone understands that 80% of the people who play this game will lose – and hence earn zero or, more likely, negative returns – the returns for those who succeed have to be very high in order for the average or expected return to be acceptable to investors. If the reality were "there is an 80% chance you will lose your shirt, and a 20% chance you will earn the same return that is earned in a typical (much less risky) business," no one would enter.

Dr. Nagle's analysis is based on the maximum amount a "viable" webcaster would be willing to pay. It is difficult, however, to understand how the model presents information that is relevant to the Panel's task of determining reasonable fees for particular time periods. Dr. Nagle determines the RIAA fee based on the profitability of a viable webcaster; the profitability is determined, in turn, by the number of unique listeners. But Dr. Nagle does not know the number of unique listeners that any webcaster has or will be able to attract. The figure he uses for number of unique listeners is the result of "backing into" the number of listeners needed for profitability, rather than determining whether a

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[103] Under some circumstances, the expected return on risky investments would have to *exceed* the expected return on less risky investments, in order to compensate investors for bearing risk. This risk premium would apply if the investors were risk-averse and unable to eliminate the consequences of risk through diversification. In criticizing Dr. Nagle's analysis, I am *not* assuming such a risk premium, which would further increase the required return, and hence decrease the rate Dr. Nagle's hypothetical webcaster would be willing to pay for performance rights.

webcaster would be able to attract that number and hence actually be profitable.[104]

Many of the assumptions that Dr. Nagle used to construct a profitable webcaster are quite inconsistent with current market conditions. As an example, Dr. Nagle assumes that the theoretical viable webcaster will sell audio ads at $30 CPM, selling about 60% of its inventory. Current industry conditions are quite different.[105]

VIII. SIGNIFICANCE OF BROADCASTER/WEBCASTER PROJECTIONS

The financial and business plan projections made by the broadcasters and webcasters do not have any direct relevance to determining the willing buyer/willing seller valuation of the sound recording internet performance right. First, to the extent that they bear on valuation at all, they would be relevant only to the maximum willingness to pay, which cannot be related to the competitive-market, willing buyer/willing seller valuation unless one can determine what share of this maximal valuation the competitive market would convey to the holders of rights in the sound recording. In any event, whatever this share of value is, there is no reason why it should differ between the

[104] Nagle, Transcript at 2570. Nagle testified that, all else equal, his model will yield lower royalties, the lower the number of unique listeners. Nagle, Transcript at 2734.

[105] For example, Michael Wise of NetRadio testified that audio ads were in the range of
Wise, Transcript at 4208-4209. Other webcasters testified that audio ads were in the range of $4 to $20. Moore, Transcript at 7520; Jeffrey, Transcript at 8201; Porteus, Transcript at 4597.

sound recording and the musical work. Since we have direct evidence of the willing buyer/willing seller valuation of the musical work, this provides a much more direct route to the willing buyer/willing seller valuation of the sound recording.

Second, even as to this maximal value, these projections can inform us about what that value might be in the future, but they cannot inform us as to what the value is during the 1998-2002 period. In a competitive market, these future valuations would affect royalties today only if the royalty agreements were for long durations. But the statutory framework explicitly adopted relatively short valuation periods precisely so the Panel could avoid having to gaze into the future. A competitive market valuation for rights being conveyed for a short duration would relate only to valuations of those rights during the period of the rights transfer.

Finally, even as to future market conditions, the projections that were produced do not tell any consistent story. The projections are very difficult to compare one to another, and they have been subject to drastic revision even over very short time periods.[106] Hence, it is not possible,

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106 For example, [!

on the basis of these projections, to say anything about what the "typical"webcaster will look like at some point in the future, let alone before the end of 2002.

One conclusion that does emerge from the projections that were produced is that expectations about the ultimate profitability of the streaming business were generally revised downward over the time period from the fall of 2000 to the spring of 2001. (For example, [

In my view, expectations about ultimate profitability are not relevant to the willing buyer/willing seller rate for a short time period, because the competitive market rate for such a period would be based on current conditions, not future projections. The dramatic revisions of these forecasts that occurred over time periods of just a few months illustrate a further difficulty with using forecasts of future conditions for royalty determination – they are inherently volatile and hence unreliable as a royalty basis.

If the Panel does conclude, however, that the royalty should be tied somehow to such expectations, these forecasts do have one strong

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[107] SERV 00285-SERV 00352, SERV 00167-SERV 00209, SERV 00453-SERV 00504, SERV 00687-SERV 752.

implication. Any royalty based in some way on expectations of future profitability would have to be much lower for the 2000-2001 period than for the 1998-1999 period, since such expectations were clearly much lower in the later period.

IX. CONSEQUENCES OF THE RIAA FEE PROPOSAL

The RIAA fee proposal is a complex one. At first blush, it appears to offer important flexibility by allowing the licensee to choose between a fee based on the number of performances ($.004 per performance) or a fee based on the licensee's revenues (15%) and expenses (5%).But this apparent flexibility is illusory, limited by (1)the intrinsically much greater rate embedded in the performance fee, and (2)the fact that the alternative to this high rate is itself the greaterof two fees, one based on revenue, and one based on expenses.

The fact that the per-performance fee is intrinsically much greater than the percent-of-revenue fee can be seen by comparison of the RIAA proposed rate to the musical work rate. In over-the-air radio, musical work performance royalties make up approximately *3%* to 3.5%of revenue, so the RIAA proposal of 15%is between 4 and 5 times as great as the musical work rate. As described in my direct testimony, I have computed that the percent-of-revenue formula for over-the air radio on a per-performance basis is about $.00020 per performance.[108] Thus on a

[108] See Figure *3*.

per-performance basis, the RIAA rate of $.004 per performance is approximately 20 times the musical work rate, and at least 4 times greater than RIAA's own percent-of-revenue proposal.[109]

Turning to the revenue/ expense alternative, licensees who want to avoid the high per-performance fee must pay the *greater* of 15%of. revenue or 5% of expenses. Certainly, any licensee who achieves a viable business position will have to have revenues that exceed its expenses, so it is clear that for any viable business the revenue/cost alternative is really just a 15% of revenue alternative.

Because the per-performance alternative is much greater than the percent-of-revenue alternative, the only kind of licensee who might prefer the per-performance model would be one who is somehow spending a lot of money or earning a lot of revenue, but not actually making very many performances. In such a circumstance, it is very likely that the revenue has relatively little to do with the performances themselves, and RIAA's collecting this exceedingly high rate would essentially amount to its taxing other sources of value besides the performances.[110]

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[109] A similar relationship exists in comparison to musical work performance rates on the internet. The combined royalty rates of ASCAP and BMI on the internet are 3.5% of revenue. (See Section IV above).
; So in this case the RIAA revenue proposal is 4 times the musical work rate, while its per-performance proposal is 100 times the musical work rate.

[110] [[

To date, the majority of licensees have expenses that significantly exceed their revenue. In such circumstances, RIAA does not permit them to pay on the basis of percent-of-revenue. Rather, they must pay 5% of expenses, if that results in a royalty greater than 15% of revenue. RIAA justifies this "greater of" requirement by the argument that they should be entitled to minimum compensation for the use of the performance right even if the licensee has not achieved significant revenue.[111] Of course, an alternative and much more direct way to make sure that RIAA gets a royalty even if revenue is low would be to have a reasonable fee on a per-performance basis. Such a fee would accomplish exactly the objective RIAA claims to seek: to get compensation that reflects the use of sound recordings. But a reasonable per-performance fee is not part of the RIAA proposal, as evidenced by the fact that its per-performance alternative is attractive for very few licensees.

One red herring that has been raised by RIAA is the magnitude of payments for sound recordings compared to payments for other inputs, such as bandwidth.[112] RIAA seems to take it as an article of faith that the sound recording rights are the major, or a major, source of value in streaming. But this is entirely an empirical question. There is no *a priori* basis for concluding that a large part of the value of streaming is associated with the sound recording performance rights.

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[111] Direct Written Testimony of Steven M. Marks at 17-18.

[112] Opening Statement, Transcript at 89-92.

that ATH is, for many licensees, an already available indicator of listenership, it is important that an alternative based on ATH be available. This is not an issue of the level of fees, but only of making the blanket license as efficient as possible as a mechanism for securing the necessary rights. For any per-performance fee that is determined to be reasonable, an equivalent listener-hour (ATH)fee can be calculated by multiplying the per-performance fee by average or typical performances per hour.

X. EPHEMERAL ISSUES

In my direct testimony, I noted that from an economic perspective, there is no function served by charging a distinct royalty for the making of ephemeral copies, the economic purpose of which is limited to facilitating performances. In such a context, the value received by the licensee is derived from the performance. One can, if one wishes, split this performance-derived value into two pieces, and assign one piece to the performance itself, and a second piece to the right to make copies that facilitate the performance. But the sum of these two pieces should equal the reasonable royalty for the right to make performances.[113]

Since the direct testimony phase, the Copyright Office has issued a report, in connection with its reporting obligations under the Digital

[113] RIAA witness Nagle puts forth the identical economic interpretation. See Nagle, Transcript at 2632.

Millennium Copyright Act (DMCA), that confirms both this conclusion and the reasoning that I utilized in reaching the conclusion:

> "...section 112(e) can best be viewed as an aberration...Nor did we 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."[114]

Note that I am *not* arguing that there is never independent value in different uses of a given piece of intellectual property. For example, in the case of jukeboxes, a Copyright Royalty Tribunal reasoned, correctly, that the fact that a mechanical royalty is paid to musical work rights holders when their songs are reproduced on CDs does not obviate the need for payment of a reasonable royalty when such a CD is performed publicly on a jukebox.[115] What distinguishes that situation from the current one is that, unlike ephemeral copies, the CD copy has a clear economic value that is independent of its use in making public performances in a jukebox. Further, the use of the CD to make public performances clearly creates value that is not associated with most CDs, and which could not reasonably be expected to be captured in the mechanical royalty paid when the CD is created. What makes the ephemeral copies somewhat unusual, and leads to the conclusion that there can be no economically sensible royalty for ephemeral copies that

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[114] See Jaffe Rebuttal Exhibit 6, DMCA Section 104 Report, U.S. Copyright Office, August 2001, at 144, fn. 434.

[115] See Jaffe Rebuttal Exhibit 7, Final Rule of the Copyright Royalty Tribunal, 46 Fed. Reg. 884, 889, Docket No. CRT 80-1 (January 5, 1981).

is in addition to the reasonable royalty for performances, is the fact that the ephemeral copy serves no economic function other than facilitating performances.

The conclusion that there is no independent value that can be attached to ephemeral copies does not depend on the number of such copies being technologically determined, with no flexibility available to streamers with respect to the number of such copies made. It is my understanding, based on the testimony of Professor Zittrain, that a major reason that multiple ephemeral copies are made is to allow streaming of music in different formats to accommodate potential users with different software or at different rates to accommodate potential users with different modem speeds.[116] Clearly, by making the stream available in different formats or at different speeds needed by different users, these copies increase the number of performances that occur. The economic consequence of fewer such copies would be fewer performances. *So* again, the creation of these copies serves to create value by increasing the number of performances. The appropriate measure of this value is the reasonable performance royalty, and under my proposed performance-based model, increased royalties would be paid as a result of the increased performances.

[116] Zittrain, Transcript at 6037-6045.

The making of ephemeral copies by the services frequently results in other benefits to copyright owners. For instance, Douglas Talley testified to the security benefits enabled by the use of buffer and cache copies in encrypting/decrypting and encoding/decoding data. The sound recording owners likewise benefit from the increased sound quality enabled by the use of ephemeral copies.[117]

Finally, I note that minimum fees are mentioned by the statute in both Section 112 and 114. As discussed above, however, the economic justification for a minimum fee is to ensure that the incremental costs of servicing a licensee are covered by that licensee's royalty payments. I see no reason why the cost of servicing a licensee with both section 112 and 114 licenses would differ from servicing a licensee with only a 114 license. Hence there is no economic justification for distinct minimum fees for the two rights being licensed.

[117] Talley, Transcript at 8649.

I hereby declare under penalty of perjury under the laws of the United States that the foregoing testimony is true and correct to the best of my knowledge, information and belief.

Adam B. Jaffe

Executed this 3rd day of October, 2001.

ASCAP EXPERIMENTAL LICENSE AGREEMENT FOR INTERNET SITES ON THE WORLD WIDE WEB – RELEASE [illegible]

1. **Parties:** This is an agreement between the American Society of Composers, Authors and Publishers ("We," "Us" or "ASCAP"), located at One Lincoln Plaza, New York, New York **10023** and

_______________________________________ ("You" or "Licensee'?, located at
Licensee Name

____
Street Address or PO **Box** City State ZIP Code

2. **Experimental Agreement:** This is an experimental agreement which applies for its term only and is entered into without prejudice to any position you or we may take for any period subsequent to its termination.

3. **Definitions:**

(a) Your **"Web Site"** is the Internet site on the World Wide Web generally known as

____

with the principal Universal Resource Locator (URL) of:

http://_______________________________

(b) **"Web Site Transmissions"** are all transmissions of content to Web Site Users from or through your Web Site, or fiom any other web site pursuant to an agreement between you and the operator of the other web site, when accessed by means of any connection from your Web Site.

(c) **"Web Site Users"** are all those who access Web Site Transmissions.

(d) Our **"Repertory"** consists of all copyrighted musical compositions written or published by our members or by the members of affiliated foreign performing rights societies, including compositions written or published during the term of this agreement, and of which we have the right to license nondramatic public performances.

4. **Grant of License:** We grant you a license to publicly perform, by means of Web Site Transmissions, non-dramatic renditions of the separate musical compositions in our Repertory.

5. **Term of License:** The license granted by this agreement commences on ____________ (the "Effective Date"), and ends on December 31 of the same calendar year, and continues after that for additional terms of one year each unless you or we terminate it by giving the other party notice at least thirty days prior to the end of a calendar year.

6. **Limitations on License:**

(a) This license extends only to you and your Web Site and is limited to performances presented by means of Web Site Transmissions, and by no other means; provided, however, that (i) nothing in this agreement authorizes such performances when transmitted from your Web Site pursuant to an agreement between you and any other web site operator, when accessed by means of a connection from that other web site, even if such performances fall within the definition of Web Site Transmissions; and provided further, that (ii) if you are an Internet access provider, nothing in this agreement authorizes such performances when transmitted from or through any homepage(s) hosted on your Web Site for those for whom you provide the service of Internet access.

(b) This license may not be assigned without our written consent.

(c) This license is limited to the United States, its territories and possessions, and the Commonwealth of Puerto Rico.

(d) Nothing in this agreement grants you, or authorizes you to grant to any Web Site User, or to anyone else, any right to reproduce, copy or distribute by any means, method or process whatsoever, any of the musical compositions licensed by this agreement, including, but not limited to, transferring or downloading any such musical composition to a computer hard drive, or otherwise copying the composition onto any other storage medium.

(e) Nothing in this agreement grants you, or authorizes you to grant to anyone else, any right to reproduce, copy, distribute or perform publicly by any means, method or process whatsoever, any sound recording embodying any of the musical compositions licensed under this agreement.

(f) Nothing in this agreement grants, or authorizes you to grant, to any Web Site User, or to anyone else, any right to perform publicly by any means, method or process whatsoever, any of the musical compositions licensed under this agreement, including, but not limited to, any transmission, retransmission, or further transmission of any of those compositions.

(g) This license is limited to non-dramatic performances, and does not authorize any dramatic performances; nor does it extend to or include the public performance of any opera, operetta, musical comedy, play, or like production, as such, in whole or in part.

7. License Fees: For each year during the term of this agreement you agree to pay us the license fee calculated in accordance with the Rate Schedules applicable for that year.

8. Rate Schedules: There are three alternative Rate Schedules, (Schedules "A," "B" and "C,") attached to and made a part of this agreement. For each year, you may choose any one of the three rate schedules we offer and for which you can provide the required information, using either your own technology, or technology supplied by an industry acknowledged technology company.

9. Reports and Payments: You agree to furnish license fee reports and payments to us as follows:

(a) Initial License Fee Report. Upon entering into this agreement, you will submit an Initial License Fee Report based on a good faith estimate of either "Web Site Revenue" or "Web Site Sessions" for the period from the Effective Date of this agreement until December 31 of the year in which this agreement is executed.

(b) Annual License Fee Reports. You will submit an Annual License Fee Report for each year of this agreement, by the first day of April of the following year on the Report Form we will provide you free of charge.

(c) License Fee Payments. You will submit license fee payments quarterly on or before January 1, April 1, July 1 and October 1 of each year. Each such payment shall be equal to one-fourth of the license fee for the preceding calendar year; provided, however, that in any year for which your estimated license fee is less than $1,000, you will submit payments of $250 each, or the balance of the license fee due for that year, whichever is less.

(d) Late Report Payments. If we do not receive your Annual License Fee Report when due, you will submit quarterly license fee payments that are 24% higher than the quarterly payments due for the preceding year, and payments will continue at that increased rate until we receive the late report.

(e) Annual Adjustment. With each Annual License Fee Report you will submit payment of any license fees due over and above all amounts that you paid for the year to which the report pertains. If the fee due is less than the amount you paid, we will apply the excess to the next quarterly payment due under this agreement. If the excess is greater than one quarterly payment, we will refund the excess over and above the amount of one quarterly payment to you at your written request.

(f) Late Payment Charge. You will pay a finance charge of 1-1/2% per month, or the maximum rate permitted by state law, whichever is less, from the date due, on any required payment that is not made within thirty days of its due date.

(g) Music Use Reports. You agree to provide us with reports regarding the musical compositions contained in your Web Site Transmissions. If the annual license fee payable to ASCAP is less than $10,000, you will submit such reports for the first three days of each calendar quarter. If the annual license fee payable to ASCAP is $10,000 or greater, you will submit such reports for at least one week in each calendar quarter, for which we will request in writing and send it to you at least thirty days prior to commencement of the period to be covered by the report. Your reports will be in the form we provide, and will contain the information specified by us.

10. Report **Verification:**

(a) We have the right to examine your books and records, and you agree to obtain for us the right to examine the books and records of any partner in, or co-publisher of, your Web Site, in order to verify any required report. We may exercise this right by giving you thirty days notice of our intention to conduct an examination. We will consider all data and information derived from our examination as completely confidential. You agree to furnish all pertinent books and records, including electronic records, to our authorized representatives, during customary business hours.

(b) If our examination shows that you underpaid license fees, you agree to pay a finance charge of 1-1/2% one month, or the maximum rate permitted by state law, whichever is less, on the license fees due from the date we bill you for that amount or, if the underpayment is 5% or more, from the date or dates that the license fees should have been paid.

(c) You may dispute all or part of our claim for additional fees. You may do so by advising us in writing within thirty days from the date we bill the additional fees to you of the basis for your dispute, and by paying the undisputed portion of our claim with the applicable finance charges. If there is a good faith dispute between us concerning all or part of our claim, we will defer finance charges on the disputed amount until sixty days after we have responded to you, and will pro-rate finance charges based on our resolution of the dispute.

11. **Breach or Default:** If you fail to perform any of the terms or conditions required of you by this agreement, we may terminate your license by giving you thirty days notice to cure your breach or default. If you do not do so within that thirty day period, your license will automatically terminate at the end of that period without any further notice from us.

12. **Interference with ASCAP's Operations:** We have the right to terminate this license effective immediately, if there is any major interference with, or substantial increase in the cost of, our operation as a result of any law in the state, territory, dependency, possession or political subdivision in which you or your Web Site is located which is applicable to the licensing of performing rights.

13. **Indemnification:** We will indemnify you from any claim made against you with respect to the non-dramatic performance licensed under this agreement of any composition(s) in our Repertory, and will have full charge of the defense against the claim. You agree to notify us immediately of any such claim, furnish us with all the papers pertaining to it, and cooperate fully with us in its defense. If you wish, you may engage your own counsel, at your expense, who may participate in the defense. Our liability under this paragraph is strictly limited to the amount of license fees that you actually paid us under this agreement for the calendar year(s) in which the performance(s) which are the subject of the claim occurred.

14. **Covenant Not to Sue:**

(a) ASCAP, on its own behalf and on behalf of our members, covenants not to make any claim against you for unauthorized public performances of any of our members' compositions in our Repertory which would have been licensed under this agreement except for the limitation set forth in subparagraph 6(a)(i), provided that the agreement between you and the operator of the other web site referred to in subparagraph 6(a)(i) expressly requires that the operator of the other web site obtain needed authorization for performances of copyrighted musical compositions on or through its web site, and provided further, that within 24 hours of receipt of notice from us that the operator of the other web site does not have such needed authorization, you will remove or block the connection from that other web site to your Web Site.

(b) ASCAP, on its own behalf and on behalf of our members, covenants not to make any claim against you for unauthorized public performances of any of our members' compositions in our Repertory which would have been licensed under this agreement except for the limitation set forth in subparagraph 6(a)(ii), provided that the agreement between you and the owner of the homepage referred to in subparagraph 6(a)(ii) expressly requires that that owner obtain needed authorization for performances of copyrighted musical compositions on or through its homepage, and provided further, that within 24 hours of receipt of notice from us that the owner of the homepage does not have such needed authorization, you will remove that homepage from your Web Site.

15. **Notices:** We or you may give any notice required by this agreement by sending the notice to the other party's last known address by United States Mail or by generally recognized same-day or overnight delivery service. We each agree to inform the other in writing of any change of address.

16. **Governing Law:** This agreement will be governed by and construed in accordance with the laws of the state of New York

17. **Entire Agreement:** This agreement constitutes the entire agreement between you and ASCAP, and may only be modified, or any rights under this agreement may be waived, by a written document executed by both you and ASCAP.

IN WITNESS WHEREOF, this Agreement has been duly executed by ASCAP and Licensee this _____ day of ____________, 20________

AMERICAN SOCIETY OF COMPOSERS, *AUTHORS AND* PUBLISHERS By ______________________________ ______________________________ Title	______________________________ Licensee Name By ______________________________ Signature ______________________________ Print *Your* Name ______________________________ Title (Fill in capacity in which signed: (a) If corporation, state corporate office held; *(b)* If partnership, write word "partner" under printed name of signing partner; (c) If individual owner, write "individual owner" under printed name.)

RATE SCHEDULE "A"

REPORT FORM
ASCAP EXPERIMENTAL LICENSE AGREEMENT FOR INTERNET SITES ON THE WORLD WIDE WEB - RELEASE 3.0

PART I. ACCOUNT INFORMATION

REPORT PERIOD:____________ THRU 12/31/_____

LICENSEE NAME:____

POSTAL ADDRESS:____

WEB SITE URL: http://__________________________ E-MAIL:____________________

FACSIMILE NUMBER:____________________ PHONE NUMBER:________________

PART 11. DEFINITIONS

(a) The terms **"Web Site," "Web Site Transmissions"** and **"Web Site Users"** are defined in subparagraphs 3(a), (b) and (c) of the license agreement.

(b) **"Sponsor Revenue"** means all payments made by or on behalf of sponsors, advertisers, program suppliers, content providers, or others for use of the facilities of your Web Site including, but not limited to, payments associated with syndicated selling, on-line franchising and associates programs. **"Sponsor Revenue"** also means all payments from whatever source derived upon your sale or other disposition of goods or services you received as barter for use of the facilities of your Web Site including, but not limited to, payments for the sale of advertising time or space.

(c) **"Adjustment to Sponsor Revenue"** means advertising agency commissions not to exceed 15% actually allowed to an advertising agency that has no direct or indirect ownership or managerial connection with you or your Web Site.

(d) **"Web Site User Revenue"** means all payments made by or on behalf of Web Site Users to access Web Site Transmissions including, but not limited to, subscriber fees, connect time charges, and any other access fees.

(e) **"Web Site Revenue"** includes all specified payments and expenditures whether made directly to you or to any entity under the same or substantially the same ownership, management or control as you, or to any other person, firm or corporation including, but not limited to, any partner or co-publisher of your Web Site, pursuant to an agreement or as directed or authorized by you or any of your agents or employees.

(f) "Web Session Value" is the value derived from the number of Web Sessions that a Web Site generates.

(g) "Web Site Sessions" are the total number of periods that begin when a Web Site User first accesses any Web Site Transmission and end when that Web Site User has not accessed any Web Site Transmission within 10 minutes.

PART III. REVENUE BASED
LICENSE FEE CALCULATION FOR RATE SCHEDULE "A"

NET SPONSOR REVENUE

1. Sponsor Revenue .... $_____
2. Adjustment to Sponsor Revenue .... $_____
3. Net Sponsor Revenue (subtract line 2 from line 1) .... $_____

WEB SITE REVENUE

4. Web Site User Revenue .... $_____
5. Net Sponsor Revenue (from line 3) .... $_____
6. Web Site Revenue (add lines 4 and 5) .... $_____
7. Rate Based on Revenue .... x .01615
8. Revenue Based License Fee (multiply line 6 by line 7) .... $_____

PART IV. WEB SESSION BASED
LICENSE FEE CALCULATION FOR RATE SCHEDULE "A"

WEB SESSION VALUE

9. Web Site Sessions .... _____
10. Rate Based on Web Sessions .... x $ .00048
11. Web Session Based Licensee Fee (multiply line 9 by line 10) .... $_____

PART V. LICENSE FEE CALCULATION FOR RATE SCHEDULE "A"

12. Licensee Fee (enter line 8, line 11, or Maximum License Fee, if applicable,* whichever is greater) .... $_____
13. Minimum License Fee .... $ 264.00
14. LICENSE FEE DUE (enter amount from line 12 or line 13, whichever is greater) .... $_____

PART VI. CERTIFICATION

We certify that this report is true and correct and that all books and records necessary to verify this report are now and will continue to be available for your examination in accordance with the terms of the license agreement.

____________________ ____________________
Signature Date

____
Print Name and Title

* If Web Site Revenue exceeds $19,000,000.00 per year, or if you choose not to report Web Site Revenue or Web Session Value, your annual Maximum License Fee is 5300.000.00.

RATE SCHEDULE "B"

REPORT FORM
ASCAP EXPERIMENTAL LICENSE AGREEMENT FOR INTERNET SITES ON THE WORLD WIDE WEB-RELEASE 3.0

PART I. ACCOUNT INFORMATION

REPORT PERIOD: ____________ THRU 12/31/______

LICENSEE NAME:____

POSTAL ADDRESS:____

WEB SITE URL: http://__________________________ E-MAIL:__________________

FACSIMILE NUMBER:____________________ PHONE NUMBER:__________________

PART II. DEFINITIONS

(a) The terms **"Web Site," "Web Site Transmissions"** and **"Web Site Users"** are defined in subparagraphs 3(a), (b) and (c) of the license agreement.

(b) **"Sponsor Revenue"** means all payments made by or on behalf of sponsors, advertisers, program suppliers, content providers, or others for use of the facilities of your Web Site including, but not limited to, payments associated with syndicated selling, on-line franchising and associates programs. **"Sponsor Revenue"** also means all payments from whatever source derived upon your sale or other disposition of goods or services you received as barter for use of the facilities of your Web Site including, but not limited to, payments for the sale of advertising time or space.

(c) **"Adjustment to Sponsor Revenue"** means advertising agency commissions not to exceed **15%** actually allowed to an advertising agency that has no direct or indirect ownership or managerial connection with you or your Web Site.

(d) **"Web Site User Revenue"** means all payments made by or on behalf of Web Site Users to access Web Site Transmissions including, but not limited to, subscriber fees, connect time charges, and any other access fees.

(e) **"Web Site Revenue"** includes all specified payments and expenditures whether made directly to you or to any entity under the same or substantially the same ownership, management or control as you, or to any other person, firm or corporation including, but not limited to, any partner or co-publisher of your Web Site, pursuant to an agreement or as directed or authorized by you or any of your agents or employees.

(f) "Web Site Sessions" are the total number of periods that begin when a Web Site User first accesses any Web Site Transmission and end when that Web Site User has not accessed any Web Site Transmission within 10 minutes.

(g) "Music Sessions" are the number of Web Site Sessions in which Web Site Users access any performance(s) of music.

(h) "Web Session Value" is the value derived from the number of Web Sessions that a Web Site generates.

PART III. REVENUE BASED
LICENSE FEE CALCULATION FOR RATE SCHEDULE "B"

NET SPONSOR REVENUE

1. Sponsor Revenue .... $__________
2. Adjustment to Sponsor Revenue .... $__________
3. Net Sponsor Revenue (subtract line 2 from line 1) .... $__________

WEB SITE REVENUE

4. Web Site User Revenue .... $__________
5. Net Sponsor Revenue (from line 3) .... $__________
6. Web Site Revenue (add lines 4 and 5) .... $__________

VALUE ATTIUBUTABLE TO PERFORMANCES OF MUSIC

7. Web Site Sessions .... __________
8. Music Sessions .... __________
9. Ratio (divide line 8 by line 7) (to 3 decimals) .... __________
10. Web Site Revenue (from line 6) .... $__________
11. Value Attributable to Performances of Music (multiply line 9 by line 10) .... $__________
12. Rate Based on Revenue .... x .0242
13. Revenue Based License Fee (multiply line 11 by line 12) .... $__________

PART IV. WEB SESSION BASED
LICENSE FEE CALCULATION FOR RATE SCHEDULE "B"

WEB SESSION VALUE

14. Web Site Sessions (from line 7) .... __________
15. Music Sessions (from line 8) .... __________
16. Rate Based on Web Sessions .... x $ .00073
17. Web Session Based Licensee Fee (multiply line 15 by line 16) .... $__________

PART V. LICENSE FEE CALCULATION FOR RATE SCHEDULE "B"

18. Licensee Fee (enter line 13, line 17, or Maximum License Fee, if applicable,* whichever is greater) .... $__________
19. Minimum License Fee .... $ 264.00
20. LICENSE FEE DUE (enter mount from line 18 or line 19, whichever is greater) .... $__________

* If Web Site Revenue exceeds $19,000,000.00 per year, or if you choose not to report Web Site Revenue or Web Session Value, your annual Maximum License Fee is $300,000.00.

PART VI. CERTIFICATION

We certify that this report is true and correct and that all books and records necessary to verify this report are now and will continue to be available for your examination in accordance with the terms of the license agreement.

Signature

Date

Print Name and Title

RATE SCHEDULE "C"

REPORT FORM
ASCAP EXPERIMENTAL LICENSE AGREEMENT FOR INTERNET SITES ON THE WORLD WIDE WEB – RELEASE 3.0

PART I. ACCOUNT INFORMATION

REPORT PERIOD: ____________ THRU 12/31/_____

LICENSEE NAME:____

POSTAL ADDRESS:____

WEB SITE URL: http://__________________________ E-MAIL:__________________

FACSIMILE NUMBER:____________________ PHONE NUMBER:__________________

PART II. DEFINITIONS

(a) The terms **"Web Site," "Web Site Transmissions"** and **"Web Site Users"** are defined in subparagraphs 3(a), (b) and (c) of the license agreement.

(b) **"Sponsor Revenue"** means all payments made by or on behalf of sponsors, advertisers, program suppliers, content providers, or others for use of the facilities of your Web Site including, but not limited to, payments associated with syndicated selling, on-line franchising and associates programs. **"Sponsor Revenue"** also means all payments fiom whatever source derived upon your sale or other disposition of goods or services you received as barter for use of the facilities of your Web Site including, but not limited to, payments for the sale of advertising time or space.

(c) **"Adjustment to Sponsor Revenue"** means advertising agency commissions not to exceed **15%** actually allowed to an advertising agency that has no direct or indirect ownership or managerial connection with you or your Web Site.

(d) **"Web Site User Revenue"** means all payments made by or on behalf of Web Site Users to access Web Site Transmissions including, but not limited to, subscriber fees, connect time charges, and any other access fees.

(e) **"Web Site Revenue"** includes all specified payments and expenditures whether made directly to you or to any entity under the same or substantially the same ownership, management or control as you, or to any other person, fim or corporation including, but not limited to, any partner or co-publisher of your Web Site, pursuant to an agreement or as directed or authorized by you or any of your agents or employees.

(f) "Web Site Sessions" are the total number of periods that begin when a Web Site User first accesses any Web Site Transmission and end when that Web Site User has not accessed any Web Site Transmission within 10 minutes.

(g) "Music Sessions" are the number of Web Site Sessions in which Web Site Users access any performance(s) of music.

(h) "Web Session Value" is the value derived from the number of Web Sessions that a Web Site generates.

(i) "Performances of Music" are the total number of performances of all musical works contained in Web Site Transmissions.

(j) "Performances of ASCAP Music" are the number of Performances of Music which are of musical works in the ASCAP repertory not otherwise licensed.

PART III. REVENUE BASED
LICENSE FEE CALCULATION FOR RATE SCHEDULE "C"

NET SPONSOR REVENUE

1.	Sponsor Revenue	$______
2.	Adjustment to Sponsor Revenue	$______
3.	Net Sponsor Revenue (subtract line 2 from line 1)	$______

WEB SITE REVENUE

4.	Web Site User Revenue	$______
5.	Net Sponsor Revenue (fiom line 3)	$______
6.	Web Site Revenue (add lines 4 and 5)	$______

VALUE ATTRIBUTABLE TO PERFORMANCES OF MUSIC

7.	Web Site Sessions	______
a.	Music Sessions	______
9.	Ratio (divide line 8 by line 7) (to 3 decimals)	______
10.	Web Site Revenue (from line 6)	$______
11.	Value Attributable to Performances of Music (multiply line 9 by line 10)	$______

VALUE ATTRIBUTED TO PERFORMANCES OF ASCAP MUSIC

12.	Performances of Music	______
13.	Performances of ASCAP Music	______
14.	Ratio (divide line 13 by line 12) (to 3 decimals)	______
15.	Value Attributable to Performances of Music (from line 11)	$______
16.	Value Attributable to Performances of ASCAP Music (multiply line 14 by line 15)	$______
17.	Rate Based on Revenue	x .0446
18.	Revenue Based License Fee (multiply line 16 by line 17)	$______

PART IV. WEB SESSION BASED
LICENSE FEE CALCULATION FOR RATE SCHEDULE "C"

WEB SESSION VALUE

19.	Web Site Sessions (fiom line 7)	______
20.	Music Sessions (from line 8)	______

21. Performances of Music (from line 12) .... ______

22. Performances of ASCAP Music (from line 13) .... ______

23. Ratio (divide line 22 by line 21) .... ______

24. Sessions Attributable to Performances of ASCAP Music (multiply line 20 by line 23) .... ______

25. Rate Based on Web Sessions .... x $ .00134

26. Web Session Based Licensee Fee (multiply line 24 by line 25) ________ $______

PART V. LICENSE FEE CALCULATION FOR RATE SCHEDULE "C"

27. Licensee Fee (enter line 18, line 26, or Maximum License Fee, if applicable,* whichever is greater) .... $______

28. Minimum License Fee .... $ 264.00

29. LICENSE FEE DUE (enter amount from line 27 or line 28, whichever is greater) .... $______

PART VI. CERTIFICATION

We certify that this report is true and correct and that all books and records necessary to verify this report are now and will continue to be available for your examination in accordance with the terms of the license agreement.

______________________ ______________________

Signature Date

____

Print Name and Title

* If Web Site Revenue exceeds $19.000.000.00per year, or if you choose not to report Web Site Revenue or Web Session Value, your annual Maximum License Fee is $300,000.00.

Jaffe Rebuttal Exh.1B

BMI

http://www.bmi.com

INTERNET-01

WEB SITE
MUSIC PERFORMANCE AGREEMENT

AGREEMENT, made on ____________________, 200_, by and between BROADCAST MUSIC, INC. ("BMI"), a New York corporation with its principal offices at 320 West 57th Street, New York, New York 10019 and ________________________________ ("LICENSEE"), a ______________________ (State)

(check one) ☐ corporation
☐ partnership
☐ limited liability company
☐ individual d/b/a __________________________ (complete if applicable)

with its principal offices at ____
____(the "Agreement").

IT IS HEREBY AGREED AS FOLLOWS:

1. Term

The Term of this Agreement shall mean the period from either January 1, 2001 or ___________ (date after January 1, 2001 on which audio was launched), whichever is later, through December 31, 2003 and continuing on a year-to-year basis thereafter. Either party may terminate the Agreement upon 60 days' prior written notice at the end of December of any year beginning with December 31, 2003. BMI shall have the right to cancel this Agreement along with the simultaneous cancellation of the Agreements of all other licensees of the same class and category as LICENSEE as of the end of any month during the initial term or any subsequent renewal term, upon 60 days' prior written notice.

2. Definitions

As used in this Agreement, the following terms shall have the following respective meanings:

(a) "Allocation of Run-Of-Site Revenue" shall mean Run-Of-Site Revenue multiplied by a fraction the numerator of which is the total Music Page Impressions for the reporting period, and the denominator of which is the total Page Impressions for the reporting period. (Run-Of-Site Revenue x (total Music Page Impressions ÷ total Page Impressions))

(b) "Direct Music Area Revenue" shall mean the total of: (1) In-Stream Advertising Revenue; (2) Music Page Banner Advertising Revenue; (3) Music Subscriber Revenue; and (4) Other Music Revenue.

(c) "Gross Revenue" shall mean all revenue, including all billings on behalf of, and all payments made to, LICENSEE, or as authorized by LICENSEE, its employees, representatives, agents or any other person acting on LICENSEE's behalf, and all billings on behalf of, and payments made to, any person, company, firm or corporation under the same or substantially the same ownership, management and control as LICENSEE for: (1) access to and/or use of the Web Site or portions thereof, including online time, subscriptions, and other transactional charges (excluding revenue generated by LICENSEE for the direct sale of manufactured products), including commissions from third parties on transactions; (2) advertising (including sponsor "hot links") on the Web Site, including billings to and payments received from sponsors, less advertising agency commissions not to exceed 15% actually incurred to a recognized advertising agency not owned or controlled by LICENSEE; (3) the provision of time or space on the Web Site to any other person or company; (4) donations; (5) the fair market value of merchandise, services or any thing or service of value which LICENSEE may receive in lieu of cash consideration for the use of the Web Site (i.e. trade and barter); and (6) LICENSEE's proprietary software used to access the Web Site, or download any aspect thereof. Gross Revenue shall include such payments as set forth in (1) through (6) above to which LICENSEE is entitled but which are paid to a parent, subsidiary, or division of LICENSEE or any third party, in lieu of payment to LICENSEE, for LICENSEE's Web Site. LICENSEE may deduct from Gross Revenue any bad debts actually written off during a reporting period which are related to any billings previously reported, but shall increase Gross Revenue by any recoveries thereof.

(d) "In-Stream Advertising Revenue" shall mean that portion of Gross Revenue as defined in Paragraph 2(c)(2) and 2(c)(5) which is derived from advertising embedded in audio or audiovisual programming on the Web Site which contains music.

(e) "Music Area Revenue" shall mean Direct Music Area Revenue plus the Allocation of Run-Of-Site Revenue.

(f) "Music Page" shall mean a Web Page which presents one or more icons or hyperlinks that may be clicked on to access performances of music or at which music is played upon loading the Web Page.

(g) "Music Page Banner Advertising Revenue" shall mean that portion of Gross Revenue as defined in Paragraph 2(c)(2) and 2(c)(5) which is derived from advertisements appearing on or in connection with Music Pages or portions thereof on the Web Site.

(h) A "Music Page Impression" shall mean a transfer request for a single Music Page.

(i) "Music Subscriber Revenue" shall mean that portion of Gross Revenue as defined in Paragraph 2(c)(1) which is derived from granting access to performances of music or Music Pages or portions thereof on the Web Site.

(j) "Online Service" shall mean a commercial computer online information and/or entertainment programming packaging service including, but not limited to America Online, @Home Network, Road Runner, Microsoft Network, CompuServe and Prodigy, which offers consumers, for a fee, access to proprietary centralized databases and remote sources of audio and video programming and which may provide Internet access.

(k) "Other Music Revenue" shall mean that portion of Gross Revenue as defined in Paragraphs 2(c)(1)-(6) (other than Gross Revenue defined in Paragraphs 2(d), 2(g) and 2(i)) which is directly attributable to performances of music or Music Pages or portions thereof on the Web Site.

(l) "Page Impression" shall mean a transfer request for a single Web Page.

(m) "Run-Of-Site Revenue" shall mean that portion of Gross Revenue as defined in Paragraphs 2(c)(1)-(6) which is attributable to the entire Web Site, or any part or parts of the Web Site that include one or more Music Pages or portions thereof. Run-Of-Site Revenue shall not include Direct Music Area Revenue or other revenue derived from targeted advertising buys where an advertiser buys advertising banners or other opportunities on or in connection with, or LICENSEE charges for access to, specific Web Page(s) other than Music Page(s) or portions thereof.

(n) "Territory" shall mean the United States, its Commonwealth, territories, and possessions, and the territories represented by non-U.S. performing rights licensing organizations listed on Exhibit C as may be amended from time to time by BMI during the Term of this Agreement by adding to or deleting from the list of countries posted in the licensing section of the BMI web site located at http://www.bmi.com/. BMI will provide notice to LICENSEE (by e-mail to the address provided by LICENSEE on the profile attached hereto as such may be amended in writing by LICENSEE) of the deletion of any non-U.S. performing rights licensing organization from Exhibit C during the Term hereof.

(o) "U.S. Territory" shall mean the United States, its Commonwealth, territories, and possessions.

(p) "Web Page" shall mean a set of associated files transferred sequentially from the Web Site to, and rendered more or less simultaneously by, a browser. For purposes of this Agreement, such associated files shall include, but shall not be limited to, 'pop-up' windows that open upon accessing the Web Page as well as proprietary software 'players' that open when accessing an audio or audiovisual file associated with the Web Page.

(q) "Web Site" shall mean an Internet computer service comprising a series of interrelated Web Pages currently registered with a domain name registration service and known as ________________________ that LICENSEE produces and/or packages and then transmits or causes to be transmitted either directly or indirectly to persons who receive the service from the URL http://________________________ over the Internet by means of a personal computer or by means of another device capable of receiving Internet transmissions. LICENSEE may license additional Web Sites owned, operated and/or controlled by LICENSEE by listing such additional sites on Exhibit A hereto, and may amend Exhibit A from time to time during the Term hereof by written agreement signed by both parties. LICENSEE must comply separately with all reporting requirements and pay separate license fees under this Agreement, including Annual Minimum License Fees, for each Web Site listed on Exhibit A. References herein to Web Site shall include those additional sites listed on Exhibit A.

3. Grant of Rights

(a) BMI hereby grants to LICENSEE, for the Term, a non-exclusive license to perform publicly within the Territory (subject to Paragraph 3(b) below), in and as part of LICENSEE's Web Site transmitted or caused to be transmitted either directly or indirectly by LICENSEE over the Internet all musical works, the right to grant public performance licenses of which BMI controls. This Agreement shall only include public performances in the Territory of musical works by transmissions over the Internet received via personal computers or by means of another device capable of receiving the Internet through streaming technologies as well as those transmissions that are downloaded by persons on personal computers or otherwise, where such transmissions are accessed through the Web Site simultaneous to viewing a page on the Web Site. Public performances outside of the Territory may be subject to appropriate separate licensing. This Agreement shall not license transmissions of musical works that are accessed through a web site owned or controlled by a third party simultaneous to viewing a page on the third party's web site. This Agreement does not include dramatic rights or the right to perform dramatico-musical works in whole or in substantial part. This Agreement also does not license public performances in any commercial establishments, including, but not limited to, where all or a portion of LICENSEE's Web Site is used as a commercial music service (as that term is customarily understood in the industry); such performances of BMI music shall be subject to appropriate separate licensing.

(b) Notwithstanding the foregoing, the territorial scope of the grant of rights with respect to any musical works which are affiliated with BMI through a non-U.S. performing rights licensing organization not listed on Exhibit C hereto is limited to public performances in the U.S. Territory. Public performances of such musical works outside of the U.S. Territory may be subject to appropriate separate licensing.

(c) Nothing herein shall be construed as the grant by BMI of any license in connection with any transmission which is not part of LICENSEE's Web Site transmitted or caused to be transmitted by LICENSEE and nothing herein shall be construed as authorizing LICENSEE to grant to others (including, but not limited to, third party web sites, Online Services, cable television system operators and open video systems (acting as other than Internet service providers)) any license or right to reproduce or perform publicly by any means, method or process whatsoever, any of the musical compositions licensed hereunder.

(d) This Agreement grants only public performing rights to LICENSEE, and does not grant any reproduction, distribution, performance right in sound recordings or any other intellectual property right(s) in any musical works to any person or entity that may receive and/or download or otherwise store the transmission of musical works.

(e) In the event that all or a portion of LICENSEE's Web Site is offered for resale by a third party as a pay or premium audio or audiovisual service, or is packaged or included on a tier of services by a third party for additional revenue, either independently or with other Web Sites, LICENSEE shall immediately notify BMI in writing of any such arrangements. BMI and LICENSEE expressly agree that any such uses are not licensed under this Agreement and shall be subject to appropriate separate licensing.

4. License Fee

In consideration of the license granted herein, LICENSEE shall pay to BMI for each calendar quarter of the Term hereof a license fee in accordance with the following rate calculations at LICENSEE's option:

(a) Gross Revenue Calculation

LICENSEE shall pay to BMI 1.75% of LICENSEE's Gross Revenue generated by LICENSEE's Web Site during each quarter year of the Term according to the Payment Schedule below (Gross Revenue X 1.75%); *or*

(b) Music Area Revenue Calculation

LICENSEE shall pay to BMI the greater of: (1) 2.5% of LICENSEE's Music Area Revenue generated by LICENSEE's Web Site during each quarter year of the Term according to the Payment Schedule below (Music Area Revenue X 2.5%); and (2) total Music Page Impressions during each quarter year of the Term according to the Payment Schedule below divided by 1,000 and multiplied by $0.12 ((Music Page Impressions ÷ 1,000) X $0.12).

(c) Payment Schedule: LICENSEE may elect between the Gross Revenue Calculation and Music Area Revenue Calculation upon filing each of its Financial Reports for each immediately preceding calendar quarter of the Term in accordance with Paragraph 6 according to the following Payment Schedule:

PAYMENT SCHEDULE

Quarter	Period Ending	Payment Due Date
First	March 31	April 30
Second	June 30	July 31
Third	September 30	October 31
Fourth	December 31	January 31

5. Annual Minimum License Fee

For each calendar year of the Agreement, LICENSEE shall pay to BMI an Annual Minimum License Fee as follows:

(a) Upon signing this Agreement, LICENSEE shall estimate its annual Gross Revenue and shall pay to BMI an estimated Annual Minimum License Fee in accordance with the Minimum Fee Table below prorated based on the number of months remaining in the first calendar year covered by the Agreement. Thereafter, LICENSEE shall pay to BMI any additional amount that may be due based on actual Gross Revenue upon filing its Financial Reports in accordance with Paragraph 6. Annual Minimum License Fee payments are credited against any additional license fees that LICENSEE shall owe to BMI in the same year to which the Annual Minimum License Fee shall apply. Overpayments shall be credited to LICENSEE's account. Web Sites paying only Annual Minimum License Fees must still submit financial reports under Paragraph 6.

(b) The Annual Minimum License Fee due for 2001 is specified in the Minimum Fee Table below. For each year of this Agreement after 2001, the Annual Minimum License Fee shall be adjusted to reflect the increase (or decrease) in the United States Consumer Price Index (National, All Items) between October 2000 and October of the year preceding the year subject to the minimum fee, and shall be rounded to the nearest dollar amount.

MINIMUM FEE TABLE

Gross Revenue	2001 Annual Minimum Fee
Up to $12,000	$259.00
$12,001 to $18,500	$388.00
$18,501+	$517.00

6. Financial Reports and Audit

(a) LICENSEE shall submit to BMI separate Financial Reports as to Gross Revenue generated by LICENSEE's Web Site as follows:

(i) For each calendar quarter of this Agreement, a report, certified by an authorized representative of LICENSEE, for the Web Site, in the form substantially the same as the Web Site Music Performance License Quarterly Report Form annexed to this Agreement as Exhibit B. LICENSEE's Financial Reports are due at the same time as the applicable quarterly license fee, including the Annual Minimum License Fee, as set forth in Paragraph 4. LICENSEE agrees to use commercially reasonable efforts to use software which BMI may provide to LICENSEE to prepare and deliver such reports electronically, or such other commercially reasonable alternative method upon which the parties agree. LICENSEE's Financial Reports shall be treated as confidential. BMI will not disclose the contents of such reports except as may be required by law or legal process; *provided, however,* that nothing contained herein shall limit or preclude BMI from providing affiliated or represented songwriters, composers, music publishers, and/or non-U.S. performing rights licensing organizations with itemized royalty statements and responding to inquiries from such affiliates or non-U.S. organizations related thereto.

(ii) BMI shall have the right to estimate the fees due for a given quarter year on the basis of the highest quarterly fee during the previous twelve (12) months and bill LICENSEE therefor in the event that LICENSEE fails to report as required. Neither BMI's estimation of the fee for a reporting period nor anything else shall relieve LICENSEE of the obligation to report and make actual fee payments for the reporting period. If BMI's estimate was less than the actual license fee due, LICENSEE shall pay BMI, at the time the report is rendered, the difference between the actual fee due and the estimated fee paid. If LICENSEE's report reflects that the actual fee for the quarter year was less than the estimated fee paid, BMI shall credit the overpayment to LICENSEE's account. If LICENSEE has submitted all contractually required prior reports and payments to BMI and this Agreement is terminated, BMI shall refund the overpayment to LICENSEE.

(b) BMI shall have the right to require that LICENSEE provide BMI with data or information sufficient to ascertain the license fee due hereunder.

(c) BMI shall have the right, at BMI's sole cost and expense, once with respect to each year of the Term (or portion thereof), by its duly authorized representatives, at any time during customary business hours and upon thirty (30) days' advance written notice, to examine the books and records of account of LICENSEE necessary to verify any and all statements, accounting and reports rendered and/or required by this Agreement and in order to ascertain the license fee due BMI for any unreported period. The period for which BMI may audit LICENSEE shall be limited to three (3) calendar years preceding the year in which the audit is made; *provided, however,* that if an audit is postponed at the request of LICENSEE, and BMI grants such postponement, BMI shall have the right to audit for the period commencing with the third calendar year preceding the year in which notification of intention to audit was first given by BMI to LICENSEE. In the event that an audit reveals a deficiency of ten percent (10%) or greater, BMI shall have the right to audit one (1) additional calendar year, for a total of four (4) calendar years preceding the year in which the audit is made. This limitation on the period for which BMI may audit LICENSEE shall not apply if: (i) LICENSEE fails to file its financial reports due under Paragraph 6(a)(i) in a timely manner; and/or (ii) LICENSEE fails or refuses after written notice from BMI to produce the material books and/or records of account necessary to verify any report or statement required under the Agreement. BMI shall treat as confidential all data and information coming to its attention as the result of any such examination of books and records, and shall not use any such information other than in connection with its administration of this Agreement.

(d) In addition to any other remedy that BMI may have, in the event that BMI conducts an audit under Paragraph 6(c) and such audit reveals that LICENSEE has underpaid license fees to BMI, LICENSEE shall immediately pay the amount LICENSEE owes BMI and, in addition, if such underpayment amounts to ten percent (10%) or more of LICENSEE's annual fees for the audited period, LICENSEE shall pay BMI a late payment charge in the amount of one and one-half percent (1 1/2%) per month of all monies owed commencing on the actual date such monies were due.

7. Late Payment Charge

BMI may impose a late payment charge of one and one-half percent (1 1/2 %) per month from the date payment was due on any quarterly payment that is received by BMI more than ten (10) days after the due date.

8. Music Use Reports

(a) LICENSEE shall provide BMI, in electronic form, quarterly Music Use Reports which shall contain detailed information from LICENSEE's Web Site usage logs concerning the transmission of all musical works on LICENSEE's Web Site. Such information shall identify each musical work by title, composer/writer, author, artist, record label, any unique identifier (e.g. ISWC, ISAN), length, type of use (i.e., theme, background or feature performance) and manner of performance (i.e. instrumental or vocal) (or any other methodology agreed to by BMI and LICENSEE) and specify the number of times each musical work was transmitted and whether such transmission was streamed or downloaded. In the event that a charge was made for an on-demand transmission where the user chose to access a particular work and paid a fee to LICENSEE for such service, LICENSEE shall include the gross price that the end user was charged to receive such transmission(s). With respect to transmissions of audiovisual works, such information shall also include the title of each audiovisual work, and the primary author, director, and principal actor(s) of the audiovisual work. With respect to on-demand transmissions where users are able to access transmissions of specific works upon request, such information shall also include the country where the end-user received such transmission. LICENSEE shall request reports from its licensors or outside producers with respect to all content provided by others and transmitted by LICENSEE as part of LICENSEE's Web Site. LICENSEE shall notify BMI immediately in the event that LICENSEE is unable to obtain such reports, and BMI shall use commercially reasonable efforts to secure any missing reports from LICENSEE's licensors or outside producers, but nothing contained herein shall relieve LICENSEE of its obligation to deliver the reports to BMI in the event that BMI is unable to obtain such reports.

(b) LICENSEE shall deliver to BMI Music Use Reports on or before the thirtieth day following the end of such quarter pursuant to the Payment Schedule set forth in Paragraph 4. LICENSEE agrees to use commercially reasonable efforts to use software which BMI may provide to LICENSEE to prepare and deliver such reports electronically, or such other commercially reasonable alternative method upon which the parties agree.

(c) BMI shall not disclose, other than as individualized music use information accompanying royalty statements, any specific music performance data contained in the Music Use Reports without LICENSEE's prior written consent. Nothing contained herein shall preclude BMI from using the music use information as part of aggregated, publicly disseminated market data, so long as the source of such information is not specifically identifiable as coming from LICENSEE, or disclosing any such data as may be required by law or legal process.

9. Indemnification

Provided that LICENSEE has not failed to cure a breach or default within thirty (30) days of receiving notification from BMI thereof under the Agreement, BMI shall indemnify, save and hold harmless and defend LICENSEE and its officers and employees from and against any and all claims, demands and suits alleging copyright infringement that may be made or brought against them or any of them with respect to the public performance within the Territory of any musical works licensed hereunder; *provided, however,* that such indemnity shall be limited to those claims, demands or suits that are made or brought within the U.S. Territory, and provided further that such indemnity shall be limited to works which are BMI-affiliated works at the time of LICENSEE's performance of such works. This indemnity shall not apply to transmissions of any musical work performed by LICENSEE after written request from BMI to LICENSEE that LICENSEE refrain from performance thereof. BMI shall, upon reasonable written request, advise LICENSEE whether particular musical works are available for performance as part of BMI's repertoire. LICENSEE shall provide the title and the writer/composer of each musical composition requested to be identified. LICENSEE agrees to give BMI immediate notice of any such claim, demand, or suit, to deliver to BMI any papers pertaining thereto, and to cooperate with BMI with respect thereto, and BMI shall have full charge of the defense of any such claim, demand, or suit; provided, however, that LICENSEE may retain counsel on its behalf and at its own expense and participate in the defense of such claim, demand or suit.

10. Warranty; Reservation of Rights

This Agreement is experimental in nature. BMI and LICENSEE recognize that the license granted herein covers certain transmissions originating from and/or received in certain territories outside of the U.S. Territory pursuant to experimental agreements with certain non-U.S. performing rights licensing organizations around the world, and that this Agreement is broader in geographical scope than BMI's previous Internet licenses. Notwithstanding, BMI is offering this Agreement at the same rate as its previous Internet license on an experimental and non-prejudicial basis for the sole purpose of evaluating such international licensing initiatives. Nothing contained in this Agreement is intended to reflect BMI's position with respect to the reasonable value of the license granted herein; BMI hereby expressly reserves its right to re-evaluate the appropriateness of the fees and terms herein, including, but not limited to, the reasonable value of a license that covers transmissions beyond the U.S. Territory, for periods following the Term.

11. Breach or Default

Upon any breach or default of the terms and conditions of this Agreement by LICENSEE, BMI shall have the right to cancel this Agreement, but any such cancellation shall only become effective if such breach or default continues thirty (30) days after LICENSEE's receipt of written notice thereof. The right to cancel shall be in addition to any and all other remedies which BMI may have. No waiver by BMI of full performance of this Agreement by LICENSEE in any one or more instances shall be a waiver of the right to require full and complete performance of this Agreement thereafter or of the right to cancel this Agreement in accordance with the terms of this Paragraph.

12. Discontinuance of Music

In the event that LICENSEE ceases to publicly perform music in connection with its Web Site, LICENSEE may cancel this Agreement by sending written notice to BMI prior to the effective date of cancellation as specified in such notice by LICENSEE. BMI will cancel this Agreement, retroactive to the effective date of cancellation, but only if, within ninety (90) days after the effective date, LICENSEE: (a) has submitted to BMI all reports and payments due under the Agreement through the effective date; and (b) has not resumed publicly performing music in connection with its Web Site. In the event that LICENSEE fails to provide such reports and payments or resumes publicly performing music in connection with its Web Site within the ninety (90) day period, LICENSEE's request to cancel this Agreement shall be deemed withdrawn and this Agreement shall remain in full force and effect for the duration of the Term in accordance with Paragraph 1 above.

13. Arbitration

All disputes of any kind, nature or description arising in connection with the terms and conditions of this Agreement (except for matters within the jurisdiction of the BMI rate court) shall be submitted to arbitration in the City, County, and State of New York under the then prevailing rules of the American Arbitration Association by an arbitrator or arbitrators to be selected as follows: Each of the parties shall, by written notice to the other, have the right to appoint one arbitrator. If, within ten (10) days following the giving of such notice by one party the other shall not, by written notice, appoint another arbitrator, the first arbitrator shall be the sole arbitrator. If two arbitrators are so appointed, they shall appoint a third arbitrator. If ten (10) days elapse after the appointment of the second arbitrator and the two arbitrators are unable to agree upon the third arbitrator, then either party may, in writing, request the American Arbitration Association to appoint the third arbitrator. The award made in the arbitration shall be binding and conclusive on the parties and judgment may be, but need not be, entered in any court having jurisdiction. Such award shall include the fixing of costs, expenses, and attorneys' fees of arbitration, which shall be borne by the unsuccessful party.

14. Withdrawal of Works

BMI reserves the right at its discretion to withdraw from the license granted hereunder any musical work as to which legal action has been instituted or a claim made that BMI does not have the right to license the performing rights in such work or that such work infringes another composition.

15. Notice

All notices and other communications between the parties hereto shall be in writing and deemed received (i) when delivered in person; (ii) upon confirmed transmission by telex or facsimile device; or (iii) five (5) days after deposited in the United States mails, postage prepaid, certified or registered mail, addressed to the other party at the address set forth below (or at such other address as such other party may supply by written notice):

BMI: 320 West 57th Street
New York, New York 10019
Attn: Senior Vice President Licensing

with a separate copy to:

Senior Vice President and General Counsel

LICENSEE:

with a separate copy to:

16. Assignment

This Agreement shall inure to the benefit of and shall be binding upon the parties hereto and their respective successors and assigns, but no assignment shall relieve the parties hereto of their respective obligations hereunder.

17. Entire Agreement

This Agreement constitutes the entire understanding between the parties with respect to the subject matter hereof. This Agreement cannot be waived, added to or modified orally and no waiver, addition or modification shall be valid unless in writing and signed by the parties. This Agreement, its validity, construction, and effect, shall be governed by the laws of the State of New York. The fact that any provisions herein are found by a court of competent jurisdiction to be void or unenforceable shall not affect the validity or enforceability of any other provisions.

BROADCAST MUSIC, INC.

By: ______________________________
(Signature)

____
(Print Name of Signer)

____
(Title of Signer)

Please return signed agreement together with minimum fee to :

BMI
320 West 57th Street
New York, NY 10019
ATTN: Web Site Licensing

PLEASE COMPLETE ALL OF THE FOLLOWING:

LICENSEE's main offices are located in the U.S. Territory
YES_____ NO_____

The majority of LICENSEE's employees are located in the U.S. Territory
YES_____ NO_____

LICENSEE's annual accounts are audited in the U.S. Territory
YES_____ NO_____

____
(LICENSEE)

By: ______________________________
(Signature)

____
(Print Name of Signer)

____
(Title of Signer)

BMI
http://www.bmi.com

INTERNET-01

WEB SITE
MUSIC PERFORMANCE AGREEMENT

EXHIBIT A

WEB SITE NAME	URL

EXHIBIT B

BMI®

WEB SITE MUSIC PERFORMANCE AGREEMENT

Gross Revenue Calculation

QUARTERLY FINANCIAL REPORT FORM

Report For Calendar Quarter:	Jan. 1 – Mar. 31	Apr. 1 – June. 30	July. 1 – Sept. 30	Oct. 1 – Dec. 31	YEAR
	☐	☐	☐	☐	________

Company Name: ______________________

Address: ______________________

____

Telephone No.: ______________________

Name of Web Site: ______________________

URL: ______________________

YOUR GROSS REVENUE

1. Subscriber Revenue (including commissions on third party transactions) $ ____________
2. Advertising Revenue (less agency commissions) $ ____________
3. Provision of Space or Time $ ____________
4. Donations $ ____________
5. Trade or Barter $ ____________
6. Proprietary Software $ ____________

TOTAL GROSS REVENUE (add lines 1 through 6) $ ____________

TOTAL GROSS REVENUE $ ____________ X 1.75% = $ ____________
LICENSE FEE

TOTAL PAYMENT DUE = $ ____________

I hereby certify on this ________ day of ________________, ______ that the above is true and correct.

BY: ______________________
(SIGNATURE)

____
(PRINT NAME OF SIGNER)

____
(TITLE OF SIGNER)

Please return report and payment to:

Web Licensing
BMI
320 West 57th Street
New York, NY 10019

Please e-mail any questions to weblicensing@bmi.com

EXHIBIT B

BMI®

WEB SITE MUSIC PERFORMANCE AGREEMENT

Music Area Revenue Calculation

QUARTERLY FINANCIAL REPORT FORM

Report For Calendar Quarter:

Jan. 1 – Mar. 31	Apr. 1 – June. 30	July. 1 – Sept. 30	Oct. 1 – Dec. 31	YEAR
☐	☐	☐	☐	______

Company Name: ______________________

Address: ______________________

____

Phone #: ______________________

Name of Web Site: ______________________

URL: ______________________

MUSIC AREA REVENUE

DIRECT MUSIC AREA REVENUE

1. In-Stream Advertising $__________ less agency commissions $__________ $__________
2. Music Page Banner Advertising $__________ less agency commissions $__________ $__________
3. Music Subscriber Fees $__________
4. Other Music Revenue $__________
5. DIRECT MUSIC AREA REVENUE (add lines 1 through 4) $__________

ALLOCATION OF RUN OF SITE REVENUE

6. Subscriber Revenue (including commissions on third party transactions) $__________
7. Advertising Revenue $__________ less agency commissions $__________ $__________
8. Provision of Space or Time $__________
9. Donations $__________
10. Trade or Barter $__________
11. Proprietary Software $__________
12. RUN OF SITE REVENUE (add lines 6 through 11) $__________
13. ALLOCATION OF RUN OF SITE REVENUE

    __________ x (__________ ÷ __________) $__________

    RUN OF SITE REVENUE (TOTAL MUSIC PAGE IMPRESSIONS) (TOTAL PAGE IMPRESSIONS)
14. TOTAL MUSIC AREA REVENUE (add lines 5 and 13) $__________

MUSIC AREA LICENSE FEE

(the greater of A and B)

A. TOTAL MUSIC AREA REVENUE

$__________ x 2.5% = $__________

(from Line 13)

B. MUSIC PAGE IMPRESSIONS

__________ ÷ 1,000 x $0.12 = $__________

Total Music Page Impressions

MUSIC AREA LICENSE FEE $ __________

I hereby certify on this ________ day of ______________, ______ that the above is true and correct.

BY: ______________________

(SIGNATURE)

____

(PRINT NAME OF SIGNER)

____

(TITLE OF SIGNER)

Please return report and payment to:
Weblicensing
BMI
320 West 57th Street
New York, NY 10019
Please e-mail any questions to weblicensing@bmi.com

EXHIBIT C

Last Updated: 7/23/01

PERFORMING RIGHTS ORGANIZATION	COUNTRY
AEPI	Greece
AKM	Austria
APRA	Australia
ARTISJUS	Hungary
BUMA	The Netherlands
CASH	Hong Kong
COMPASS	Singapore
GEMA	Germany
IMRO	Ireland
JASRAC	Japan
KCI	Indonesia
KODA	Denmark
MACP	Malaysia
MUST	Taiwan
PRS	United Kingdom
SABAM	Belgium
SACEM	France
SACM	Mexico
SADAIC	Argentina
SCD	Chile
SGAE	Spain
SIAE	Italy
STIM	Sweden
SUISA	Switzerland
TEOSTO	Finland
UBC	Brazil

BMI
http://www.bmi.com

INTERNET-01

WEB SITE
MUSIC PERFORMANCE AGREEMENT

WEB SITE PROFILE

Please complete and return with your signed agreements
so we can service your account properly

Site URL: ______________________________

Site Name: ______________________________

Corporate Name: ______________________________

Corporate Contact: ____________________ **Title:** ____________________

Corporate Address: ______________________________

Telephone: ____________________ **Fax:** ____________________

E-Mail: ______________________________

Financial Contact: ____________________ **Title:** ____________________
If different from above

Billing Address: ______________________________
If different from above

Telephone: ____________________ **Fax:** ____________________

E-Mail: ______________________________

Music
Use Reports Contact: ____________________ **Title:** ____________________
If different from above

Telephone: ____________________ **Fax:** ____________________

E-Mail: ______________________________

Questions? Please visit our web site at
http://www.bmi.com

SESAC INTERNET/NEW MEDIA LICENSE

This experimental Internet/New Media License for performance rights is entered into without prejudice to the positions either party may take in subsequent discussions.

1. PARTIES

This Internet/New Media License, including all attached Schedules ('Agreement"). is made by and between SESAC, Inc. ('SESAC'). 421 West 54th Street, New York. New York 10019, and

______________________________ ('LICENSEE-)
(Name of corporation, partnership, sole proprietorship, etc.)

(Address)

City ______________ ST ____ Zip ______

(Web Site Base URL Address)

A ○ Corporation ○ Partnership ○ Sole Proprietorship (check one) State of Incorporation (if applicable) ______

Telephone: ______ Fax ______ E-mail: ______

(Billing Address, if different from above)

SESAC and LICENSEE hereby mutually agree as follows:

2. MISCELLANEOUS DEFINITIONS

A "Web Site" - A Web Site, under this Agreement, is a "location" on the Internet that broadcasts, transmits or otherwise makes musical works available to computer users on or through its own unique domain name and base Uniform Resource Locator ('URL') address, and includes all subpages under the base URL address.

B. "Compositions" - Compositions includes all of the musical works which SESAC controls and for which SESAC is empowered to license the performance right during the term of this Agreement as defined below.

3. GRANT OF RIGHTS

As of January 1 2001 ("Effective Date'), SESAC grants to LICENSEE the non-exclusive right and license to publicly perform non-dramatic renditions of the Compositions, by transmission on or through the LICENSEE's Web Site, as described in the Schedule "B" Web Site (URL) Address field. Any authorization made under this Agreement is limited to the United States, its territories and possessions and the Commonwealth of Puerto RicoRico ("U.S. Territory' or "U.S. Territory Rights"), unless LICENSEE is eligible and elects to secure Foreign Territory Rights (defined in the Foreign Territory Addendum), for an additional fee.

4. LIMITATIONS OF RIGHTS

The rights granted pursuant to Paragraph 3, above, specifically exclude:

A The right to transmit the Compositions from web sites or computer online services other than the Web Site described in Schedule "B," below;

If your Web Site aggregates audio or audio visual streams from *two* (2) or more web sites *or* other sources; or, if *you* provide proprietary content and/or services *to* third party web sites *(E.g.* subscriptions, brandedplayers, streamed *audio/video*, music samples, downloads, *etc.),* please contact ***SESAC*** for the appropriate license.

B. The authority to grant or sublicense to any third party or entity which may receive, download or otherwise capture transmissions from LICENSEE's Web Site, the right to publicly performthe Compositions licensed hereunder, either by any transmission, retransmission or rebroadcast by any means, medium, method, device or process now or hereafter known; and

C. "Grand Rights" in and to the Compositions ("Grand Rights" include, but are not limited to, the right to perform in whole or in part, dramatico-musical and dramatic works in a dramatic setting).

5. TERM OF LICENSE AGREEMENT

The term of this Agreement shall be for an initial period that commences upon the Effective Date and continues for a period of six (6) months (the 'Initial Period'). Thereafter, the Agreement shall automatically continue in full force and effect for successive additional periods of six (6) months ("Renewal Period(s)"). SESAC and/or LICENSEE shall have the right to terminate this Agreement as of the last day of the Initial Period or as of the last day of any Renewal Period(s), upon giving written notice to the other party by certified mail, return receipt requested, at least thirty (30) days prior to the commencement of any Renewal Period(s). The Initial Period and Renewal Period(s) are sometimes collectively referred to hereafter as the "Term."

6. LICENSE FEE

A. As consideration for the rights granted herein, LICENSEE shall pay to SESAC a fee ('License Fee') in accordance with the then current Internet/New Media Fee Schedule ("License Fee Schedule").

B. SESAC shall have the right to change the License Fee Schedule, upon thirty (30) days prior written notice, by Certified Mail. In the event LICENSEE's fees are increased as a result of a change in the License Fee Schedule, LICENSEE shall then have the right to terminate this Agreement, effective as of the date of the increase, provided that within thirty (30) days of SESAC's notice of increase, LICENSEE provides written notice of termination to SESAC by Certified Mail.

C. The License Fee may be subject to an increase effective January 1 of each calendar year by an amount equivalent to the percent increase, if any, in the Consumer Price Index - All Urban Consumer (CPI-U) as published by the Bureau of Labor Statistics, U.S. Department of Labor, between the preceding October and the next preceding October.

D. SESAC shall have the right to impose a late payment charge of one and one-half percent (1.5%) per month for any License Fee payment that is more than thirty (30) days past due. SESAC shall have the right to impose an additional charge of $25.00 for each dishonored check. In the event SESAC incurs costs and fees, including attorneys fees, in connection with the collection of any amount(s) past due hereunder, LICENSEE shall be responsible for paying all such costs and fees to SESAC.

E. In the event that SESAC is determined by the taxing authority or courts of any state in which LICENSEE conducts its operation to be liable for the payment of a gross receipts, sales, business use or other tax which is based on the amount of SESAC's receipts from LICENSEE, then LICENSEE shall reimburse SESAC, within thirty (30) days notification thereof, for LICENSEE's pro rata share of any such tax.

7. MISCELLANEOUS

A. In the event LICENSEE fails to pay the License Fee when due, or is otherwise in default of any other provision of this Agreement, SESAC shall have the right to terminate this Agreement in addition to pursuing any and all other rights and/or remedies available if LICENSEE has not cured such breach within thirty (30) days following SESAC's written notice of default.

B. In the event LICENSEE fails to submit a timely Report as required by the incorporated Schedule "A" SESAC will provide a written request for the Report. If LICENSEE fails to respond to the written request within fifteen (15) days, LICENSEE's License Fee may be adjusted to reflect the current Maximum License Fee.

C. SESAC shall have the right upon written notice, to withdraw from the scope of this License the right to perform any musical composition authorized hereunder as to which an action has been threatened, instituted, or a claim made that SESAC does not have the right to license the performance rights in such composition.

D. This Agreement shall be binding upon and inure to the benefit of SESAC's and LICENSEE's legal representatives, successors, and assigns, but no assignment shall relieve SESAC or LICENSEE of their respective obligations under this Agreement. LICENSEE shall notify SESAC in writing within thirty (30) days of any change of ownership or control of the online entity licensed hereunder.

E. This Agreement shall be governed by and subject to the laws of the State of New York, applicable to agreements made and to be wholly performed in New York.

F. This Agreement supersedes and cancels all prior negotiations and understandings between SESAC and LICENSEE in connection with the online entity licensed hereunder. No modification of this Agreement shall be valid or binding unless in writing and executed by SESAC and LICENSEE.

G. If any part of this Agreement shall be determined to be invalid or unenforceable by a court of competent jurisdiction or by any other legally constituted body having the jurisdiction to make such determination, the remainder of this Agreement shall remain in full force and effect.

H. No waiver of any breach of this Agreement shall be deemed a waiver of any preceding continuing or succeeding breach of the same, or any other provision of this Agreement.

I. This agreement, with schedules and addenda, is experimental in nature and shall not be prejudicial to either patty's position concerning the reasonableness or breakdown of Fees, terms or condltions in any subsequent negotiation andlor licensing agreement between SESAC and LICENSEE.

8. **RESERVATION OF RIGHTS**

A SESAC shall have the right to verify. by independent means, all Internet/New Media Report Information that LICENSEE provides for its License Fee determination or eligibility for this Agreement and make any necessary adjustments.

B. Notwithstanding anything to the contrary contalned herein, SESAC shall have the right to terminate this Agreement: (I) at any time upon written notice to LICENSEE in the event LICENSEE is adjudicated bankrupt, or a petition in bankruptcy is filed with respect to LICENSEE, or LICENSEE is declared or becomes insolvent; or (ii) upon thirty (30) days written notice by reason of any law, rule, decree, or other enactment having the force of law. by any authority, whether federal, state, local, territorial or otherwise, which shall result in substantial interference in SESAC's operation or any substantial increase in the cost of conducting its business.

IN WITNESS THEREOF, the parties have caused this Agreement to be duly signed as of ____________
(Please insert today's date)

LICENSEE - Please sign here	SESAC
BY: X ____________	BY: ____________
____________ (Type or print name)	
TITLE: ____________	TITLE: ____________

4/01

SCHEDULE 'A'
INTERNET/NEW MEDIA FEE SCHEDULE
WEB SITES - 2001

1. The License Feefor Year 2001 shall be determined as follows:

A With no advertising

.0075 multiplied by the average number of monthly Page Requests'

Minimum License Fee per Web Site for each six (6) month Report Period: $75.00
Maximum License Fee per Web Site with no advertising for each six (6) month Report Period: $1,500.00

Note: Ifyou are an educational institution or a non-commercial entity, you may be eligible for a reduced *Mnlmum License* Fee. Please contact SESAC to qualify.

B. With advertising

.0075 multiplied by the average number of monthly Page Requests multiplied by 1.3

Minimum License Fee per Web Site for each six (6) month Report Period: $75.00
Maximum License Fee per Web Site with advertising for each six (6) month Report Period: $1,950.00

* 'Page Requests" is the number of requests for HyperText Markup Language documents commonly referred to as 'HTML pages' (often using file extensions such as .htm, .html, .shtml, .phtml, .php or .asp) which result in being viewed by a browser.

2. New Media Report (Schedule "B") Calculation

A Initial Internet/New Media Report

For Web Sites in operation less than six (6) months prior to the Effective Date, the average number of monthly Page Requests shall be determined by the total number of Page Requests during the period of operation divided by the actual number of months in operation.

For Web Sites not in operation prior to the Effective Date. LICENSEE shall pay an estimated License Fee based on a good faith estimate of anticipated average Page Requests.

LICENSEE shall complete the following Internet/New Media Report Form (Schedule 'B") for the Initial Period of this Agreement and submit payment to the address below. LICENSEE shall pay the License Fee upon execution of this Agreement. with fees due and payable in advance.

B. All Subsequent Internet/New Media Reports

LICENSEE shall submit an updated Internet/New Media Report Form (Schedule "B") thirty (30) days prior to the start of each 'Billing Period" (defined below). The Report of average monthly page views during January 1 through June 30 shall be submitted on or before June 1st (estimate June page views) and will be reflected in the Billing Period of July 1 through December 31. The Report of average monthly page views during July 1 through December 31 shall be submitted on or before December 1st (estimate December page views) and will be reflected in the Billing Period of January 1 through June 30 of each calendar year.

The average number of monthly Page Requests shall be calculated by determining the total number of monthly Page Requests for the six (6) month Report Period divided by six (6).

For your convenience. annual electronic submission is encouraged and can be accomplished at WWW.SESAC.COM. SESAC will also accept timely submission of the Schedule "B" Report Form by mail, fax or E-mail.

3. License Fee Calculation for Year 2001

A Initial Billing Period

'Initial Billing Period" - The Initial Billing Period represents the period from the Effective Date of this agreement through June 30 for agreements with Effective Dates from January 1 through June 1; or, the period from the Effective Date of this Agreement through

- December 31 for agreements with Effective Dates from July 1 through December 1.

The initial License Fee payment shall be a pro-rated amount calculated by applying the then current License Fee Schedule to the 'eriod from the Effective Date through the end of the Initial Billing Period.

B. Subsequent Billing Periods

'Billing Period' -The Billing Period represents the period of either January 1 through June 30, or July 1 through December 31 of each calendar year.

All subsequent License Fee payments shall be submitted on or before the first day of January, for the Billing Period of January 1 through June 30; and on or before the first day of July, for the Billing Period of July 1 through December 31 of each calendar year.

4. Foreign Territory Rights

If LICENSEE would like to secure Foreign Territory Rights, please contact SESAC directly to learn more.

All License Fees may be paid online or by mail (*If* by mail, please write your Web Site Address on your check). Upon SESAC's acceptance of this Agreement, your account number will be mailed to you. The account number is required for making all subsequent online payments and reports.

SESAC
55 Music Square East
Nashville, TN 37203

Fax No: 615-321-6292
Questions: 615-320-0055
Email: billing@sesac.com

SCHEDULE "B"
INTERNET/NEW MEDIA REPORT FORM FOR WEB SITES - 2001

LICENSEE's Web Site (URL) Address: ______

Internet/New Media Report Period From: ______ To: ______

LICENSE FEE CALCULATION for Year 2001:

1. Average Number of Monthly Page Requests: ______
2. Per Page Request multiplier: x .0075 ______
3. License Fee** without advertising: $ ______
   (Line 1 times Line 2)

Continue if your Web Site has advertising; otherwise line 3 is your Period License Fee due for this Web Site

4. Advertising multiplier: x 1.3 ______
5. License Fee** if advertising is present: $ ______
   (Line 3 times Line 4)

**Minimum License Fee for each six (6) month Period - 2001: $75.00
Maximum License Fee for each six (6) month Period without advertising - $1,500.00
Maximum License Fee for each six (6) month Period with paid advertising - $1,950.00

CERTIFICATION:

I hereby certify that the information contained in this Agreement, including all Schedules, is true and complete. I warrant and represent that I am legally eligible to enter into this Agreement as an authorized agent of the entity to which this License will be issued.

Name X ______ Title X ______ Today's Date ______

Please return the completed Agreement and Schedule "B" Internet/New Media Report Form with appropriate payment to:

SESAC
55 Music Square East
Nashville, TN 37203

Fax No: 615-321-6292
Questions: 615-320-0055
Email: billing@sesac.com

1. Term of License. This license is for the term commencing as of , 199

H. "Gross Revenue" means all:

(1) cash payments made by or on behalf of:

a. sponsors or donors for the use of radio broadcasting facilities *of* the Station,

b. sponsors of, or donors to, your *simulcast program.*

c. sponsors of, or donors to, your *occasional* network *programs,*

d. *time* brokers who each provide programs for less than 10% of the time the Station is on the air. or recognized independent companies engaged in arrangements with radio or television stations generally for the resale of the radio broadcasting facilities of the Station, and

e. independent networks or other program suppliers for the broadcasting of such networks' or program suppliers' programs or announcements by the Station; and

(2) net promotional revenue

Such payments shall include all payments made directly to, or as authorized by, you, your employees, representatives, agents or any other person acting on your behalf. Such payments shall not include payments made to independent third parties, such as networks or program suppliers, or non-cash payments such as payments in goods or services commonly referred to as "trades" or "barter".

I. "Adjusted Gross Revenue" means *gross revenue* less:

(1) advertising agency commission not to exceed 15% actually allowed to an independent advertising agency;

(2) any sums received from your political radio programs and announcements, net of agency commissions;

(3) bad debts actually written off and discounts allowed or rebates paid; and

(4) rate card discounts, cash, quantity and/or frequency actually allowed.

J. "Revenue Subject to Fee" means *adjusted gross revenue* or, at Station's option, *adjusted gross revenue* less the total of the following itemized deductions which exceeds 11% of *adjusted gross revenue:*

(1) All compensation over and above the total annual amount indicated below, actually paid by the Station to personnel whose duties primarily are acting as (a) master of ceremonies or disc jockey on musical programs, or (b) vocalist or instrumentalist engaged for a specific program; or (c) featured newscaster and news commentator; or (d) featured sportscaster, or (e) master of ceremonies on an entertainment program, or (f) announcer:

Station's Annual *Adjusted* Gross *Revenue*	Total Annual Amount Not Deductible
Under - $ 50,000	$ 6,200
$ 50,000 - $ 149,999	$18,600
$ 150,000 - $ 299,999	$27,900
$ 300,000 - $ 499,999	$41,900
$ 500,000 - $ 749,999	$46,500
$ 750,000 - $ 999,999	553,700
$ 1,000,000 and Over	$62,000

You may not deduct any compensation paid to any person who has a stock or other ownership interest in Licensee or in the station of 40% or more.

(2) The actual payment by the Station to an independent supplier of general news service (such as AP or UPI) or specialized news service (such as weather, traffic, business or agricultural reports).

(3) The following actual costs incurred by the Station for a specific program: (a) payments to the telephone company or like transmission utility for remote pick-up necessary to broadcast the program from a point outside a studio of the Station; and (b) rights for broadcasting a sports or other special event.

(4) The following actual payments made by the Station to an independent network not licensed by ASCAP for a specific local program: (a) If the network is owned and operated by a college or university, the actual payment made by the station to the college or university; (b) *If the* network is not owned and operated by a college or university, the actual payments made for talent and for broadcast rights (which may not exceed the amount actually paid to or for the original holder of the broadcast rights for the particular program), and the actual payments made to or for the telephone company or like transmission utility for interconnecting lines and remote lines necessary to broadcast the program from a point outside the studio of the Station, which may not exceed the amount actually paid to or for the telephone company or like transmission utility.

(5) The following actual costs incurred in connection with your *occasional network programs:* (a) the payments to your affiliated stations in connection with those programs; (b) the actual payments made for talent and broadcast rights (which may not exceed the amount actually paid to or for the original holder of such broadcast rights); and (c) the actual payments made to or for the telephone company or like transmission utility for interconnecting lines and remote lines necessary to broadcast that program from a point outside the studio of the Station, which may not exceed the amount actually paid to or for the telephone company or like transmission utility.

6. Music Reports. You agree to furnish to us upon request a list of all musical compositions on your *radio programs,* showing the title, composer and author of each composition. You will not be obligated to furnish such list for a period or periods which in the aggregate exceed one month in any one calendar year during the term of this agreement.

7. Right to Restrict.

A. Our members may restrict the radio broadcasting of their compositions up to a maximum of 500 at any given time, only for the purpose of preventing harmful effect upon other interests under the copyrights of such works; provided, however. that (1) limited licenses will be granted upon application to us entirely free of additional charge if the copyright owners are unable to show reasonable hazards to their major interests likely to result from such radio broadcasting; (2) the right to restrict any composition will not be exercised for the purpose of permitting the fixing or regulating of fees for the recording or transcribing of the composition; (3) in no case will any charges, "free plugs", or other consideration be required for permission to perform a restricted composition; and (4) in no event will any composition be restricted after its initial radio broadcast for the purpose of confining further radio broadcasts to a particular artist, station, network or program.

B. We may also in good faith restrict the radio broadcasting of any composition, over and above the number specitied in the previous paragraph, only as to which any suit has been brought or threatened on a claim that the composition infringes a composition not contained in the ASCAP *repertory* or on a claim that we do not have the right to license the public performance of the composition by radio broadcasting.

8. License Fee.

A. You agree to pay us the following license fee for each year of the agreement:

(1) Gross Revenue up to $150,000. If your annual (or annualized) *gross revenue* is $150,000 or less use the following fee schedule to determine your annual fee for the year. Any period of less than a year should be annualized and the applicable annual fee for a station with that annualized revenue should be pro-rated for the period.

Annual Revenue	License Fee
up to $50,000	$ 450
$50,001 - $75,000	$ 800
$75,001 - $ 100.000	$1150
$ 100.001 - $ 125.000	$1450
$125,001 - $150,000	$1800

(2) Gross Revenue over $150,000. If your annual (or annualized) *gross revenue* is over $150,000 your fee is 1.615% of your *revenue subject to fee* but not less than 1% of your *adjusted gross revenue.*

B. In the event that your payment of fees under this agreement causes us to incur a liability to pay a gross receipts, sales, use, business use, or other tax which is based on the amount of our receipts from you, and (1) we have taken reasonable steps to be exempted or excused from paying the tax; and (2) we are permitted by law to pass through the tax to our licensees, you will pay us the full amount of the tax.

9. Reports and Payments.

A. Annual Reports. You will send us a report of the license fee due for each year of this agreement, by April 1st of the following year, by fully completing the Statement of Account form which we will supply free of charge. A copy of the Statement of Account form is annexed and made a part of this agreement.

B. Monthly Payments. For each month during the term of this Agreement, you will pay us on or before the first day of the following month, a sum equal to 1/12th of the license fee for the preceding calendar year (annualized for any reported period less than a year), adjusted in accordance with any increase in the Consumer Price Index (National, all items) between the preceding October and the next preceding October. If we do not receive the report required by Paragraph 9.A. for any calendar year when due, the monthly payments will be in the amount of the monthly payments due for the preceding year, plus 24%, and payments at that rate will continue until we receive the late report. If the station commenced broadcasting after January 1,1996, you will furnish us with a good faith estimate of your revenue for the first year of operation and the monthly payments during the first calendar year of broadcasting will be 1/12th of the fee provided in Paragraph 8.A. for a station having such revenue.

C. Annual Adjustments. If the monthly payments that you have made to us for a year pursuant to Paragraph 9.B are less than the license fee for that year, you will pay us the additional amount due with the annual report. If the amount that you paid for that year exceeds the license fee due for the year we will apply the excess payment against your future monthly payments, or refund it to you upon your written request if it is greater than three monthly payments required by Paragraph 9.B.

D. Late Payments. If we do not receive any payment required under Paragraph 9.B. or 9.C. before the first day of the month following the date when the payment was due, you will pay us a finance charge of 1½% per month from the date the payment was due.

E. Billing Basis. License fee reports will be made on a billing basis by all stations, except that any station may report on a cash basis if (1) its books have been kept on a cash basis and (2) it reported to us only on a cash basis and at no time on a billing basis during the entire term of its agreement with us ending February 28, 1977, and continuously thereafter. You will account for all billings made subsequent to the termination of this agreement with respect to radio broadcasts made during the term of the agreement as and when you make such billings.

F. Late Reports. If we do not receive a report required by Paragraph 9.A. of this agreement within 30 days of the date that the report was due, we may give you notice that you have an additional 30 days within which to submit the report on either the ***adjustedgross revenue*** or ***adjustedgross revenue*** less itemized deductions basis. If you fail to submit the report within the additional 30-day period, the report must be on the ***adjusted gross revenue*** basis.

G. Multiple Station Reports. You will submit a single license fee report for:

(1) AM and FM stations that you own in the same city if the combined ***gross revenue*** for the stations is less than $75,000, or

(2) all stations that you own that simultaneously broadcast programs for 80% or more of the time the stations are on the air concurrently.

If you act as a ***rime broker*** for one or more other radio stations that are licensed pursuant to this form of local station blanket radio license, you will include in your license fee reports for the Station all ***gross revenue*** relating to periods on those other station or stations that are simulcast or are sold in combination with the Station. All other stations that you own or act as a ***time broker*** for will repon and pay separately, and be treated for all purposes as separate stations.

H. Combination Sales. If the use of the broadcasting facilities of the station is sold in combination with any other stations that you own, operate or control that are licensed by us under a form of agreement other than this form of local station blanket radio license, the combination revenue shall be allocated among the stations on a reasonable basis taking into account factors such as, but not limited to, separate sales by the stations for comparable facilities during the report period or the immediately preceding period, and/or the relative ratings of the stations during the report period.

10. Audits.

A. Right to Audit. We have the right by our duly authorized representatives, at any time during customary business hours, upon reasonable notice, to examine your books and records of account only to the extent necessary to verify any report required by this agreement. We will consider all data and information coming to our attention as a result of any such examination of books and records as completely and entirely confidential.

B. Audit Period. The period for which we may audit is limited to the four calendar years reported preceding the year in which the audit is made. However, if you request a postponement, we have the right to audit for the period commencing with the fourth calendar year reported preceding the year in which we first notified you of our intention to audit. This limitation does not apply if you fail or refuse after written notice from us to produce the books and records necessary to verify any report or statement of accounting pursuant to the agreement.

C. Correction of Errors. You may correct computational errors, or errors relating to deductions permitted under the agreement on your license fee reports for the four calendar years preceding the year in which the corrected reports are submitted. However, you may not submit a report on the ***adjusted gross revenue*** less itemized deductions basis for a period previously reported on the ***adjusted gross revenue*** basis.

D. Audit Finance Charges. If our audit discloses that you underpaid license fees due us:

(1) You will pay a finance charge on the additional license fees of 1½% per month from the date(s) the fees should have been paid pursuant to this agreement if the underpayment is 5% or more, but not less than $1000.

(2) You will pay a finance charge on the additional license fees of 1½% per month beginning thirty (30) days after the date we bill the additional license fees to you if the underpayment is less than 5% or less than $1000.

(3) You may dispute all or part of our audit claim. If you do, you must, within thirty (30) days from the date that we bill the additional fees, (i) advise us, in writing, of the basis for your dispute and (ii) pay us any fees indisputably owed together with any applicable finance charges. If there is a good faith dispute between us with respect to all or part of the additional fees that we have billed pursuant to this Paragraph, no finance charges will be billed with respect to the disputed fees for a period beginning on the date we billed the fees to you and ending sixty (60) days from the date that we respond to your written notification of the existence of a dispute.

(4) Finance charges computed in accordance with this Paragraph and pertaining to additional fees which you dispute in accordance with subparagraph (3) above will be adjusted pro-rata to the amount arrived at by you and us in resolution of the dispute.

11. Breach or Default. If you fail to perform any of the terms or conditions of this agreement relating to the reports, accountings or payments required to be made by you, we may give you thirty (30) days' notice in writing to cure your breach or default. If you do not do so within the thirty (30) days, we may then promptly terminate this license.

12. Time Brokerage Arrangements. If you enter into a *time brokeruge* arrangement, the license granted by this agreement will automatically terminate thirty (30) days after the commencement date of the *time brokeruge* unless you have furnished *us* a complete copy of the *time brokeruge* agreement and you and *time broker* have executed a letter to us in the form annexed and made a part of this agreement requesting amendment of the license agreement to add *time broker* as a party. When that letter has been fully executed by you, *time broker* and us. this agreement will be amended accordingly.

13. indemnity Clause. We will indemnify, save and hold harmless and defend you, your advertisers and their advertising agencies, and your and their officers, employees and artists, from and against all claims, demands and suits that may be made or brought against you or them with respect to the performance under this agreement of any compositions in the ASCAP *repertory* which are written or copyrighted by our members. You must give us immediate notice of any such claim, demand or suit and immediately deliver to us all papers pertaining thereto. We will have full charge of the defense of any such claim, demand or suit and you agree to cooperate fully with *us* in such defense. You may however engage your own counsel at your own expense who may participate in the defense of any such action. At your request we will cooperate with and assist you, your advertisers and their advertising agencies and your and their officers, employees and artists in the defense of any action or proceeding brought against them or any of them with respect to the performance of any musical compositions contained in the ASCAP *repertory*, but not copyrighted or written by members of ASCAP. This Paragraph 13 does not apply to performances of any works that may be restricted under Paragraph 7 of this agreement.

14. Rights of Termination.

A. You have the right to terminate this license on seven (7) days' written notice in the event of the termination, suspension or any substantial alteration or variation of the terms and conditions of the governmental licenses covering the Station, or any major interference with the operations of the Station due to governmental measures or restrictions.

B. We have the right to terminate this license on thirty (30) days' notice if there is any major interference with, or substantial increase in the cost of, our operation as a result of any law of the state, territory, dependency, possession or political subdivision in which the Station is located which is applicable to the licensing of performing rights.

15. Notices. All notices required or permitted to be given by either of us to the other under this agreement will be duly and properly given if:

A. mailed to the other party by registered or certified United States mail; or

B. sent by electronic transmission (i.e., Mailgram, facsimile or similar transmission); or

C. sent by generally recognized same-day or overnight delivery service;

addressed to the party at its usual place of business.

16. Successors and Assignees. This agreement will enure to the benefit of and be binding upon you and us and our respective successors and assignees, but no assignment will relieve either of us of our respective obligations under this agreement.

17. Per Program License. The "local station per program license" for the term ending December 31, 2000 is being offered to you simultaneously with this agreement. In accepting this agreement, you acknowledge that you have a choice of entering into either this agreement or the per program license with us; that you have the opportunity to negotiate for separate licenses with our individual members; and that you are voluntarily entering into this agreement with us. You may substitute the per program agreement in place of this agreement by giving us written notice at least 10 days prior to the commencement of any month during the term of this agreement. In such event, effective with the commencement of that month, the per program agreement will be in full force and effect between us.

18. Applicable Law. The fees set forth in this agreement have been approved by the United States District Coun for the Southern District of New York as reasonable and non-discriminatory in accordance with the Amended Final Judgment in United States v. ASCAP. The meaning of the provisions of this agreement will be construed in accordance with the laws of the State of New York.

IN WITNESS WHEREOF, this agreement has been duly executed by ASCAP and Licensee this ______ day of ______________, 199 /2000.

AMERICAN SOCIETY OF COMPOSERS, AUTHORS AND PUBLISHERS	LICENSEE
	(Full corporate or other name of station owner)
By ______________________________	By ______________________________
	(Fill in capacity in which signed)

(a) If corporation, state corporate office held;

(b) If partnership, write word "partner" under signature of signing partner

(c) If individual owner, write "individual owner" under signature

TIME BROKERAGE AMENDMENT LETTER

(Letterhead of Licensee)
Licensee ________
Call Letters ________
City and State ________
Date ________

Dear ASCAP:

1. Radio station ______________ ["STATION"] has entered into a time brokerage agreement with ______________ ["BROKER] for the period ______________ through ______________

2. STATION and BROKER wish to add BROKER as a party to the Local Station Radio License Agreement in effect between STATION and ASCAP ("the license") with all of the rights and obligations of the Licensee as set forth in the license for the full period of the brokerage agreement referred to in (1) above.

3. We agree that for all periods that STATION simulcasts or is sold in combination with another radio station owned or operated by BROKER ["BROKER STATION"] that has an ASCAP Local Station Radio License we shall report all gross revenue of STATION as follows:

a. All BROKER revenue relating to STATION will be included in BROKER's license fee reports for BROKER STATION. If such revenue constitutes all gross revenue for STATION, no license fee or license fee reports will be required of STATION.

b. All of STATION's other revenue (as defined in the license) will be included in STATION's license fee reports.

c. Amounts payable by BROKER to STATION as consideration for the time brokerage agreement shall not be reportable by STATION or deductible by BROKER STATION.

d. In the event that STATION and BROKER STATION have different forms of ASCAP license, all BROKER revenue relating to programs of STATION which simulcast or are sold in combination with BROKER STATION shall be apportioned between STATION and BROKER STATION in the same ratio as the adjusted gross revenue of STATION and BROKER STATION bear to each other for the most recent year prior to the brokerage agreement reported by STATION and BROKER STATION to ASCAP (annualized for any period less than a year). Any such revenue apportioned to. and reported for, STATION pursuant to this paragraph shall not be reportable by BROKER on its license fee reports for BROKER STATION.

4. If STATION fully simulcasts programs broadcast by BROKER STATION and has no separate programs, STATION and BROKER agree to maintain the same form of ASCAP license (blanket or per program) for STATION as BROKER has for BROKER STATION. In the event that BROKER has a different form of license for BROKER STATION at the time this agreement is executed, this letter shall constitute our notice in accordance with the license agreement (Paragraph 17 of the blanket license or Paragraph 18 of the per program license) to substitute the other form of license in place of our current agreement. In the event that STATION and BROKER STATION have the same form of license at the time this agreement is executed, and BROKER STATION subsequently provides notice pursuant to its license agreement to substitute the other form of license, said notice shall be deemed to apply as well to STATION.

5. For all periods that STATION has a per program license agreement, BROKER STATION shall submit the reports required by Paragraph 8 of the per program license for all programs provided by BROKER STATION which are broadcast by STATION, and STATION shall submit such reports for all other programs broadcast by STATION. If STATION fully simulcasts programs broadcast by BROKER STATION and has no separate programs, and if all revenue relating to STATION is included in BROKER's license fee reports for BROKER STATION in accordance with Paragraph 3.a. above, STATION shall not be required to submit separate reports pursuant to Paragraph 8 of the per program license.

6. STATION and BROKER jointly designate the following single address for billing and all other purposes:

Address: ______________
____
____

Please indicate your consent to the amendment of our license agreement in accordance with this letter by countersigning the letter in the space provided below and returning a copy to us.

Very truly yours,

(LICENSEE)

By ______________

(BROKER)

Dated ______________ By ______________

The undersigned, American Society of Composers, Authors and Publishers, hereby consents and agrees to the amendment of the above mentioned license agreement.

American Society of Composers
Authors and Publishers

Dated ______________ By ______________

ANNUAL STATEMENT OF ACCOUNT* BLANKET

FORM AB-96

PART 1 Account Information

*Report must be on Calendar Year Basis 19 ☐

If less than full year Reporting Period ☐ Month ☐ Day ☐ Year to ☐ Month ☐ Day ☐ Year

AMERICAN SOCIETY OF COMPOSERS, AUTHORS AND PUBLISHERS

ASCAP

ASCAP Building
One Lincoln Plaza, New York, N.Y. 10023

Type of Station	Accounting Method	Submitted by:
AM ☐ FM ☐	Billing Basis ☐ Cash Basis* ☐ *Lic. 9E	
If station is brokered by another station—enter calls: ☐-☐		Signature / Title / Date
If all revenue to be reported by broker—check box ☐		

FOR RADIO STATION:	Other stations covered by Report	
	Co-owned stations: (80% simulcast or <75,000 gross)	Time Broker for:
Call Letters		
Licensee		
Address		

PART 2 GROSS < $150,000

GROSS REVENUE UP TO $150,000

If your gross revenue is $150,000 or less (on an annualized basis if the report period is less than a year) enter your GROSS REVENUE on Line 1 and the applicable LICENSE FEE from the Schedule at Right (pro-rated for any period less than a year) on line 2. Your report is now complete.

REVENUE	FEE
$ Up to $ 50,000	$ 450
$ 50,001 - $ 75,000	$ 800
$ 75,001 - $100,000	$1150
$ 100,001 - $125,000	$1450
$ 125,001 - $150,000	$1800

Line	Item		
1	Gross Revenue (excluding noncash payments in goods and/or services) (Lic. P.5H)	1	
2	License Fee	2	

PART 3 GROSS > $150,000

Line	Item			
3	Gross Revenue (excluding noncash payments in goods and/or services) (Lic. P.5H)			3
4	Advertising Agency Commissions (Lic. P.5I (1))		4	
5	Revenue for Political Broadcasts (Lic. P.5I (2))	5		
6	Net Agcy. Comm. included in 4 above	6		
7	Net Revenue for Political Broadcasts		7	
8	Bad Debts (Lic. P.5I (3))	8		
9	Less: Bad Debt Recoveries	9		
10	Net Revenue for Bad Debts		10	
11	Rate Card Discounts (Lic. P.5I (4))		11	
12	Total Adjustments to Gross (Add lines 4.7.10 and 11			12
13	Adjusted Gross Revenue/Revenue Subject to Fee (Subtract line 12 from line 3)			13

PART 4 COMPLETE ONLY IF YOU ITEMIZE DEDUCTIONS

Line	Item		
14	Total Itemized Deductions (from line 26)	14	SKIP LINES 14-17 UNLESS YOU ITEMIZE DEDUCTIONS
15	Enter 11% of line 13 (Adjusted Gross Revenue)	15	
16	Subtract line 15 from line 14	16	
17	Revenue Subject to Fee (Subtract line 16 from line 13)	17	
18	License Fee (1.615% of line 13 or line 17 *but not less than 1% of line 13)*		18

19 Schedule: Compensation Under Lic. P.5J (1) (Attach additional sheets if necessary)

NAMES OF PERSONNEL	ANNUAL COMPENSATION
Total	19

Adjusted Gross Revenue (Line 13)	Amount Not Deductible
$ Under - $ 50,000	$ 6,200
$ 50,000 - $149,999	$ 18,600
$150,000 - $299,999	$ 27,900
$300,000 - $499,999	$ 41,900
$500,000 - $749,999	$ 46,800
$750,000 - $999,999	$ 53,700
$1,000,000 and over	$ 62,000

Line	Item		
20	Amount Non-Deductible (see Table at right)	20	
21	Deductible Compensation (Lic. P.5J (1)) (Subtract 20 from 19)		21
22	News Service (Lic. P.5J (2))		22
23	Remote Pickups (Lic. P.5J (3)(a))		23
24	Broadcast Rights (Lic. P.5J (3)(b))		24
25	Other. Specify License Paragraph ______		25
26	Total Itemized Deductions (Add lines 21 through 25. Enter on line 14)		26

Jaffe Rebuttal Exh.2B

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BMI

BROADCAST MUSIC, INC.

RADIO—92
BLANKET

SINGLE STATION RADIO BLANKET LICENSE AGREEMENT
SHORT METHOD OPTION OR LONG METHOD OPTION

AGREEMENT made at New York, New York, on this ______ day of ______________ 19____ between BROADCAST MUSIC, INC., a corporation organized under the laws of the State of New York (hereinafter BMI) with principal offices at 320 West 57th Street, New York, N.Y. 10019 and ______________

____
(Legal Name of LICENSEE)

PLEASE CHECK APPROPRIATE BOX AND COMPLETE

☐ A corporation organized under the laws of the State of ______________

☐ A partnership consisting of ______________

____

☐ An individual residing at ______________

____

(hereinafter called LICENSEE) with offices presently located at ______________

____
(Street Address)

City ____________ state ____________ Zip ________ Telephone No. (______) ____________
Area Code

and operating the radio broadcasting station presently located at ______________

____
(Street Address)

city ____________ State ____________ Zip ________ Telephone No. (______) ____________
Area Code

and presently designated by the call letters ____________ ☐ AM ☐ FM and assigned frequency ____________
(Check Appropriate Box)

1. **Term.**

The Term of this License Agreement commences as of January 1, 1992 and ends on December 31, 1996, unless earlier terminated as hereinafter provided.

2. **Definitions.**

A. **"Radio** broadcasting" shall mean aural broadcasting in all of its forms.

B. "Local program" shall mean any radio program, including a "cooperative program," broadcast by a station other than a "network program". For the purposes of this License Agreement, sports, special events and other programs furnished by networks not licensed by BMI, as well as any program originating from a station which holds a BMI Single Station Radio Blanket License Agreement, shall be deemed to be "local programs".

C. **"Cooperative program"** shall mean any program furnished by a network to the station under an agreement permitting the station to broadcast such program on a sustaining basis or on a commercial basis under the sponsorship of a local, regional or national advertiser contracting directly with the station or its representative for the incorporation of the commercial credits of such advertiser into such program, as broadcast by the station.

D. "Network program" shad mean any radio program simultaneously broadcast by any means by any network licensed as a network by BMI. "Network program" shall include "rebroadcasts," "delayed broadcasts" and "repeat broadcasts" of a network program as those terms are now understood in the broadcasting industry, even though non-simultaneous. Payments made to the originating network by an affiliated station in connection with such program may not be deducted. LICENSEE shall report all billings to and/or cash received from the furnishing network. "Billing(s)" as used in this License Agreement shall exclude the non-cash portion of transactions such as trade and barter sales with respect to a station reporting on a Billing Basis as referred to in Paragraph 2.F.(1).

PLEASE COMPLETE SHADED AREAS ONLY

XJAF 6990

(1) Any program furnished by a network which is not licensed as a network by BMI shall be deemed to be a local program. With respect to any such program:

(a) LICENSEE shall report all billings to and/or cash received from the furnishing network; and

(b) LICENSEE may deduct amounts paid to the furnishing network for: (i) the use of interconnecting facilities necessary to broadcast the program from outside the station's studios (not more than the amount actually paid to a utility company for such), and (ii) broadcast rights (not more than the amount actually paid to or for the original holder of the broadcast rights for the program).

(2) Any program which originates from a station which holds a BMI Single Station Radio Blanket License Agreement shall be deemed to be a local program. With respect to any such program:

(a) The originating station shall report all billings to and/or cash received from, or on behalf of, (1) the sponsors of any such program, and (2) affiliated stations. The following deductions shall be allowed against such revenue:

(i) The actual payments made to an outside vendor (e.g., a utility or satellite company) for the use of transmission facilities necessary to broadcast the program from outside the station's studios;

(ii) The actual payments made for broadcast rights, but not more than the amount actually paid to or for the original holder of them; and

(iii) The actual payments made by the originating station to its affiliates in connection with such program.

(b) The affiliated station shall include all billings to and/or cash received from the originating station in connection with such program, or from or on behalf of sponsors of cooperative announcements. If payments are made to the originating station by the affiliated station in connection with such program, the affiliated station may deduct such payments.

E. "Simulcast program" shall mean any program broadcast by two or more stations which are owned by LICENSEE and are broadcast either simultaneously or on a "delayed broadcast" or "repeat broadcast" basis. Simulcast programs shall also include such programs for which LICENSEE acts as a "Local Manager."

F. "Gross Revenue" shall mean:

(1) When reporting on a "Billing Basis" (see Paragraph 5.B.), all billings (standard accrual method) charged to or on behalf of sponsors and donors, but excluding noncash billings applicable to transactions such as trade and barter sales, for the use of the broadcasting facilities of the station from:

(a) local programs (including programs furnished by a network not licensed as a network by BMI and programs originating from another station which holds a BMI Single Station License Agreement);

(b) network programs;

(c) cooperative programs;

(d) simulcast programs;

(e) contributions and donations; and

(f) the cash portion of billings attributed to Time Brokers or providers of "program services" in "barter" arrangements by such parties that have no direct or indirect managerial ownership or connection with LICENSEE

(2) When reporting on a "Cash Receipts Basis" (see Paragraph 5.B.), all cash payments made by or on behalf of sponson and donors for the use of the radio broadcasting facilities of the station in the areas indicated in Paragraph 2.F.(1)(a) through *(f)* above.

(3) Gross Revenue shall also include all billings on behalf of (if reponing on a Billing Basis) and payments made directly to (if reporting on a Cash Receipts Basis), or as authorized by, LICENSEE, its employees, representatives, agents or any other person acting on LICENSEEs behalf, and all billings on behalf of and payments made to any company, firm or corporation under the same or substantially the same ownership, management or control as LICENSEE. Such billings and payments shall not include billings on behalf of and payments made to third parties, such as networks or program suppliers, that are not under the same ownership, management or control as the LICENSEE, or noncash payments such as payments in *goods* or services commonly referred to as trade or barter. Subject to Paragraph 2.D., above, if LICENSEE is owned or controlled by a network, Gross Revenue shall not include billings by or cash payments to the network.

(4) In the event LICENSEE acts as a Local Manager for another station's facilities, *Gross* Revenues shall also include all billings charged to, or cash payments made by, sponsors or donors for the use of the managed station's facilities in the areas indicated in Paragraph 2.F.(1)(a) through (f), above, subject to the terms of any LMA-92-A Agreement entered into by LICENSEE pursuant to Paragraph 8, below.

(5) In the event that LICENSEE owns or controls one or more stations which are licensed by BMI under separate Blanket or Per Program license agreements, and LICENSEE's Gross Revenues are derived from any source, either in whole or in part, as the result of offerings of the stations' broadcast facilities in combination, LICENSEE shall *make* an allocation on a reasonable basis of the *combined* Gross Revenues and applicable deductions when filing Annual Statements and/or Annual Financial Reports required under the terms of the BMI Single Station Radio Blanket and Per Program License Agraments.

G. "Net Revenue" shall mean:

(1) When reporting on a Billing Basis, Gross Revenue

reduced by,

(i) bad debts written off (increased by any bad debt recoveries) or rebates paid;

(ii) rate card discounts (cash, quantity and/or frequency actually allowed); and

(ii) advertising agency commissions actually incurred (not to exceed 15% of commissionable sales).

(2) When reporting on a Cash Receipts Basis, Gross Revenue *reduced* by advertising agency commissions actually incurred (not to exceed 15% of commissionable sales). The deduction for advertising agency commissions shall not be permitted if LICENSEE reports its net cash received from such agency sales as Gross Revenue

H. "Adjusted Net Revenue" shall mean Net Revenue less any sums received for the broadcasting of local political programs.

I. "Amount Subject to BMI Fee" shall mean Adjusted Net Revenue (Short Method Option—See Paragraph 4.A.) or, at the option of LICENSEE Adjusted Net Revenue less the total of the following itemized deductions to the extent they exceed 15% of Adjusted Net Revenue (Long Method Option—See Paragraph 4.B.):

(1) Net Talent Fees Allowed. All compensation in excess of the Total Yearly Amount set forth below actually paid by the station directly to "on-air" personnel acting as: (a) master of ceremonies or disk jockey on musical programs; (b) vocalist or instrumentalist engaged for a special program; (c) featured newscaster or news commentator; (d) featured sportscaster; (e) master of ceremonies on an entertainment program; or (f) announcer. If such person(s) has a 40% or more ownership interest in the station, this deduction shall not be allowed. If such person(s) holds a managerial capacity at the station and spends less than 100% of his or her time performing any of the duties enumerated in this Paragraph 2.I.(1), the total compensation amount shall be reduced in proportion to the amount of time spent on said duties.

Station's Annual Adjusted Net Revenue	Total Yearly Amount
Less than $50,000	$ 6,200
$ 50,000 to $149,999	18,600
$150,000 to $299.999	27.900
$300,000 to $499.999	41,900
$500,000 to $749,999	46.500
$750,000 to $999,999	53,700
$1,000,000 and over	62,000

The names, description of on-air duties and compensation must be indicated separately on the Annual Statement supplied by BMI. If the Annual Statement covers less than a full calendar year, Adjusted Net Revenue must be annualized, and the corresponding Total Yearly Amount must be prorated over the reporting period.

(2) News Service and Audio News Service. LICENSEE may deduct the actual payment made by it to an independent supplier of news service (e.g., AP, UPI), whether for hard or electronic copy or audio service. These costs must be for general news services and must be paid to an independent supplier of news service.

(3) The actual cost incurred by the station for a specific local commercial program for: (a) payments to the telephone company or similar transmission facility for remote pick-up necessary to broadcast such program from outside the station's studios; and (b) rights for broadcasting a sports or other special event but not to exceed the amount actually paid to or for the original holder of the broadcast rights for the program.

J. "Time Broker" shall mean any entity that has no direct or indirect managerial ownership or connection with LICENSEE that purchases and resells any portion of the station's air time or the station's radio broadcasting facilities.

K. "Local Manager" shall mean any entity not under common ownership or control of LICENSEE which is authorized to resell 10% or more of the station's air time and (1) simulcasts or sells announcements on the station in combination with a radio station owned or operated by the entity, which station has entered into a BMI Single Station Radio License Agreement; or (2) has assumed, contractually or otherwise, responsibility for the management of the station. An entity which would otherwise qualify as a Local Manager but which is authorized to resell less than 10% of the station's air time shall be deemed to be a Time Broker.

L. "Local Management Agreement" shall mean any agreement under which any other entity becomes a Local Manager in regard to the station licensed under this License Agreement

3. BMI Grant.

A. BMI hereby grants to LICENSEE, for the Term hereof, a non-exclusive license to perform, by radio broadcasting on LICENSEE's local programs by the station, non-dramatic performances of all musical works, the right to grant public performance rights of which BMI may, during the Term hereof, own or control.

B. The rights granted hereby shall not include the right to perform more than thirty (30) minutes of a full-length dramatic or dramatico-musical work (or a substantial part of a short dramatic or dramatico-musical work) such as an opera, operetta musical show or ballet, but this exclusion shall not apply to such performances from (1) a score originally written for and performed as part of a radio program. or (2) the original cast, soundtrack or similar album of a dramatic or dramatico-musical work other than an opera.

C. The performances licensed hereunder may originate at any place, whether or not such place is licensed to publicly perform the musical works licensed hereunder. and regardless of the manner, means or methods of such origination. Nothing in this License Agreement shall be deemed to grant a license to anyone authorizing any public performance in such other place of any such composition.

D. Nothing herein shall be construed as authorizing LICENSEE to grant to any cable system (including MMDS or similar wireless services) the right to retransmit to the public or publicly perform by any means. method or process whatsoever. any of the musical compositions licensed hereunder.

E. BMI will. upon specific reasonable written request made by LICENSEE, indicate whether a number of specific musical compositions listed by LICENSEE are licensed by BMI. LICENSEE shall provide: (1) title; (2) writer/composer; (3) publisher; and (4) recording artist of each musical composition requested to be identified. In the event LICENSEE does not provide BMI with all of the information requested herein, BMI will attempt to identify whether such musical compositions are licensed by BMI. but will be under no obligation to make such identifications.

4. **Fee Computation Options; Minimum Fee; Taxes.**

A. *SHORT METHOD OPTION:*
The fee under the Short Method Option will be calculated as follows:

Gross Revenue*

Less:
(1) Bad debts written off or rebates paid
(2) Rate card discounts and
(3) Advertising agency commissions

Equals:
Net Revenue*

Less:
Net Revenue from Political Broadcasting

Equals:
Adjusted Net Revenue* (Amount Subject to BMI Fee*)
Apply the applicable rate for the calendar year indicated:

Year	If Net Revenue is $150,000 or greater	If Net Revenue is less than $150,000
1992	1.475%	1.328%
1993	1.510%	1.359%
1994	1.535%	1.382%
1995	1.585%	1.427%
1996	1.605%	1.445%

Equals:
License Fee

B. *LONG METHOD OPTION:*
The fee under the Long Method Option will be calculated as follows:

Gross Revenue.

Less:
(1) Bad debts written off or rebates paid
(2) Rate card discounts and
(3) Advertising agency commissions

Equals:
Net Revenue*

Less:
Net Revenue from Political Broadcasting

Equals:
Adjusted Net Revenue.
Less amount by which sum of the following exceeds 15% of Adjusted Net Revenue:
(1) Net Talent Fees Allowed
(2) News Services
(3) Remote Lines
(4) Broadcast Rights

Equals:
Amount Subject to BMI Fee*
Apply the applicable rate for the calendar year indicated:

Year	If Net Revenue is $150,000 or greater	If Net Revenue is less than $150,000
1992	1.475%	1.328%
1993	1.510%	1.359%
1994	1.535%	1.382%
1995	1.585%	1.427%
1996	1.605%	1.445%

Equals:
License Fee

*DEFINED IN PARAGRAPH 2

C. In either case LICENSEE shall pay a minimum fee per calendar year for each year this License Agreement is in effect in the amount of $412 for 1992, and for each subsequent year an amount equal to the minimum fee for the prior year adjusted to reflect any percentage increase in the Consumer Price Index (National, All Items) between October of the preceding year and October of the next preceding year.

D. In the event that the payment of any license fee to BMI by LICENSEE pursuant to this License Agreement causes BMI to become liable to pay any state or local tax which is based upon the license fees received by BMI from licensees, the LICENSEE agrees to pay to BMI the full amount of such tax together with LICENSEE's fee payment(s) as invoiced by BMI; provided. however, that (1) BMI shall make reasonable efforts to be exempted or excused from paying such tax, and (2) BMI is permitted by law to pass through such tax to LICENSEE

5. Annual Statements; LICENSEE Breach.

A. Commencing on or before April 1, 1993, and on or before April 1 of each year thereafter, LICENSEE shall render Annual Statements to BMI, on forms supplied by BMI. covering the period of the preceding calendar year with respect to billings and/or cash receipts for the use of the facilities of the station for the broadcasting of local programs. If LICENSEE reports via the Long Method Option, it must show all deductions in order to arrive at Amount Subject to BMI Fee as herein provided. In the event that LICENSEE shall fail to make payment or render any report or Annual Statement under this License Agreement, when and as due. BMI may, in addition to any and all other remedies which it has at law or in equity, terminate this License Agreement upon thirty (30) days' notice in writing, and this License Agreement shall thereupon so terminate at the end of such period unless said default shall previously have been cured. The right to cancel shall be in addition to any and all other remedies which BMI may have No waiver by BMI of full performance of this License Agreement by LICENSEE in any one or more instances shall be deemed a waiver of the right to require full and complete performance of this License Agreement thereafter or of the right to cancel this License Agreement in accordance with the terms of this Paragraph 5.

Reporting Basis

B. (1) LICENSEE must report for the Term of this License Agreement on a Billing Basis unless:

(a) LICENSEE has filed its 1991 and 1992 Annual Statements on a Cash Receipts Basis, or

(b) LICENSEE is a new owner of the station, which was previously licensed by BMI. and both the prior licensee maintained and LICENSEE maintains the books and records of account of the station on a Cash Receipts Basis.

(2) If LICENSEE reported on a Cash Receipts Basis for calendar year 1992, LICENSEE may report for the Term of this License Agreement on a Billing Basis, but only *after* paying any fees owed BMI for receipts accrued in calendar year 1992 but not reported to BMI, and after receiving Written permission from BMI. However, nothing herein shall be interpreted to permit LICENSEE to change the basis of reporting retroactively.

(3) All billings made prior to the termination of this License Agreement with respect to local radio broadcasts made during the Term hereof shall be accounted for by LICENSEE as and when such billings are made by LICENSEE

C If any Annual Statement is not received by BMI within sixty (60) days after the due date, LICENSEE will be required to use the Short Method Option for such statement

Joint Annual Statement

D. If LICENSEE owns an AM and FM station in the same market, LICENSEE will be governed as follows:

(1) If LICENSEE filed a joint Annual Statement for its first contract year of this Licente Agreement for said AM/FM stations, LICENSEE must continue to file Annual Statements on a combined basis for the duration of this License Agreement If one of the stations is sold *after* the initial joint Annual Statement has been filed by LICENSEE, no other station may be substituted in place of the station sold. Under no circumstances may a joint Annual Statement be filed with BMI where the AM/FM stations are in separate markets.

(2) If LICENSEE filed separate Annual Statements for its first contract year of this License Agreement for the AM/FM stations, LICENSEE must continue to file separate Annual Statements for said AM/FM stations for the duration of this License Agreement.

Estimated Fees

E. For each month during the Term hereof LICENSEE shall, on or before the first day of the following month, pay to BMI a sum qual to one twelfth of the annual fee payable hereunder for the preceding calendar year (if less than a calendar year, said sum shall be annualized), adjusted to reflect the percentage increase in the Consumer Price Index (National, All Items) between October of the preceding year and October of the next preceding year; provided, however, that if, as and when any Annual Statement required to be supplied to BMI by LICENSEE pursuant to this Paragraph 5 is not received when due, all subsequent monthly payments due hereunder shall be increased by an amount equal to 24% thereof, and such increase shall remain in effect up to and including the month in which any such overdue Statement is finally received by BMI. Notwithstanding any of the foregoing, in any *calendar* year of the Term hereof, as of the month when BMI receives the Annual Statement required to be supplied by Paragraph 5.A. hereofapplicableto any immediately prior year, any adjustment required by a discrepancy between prior billings and monthly payments actually due in accordance with this Paragraph 5.E. shall, at BMI's option, be prorated over the remaining monthly payments due during that calendar year.

Adjustments

F. (1) For *calendar* year 1992, if the annual license fee exceeds the amount previously billed for that year. LICENSEE shall pay any such additional amount to BMI within thiiy (30) days of invoicing by BMI.

(2) If the annual license f a for any calendar year of the Term subsequent to 1992 exceeds the monthly installments applicable to such year's fee, LICENSEE shall pay any such additional amount to BMI at the time the Annual Statement is due

(3) If the amount paid by LICENSEE for any calendar year exceeds the annual license fee due for said year. LICENSEE will be entitled to a credit of the overage paid; provided however, that if the overage paid is greater than three times the monthly payments required by Paragraph 5.E. for said calendar year, BMI shall, within thirty (30) days of receipt of written request from LICENSEE, refund the excess payment; and provided

further that LICENSEE shall be entitled to a refund only if the overage (which exceeds three times LICENSEE's monthly payments) by LICENSEE, results in a net balance due LICENSEE. In this event, the amount of the refund shall not exceed the amount of the net balance due the LICENSEE. Any fees subject to a good faith dispute as a result of a BMI audit shall not be considered in determining whether there is a net balance due LICENSEE for purposes of this subparagraph.

Late Payment Charge

G. BMI may impose a late payment charge of 1½% per month from the date the payment was due on any monthly or annual payment that is received by BMI more than one month after the date payment was due.

Audits

H. (1) BMI shall have the right by its duly authorized representatives, during customary business hours, on notice in writing of not less than ten (10) business days, to examine the books and records of account of LICENSEE only to such extent as may be necessary to verify any Annual Statements required by this License Agreement. All data and information coming to BMI's attention as a result of any such examination of LICENSEE's books and records shall be held completely and entirely confidential and shall not be used by BMI other than in connection with its administration of this License Agreement.

(2) The period for which BMI may audit pursuant to Paragraph 5.H.(1) hereof shall be limited to four (4) calendar years preceding the year in which the audit is made; provided. that if an audit is postponed at the request of LICENSEE, and BMI grants such postponement, BMI shall have the right to audit for the period commencing with the fourth calendar year preceding the year in which notification of intention to audit was first given by BMI to LICENSEE Notwithstanding the above, BMI shall not audit LICENSEE's books and records for years prior to calendar year 1991, unless: (a) no Annual Statement was filed by LICENSEE for such earlier calendar year(s); or (b) the audit for calendar year 1991 or subsequent calendar year(s) pursuant to this License Agreement reveals a deficiency of 20% or more in license fees payable to BMI by LICENSEE. The four year limitation on BMI's right to audit shall not apply if LICENSEE fails or refuses after written notice from BMI to produce the books and records necessary to verify any report or statement required hereunder; however, in such instance BMI shall not audit for any reponed calendar years prior to 1989.

(3) In the event that any BMI audit reveals that additional license fees are owed to BMI. LICENSEE shall pay interest on such additional license fees of 1½% per month from the date(s) such fees should have been paid pursuant to this License Agreement if the underpayment is 7% or more of the annual license fee previously reported, and at least $1,000. LICENSEE shall pay interest on such additional license fees of 1½% per month beginning thirty (30) days after the date BMI invoices such additional license fees to LICENSEE if the underpayment is less than 7% or less than $1,000.

(4) If LICENSEE disputes all or part of BMI's claim for such additional license fees arising from an audit, LICENSEE shall, within thirty (30) days from the date BMI invoices additional fees. (a) notify BMI in writing, of the basis for such dispute and (b) pay to BMI any license fees not in dispute together with the applicable interest on additional license fees not in dispute in accordance with subparagraph (3) above. If there is a good faith dispute between LICENSEE and BMI with respect to all or part of the additional license fees which BMI has invoiced pursuant to this Paragraph, upon resolution of the disputed amount, subparagraph (3) shall govern payment of the interest due; provided, however, that no interest will be charged LICENSEE for the disputed license fees for the period beginning on the date of LICENSEEs written notice to BMI of the dispute and ending sixty (60) days after BMI responds to LICENSEEs notice of the dispute.

(5) Interest calculated in accordance with this Paragraph and concerning additional license fees which LICENSEE disputes in accordance with subparagraph (4) above shall be adjusted pro-rata to the amount arrived at by LICENSEE and BMI in resolution of the dispute with respect to additional license fees due.

I. The period for which LICENSEE may amend any Annual Statement submitted pursuant to this License Agreement shall be limited to four (4) calendar years (but in no event prior to calendar year 1991) following the year for which such statement was required to be filed pursuant to Paragraph 5.A.; provided, however, that if BMI audits for years prior to 1991, LICENSEE may amend its Annual Statement for such year(s). LICENSEE shall have the right to amend any portion of a previously submitted Annual Statement and the right to correct computational or reporting errors. O n a LICENSEE submits an Annual Statement to BMI pursuant to this License Agreement, LICENSEE may amend said Annual Statement only one time. If LICENSEE amends an Annual Statanent pursuant to this provision, the time for BMI to audit said Annual Statement will be four (4) years after the filing of *said* amended *Annual* Statement by LICENSEE.

6. **Per Program Option.**

The BMI Single Station Radio P a Program License Agreement for the Term ending December 31, 1996 is being offered to LICENSE simultaneously with this License Agreement. In accepting this License Agreement LICENSEE acknowledges that it has been offered the option of entering into either this License Agreement or the BMI Single Station Radio Per Program License Agreement with BMI. LICENSEE may, as of the first day of any month, upon not less than thirty (30) days written notice to BMI elect to enter into the BMI Single Station Radio Per Program License Agreement, provided LICENSEE is current in all payments (excluding payments subject to a good faith dispute as a result of a BMI audit), reports and Annual Statements required by the BMI Single Station Radio Blanket License Agreement as of the effective date of LICENSEEs election.

7. Indemnification.

BMI agrees to indemnify, save and hold harmless and to defend LICENSEE, its advertisers and their advertising agencies, and its and thek officers, employees and artists, from and against all claims, demands and suits that may be made or brought against them or any of than with respect to the performance under this License Agreement of any material licensed hereunder; provided that this indemnity shall not apply to broadcasts of any musical work performed by LICENSEE after written request from BMI to LICENSEE that LICENSEE refrain from performance thereof. LICENSEE agrees to give BMI immediate notice of any such claim. demand or suit, and agrees immediately to deliver to BMI all papers pertaining thereto. BMI shall have full charge of the defense of any such claim. demand or suit, and LICENSEE shall cooperate fully with BMI therein.

8. **Local Management Agreement**

A. In the event LICENSEE enters into a Local Management Agreement as defined in Paragraph 2.L. hereof, within thirty (30) days of such agreement (1) LICENSEE shall provide BMI with a copy of such agreement and (2) LICENSEE and Local Manager shall provide BMI with two (2) fully executed copier of BMI's LMA-92-A Agreement, a sample copy of which is annexed hereto and made part hereof. The fully executed LMA-92-A Agreement makes Local Manager a party to this License Agreement. and this License Agreement shall be deemed amended by said LMA-92-A Agreement.

B. In the event LICENSEE becomes a Local Manager by entering into a Local Management *Agrement* with another station, LICENSEE shall notify BMI within thirty (30) days of entering into the agreement.

C. In the event that LICENSEE and/or Local Manager do not provide to BMI, on a timely basis, the documentation required by Paragraph 8.A., this License Agrament may be terminated by BMI on ten (10) days' written notice.

D. In the event that the Local Management Agreement provided to BMI terminates prior to its stated termination date, LICENSEE and Local Manager shall immediately notify BMI of such termination.

9. Assignment.

This License Agreement shall be non-assignable except to the person. firm or corporation acquiring the Federal Communications Commission license of the station, and upon assignment to such station and upon acceptance in form approved by BMI of the application of LICENSEE hereunder, LICENSEE shall be relieved of future liability under this License Agreement as long as all Annual Statements have ban filed by LICENSEE and all fees due BMI under this License Agreement have been paid to BMI.

10. **Arbitration.**

All disputes of any kind. nature or description arising in connection with the terms and conditions of this License Agreement shall be submitted to the American Arbitration Association in the City and State of New York for arbitration under its then prevailing ruler. the arbitrator(s) to be selected as follows: Each of the parties hereto shall by written notice to the other have the right to appoint one arbitrator. If. within ten (10) days following the giving of such notice by one party, the other shall not, by written notice, appoint another arbitrator, the first arbitrator shall be the sole arbitrator. If two arbitrators are so appointed, they shall appoint a third arbitrator. If ten (10) days elapse after the appointment of the second arbitrator and the two arbitrators are unable to agree upon the third arbitrator, then either party may, in Writing, request the American Arbitration Association to appoint the third arbitrator. The award made in the arbitration shall be binding and conclusive on the parties and judgment may be, but need not be, entered in any court having jurisdiction. Such award shall include the fixing of the costs, expenses and reasonable attorneys' fees of arbitration, which shall be borne by the unsuccessful party.

MISCELLANEOUS

11. LICENSEE, upon written request from BMI made not less than one (1) week's notice specifying the period to be covered, agrees to furnish to BMI (upon forms to be supplied by BMI) a report of LICENSEE's performances of all musical works, indicating the compositions performed by title, writer/composer and artist, or by such other convenient method as may be designated by BMI, but such report need not be furnished for more than one (1) week of each year of the Term.

12. In the event that the Federal Communications Commission revokes or fails to renew the broadcasting License of LICENSEE or in the event that the governmental rules and regulations applicable to the station are suspended or amended so as to forbid the broadcasting of commercial programs by LICENSE LICENSEE may notify BMI thereof, and BMI, within ten (10) days of the receipt of such notice shall, by written notice to LICENSEE, at BMI's option, either terminate or suspend this License Agreement and all payments and services hereunder for the period that such condition continues. In the event that BMI elects to suspend this License Agreement, such suspension shall not continue for longer than six (6) months, and this License Agreement shall automatically terminate at the end of six (6) months' suspension. In the event that the condition giving rise to the suspension shall continue for less than six (6) months, BMI at its option, and on written notice to LICENSEE, may reinstate this License Agreement at any time within thirty (30) days after the cessation of such condition.

13. In the event that any law now or hereafter enacted of the state, or political subdivision thereof, in which the station and/or LICENSEE is located shall result in major interference with BMI's operations or in the refusal of a substantial number of radio stations therein to enter into license agreements with BMI or to make payments to BMI, BMI shall have the right at any time to terminate this License Agreement on no less than sixty (60) days' written notice to LICENSEE.

14. Any notice required or permitted to be given under this License Agreement shall be in writing and shall be deemed duly given when sent by ordinary first-class U.S. mail to the party for whom it is intended, at its address hereinabove stated, or any other address which either party hereto may from time to time designate for such purpose, and when such notice is so mailed it shall be deemed given upon the mailing thereof. Any such notice sent to BMI shall be to the attention of the Licensing-Telecommunications Department. Any such notice sent to LICENSEE shall be to the attention of the person signing this License Agreement on behalf of LICENSEE or such other person as LICENSEE may advise BMI in writing.

15. On written notice to LICENSEE, BMI may, effective with such notice, withdraw from the license granted hereunder any musical work as to which any legal action has been instituted or a claim made that BMI does not have the right to license the performing rights in such work or that such work infringes another composition.

16. This License Agreement shall enure to the benefit of and shall be binding upon the parties and their respective successors and assigns, but no assignment shall relieve the parties of their respective obligations under this License Agreement.

17. This License Agreement constitutes the entire understanding between the parties, shall not be binding until signed by both parties and cannot be waived or added to or modified orally, and no waiver, addition or modification shall be valid unless in writing and signed by the parties. This License Agreement, its validity, construction and effect shall be governed by the laws of the State of New York. The fact that any provisions herein are found to be void or unenforceable by a court of competent jurisdiction shall in no way affect the validity or enforceability of any other provisions. All headings in this License Agreement are for the purpose of convenience and shall not be considered to be part of this License Agreement

BROADCAST MUSIC, INC.	______________________ LICENSEE (Legal Name)
By ______________________ (Signature)	By ______________________ (Signature)
______________________ (Print Name of Signer)	______________________ (Print Name of Signer)
______________________ (Title of Signer)	______________________ (Title of Signer)

PLEASE *COMPLETE* SHADED AREA ONLY

LMA AGREEMENT

Whereas, radio station ______________________ ("STATION") has entered into a Local Management Agreement with ______________________ ("LOCAL MANAGER") for the period ______________________ through ______________________; and

Whereas, STATION and LOCAL MANAGER wish to add LOCAL MANAGER as a party to the Single Station Radio License Agreement in effect between STATION and BMI ("the License Agreement") with all of the rights and obligations of LICENSEE as set forth in the License Agreement for the period of the Local Management Agreement beginning January 1.1992 and ending at the time referred to above;

It is hereby agreed as follows:

1. For all periods that STATION simulcasts or is sold in combination with another radio station owned or operated by LOCAL MANAGER ("MANAGERs STATION") that has a BMI Single Station Radio License Agreement, all Gross Revenue (as defined in the License Agreement) of STATION shall be reported as follows:

a. All LOCAL MANAGER Gross Revenue relating to STATION will be included in LOCAL MANAGERs license fee reports for MANAGER's STATION. If such Gross Revenue constitutes all Gross Revenue for STATION, no license fee or license fee reports will be required of STATION.

b. The balance of STATION's Gross Revenue will be included in STATION's license fee reports.

c. Amounts payable by LOCAL MANAGER to STATION pursuant to the Local Management Agreement shall not be reportable by STATION or deductible by MANAGER's STATION.

d. In the event that STATION and MANAGER's STATION have different forms of BMI License Agreement, all LOCAL MANAGER's Gross Revenue relating to programs of STATION which are simulcast or sold in combination with MANAGER's STATION shall be apportioned between STATION and MANAGER's STATION in the same ratio as the Adjusted Net Revenue of STATION and MANAGER's STATION bear to each other for the most recent year prior to the Local Management Agreement reported by STATION and MANAGER's STATION to BMI (annualized for any period less than a year). Any such Gross Revenue apportioned to, and reported for, STATION pursuant to this paragraph shall not be reportable by LOCAL MANAGER on its license fee reports for MANAGER's STATION.

2. If STATION fully simulcasts programs broadcast by MANAGERs STATION and has no separate programs, STATION and LOCAL MANAGER agra to maintain the same form of BMI license (blanket or per program) for STATION as LOCAL MANAGER has for MANAGER'S STATION. In the event that LOCAL MANAGER has a different form of license for MANAGERs STATION at the time this agreement is executed, it is agreed that such other form of license shall be substituted in place of the License Agreement, and the appropriate documentation shall be executed

In the event that STATION and MANAGER's STATION have the per program form of license at the time this agrament is executed, and LOCAL MANAGER subsequently changes or is converted to the blanket form of license, such change or conversion shall be deemed to apply as well to STATION.

3. For all periods that STATION has a per program license agreement, MANAGER's STATION shall submit the reports required by Paragraph 4 of the per program license for all programs provided by MANAGER's STATION which are broadcast by STATION, and STATION shall submit such reports for all other programs broadcast by STATION. If STATION fully simulcasts programs broadcast by MANAGER's STATION and has no separate programs. and if all Gross Revenue relating to STATION is included in LOCAL MANAGERs license fee reports for MANAGER's STATION in accordance with Paragraph 1a above, STATION shall not be required to submit separate reports pursuant to Paragraph 4 of the per program license.

4. If STATION has a Local Management Agreement With a LOCAL MANAGER that does not own or operate another local radio station that has a BMI Single Station Radio License Agreement, then all Gross Revenue relating to STATION shall be reported as follows:

a. All LOCAL MANAGER Gross Revenue relating to STATION will be included in LOCAL MANAGER's license fee reports to BMI. If such revenue constitutes all Gross Revenue for STATION, no license fee or license fee reports will be required of STATION.

b. The balance of STATION's Gross Revenue will be included in STATION's License fee reports.

c. Amounts payable by LOCAL MANAGER to STATION pursuant to the Local Management Agreement shall not be reportable by STATION, or deductible by LOCAL MANAGER

d. If STATION's License *Agreement* is a per program license agreement, then LOCAL MANAGER will be responsible for submitting Monthly Music Reports required by Paragraph 4 of the License Agreement for the programming covered by the Local Management Agreement.

5. STATION and LOCAL MANAGER jointly designate the following single address for billing and other regular correspondence, and the following single address for any notices in accordance with the license agreement (Paragraph 14 of the blanket license or Paragraph 24 of the per program license):

Billing Address: ______________________ Notice Address: ______________________

______________________ ______________________

______________________ ______________________

6. In the event that the Local Management Agreement between STATION and LOCAL MANAGER terminates, STATION and LOCAL MANAGER shall notify BMI of the termination within 20 days, and submit all required statements, reports and payments through the date of said termination. In the event that both STATION and LOCAL MANAGER fail to notify BMI of the termination of the Local Management Agreement between STATION and LOCAL MANAGER, then both STATION and LOCAL MANAGER shall remain obligated under this agreement for all statements, reports and payments.

____
LICENSEE (Legal Name)

BY: ______________________
(Signature)

____
(Print Name of Signer)

____
(Title of Signer)

____
LOCAL MANAGER (Legal Name)

____
(Call Letters, if applicable)

BY: ______________________
(Signature)

____
(Print Name of Signer)

____
(Title of Signa)

Accepted and agreed:
BROADCAST MUSIC, INC.

BY: ______________________

____
(Title)

Date: ______________________

BMI

2000 BMI Radio Station Interim License Agreement

The following are the terms and conditions of your station's 2000 BMI Radio Station Interim License Agreement (hereinafter 'Interim License Agreement"), pending the outcome of negotiations for find agreements between BMI and the Radio Music License Committee (the "RMLC") or, if necessary, a determination by the BMI Rate Court of appropriate license terms pursuant to United States of America v. Broadcast Music, Inc. (In the Matter of the Application of Hicks Broadcasting of Indiana, et al.) ,No. 64 Civ. 3787 (S.D.N.Y.).

It is hereby agreed as follows:

1. The term of Station's Interim License Agreement shall begin on ____________ (date ownership began). The Interim License Agreement shall embody each and every term and condition except for the duration of the License Agreement, as set forth in the BMI Single Station Radio License (form Radio-92) annexed hereto as Schedule A and incorporated herein by reference, and pay the rate set forth therein for the year 1996. The Interim License Agreement shall continue until a find agreement is reached as a result of the ongoing negotiations between BMI and the RMLC or as a result of a BMI Rate Court proceeding pursuant to United States of America v. Broadcast Music, Inc. (In the Matter of the Application of Hicks Broadcasting of Indiana, et al.), No. 64 Civ. 3787 (S.D.N.Y.).

2. Station agrees that Station will be bound by the final BMI license agreement reached as a result of the negotiations between BMI and the RMLC or a BMI Rate proceeding with the RMLC and that the fees agreed to by BMI and RMLC or as determined by the BMI Rate Court in such a proceeding shall be applied retroactively to the date of the commencement of the term of this agreement. As such, Station shall be obligated to pay BMI any monies owed by BMI as a result of such retroactive adjustment of fees, and BMI shall be obligated to pay Station any monies owed Station as a result of such retroactive adjustment of fees.

3. Station hereby waives its rights to make an application for reasonable fees to BMI, or to make an application to the BMI Rate Court.

Station's agreement to the above terms and conditions shall be evidenced by the signature below of an individual duly authorized to bind Station to this Interim Agreement.

Call Letters: ______________________

City: ______________________

State: ______________________

(PLEASECHECK ONE)
License Type ☐ Blanket ☐ Per Program

Accepted:
BROADCAST MUSIC, INC.
By: ______________________

Title: ______________________
under

Date: ______________________

____
Licensee of Station (as listed with the FCC)

____
Authorized Signature

____
Print Name of Signatory

____
Print Title of Signatory

(a) If corporation, signatory must be an officer. Print corporate office held under signature;

(b) If partnership, print the word "partner"

signature of signing partner;

(c) If individual owner, print "individual owner" under signature

XJAF 7001

The parties hereto mutually agree as follows:

1. GRANT OF RIGHTS

Effective as of January 1 2000 (the "Effective Date") SESAC grants to LICENSEE the non-exclusive license to publicly perform such nondramatic musical compositions as SESAC may during the period hereof have the right to so license solely by radio broadcasting on the following radio station (the "Station"):

Current Call letters: Frequency:
AM: Yes O if yes, then, Fulltime Yes O NO O
FM: Yes O
FCC City of License: ,

Station's Metro Survey Area ("MSA") as designated by Arbitron.
Choose One
or
County in which the FCC City of License is located
and the 1990 U.S. Census County Population Choose One

Station's High One Minute Spot Rate as reported to SESAC ("Spot Rate") $

2.LIMITATION OF GRANT

A. Except as set forth above, LICENSEE shall not have the right to broadcast, televise, or otherwise perform, transmit, record, film, videotape or otherwise reproduce or capture by any means, medium, method, device or process now or hereafter known, any of the musical compositions and performances thereof licensed hereunder, nor shall LICENSEE have the right to grant to any receiver of the broadcast or any other party any such right. This license excludes any experimental station of any kind, and background music service by means of multiplex, simplex, or like device.

B. "GRAND RIGHTS" are not included in this License. "GRAND RIGHTS" include, but are not limited to, the right to perform in whole or in part, dramatico-musical and dramatic works in a dramatic setting.

C. SESAC reserves the right to prohibit upon written notice, the performance of any musical composition licensed hereunder as to which any action has been instituted or a claim made that SESAC does not have the right to license the performance rights in such composition. In addition, SESAC reserves the right to prohibit upon written notice, for any reason deemed appropriate in the exercise of its sole discretion, the performance of any of the musical compositions licensed hereunder, provided only that the number of musical compositions so prohibited does not exceed ten percent (10%) of the total number of musical compositions licensed hereunder.

3. LICENSE FEE

A. In consideration of the grant of rights herein, LICENSEE shall pay to SESAC an annual license fee as determined by the SESAC's Schedule of Annual Performance License Fees For Radio ("Fee Schedule") then in effect.

B. LICENSEE represents and warrants that the Station's high one minute spot rate contained in Paragraph 1. above is true and correct.

C. Thirty days before the beginning of each contract year of this Agreement LICENSEE shall notify SESAC of its current high one minute spot rate. LICENSEEs annual fee for the next ensuing contract year shall be adjusted in accordance with the FEE SCHEDULE to reflect any change in the Station's Spot Rate, population or MSA from that set forth in Paragraph 1.A. If LICENSEE shall fail to report its current high one minute spot rate, then LICENSEE's fee for the next ensuing contract year shall be increased by eight percent (8%) above the fee set forth in the FEE SCHEDULE.

D. In the event that LICENSEEs fee shall increase as a result from a change in the FEE SCHEDULE, LICENSEE shall have the right to terminate this Agreement effective as of the date of such increase, provided that written notice of termination by Certified Mail, return receipt requested is given to SESAC within thirty (30) days after SESAC sends by certified mail written notice of such change to LICENSEE.

E. Each annual license fee shall be paid as follows: (CHECK ONE)

- ○ Annually, on or before the first day of each contract year;
- ○ Semi-Annually, on or before the first day of each semi-annual period of each contract year;
- ○ Quarterly, on or before the first day of each quarter of each contract year: or
- ⊙ Monthly, on or before the first day of each month of each contract year.

F. In the event that SESAC is determined by the taxing authority or courts of any state in which LICENSEE conducts its operations to be liable for the payment of a gross receipts, sales, use, business use or other tax which is based on the amount of SESAC's receipts from LICENSEE, then LICENSEE shall reimburse SESAC, within thirty (30) days of demand therefor, for LICENSEEs pro rata share of any such tax derived from receipts received from LICENSEE.

4. BREACH AND CURE, LATE PAYMENT CHARGE

A. In the event LICENSEE is in arrears for any payment or has breached any other term of this agreement, SESAC may give LICENSEE thirty (30) days notice in writing to cure such breach or default. In the event that the breach or default is not cured within thirty (30) days of such notice, SESAC may at its election, cancel and terminate this agreement.

B. SESAC shall have the right to impose a late payment charge of one and one-half percent (1.5%) per month for any payment not received by SESAC within thirty days of billing therefor.

5. REPORTING OF WORKS; RIGHT Of VERIFICATION

A. LICENSEE shall furnish to SESAC, upon request, copies of its program records, logs, and all other records relating to the musical compositions performed on the station.

B. SESAC shall have the right on ten (10) days prior written notice, to examine during customary business hours, LICENSEEs books and records to such extent as may be necessary to verify any and all payments, statements, computations and reports rendered and accountings made or required hereunder. All data and information brought to SESAC's attention as a result of any examination shall be treated as confidential.

6. TERM OF LICENSE

A. Subject to the provisions of Paragraph 4. above, this agreement shall be in full force and effect for a period of one (1) year beginning on the date set forth in paragraph 1. above and shall continue thereafter in full force and effect for successive additional periods of one (1) year each. Either party may cancel and terminate this Agreement effective as of the last day of the initial or any renewal term upon giving ninety (90) days written notice to the other party by United States Certified Mail, Return Receipt Requested.

B. Notwithstanding anything to the contrary contained herein, SESAC may cancel and terminate this agreement: (I) at any time upon written notice in the event LICENSEE is adjudicated bankrupt, or a petition in bankruptcy is filed with respect to LICENSEE, or LICENSEE is declared or becomes insolvent: or (ii) upon thirty (30) days written notice by reason of any law, rule, decree, or other enactment having the force of law, by any authority, whether federal, state, local, territorial or otherwise, which shall result in substantial interference in SESAC's operation or any substantial increase in the cost of conducting its business.

7. CONTRACT CONSTRUCTION

A. This agreement has been read and is understood by both parties and contains their entire understanding. No waiver, addition or modification shall be valid unless in writing, executed with the same formality as this instrument. No waiver of any breach of this agreement shall be deemed a waiver of any subsequent breach of like or similar nature. There are no representations, promises or covenants other than contained herein.

B. This Agreement shall be governed by and subject to the laws of the State of New York, applicable to agreements made and to be wholly performed within such State. The fact that any provision of this agreement may be found to be void or unenforceable by a court of competent jurisdiction shall in no way affect the validity or enforceability of any other provision.

C. This agreement shall not be valid until accepted and executed in the name of SESAC by its authorized signatory.

D. This agreement shall be binding upon and inure to the benefit of the parties' legal representatives, successors, and assigns, but no assignment shall relieve the parties of their obligations under this agreement.

E. Captions and titles are for the convenience of the parties and shall be given no effect in the construction or interpretation of this agreement.

IN WITNESS WHEREOF, the parties have caused this agreement to be duly signed as of the day and year first written above.

LICENSEE	SESAC, Inc.
BY: X____________ (please sign here)	BY: ____________
(Type or print name)	TITLE: ____________
TITLE:	

SESAC

SESAC Schedule of Annual Performance License Fees for Commercial Radio Stations

The annual fee is determined by the population of persons 12+ in the station's Metro Survey Area as designated by Arbitron and the station's high one minute spot rate as reported to SESAC. In the event that the station is not in an Arbitron-designated Metro Survey Area, the U.S. Census population of the county in which the station's FCC City of License is located will determine market classification.

Market	Population		
AA	6,000,000		and over
A	2,000,000	-	5,999,999
B	1,000,000	-	1,999,999
C	500,000	-	999,999
D	250,000	-	499,999
E	100,000	-	249,999
F	50,000	-	99,999
G	10,000	-	49,999
H	0	-	9,999

2000 Radio Fee Schedule – Effective January 1 - December 31, 2000

	Market								
High One Minute Spot Rate	H	G	F	E	D	C	B	A	AA
0.00 - 2.49	468.00	552.00	684.00	816.00	984.00	1,152.00	1,332.00	1,668.00	2,016.00
2.50 - 4.99	516.00	600.00	732.00	852.00	1,032.00	1,200.00	1,368.00	1,716.00	2,052.00
0 - 7.49	552.00	648.00	768.00	900.00	1,068.00	1,248.00	1,416.00	1,752.00	2,100.00
.50 - 9.99	600.00	684.00	816.00	948.00	1,116.00	1,284.00	1,452.00	1,800.00	2,148.00
10.00 - 12.49	648.00	732.00	852.00	984.00	1,152.00	1,332.00	1,500.00	1,848.00	2,184.00
12.50 - 14.99	684.00	768.00	900.00	1,032.00	1,200.00	1,368.00	1,548.00	1,884.00	2,232.00
15.00 - 17.49	732.00	816.00	948.00	1,068.00	1,248.00	1,416.00	1,584.00	1,932.00	2,268.00
17.50 - 19.99	768.00	852.00	984.00	1,116.00	1,284.00	1,452.00	1,632.00	1,968.00	2,316.00
20.00 - 29.99	852.00	948.00	1,068.00	1,200.00	1,368.00	1,548.00	1,716.00	2,052.00	2,400.00
30.00 - 39.99	948.00	1,032.00	1,152.00	1,284.00	1,452.00	1,632.00	1,800.00	2,148.00	2,484.00
40.00 - 49.99	1,032.00	1,116.00	1,248.00	1,368.00	1,548.00	1,716.00	1,884.00	2,232.00	2,568.00
50.00 - 59.99	1,116.00	1,200.00	1,332.00	1,452.00	1,632.00	1,800.00	1,968.00	2,316.00	2,652.00
60.00 - 69.99	1,200.00	1,284.00	1,416.00	1,548.00	1,716.00	1,884.00	2,052.00	2,400.00	2,736.00
70.00 - 79.99	1,284.00	1,368.00	1,500.00	1,632.00	1,800.00	1,968.00	2,148.00	2,484.00	2,832.00
80.00 - 89.99	1,368.00	1,452.00	1,584.00	1,716.00	1,884.00	2,052.00	2,232.00	2,568.00	2,916.00
90.00 - 99.99	1,452.00	1,548.00	1,668.00	1,800.00	1,968.00	2,148.00	2,316.00	2,652.00	3,000.00
100.00 - 124.99	1,752.00	1,848.00	1,968.00	2,100.00	2,268.00	2,436.00	2,616.00	2,952.00	3,300.00
125.00 - 149.99	2,052.00	2,148.00	2,268.00	2,400.00	2,568.00	2,736.00	2,916.00	3,252.00	3,600.00
150.00 - 174.99	2,352.00	2,436.00	2,568.00	2,700.00	2,868.00	3,036.00	3,216.00	3,552.00	3,900.00
175.00 - 199.99	2,652.00	2,736.00	2,868.00	3,000.00	3,168.00	3,336.00	3,516.00	3,852.00	4,200.00
200.00 - 224.99	3,084.00	3,168.00	3,300.00	3,432.00	3,600.00	3,768.00	4,152.00	5,136.00	6,132.00
5.00 - 249.99	3,516.00	3,600.00	3,732.00	3,852.00	4,032.00	4,200.00	4,800.00	6,432.00	8,052.00
.00 - 274.99	3,936.00	4,032.00	4,152.00	4,284.00	4,452.00	4,632.00	5,436.00	7,716.00	9,984.00
275.00 - 299.99	4,368.00	4,452.00	4,584.00	4,716.00	4,884.00	5,052.00	6,084.00	9,000.00	11,904.00
300.00 And Over	4,800.00	4,884.00	5,016.00	5,136.00	5,316.00	5,484.00	6,720.00	10,284.00	13,836.00

2001 Radio Fee Schedule -- Effective January 1 - December 31, 2001

High One Minute Spot Rate	Market H	G	F	E	D	C	B	A	AA
0 - 2.49	528.00	624.00	768.00	912.00	1,104.00	1,296.00	1,488.00	1,872.00	2,256.00
2.50 - 4.99	576.00	672.00	816.00	960.00	1,152.00	1,344.00	1,536.00	1,920.00	2,304.00
5.00 - 7.49	624.00	720.00	864.00	1,008.00	1,200.00	1,392.00	1,584.00	1,968.00	2,352.00
7.50 - 9.99	672.00	768.00	912.00	1,056.00	1,248.00	1,440.00	1,632.00	2,016.00	2,400.00
10.00 - 12.49	720.00	816.00	960.00	1,104.00	1,296.00	1,488.00	1,680.00	2,064.00	2,448.00
12.50 - 14.99	768.00	864.00	1,008.00	1,152.00	1,344.00	1,536.00	1,728.00	2,112.00	2,496.00
15.00 - 17.49	816.00	912.00	1,056.00	1,200.00	1,392.00	1,584.00	1,776.00	2,160.00	2,544.00
17.50 - 19.99	864.00	960.00	1,104.00	1,248.00	1,440.00	1,632.00	1,824.00	2,208.00	2,592.00
20.00 - 29.99	960.00	1,056.00	1,200.00	1,344.00	1,536.00	1,728.00	1,920.00	2,304.00	2,688.00
30.00 - 39.99	1,056.00	1,152.00	1,296.00	1,440.00	1,632.00	1,824.00	2,016.00	2,400.00	2,784.00
40.00 - 49.99	1,152.00	1,248.00	1,392.00	1,536.00	1,728.00	1,920.00	2,112.00	2,496.00	2,880.00
50.00 - 59.99	1,248.00	1,344.00	1,488.00	1,632.00	1,824.00	2,016.00	2,208.00	2,592.00	2,976.00
60.00 - 69.99	1,344.00	1,440.00	1,584.00	1,728.00	1,920.00	2,112.00	2,304.00	2,688.00	3,072.00
70.00 - 79.99	1,440.00	1,536.00	1,680.00	1,824.00	2,016.00	2,208.00	2,400.00	2,784.00	3,168.00
80.00 - 89.99	1,536.00	1,632.00	1,776.00	1,920.00	2,112.00	2,304.00	2,496.00	2,880.00	3,264.00
90.00 - 99.99	1,632.00	1,728.00	1,872.00	2,016.00	2,208.00	2,400.00	2,592.00	2,976.00	3,360.00
100.00 - 124.99	1,968.00	2,064.00	2,208.00	2,352.00	2,544.00	2,736.00	2,928.00	3,312.00	3,696.00
125.00 - 149.99	2,304.00	2,400.00	2,544.00	2,688.00	2,880.00	3,072.00	3,264.00	3,648.00	4,032.00
150.00 - 174.99	2,640.00	2,736.00	2,880.00	3,024.00	3,216.00	3,408.00	3,600.00	3,984.00	4,368.00
175.00 - 199.99	2,976.00	3,072.00	3,216.00	3,360.00	3,552.00	3,744.00	3,936.00	4,320.00	4,704.00
200.00 - 224.99	3,456.00	3,552.00	3,696.00	3,840.00	4,032.00	4,224.00	4,656.00	5,760.00	6,864.00
225.00 - 249.99	3,936.00	4,032.00	4,176.00	4,320.00	4,512.00	4,704.00	5,376.00	7,200.00	9,024.00
250.00 - 274.99	4,416.00	4,512.00	4,656.00	4,800.00	4,992.00	5,184.00	6,096.00	8,640.00	11,184.00
275.00 - 299.99	4,896.00	4,992.00	5,136.00	5,280.00	5,472.00	5,664.00	6,816.00	10,080.00	13,344.00
300.00 And Over	5,376.00	5,472.00	5,616.00	5,760.00	5,952.00	6,144.00	7,536.00	11,520.00	15,492.00

2001

2002 Radio Fee Schedule -- Effective January 1 - December 31, 2002

High One Minute Spot Rate	Market H	G	F	E	D	C	B	A	AA
0.00 - 2.49	588.00	696.00	864.00	1,020.00	1,236.00	1,452.00	1,668.00	2,100.00	2,520.00
2.50 - 4.99	648.00	756.00	912.00	1,080.00	1,284.00	1,500.00	1,716.00	2,148.00	2,580.00
5.00 - 7.49	696.00	804.00	972.00	1,128.00	1,344.00	1,560.00	1,776.00	2,208.00	2,628.00
7.50 - 9.99	756.00	864.00	1,020.00	1,188.00	1,392.00	1,608.00	1,824.00	2,256.00	2,688.00
10.00 - 12.49	804.00	912.00	1,080.00	1,236.00	1,452.00	1,668.00	1,884.00	2,316.00	2,736.00
12.50 - 14.99	864.00	972.00	1,128.00	1,284.00	1,500.00	1,716.00	1,932.00	2,364.00	2,796.00
15.00 - 17.49	912.00	1,020.00	1,188.00	1,344.00	1,560.00	1,776.00	1,992.00	2,424.00	2,844.00
17.50 - 19.99	972.00	1,080.00	1,236.00	1,392.00	1,608.00	1,824.00	2,040.00	2,472.00	2,904.00
20.00 - 29.99	1,080.00	1,188.00	1,344.00	1,500.00	1,716.00	1,932.00	2,148.00	2,580.00	3,012.00
30.00 - 39.99	1,188.00	1,284.00	1,452.00	1,608.00	1,824.00	2,040.00	2,256.00	2,688.00	3,120.00
40.00 - 49.99	1,284.00	1,392.00	1,560.00	1,716.00	1,932.00	2,148.00	2,364.00	2,796.00	3,228.00
50.00 - 59.99	1,392.00	1,500.00	1,668.00	1,824.00	2,040.00	2,256.00	2,472.00	2,904.00	3,336.00
60.00 - 69.99	1,500.00	1,608.00	1,776.00	1,932.00	2,148.00	2,364.00	2,580.00	3,012.00	3,444.00
70.00 - 79.99	1,608.00	1,716.00	1,884.00	2,040.00	2,256.00	2,472.00	2,688.00	3,120.00	3,552.00
80.00 - 89.99	1,716.00	1,824.00	1,992.00	2,148.00	2,364.00	2,580.00	2,796.00	3,228.00	3,660.00
90.00 - 99.99	1,824.00	1,932.00	2,100.00	2,256.00	2,472.00	2,688.00	2,904.00	3,336.00	3,756.00
100.00 - 124.99	2,208.00	2,316.00	2,472.00	2,628.00	2,844.00	3,060.00	3,276.00	3,708.00	4,140.00
125.00 - 149.99	2,580.00	2,688.00	2,844.00	3,012.00	3,228.00	3,444.00	3,660.00	4,080.00	4,512.00
150.00 - 174.99	2,952.00	3,060.00	3,228.00	3,384.00	3,600.00	3,816.00	4,032.00	4,464.00	4,896.00
175.00 - 199.99	3,336.00	3,444.00	3,600.00	3,756.00	3,972.00	4,188.00	4,404.00	4,836.00	5,268.00
200.00 - 224.99	3,864.00	3,972.00	4,140.00	4,296.00	4,512.00	4,728.00	5,208.00	6,444.00	7,680.00
225.00 - 249.99	4,404.00	4,512.00	4,680.00	4,836.00	5,052.00	5,268.00	6,024.00	8,064.00	10,104.00
250.00 - 274.99	4,944.00	5,052.00	5,208.00	5,376.00	5,592.00	5,808.00	6,828.00	9,672.00	12,516.00
275.00 - 299.99	5,484.00	5,592.00	5,748.00	5,916.00	6,132.00	6,336.00	7,632.00		
300.00 And Over	6,024.00	6,132.00	6,288.00	6,444.00	6,660.00	6,876.00	8,436.00	12,900.00	17,352.00

2002

2003 Radio Fee Schedule -- Effective January 1 -December 31, 2003

Market

High One Minute Spot Rate	H	G	F	E	D	C	B	A	AA
0 - 2.49	660.00	780.00	960.00	1,140.00	1,380.00	1,620.00	1,860.00	2,340.00	2,820.00
.50 - 4.99	720.00	840.00	1,020.00	1,200.00	1,440.00	1,680.00	1,920.00	2,400.00	2,880.00
5.00 - 7.49	780.00	900.00	1,080.00	1,260.00	1,500.00	1,740.00	1,980.00	2,460.00	2,940.00
7.50 - 9.99	840.00	960.00	1,140.00	1,320.00	1,560.00	1,800.00	2,040.00	2,520.00	3,000.00
10.00 - 12.49	900.00	1,020.00	1,200.00	1,380.00	1,620.00	1,860.00	2,100.00	2,580.00	3,060.00
12.50 - 14.99	960.00	1,080.00	1,260.00	1,440.00	1,680.00	1,920.00	2,160.00	2,640.00	3,120.00
15.00 - 17.49	1,020.00	1,140.00	1,320.00	1,500.00	1,740.00	1,980.00	2,220.00	2,700.00	3,180.00
17.50 - 19.99	1,080.00	1,200.00	1,380.00	1,560.00	1,800.00	2,040.00	2,280.00	2,760.00	3,240.00
20.00 - 29.99	1,200.00	1,320.00	1,500.00	1,680.00	1,920.00	2,160.00	2,400.00	2,880.00	3,360.00
30.00 - 39.99	1,320.00	1,440.00	1,620.00	1,800.00	2,040.00	2,280.00	2,520.00	3,000.00	3,480.00
40.00 - 49.99	1,440.00	1,560.00	1,740.00	1,920.00	2,160.00	2,400.00	2,640.00	3,120.00	3,600.00
50.00 - 59.99	1,560.00	1,680.00	1,860.00	2,040.00	2,280.00	2,520.00	2,760.00	3,240.00	3,720.00
60.00 - 69.99	1,680.00	1,800.00	1,980.00	2,160.00	2,400.00	2,640.00	2,880.00	3,360.00	3,840.00
70.00 - 79.99	1,800.00	1,920.00	2,100.00	2,280.00	2,520.00	2,760.00	3,000.00	3,480.00	3,960.00
80.00 - 89.99	1,920.00	2,040.00	2,220.00	2,400.00	2,640.00	2,880.00	3,120.00	3,600.00	4,080.00
90.00 - 99.99	2,040.00	2,160.00	2,340.00	2,520.00	2,760.00	3,000.00	3,240.00	3,720.00	4,200.00
100.00 - 124.99	2,460.00	2,580.00	2,760.00	2,940.00	3,180.00	3,420.00	3,660.00	4,140.00	4,620.00
125.00 - 149.99	2,880.00	3,000.00	3,180.00	3,360.00	3,600.00	3,840.00	4,080.00	4,560.00	5,040.00
150.00 - 174.99	3,300.00	3,420.00	3,600.00	3,780.00	4,020.00	4,260.00	4,500.00	4,980.00	5,460.00
175.00 - 199.99	3,720.00	3,840.00	4,020.00	4,200.00	4,440.00	4,680.00	4,920.00	5,400.00	5,880.00
200.00 - 224.99	4,320.00	4,440.00	4,620.00	4,800.00	5,040.00	5,280.00	5,820.00	7,212.00	8,592.00
225.00 - 249.99	4,920.00	5,040.00	5,220.00	5,400.00	5,640.00	5,880.00	6,720.00	9,012.00	11,292.00
250.00 - 274.99	5,520.00	5,640.00	5,820.00	6,000.00	6,240.00	6,480.00	7,632.00	10,812.00	13,992.00
275.00 - 299.99	6,120.00	6,240.00	6,420.00	6,600.00	6,852.00	7,092.00	8,532.00	12,612.00	16,692.00
300.00 And Over	6,720.00	6,852.00	7,032.00	7,212.00	7,452.00	7,692.00	9,432.00	14,412.00	19,392.00

1999 Radio Fee Schedule -- Effective January 1 - December 31, 1999

Market

High One Minute Spot Rate	H	G	F	E	D	C	B	A	AA
0.00 - 2.49	396.00	468.00	576.00	684.00	828.00	972.00	1,116.00	1,404.00	1,692.00
2.50 - 4.99	432.00	504.00	612.00	720.00	864.00	1,008.00	1,152.00	1,440.00	1,728.00
5.00 - 7.49	468.00	540.00	648.00	756.00	900.00	1,044.00	1,188.00	1,476.00	1,764.00
7.50 - 9.99	504.00	576.00	684.00	792.00	936.00	1,080.00	1,224.00	1,512.00	1,800.00
10.00 - 12.49	540.00	612.00	720.00	828.00	972.00	1,116.00	1,260.00	1,548.00	1,836.00
12.50 - 14.99	576.00	648.00	756.00	864.00	1,008.00	1,152.00	1,296.00	1,584.00	1,872.00
15.00 - 17.49	612.00	684.00	792.00	900.00	1,044.00	1,188.00	1,332.00	1,620.00	1,908.00
17.50 - 19.99	648.00	720.00	828.00	936.00	1,080.00	1,224.00	1,368.00	1,656.00	1,944.00
20.00 - 29.99	720.00	792.00	900.00	1,008.00	1,152.00	1,296.00	1,440.00	1,728.00	2,016.00
30.00 - 39.99	792.00	864.00	972.00	1,080.00	1,224.00	1,368.00	1,512.00	1,800.00	2,088.00
40.00 - 49.99	864.00	936.00	1,044.00	1,152.00	1,296.00	1,440.00	1,584.00	1,872.00	2,160.00
50.00 - 59.99	936.00	1,008.00	1,116.00	1,224.00	1,368.00	1,512.00	1,656.00	1,944.00	2,232.00
60.00 - 69.99	1,008.00	1,080.00	1,188.00	1,296.00	1,440.00	1,584.00	1,728.00	2,016.00	2,304.00
70.00 - 79.99	1,080.00	1,152.00	1,260.00	1,368.00	1,512.00	1,656.00	1,800.00	2,088.00	2,376.00
80.00 - 89.99	1,152.00	1,224.00	1,332.00	1,440.00	1,584.00	1,728.00	1,872.00	2,160.00	2,448.00
90.00 - 99.99	1,224.00	1,296.00	1,404.00	1,512.00	1,656.00	1,800.00	1,944.00	2,232.00	2,520.00
100.00 - 124.99	1,476.00	1,548.00	1,656.00	1,764.00	1,908.00	2,052.00	2,196.00	2,484.00	2,772.00
125.00 - 149.99	1,728.00	1,800.00	1,908.00	2,016.00	2,160.00	2,304.00	2,448.00	2,736.00	3,024.00
150.00 - 174.99	1,980.00	2,052.00	2,160.00	2,268.00	2,412.00	2,556.00	2,700.00	2,988.00	3,276.00
175.00 - 199.99	2,232.00	2,304.00	2,412.00	2,520.00	2,664.00	2,808.00	2,952.00	3,240.00	3,528.00
0.00 - 224.99	2,592.00	2,664.00	2,772.00	2,880.00	3,024.00	3,168.00	3,492.00	4,320.00	5,148.00
5.00 - 249.99	2,952.00	3,024.00	3,132.00	3,240.00	3,384.00	3,528.00	4,032.00	5,400.00	6,768.00
50.00 - 274.99	3,312.00	3,384.00	3,492.00	3,600.00	3,744.00	3,888.00	4,572.00	6,480.00	8,388.00
275.00 - 299.99	3,672.00	3,744.00	3,852.00	3,960.00	4,104.00	4,248.00	5,112.00	7,560.00	10,008.00
1300.00 And Over	4,032.00	4,104.00	4,212.00	4,320.00	4,464.00	4,608.00	5,652.00	8,640.00	11,628.00

Jaffe Rebuttal Exh.3

·· ·ED STATES DISTRICT COURT
..THERN DISTRICT OF NEW YORK
- - - - - - - - - - - - - - - - -X

. ED STATES OF AMERICA,

Plaintiff,

against -

..A. · MUSIC, INC., et ano.,

Defendant.

- - - - - - - - - - - - - - - - - -X

.n . :le Matter of the Application
..'SIC CHOICE, et al.. ..

Applicants,

- the Determination of Reasonable
nse Fees.

- - - - - - - - - - - - - - - - - -X

MEMORANDUM and ORDER

64 Civ. 3787 (LLS)

De..ndant Broadcast Music Inc. ("BMI")[1] applies to this
. .. its rate-setting capacity under Article XIV of the
.. ted Final Judgment entered in United States v. Broadcast
. ..Inc., 1966 Trade Cases (CCH) ¶71,941 (S.D.N.Y. 1966),
.e. by 1996-1 Trade Cases (CCH) ¶71,378 (S.D.N.Y. 1994) (the
Consent Decree"). It seeks an order setting reasonable
.) fees for a blanket license for applicant Music Choice's
.. -, satellite, and Internet services from October 1, 1994
... ugh September 30, 2004.

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[1] BMI is a non-profit music licensing organization founded
.39 that licenses the non-dramatic public performing rights
- affiliated songwriters, composers and music publishers.

07/20/2001 16:08 FAX

For the reasons that follow, the fee far the blanket license ... Music Choice's cable and satellite service is set at 1.75% of ... gross revenues as that term is defined in the 1995 license agreement between BMI and DMX. The fee for its Internet service ... at an[2] 3.75% of its gross revenues as that term is defined in ... standard BMI "Web Site Music Performance Agreement."

Background

The BMI Consent Decree requires BMI to make through-to-the-... general licenses available for public performances of its music, ... to provide applicants with proposed license fees upon request. If BMI and the applicant cannot agree on a fee, either ... may apply to the rats court for the determination of a reasonable fee.[3] In the rate court proceeding, BMI bears the burden of proving that its proposed fee is reasonable. While the ... determination is pending, the parties may ask the court to ... an interim fee, subject to later adjustment.

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[2] From the outset of this proceeding, BMI has offered to license Music Choice's Internet service at a rate of 1.75%. Music Choice hae not objected to that race as unreasonable, and ... adopted by this court.

[3] The Decree was amended in 1994 to provide for a rate court.

1. Prior history of this action

By letter dated January 31, 1997 Music Choice applied to BMI for a blanket license[4] for its residential music services distributed to the home by cable, satellite and the Internet. When the parties were unable to agree on a license rate, BMI applied to this court for determination of reasonable license fees for the period from October 1, 1994 through September 30, 2004.

By order dated November 15, 1999, the court set an interim fee, subject to retroactive adjustment, of 3.0% of Music Choice's[5] gross revenues for its cable and satellite services, and 1.75% of its gross revenues for its Internet service. The court warned that "the parties, and all concerned, must appreciate that the interim fee may bear little resemblance to the final fee."

During May 22-31, 2001, a six-day trial was held on the issues affecting the determination of a reasonable fee.

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[4] A blanket license grants the licensee the right to perform any composition in the BMI repertory as frequently as the licensee wishes during the term of the license.

[5] The order also set an interim fee for Muzak LLC, which has since withdraw as an active applicant in this action.

2. Music Choice

Applicant Music Choice[4], which commenced consumer operatione :: 1991,[5] transmits an audio service consisting of 55 different hannelc of music Eo consumers' televisions sets via cable and satellite and to their computers via the Internet. It was the . . entrant into the reeidential music service industry, which ... ste of companies[6] offering music to cable and satellite subscribers in the home.

Music Choice's channels consist almost entirely of CD-quality music, transmitted continuauely throughout the day without commercial interruption. Each channel is programmed with different musical compositions within a *specific genre*, such as .. pcp or classical.[7] Information about each song, including t.e, author, and album appears in *text* format on the

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[4] Music Choice is a Pennsylvania general partnership. Its current partners include Warner Music, Sony Music, EMI Music, . . Warner Cable, AT&T Broadband and Information Services, . .st Cable, Cox Cable, Adelphia Cable, Microsaft and Motorola.

[5] At the time, Music Choice was known as Digital Cable Radio.

[6] DMX, Inc. (formerly Digital Music Express) and DISH-CD are the two other companies currently offering residential music service. SuperAudio Cable Radio service, which *provided* a similar service in the 1990s, went out of business in January 2000.

[7] Sane of Muaic Choice's channels are entitled "Big Band", "Today's Country", "Jazz" and "70's Super Wits".

ubscribers' television or computer screen at the beginning of each song.

For its programming transmitted by cable and satellite, Music Choice licenses a package of up to 45 music channels to cable and satellite operators, who in turn transmit the music service to their customers. To deliver its cable service, Music Choice first transmits its programming onto its own satellite, where it is received by cable operators, who then transmit the programming through their cable systems into the home. Similarly, Music Choice's satellite programming is transmitted from its own satellite to that of the satellite operator. Customers then receive the programming directly from the satellite operator through their own satellite receivers. The cable and satellite operators transmit Music Choice's service without addition, subtraction, or change to the programming, and they do not alter the signal in any way.

Music Choice's Internet programming, which provides up to 40 channels of music, is available directly to the consumer through its web site. Internet customers (also known as "Backstage Pass" subscribers) access the web site for a fee through an Internet service provider ("ISP"), such as America-On-Line or Netscape. In March 2001, Music Choice had approximately six million cable and wireless customers, about nine million satellite customers, and fifteen hundred "Backstage Pass" subscribers.

Initially, Music Choice's service was only available through ..., and cable operatars offered it to customers as a "premium" or "à la carte" channel. Under that businesa plan, customers ... the cable operatore separataly for access to that service, and the operatora rrmitted a portion of that payment to Music Choice. At that time the available technology required the cable operators to attach a separate "tuner" to their customers' cable boxes to decode the digital music signals, and the separate premium fee allowed the operatore to cover those additionsl hardware costs.[10]

By 1993, however, it was evident that fewer subscribers than expected were willing to pay separately for the service, and that selling Music Choice as a premlum channel would never be profitable. Thus, when Music Choice began offering its service via satellite through a company called DirectTV, it did so as part of DirectTV's "basic" or "enhanced basic" service, rather than as a premium service requiring an additional fee. The change in pricing structure was facilitated by satellite digital technology which did no& require an additional tuner for DirectTV's customers to listen to Mueic Choice.

[10] Cable operators initially sold *Music* Choice to subscribars for $9.95 per month, $3.95 of which was paid back to Music Choice. When profits failed to materialize, and operatore became lese interested in marketing tha service, Music Choice lowered its charges to tho operators to $2.50 *per* subscriber.

Over time, the pricing of Music Choice's cable service also hanged from that of a premium channel to basic service,[11] and ow able operators only offer it to new cable customers as part · basic, or enhanced basic, cable package. At the time of rial, cnly about 100,000 cable customers, who subscribed to the ervice before 1995, still paid for Music Choice as a premium hannel, and that number is rapidly diminishing.

In contrast with the cable and satellite customers, Internet : ribers pay Music Choice directly[12] for access to its Backstage Pass' programming; they also pay their Internet ervice provider a separate fee far access to the Internet.

3. Music Choice's licensing history

A few years before starting its service, Music Choice began egotiating with BMI for a blanket license. In 1990, BMI and Music Choice signed a three-year agreement requiring Music Choice to pay a license fee equal to 2% of its gross revenue plus 2% of he cable operators' gross revenues from Music Choice's service minus the operators' payment to Music Choice) for the First two years; both percentages increased to 2.1% for the third year.

[11] Cable technology also advanced, so that a separate tuner was no longer needed for decoding the digital signal.

[12] Music Choice retains most of its Internet subscriber revenue; it has one agreement in which it pays an ISP a percentage of its revenue in exchange for better positioning by the ISP to its customers.

from BMI's standpoint, that allowed it to capture what it saw as the full value of what a customer was willing to pay to receive Music Choice's music programs. The license also had a "most favored nation" provision: that if a similarly situated licensee obtained more favorable terms from BMI, BMI would offer those terms to Music Choice as well.

At that time, because Music Choice's service was sold only as a premium channel, one easily identified the portion of cable operators' revenues attributable to Music Choice by the subscriber's payment to the operator for the premium channel. However, as the business changed and technology advanced so that a separate tuner was no longer needed and the cable operators increasingly included Music Choice's service in their basic cable packages, it became harder to separate the portion attributable to Music Choice's channels from the operators' general revenues, which the operators were slow and reluctant to disclose.

Ultimately the problem of timely ascertaining the operators' relevant revenues was resolved on terms which BMI reached with a similarly situated competitor, DMX, Inc. (discussed below): Music Choice's rates were adjusted[13] to abolish the two-tier

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[13] The adjustment was only on an interim basis, since its prior license had expired September, 30, 1994. After January 31, 1997, BMI declined to extend the interim rate further, and required Music Choice to apply for a license. The present application reflects the parties' inability to agree on the rate ... that license.

[ag]reed to the change, provided that the rate be adjusted to [ca]pture what BMI considered to be the full value of its music license (i.e., reflecting the total amount the subscriber was willing to pay).[16]

Ultimately, DMX and BMI resolved the issues in separate agreements, signed simultaneously on August 7, 1995. The hardware dispute was settled for $222,625.22 (half of the disputed amount), to be paid by DMX over an 18-month period. The fee for the new license agreement (the "1995 DMX agreement") was [?].75% (a bit less than the total of DMX's plus the operators' [prio]r percentages) of its gross revenues from October 11, 1994 to [S]eptember 30, 1996, and 4% of its gross revenues from October 1, [19]96 to September 30, 1999. The license agreement also contained a most favored nation provision.

4. The positions of the parties

BMI argues that the court should take the 1995 DMX agreement as an appropriate benchmark for setting a reasonable fee for Music Choice's cable and satellite programming. BMI contends it is appropriate because the agreement was a fairly negotiated arms-length transaction, DMX and Music Choice are engaged in the

---

[16] When Marvin Berenson, BMI's general counsel, began negotiating the rates for the 1995 DMX agreement, his initial offer was 4.2%--the exact total of the licensee's and the operators' then 2.15 rates in each of the 1990 Music Choice and 199[?] DMX agreements.

same business, and they program and distribute music in the same manner.

Music choice argues that the 1995 agreement *is* unreasonable because its fees reflect BMI's monopolizing and superior bargaining power, are inflated to some decree by the settlement of he hardware dispute, and are derived from the two-tiered fee structure of DMX's 1991 agreement, which was negotiated *before* there was a rate court and under which BMI improperly included revenues received by the cable operatora. Music Choice suggests that the 1.35% rate BMI charges radio broadcasters[17] or the 1.75% rate BMI charges its Internet licensees are more appropriate.

Discussion

Although the BMI Conoent Decree directs the court: to set a reasonable" *fee*, it provides no guidance for making that determination. Prior cases Involving rate-setting under the American *Society* of Composers and Publishers ("ASCAP")[18] Consent Decree, which also requires its rate court to set a reasonable fee, have viewed *the* court's tank as defining a rate *or* range of

[17] Although Music choice claims that the BMI radio licensee rate is 1.355, BMI contende that the rate it charges its radio licensees is actually 1.605% of net revenues.

[18] ASCAP is the other major organization holding rights to copyrighted music in the United States.

rates reflecting the *fair* market value for a particular license, i.e. "the price that a willing buyer and a willing seller would agree to in an arm's length transaction: ASCAP v. Showtime/The Movie, 912 F.2d 563, 569 (2d Cir. 1990) (hereinafter ASCAP v. Showtime).

The efficiencies and benefice of a blanket license imbue it with a value different than the sum of its constituent compositions. Moreover, becauee the music licensing industry is predominantly controlled by two competitors, BMI and ASCAP, the market for blanket licenses "appears to be one whose natural consequence is the lack of broad-based competition." United States v. ASCAP (Application of Capital Cities/ABC, Inc.), 831 F.Supp. 137, 144 (S.D.N.Y. 1993).

Thus, ASCAP rate decisions have coneidered "very imperfect surrogates, particularly agreements reached either by these parties or by othera for the purchase of comparable tights," a6 a starting point for their analysis. ASCAP v. Showtime, 912 F.2d at 577 (App: Opinion of Trial court). Whether such an agreement is an appropriate benchmark depenas on "the degree of comparability of the negotiating parties to the partiee contending in the rate proceeding, the comparability of the rights in question, and the similarity of the economic circumstances affecting the earlier negotiators and the current litigants", United States v. ASCAP (Application of Buffalo Broadcasting Co., Inc.), Civ.No. 13-95, 1993 WL 60687, at *18 (S.D.N.Y. Mar. 1, 1993), aff'd in part, vacated in part, United States v. ASCAP (Application of Capital Cities/ABC, Inc,), 157 F.R.D. 173 (S.D.N.Y. 1994), as Well as the "degree to which the assertedly analogous market under examination reflecte an adequate degree of competition to justify reliance on agreements that it has spawned." ASCAP v. Showtime, 912 F.2d at 577 (App: Opinion of Trial court). See also United States v. ASCAP (Application of Capital Cities/ABC, Inc.), 157 F.R.D at 198-99 (it is "necessary to examine those prior agreements so as to determine whether anomalous condition8 impacted them or whether they were the product of a disparity in bargaining leverage so as to render them unreliable as benchmarks for subsequent periods.").

1. BMI's proposal

It is uncontroverted that Music Choice and DMX ara similarly situated competitors[19] in the residential music services industry, have similar business structures for the distribution of their product (although DMX still sells more of its programming on premium channels than Music Choice), and program and distribute music in a similar fashlon.

[19] Mucic Choice and DMX primarily compete fox affiliate cable operators, not for listeners, becauee a listener's access to their services depends on which cable service the listener receives. Music Choice contends that it competes for listeners with radio stations and Internot music broadcaotera.

The dispute in this application centers on whether the 1995 DMX agreement with BMI should be adopted as the basis for a reasonable fee. It was taken as "the best guide towards an interim fee" in the court's November 15, 1999 order, but with adjustments reflecting doubts which the May, 2001 trial has clarified.

a. Negotiation of the 1995 agreement

DMX had no palatable licensing alternatives to accepting a blanket license from BMI. Without such a license, it could use only ASCAP music (which would have unacceptably restricted its music inventory), negotiate piecemeal for licenses with individual songwriters or music publishing firms (which would have been totally impracticable), or resort to the rate court (at a time when DMX's serious cash flow problem left it not knowing if it could meet its payroll, and the idea of arbitrating the hardware dispute "was very distressing", Tr. at 231).

DMX's counsel Peter Laird testified that the "position became one of survival. In other words, we had to find a way out of this mess that we could live with on the short term because we were not going to be able to fight . . ." (Tr. 232).

Jerold Rubenstein, DMX's Chairman and CEO at the time of the negotiations, testified that the rate in the 1995 agreement was high, but affordable in light of his two more urgent concerns:

that the rate be the same for both DMX and its competitor Music Choice, and that the cable operators' revenues be removed from the fee calculation, so that DMX would not be subject in the future to license fees based on cable operators' revenues from which it did not benefit, and which it could not control (see generally, tr. at 193-95).

On the basis of the trial evidence as a whole, one cannot say with confidence that the "hardware dispute" or its resolution had any particular effect on the license rate.

However, it is clear that in view of DMX's strained finances, the lack of feasible alternatives, and the special considerations affecting DMX's position in the negotiations, the 1995 DMX agreement should not be regarded as reflecting normal competitive market terms.

b. Reasonableness of 1995 DMX license fee

The basic premise on which BMI asserts the propriety of the 4.75-4% rate in the 1995 DMX agreement is that it includes both components for which the music subscriber is willing to pay; the music itself (approximately 2U of Mueic Choice's revenues) and the transmission by the operator to the hems (approximately 2% of the operators' revenues from Music Choice's programs). The subscriber enjoys only the music, rather than the machinery of its delivery, but BMI argues that the combined rate is what the subscriber is willing to pay to receive the music, i.e., its fair value.

But the fair value of the total package is not necessarily the fair value of the music or the music license. The other components of the package for which the subscriber pays (the former tuner, the cable, the connections, the labor of installation, etc.) are not contributed by the author of the music, and there is no reason why the author should be compensated for their cost. Quite to the contrary, the true value of the music is expressed at the earlier stage where it is incorporated into Music Choice's programs. The blanket license authorizes the use of the music, and should have no regard to whether the mechanics of delivery are cheaper or costlier. Thus, the idea that to recover the full value of the music, the blanket license rate should include a component based on the cable or satellite operators' revenues, is misconceived.

The notion that the rate should rest on both the licensee's and the operators' revenues originated in 1990, when Music Choice's business was starting and it needed BMI's license before it could get commitments from cable operators, and before recourse to the rate court was available. It found support in the view that Music Choice's transmittals to the cable operators, and the cable operators' transmittals to the subscriber, each constituted "performances" which would infringe the music composer's copyright unless licensed by BMI.

That idea has since been rejected by the ASCAP rate court for license fee purposes, regardless of how the transmittals may be regarded a0 a matter of copyright-infringement law. See United States v. ASCAP (Application of Pox Broadcasting Company), 870 F. Supp. 1211, 1219 (S.D.N.Y. 1995)("This is not a copyright case; our job is to set reasonable rates for Fox's use of ASCAP music and not to decide whether Fox has infringed the copyrights held by ASCAP members.").

The earlier facility with which the operators' revenues could be derived through the usage of premium channels has been eradicated with the passage of time and the change in tho industry's business practices. To the extent that the 1995 DMX agreement contemplated distribution of music service substantially as premium channels, it doee not serve as a useful benchmark for Music Choics, whose service wall soon only be part of basic Cable packages.

For all the above reasons, the concepr on which the 1995 DMX rate agreement rests--that the license fees should capture a portion of the cable operators' revenues--is flawed, and should be disregarded in considering that agreement as a reference point. Removing the 2% initially allocated as the cable operator's portion from the Initial total rate of 3.759 in the DMX agreement leaves a rate of 1.75%.

2. Music Choice's proposal

Music Choice proposes two rates as potential benchmarks: the 1.35% rate BMI charges radio broadcasters, and the 1.75% rate BMI charges its Internet licensees.

a. Broadcast radio licenses

Music Choice argues that the broadcast radio blanket license is an apt benchmark, because Music Choice competes with broadcast radio for listeners.

However, there are substantial differences between the residential music services industry and the radio broadcast industry. The broadcast radio license has a "blended" rate offered to radio stations that broadcast music, whether their programming consists of music interspersed with commercial, news and disc jockey interruptions, or almost no music at all. That rate has little relationship to the value of a blanket license to a service like Music Choice's or DMX's, which consists almost entirely of continuous music.

b. Internet licenses

Music Choice also argues far the 1.75% Internet license rate, because it is applied to web sites (like Music Choice's and

DMX's) that have music programming identical in format, music usage and quality to Mueic Choice's cable and satellite service.

BMI disparages the Internet licenses as "experimental", and thus not establishing a reaaonablr fee.

Because Internet technology and business structures are constantly evolving, BMI states, it has attempted to keep its licensing agreements "as flexible as they can be and give the market an opportunity to experiment with different ways of putting music our there and also different ways of making money." (Tr at 297).

However, during the six years since BMI began its licensing in 1995, the 1.754 license (first offered in 1997) haa been applied consistently to revenue-genefating music programming at web sites other than those belonging to radio and television stations or offering primarily visual texts and images.

BMI offers no reason[20] why Muaic Choice's Internet race should differ from its cable and satellite rate except that its cable snd satellite distribution involves third-party operators.

Notably, when the misconception that the presence of an operator should affect the rate is removed, the resulting rate

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[20] While BMI argues that a higher rate is justified becauee of the continuous, uninterrupted 14-hour-a-day multi-channel service, which offers a breadth and depth of music utilization ("intensity" of use), not found in industries other than ths residential music services industry, that dietinction cannot be made with respect to Internet music services, a number of which have the same characteristics.

under the 1995 DMX agreement is almost the same as the Internet rate.

Conclusion

For the foregoing reasons, the fee far the blanket license for Music Choice's cable and satellits service from October 1, 1994 through September 30, 2004 is set at 1.75% of it6 gross revenues as that term is defined in the 1995 License Agreement between BMI and DMX. Without objection, the fee for its Internet service for the same period is 1.75% of its gross revenues as that term is defined in the standard BMI "Web Site Music Performance Agreement."

So ordered.

bated: New York, New York
July 20, 2001

Louis L. Stanton
LOUIS L. STANTON
U. 6. D. J.

COPYRIGHT ARBITRATION ROYALTY PANEL

In the Matter of Determination of Statutory License Terms and Rates for Certain Digital Subscription Transmissions of Sound Recordings	Docket No. 96-5 CARP DSTRA

ORDER

On October 10, 1996, closing arguments were held in this proceeding. At that time, there was discussion with the parties concerning the fact that much of the data which would be relied upon by the Panel to support its final Report was provided pursuant to the terms of a protective order. Counsel for DCR advised the panel as follows (TR.2931).

> Mr. Laguarda: "The proposal that we previously made, your honor -- I believe it wasn't objected to by the RIAA -- was that you simply write your order and that then we be given the opportunity, prior to its public release, to designate formally those portions that rely on information that has been provided pursuant to the protective order. And we think we can accomplish that."

In light of the foregoing, the parties are herewith provided with signed copies of the Panel's final Report in this proceeding and are given until November 19, 1997 to designate those portions of the Report which, pursuant to the protective order, they do not wish to be made public. Thereafter, the public and non-public versions of the Panel's Report will be filed officially with the Copyright Office.

SO ORDERED.

Lenore G. Ehrig

The Honorable Lenore G. Ehrig
Chairperson

Thomas Fortkort

The Honorable Thomas A. Fortkort
Panelist

Sharon T. Nelson

The Honorable Sharon T. Nelson Lgx
Panelist

DATED: November 12, 1997

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In Copyright Office
Docket No. 2000-9 CARP DTRA 1&2

Before the
COPYRIGHT OFFICE
LIBRARY OF CONGRESS
Washington, D.C. 20540

In re: Determination of Statutory License Terms and Rates for Certain Digital Subscription T-ansmissions of Sound Recording	No. 96-5 CARP DSTRA

REPORT OF THE COPYRIGHT ARBITRATION ROYALTY PANEL

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Docket No. 2000-9 CARP DTRA 1&2

LIST OF ABBREVIATIONS

ASCAP	American Society of Composers, Authors and Publishers
BMI	Broadcast Music, Inc.
CARP	Copyright Arbitration Royalty Panel
CRT	Copyright Royalty Tribunal
DAT	Digital Audio Tape
DBS	Direct Broadcast Satellite
DCR	Digital Cable Radio Associates
DMX	Digital Music Express
DPRSRA	Digital Performance Right in Sound Recordings Act
Ex.	Exhibit
RIAA	Recording Industry Association of America
RX.	Rebuttal Exhibits
Services	DMX, DCR and Muzak
TCI	Tele Communications, Inc.
Tr.	Hearing Transcript (followed by page number, with last name of witness in parentheses).
W.D.T.	Written Direct Testimony
W.R.T.	Written Rebuttal Testimony

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FINDINGS OF FACT

I. THE PANEL'S STATUTORY RESPONSIBILITIES

1. This proceeding is conducted under Section 114 of the Copyright Act, 17 U.S.C. §114, as amended by the Digital Performance Right in Sound Recordings Act of 1995, Pub. L. No. 104-39 (1995) ("DPRSRA"). Section 114(d)(2), 17 U.S.C. §114(d)(2), affords certain subscription digital audio services a compulsory license to perform sound recordings. Although the purpose of this proceeding is to set the rates and terms under which three services -- Digital Cable Radio Associates ("DCR"), DMX, Inc. ("DMX") and Muzak Corp. ("Muzak") (collectively, the "Services") -- may avail themselves of that compulsory license, 17 U.S.C. §114(f)(2) provides that this proceeding "shall be binding on all copyright owners of sound recordings and entities performing sound recording".

2. The DPRSRA contains a number of significant provisions. First, The DPRSRA created for the first time a right of public performance in sound recordings. Section 106 of the Copyright Act, which specifies the bundle of rights accorded copyright owners, was amended to afford copyright owners of sound recordings the exclusive right "to perform the copyrighted work publicly by means of digital audio transmission." 17 U.S.C. 106(6); see Tr. 116-19 (Berman) (discussing Section 106 rights).

3. Second, Congress drew a distinction between subscription services (such as those provided by DMX, DCR and Muzak) and non subscription services (such as those provided by commercial radio). RIAA Ex. 8B (S. Rep. 104-128) at 16. Commercial radio was exempted from liability under Section 106(6). The digital audio services, on the other hand, were afforded a compulsory license under certain circumstances.

4. The compulsory license means that the Services have the option to perform sound recordings without obtaining the permission of recording companies and artists. Tr. 235-236 (Rosen). Normally, the owner of a copyrighted work

determines to whom and how often the copyrighted work will be sold in the market for a price (and under other terms) mutually agreed upon by the respective parties. Congress recognized that "[i]ndividual marketplace negotiations between copyright owners and users . . . entail inordinately high transaction costs."[1] Under the DPRSRA, recording companies and artists cannot control how their works are performed; they are compelled to license those works to digital audio services so long as the statutory conditions are satisfied by those services. Tr. 248 (Rosen).

5. The <u>third</u> significant provision of DPRSRA is the requirement that to take advantage of the Section 114 compulsory license, a subscription digital audio service must meet certain criteria. Tr. 191 (Berman). Congress enacted conditions of entitlement to the compulsory license in order to alleviate the recording industry's concerns over any potential for displacement of recording sales by subscription services. See H.R. Rep. No. 104-274, at 21 (17 U.S.C. §114(d)2(C) and (D) would preclude solicitation of home taping).

6. Specifically, the service must not be interactive; it must not exceed the "sound recording performance complement" (which concerns the manner in which sound recordings may be transmitted (17 U.S.C. §114(j)(7)); it must not publish in advance of programming a schedule of the sound recordings to be performed; it must not cause any device receiving the transmission to switch from one program channel to another; and it must include in each transmission identifying information encoded in the sound recording. 17 U.S.C. §114(d)(2)(A)-(E). Absent a voluntarily-negotiated agreement, the digital audio services also must pay the license fee and comply with the license terms established through the CARP process; they also must comply with certain recordkeeping requirements established by the Copyright Office. 17 U.S.C. §114(f)(2).

7. The <u>fourth</u> significant provision grants digital audio services the ability to transmit sound recordings to business establishments under certain circumstances without

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[1] <u>NCTA v. CRT</u>, 724 F.2d 176, 179 (D.C. Cir. 1983).

incurring any copyright liability. 17 U.S.C. §114(d)(1)(C)(iv). Thus, the Services will pay no Section 114 royalties for their commercial operations; nor will they pay any Section 114 royalties for their international operations because Section 114 applies only to performances within the United States.

8. <u>Fifth</u>, cable and DBS systems that transmit the digital audio services make a separate performance of sound recordings -- in addition to the performance made by the service. Congress determined that the license accorded the digital audio services should permit the performance "through to the listener." See 17 U.S.C. §114(d)(1)(C)(iii). As long as the original transmission from the digital audio service to the cable and DBS operator is licensed by the copyright owner of the sound recording, the cable and DBS operator need not obtain a separate license. However, it does impose certain restrictions on the licensing of sound recordings to affiliated digital audio services.

9. <u>Finally</u>, it requires that the Section 114 sound recording royalties be split equally among recording companies, on the one hand, and recording artists, on the other hand. And it provides that these royalties shall not be taken into account in determining royalties for the works underlying sound recordings. See (17 U.S.C. §111(i))

10. The Copyright Act requires that the Panel must adopt "reasonable" rates and terms (17 U.S.C. §114(f)(2) & 801(b)(1)), which are "calculated to achieve" the following objectives:

A. To maximize the availability of creative works to the public;

B. To afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions;

C. To reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk, and contribution to the opening of new markets for creative expression and media for their communication; and

D. To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices.

17 U.S.C. 801(b)(2); see also RIAA Ex. 8B (S. Rep. 104-28) at 30.

11. The Panel may "consider the rates and terms for comparable types of digital audio transmission services" in determining the reasonable rate. 17 U.S.C. 114(f)

12. Finally, the Panel is required to "act on the basis of a fully documented written record, prior decisions of the Copyright Royalty Tribunal, prior copyright arbitration panel determinations, and rulings by the Librarian of Congress under section 802(c)" 17 U.S.C. 801(c)

II. INTRODUCTION AND SUMMARY

A. Procedural History

13. 17 U.S.C. §114(f) provides that the terms and rates of the statutory license may be determined by voluntary negotiation among the affected parties or, where necessary, binding arbitration. On December 1, 1995, the Copyright Office published a notice in the Federal Register initiating the voluntary negotiation period from December 1, 1995, to June 1, 1996. 60 Fed. Reg. 61,655-56 (Dec. 1, 1995). The Office directed parties not subject to a voluntary agreement to file their petitions for a CARP proceeding by August 1, 1996.

14. On June 4, 1996, the Office received a petition from the Recording Industry Association of America (RIAA) requesting the Copyright Office to commence proceedings to determine a schedule of rates and terms for a statutory license for the public performance of sound recordings via digital audio subscription transmission services.

15. On August 2, 1996, the Librarian of Congress established a schedule for the filing of written notices of intent to participate and the conduct of pre-controversy discovery, with the filing of written direct cases on September 9, 1996, and the initiation of arbitration scheduled for December 2, 1996. 61 Fed. Reg. 40,464-66 (Aug. 2, 1996).

16. RIAA, DCR, DMX, Muzak, America Online, Inc., and CompuServe Incorporated all filed timely Notices of Intent to Participate.[2]

17. On September 6, 1996, the Librarian suspended the pre- controversy discovery schedule pending resolution of the Services' motion for a protective order governing treatment of confidential information. On September 18, 1996, the Librarian entered a protective order proposed by the parties and established a new pre-controversy discovery schedule. Discovery, motion practice, and additional modifications of the pre-controversy discovery schedule ensued.[3]

18. The Librarian initiated the 180-day arbitration period on June 2, 1997. The Panel held a prehearing conference on June 3, 1997. Beginning June 9, 1997, the Panel heard opening arguments and eight days of witness testimony regarding the parties' direct cases and proposed

[2] By Order dated November 4, 1996, the Librarian dismissed America Online and CompuServe from this proceeding for failure to file timely a written direct case.

[3] In October, 1996, the parties' disagreement regarding the appropriate scope of discovery gave rise to several motions by the parties and a _de facto_ suspension of discovery proceedings. The Services understood the discovery process to be more liberal (as in traditional civil litigation), in contrast to RIAA's restrictive view of the parties' discovery obligations. As a result, the Services' initially produced documents specifically underlying their Direct Cases as well as additional documents upon which their witnesses did not specifically rely. See, _e.g._, DMX Inc.'s Opposition to RIAA's Motion to Compel Services to Identify to Which Request Each Produced Document is Responsive, at 2 (filed Jan. 8, 1997). The Librarian ultimately clarified that discovery in CARP proceedings is limited to documents that underlie specific assertions in witnesses' testimony and underlying documents and data verifying "bottom-line figures." Order at 6-7, 16 (Nov. 27, 1996).

statutory license rates. Beginning July 26, 1997, the Panel heard five days of testimony regarding the parties' proposed statutory license terms and their rebuttal cases.

19. By Order dated July 30, 1997, and with prior agreement of the parties, the Panel set September 5, 1997, as the deadline for filing Proposed Findings of Fact and Conclusions of Law; September 26, 1997, for filing Reply Findings; and October 10, 1997, for closing arguments. The record was closed as of that date.

B. The Parties and Witnesses

1. The Recording Industry

20. RIAA represents a collective that consists of more than 275 record labels. Berman W.D.T. at 2; RIAA Ex. 1. The members of the RIAA collective, which was established to administer rights granted by the DPRSRA, are responsible for the creation of more than 90 percent of all legitimate sound recordings sold in the United States. Tr. 113-14 (Berman). By law, the Section 114 royalties must be split evenly between the recording companies, as copyright owners, and recording artists (featured artists, non-featured vocalists and non-featured musicians). 17 U.S.C. §114(g)(2).

21. RIAA presented the following witnesses at the hearing:

A. Jason Berman (Berman) has been the Chairman and Chief Executive Officer of RIAA since December, 1993. Tr. 108 (Berman).

B. Larry D. Gerbrandt (Gerbrandt) is Senior Vice-President of Paul Kagan Associates, Inc., where he serves as the Senior Analyst for 13 of Paul Kagan Associates' 48 industry newsletters. Gerbrandt W.D.T. at cover page.

C. Zachary Horowitz (Horowitz) is President of MCA Music Entertainment Group, one of the six "major" recording labels in the United States. Horowitz W.D.T. at 1-2.

D. David E. Leibowitz (Leibowitz) is a consultant to RIAA and also serves as Vice-Chairman of the Board of Aris Technologies. Leibowitz was Senior Vice-President and General Counsel of RIAA from 1989 through March, 1997. Tr. 1851-52 (Leibowitz).

E. Barry M. Massarsky (Massarsky) of Barry M. Massarsky Consulting, Inc., has represented RIAA as an economic consultant since 1992. Tr. 445-446 (Massarsky).

F. Gary Morris (Morris) is a country music artist who has recorded 14 albums over 15 years, including five number one songs and eleven other top ten hits. Morris W.D.T. at 1.

G. Hilary Rosen (Rosen) is the President and Chief Operating Officer of RIAA. Tr. 228 (Rosen).

H. James M. Trautman (Trautman) is Senior Vice-President of Bortz & Company, Inc., a research and consulting firm. Tr. 360 (Trautman). Trautman has testified as RIAA counsel's witness in prior CARP proceedings. Tr. 366 (Trautman).

I. Paul J. Vidich (Vidich) is Senior Vice-President of Strategic Planning and Business Development at Warner Music Group. He is also a member of the DCR Board of Directors. Vidich W.D.T. at 1.

J. Steven S. Wildman (Wildman) is an Associate Professor of Communications Studies at Northwestern University and Director of Northwestern's program in Telecommunications Studies, Management & Policy. Wildman W.D.T. at 1.

K. David Wilkofsky (Wilkofsky) is an economist and principal of Wilkofsky Gruen Associates, Inc., a consulting firm that specializes in the communications and entertainment industries. Wilkofsky W.D.T. at cover page.

2. Digital Cable Radio Associates

22. DCR is a partnership of companies from the music, cable, and cable technology industries. DCR was formed in 1987 by the Jerrold Communications Division of General Instrument Corporation. Its current partners also include Warner Music, Sony Corporation, EMI, Time Warner Cable, Continental Cablevision, Comcast Cable, Cox Cable, and Adelphia Cable. DCR was the first digital audio service in the United States, and provides its programming under the brand name "Music Choice." Del Beccaro W.D.T. at 1.

23. The following witnesses testified on behalf of DCR:

A. David J. Del Beccaro (Del Beccaro) is the President and Chief Executive Officer of DCR, having served in this role since the inception of the company. Del Beccaro is responsible for DCR's overall management and assists the partners with strategic planning for the company. Prior to DCR, he was Vice-President of New Business Development at Jerrold Communications. Del Beccaro W.D.T. at 1.

B. Barry McCarthy, Jr. (McCarthy) is the Senior Vice-President and Chief Financial Officer of DCR. McCarthy oversees DCR's financial operations and legal affairs. Before joining DCR, he was Managing Partner of BMP Partners, a consulting firm, a Director with the First Boston Corporation, and a consultant with Booz, Allen & Hamilton. McCarthy W.D.T. at 1.

C. Lou Simon (Simon) is Senior Vice-President of Programming at DCR. Simon has overseen research and marketing for DCR, and currently manages DCR's music programming operations. He previously worked as a Senior Director of Research and Senior Director of Artists and Repertoire at RCA Records. Prior to that, he was involved in the radio business in both on-air and off-air roles. Simon W.D.T. at 1.

3. DMX Inc.

24. Jerold Rubinstein founded International Cablecasting Technologies, Inc. ("ICT") in 1986. Rubinstein W.D.T. at 6; Tr. 1261 (Rubinstein). ICT was renamed DMX Inc. in April, 1995. Rubinstein W.D.T. at 6. See generally DMX

Exs. 4-9 (1991-1994 Annual Reports for ICT, 1995 10-K filing for DMX Inc., and 10-Q filing for DMX Inc. for quarter ended June 30, 1996); DMX Ex. 5RX (Schedule 14A), at 150.

25. On July 11, 1997, DMX merged into TCI Music, Inc. Troxel W.R.T. at 5; Tr. 2536 (Troxel); see also Tr. 1285, 1315-16 (Rubinstein). TCI Music is a publicly traded company with approximately 80% of its shares owned by TCI, Inc., and the remaining 20% of its shares owned by individuals or entities other than TCI. Tr. 1285-86 (Rubinstein); Tr. 2439 (Trautman); DMX Ex. 5RX (Schedule 14A) at 62.

26. DMX presented the following witnesses at the hearing:

A. Jerold H. Rubinstein (Rubinstein) is the founder of DMX and served as its Chairman and Chief Executive Officer until July, 1997. He is also a CPA and attorney, former chief executive of two sound recording companies, ABC Records and United Artists Records, and a former member of the Board of Directors of RIAA. Rubinstein W.D.T. at 1; Tr. 1217-19 (Rubinstein); DMX Ex. 1 (Rubinstein's curriculum vitae).

B. Douglas G. Talley (Talley) is Executive Vice-President and Chief Technical Officer of DMX, with responsibility for research and development, and all technical operations of DMX worldwide. From 1988 to 1992, Talley was the Chairman and founder of Digital Radio Labs, which eventually became Digital Planet, one of the first satellite-delivered digital audio services for cable TV. Talley W.D.T. at 1; Tr. 1171-72 (Talley); DMX Ex. 35 (Talley resume).

C. Lon A. Troxel (Troxel) has served as Chief Executive Officer and President of DMX since July, 1997. Prior to that, Troxel served as Executive Vice-President for DMX, and before that, President of the Commercial Division of ICT. Previously, Troxel was the Vice-President for United States and Canada Dealer Sales for AEI Music Networks, Inc., a commercial music service that provides background music services. Troxel W.R.T. at 2; Tr. 2510-11, 2513 (Troxel); DMX Ex. 41 (Troxel's curriculum vitae).

4. Muzak, L.P.

27. Muzak is America's oldest background music provider for businesses, with roots dating back to 1922. More than 60 years after being driven out of the consumer music market in 1934 by the growing popularity of radio, Muzak re-entered that market in March, 1996, when it began providing 27 channels of digital music under the name DiSH CD, as part of Echostar's satellite-based DiSH Network. Funkhouser W.D.T. at 1.

28. Muzak presented the testimony of Bruce Funkhouser (Funkhouser) at the hearing. Funkhouser has served as Vice-President of Programming and Licensing for Muzak since 1987. Funkhouser has worked extensively throughout the music industry, including as a broadcaster, studio recorder, teacher, consultant, and record company manager. He is also a voting member of the National Academy of Recording Arts and Sciences. Funkhouser W.D.T. at 1.

5. Expert Witnesses for all the Services

29. The Services jointly sponsored testimony by the following hearing witnesses:

A. John R. Woodbury, Ph.D. (Woodbury) is a Vice-President at Charles River Associates, Inc., an economics consulting firm. He received his B.A. *summa cum laude* in Economics from Holy Cross in 1971, and his Ph.D. in Economics from Washington University (St. Louis) in 1977. Before joining Charles River Associates, Dr. Woodbury served as a Brookings Economic Policy Fellow at the Civil Aeronautics Board (1978-79), as a member of the Network Inquiry Special Staff at the Federal Communications Commission (1979-80), as a Senior Staff Economist and Assistant Director for Special Projects in the Federal Trade Commission's Bureau of Economics (1982-83, 1985-89), and as a Vice-President of Research and Policy Analysis at the National Cable Television Association (1983-85). Woodbury W.D.T. at 1.

B. Jay A. Rosenthal (Rosenthal) is an attorney with the law firm of Berliner, Corcoran & Rowe, L.L.P., in Washington, D.C. His legal practice focuses on the representation of recording artists, writers, production companies, independent publishing and independent record companies, and multimedia companies, including the licensing of musical compositions and performances. Tr. 1700-01 (Rosenthal); DMX Ex. 55 (Rosenthal's curriculum vitae).

C. David Sehring (Sehring) is Vice-President of Acquisition for American Movie Classics Company (AMCC). Sehring is responsible for identifying movie products to license and for negotiating licenses with copyright owners, including major motion picture studios and other film libraries.

6. <u>Songwriters and Publishers are Not Parties.</u>

301. The songwriters (including the creators of the notes and the lyrics) and their publishers (which print the sheet music) are not part of this proceeding. 17 U.S.C. 114(i) (Section 114 royalties shall not be taken into account in any proceeding to set or adjust the royalties paid to the copyright owners of musical works for the public performance of their works).

a. <u>Mechanical Rights</u>

31. Recording companies pay composers and publishers "mechanical" royalties in order to reproduce the musical works on sound recordings. These royalties are paid pursuant to the compulsory licensing provisions of Section 115 of the Copyright Act, 17 U.S.C. §115. The existing mechanical royalty rate amounts to approximately <u>90 cents</u> for the typical compact disc or cassette (9 percent of the average wholesale price for a CD and 20 percent for the average wholesale price of a cassette). Massarsky W.R.T. at 9; Tr. 1662 (Massarsky); Tr. 214 (Berman). However, recording companies may negotiate below that rate. Tr. 1660 (Massarsky); Tr. 1707 (Rosenthal). According to Mr. Rosenthal, recording companies pay the copyright owners of musical works a mechanical royalty that amounts to about <u>52 cents</u> for the typical compact disc or cassette (5 percent of the average wholesale price of a CD and 12 percent of the average wholesale price of a cassette). Rosenthal W.R.T. at 5; Tr. 1711 (Rosenthal).

b. Music Works

32. The composers and publishers also receive royalties when their musical works are performed publicly (e.g., when they are played on radio or when the Services transmit sound recordings). The performance rights in each work are assigned to one of three collectives -- ASCAP, BMI or SESAC. Each collective negotiates blanket licenses which permit the Services and others to perform any musical work within that collective's repertoire. Massarsky W.R.T. at 4; Tr. 1645-47 (Massarsky); Tr. 1762-63 (Rosenthal). Disputes involving the proper amount of music license fees may be adjudicated by the rate courts in the Southern District of New York, which have the authority to set "reasonable" fees. See RIAA Ex. 3RX (United States v. ASCAP, slip op. at 4 (S.D.N.Y. 1989).

C. Summary of Parties' Positions

33. RIAA requests that the section 114(f) royalty for each Service be set at 41.5% of that Service's gross revenues resulting from U.S. residential subscribers, and also seeks certain flat rate minimum fee royalty payments. RIAA Direct Case at 4; Tr. 208 (Berman). RIAA also proposes certain statutory license terms, concerning the timing of license fee payments, late fees for untimely payments, contents of statements of account to be submitted by the Services, record keeping requirements, and audit rights. Leibowitz Amended W.D.T. at 1, 5-7.

34. DCR requests that the section 114(f) of the 1995 Act royalty for each Service be set at 2.0% of that Service's gross revenues resulting from U.S. residential subscribers. Del Beccaro W.D.T. at 9.

35. DMX requests that the section 114(f) royalty for each Service be set at 1.25% of that Service's gross revenues resulting from U.S. residential subscribers. Rubinstein W.D.T. at 28-29; Tr. 1287, 1353, 1426 (Rubinstein).

36. Muzak requests that the section 114(f) royalty for each Service be set at 0.50% of that Service's gross revenues resulting from U.S. residential subscribers. Tr. 1500 (Funkhouser).

37. The Services also jointly proposed that the statutory digital sound recording performance license include certain terms and conditions in connection with notice, payment, confidentiality, record keeping and auditing procedures. Services' Terms Submission. Tr. 1975-76 (McCarthy).

III. THE SUBSCRIPTION PROGRAMMING INDUSTRY

A. Cable And DBS

38. Cable systems, which provide subscribers with multiple channels of programming via coaxial cable, originated as a means of offering improved reception of over-the-air broadcast stations. Since the 1970's, cable has extended its reach by transmitting (in addition to broadcast signals) a large number of non-broadcast services that feature a variety of programming types. More than 60 million households currently subscribe to cable. RIAA Ex. 13 at Attachment A, p. 7 (DMX 10K); Trautman W.D.T. (RIAA Ex. 12) at 1; RIAA Ex. 12A (FCC Report) at 10-18.

39. Beginning in 1991 subscription programming has also been provided by direct broadcast satellite (DBS). Like cable, DBS operators transmit multiple channels of programming to paying subscribers. Unlike cable, DBS operators transmit in a digital format via satellite to small home receivers (or "dishes"). Because they transmit digitally, DBS services offer more channels of programming (with enhanced quality) than cable operators. There are three principal DBS operators -- DirecTV, Primestar and EchoStar. The DBS industry currently serves over 4 million households and is projected to serve around 15 million households by the year 2000. Trautman W.D.T. (RIAA Ex. 12) at 2-3; RIAA Ex. 12A at 19-28 (FCC Report).

40. Most cable networks are offered by cable and DBS as part of a "basic service" -- that is, subscribers receive these networks in a package of programming for a single monthly fee. The basic networks generate revenue by charging license fees and (in most cases) by selling advertising. Some networks, however, are commercial free and thus receive all or essentially all of their revenues from license fees.

License fees range from only a few cents per subscriber per month to over $1 per subscriber per month. Trautman W.D.T. (RIAA Ex. 12) at 12-13; DCR Ex. 10; RIAA 155 et seq.

41. Many of the basic cable networks were designed to appeal to a specific (and often relatively narrow) audience segment which was perceived to be "underserved." These "niche" services are a key element of cable and DBS marketing strategies in that they help attract and retain specific groups of subscribers willing to pay the full basic service fee. These incremental subscribers enhance cable and DBS cash flow and, as a result, market value. Trautman W.D.T. (RIAA Ex. 12) at 12; Tr. 371-72 (Trautman).

42. Cable and DBS operators also offer cable networks on a premium or a la carte basis -- that is, the subscriber pays a monthly fee (in addition to the basic fee) to receive only that network. These premium services include movie-based services such as Home Box Office and Showtime. They are typically commercial free and are supported primarily by the sale of subscriptions to consumers. Some basic cable networks (such as AMC and Bravo) began as premium services and then switched to basic services; others, such as the Disney Channel, are offered on both a basic and a premium basis. Trautman W.D.T. (RIAA Ex. 12) at 13-14.

B. Digital Audio Subscription Services

43. There are currently only three digital audio music subscription services available to residential subscribers in the United States: DCR (Music Choice), DMX, and Muzak. The Services offer their digital music via satellite, or cable, or both.

1. Use Of Sound Recordings

44 Each of the Services provides residential subscribers with approximately 30 channels of uninterrupted CD-quality music across a wide spectrum of musical styles and genres. Rubinstein W.D.T. at 1, TR. 1225 (Rubinstein), Del Beccaro W.D.T. 1-2, DCR Ex. 1. Each highly-themed channel, which is transmitted 24 hours per day, 7 days per week, consists of wall-to-wall sound recordings -- with no

commercials, announcers or public interest programming. RIAA Ex. 13 at Attachment B (DMX web site) p. B1.[4]

45. Each channel explores in depth a particular musical era or genre and has the capacity to access more than 2700 songs at any given time. RIAA Ex. 13 at Attachment B (DMX web site) p. B-2. Thus, each Service offers a broad variety of available music formats, many of which cannot be found on commercial radio broadcasts or on other preprogrammed music services. Tr. 1085 (Simon); Rubinstein W.D.T. at 7; Tr. 1237-40 (Rubinstein); DMX Exs. 10-11 (DMX brochures describing DMX service, programming, and channel line-up for residential subscribers). See generally DMX Exs. 32-34 (various articles describing DMX service) Rubinstein W.D.T. at 1, TR. 1225 (Rubinstein), Del Beccaro W.D.T. 1-2, DCR Ex. 1, RIAA Ex. 13 at Attachment A (DMX 10K) p. 4.

46. The Services also transmit sound recordings to commercial subscribers. See, e.g., RIAA Ex. 13G (DMX 10K) at 12. DMX and DCR also have international operations which consist of several channels of audio programming. See, e.g., RIAA Ex. 13, Attachment A, p. 12.

47. Consequently, The Panel finds that the Services provide invaluable promotional benefits for the recording industry.

48. Listeners can hear the Services through existing consumer electronic equipment, such as stereo receivers, televisions, stereo VCRs, or amplified speakers. But in addition, they need a special receiver provided by the cable company or a satellite dish and receiver as in the case of Muzak. See Del Beccaro W.D.T. at 1-2; Tr. 939-40 (Del Beccaro); Rubinstein W.D.T. at 6, Tr. 1227-28 (Rubenstein); Funkhouser W.D.T. at 2.

49. The Services are all new and, during the past six years, have been struggling to create an industry and to stay in that business. They have required a tremendous capital investment to start operations and require significant

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[4] Of the many channels offered by the Services, one or two have some news or informercials. (Simmon)

ongoing operating capital to cover costs. Thus far, none of the three Services has "broken even." Profitability for any of the Services currently is projected to be years away, at best. In the meantime, the Services face increasing competition in a rapidly changing marketplace. (See paragraphs 54-56, 65-67, and 73)

50. As of the date of this hearing, each of the three Services was in compliance with the factors set forth in the 1995 Act, 17 U.S.C. §114(d)(2), that qualify a digital subscription transmission for a statutory license. Del Beccaro W.D.T. at 2; Tr. 855-56, 882 (Del Beccaro); Rubinstein W.D.T. at 9-10; Tr. 1232, 1240-41 (Rubinstein); Funkhouser W.D.T. at 2 n.1.

2. Digital Cable Radio Associates (DCR or Music Choice)

51. Music Choice, with more than 30 diverse channels, is available nationwide on approximately 225 cable systems and by satellite on DirecTV. See Del Beccaro W.D.T. at 1-2; DCR Ex. 1 (Music Choice Formats).

52. Music Choice formats include reggae, big band, blues, jazz, alternative rock, country, heavy metal, contemporary Christian, Mexicana, assorted vocal offerings, and children's programming. These formats expose a vast array of artists to their primary audience: music lovers and consumers. Simon W.D.T. at 3. In all, Music Choice plays a total of 60,000 titles in its active library, and there are many other songs entered in the Music Choice database that are out of rotation at any one time. Tr. 1077-78 (Simon).

53. DCR's best cable affiliates to date have achieved subscriber penetration in the 3%-4% range, with an average established system penetration range of less than 2%. Del Beccaro W.D.T. at 2. Overall penetration has averaged 1.2%. Del Beccaro W.D.T. at 2; McCarthy W.D.T. at 2. Time Warner cable serves approximately 12.5 million customers, but DCR reaches only about 1% of Time Warner's entire customer base. Tr. 994 (Del Beccaro). Results such as these have caused DCR to re-evaluate both the marketing and pricing of its service. Del Beccaro W.D.T. at 2. DCR would like to see its average

penetration rate increase from 1%-2% to 30%-40% through new price points. McCarthy W.D.T. at 2.

54. Originally, DCR was positioned as a premium (or "a la carte") cable service with an average retail price of $9.55 and a license fee of $3.95. McCarthy W.D.T. at 2. To attract and retain cable affiliates, DCR had to reduce its wholesale price for a la carte cable service to $3.50, $3.00, and then $2.50. Tr. 974-75 (Del Beccaro); see also Tr. 939-40 (Del Beccaro). When sold as a premium service, the cable operators retained about $7.50 (the difference between the retail and wholesale price) to partially pay for the subscriber's tuner, which cost between $100 to $150, as well as installation and marketing. Unfortunately, the $7.50 never came close for any individual operator to pay for its expenses, so the cable operators lost money. Tr. 939-40 (Del Beccaro).

55. DCR is in the process of repositioning Music Choice as a basic and near-basic service. McCarthy W.D.T. at 2. DCR reaches almost 2.5 million residential subscribers. DCR Ex. 48. The vast majority (95%)of these subscribers receive the service as part of a basic or near-basic tier. Id. DCR started pricing its basic or "tier packaging" at $1.00, but now averages about 30¢. Tr. 975 (Del Beccaro). DCR's standard tier pricing is between 20¢ and 35¢. Tr. 975-77, 986 (Del Beccaro). DCR charges 13¢ to 15¢ for DirecTV DBS basic or intermediate service. Tr. 978-79 (Del Beccaro).

56. DCR is owned in part by several major cable operators that account for over 90 percent of DCR's cable subscribers. Tr. 941 (Del Beccaro). The DCR partners include Time Warner Cable, the nation's second largest cable operator and subsidiary of Time Warner (a large conglomerate with more than $17 billion in annual revenues). Massarsky W.D.T. (RIAA Ex. 13) at 7. As discussed below at paragraph 163, Time Warner Cable acquired an interest in DCR in 1993 as part of a larger transaction in which DCR agreed to provide the Time Warner systems with five years of free service. However, only 3.2% of Time Warner subscribers actually receive the DCR service despite the fact that Time Warner pays nothing for the Music Choice service. DCR Ex. 48 (DCR Monthly Customer Report May 1997) DCR's other partners include three major recording

companies (Warner Music, Sony Music and EMI Music) -- as well as Comcast, Continental, Cox and Adelphia (the nation's third, fourth, fifth and ninth largest cable operators). Despite access to more than 10 million potential subscribers, DCR's partners have launched the Music Choice service in only about 300,000 homes (3% of the total). DCR Ex. 48

57. DCR's remaining partner is General Instrument. DCR originated as a project of General Instrument, which developed the technology necessary to transmit sound recordings digitally via cable systems. Tr. 936 (Del Beccaro). General Instrument has received approximately $40 million from DCR cable affiliates for use of that technology. Tr. 938 (Del Beccaro); McCarthy W.D.T. at 2. See also Tr. 951 (Del Beccaro) (DCR may use only General Instrument technology).

3. Digital Music Express (DMX)

58. The DMX signal currently is delivered to the home primarily in two ways. First, the DMX service is distributed as a premium service by cable television signal suppliers. Rubinstein W.D.T. at 7; Tr. 1225 (Rubinstein); DMX Ex. 16 (DMX program guide). A few cable systems that offer digital services include DMX in a basic digital package at no extra cost to the subscriber. Tr. 1225-26 (Rubinstein).

59. The second delivery method, for the vast majority of DMX subscribers, is through the DBS system operated by PrimeStar Partners, L.P. The DMX studio uplinks to a Ku-Band satellite that delivers the signal directly to a satellite receiving dish at the subscriber's residence. Rubinstein W.D.T. at 8; DMX Ex. 5RX (Schedule 14A) at 152. Until recently, PrimeStar DBS "basic" subscribers received eight DMX channels as part of their basic television package. Very recently, PrimeStar began offering 30 channels of DMX programming. Rubinstein W.D.T. at 8; Troxel W.R.T. at 10; Tr. 1235, 1347 (Rubinstein). See also DMX Ex. 12 (PrimeStar 8-channel line-up).

60. In addition, fewer than 100 homes receive the 92-channel "DMX Direct" service by direct-to-home ("DTH") satellite transmission. Rubinstein W.D.T. at 8; Tr. 1281

(Rubinstein); Tr. 2517 (Troxel); DMX Ex. 42. See also DMX Ex. 13 (list of the channels that DMX currently programs for commercial subscribers and for the small number of residential DMX Direct subscribers). DMX believes that number will not increase significantly given the many digital services available (e.g., DirecTV) that include audio in their product offering. Rubinstein W.D.T. at 11. Compare DMX Ex. 14 (showing 20 DMX Direct subscribers as of June, 1996) with DMX Ex. 42 (showing 94 DMX Direct subscribers as of March 31, 1997).

61. DMX has approximately 1.8 million subscribers. Approximately 1.5 million of those are basic subscribers through PrimeStar and about 260,000 are premium subscribers. DMX Ex. 42 (showing 1,527,000 DBS subscribers, and 94 DMX Direct subscribers as of March 31, 1997); DMX Ex. 43 (decline in DMX premium subscribers July, 1996 - June, 1997); DMX Exs. 48(d)-(e) (showing breakdown of residential subscribers to DMX).

62. The cable operator sets the retail price charged to the subscriber for the DMX premium service. Cable operators typically charge premium subscribers about \$8.95 or \$9.95 per month. Rubinstein W.D.T. at 7; Tr. 1283 (Rubinstein).

63. When cable operators offer the DMX programming on a premium basis, they generally pay DMX a license fee or "wholesale price" of \$2.50 per month per subscriber, although the fee is as high as \$3.00 per month per subscriber under some affiliation agreements. Tr. 1283, 1322-23 (Rubinstein); Tr. 2542 (Troxel). When cable operators offer DMX as part of basic or packaged service, they pay DMX a license fee of 15¢ to 25¢ per month per subscriber. Tr. 1285, 1340-41 (Rubinstein); Tr. 2542 (Troxel) ("hoping" digital cable wholesale price will be 25¢ per subscriber). Cable operators retain the difference between the retail price and the wholesale price to have some margin to recoup their substantial investment in equipment. Tr. 1284 (Rubinstein). Each cable system operator must pay approximately \$20,000 to \$40,000 for the headend equipment, plus an additional \$150 for each subscriber's receiving box. Rubinstein W.D.T. at 6; Tr. 1227-28 (Rubinstein).

64. For DBS subscriptions through the PrimeStar system, DMX currently is paid 30¢ per month per subscriber; DMX, however, offers PrimeStar a 20¢ per month per subscriber marketing credit, resulting in net payment of a 10¢ per month per subscriber license fee to DMX for DBS carriage. Rubinstein W.D.T. at 23; Troxel W.R.T. at 8; Tr. 1235, 1350-54, 1357-60 (Rubinstein); Tr. 2534, 2542 (Troxel). DMX anticipates that PrimeStar will pay a license fee of only 10¢ per subscriber per month after 1998. Tr. 2542-44 (Troxel). See DMX Exs. 49(a)-(d) (forecasts of DMX losses with various royalty rates).

65. The 92 current residential DMX Direct subscribers pay DMX $15 per month with an annual prepaid subscription, or $20 monthly. Rubinstein W.D.T. at 23.

66. After five years of operation, DMX has not reached a break-even level of market penetration in the premium service. DMX is potentially available as a premium service on more than 940 cable systems in the United States, representing more than 11-14 million cable households. Thus, the actual rate of penetration for DMX as a premium service is less than 2% of the total market available through DMX's affiliates. Rubinstein W.D.T. at 10, 24; Tr. 1241-42 (Rubinstein); Tr. 2654 (Troxel); Tr. 2389 (Trautman); DMX Exs. 14, 29, 30(e).

67. Tele-Communications, Inc. (TCI), the nation's largest cable system operator with more than $5 billion in annual revenues, first acquired a small minority interest in DMX in 1989. Notwithstanding DMX's financial losses, TCI has steadily increased that interest over the years. And, in July 1997, TCI (through a wholly-owned subsidiary) acquired 80 percent of DMX and DMX shareholders (representing the remaining 20%) have the right to put their shares to TCI Music at $2.00 per share if the DMX class A common stock does not trade at that price for at least 20 consecutive days. DMX Ex. 5RX at 2, 14. Massarsky W.D.T. (RIAA Ex. 13) at 2; id. at Attachment A (DMX 10K) at 7; DMX Ex. 5RX (DMX Schedule 14A) at 2-5 ; Tr. 2640 (Troxel).

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4. Muzak, L.P.

68. Muzak's primary business is directed not toward home consumers, but toward commercial business establishments that have a need to broadcast music and other audio services within their premises. Muzak is the nation's largest provider of music to commercial establishments, with approximately $87 million in annual revenues. RIAA Ex. 13 at Attachment E (Muzak SEC Form S-1) p. 3. Muzak provides both background and foreground music to approximately 180,000 business locations throughout the United States. Funkhouser W.D.T. at 2.

69. In the past few years, Muzak began to recognize the potential advantage of adding video service to its traditional audio-only business customers. Lacking any means of providing video service, however, Muzak began to explore the possibility of linking its music programming expertise with a video distributor, in order to gain access to video-service capability. Eventually, Muzak entered into such a relationship with Echostar, a satellite video distributor that provides service to both businesses and homes through its DiSH Network. The DiSH Network is available to home consumers who purchase a small satellite dish and receiver and who pay a monthly subscription fee similar to a cable bill. Funkhouser W.D.T. at 2.

70. In March, 1996, Muzak started providing 27 channels of its unique music programming under the name DiSH CD, as part of Echostar's DiSH Network. DiSH CD is available to DiSH Network subscribers through all but the most limited of programming packages, and can also be purchased as an a la carte offering. Currently, approximately 70% of all DiSH Network subscribers receive a programming package that includes DiSH CD as part of the basic programming package fee. Since DiSH CD became available as part of the basic programming package, almost no subscribers have paid for DiSH CD on an a la carte basis. Tr. 1484 (Funkhouser). By the end of 1996, approximately 300,000 residential subscribers were receiving DiSH CD, and Muzak had expanded its channel offerings from 27 to 30. Funkhouser W.D.T. at 2; Tr. 1485 (Funkhouser).

71. Pursuant to its contract with Echostar, Muzak receives one-half cent per channel per residential subscriber per month (15¢ per subscriber per month based on an offering of 30 channels). Tr. 1485 (Funkhouser).

72. Muzak's Vice President of Programming and Licensing, Bruce Funkhouser (Funkhouser), testified that Muzak would not continue its residential music service unless it could survive on its own as a profitable entity. Tr. 1475 (Funkhouser)

5. <u>The Services' Business Model is Shifting From Premium Analog Cable to Basic Digital Cable and DBS.</u>

73. The premium service model has clearly shifted to a basic service one. Rubinstein W.D.T. at 24-26; Troxel W.R.T. at 2; Tr. 1007 (McCarthy); Tr. 1282-83 (Rubinstein); Tr. 2515-25 (Troxel). Several factors caused the shift from premium to basic service, including: (1) the trend among cable suppliers to include subscription music programming as part of the basic subscription service; (2) the increasing popularity of DBS television; (3) competition from other digital subscription music services; and (4) the availability of new equipment that can handle both video and audio services. Rubinstein W.D.T. at 24-26; Tr. 1243, 1249-50 (Rubinstein).

74. Several factors suggest that the trend toward basic service will continue, including: (1) improved cable delivery systems; (2) cable and communications deregulation; and (3) the advent of digital audio radio broadcasting. Rubinstein W.D.T. at 26; Troxel W.R.T. at 3; Tr. 1249-50 (Rubinstein); Tr. 2519, 2536-38 (Troxel); DMX Exs. 33, 34 (various articles describing DMX service).

75. To date, DCR and DMX combined have achieved less than a 1% penetration rate as a premium cable service. In total, only about 500,000 customers out of over 60 million cable customers receive a digital audio music service. Tr. 850-51 (Del Beccaro).

76. DMX's premium subscriber base is eroding rapidly at approximately 2%-3% per month and DMX's basic subscriber population, served through PrimeStar, is increasing at approximately 3% per month. Tr. 1448 (Rubinstein); Tr. 2517, 2658 (Troxel); DMX Exs. 42, 43, 48(d)-(e) (showing decline in DMX premium subscribers and increase in basic subscribers).

77. Based on the revenue differentials, every time DMX loses one premium subscriber, it must acquire ten basic subscribers. Troxel W.R.T. at 3; Tr. 2517 (Troxel). If the license fee paid by PrimeStar drops to 10¢ as anticipated, DMX will have to acquire even more (25 to 30) basic subscribers to offset the loss of one premium subscriber. See Tr. 2542-45 (Troxel). Therefore, the 3% decline in the premium base is not offset by the 3% increase in the basic base. Tr. 2516-18 (Troxel).

78. The shift from premium to basic drastically reduced the per subscriber revenue and is delaying profitability. DMX Exs. 42, 48(c), 48(e). Under the premium service model, DMX would receive about $2.50 per subscriber per month. At that rate, DMX had projected that it might reach a break-even point with between 500,000 to 700,000 residential premium cable subscriptions, anticipating a revenue stream from domestic residential subscribers of approximately $20 million. Rubinstein W.D.T. at 24; Tr. 1446 (Rubinstein); Tr. 2542 (Troxel); DMX Exs. 14, 30(e). With basic subscribers, however, DMX anticipates breaking even with approximately 3 million to 3.5 million digital basic subscribers at 25¢ per subscriber. Tr. 2546-49 (Troxel).

IV. STATUTORY OBJECTIVES

A. Relative Creative Contributions (17 U.S.C. §801(b)(1)(C))

79. The recording artists, the recording companies, and the Services each make significant creative contribution to the music product aired by the Services.

1. Recording Artists

80. The testimony of Gary Morris explains the vital role that both featured and non-featured recording artists play in the creation of sound recordings. Morris W.D.T. at 1-3; Tr. 431-42 (Morris); see also RIAA Exs. 4 & 10; Tr. 1821 (Rosenthal). Mr. Morris' testimony also highlights the distinction between the sound recording and the underlying musical work (i.e., the written notes and lyrics). See also 17 U.S.C. 102(a)(2) & (10) (distinguishing between musical works and sound recordings); Tr. 1755 (Rosenthal) (same); Tr. 242 (Rosen) (same).

81. As Mr. Morris testified, the success of a song depends

> on the artist's ability to breathe life into that song. The artist is responsible for adding the mood and feeling that will resonate with an audience. A listener hears the emotion that the artist supplies to musical notes, not merely the notes.
>
> The marriage of a song to the correct artist is critical. The artist draws from his own experience when interpreting lyrics and musical notes, thereby bringing a unique creative style to a song.

Morris W.D.T. at 1-2; see also id. at 2 (describing the role of background musicians and vocalists in interpreting a musical work); RIAA Ex. 4 at 3-4 (same); RIAA Ex. 10 (same). A musical work is "one dimensional" until the artist interprets it by adding emotion and feeling. Tr. 431 (Morris).

82. As Mr. Morris also testified, the fact that songs are often recorded multiple times demonstrates the importance of the artist -- "if an artist's interpretation was not important, then the first recording would suffice forever." Morris W.D.T. at 2. See also Tr. 432-41 (Morris) (illustrating how a song that is recorded by two different

artists may yield dramatically different results in the marketplace); Tr. 239-40 (Rosen) (same).

2. The Recording Companies

83. The Recording Companies make a substantial creative contribution to the final recorded product. The recording company works with the artist to create a commercially viable sound recording. It assists in the selection of musical works and provides the creative means by which the sound recording is produced (e.g., record producers, engineers, supporting musicians and vocalists). The recording company also creates the cover art and graphics for the album. See Horowitz W.D.T. at 3-10; TR. 289-309 (Horowitz); Tr. 1802-19 (Rosenthal).

3. The Services

84. The Services make a significant creative contribution in the programming of sound recordings.

85. Each of these services uses a sophisticated and proprietary methodology for programming the music based on extensive research and audience ascertainment efforts. This method required not only the use of newly developed computer technology by the Services but also sophisticated music experts who program each of the channels. For example, DMX uses proprietary programming concepts, software and hardware to choose each selection according to 18 separate demographic factors and musical characteristics so as to maximize favorable consumer response to the musical programming and to minimize jarring or annoying transitions. Rubinstein W.D.T.. at 9; Tr. 1229 (Rubinstein); see also DMX Ex. 10 at 2 (A Guide to DMX, describing programming techniques).

86. Similarly, the Music Choice service is the end-product of a multi-faceted programming and transmission process that begins with programmers developing "playlists" for each format. Del Beccaro W.D.T.. at 3. Music Choice employs 24 experts in particular musical genres who oversee the programming of one to three channels. Tr. 1066-67 (Simon). Programming involves a methodical process which requires Music Choice personnel to hand design the hours of

music, keeping in mind the sound recording performance complement of the 1995 Act. Tr. 1067-71 (Simon).

87. While all parties make significant contributions to the creative product, the Panel finds that the artists and the record companies provide greater creative contributions to the release of sound recordings to the public than do the Services.

B. Relative Technological Contributions (17 U.S.C. §801(b)(1)(C))

88. The Services have made substantial technological contributions in developing and implementing digital music transmission services and consumer reception equipment to further expand the market for sound recordings.

89. DMX has invested a substantial amount of money in research, development and production of both a method to transmit the digital audio signal and the digital receiver, which enables the signal to be delivered via cable lines and to be played through a consumer's home stereo equipment. Tr. 1261-65 (Rubinstein); Rubinstein W.D.T.. at 1261-63; DMX Ex. 48(a)-(b) (showing property and equipment, research and development costs). See generally DMX Exs. 37-39 (DMX 10-Qs & 10-K/A); DMX Ex. 5RX (Sched. 14A) at 160-61, 171, 191.

90. DMX developed technology that uplinks the DMX signal from the DMX studio to a C-Band satellite, and then delivers the DMX programming directly to the cable operators' system head-end for distribution to subscribers. DMX developed the technology for signal transmission, for the cable head-end unit, and for the consumers' cable or DBS tuner and remote control unit. Rubinstein W.D.T.. at 7; Tr. 1262-65 (Rubinstein); see also DMX Exs. 15, 23 (showing Scientific Atlanta Digital Music Terminal, Comstream DR2000 Digital Audio Receiver, and DMX-DJ remote control).

91. DMX developed, at its own expense, the DMX DJ Remote and transmission technology that enables the name of the sound recording and the name of the recording artist to appear while the sound recording is being performed or to be

stored for future examination. Tr. 171-172 (Berman). The recording industry neither developed nor contributed capital for the technology that enables the name of the recording and the name of the recording artist to appear while the sound recording is being performed or to be stored for future examination. Tr. 171-72 (Berman); Tr. 1261-63 (Rubinstein).

92. DCR also developed technology for programming, compression, encryption, and transmission of sound recordings. Music Choice's playlists are transferred into data files, each of which is used to control a CD jukebox or digital audio tape ("DAT") player. A sophisticated computer network is involved throughout this process, scheduling the playback time for each recording, monitoring playback information, and ensuring quality service. Del Beccaro W.D.T.. at 3; Tr. 849 (Del Beccaro); DCR Ex. 3 (Music Choice Signal Distribution).

93. The recording industry did not introduce any specific evidence of technological contributions to the digital subscription services.

C. <u>Relative Capital Investments in Equipment and Technology. (17 U.S.C. §801(b)(1)(C))</u>

94. The Services have made significant capital investments in equipment and technology.

95. Through March 31, 1997, DMX has invested over $10 million ($10,074,784) in property and equipment. DMX Exs. 45, 48(a); see also DMX Ex. 37 (DMX Form 10-Q for quarter ending Dec. 31, 1996) at 2, 7, 12; DMX Ex. 38 (DMX Form 10-Q for quarter ending Mar. 31, 1997) at 2-3, 8, 13; DMX Ex. 39 (DMX Form 10-K for year ending Sept. 30, 1996) at 2, 5, 15. DMX invested a substantial amount of money in research, development and production of a transmission scheme and digital receiver. Tr. 1261-65 (Rubinstein). Among the principal costs to DMX have been the acquisition of technology, research and development, and property and equipment, including particularly studio equipment, computer systems, music library, furniture and office equipment. Rubinstein W.D.T.. at 16-17; Tr. 1261-67 (Rubinstein); Tr. 2532 (Troxel); DMX Ex. 18 (technology costs), DMX Ex. 19

(equipment costs through June, 1996); DMX Ex. 30(a) (property and equipment costs 1990 to June 30, 1996); DMX Ex. 45 (equipment costs through March 31, 1997); DMX Ex. 48(a) (property and equipment 1990 to March 31, 1997). Significant capital investments were likewise made by Muzak. Tr. 1490 (Funkhouser); Funkhouser W.D.T.

96. DCR also has invested in a significant amount of hardware for its programming, transmission and playback process. Del Beccaro W.D.T.. at 3; Tr. 849 (Del Beccaro); DCR Ex. 3 (Music Choice Signal Distribution).

97. The recording industry did not suggest that any capital investment was required on its part to transmit sound recordings to the public through the subscription service.

D. <u>Relative Costs and Risk (17 U.S.C. §801(b)(1)(C))</u>

98. While the recording companies incur substantial costs and risks in the production of the product used by the Services, their financial risk in the success of the digital subscription industry is minor in comparison to that of the Services.[5]

99. The Services are costly and risky ventures which will continue to face difficult financial circumstances in their attempt to launch and operate profitable digital music subscription services. Talley W.D.T. at 3-6. As discussed <u>supra</u>, the business model for the Services has shifted dramatically over the six years of their existence, and future competition poses new uncertainties (<u>e.g.</u>, internet and digital radio). This is a new and unproven business. The ultimate success of the digital music subscription business is not assured. Rubinstein W.D.T. at 29; Tr. 1471

[5] Although some of the recording companies are shareholders of the Services and therefore share a portion of that risk, they are treated as separate entities. Even if the risk to those shares were included, it would not be significant to the survival of the recording companies. The recording industry earned more than $12.5 billion in domestic sales last year compared to approximately $19.5 million in 1996 U.S. residential revenues for the three services combined. RIAA Ex. 22, DMX 37X, 49(a), DCR Ex 46.

(Funkhouser) (characterizing new digital music services as "struggling").

100. Digital Planet failed as a Service when it was unsuccessful in obtaining key distribution affiliations with cable companies and could not raise sufficient funds. Talley W.D.T. 5-6; Tr. 1180-81 (Talley): Rubinstein W.D.T. 13; Tr. 1471 (Funkhouser).

101. DCR incurs 97% of its operating expenses to program, playback, uplink, market, and sell Music Choice programming. McCarthy W.D.T. at 1.

102. It has taken more than $120 million to launch DMX and to guide the growth of DMX over the last 10 years. Rubinstein W.D.T.. at 2, 18-21; Tr. 1264-65, 1268-75 (Rubinstein); Tr. 2530 (Troxel); DMX Exs. 4-9 (annual reports); DMX Ex. 17 (sales and marketing costs); DMX Ex. 18 (technology costs, showing $72,675 in total licensing payments to Dolby Laboratories as of Fall 1996 for use of the Dolby AC-3 digital audio compression algorithm in digital transmissions); DMX Ex. 19 (equipment costs); DMX Ex. 20 (rental costs); DMX Ex. 21 (payroll); DMX Ex. 22 (annual transmission costs); DMX Exs. 24-27 (copyright license agreements with ASCAP, BMI, and SESAC); DMX Ex. 30(b) (operating expenses); DMX Ex. 44 (sales and marketing expenses through March 31, 1997); DMX Ex. 46 (satellite and uplinking costs through March 31, 1997); DMX Ex. 48(b) (operating expenses 1991 to March 31, 1997).

103. DMX's expenditures for satellite transmission of residential service for the fiscal year ending 1996 were more than $2.44 million. DMX Ex. 46. DMX's expenditures for satellite transmission of residential service through the first half of Fiscal Year 1997 (i.e., six months ending March 31, 1997) total more than $1.24 million. DMX Ex. 46.

104. DMX engages in extensive sales and marketing efforts with respect to the residential market. Rubinstein W.D.T.. at 19-20. DMX's cumulative sales and marketing expenses for its residential service from 1990 through March 31, 1997 totaled over $40 million ($40,586,384). DMX Ex. 44 (sales and marketing expenses through March 31, 1997). DMX's

sales and marketing expenses for Fiscal Year 1996 were nearly $6 million ($5,945,859), and over $2.27 million ($2,273,275) for the first half of Fiscal Year 1997 alone. DMX Ex. 44.[6]

105. The recording company assumes significant costs and risks in the production of sound recordings. The cost of a single album generally ranges from $200,000 to over $1 million. Horowitz W.D.T. at 5-6; Tr. 148 (Berman); Tr. 1796-98 (Rosenthal). Approximately 85 percent of all sound recordings do not recoup the costs that are spent to make and to market those recordings. Horowitz W.D.T. at 9. Indeed, over two-thirds of all sound recordings sell less than 1,000 copies; less than one percent of all sound recordings account for almost half of all revenues. Tr. 163 (Berman); Wildman W.R.T. at 20-22; Horowitz W.D.T. at 9-10.

106. The total retail revenues received from the sale of sound recordings amounted to about $12.5 billion in 1996. Tr. 138 (Berman); DMX Ex. 37X.

107. The risk to the recording industry lies in their ability to produce enough "hits" in their selection of music and an artist to cover their losses for the large number of recordings that do not result in profitable sales. That risk is not increased by the advent of subscription services unless the customers of the Services record the sound transmissions in lieu of purchasing these products at a retail store. While there is evidence that some customers do indeed record from the subscription service programs, the evidence is also that there is no decrease in the number of recording purchases by the subscribers. See paragraph 111, infra.

108. In assessing the cost risk component of the statute, the Panel finds that risk lies largely with the Services who are venturing into uncharted waters with a product that may or may not find acceptance in the marketplace. The recording industry as a whole is a large, well-established entity. Its unit shipments and dollar values of compact discs, cassettes,

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6 These figures are adjusted to show residentia. expenses by removing expenses relating solely to commercial subscribers and allocating expenses shared with the commercial business of DMX. Troxel W.R.T. at 3; Tr. 2529 (Troxel).

records and music videos have consistently increased from 1982-1996. (See DMX Ex. 37X). The Services, as a group, have yet to achieve profitability and their future prospects remain speculative.

E. Relative Contribution to the Openings of New Markets for Creative Expression and Media for their Communication (17 U.S.C. §801(b)(1)(C))

109. The Panel finds that the Services are primarily responsible for creating a new media and market for digital music subscription services for residential consumers.

110. Through this new media and market, the Services provide needed promotional benefits as they provide new music and expose new artists, while not overexposing any one particular artist or record. Tr. 1076 (Simon). The Services play a wider range of music than traditional over-the-air radio in terms of both formats and musical selections. Simon W.D.T.. at 3. Tr. 2685 (Woodbury) (noting that, unlike radio, the Services are not "hit driven"). "In any major city, the audience for Top-40 rock is large enough to support several FM stations, but few cities can support more than one classical station, and maybe an occasional jazz station." Simon W.D.T.. at 4. The Services, in contrast, offer multiple classical, jazz, alternative, and ethnic formats. E.g., Tr. 853-54 (Del Beccaro) (DCR's "basic charter is to try to provide more choice to customers [and] differentiate ourselves from really what is radio today, by providing a lot more music than would normally have been heard on a radio station."); Simon W.D.T. at 3-4 (stating that Music Choice even dedicates programs to unsigned and new artists, stimulating interest in nascent performers and bringing new synergy's to the recording industry); Rubinstein W.D.T.. at 13-14, 32; Tr. 1238 (Rubinstein); Tr. 1476-78 (Funkhouser); DMX Ex. 32 (attaching Johnnie L. Roberts, Time Warner, Sony Invest in Company Offering Digital-Quality Radio on Cable, Wall St. J., Feb. 1, 1993, at B6 (quoting Michael Schulhof, vice chairman, Sony U.S.A., stating in an interview that "[DCR] can expose more listeners to more forms of music and, we hope, drive them into stores to buy our product . . . . Traditional radio is very limiting.") and Jeffrey A. Trachtenberg, Thorn EMI Unit, Joining Music Rivals, Acquires

Stake in Digital Cable Radio, Wall St. J., Apr. 19, 1994 (quoting James Fifield, president and chief executive of EMI, "[T]his is a way for us to help expose people to music that they might not otherwise hear on regularly formatted radio")); DMX Ex. 34 (various articles describing the Services' broad and eclectic programming). Given radio's shrinking playlists and the general oversupply of sound recordings, record companies benefit from exposing new music through the Services. Tr. 1077 (Simon) (DCR "fills the void" left by radio); Tr. 2248 (Wildman).

111. RIAA presented no evidence to demonstrate that patronage of the Services actually results in a net displacement of record and CD sales. RIAA's Chairman and CEO, and RIAA's chief recording industry witness were unaware of any such evidence. See Tr. 215-16 (Berman); Tr. 320 (Horowitz).

112. Rather, there is evidence that subscribers frequently purchase new music precisely because they heard it on one of the Services. Simon W.D.T.. at 1; Rubinstein W.D.T.. at 34 (noting that DMX "has received many testimonials and listener comments indicating that DMX subscribers purchased recordings by artists that they first heard on DMX"); Tr. 1442 (Rubinstein); Tr. 1493-96 (Funkhouser) (discussing how Muzak reports airplay to multiple recording industry services); DMX Ex. 33 (Rebecca Day, No Static At All: Digital Music Express (DMX), Stereo Review, July, 1995, at 24, 25 ("[W]hat really gets me in trouble is buying all the CD's I decide I can't live without after getting a taste of them on DMX.")); DMX Ex. 34 (various articles). Almost 40% of DCR's listeners report hearing a new type of music they had never heard before subscribing. Simon W.D.T.. at 1. Record companies themselves understand the Services' promotional value, since they provide complementary copies of their product to help promote album sales. See, e.g., Rubinstein W.D.T.. at 32 (noting that all the major labels and many significant independent labels now provide DMX with free "promotional use only" sound recordings); Tr. 1291 (Rubinstein); DMX Ex. 31 (list of record companies that regularly provide promotional recordings to DMX); Tr. 1182-83, 1201 (Talley) (noting that record companies provided Digital Planet with promotional CDs

and encouraged airplay of their sound recordings). RIAA failed to dispute this testimony.

113. In addition, unlike radio, the Services provide the listener with convenient and extensive information about every song. "Over 90% of [DCR's] domestic residential listeners have immediate on-screen access to the title, artist and label of the selection playing on each channel." Del Beccaro W.R.T. at 3; see also Tr. 1101 (Simon).

114. The Services are either now offering or have plans to soon offer their listeners the ability to buy the prerecordings of the music they hear. Tr. 2289-95 (Del Beccaro). The Music Choice Store has sold "well over fifteen hundred CDs a month since [it] started . . . in formats from Pop to Native American, Classical to Rhythm and Blues." Del Beccaro W.R.T. at 4. The Music Choice Store has been selling a greater percentage of music that is not "hits" or "the stuff that other outlets like record stores or record clubs" sell. Tr. 2289-90 (Del Beccaro). The Music Choice Store sells "a lot more product that is catalog product, older product, or a lot more product that is niche format types that you wouldn't hear on radio." Id.

115. These new offerings will enhance the convenience of purchasing and "undoubtedly open new markets for the recording industry, [bringing] new music to an ever expanding audience." Del Beccaro W.R.T. at 4.

116. In addition, the DMX Internet Website provides information to internet users about composers and artists, record stores, and record companies. The site allows browsers to check out hundreds of Internet sites to learn more about artists and their music, where to buy particular recordings, and even to buy recordings on-line via 800 telephone numbers. Troxel W.R.T. 11-12; Tr. 2562-64 (Troxel). Music Choice also has a Website. Massarsky W.D.T.

F. <u>To Minimize Any Disruptive Impact On The Structure Of The Industries Involved (17 U.S.C. §801(b)(1)(D)</u>

117. The Services have made a strong case that a rate set too high will result in one or all of them leaving this new industry. The Panel finds that nothing could have more of a disruptive impact on this competitive market structure.

118. While some cable television networks have attained substantial profitability; to date, such profitability has eluded the Services. Digital Planet, for example, started broadcasting its digital music subscription service in April, 1991, and was discontinued in August, 1992. Talley W.D.T. at 2; Tr. 1174-75 (Talley). Digital Planet was unsuccessful in obtaining key distribution affiliations with cable companies and could not raise sufficient funds for the advertising and marketing necessary to develop a subscriber base. Talley W.D.T.. at 5-6; Tr. 1180-81 (Talley); Rubinstein W.D.T.. at 13; Tr. 1471 (Funkhouser). See also ¶¶ 99-109. A rate set too high could easily drive one or all of the Services out of this business. See also Tr. 2553-54 (Troxel); Troxel W.R.T. at 1, 5-6; DMX Ex. 49(b). Tr. 2553-55 (Troxel) (explaining that "if we don't demonstrate performance as you would in a normal operating company, I don't have high hopes that [investors] would continue to try to fund and invest [in] our residential business"), Rubinstein W.D.T. at 29; Tr. 1486,1471 (Funkhouser) (characterizing new digital music services as "struggling").

119. The total receipts for the year 1996 for all three Services in U.S. residential sales was $19.5 million. RIAA Ex. 22. A royalty fee of 41.5% would increase the recording industry annual receipts by $8,092,250 or 0.06% of their gross revenues of 12.5 billion dollars. (See RIAA Ex. 22.) At the same time, the financially ailing Services would be pushed deeper into debt. Some of the effects of the 41.5% rate are as follows:

a. Based on DCR projections, DCR would need to raise $23 million of additional capital to fund a 41% performance rate until the Service can reach a break-even. Tr. 1953-54 (McCarthy). DCR, as noted earlier, earned $5.5 million in 1996.

b. DMX state that the 41.5% royalty rate would compel an immediate shut-down of DMX services. Troxel W.R.T. 1-6; Tr. 2553-55 (Troxel).

c. With no performance royalty, DMX projects its break-even point to be at about 3 to 3.5 million digital basic cable subscribers. TR. 2546-49 (Troxel). DMX believes that their break-even point may not occur until the years 2001 or 2002, with profitability even later. TR. 2546-49 (Troxel).

d. Using the 41.5% rate, DMX estimates it would need 5 million digital basic cable subscribers to break even. Tr. 2550-51 (Troxel); DMX Ex. 49(b).

120. The Panel finds that the impact of any royalty rate on the recording industry will be minimal, although individual artists, featured and non-featured, will benefit to some small extent. On the other hand, a rate to high could devastate the Services.

G. To Maximize the Availability of Creative Works to the Public (17 U.S.C. §801(b)(1)(A)

121. The Panel finds that the Services substantially increase the availability of recordings by providing many channels of uninterrupted music of different genres.

122. A decrease in the number of Services would decrease the diversity of the music being played. Each Service has one or two people who, with the aid of a computer, select all music for a given channel. A decrease in the number of Services, decreases the number of individuals selecting the music and therefore decrease the diversity of the music played on any one channel. Therefore, it is important to select a reasonable fee which will not drive any one of the Services out of business.

H. To Afford The Copyright Owner A Fair Return For His Creative Work And The Copyright User A Fair Income Under Existing Economic Conditions. (17 U.S.C. §801(b)(1)(B)

RESTRICTED:
Contains Protected Materials
Subject to Protective Order
In Copyright Office
Docket No. 2000-9 CARP DTRA 1&2

1. The Benchmarks

123. In prior royalty adjustment proceedings, the CRT and CARPs have utilized a consistent approach to rate-setting. They looked initially at specific "benchmarks" -- rates negotiated in analogous market transactions. They then analyzed those benchmarks in light of the applicable statutory criteria and record evidence to determine a reasonable royalty rate.[7]

124. RIAA and the Services seem to agree that the best proxy for reasonable compensation is to look to marketplace rates. The fundamental dispute between the parties' positions is which marketplace serves as the proper point of reference. Services Reply page 1. It must also be noted that pursuant to DPRSRA, reasonable compensation is not synonymous with fair market rate. Rather DPRSRA requires such rate to be balanced with other factors. See ¶2 through 10, supra.

125. The parties do agree that the rate should be based on gross revenues. In addition, they agree that the Panel should adopt the same definition of "gross revenues" that is contained in DMX's current residential agreement with BMI. See DMX Ex. 26 at 4-5. RIAA Proposed Findings and Conclusions ¶ 55, Services' Reply ¶ 51.

a. Cable Television Network License Fees

126. RIAA has presented the Panel with two separate studies that show the license fees paid by cable television networks to acquire their programming. One study was prepared by Paul Kagan Associates ("Kagan"), a media research company that routinely tracks and publishes financial data from the media and entertainment industries, including cable

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7 This approach was recently followed by the CARP that adjusted the Section 119 royalty rates. See Report of the Panel in Docket No. 96-3 CARP-SRA, slip op. at 31 (Aug. 28, 1997) ("Section 119 Rate Determination"). See also Adjustment of the Royalty Rate for Coin-Operated Phonorecord Players, 46 Fed. Reg. 884, 888-89 (1981), aff'd, Amusement & Music Operators Ass'n v. CRT, 676 F.2d 1144 (7th Cir.), cert. denied, 459 U.S. 907 (1982) (AMOA v. CRT); Adjustment of the Royalty Rate for Cable Systems, 47 Fed. Reg. 52146 (1982) (RIAA Ex. 12RX), aff'd 724 F.2d 176, 183, 185-87 (D.C. Cir. 1983).

networks. Tr. 571-73, 579 (Gerbrandt); see RIAA Ex. 14. The other study (which was based on the first study) was prepared by Wilkofsky Gruen Associates (WGA), an economic consulting firm that specializes in the media and entertainment industries. Tr. 674-89, 701 (Wilkofsky); see RIAA Ex. 15.

(1) Kagan Study.

127. The Kagan study examined a substantial amount of data concerning the revenues and programming expenses of cable television networks during the period 1985-96. Based upon an analysis of these data (which reflected literally thousands of free market negotiations totaling approximately $15 billion (Tr. 621 (Gerbrandt)), the Kagan Study concluded:

> cable/DBS network which acquires all or essentially all of its programming from outside sources will spend, on average, approximately 40% of its gross revenues in program licensing fees alone.

RIAA Ex. 14 at 7; see Tr. 606 (Gerbrandt). The 40 percent figure consists of license fees to all copyright owners with which the cable television networks negotiate for their programming, including copyright owners of musical works. Tr. 639 (Gerbrandt).

128. Attached to the Kagan Study are underlying data tables that show the revenues and programming expenses of 31 basic cable television networks. For example, the Kagan tables show that Country Music Television's (CMT) total net revenues for each of the years 1985-89 ranged from $1.2 million to $20.4 million (amounts comparable to the combined Services' gross revenues). See note 7 supra. See RIAA Ex. 14 at A3. The tables also show that CMT's programming expenses ranged from 11.8 percent to 53.1 percent of those revenues in any given year. Id. at A1. MTV also ranged from 36.6% to 25.2% from 1985 to 1996. Similar data containing other networks are included in the Kagan tables. See also DCR Ex. 10X (providing additional cable network financial data underlying the Kagan analysis).

129. The Kagan Study also shows that it is not unusual for a new cable television network to pay more than 100 percent of its revenues in program expenses. Tr. 607 (Gerbrandt). The reason for this is that a new network must provide quality programming from the very beginning of its service in order to be valuable to a cable or DBS operator. Id. In arriving at the average cost, The Kagan study includes these start-up years, thus inflating the final number.

(2) WGA Study

130. The WGA study claims that the amount of license fees that Services would pay in free market negotiations (i.e., absent compulsory licensing) is equal to the weighted average of the programming costs of selected cable television networks. RIAA Ex. 15 at 1. Wilkofsky, the expert for the study, claimed an analogy to cable movie networks was appropriate because the "pricing characteristics and dynamics" of cable movie networks were "comparable" to those of the digital audio services. Wilkofsky W.D.T.. at 3 (submitted as RIAA Ex. 15). Wilkofsky based this conclusion on the basis of three characteristics of cable movie services: they lack commercials; they generate revenues through subscriber fees; and they generally purchase programming from third parties. Tr. 697 (Wilkofsky). Further, both Studies claimed the reason for the comparison was that the Services compete with other cable television networks -- not only for carriage by cable and DBS systems but also for consumer time and discretionary income. See, e.g., RIAA Ex. 13G (DMX 10K) at 15.

131. The WGA study concluded that since selected television networks pay a weighted average of 41.5 percent of their revenues for programming that they acquire from outside sources (Tr. 720-21 (Wilkofsky); RIAA Ex. 15 at 9-11, 18-19), the Services should pay the same amount. (RIAA Ex. 15 at 3, 14)

(3) RIAA's cable movie network analogy ignores fundamental differences between cable movie networks and digital audio services.

132. RIAA's approach is wholly inappropriate for a number of reasons. RIAA failed to introduce any evidence demonstrating that the demand and cost characteristics of digital audio services and cable movies are alike. Woodbury W.R.T. at 2-3.

(a) Not technically competitors on the same shelf but, even if, the analogy is still wrong.

133. The Services did present evidence, however, demonstrating that they do not "compete" for access to analog cable channels in the same manner as cable movie networks.[8] The Services use portions of spectrum that are not suitable for video. Tr. 1252-53 (Rubinstein); Tr. 1476 (Funkhouser); Tr. 1177 (Talley).

134. Many products are distributed to consumers through the same distribution channel, but are not necessarily expected to have similar demand and cost structures. Woodbury W.R.T. at 2. Products sold to consumers through grocery stores, for example, compete for shelf space in the store, but there is no reason to expect that the cost components of different products (e.g., cookies and ketchup) are the same. See id.; Tr. 2671-72 (Woodbury). Artificially applying expense ratios from one product to another to determine an appropriate level simply makes no sense. Id.

135. RIAA failed to show why HBO or AMC -- or any of the cable movie networks chosen by RIAA -- were the right cable movie networks to use for purposes of comparison to the Services. To the extent that the Services compete for shelf space on cable systems, there is nothing in the record indicating that they compete with HBO or AMC. Tr. 828-29 (Wilkofsky). See also Tr. 788-89 (Wilkofsky) (describing how the cable operator decides whether the Services should be given the channel space rather than the International Food Network).

[8] Wilkofsky admitted that his analysis would not help the Panel determine a license fee for any non-cable delivered music service. Tr. 797-98, 801 (Wilkofsky). This is a significant concession given that DMX and Music Choice are only partly delivered by cable, and Muzak is not delivered by cable at all.

(b) Economic value of Exclusivity Renders the analogy inappropriate.

136. Motion pictures and sound recordings are exploited in different ways. Until the mid-1980s, motion pictures were exploited only in theatrical release and in performances on broadcast or cable television. Following the acceptance by the motion picture industry of the videocassette recorder, motion pictures began to be sold to the public. Still, the sale of movies on tapes or laser discs or DVD generally comes several months after the theatrical release of the movie has been fully exhausted. The theatrical release historically has been a primary source of income for motion pictures and was not intended to be a promotional vehicle for sales of videocassettes. Rosenthal W.R.T. at 12-13; Tr. 151-52 (Berman).

137. This "windowing process" allows motion picture copyright owners to extract "as much money as they can" from different classes of consumers. Tr. 2673 (Woodbury). Through the windowing process, movie studios release movies sequentially, so that:

> Those consumers that value seeing the movie sooner rather than later will pay a higher price than other consumers. By controlling the timing of a movie's release to the various windows, movie studios will attempt to extract as much revenue as the various time-sensitive classes of consumers are willing and able to pay.

Woodbury W.R.T. at 3-4. Hence, comparing movie license fees, which reflect the value of exclusivity, to sound recording performance fees, which will not convey exclusivity, would be misleading. Id. See also Tr. 2674 (Woodbury) (not being able to purchase exclusivity will drive down the price of the license).

138. Copyright purchasers will value exclusivity for a number of reasons. Exclusivity allows a programmer to define

its identity in the marketplace. Sehring W.R.T. at 4. In addition, exclusivity facilitates promotion and marketing and alerts consumers to the attractiveness of the offered service. Id. Exclusivity also enhances the diversity of available programming. Id. at 5.

139. RIAA's reliance on cable movie networks generally and AMC particularly is misplaced.[9] "Exclusive distribution rights are the touchstone" of movie program acquisition. Id. at 3. Thus, AMC "would pay substantially less in license fees" absent the guarantee of exclusivity. Id. See also DCR Ex. 8X (Complaint, American Movie Classics Co. v. Turner Entertainment Co., No. 95 Civ. 4591 (S.D.N.Y., filed June 19, 1995)).

140. The fundamental value of exclusivity has been recognized by the Federal Communications Commission and the Copyright Office in the course of numerous proceedings dealing with copyright licensing. Until 1980, the Federal Communications Commission required local cable systems to "black out" programs on a distant broadcast signal that also appeared on a local broadcast station, if the local

[9]As David Sehring testified:

> Exclusive licensing is the paramount strategy of AMCC's business model and extremely important to our success in the highly competitive video marketplace. AMCC pays to have the exclusive television rights to motion pictures over every other cable and broadcast television station. The RIAA and its economic witness are dead wrong to claim that the value of exclusivity for performing motion pictures on cable television can be ignored. By importing intact the value of our purchases of promotable and exclusive movie product, the RIAA has written off the most basic and fundamental aspect of the market itself.

Sehring W.R.T. at 2.

broadcaster so requested.[10] When these rules were repealed in 1980,[11] the Copyright Royalty Tribunal raised the fees for compulsory licenses paid to program owners in order to compensate copyright owners for the loss of their "exclusive" licensing ability.[12] When the FCC reimposed the syndicated exclusivity rules, it recognized the fundamental value of exclusivity in the marketplace.[13]

141. RIAA itself testified that it sought to obtain an "exclusivity window" in the 1995 Act, but failed to convince Congress to do so. Rosen W.D.T. at 9; Tr. 250-51 (Rosen). Moreover, RIAA's recording industry witness testified that exclusivity plays an important role in determining the amount that a record company receives for licensing music videos. Tr. 326, 328 (Horowitz). Thus, RIAA understands the value of exclusivity. Since there is no comparable "window" protection in music distribution, RIAA's reliance on estimated cable movie license fee expenditures must be further discounted.

142. Notwithstanding, RIAA's chief economic witness failed to account for the importance of exclusivity, testifying that it would not matter to a cable movie service. Tr. 761-62 (Wilkofsky) (the value of exclusivity is "not a significant part of the dollars" and "de minimis"). Wilkofsky "did not adjust" for exclusivity in his calculations. Tr. 770 (Wilkofsky). By ignoring the value of exclusivity, RIAA grossly misstated the value of program acquisition costs in its analogy. See generally Sehring

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10 See Amendment of Part 74, Subpart K, of the Commission's Rules and Regulations Relative to Community Antenna Television Sys.; and Inquiry into the Development of Communications Technology and Services to Formulate Regulatory Policy and Rule Making and/or Legislative Proposals, 36 F.C.C.2d 141, recon. granted 36 F.C.C.2d 326 (1972).
11 In the Matter of Cable Television Syndicated Program Exclusivity Rules, Report & Order, 79 F.C.C.2d 663 (1980).
12 See Adjustment of the Royalty Rate for Cable Systems; Federal Communications Commission's Deregulation of the Cable Industry, 47 Fed. Reg. 52,146 (Nov. 19, 1982).
13 In re Amendment of Parts 73 and 76 of the Commission's Rules Relating to Program Exclusivity in the Cable and Broadcast Industries, 3 F.C.C.R. 5299, 5310 ¶ 66 (1988) (received in evidence as DCR Ex. 9X).

W.R.T. RIAA's failure to account for exclusivity in movie licensing demonstrates the complete irrelevance of the cable movie analogy.

(c) Basic Difference in Consumer Usage Effects Economic Value.

143. Consumer usage characteristics reflect this difference in the value of exclusivity. Generally, consumers listen to music while engaged in other activities. Watching a motion picture engages both the visual and auditory senses, and consumers generally must pay close attention to the movie as their primary activity. Watching a motion picture once or perhaps twice often exhausts consumer interest in a motion picture, whereas hearing a sound recording once or twice can stimulate consumer interest in buying the recording. Rosenthal W.R.T. at 13; Tr. 1251 (Rubinstein).

(d) The Relative Differences in their Value of Performance Renders Analogy Invalid.

144. In contrast to the windowing process for movies, records historically have been exploited almost exclusively by sales. To stimulate those sales, sound recordings almost always are made available for airplay simultaneously with their release for sale in stores, so that the airplay serves as a means to promote the sales of the recordings and not as a means of generating an independent income stream. Rosenthal W.R.T. at 13. Another difference rendering the analogy invalid is that motion pictures on cassette or disc can be rented, with no revenue flowing back to the movie company after the sale. Sound recording copyright owners have the legal right to prevent rental of sound recordings, which forces the consumer to purchase the recording to hear it in its entirety. Rosenthal W.R.T. at 13.

145. In addition, RIAA completely ignored the fact that "the promotional value of airplay in the sale of records and CDs is likely to be far more significant than that for movies appearing on cable networks." Woodbury W.R.T. at 5. Movie studios "actively restrict or limit the availability of their movies" through the use of the windowing process. Tr. 2677 (Woodbury). Recording companies, on the other hand, try to

seek the greatest possible exposure for their music. Tr. 2678 (Woodbury). That distinction points out that "the promotional value of getting songs [widely distributed] . . . is a very valuable commodity for the recording industry as compared to movies, where in fact just the opposite is true." Tr. 2678 (Woodbury). Accord Rosenthal W.R.T. at 12-13.

(4) Even if one accepted RIAA's analogy, the actual numbers are unuseable.

146. There are significant deficiencies in the WGA Study's methodology and underlying data. For example, the WGA Study multiplied the estimated amount that AMC, Bravo, and TCM (basic services) pay for programming times the ratio WGA believed that premium services spend on movies. Tr. 715-16 (Wilkofsky). WGA did not utilize the penetration rates of any of the services (audio or video) that it compared to adjust these expenditure amounts. Tr. 805-06 (Wilkofsky). WGA did not adjust the premium channel expenditure ratio before applying it to basic channel expenditures. Tr. 715-16 (Wilkofsky).

147. WGA relied upon inflated data, resulting in an artificially high license fee projection. The data excluded music-intensive cable channels (e.g., MTV, VH-1, and TNN) with low license fees in favor of cable movie channels with high license fees. WGA failed to perform any sort of analysis to confirm whether its admittedly "high" license fee was reasonable. Tr. 802 (Wilkofsky).

148. Most importantly, there isn't a consistent cable cost for programming. Cable doesn't negotiate a rate based on its gross income. Rather, it negotiates for programs on individual or block basis for a set period of runs or number of years. (Sehring) The rates vary so widely as to make an average, even a weighted average, unuseable. There is a tremendous disparity of rates whether comparing the various networks in a particular year (RIAA Ex. 14 at A1) or reviewing the same network over the eleven years of the chart (RIAA Ex. 14 at A3).

(5) RIAA Totally Failed to Reduce Claim by Music Works Cost.

149. Although the 41.5% averages utilized by both Studies include the cost of music works, neither study subtracted that amount from the amount it believed the Services should pay for the performance rights. This is especially egregious as RIAA claims the rate the Services pay is at least 10% for music works. RIAA's Reply Brief ¶ 111.

150. In light of these major deficiencies in the WGA study, there is no basis upon which to credit the end product of WGA's analysis (an artificially high 41.5% license rate), or Wilkofsky's conclusion that the Services likewise would pay this 41.5% rate to record companies in a free market.

b. Services' Estimates of Market Rate

(1) John R. Woodbury, Ph.D.

151. As part of their direct cases, the Services sponsored the testimony of John R. Woodbury, Ph.D., who testified that a competitive market for digital sound recording performance rights would produce outcomes along a range of possibilities. Dr. Woodbury then demonstrated that a competitive market rate consistent with the objectives of the 1995 Act would be "closer to the lower rather than the higher end of the competitive range." Woodbury W.D.T. at 7. Several factors weighed into this analysis.

152. Dr. Woodbury considered that the recording industry is relatively competitive under the standards utilized by the Department of Justice and the Federal Trade Commission. Id.[14] The market price for performance rights is "likely to be substantially less than the monopoly level, absent any factors that would facilitate collusion among the recording companies." Id. at 8.[15]

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14 U.S. Department of Justice and Federal Trade Commission Horizontal Merger Guidelines (1992), reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,104.
15 The Act provides an exemption for copyright owners to negotiate collectively, but this does not obviate Dr. Woodbury's empirical conclusion as buttressed by the economics underlying the federal agencies' merger guidelines.

153. Dr. Woodbury testified that the high promotional value of airplay would encourage record companies to "reduce performance fees [in order] to encourage the playing of their songs." Woodbury W.D.T. at 8. The record shows that the business model for the recording industry relies upon exposure to stimulate sales. Tr. 154 (Berman); Tr. 1289-91 (Rubinstein); Tr. 335-37, 343, 345 (Horowitz); Tr. 2220 (Wildman).

(2) Radio

154. Each of the Services believes that radio is its most significant competition (Tr. 2289 (Del Beccaro); Rubinstein W.D.T. at 35-36; Tr. 1491-92 (Funkhouser)), although some of their SEC filings also note that they compete with cable television programs for consumer dollars and time. (RIAA Ex. 13G (DMX 1996 Form 10K) at 15.) Congress clearly considered the comparison and decided that the Services were to pay a fee for performance. Therefore any comparison with radio to determine that Services should pay nothing or near nothing is unnecessary.

(3) <u>DCR Negotiated Performance Rate with 60% of Recording Industry.</u>

155. DCR's partnership agreement contains a sound recording performance license. See DCR EXs. 7, 8, and 15. See also Del Beccaro W.D.T. at 8-9. This license, negotiated between DCR's record company and cable industry partners, provides the Panel with a useful benchmark in this proceeding. Woodbury W.D.T. at 12.

156. A sound recording performance right did not exist when DCR's license was negotiated. However, the significance of the license is not that it "creates" a sound recording performance right. Instead, through the license, DCR "sold" to its record company partners the recognition they sought "that the right existed for a particular rate." Tr. 2777 (Woodbury).

157. Performers and record producers had been arguing for years that the copyright law should be amended to include a "performance right." Tr. 2099 (Vidich) Legislation had

been introduced as recently as 1981 and 1991. Del Beccaro W.D.T. at 8. Indeed, the Copyright Office had recommended "amendment of the 1976 Copyright Act to extend a public performance right to sound recordings" less than four months before DCR commenced negotiations with the record companies.[16]

158. At that time, DCR was experiencing severe financial pressures. Del Beccaro W.D.T. at 8. Management believed that it was absolutely essential to sign on at least one record company partner. Id. However, every record company DCR approached was "adamant about obtaining a sound recording performance license as part of any deal." Id. DCR's partners were skeptical about such an arrangement. Id. at 9.

159. Eventually, Sony and Warner Music Group commenced negotiations with DCR and, separately, with DMX. In their negotiations, both record companies insisted on the license as part of any deal. Del Beccaro W.D.T. at 9; Tr. 874 (Del Beccaro) (noting that the record companies made clear throughout the course of the negotiations that "there was no deal without a copyright deal"); Rubinstein W.D.T. at 37; Tr. 1294-96 (Rubinstein) ("we knew that part of the price of doing the deal was a licensing agreement that under current law we were not obligated to do or pay").

160. Soon after the negotiations commenced with DCR, Sony and Warner provided David Del Beccaro with deal points and a proposal entitled "Grant of Performance Right." DCR Ex. 1RX ("Deal Points"); DCR Ex. 2RX ("performance rights proposal"). The deal points did not mention five free years of service to Time Warner Cable. Tr. 2136 (Vidich). The performance rights proposal "grant[ed] DCR a non-exclusive blanket license to perform publicly all sound recordings controlled" by Sony and Warner Music. DCR Ex. 2RX.

[16] Register of Copyrights, Copyright Implications of Digital Audio Transmissions Services, at 160 (Oct. 1991) ("1991 Copyright Office Report"). DCR had participated in that proceeding, as had RIAA on behalf of the recording industry.

161. Shortly into the negotiations with DCR, Sony and Warner broke off the talks and began negotiating with DMX. The two companies submitted to DMX a proposed sound recording performance license that would be an express condition of any deal. Rubinstein W.D.T. at 37-38; Tr. 1295-97 (Rubinstein). The license contained a royalty rate of 2% of DMX's revenues multiplied by the percentage of recordings performed by DMX that were controlled by those companies. Rubinstein W.D.T. at 37. The proposed license was for a 25-year term. Id. at 38. DMX was never told by anyone on behalf of Time-Warner or Sony Music that the rate was anything other than a fair rate for the performance right. Rubinstein W.D.T. at 37; Tr. 1297 (Rubinstein).

162. An agreement with DMX was not signed, however. Still eager for a deal, DCR called Sony and Warner. Del Beccaro W.D.T. at 9. To remain competitive with the DMX offer, DCR agreed to give Time-Warner Cable five free years of service. Id.; Tr. 946-48 (Del Beccaro). In addition, DCR agreed to amend the "Effect" clause in the license to read that:

> execution of this Agreement [does not constitute] an acknowledgment . . . that United States law, as of the date of this Agreement, requires the obtaining of a license or the payment of a fee or royalty to perform sound recordings publicly. Notwithstanding the foregoing, DCR is entering into this Agreement as one part of a complex commercial transaction . . . .

DCR Ex. 7 (emphasis added). This language was substantially more limited in scope than the language originally proposed by DCR. The parties further negotiated the performance rights fee, eventually arriving at 2% of gross revenues, allocated on the basis of DCR's playlist. Tr. 2123-24 (Vidich).

163. The recording companies insisted that the DCR license agreement provide (1) that the two percent rate would be superseded if Congress established a performance right in sound recordings and (2) for a most favored nations clause which would give all parties the right to receive the benefit of a more favorable rate. DCR Ex. 7, 8 & 15 at ¶ 9

164. In January, 1993, Sony and Warner invested in DCR. As part of the deal, each record company granted DCR a license to perform its recordings. See DCR Exs. 7, 8. In April, 1994, EMI joined the partnership under substantially similar terms. See DCR Ex. 15.

165. When the deal was eventually announced, Sony and Warner trumpeted the fact that DCR "entered into a licensing agreement for use of their repertoire" and that the agreement called for DCR to support a performance rights royalty on sound recordings. See DCR Ex. 27 (Paul Verna, Time Warner Breaks New Cable Ground: Enters Cable Radio Venture With Sony, Billboard, Feb. 6, 1995, at 1). These statements were authorized by Warner, according to its chief negotiator. Tr. 2127 (Vidich). It is clear, therefore, that the license agreement had "substantial precedential value to Warner and Sony." Woodbury W.D.T. at 15-16. Accord Woodbury W.R.T. at 18.

166. Since the negotiated rate was 2% for only 60% of the record industry the logical conclusion of that argument is that the rate should be 3.3% for 100% of the market. That 3.3% is not quite a perfect comparison for the section 114 fee as it is unclear what portion if any would go to the performers. While there was nothing in the documentation to delineate what portion if any, would go to the performers, some performers' contracts may have made them entitled to a portion of the fee. Based on the foregoing, the Panel finds that a pure doubling of the 3.3% to 6.6% would be inappropriate. However the Panel finds that this freely negotiated rate does set a reasonable range between 3.3% to 6.6%.

c. Music Works Rates Provide a Market Place Comparison.

167. Given the pending ASCAP litigation, the royalty fees that the Services will ultimately pay for performing musical works during the period 1996-2001 cannot be determined precisely at this time. However, several facts, as discussed above, suggest that the total payments will be between 5 and 10 percent of the Services' "gross revenues" --

A) Music performance license rates paid by radio stations to BMI and ASCAP combined are approximately 3.2% of station revenues, and payments to SESAC are also within the low single digit range. Rosenthal W.R.T. at 3; Tr. 1705 (Rosenthal); Tr. 1646, 1669-70 (Massarsky). Commercial radio thus pays approximately 4% for a blanket music works license.

B) ASCAP's small percentage rate from commerical radio stations generates over 100 million dollars a year. Tr. 1694 (Massarsky). ASCAP takes the position that the larger the revenue base the smaller the percentage they are willing to take. Since the Services have a smaller revenue base, ASCAP, as well as the other music works providers will look for a higher percentage. Tr. 1694-95 (Massarsky).

C) DMX has negotiated an agreement with BMI requiring a 4 percent of gross license fee during the period October 1, 1996 through September 1999. Tr. 1652 (Massarsky).

D) DCR is also paying BMI 4 percent of gross as an interim license fee. Tr. 1653 (Massarsky).

E) ASCAP license fees are generally greater than, but at least no less than, BMI license fees.[17] Tr. 1648-69 (Massarsky).

F) Based upon DMX's negotiated agreement with SESAC, the SESAC payments will account for approximately one percent of the Services' revenues.

[17]The Services have not negotiated any final agreement with ASCAP. Rather, along with other cable networks, they are currently paying an interim fee set in 1989 while awaiting a decision by the ASCAP rate court in the Southern District of New York. Tr. 1029 (McCarthy). The interim fee is 15 cents per subscriber per year. Tr. 1423 (Rubinstein); see RIAA Ex. 3RX. The same 15 cent fee is charged regardless of whether the subscriber receives the Service as a premium channel or as part of a basic tier. Tr. 1424 (Rubinstein).

G) Thus the Services may pay on the high range approximately 10% (BMI 4%, ASCAP 4-5%, and SESAC 1%).

See Rosenthal W.R.T. at 3; Tr. 1646-67 (Massarsky); Tr. 1668-70 (Rosenthal); Tr. 2415 (Trautman); DMX Exs. 24-27 (DMX license agreements with ASCAP, BMI and SESAC).

168. The Services' argument that the 114 fee should be compared individually to the BMI, ASCAP and SESAC rates does not withstand analysis. BMI, ASCAP and SESAC can be viewed collectively as collecting money for all the songwriters and publishers. Their fees, as calculated here, are a percentage of gross revenues. The fees are not limited to income designated from certain songs. The Services must deduct that full cumulative 5-10 percent against their gross income. Since the Section 114 fee is also a collective fee, it becomes a cumulative number to use for comparison.

169. There was insufficient and conflicting evidence to make a determination that the performers and record companies deserve a larger percentage from the Services than granted to the music works. They are both parents of the music.

V. LICENSE TERMS

170. The Panel is required to set license terms as well as a royalty rate pursuant to 17 U.S.C. §114(f)(2). See also RIAA Ex. 8B (S. Rep . 104-128) at 30 ("By terms, the Committee means generally such details as how payments are to be made, when, and other accounting matters (such as are prescribed in Section 115"). License terms are needed to assure that the license fee established by the Panel is properly calculated, paid and verifiable. The license terms should specify:

A. A minimum fee;

B. The timing of license fee payments, including late fees for untimely payments;

C. Reporting requirements prescribing the information to be provided in, and the timing of, statements of account to be submitted by the Services; and

D. Provisions requiring the Services to maintain accurate books and records of the information used to calculate the license fee, and to permit those books and records to be audited to assure that the appropriate fees have been paid.

Leibowitz W.D.T. at 1 and 5: Tr. 1863, 1877-80 (Leibowitz).

A. The Minimum Fee

171. Both RIAA and the Services have requested that the Panel establish a license fee based on a percentage of gross revenues. In addition, RIAA requests the Panel to set a minimum fee based upon a flat rate. In support of its request, RIAA asserts that such minimum fee is necessary:

1. To ensure that the license fee is not eroded by discounts or credits which might occur, when a Service deals with a commonly-owned affiliate or when it sells both residential and commercial programming to a cable operator or DBS provider;

2. To address new marketing strategies that could undercut the statutory license fee; and

3. To safeguard the value of sound recording given the possibility of providing increased numbers of music channels without adequate compensation.

Leibowitz W.D.T. at 2; Tr. at 1864-66 (Leibowitz).

172. The Services oppose any minimum fee. Each of RIAA's arguments is considered below:

1. Discounts or Credits

173. RIAA's concerns that warrant a minimum fee are best illustrated by the situation involving Time Warner Cable. As noted above, DCR granted Time Warner Cable five free years of music programming as part of a series of agreements in which Time Warner Cable and Warner Music made

a multi-million dollar investment in DCR. Tr. 891, 957 (Del Beccaro). Time Warner Cable, which accounts for approximately 40 percent of all DCR premium subscribers, pays DCR only about 30 cents per subscriber per month to cover license fees owed to ASCAP, BMI and SESAC. Tr. 891, 919-20 (Del Beccaro); DCR Ex. 48 at 1. This is far less than the $2.50 per subscriber per month average wholesale price that DCR normally receives. Tr. 974-75 (Del Beccaro).

174. Absent a minimum fee, DCR could argue that its "gross revenues" for Time Warner Cable's premium service are only 30 cents per subscriber per month, and that DCR only has to pay license fees as a percentage of those revenues. See Tr. 2034-37 (McCarthy). This, RIAA argues, would undermine the statutory license fees to be paid to record companies, and those paid to artists and performers. See Tr. 1894-95 (Leibowitz).

175. The protection that RIAA is seeking through a minimum fee is, in part, what the performing rights societies have achieved through marketplace negotiations concerning the five years of free service that DCR is providing to Time Warner Cable. Despite DCR's agreement to provide Time Warner with free service, DCR still pays BMI, ASCAP and SESAC license fees for the performance of musical works. See Tr. 2023-24 (McCarthy).

176. The Services argue that the DCR deal was an aberration, caused by DCR's extreme business duress. Rather, as Woodbury testified, the Services will seek a profit-maximizing rate for their offerings. See Services Proposed Findings. 162-70.

177. In addition to the concern about the DCR agreement, the Panel notes that Music Choice's partners account for more than 90 percent of its cable revenues. Tr. 2068 (McCarthy). Moreover, TCI's recent purchase of DMX also poses the risk of license arrangements that would not typically be made by unrelated companies. See Tr. 1396-97, 1929-30 (Leibowitz). Notwithstanding RIAA's concerns, the Services contend and the Panel agrees that there are strong deterrents to such artificial pricing strategies including: MFN clauses in

license agreements with unaffiliated entities; likely detection in the auditing process; the inherent need for any business to maximize income from all sources; and probable objections from the Services' non-cable system partners and investors. Services Proposed Findings 163-166.

2. Marketing Strategies that Could Undercut the Fee.

178. RIAA also argues that a minimum fee is needed to respond to marketing strategies that could undermine the license fee that the Panel determines reflects the market value of the thirty channels of digital programming now offered by the Services.

179. Both Del Beccaro and Lon Troxel (president and chief executive officer, respectively of DMX and DCR) testified that the Services need pricing flexibility to meet the demands of an increasingly competitive market and emerging technologies, and that performance royalties should be commensurate with the Services' gross revenues as a percentage of those revenues. Tr. 2578-80 (Troxel); Tr. 2303 (Del Beccaro).

180. The Panel finds the argument that a minimum license fee would address new marketing strategies which might undercut the statutory fee to be specious. The statutory fee is based upon the Services' total revenues. The Services will survive if they can increase their penetration into new markets with a basic service rather than a premium product. Their gross revenues will increase if the combination of new subscribers times their revenue per subscriber yields an overall higher gross revenue. If the lower cost basic service does not grow as anticipated by the Services, they will not survive in the market place. Clearly, the increase in gross revenues will yield higher fees to RIAA. If the new marketing strategies do not work, then both the Services and RIAA will suffer losses.

3. The Amount of Music Performed.

181 RIAA asserts that a minimum fee should take into account the amount of music performed by the Services.

RIAA requests a minimum fee for every channel.[18]

182. While some of the Services charge per channel rates for some of their services,[19] they also charge flat wholesale rates.

183. The Panel finds that RIAA's proposed per channel rates would provide an incentive for the Services to offer fewer channels of music, Tr. 2262, 2268 (Wildman); Tr. 2560-61 (Troxel), ultimately reducing the availability of sound recordings generally and less popular music specifically, clearly contrary to the objectives of copyright law.

B. <u>The Timing of License Fee Payments: Notice and Payment Provisions</u>

184. First, the Panel agrees with both RIAA and the Services that any notices and payments required by the CARP "should be submitted to a single private entity or government agency that will distribute the funds to sound recording copyright holders." Services Proposed Findings & Conclusions at ¶ 123, Reply of RIAA at ¶ 139, Services' Terms Submission at 2; Tr. 1975-76 (McCarthy). The members of the RIAA Collective represent more than 90 percent of all legitimate sound recordings made in the United States. See ¶ 20, <u>supra</u>. RIAA requests that it be named the single entity. The Services did not object to RIAA's request. Accordingly, the

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[18] RIAA's argument that judicial precedent supports consideration of the amount of music used in establishing license fee rates is overstated. RIAA cites <u>United States v. ASCAP</u>, Civ. No. 13-95 Mem. and Order (S.D.N.Y. Oct. 12, 1989) for the proposition that courts will consider the amount of music used in setting interim rates. The District Court explained, however, that the amount of music used is only one factor it will consider in the context of calculating a market price.

[19] Muzak's wholesale price is based upon a per channel charge. Tr. 1415 (Funkhauser); and see RIAA Ex. 19 at 6, Muzak Affiliation Agreement with EchoStar (12/28/95) which specifies a per subscriber monthly license fee of $.005 "per music Channel". DMX offers 90 channels of programming for a retail charge of $19.00 or $20.00 per month. Tr. 2589-90 (Troxel). This is roughly twice the retail price for DMX's 30 channel premium service. Tr. 1283 (Rubinstein). Mr. Rubenstein stated the rationale for this difference in price is that DMX Direct provides the subscribers with a greater selection of music. Tr. 2589-90 (Troxel).

Panel finds that the RIAA Collective shall serve as that "single private entity."[20]

185. Next, the Panel rejects the Services' proposal that license fee payments should be made on a quarterly basis, 45 days after the end of the first three quarters of each year and 60 days after the end of the year. Services' Terms Submission at 2-3; Tr. 1975-76 (McCarthy).[21] Rather, it adopts RIAA's proposal and finds that monthly payments shall be made on the twentieth day after the end of each month, commencing with the month succeeding the month in which the royalty fees are set. Leibowitz W.D.T. at 5; Tr. 1881 (Leibowitz). There is ample support for requiring monthly payments both in Copyright Office regulations and in the Services' negotiated agreements with BMI. See, e.g., 37 C.F.R. 201.19(e)(7)(i) (mechanical license payments are due on the twentieth day after the end of each month) and DMX Ex. 26 at 5 (DMX agreement with BMI requiring advance monthly payments of performance fees). A monthly payment schedule is also supported by DMX's and Muzak's affiliation agreements, which require cable operators and DBS providers to pay the Services each month. See, e.g., RIAA Ex. 11X at 4 (DMX affiliation agreement requiring Primestar to pay DMX 30 days after the end of each month); RIAA Ex. 19 at 8 (Muzak affiliation agreement requiring EchoStar to pay Muzak within 45 days of

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20 The Panel recognizes that in addition to its responsibility to set reasonable rates and terms governing the use of sound recordings, Section 114(f)(2) directs the Librarian of Congress to "establish requirements by which copyright owners may receive reasonable notice of the use of their sound recordings under this section, and under which records of use shall be kept and made available by entities performing sound recordings." In response to this provision, the Copyright Office has commenced a rulemaking proceeding, Docket 96-3, to address the notice and recordkeeping requirements.

21 The Services seek to include various payment terms in their Proposed Conclusions of Law that have no support in the record evidence, were not the subject of any written or oral testimony, and are not mentioned or supported by anything in their Proposed Findings of Fact. These proposed terms would establish payment schedules for the RIAA Collective to distribute license fees among featured artists and nonfeatured musicians and vocalists. Services Proposed Findings & Conclusions ¶¶ 287-89. While there is no question that these featured artists and other performers are entitled to a statutory share of the license fees (17 U.S.C. §114(g)), the Panel has not been presented with any testimony or other evidence about an appropriate payment schedule for these individuals. Furthermore, the issue of the timing of payments from the RIAA Collective to artists and other performers is not within the scope of this proceeding.

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the end of each month). It is also noted that Section 114(f)(5)(B) of the DPRSA, discussing back payments, speaks in terms of payment within a month. See also Leibowitz W.R.T. and Tr. 1881 (Leibowitz).

1. Phasing-in the "back payment".

186. The Panel finds that the back payment required by 17 U.S.C. §114(f)(5)(B) covering the period between the 1995 Act's February 1, 1996 effective date and the end of the month in which the Panel sets the royalty rate should be phased-in. There is CRT precedent for phasing-in license fees. For example, in 1981, the CRT adjusted the license fee to be paid by the jukebox industry to composers and music publishers for the performance of musical works. The CRT found that the fair and reasonable license fee --which had been $8 per jukebox--was $50 per jukebox. The CRT phased-in this rate, starting at $25 per jukebox and then adjusting to the full rate of $50 roughly a year after the CRT issued its decision. 46 Fed. Reg. 884,886,888 (1981). The CRT phased-in the jukebox license fee "to accord the jukebox industry an opportunity to adjust, since in [the CRT's] view the jukebox industry has never previously paid reasonable compensation for the use of copyrighted music." 46 Fed. Reg. at 888. The CRT reasoned that phasing-in the fee satisfied the statutory criteria in section 801(b)(1)(D) --which also applies here-- "[t]o minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices." 46 Fed. Reg. at 889. The Panel finds, as did the CRT, that such phasing-in will achieve the objective of § 801(b)(1)(D) of the Act. See also RIAA Ex. 8B (S.Rep. 104-28) at 30.

187. The Panel finds that the least disruptive impact will be achieved as follows: The first back payment shall be delayed for six months. Thereafter, the Services shall pay 1/30th of the total arrearage each month for the following 30 months. These payments shall be in addition to the current royalty payments dues each month. Since the 1995 Act does not provide for interest on back payments, no interest will be charged.

2. Liability for Copyright Infringement

188. If a Service fails to make timely payment of the statutory license fees, it will be subject to liability for copyright infringement. See 17 U.S.C. §114(f)(5)(A)(i) (sound recordings may be performed by qualifying subscription services "without infringing the exclusive right of the copyright owner of the sound recording - (i) by complying with such notice requirements as the Librarian of Congress shall prescribe by regulation and by paying royalty fees in accordance with this subsection..."). However, given the possibility of an inadvertent breach, such as a violation of the sound recording performance complement due to computer programming errors or equipment failure, the Panel finds that liability for copyright infringement will only come about for knowing and willful acts which materially breach the statutory license terms.

3. <u>Late Fee</u>

189. A late fee will be imposed at 1.5% per month or the highest lawful rate, whichever is lower, from the due date until payment is received by RIAA. Leibowitz W.D.T. at 5; Tr. 1882 (Leibowitz). This is consistent with the payment terms negotiated by the Services with cable operators and DBS providers. See, <u>e.g.</u>, RIAA Ex. 11X at 4, DMX Affiliation Agreement with Primestar (1/25/96) (imposing a late fee of 1.5% per month "or the highest lawful rate, whichever is less, from the due date until payment is received by [DMX]"); RIAA Ex. 16 at 5, DMX Affiliation Agreement with Moffat International Corp. (12/22/95) (same); RIAA Ex. 19 at 9, Muzak Affiliation Agreement with EchoStar (12/28/95) (imposing the same late fee, but allowing one late payment of not more than 10 days per calendar year).

C. <u>Reporting Requirements</u>

1. <u>Statements of Accounts</u>

190. The Panel adopts RIAA's proposal that the Services submit monthly statements of accounts along with their payments on a form to be provided by RIAA. The Panel agrees with the position taken by the Services that the form must be confined to information necessary to verify the Services'

royalty payments. Toward this end, the form should generally conform to the Copyright Office statements in the parallel Copyright Office performance right rulemaking proceedings. See Notice of Proposed Rulemaking, 62 Fed. Reg. 34035-34039 (June 24, 1997). It is emphasized that the Panel is of the view that RIAA may not seek additional information in its statements of account beyond that necessary to calculate the royalty payments. See Tr. 1920-21 (Leibowitz).

2. Confidentiality

191. As the Services propose (Service Terms Submission at 3; Tr. 1973-75 (McCarthy)) and to which RIAA does not object (RIAA Reply Findings ¶144), effective safeguards must be established to protect against disclosure of confidential financial and business information to recording companies, copyright owners and subscription service competitors. In this regard, the amount of royalty payments made by each Service shall be considered Confidential Material and shall be kept by RIAA in locked files. Access to Confidential Material shall be limited to:

(a) those persons who are employed by RIAA, including independent contractors,[22] who require access to this information to perform their assigned duties in the ordinary course of their employment, and who are not an employee or officer of a sound recording copyright owner or recording artist; and,

(b) an independent auditor who is not an employee or officer of a sound recording copyright owner or recording artist, but is authorized to act on behalf of RIAA with respect to the auditing of underlying records and who is independent and qualified.

D. RecordKeeping and Audits

192. Both RIAA and the Services agree that the Services should be required to keep and maintain accurate books and records on matters directly related to payment of the license

[22] The need for the information "in the ordinary course" of one's work for RIAA, and not the person's technical employment status will be controlling

fees in accordance with generally accepted accounting principles. RIAA maintains that these books and records should be retained for at least four years after the period to which they relate. Leibowitz W.D.T. at 6; Tr. 1884 (Leibowitz). The Services' position is that supporting data should be maintained for no more than three years. Terms Submission at 3. See also Copyright Office, Notice and Recordkeeping for Subscription Digital Transmission, Notice of Proposed Rulemaking, 62 Fed. Reg. 34035-34039 (Question for Comment NO.9)(June 24, 1997). The Panel finds that the retention period should be three years. As indicated infra, RIAA itself acknowledges that it should only have the right to audit for three years, and there is a three-year statute of limitations for bringing suit under the Copyright Act. Tr.1992 (Leibowitz); Leibowitz Amended W.D.T. at 7.

193. The Services propose and RIAA agrees that the audit procedure should require timely filing by an interested person of "a notice of intent to audit"; publication of notice in the Federal Register; and that "[o]nly one audit of any service...be allowed with respect to financial records for any given year." Terms Submission at 3; Tr. 1974-75 (McCarthy). So, too, RIAA does not object to the Services' proposal contained at paragraph 300 of its Proposed Findings and Conclusions (even through not originally set forth in the Services' Terms Submission) that RIAA be required to retain an auditor's report for the same period of time that the Services are required to retain documents. See RIAA Reply Findings at paragraph 147. The Panel finds and adopts the foregoing agreements.

194. The Panel also agrees with the Services' position, consistent with the principle of limiting unnecessary expense and disruption, that where a Service can provide an audit already performed in the ordinary course of business by an independent auditor, pursuant to generally accepted auditing standards, such audit and underlying work papers should serve as the audit on behalf of all interested persons unless it can be shown that the auditor did not follow generally accepted auditing standards. This procedure would result in fair opportunity to audit for copyright owners, while

reducing the burden and expense of auditing upon the Services. Terms Submission at 3-4; Tr. 1974-75 (McCarthy).

195. The Services propose that RIAA and other interested parties pay the expenses of an audit unless there is a "judicial determination" or an agreement by the affected Service that there was an underpayment of royalties of 5 percent or more. Services PROPOSED FINDINGS & CONCLUSIONS at ¶ 166. Leibowitz W.D.T. at 6-7; Tr. 1884-85 (Leibowitz). However, RIAA contends and the Panel concurs with RIAA that the Collective should not have the burden of filing a lawsuit to have a Service reimburse the audit expenses where an independent auditor concludes that there has been such an underpayment. In that situation, the burden should fall on the Service to justify its payment. Indeed, RIAA's audit proposal is modeled after the Services' own affiliation agreements. See, e.g., RIAA Ex. 11X at 5 (requiring that PrimeStar pay DMX's audit expenses if there is a "deficiency variance" of 5 percent or more); RIAA Ex. 19 at 9-10 (requiring that EchoStar pay Muzak's audit expenses if there is an underpayment of more than 5 percent).

CONCLUSIONS

196. On the basis of the written record constituting the testimony and evidence in this proceeding, prior decisions of the Copyright Royalty Tribunal, prior copyright arbitration panel determinations and rulings by the Librarian of Congress under section 801(c), 17 U.S.C. §801(c), and the Findings of Fact set forth above, the Panel concludes that:

I. COMPLIANCE WITH THE STATUTORY OBJECTIVES LEADS TO A ROYALTY RATE OF 5%

197. DCR, DMX and Muzak each comply with the factors set forth in the 1995 Act, 17 U.S.C. §114 (d)(2), and thus qualify for a compulsory license to perform sound recordings.

198. The Panel has considered the various objectives set forth in the Copyright Act in going about its task of setting a "reasonable" rate and terms. As to each objective, it concludes as follows:

A. To maximize the availability of creative works to the public (17 U.S.C. § 801(b)(2)(A)), the Panel concludes that the rate should be set on the low side. A lower rate will hopefully ensure the Services' continued existence and encourage competition so that the greatest number of recordings will be exposed to the consumers.

B. The Panel has reviewed the evidence to establish a rate that will "afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions" (17 U.S.C. § 801(b)(2)(B)). Since the economic conditions are so strained at this early stage in this new digital subscription business, a rate on the low side is warranted, although a rate needs to be significant to afford a fair return to the performance rights holders.

C. In assessing the objectives suggested by Section C, (17 U.S.C. § 801(b)(2)(C)), the Panel concludes that the copyright owner makes the largest creative contribution in the product made available to the public. The technical contributions, with the exclusion of the development of the compact disc, the capital investment and cost risk have been almost totally borne by the subscription services in their attempt to bring music into the homes of the public. The subscription services have made substantial efforts to open new markets for sound recordings, although any success in this effort has yet to be quantified. On balance, the objectives in Section C favor the Services and support a minimum royalty rate.

D. In setting forth a rate which will have the least disruptive impact on the structure of the industries involved and on the generally prevailing industry practices (17 U.S.C. § 801(b)(2)(D)), the Panel again concludes that the rate must be on the low range. A rate too high will clearly be disruptive.

199. RIAA suggests that a royalty rate of 41.5% would be a fair return. This number was calculated by determining the average cost of procuring creative works by cable networks which acquire essentially all of their programming from outside sources. The Panel concludes that this comparison is

not analogous to the Digital Audio Subscription Service industry.

200. One of the members of the Services, on the other hand, suggests that a contract entered into between DCR and Sony Music and Time-Warner which contains a performance rights royalty of 2% provides a useful precedent for setting a royalty rate in this proceeding. The Panel concludes that although this 2% royalty rate does provide an appropriate benchmark, there are certain obvious flaws. Since, as indicated in the Findings, this negotiated rate was for only 60% of the record industry (the sound recordings controlled by Sony and Warner Music), a rate of 3.3% should arguably apply to 100% of the recording industry market. Such 3.3% rate does, however, not clearly recognize the fact that half of the royalty must go to the performers. Since there is no documentation in this record as to what, if any, portion of that amount would go to the performers, the Panel concludes that a pure doubling of the 3.3% rate would be inappropriate. However, this freely negotiated rate does set a reasonable range between 3.3% and 6.6%. It is the Panel's view that compliance with the statutory objectives leads to a royalty rate of 5%, well within this range.

201. Further support is found in the record evidence suggesting that the royalty fees which the Services will ultimately pay for performing musical works during the period 1996-2001 will likely be between 5 and 10% of the Services' gross revenues (see paragraphs 167-169 <u>supra</u>). There was insufficient and conflicting evidence upon which to make a determination that the performers and record companies deserve a larger percentage from the Services than granted to the music works.

202. In sum, the Panel has concluded that the cumulative Music Works rate and the Warner/Sony negotiated rate are the most comparable types of "digital audio transmission services" rates (17 U.S.C. § 114(f)), and that a royalty rate of 5% will further the statutory objectives set out by Congress. RIAA asks the Panel to gamble that the estimates that the Services testified to are low. We find no reason to gamble, to set a rate so high as to force one or all of these Services out of this business. Rather, we prefer to

encourage competition among the Services in an attempt to expand the number of artists whose works are played on this new subscription digital media. Our position is strengthened by the knowledge that there will be another rate setting hearing in the year 2001. In this new era of technological advancements, this digital subscription industry may have a different face by then. By that time, perhaps the Services will be profitable, and perhaps they will be able to show that they do encourage substantial increases in record sales. Either way, that CARP Panel may reach a substantially different decision.

II. THE LICENSE TERMS

203. Finally, the Panel is required to set license terms as well as a royalty rate. In this regard, the Panel concludes, in order to assure that the 5% license fee it has established will be properly calculated, paid and verifiable, that the following terms shall prevail:

A. Minimum Fee

204. The Panel concludes that there is no reason at this point to impose a minimum license fee upon the Services. There is some concern on the part of the Panel that the Services could offer free service to their partners and affiliates in exchange for other benefits, thus lowering or eliminating royalties to the artists and recording companies. However, the Panel rejects the minimum fee on the grounds that it unnecessarily adds new factors to an already complex undertaking. The application of a percent of gross revenues to determine royalty fees is straight-forward. In the rapidly changing market place, tying a minimum fee to subscribers or number of channels of music offered could conceivably result in payments higher than the statutory fee. In our view, the application of a minimum fee could create confusion and mischief and could replace a carefully calculated rate with a bundle of payments of uncertain origin and without relation to the statutory mandates governing this Panel. Again, the Panel recognizes that in the year 2001, the royalty rate will be reviewed, along with the question of the need for a minimum fee. Such future Panel will surely consider any attempts to avoid the royalty rate.

B. <u>The Timing of License fee Payments: Notice and Payment Provisions</u>

205. Notices and payments required shall be submitted to the RIAA Collective which shall be responsible for the distribution of the funds collected to the sound recording copyright holders.

206. License fee payments shall be due on or before the twentieth day of the month succeeding the month in which the royalty fees are set. Subsequent payments will be due on the twentieth day after the end of each month.

a. The "back payment" required by 17 U.S.C. § 114(f)(5)(B) covering the period between February 1, 1996 and the end of the month in which the royalty rate is set shall be phased-in as follows: The first back payment shall be delayed for six months. Thereafter, the Services shall pay 1/30th of the total arrearage each month for the following 30 months. These payments shall be in addition to the current royalty payments due each month. No interest will be charged on these back payments if paid on time. However, a late fee will be imposed to the extent they are not paid as required by this subparagraph.

b. If a Service fails to make timely payment, it will be subject to liability for copyright infringement. Such liability will only come about, however, for knowing and willful acts which materially breach the statutory license terms.

c. A late fee will be imposed at 1.5% per month or the highest lawful rate, whichever is lower, from the due date until payment is received by RIAA.

C. <u>Reporting Requirements:</u>

207. The Services shall submit monthly statements of account along with their payments on a form to be provided by RIAA.

208. Safeguards must be established to protect against disclosure of confidential financial and business information to recording companies, copyright owners and subscription service competitors.

D. <u>RecordKeeping and Audits:</u>

209. Books and records on matters related to payment of the license fees shall be kept in accordance with generally accepted accounting principles for a period of three years.

210. Audit procedure:

a. Interested persons shall file a notice of intent to audit.

b. Such notice shall be published in the <u>Federal Register</u>.

c. Only one audit of any Service shall be allowed with respect to financial records for any given year.

d. RIAA must retain an auditor's report for three years.

e. Where a Service can provide an audit already performed in the ordinary course of business by an independent auditor, pursuant to generally accepted auditing standards, such audit and underlying work papers shall serve as the audit on behalf of all interested persons.

f. RIAA and other interested parties shall pay the expense of an audit unless an independent auditor concludes that there was an underpayment of royalties of five (5) percent or more.

III. <u>DETERMINATION AND ASSESSMENT OF COSTS</u>

211. For the reasons set forth above and based upon the delineated facts of record, the Panel determines that the Section 114 royalty rate to be paid by all subscription digital transmission services not subject to voluntary agreement to the copyright owners of the sound recordings

shall be 5% of the service's gross revenues from its U.S. residential services payable in accordance with the license terms set forth herein.

212. Pursuant to 17 U.S.C. §802(C), the Panel further determines that the entire cost of this arbitration proceeding shall be borne equally by the respective sides, the Recording Industry Association of America on the one side and the Subscription Services (DCR, DMX, and Muzak) on the other.

IV. CERTIFICATION BY CHAIR

Pursuant to 37 CFR §251.53(b), on this 12th day of November, 1997, the Panel Chair hereby certifies the Panel's determinations contained herein.

Lenore G. Ehrig

Honorable Lenore G. Ehrig
Chair

Thomas Fortkort

Honorable Thomas A. Fortkort

Sharon T. Nelson

Honorable Sharon T. Nelson

Jaffe Rebuttal Exh.5

Copyright Board Canada | Commission du droit d'auteur Canada

CANADA

FILE: **Public Performance** of Sound Recordings **1998-2002**	DOSSIER : **Exécution** pubtique **d'enregistrements sonores 1998-2002**
Public **Performance** of**Sound** Recordings	**Exécution publique d'enregistrements sonores**
Copyright Act. section 68(3)	*Loi sur le droit* d'auteur. article 68(3)
STATEMENT OF *ROYALTIES* TO BE COLLECTED BY NRCC FOR *THE* PUBLIC PERFORMANCE OR THE COMMUNICATION TO THE PUBLIC BY TELECOMMUNICATION. IN *CANADA*. OF PUBLISHED SOUND RECORDINGS EMBODYING MUSICAL WORKS AND PERFORMER'S PERFORMANCES OF SUCH WORKS	TARIF DES REDEVANCES À PERCEVOIR PAR LA SCGDV *POUR* L'EXÉCUTION EN PUBLIC OU LA COMMUNICATION AU PUBLIC PAR TÉLÉCOMMUNICATION. AU CANADA. D'ENREGISTREMENTS SONORES PUBLIÉS CONSTITUÉS D'ŒUVRES MUSICALES ET DE LA PRESTATION DE TELLES ŒUVRES
[TARIFF 1.A - *COMMERCIAL* RADIO IN 1998. 1999, 2000, 2001 AND 2002]	[TARIF 1.A - RADIO COMMERCIALE EN 1998. 1999. 2000. 2001 ET 2002]
DECISION OF THE BOARD	**DÉCISION DE LA COMMISSION**
Reasons *delivered by:*	*Motifs exprimés par* :
Michel Hétu. Q.C. Mrs. Adrian Burns Mr. Andrew E. Fenus	Michel Hétu, c.r. M^me^ Adrian Burns M. Andrew E. Fenus
Date of the Decision	*Date de la décision*
August 13. 1999	Le 13 août 1999

Ottawa, August 13, 1999

File: Public Performance of Sound Recordings 1998-2002

Public Performance of Sound Recordings

Reasons for the decision *certifying* NRCC Tariff 1.A (Commercial Radio) for the years 1998 to 2002

I. INTRODUCTION

Pursuant to section 67 of the Copyright *Act* [the *Act*] and section 53.1 of the *Act to amend the Copyright Act* [S.C. 1997, ch. 24], the Neighbouring Rights Collective of Canada (NRCC) and the *Société de gestion des droits des artistes-musiciens* (SOGEDAM) filed with the Board on or before September 1, 1997, statements of proposed royalties for the public performance, or the communication to the public by telecommunication in Canada, of performer's performances of musical works, or of sound recordings embodying such performer's performances, with an effective date of January 1, 1998. The statements were published in the *Canada Gazette* on October 18, 1997. At the same time, the Board gave notice to users of their right to file objections to the proposed tariffs.

The following are the Board's reasons dealing with Tariff 1.A (Commercial Radio). Other tariffs will be disposed of later.

The Canadian Association of Broadcasters (CAB), Shaw Radio Limited and Radiomutuel Inc. filed timely objections to Tariff 1.A. Shaw eventually withdrew its objection whereas Radiomutuel informed the Board it would be represented by CAB. Hearings took place over 16 days in June, July and August 1998. Participants filed their final arguments on November 16, 1998.

Ottawa, le 13 août 1999

Dossier : Exécution publique d'enregistrements sonores 1998-2002

Exécution publique d'enregistrements sonores

Motifs de la décision homologuant le tarif 1.A (Radio commerciale) de la SCGDV pour les années 1998 à 2002

I. INTRODUCTION

Au 1er septembre 1997, conformément à l'article 67 de la *Loi sur le droit d'auteur* [la *Loi*] et à l'article 53.1 de la *Loi modifiant la Loi sur le droit d'auteur* [L.C. 1997, ch. 24], la Société canadienne de gestion des droits voisins (SCGDV) et la Société de gestion des droits des artistes-musiciens (SOGEDAM) déposaient auprès de la Commission des projets de tarifs pour l'exécution publique ou la communication au public par télécommunication au Canada de prestations d'œuvres musicales ou d'enregistrements sonores constitués de ces prestations, tarifs qu'elles entendaient percevoir à partir du 1er janvier 1998. Ces projets ont été publiés dans la *Gazette du Canada* le 18 octobre 1997. Par la même occasion, la Commission avisait les utilisateurs de leur droit de s'opposer aux projets de tarifs.

Les présents motifs traitent du tarif 1.A (Radio commerciale). Les autres tarifs feront l'objet de décisions ultérieures.

L'Association canadienne des radiodiffuseurs (ACR), Shaw Radio Limited et Radiomutuel Inc. se sont opposées dans les délais prescrits. Shaw a éventuellement retiré son opposition alors que Radiomutuel informait la Commission qu'elle serait représentée par l'ACR. Les audiences, qui ont duré 16 jours, ont été tenues en juin, juillet et août 1998. Le dépôt de l'argumentation finale a pris fin le 16 novembre 1998.

II. LEGISLATIVE FRAMEWORK

This is the first time the Board is called upon to deal with the so-called neighbouring rights regime set up in 1997. when Bill C-32 [now S.C. 1997. ch. 24] came into force. Consequently. it would be appropriate to outline the legislative evolution of the protection afforded to performers and makers of sound recordings under Canadian copyright legislation as well as some of the essential elements of the new regime.

Makers of sound recordings have long enjoyed the exclusive right to authorize their reproduction. They also enjoyed the right to authorize their public performance until 1971. They lost that right shortly after the Copyright Appeal Board certified a number of tariffs for such performances. In 1994. as a result of the North American Free Trade Agreement, makers were granted the exclusive right to rent their sound recordings.

Performers have until recently enjoyed little, if any rights under Canadian copyright legislation. Only in 1994 did legislation implementing some of Canada's obligations resulting from its adhesion to the World Trade Organization grant performers certain exclusive rights over their live performances.

The adoption of Bill C-32 allowed Canada to become a party to the Rome *Convention of 1961 for the Protection of Performers, Producers of Phonograms* and Broadcasting Organizations. On June 4, 1998, Canada joined 56 other countries. The United States is not a party to the Rome Convention.

New and pre-existing rights of performers. makers of sound recordings and broadcasters are all addressed in Part II of the *Act*. Sections 15. 18, 21 and 26 now describe the exclusive rights they enjoy, all of which are included in the definition of 'copyright" which is introduced in the *Act* for the first time. Section 19 also *grants* to

II. LE CADRE LÉGISLATIF

C'est la premiere fois que la Commission se penche sur le régime dit des droits voisins. mis en place en 1997 par l'entrée en vigueur du projet de loi C-32 [L.C.1997. ch. 24]. Il paraît donc utile de faire un survol de l'évolution de la protection que le droit d'auteur canadien accordait jusque-là aux artistes-interprètes et aux producteurs d'enregistrements sonores et de décrire les elements essentiels du nouveau régime.

Les producteurs d'enregistrements sonores ont acquis depuis longtemps le droit exclusif d'autoriser la reproduction de ces enregistrements. Jusqu'en 1971. ils jouissaient aussi du droit d'autoriser leur exécution publique. droit qu'ils ont perdu peu après que la Commission d'appel du droit d'auteur ait homologue des tarifs à cet effet. En 1994. dans le cadre de la mise en application de l'Accord de libre-échange nord-américain, les producteurs d'enregistrements obtenaient le droit exclusif de les louer.

Jusqu'à tout récemment. la legislation canadienne en matière de droit d'auteur accordait peu ou pas de droits aux artistes-interprets. Ce n'est qu'en 1994 que la loi de mise en application de certaines obligations du Canada découlant de son adhésion a l'Organisation mondiale du commerce leur a octroyé certains droits exclusifs sur leurs prestations en direct.

L'adoption du projet de loi C-32 a permis au Canada d'adhérer à la *Convention* de Rome de 1961 *pour la protection des artistes-interprètes, des producteurs de phonogrammes et des organismes de radiodiffusion*. Le 4 juin 1998, le Canada rejoignait 56 autres pays. Les États-Unis n'ont pas adhéré à cette Convention.

Tous les droits dont jouissent les artistes-interprètes, producteurs d'enregistrements sonores et radiodiffuseurs se retrouvent maintenant a la Partie II de la *Loi*. Les articles 15. 18. 21 et 26 prévoient divers droits exclusifs. tous qualifiés de droit d'auteur selon la definition de l'expression nouvellement ajoutée a la *Loi*. L'article 19 maken and performers a right of equitable remuneration for the public performance and communication to the public by telecommunication of eligible published sound recordings. This new right has several characteristics. some of which have a direct effect on this decision.

First, the right benefits jointly makers and performen of eligible sound recordings. [s. 19(1)]

Second, a recording is eligible not **only** if the maker **was.** at the date of the first fixation, a citizen or permanent resident of Canada or a Rome Convention country. but also if all the fixations done for the sound recording occurred in Canada or a Rome Convention country. [s. 20(1)] As a result. performers and makers who are not citizens or permanent residents of Canada or a Rome Convention country may be entitled *to* remuneration.

Third, the manner in which royalties are collected varies according to the nature of the underlying work. In the case of recorded music. users pay royalties to the collective society authorized under Part VII to collect them. In *the* case of recorded literary or dramatic works, users pay royalties to either the maker or the performer. [s. 19(2)]

Fourth. once they have been paid. royalties are always divided equally between the maker or maken and the performer or performers. irrespective of who received the payment. [s. 19(3)]

Fifth. even though performers and *makers* are entitled to an equal share of the remuneration, what triggers *the* remuneration is the performance or telecommunication of the *maker's* recording. [s. 19(1) *in limine]*

accorde par ailleurs aux productem et artistes-interprètes un droit a rémunération équitable pour l'exécution en public ou la communication au public par télécommunication d'enregistrements sonores admissible, publib. Certaines des nombreuses caractéristiques de ce droit ont un impact direct sur la présente décision.

Premièrement, le **droit** bénéficie conjointement aux producteurs et artistes-interprètes d'enregistrements admissibles. [a. 19(1)]

Deuxièmement, l'enregistrement *est* admissible non seulement **si** le producteur. a la date de la première fixation, était citoyen canadien ou résident permanent du Canada ou d'un pays partie a la Convention de Rome. mais aussi si touts les fixations réalisées en vue de la confection de l'enregistrement sonore ont eu lieu **dans l'un** de ces pays. [a. 20(1)] Il s'ensuit que les artistes-interprètes et productem qui ne sont pas citoyens ou résidents permanents d'un de ces pays peuvent avoir droit a la remuneration.

Troisiemement, la facon dont les redevances sont perçues varie en fonction de **la nature** de l'œuvre enregistrée. Pour les enregistrements d'œuvres musicales, le paiement se fait a la societe de gestion chargée, en vertu de la partie VII, de les percevoir. Pour les enregistrements d'œuvres littéraires ou dramatiques, le versement se fait soit au producteur. soit a l'artiste-interprète. [a. 19(2)]

Quatrièmement, les redevances. une fois versées, sont partagées par moitié entre le producteur et l'artiste-interprète, sans égard a celui qui a reçu le paiement. [a. 19(3)]

Cinquièmement bien que les artistes-interprets et les productem aient droit a une part **égale** de la rémunération, c'est l'exécution ou la télécommunication de l'enregistrement appartenant au producteur qui donne lieu a cene rémunération. [a. 19(1)]

Finally. in the case of sound recordings of musical works. the right to remuneration must be exercised through a collective society. [ss. 19(2)(*a*). 67.1(1). 67.1(4)(*b*)] Societies are subject to the rate regulation regime already in place for the performance or telecommunication of musical works. All must answer information requests about their repertoire. All must file proposed tariffs or lose their right to sue for payment of royalties without the written consent of the Minister. All tariffs are subject to essentially the same examination and certification process.

Enfii. l'exercice du droit a remuneration pow les enregistrements d'œuvres musicales s'exerce nécessairement par le truchement d'une societe de gestion. (aa. 19(2)(a). 67.1(1). 67.1(4)(*b*)] Ces sociétés sont assujetties au régime de réglementation tarifaire deja en place pour les sociétés qui gerent le droit d'exécution et de télécommunication d'œuvres musicales. Toutes doivent repondre aux demands de renseignements concernant leun répertoires. Toutes doivent déposer des projets de tarifs ou voir leur recours en recouvrement des redevances dépendre de la permission écrite du ministre. Enfii. le même processus d'examen et d'homologation s'applique pour l'essentiel a tous ces tarifs.

A few differences exist. The *Act* sets out three limits on the Board's power to decide the amount and terms of the royalties to be paid on account of the remuneration right.' The tariff must apply only in respect of eligible recordings. It must not put certain users that are subject to different linguistic and content requirements as a result of Canada's broadcasting policy at a financial disadvantage. Finally. it must provide for the payment of royalties in a single payment.

Certaines différences subsistent. Dans le cas du droit a remuneration. le pouvoir de la Commission d'etablir le montant des redevances et leurs modalités s'accompagne de trois conditions.[1] Le tarif homologue ne doit s'appliquer qu'aux enregistrements admissibles. Il ne doit pas désavantager sur le plan financier certains utilisateurs en raison d'exigences différentes concernant la langue et le contenu imposées par le cadre de la politique canadienne de radiodiffusion. Enfin. il doit prévoir que le paiement des redevances soit fait en un versement unique.

The *Act* also sets out special conditions that apply to radio stations or 'wireless transmission systems' notwithstanding the tariffs approved by the Board. Community systems pay only $100 a year. Systems other than community systems and public transmission systems pay only $100 on their first 1.25 million dollars of annual advertising revenues. All other royalties are to be phased in, with systems paying one-third of the royalties set out in *the* approved tariff in 1998. two-thirds in 1999 and *the* full amount in 2000 and thereafter. [s. 68.1(1)]

La *Loi* prévoit par ailleurs certaines conditions spéciales s'appliquant par derogation aux tarifs homologués par la Commission aux «systèmes de transmission par ondes radioélectriques» (les stations de radio). Les systèmes communautaires ne payent que 100 $ par année. Les systèmes autres que les systèmes communautaires ou les systèmes de transmission publics ne payent que 100 $ sur la partie de leurs recettes publicitaires annuelles qui ne dépasse pas 1.25 million de dollars. Autrement. les redevances sont soumises a un régime transitoire au coun des trois premieres années. aux terms duquel un tiers est payable en 1998. les deux tiers en 1999 et la totalite par la suite. [a. 68.1(1)]

Finally, the *Act* provides for the adoption of a number of regulatory definitions. The Board can

La *Loi* prévoit enfin l'adoption de définitions réglementaires. La Commission peut définir define "advemsing revenues",[2] while the Governor in Council may define "community system", 'public transmission system" and "wireless transmission system".[3]

l'expression «recettes publicitaires»,[2] et le gouverneur en conseil, les expressions «système communautaire», «système de transmission par ondes radioélectriques» et «système de transmission public».[3]

Other characteristics of the remuneration right which do not have a direct impact on this decision include the following. Fint. *the* remuneration right is not a copyright as defined in the *Act*. Consequently, a person who violates the right does not infringe copyright. Second, the Minister may limit the scope and duration of the protection granted to sound recordings of Rome Convention countries who do not grant rights similar to those afforded in section 19 of the Act. This was done on March 23. 1999.[4] However, the practical impact of the statement on *the* size of the repenoire actually used by commercial radio stations is negligible. Third, the Minister may also grant the right to remuneration to the performers and makers of sound recordings of a country other than a Rome Convention country if that country grants Canadian performers and makers of sound recordings rights substantially equivalent to those conferred by Canadian legislation. [s. 22] However, this has not been done yet.

Le droit a rémunération compone d'autres caractéristiques qui n'ont pas d'impact sur la présente décision. Premierement, il ne s'agit pas d'un droit d'auteur au sens ou la *Loi* l'entend. Par conséquent, y contrevenir ne viole pas le droit d'auteur. Deuxièmement, le ministre peut limiter l'etendue et la durée de la protection accordée aux enregistrements confectionnés dans les pays parties a la Convention de Rome qui n'accordent pas de droits semblables a ceux prévus a l'article 19 de la *Loi*. Une déclaration a cet effet a été émise le 23 mars 1999.[4] En pratique, cene déclaration ne diminue en rien l'étendue du repertoire admissible qu'utilisent les stations de radio commerciale. Troisiemement, le ministre peut aussi accorder le droit a rémunération aux artistes-interprets et producteurs d'un pays autre qu'un pays partie a la Convention de Rome qui accorde aux artistes-interprètes et producteurs canadiens essentiellement les mêmes avantages que ceux conférés par la legislation canadienne. [a. 22] A ce jour, le ministre n'a pas émis de déclaration a cet effet.

III. THE PARTICIPANTS' CONCLUSIONS

III. LES CONCLUSIONS RECHERCHÉES

The details of the participants' arguments are outlined in the relevant parts of the decision. In a nutshell, their conclusions are as follows.

Les pretentions des participants sont reprises en detail lonque nécessaire dans le reste de la décision. Les conclusions qu'ils recherchent peuvent se résumer c o m e suit.

NRCC is asking for a five-year tariff, *to* be phased in over five years instead of the three mandated by the *Act*. In the fifth year, stations would pay from 4.68 per cent for advertising revenues between 1.25 and 1.5 million dollars, to 9.78 per cent on revenues in excess of five million dollars. NRCC agreed to account for low-use stations in the final tariff. It also asked that it be the collective designated for the purposes of collecting all royalties, including royalties for rights holden it may not represent.

La SCGDV demande un tarif valide pour cinq années, entrant en vigueur progressivement sur toute cette période plutôt que celle de trois ans prévue par la *Loi*. La dernière année, les stations verseraient 4.68 pour cent de leun recettes publicitaires entre 1.25 et 1.5 million de dollars, et 9.78 pour cent de leurs recettes audela de cinq millions de dollan. La SCGDV accepte que les stations utilisant peu de musique paient à un taux moindre que les autres. Enfii, elle demande a être la societe de gestion chargée de percevoir touts les redevances, y compris cells revenant a des titulaires qu'elle pourrait ne pas représenter.

SOGEDAM asked for a three-year tariff set at five per cent of advertising revenues. It *argued* that phasing-in provisions in the tariff are unnecessary. since the *Act* already provides for this. It also asked that it be granted 2.88 per cent of total royalties payable under the tariff as compensation for the repertoire it represents.

La SOGEDAM demande que le tarif soit etabli a cinq pour cent des recenes publicitaires pour trois ans. Elle soutient qu'il n'est pas nécessaire d'inclure dans le tarif des dispositions transitoires additionnelles a cells que prevoit la *Loi*. Elle demande enfii de recevoir 2.88 pour cent des redevances pour la rémunération du repertoire qu'elle représente.

CAB asked for a three-year tariff of 0.7 per cent of advertising revenues, a low-use tariff of 0.3 per cent and a flat royalty of $1,000 per year for all-talk stations. It also found no need to add to the statutory phasing-in provisions.

L'ACR demande un tarif d'une durée de trois ans. Elle propose 0,7 pour cent des recettes publicitaires. 0.3 pour cent pour les stations utilisant peu de musique et 1 000 $ l'an pour les stations de radio parlée. Elle ne voit pas non plus la nécessité d'ajouter aux dispositions transitoires de la *Loi*.

IV. GUIDING PRINCIPLES FOR FIXING THE ROYALTIES

IV. PRINCIPES DIRECTEURS

The Board finds it useful to outline at the outset the principles that it intends to keep in mind in reaching its decision. Some have already been stated elsewhere: others flow from the terms of the *Act*. They will be fleshed out as required in the rest of the decision.

La Commission voit utile d'énoncer dès le depart les principes dont elle entend s'inspirer pour rendre sa décision. Certains sont déjà connus; d'autres s'imposent a la lecture de la *Loi*. Lorsque nécessaire, ils feront l'objet de commentaires additionnels dans le reste de la présente décision.

The *Act* requires that the Board take into account the following principles. First, the royalties must satisfy the performers' and makers' right to equitable remuneration as set out in subsection 19(1) of the *Act*. Second, the tariff must address only the use of the properly represented eligible repertoire. Third, the tariff must not place some users at a greater financial disadvantage than others because of different linguistic and content requirements of the *Broadcasting Act*. Finally, the tariff must provide that the payment of royalties by users is made in a single payment.

La *Loi* exige que la Commission tienne compte des principes suivants. Les redevances doivent représenter la rémunération a laquelle les artistes-interprets et productem ont droit en vertu du paragraphe 19(1) de la *Loi*. Le tarif doit compenser uniquement l'utilisation du répertoire admissible dûment représenté. Il ne doit pas désavantager sur le plan financier certains utilisateun en raison d'exigences différentes découlant de la *Loi sur la radiodiffusion* en matière de langue ou de contenu. Il doit prévoir que le paiement des redevances soit fait en un versement unique.

The Board also intends to rely on other principles already expressed in previous decisions. Thus, the tariff should reflect Canadian circumstances. It should be simple to administer, transparent and comprehensible. It should be based on a set of statistics for a test period.

La Commission entend aussi se fonder sur certains principes énoncés dans ses décisions antérieures. Par conséquent, le tarif devrait refléter la situation canadienne. itre facile a appliquer. a administrer et a comprendre. et être fonde sur un ensemble de données pour une période témoin.

The Board adds that by its nature, the tariff is prospective. Only by looking at the past can the Board determine the extent of the eligible repenoire or the use made of it by commercial radio stations. Should major changes occur during the life of the tariff. collectives and users are free to ask that the tariff be varied pursuant to section 66.52 of the *Act.*

La Commission ajoute que. de par sa nature, le tarif est prospectif. Par conséquent, c'est en jetant un regard sur le passé qu'elle peut etablir l'etendue du repertoire admissible ou l'usage qu'en font les stations de radio commerciale. Si des changements significatifs devaient survenir pendant la durée du tarif. l'article 66.52 de la *Loi* permet aux societb ou aux utilisateurs de demander la modification du tarif.

V. THE ISSUES

The major issues the Board needs to address in order to reach a decision in this matter *can* be reduced to the following:

- What is meant by 'equitable remuneration"?
- What is the properly represented eligible repertoire and what use do commercial radio stations make of it?
- What account should be taken of the Canadian broadcasting policy?
- How much should radio stations pay for their use of the properly represented eligible repertoire?
- How should royalties be allocated?

V. LES QUESTIONS EN LITIGE

Les principales questions auxquelles la Commission doit repondre afin de rendre sa décision dans la présente affaire se résument comme suit :

- Qu'entend-on par «rémunération équitable»?
- En quoi consiste le repertoire admissible dûment représenté et quel usage les stations de radio commemale en font-elles?
- Comment faut-il tenir compte de la politique canadienne en matiere de radiodiffusion?
- Combien les stations de radio devraient-elles payer pour l'usage qu'elles font du repertoire admissible dûment représenté?
- Comment les redevances devraient-elles être réparties?

A. What is meant by "equitable" remuneration?

Participants attempted to interpret the notion of equitable remuneration in various ways. For NRCC, *the* level of remuneration should be determined by focussing solely on the entitlements of rights holders. For its part, CAB insists that equitable remuneration ought to also take into account fairness *to* users as well as a number of other factors including certainty as to the remunerated repertoire and the benefits rights holders derive from the use of eligible sound recordings. In the end, the Board's task is no different here than it is, and has always been, in other rate regulation regimes. Therefore, setting

A. Qu'entend-on par «rémunération équitable»?

Les participants abordent le concept de rémunération équitable de diverses façons. La SCGDV soutient qu'il faut l'établir uniquement en fonction des droits des titulaires. L'ACR prétend que cene rémunération doit aussi être équitable à l'endroit des utilisateurs, en plus de refléter d'autres elements, tels l'identification précise du répertoire rémunéré et le bénéfice que *tirent* les titulaires de l'utilisation même des enregistrements. En bout de piste, la tâche qui incombe a la Commission demeure celle qui a toujours *ete* la sienne en matiere de réglementation des tarifs, a savoir : etablir un tarif qui soit juste an equitable remuneration requires a tariffthat is fair and equitable to both rights holden and users. given all the circumstances of the case.

B. What is the properly represented eligible repertoire and what use do commercial radio stations make of it?

The right to remuneration attaching to sound recordings of musical works is contingent on the recording being eligible. Essentially, this requires that the recording be published, qualify under section 20 of the *Acr* and be less than 50 years old. That right is also contingent on eligible recordings being parr of the repertoire of a collective society that has filed for a tariff.

As a result, it is incumbent on the collectives who claim royalties for the use of sound recordings to show that they do represent the repertoire they claim. The need to establish which recordings are eligible and which are not is made all the more important by the fact that almost all American recordings, which represent an important proportion of music played on radio, are not eligible. This does not mean that collectives actually bear the burden of making a case for each and every title they claim: they are clearly entitled to remuneration once they have established that they do represent those they say they do.

The determination of which recordings are before the Board requires an answer to two questions. Are NRCC and SOGEDAM collective societies? Do they represent *those* they say they represent? It will then be necessary to determine the extent to which commercial radio stations use the eligible repertoire.

1. Are NRCC and SOGEDAM collective societies?

NRCC is a collective of collectives. Its membership is limited to organisations and

et équitable tant pour les titulaires de droits que pour les utilisateun. compte tenu de toutes les circonstances de l'espèce.

B. En quoi consiste le répertoire admissible dûment représenté et quel usage les stations de radio commerciale en font-elles?

Seul l'enregistrement admissible emporte le droit a rémunération. Pour l'essentiel, cela veut dire qu'il doit avoir ete publié, remplir les conditions énumérées a l'article 20 de la *Loi* et remonter a moins de 50 ans. Le droit a rémunération de l'enregistrement d'une œuvre musicale suppose par ailleurs que l'enregistrement admissible fasse partie du repertoire d'une societe de gestion ayant déposé un projet de tarif.

Par conséquent, il incombe aux sociétés qui réclament des redevances pour l'utilisation de tels enregistrements de demontrer qu'elles représentent effectivement le repertoire dont elles se réclament. Le fait que les enregistrements sonores américains, si répandus a la radio, ne soient pas admissibles. ne fait qu'ajouter a l'importance de bien distinguer ce qui est admissible de ce qui ne l'est pas. Cela ne veut pas dire pour autant que les sociétés aient le fardeau d'etablir la titularite de chacun des titres faisant partie de leurs repertoires : leur droit a rémunération est etabli dès lors qu'elles représentent dûment les titulaires dont elles se réclament.

Établir quels enregistrements se retrouvent devant la Commission exige de répondre a deux questions. La SCGDV et la *SOGEDAM* sont-elles des sociétés de gestion? Représentent-elles les titulaires dont elles se réclament? Il faudra ensuite determiner l'usage que les stations de radio commerciale font du répertoire admissible.

1. La SCGDV et la SOGEDAM sont-elles des sociétés de gestion?

La SCGDV est une societe de gestion qui en regroupe d'autres. Peuvent en devenir membre collectives that represent a significant number of holden of remuneration rights. It was constituted to collect the monies owing to those entitled to neighbouring rights payments. It acts on behalf of five sub-collectives: ACTRA Performers' Rights Society (APRS) .the American Federation of Musicians (AFM). the *Société de gestion collective de l'Union des artistes* (ArtistI). AVLA Audio-Video Licensing Agency Inc. (AVLA) and the *Societe de gestion collective des droits des producteurs de phonogrammes et de vidéogrammes du Quebec* (SOPROQ).

SOGEDAM is a more traditional collective whose repenoire flows from two sources. It represents a small number of Canadian recording musicians who have authorized it to act for them by way of assignment. Most importantly. SOGEDAM has signed a reciprocal representation agreement with SPEDIDAM. the collective society empowered under French law to represent the rights of all perfonen whose names do not appear in the credits accompanying a sound recording.[5]

There is no doubt *that* NRCC and SOGEDAM are collective societies. Their objects are clearly those outlined in the definition of this term as set out in the *Act*. Moreover, and contrary to what CAB seemed to assert. the fact that some of NRCC's sub-collectives may not be corporate entities is a non issue. The *Act* clearly contemplates the possibility of an unincorporated association acting as a collective. Such an d a t i o n can, through agency rules. secure remuneration rights and pass them on to another person to collect them. as long as the conditions imposed by *statutes* or private law for such transfers are met.

The real issue is the extent, if any, to which NRCC and SOGEDAM represent the eligible repertoire. This in turn *requires* looking at the status of NRCC's own "sub-collectives".

uniquement les organisations et sociétés représentant un nombre important de titulaires du droit a remuneration. Créée pour percevoir les redevances awquelles les titulaires de droits voisins ont droit, elle agit pour le compte de cinq sociétés membres : *l'ACTRA Performers' Rights Society* (APRS), l'*American Federation* of *Musicians* (AFM). la Societe de gestion collective de l'Union des artistes (ArtistI). l'*AVLA Audio-Video Licensing Agency Inc.* (AVLA) et la Societe de gestion collective des droits des productem de phonogrammes et de vidéogrammes du Quebec (SOPROQ).

La SOGEDAM est une societe de type plus traditionnel, dont le repertoire provient de deux sources. Elle représente un petit nombre de musiciens canadiens qui l'ont autorisée par voie de cession. Elle a surtout signé une entente de réciprocité avec la SPEDIDAM. societe de gestion a laquelle la loi française confie la gestion des droits de tous les artistes-interprets dont le nom n'est pas mentionné dans la documentation accompagnant l'enregistrement sonore.[5]

Il ne fait aucun doute que la SCGDV et la SOGEDAM sont des societb de gestion. Leurs objets sont clairement ceux qu'énonce la *Loi*. Qui plus *est*. et contrairement a ce que semble prétendre I'ACR. le fait que certaines des societb membres de la SCGDV ne soient pas des penonnes modes n'est aucunement pertinent. La *Loi* permet clairement qu'une association non constituée en corporation agisse a titre de societe de gestion. Les règles du mandat permettent a une telle association d'obtenir la gestion du droit à rémunération et d'en confier la perception a d'autres personnes. pour autant que l'instrument par lequel le mandat est accord6 respecte les conditions prévues par la législation ou le droit privé.

La vraie difficulté *est* d'etablir l'etendue du répertoire admissible que représentent la SCGDV et la SOGEDAM. Cela exige d'examiner le *statut* des sociétés membres de la SCGDV.

2. Do NRCC and SOGEDAM represent the rights holden they claim to represent?

As stated earlier. it is incumbent on the collectives who claim royalties for the use of sound recordings to show that they do represent the repenoire they claim. CAB argues that both collectives have fallen short in this respect. It maintains that NRCC failed to establish that it represents any Canadian performers as well as any non-Canadian rights holden. It also argues that SOGEDAM failed to demonstrate the extent to which it represents any repertoire actually played by Canadian commercial radio stations. Consequently, CAB claims that the repertoire properly before the Board, consisting only of the Canadian makers' share of the remuneration right. represents only 15 per cent of all sound recordings played by radio stations, or half the 30 per cent Canadian content requirement currently imposed by the CRTC on commercial radio stations.

CAB's challenge focussed on *NRCC's* entitlement to represent Canadian as well as foreign performers: the former, because of the instrument used by AFM and APRS to acquire the rights. and the latter, because NRCC (through ArtistI) had not yet entered into reciprocal agreements with foreign societies.

There is little doubt *that SOGEDAM* administers the repenoire it says it does. The problem was more with NRCC and the way it claimed to have secured rights.

a. *Makers' rights and NRCC*

According to the uncontradicted testimony of Mn. Lucie Beauchemin. AVLA and SOPROQ represent virtually all Canadian producers. Members of AVLA have signed non-exclusive agency agreements. while members of SOPROQ have authorized it to act for them by way of assignment. In turn. NRCC holds its rights as a result of AVLA and SOPROQ having become members of NRCC.

2. La SCGDV et la SOGEDAM représentent-elles les titulaires dont elles se réclament?

C o m e on l'a dit précédemment. il incombe aux societb qui demandent a recevoir des redevances au titre du droit voisin de démontrer qu'elles représentent effectivement le repertoire dont elles se réclament. L'ACR soutient que ni la SCGDV. ni la SOGEDAM ne se sont acquittées de cette obligation. Elle pretend que la premiere n'a pu etablir sa titularite a l'égard des artistes-interpretes canadiens ou des titulaires de droits étrangers. Elle ajoute que la seconde n'a pu etablir l'usage que les stations de radio commerciale font effectivement du répertoire qu'elle représente. L'ACR en conclut que le seul repertoire dont la Commission soit réellement saisie est la part du droit a rémunération revenant aux producteurs canadiens. qui ne représente que 15 pour cent des enregistrements utilisés par les stations de radio commerciale. compte tenu du quota de 30 pour cent de contenu canadien imposé par le CRTC.

Ce que l'ACR conteste d'abord et avant tout c'est le droit de la SCGDV d'agir au nom des artistes-interprets canadiens et étrangers : pour les premiers, elle met en cause les moyens utilisés par l'AFM et l'APRS pour obtenir les droits, et pour les seconds, elle invoque le fait que la SCGDV (par le biais d'ArtistI) n'a toujours pas conch d'accords de réciprocité avec les sociétés étrangères agissant pour leur compte.

Il ne fait aucun doute que la SOGEDAM représente le répertoire dont elle se réclame. C'est plutdt la façon dont la SCGDV pretend avoir acquis certains h i t s qui pose problème.

a. *Les droits des productem et la SCGDV*

Le témoignage non contredit de madame Lucie Beauchemin démontre que l'AVLA et la SOPROQ représentent a touts fins pratiques l'ensemble des productem canadiens. Les membres de l'AVLA lui ont confié des mandats non exclusifs. alors que ceux de la SOPROQ l'ont autorisée par voie de cession. A son tour. la SCGDV détient les droits dont l'AVLA et la SOPROQ ont fait apport en devenant membres de celle-ci.

The uncontradicted testimony of several witnesses also establishes that Canadian producers bring to their collectives not only the rights to their own recordings, but also those to most foreign recordings. Most if not all foreign masters reach the Canadian market through Canadian producers, who exploit these records in Canada. Canadian independent producers enter into licencing agreements with foreign producers, while the repertoire of the six "majors" is represented in Canada through intercorporate agreements between Canadian and foreign affiliates. There may be a few foreign producers who are not represented according to either model. In their case. NRCC or its members must enter into agreements with foreign collective societies if they intend to represent them in Canada. However, the evidence in these proceedings. and especially NRCC's music use study (NRCC-21), confirms that the unrepresented repenoire represents no more than five per cent (and probably less) of the eligible repertoire.

Le témoignage non contredit de plusieurs témoins permet aussi de condure que les productem canadiens font appon non seulement des droits qu'ils détiennent sur leurs propres enregistrements. mais aussi de ceux qu'ils detiennent sur la plupan des enregistrements étrangers. Ce sont eux qui acquierent la totalite ou presque des bandes-maîtresses étrangères pour le marché canadlen et qui les exploitent dans ce marché. Les productem independants canadiens detiennent des licences que leur octroient les productem etrangen. Quant au répertoire des six societb les plus importantes (les *majors)*, il fait l'objet d'ententes inter-corporatives entre filiales canadiennes et étrangères. Il reste sans doute certains producteurs étrangers qui ne sont pas représentés au Canada ni d'une façon, ni de l'autre. En ce qui les concerne, la SCGDV ou ses membres devront s'entendre avec des sociétés de gestion étrangères avant de représenter ces productem au Canada. La preuve. particulièrement l'etude déposée sous la cote NRCC-21, permet toutefois de conclure que cette portion du répertoire représente tout au plus cinq pour cent du répertoire admissible.

It is safe to assume, therefore. that NRCC brings with it to these proceedings almost all of the makers' rights pursuant to section 19 of the *Act*. The situation is far from that simple. however, with respect to performers' rights.

Pour les fins de la présente affaire, on peut donc tenir pour acquis sans risque de se tromper que la SCGDV detient la quasi-totalité des droits dont jouissent les productem en vertu de l'article 19 de la *Loi*. La situation est loin d'être aussi simple a l'égard des droits des artistes-interprètes.

b. Performers' *rights and NRCC*

b. *Les h i t s des artistes-interprètes et la SCGDV*

NRCC has in its repertoire what its members and affiliates have authorized it to manage by way of assignment, grant of licence. appointment as agent or otherwise. Its members and affiliates must themselves have *secured* the rights from the makers or performers through similar means. Put another way, *AFM*. APRS and ArtistI can bring to NRCC the rights of their members only if they have secured from them valid authorizations within the meaning of the *Act*. Therefore, it is necessary to look at how they claim to have brought these rights into their repertoires.

La SCGDV gère ce que ses sociétés membres et associées l'ont autorisée a gérer «notamment par voie de cession, licence ou mandat». Ces dernières doivent elles-mêmes avoir obtenu des droits des productem et artistes-interpretes de la même façon. Autrement dit, l'AFM. l'APRS et ArtistI peuvent faire appon a la SCGDV des droits de leurs membres uniquement si elles-mèmes ont obtenu des autorisations valides au sens ou l'entend la *Loi*. Il faut donc se pencher sur la facon dont elles prétendent avoir obtenu ces droits pour leurs répertoires respectifs.

ArtistI was set up by the *Union des artistes* (UDA), which represents mostly French speaking performers, with a view to managing the rights of its singer members. Only it has systematically secured assignments of the remuneration right from the performers it represents.

AFM can claim as members a very large share of Canadian performing musicians. It purports to bring its members' remuneration rights as a result of amendments to its by-law, intended to give it the power to manage the remuneration right and to acquire such rights from its members. Article 12, which deals with the rights and duties of members, now provides in its paragraph 20(c), that "The Federation is authorized to act as the representative of musicians for the purpose of collecting and distributing government mandated or other compulsory royalties or remuneration payable to musicians under the laws of the United States, Canada and other countries." Everyone who applies for membership agrees to be bound by the by-laws as they may exist from time to time. AFM argues that this commitment constitutes sufficient authority for it to manage the remuneration right, without having to secure individual contracts of assignment or agency.

ACTRA is an association representing English speaking actors and performers. Its 'filiate', APRS, relies on three amendments to its 'parent's' by-law as foundation for its right to claim status as a collective. The ACTRA membership application form now contains a provision similar to that found in the AFM membership application, whereby the applicant agrees to comply with the by-law and membership agreements as they may read from time to time. The Form also contains a clause purporting to irrevocably assign the remuneration right to ACTRA Performers Guild *(APG)* and to its collective society, APRS. Finally, the amending by-law states that "Every current Guild member, as a condition of continued membership,

ArtistI a été créée par l'Union des *artistes* (UDA), qui représente surtout des artistes-interprètes francophones, dans le but de gérer les droits de ses membres qui sont des chanteurs. Elle seule a obtenu systématiquement des cessions du droit à rémunération de la part des artistes-interprètes qu'elle représente.

Sont membres de l'AFM la presque totalité des musiciens canadiens. L'AFM soutient que des modifications apportées à ses règlements administratifs visant l'acquisition et la gestion du droit à rémunération de ses membres lui permettent de faire apport de ces droits. L'article 12, qui traite des droits et obligations des membres, prévoit maintenant à son paragraphe 20(c), que [TRADUCTION] «La fédération est autorisée à agir à titre de représentante des musiciens aux fins de percevoir et de distribuer les redevances et droits à rémunération obligatoires, y compris ceux qui sont imposés par un gouvernement, que détiennent les musiciens en vertu des lois des États-Unis, du Canada ou d'autres pays.» Quiconque demande à en devenir membre consent par ailleurs à se conformer aux règlements administratifs tels que libellés ou tels qu'ils pourraient l'être à l'avenir. L'AFM prétend que cet engagement lui permet de faire apport du droit à rémunération sans qu'elle ait besoin de conclure des ententes individuelles de mandat ou de cession avec ses membres.

L'ACTRA représente les artistes-interprètes de langue anglaise. Sa «filiale», l'APRS, dit fonder son statut de société de gestion sur trois modifications aux règlements administratifs de sa «société mère». Le formulaire d'adhésion à l'ACTRA contient désormais une disposition semblable à celle qu'on retrouve dans celui de l'AFM en ce qui concerne l'obligation de se conformer aux règlements administratifs tels que libellés ou tels qu'ils pourraient l'être à l'avenir. Le formulaire comporte par ailleurs une disposition qui vise à céder à titre irrévocable le droit à rémunération à l'*ACTRA Performers Guild (APG)* et à sa société de gestion, l'APRS. Enfin, les règlements administratifs modifiés stipulent que [TRADUCTION] «Tout membre actuel de la shall be deemed to have executed the Application form as amended ... or as otherwise amended from time to time.' Contrary to AFM. APRS has sought (and in some cases, obtained) exclusive and irrevocable five-year agency contracts from its members.[6]

guilde qui entend le demeurer est repute avoir signé le formulaire d'adhésion tel qu'il a été modifié par le présent reglement. ou tel qu'il pourrait être libellé a l'avenir.» Contrairement a l'AFM. l'APRS a demande et dans certains cas, obtenu des mandats exclusifs et irrévocables de cinq ans de la part de ses membres.[6]

For the following reasons. *NRCC's* title is deficient with respect to most of the purported repertoires of APRS and AFM.

Pour les raisons qui suivent. la Commission conclut que la SCGDV ne représente pas la plus grande partie du repertoire dont se réclament l'APRS et l'AFM.

Purported acquisition of performers' rights through by-laws does not constitute authorization by way of assignment or grant of licence, given that some of the conditions set out by the *Act.* notably at paragraph 13(4), have not been met.

La prétendue acquisition des droits des artistes-interprets *par* le biais de reglements administratifs ne constitue pas une autorisation par voie de cession ou licence, certaines des conditions prévues par la *Loi*, entre auues au paragraphe 13(4), n'ayant pas été remplies.

On the other hand. the *Act* sets out no conditions for authorization by way of appointment as one's agent. Therefore. the general conditions of common law and *droit civil* apply and the validity of the appointment will be assessed according to general rules of private law. Having looked at those rules. the Board concludes that purported acquisition of performers' rights through by-laws does not constitute authorization by way of appointment as one's agent.[7]

Par contre. la *Loi* ne prevoit pas de conditions en ce qui concerne l'autorisation accordée par voie de mandat. Il faut donc s'en remettre aux règles générales de droit prive pour etablir s'il y a bien mandat. Après avoir examine ces règles, la Commission en vient a la conclusion que la prétendue acquisition des droits des artistes-interprets par le biais de règlements administratifs ne constitue pas davantage une autorisation par voie de mandat.[7]

The forms of agency that could apply under the circumstances are agency by contract or by ratification. Agency by contract *can* be express, implied, usual or *customary.* There is no express agency where title is claimed through a simple amendment to by-laws. Whether there may be an implied contractual agency will depend on whether managing remuneation rights is necessary for. and ordinarily incidental to carrying out APC's or AFM's express authority according to the usual way in which such authority is executed. This is doubtful, at least as far as those members who have not signed the new application forms: the previous forms contained no allusion to management of performing rights. Finally. there is no usual or customary agency here, since these concepts refer to special rules dealing with either agents in a specific trade.

Les formes de mandat qui pourraient s'appliquer à l'espèce sont le mandat contractuel et le mandat par voie de ratification. Le mandat contractuel peut être exprès, implicite. habituel ou coutumier. Comme les sociétés se réclament uniquement d'une modification à leurs règlements administratifs, il ne peut s'agir d'un mandat exprès. Il y aura mandat contractuel implicite si la gestion du droit à rémunération constitue un accessoire nécessaire aux pouvoirs exprès des sociétés, compte tenu de la façon dont les accords de ce type sont habituellement formulés. Cela est peu probable dans le cas présent, a tout le moins a l'égard des membres qui n'ont pas signé le nouveau formulaire d'adhésion, les formulaires antérieurs ne faisant aucune allusion a la gestion des droits d'exécution. Enfin, il ne peut s'agir de mandat usuel ou coutumier. qui vise le cas ou une profession or business or agency flowing from special rules in a specific marker.

Agency by ratification requires two conditions. First, before ratification occurs, the principal must be aware of all the material facts; assuming that AFM and APRS may have notified their members of their actions through various bulletins, this is hardly satisfactory. Second, the agent must purport to act on behalf of an identified, or identifiable principal and only *that* principal *can ratify* the act. NRCC offered no evidence that performers were beating a path to ratify the decision of AFM or APRS to "secure" their members' remuneration rights and to ask NRCC to administer them.

APRS and AFM may also have been authorized by their members to administer their neighbouring rights through other means. This is an obvious reference to all other ways in which common law and *droit* civil allow a person to transfer rights. These would include subrogation, gift, transfer through wills, etc. None of these apply here.

The issue of whether an association *can*, through its by-laws, appropriate its members' neighbouring rights will be determined according to applicable rules governing associations.[8] NRCC stated that it was not aware of any principle in the law of agency preventing an association from obtaining, through a change in its by-laws, and without consulting its members individually, the agency for all its members' remuneration rights. In the Board's view, NRCC is approaching the issue from the wrong end. When one is dealing with a right to income flowing from statute, the redirection of that income requires express consent of the interested party or, at least, a clear principle of law. NRCC pointed to none.

personne agit a titre de mandataire dans des domaines commerciaux ou professionnels bien précis ou encore, de mandats découlant de règles spéciales gouvernant certains marchés.

Deux conditions sont nécessaires pour qu'il y ait mandat par voie de ratification. Le mandant doit d'abord ttre au courant de tous les faits pertinents avant que la ratification intervienne; en supposant même que l'AFM et l'APRS aient avisé leurs membres par voie de communiqué des mesures qu'elles entendaient prendre, cela pourrait difficilement suffire. Le mandataire doit ensuite déclarer agir pour le bénéfice d'un tiers identifie ou identifiable qui, seul, peut ratifier les gestes que le mandataire a posés. Rien dans la preuve présentée par la SCGDV ne permet de dire que les artistes-interprètes se pressent pour endosser la décision de l'AFM ou de l'APRS visant à s'approprier leur droit a rémunération et a demander a la SCGDV de les gérer.

L'APRS et l'AFM pourraient aussi prétendre avoir ete autorisées a administrer les droits voisins de leurs membres par d'autres moyens. Le «notamment» dans la définition pertinente renvoie de toute evidence aux autres modes de transmission des droits prévus par le droit prive : subrogation, don, succession et ainsi de suite. Rien de cela n'est applicable ici.

Pour savoir si une association peut s'approprier les droits voisins de ses membres par le biais de ses règlements administratifs, il faut s'en remettre au droit des associations.[8] La SCGDV soutient ne connaître aucun principe du droit des mandats empêchant une association de procéder comme elle l'a fait sans consulter chacun de ses membres. La Commission est d'avis que la SCGDV aborde le problème sous le mauvais angle. On ne peut prétendre s'approprier le droit a un revenu découlant de la loi sans le consentement exprès de l'intéressé ou, a tout le moins, sans s'appuyer sur un principe de droit clair. Or, la SCGDV n'en a cité aucun.

By-laws normally deal with the pursuit of the association's common goals. What may be acceptable when dealing with payments (such as residuals) which have accrued as a matter of contract through the efforts of the association in the pursuit of its goals is not acceptable when dealing with the management or acquisition of specific entitlements in the nature of property rights accrued by the effect of law to an association's memben. AFM and APRS *can* no more rake possession of the remuneration right in the way they purport to have done than they can in the same manner declare that they own other property of their members.

It may be possible to secure administration of performers' rights through a specifically worded clause in an association's membership contract. This *can* be distinguished from a mere statement that members are bound by the association's by-laws. which is not specific enough to allow the association to secure such administration. By contrast. provisions that clearly put potential members on notice that their neighbouring rights will be managed by the association ought to be acceptable under the *Act*. although they may very well constitute a questionable practice under competition legislation. This APRS and AFM have done with respect to some. but not most. of their members.

In these matters, it is important to understand the distinction between the powers ACTRA and AFM enjoy as a bargaining agent and those they have as simple associations of persons. Bargaining agents are not automatically collective societies. Moreover, when before the Board, collective societies do not bring with them the powers and privileges they may enjoy as bargaining agents pursuant to labour or status of the artist legislation. There may be some crossover points. Thus, ACTRA or AFM may be able to sanction members who refuse to let them manage their rights or who have already authorized others to act on their behalf. in doing so, they would be acting as bargaining agents. not as collective societies. In the end, the fact remains that they have not successfully secured the necessary authorizations in the first place.

Normalement. les règlements adminismtifs d'une association traitent de la poursuite de buts communs. Ce qui peut être acceptable a l'égard de versements de nature contractuelle obtenus grâce aux efforts de l'association dans le cadre de la poursuite de ses objets (par exemple. les droits de suite) ne l'est pas lorsqu'il s'agit de la gestion ou de l'acquisition de bénéfices des membres de l'association assimilables a des droits de propriete et qui découlent de la loi. L'AFM et l'APRS ne peuvent pas plus s'approprier le droit a rémunération de la façon dont elles pretendent l'avoir fait qu'elles pourraient de la même manière s'approprier d'autres biens appartenant a leurs membres.

Une simple déclaration portant que les membres sont liés par les règlements administratifs de l'association n'est pas suffisamment précise pour lui permettre de s'approprier la gestion de leurs droits voisins. Par contre, une association peut sans doute y arriver en incluant dans son contrat d'adhésion une disposition expresse a cet effet. Une disposition avertissant clairement un postulant que ses droits voisins seront administrés par l'association demit suffire aux fins de la *Loi*, bien qu'elle puisse représenter une pratique commerciale douteuse aux fins du droit de la concurrence. L'APRS et l'AFM n'ont obtenu des autorisations de ce genre que d'une minorité de leurs membres.

Lorsqu'on se penche sur cette question. il faut bien faire la distinction entre les pouvoirs dont l'ACTRA et l'AFM jouissent a titre d'agents négociateurs et ceux dont elles disposent a titre de simples associations de personnes. Être agent négociateur ne suffit pas pour prétendre au rôle de société de gestion. Qui plus est la société de gestion qui traite avec la Commission ne dispose pas des pouvoirs et privilèges dont elle jouit par ailleurs à titre d'agent négociateur en vertu des législations du droit du travail ou du statut de l'artiste. Des recoupements sont toujours possibles. L'ACTRA ou l'AFM pourraient imposer des sanctions aux membres qui refusent de leur confier la gestion de leurs droits ou qui l'ont déjà confiée a d'autres. Dans un tel cas. c'est l'agent négociateur et non la societe de gestion qui agirait. Cela ne change toutefois rien au fait qu'elles ne détiennent tout simplement pas les autorisations qui s'imposent.

Given what has been said, there is no need to go into the various arguments CAB raised with respect to incorporation by reference of unsigned documents into a contract and other related issues. Neither is there any need to discuss the obvious proposition that SOGEDAM does properly represent those AFM members who have authorized it to act on their behalf by way of assignment.

Compte tenu de ce qui précède, il n'y a pas lieu de traiter des pretentions de l'ACR portant sur l'incorporation par renvoi de documents et autres questions du genre qu'elle a soulevées. De même, il est evident que la SOGEDAM est bien-fondée a représenter les membres de l'AFM qui l'ont autorisée par voie de cession.

Consequently, the Board finds that the only performers' rights that NRCC has secured through APRS and AFM are those of persons who have executed an instrument (be it an assignment or a membership form) which expressly deals with the remuneration right.

Par conséquent, les seuls droits des artistes-interprets que la SCGDV detient par le biais de l'APRS et de l'AFM sont ceux de personnes ayant signé une cession, un contrat d'adhésion ou autre document qui aborde expressément la question du droit a rémunération.

This does not, however, dispose of the issue of what is included in NRCC's repertoire.

Cela ne dispose pas pour autant de la question de savoir ce qui fait partie du repertoire de la SCGDV.

c. *Is NRCC nevertheless authorized to manage the remuneration rights of performers who have not chosen it as their collective society?*

c. *La SCGDV est-elle néanmoins autorisée a gérer le droit a rémunération des artistes-interprètes qui n'ont pas retenu ses services en tant que societe' de gestion?*

To determine which performers' performances are in NRCC's repertoire requires an examination of the nature of the rights granted to makers and performers pursuant to section 19 of the *Act*. Two persons (or groups of persons) are granted a remuneration right on account of a single act, the performance or telecommunication of a sound recording. In all cases, the remuneration is paid to one person, and one person only. Once paid, royalties are always split equally between the performers and makers. These are all the markings of a legal relationship involving a single debt owned by two groups of joint and several creditors.' Knowing this, it becomes easier to determine what happens when not all those who are entitled to share in the remuneration right in a sound recording are properly represented by a collective society that has filed a proposed tariff.

Pour décider quelles prestations font partie du repertoire de la SCGDV, il faut d'abord etablir la nature des droits que l'article 19 de la *Loi* accorde aux producteurs et aux artistes-interprètes. Deux personnes ou groupes de personnes se voient accorder un droit a rémunération découlant d'une utilisation unique, soit l'exécution ou la télécommunication d'un enregistrement sonore. La rémunération est toujours versée a une seule personne et ensuite partagée par moitie *entre* artistes-interprètes et producteurs. Voila bien les caractéristiques essentielles d'un rapport juridique impliquant une seule dette due a deux groupes de créanciers solidaires.' Cela etant, il devient plus aisé de determiner ce qu'il advient lorsque certains titulaires du droit a rémunération a l'égard d'un enregistrement donné ne sont pas représentés directement par une societe de gestion ayant déposé un projet de tarif.

CAB *argues* that users should pay only on account of performers and makers who have duly authorized a collective society that has filed a proposed tariff. As a result, where the maker is duly represented but the performer is not, only half the appropriate royalty would be payable. This approach is incompatible with the notion that we are dealing with joint and several creditors. It also creates a conundrum in the application of subsection 19(3) of the *Act*, which provides for the division of any payment once it has been made.

At the other end of the spectrum, one finds the approach favoured by NRCC. According to this, all qualifying sound recordings could be the object of a tariff, even those for which all of the underlying remuneration rights were outside the repenoire of a collective that has filed a tariff. This solution can be discarded because it *makes* subsection 67.1(4) of the *Act* and the statutory imposition of collective administration of performing rights in sound recordings nugatory. Only represented recordings are entitled to remuneration.

The correct interpretation is that a sound recording is properly before the Board as long as a collective society that has filed a proposed tariff represents at least one person entitled to share in the remuneration for the performance or telecommunication of that recording. This interpretation is based on the propasition that a joint and several creditor normally enjoys three complementary rights: the right to seek payment of the debt in its entirety, the right to keep his share of the proceeds and to hold that of his co-creditors if he obtains payment of the debt, and the right to claim his share of the proceeds, where the debt has been paid to his co-creditors. This interpretation clearly meets all the requirements set out in the *Act*. It also conforms to usual notions involved with joint and several creditors.

First, it gives meaning to the statutory imposition of collective administration of performing rights in sound recordings. It requires *that* a tariff be filed by one of the joint creditors in order for a recording to be properly before the Board.

L'ACR soutient que l'obligation de verser des redevances ne vise que les artistes-interprètes et productem ayant dûment autorisé une societe de gestion qui a depose un projet de tarif. Lorsque seul le produaeur est dûment représenté, c'est la moitie de la redevance qui devrait être versée. Or, cene pretention ne peut tenir si nous avons affaire a des créanciers solidaires. En outre, elle donne un sens absurde au pangraphe 19(3) de la *Loi*, qui exige le partage de tout versement après qu'il a été fait.

A l'opposé, on retrouve l'interpretation que defend la SCCDV. Selon elle, tous les enregistrements sonores admissibles peuvent faire l'objet du tarif, même si les droits a rémunération afférents ne font pas partie du répertoire d'une société ayant déposé un projet de tarif. Il faut écarter cene solution. Elle rend inopérants le paragraphe 67.1(4) de la *Loi* et l'exigence que les droits d'exécution sur les enregistrements sonores soient gérés collectivement. Seuls les enregistrements représentés ont droit à une rémunération.

L'interpretation qu'il faut retenir est que la Commission est saisie d'un enregistrement sonore dès lors qu'une société de gestion ayant déposé un projet de tarif représente au moins un des titulaires du droit a rémunération pour l'exécution ou la télécommunication de l'enregistrement en question. Cette interpretation découle des droits complémentaires que détient tout créancier solidaire : celui de se faire payer la totalité de la dette, celui d'en garder la part qui lui revient tout en détenant celle de ses co-créanciers s'il a reçu le paiement, et celui de réclamer sa quotepart si c'est un autre co-créancier qui a reçu le paiement. Cette interprétation répond clairement aux exigences de la *Loi*. Elle est aussi conforme aux principes généralement applicables aux créances solidaires.

Premièrement, elle respecte l'exigence que les droits d'exécution sur les enregistrements sonores soient gérés collectivement. Le dépôt d'un projet de tarif par l'un ou l'autre des co-créanciers opère saisine de la Commission.

Second, it allows one of the joint creditors to act as a sort of agent of the other. Joint and several creditors commonly act in *this* way for one another.

Third, this interpretation explains in part the wording of subparagraph 68(2)(*a*)(iii) of the **Act**, which imposes the single payment obligation when "examining a proposed tariff for the [performance or communication] of performer's performances of musical works, or of sound recordings embodying such performer's performances". If one accepts that a society administering performers' rights acquires the right to collect the makers' share of the royalties, the society that files a tariff for the performer's right also files a tariff for the right to collect the maker's sham, subject to the duty to remit that share to the maker, and vice versa.

Consequently, a sound recording is properly before the Board in these proceedings as long as either the maker or the performer is duly represented by NRCC or SOGEDAM. Timely filing of a proposed tariff on account of either of the joint crediton is sufficient to trigger liability for the whole of the debt, irrespective of what the other creditor did. Consequently, NRCC can claim the entire remuneration for the use of a sound recording whose maker it represents even if the performers are not represented, either because of some defect in the appointment (e.g. AFM) or simply because agreements with foreign societies are still being negotiated (e.g. ADAMI). The very nature of the rights vesting in *makers* and performers as a result of section 19 of the *Act* makes it possible that a recording be entitled to remuneration even though some of the persons entitled to share in the remuneration may not themselves have authorized a collective to represent them.[10]

Deuxiemement, elle permet a l'un des co-créanciers d'agir en quelque sorte pour le compte des autres. Il est courant que des créanciers solidaires agissent ainsi pour le Wnefice de leurs co-créanciers.

Troisiemement, elle explique en partie le libellé du sous-alinéa 68(2)(*a*)(iii) de la *Loi*, qui exige le versement unique «aux fins d'examen des projets de tarifs déposés pour [l'exécution ou la télécommunication] de prestations d'œuvres musicales ou d'enregistrements sonores constitués de ces prestations». Si, come la Commission le croit, la societe qui gere le droit a rémunération d'un artiste-interprète acquiert celui de percevoir la quote-part du produaeur, le dépôt par celle-ci d'un projet de tarif pour le compte de l'artiste-interprète vaut également pour le compte du producteur, sujet a l'obligation de partage, et vice-versa.

La Commission est donc saisie d'un enregistrement sonore dans la présente affaire dès lors que la SCGDV ou la SOGEDAM représente soit le producteur, soit l'artiste-interprète. Le dépôt en temps voulu d'un projet de tarif pour le compte de l'un ou l'autre des co-créanciers vaut pour la totalité de la dance, sans egard au comportement de l'autre créancier. Par conséquent, la SCGDV peut demander à recevoir toute la rémunération a l'égard de chaque enregistrement dont elle représente le producteur mCme si elle ne représente pas les artistes-interprètes qui y figurent, soit parce qu'il n'y a pas eu autorisation valable aux yeux de la *Loi*, come c'est le cas, par exemple, pour les membres de l'AFM, soit tout simplement parce que les ententes nécessaires n'ont toujours pas été conclues avec les sociétés étrangères, comme c'est le cas notamment pour les membres de l'ADAMI. La nature même des droits que l'article 19 de la *Loi* confère aux productem et aux artistes-interprètes fait en sorte qu'un enregistrement emporte le droit a rémunération même si certains co-titulaires n'ont pas eux-mêmes autorisé une societe a les représenter.[10]

Given the Board's earlier finding that NRCC brings with it the makers' share of virtually all the eligible recordings, it can safely be stated that the performers' share of this repenoire is equally properly before the Board in these proceedings.

Compte tenu que la Commission a deja conclu que la SCGDV gère la quote-part des productem de pratiquement tous les enregistrements admissibles. on peut dire sans crainte de se tromper que la Commission est egalement saisie de la quote-part revenant aux artistes-interpretes de ces enregistrements.

3. To what extent do commercial radio stations use the eligible repenoire?

3. Quel usage les stations de radio commerciale font-elles du répertoire admissible?

In order to help the Board establish the importance of the use made by radio stations of the eligible repertoire. NRCC filed a music use study on which it relies for its conclusion that eligible sound recordings account for 49.3 per cent of all use of sound recordings by commercial radio stations. The study involved identifying the sound recordings used by a weighted. stratified sample of radio stations over a test period. The music use data provided with the report identifies. with respect to each recording, the station on which it was aired, the name of the artist(s), the title of the song. the number of plays and the source (name of label). It also indicates whether, according to NRCC. the recording is eligible or not.

Afin d'aider la Commission a determiner quel usage les stations de radio font du repertoire admissible. la SCGDV a déposé une etude tendant a demontrer que le repertoire admissible représente 49.3 pour cent de l'ensemble des enregistrements sonores utilisés par les stations de radio commemale. Pour réaliser cette étude, on a analysé les enregistrements utilisés durant une période temoin par plusieurs stations de radio. choisies selon un échantillonnage ponder6 et stratifié. Les données d'utilisation de musique identifient, pour chaque enregistrement, la station qui l'a diffusé, le nom du ou des artistes-interprètes, le titre de la chanson. le nombre de diffusions et la maison de disque. On indique également si, selon la SCGDV, l'enregistrement est ou non admissible.

Producer members of AVLA and SOPROQ carried out most of the task of identifying titles. although in some cases, labels and independent artists were asked to help. In this respect. the study is not as complete as one might have hoped. It does not indicate the country of origin or the age of the recording. Neither does it allow the reader to establish whether a sound recording was determined to be eligible because of the nationality of the maker or because of the country in which it was made. Finally, the eligibility status of some 4.9 per cent of titles could not be ascertained. These include so-called 'imports" from non-Rome countries. but also some recordings that appeared to have been made in Rome countries and were therefore probably eligible. but whose status could not be defined. These titles were attributed to each category in the Same proportion that was observed among classified titles. On the whole. however, the

Pour l'essentiel, ce sont les productem membres de l'AVLA et de la SOPROQ qui ont identifie les enregistrements. Dans certains cas, les maisons de disque et les artistes-interprets independants ont ete mis a contribution. Sous ce rapport. l'etude n'est pas aussi exhaustive qu'on aurait pu l'espérer. Elle ne précise pas le pays d'origine ou la date de l'enregistrement. Elle ne permet pas non plus au lecteur d'etablir si l'admissibilité de l'enregistrement découle de la nationalité du productem ou de l'endroit où il a été confectionné. Enfin, dans 4.9 pour cent des cas, on ne sait pas si les enregistrements sont admissibles ou non. Cela comprend non seulement les disques importés directement de pays non-signataires de la Convention de Rome. mais aussi certains titres provenant apparemment de pays signataires et donc probablement admissibles. mais qu'on n'a pas pu identifier avec certitude. On a donc réparti ces enregistrements dans les identification process appears to have been done seriously and conservatively.

CAB did not conduct its own music use study, and opted instead to review and critique NRCC's study. The critique addressed such issues as the choice of stratification system and the weighting of stations in the determination of the random sample. CAB did not succeed in discrediting NRCC's methodology and findings. Furthermore, its own analysis proved to be flawed in several respects which were correctly identified in NRCC's argument and need not be repeated here. Consequently, CAB's analysis was of little use.

For its part, in an attempt to identify the importance of the French repertoire on radio stations, SOGEDAM used a number of sets of data to determine, first, the percentage of airtime dedicated to non-Canadian, French selections, and then the proportion of those recordings that are part of its repertoire.[11] For reasons that will become clear later, there is no need to analyse in detail SOGEDAM's claim. Suffice it to say that SOGEDAM's analysis is not very reliable, and involves some miscalculations. As a result, it cannot be used to determine the percentage of sound recordings used on Canadian commercial radio stations that are part of the French repertoire.

The Board accepts NRCC's conclusion that qualifying sound recordings account for 49.3 per cent of all use of sound recordings by commercial radio stations. The Board also accepts NRCC's evidence that it represents the makers' share of at least 95 per cent of these recordings. Given NRCC's willingness to accept a ruling according to which NRCC's repertoire accounts for 45 per cent of all use of sound recordings by commercial radio stations, the Board so finds.

mêmes proportions que ce qui avait ete constaté a l'egard des enregistrements identifiés. Cela dit, dans l'ensemble, il semble que l'analyse ait ete effectuée de façon sérieuse et conservatrice.

L'ACR n'a pas effectué d'étude distincte, se contentant de revoir et de critiquer celle de la SCGDV. Ses critiques ont porte sur des sujets tels le choix de la stratification et de la ponderation utilisées lors de l'échantillonnage des stations. L'ACR n'a pas réussi a discréditer la méthodologie et les conclusions de la SCGDV. Qui plus est, sa propre analyse s'est avérée mal fondée a plusieurs égards, tel que la SCGDV l'a relevé dans son argumentation écrite, et qu'il n'y a pas lieu de reprendre ici. L'analyse de l'ACR est donc peu utile.

Quant a elle, dans le but d'etablir l'utilisation du repertoire français sur les ondes canadiennes, la SOGEDAM a analysé, a partir de plusieurs ensembles de données, le pourcentage de temps d'antenne consacré aux enregistrements etrangers de langue française, puis la part qui lui revient de ces enregistrements.[11] Pour des motifs qui deviendront clairs par la suite, il n'est pas nécessaire de se livrer a une analyse détaillée de ces pretentions. On se contentera de dire que l'analyse semble peu fiable et comporte certaines erreurs de calcul. Elle ne peut donc servir a etablir l'etendue du répertoire de la SOGEDAM utilisé par les stations de radio commerciale canadiennes.

La Commission accepte la conclusion de la SCGDV selon laquelle le répertoire admissible représente 49.3 pour cent de l'usage d'enregistrements sonores par les stations de radio commerciale. Elle accepte aussi la preuve de la SCGDV démontrant qu'elle représente les producteurs d'au moins 95 pour cent de ces enregistrements. Puisque la SCGDV se dit prête a accepter un tarif fonde sur un repertoire représentant 45 pour cent de l'utilisation d'enregistrements sonores par les stations de radio commerciale, c'est ce chiffre qui sera utilisé pour etablir le tarif.

C. **What account should be taken of the Canadian broadcasting policy?**

Subparagraph 68(2)(*a*)(ii) of the *Act* requires that 'the tariff does not, because of linguistic and content requirements of Canada's broadcasting policy set out in section 3 of the Broadcasting *Act*, place some users that are subject to that Act at a greater financial disadvantage than others'. Based on the record of these proceedings, it appears that French language radio stations use the eligible repertoire for more than three-quarters of their airtime, while their English counterparts do so for less than half of the time. Absent this statutory requirement, a case could be made for a tariff that is significantly higher for the first stations than for the second. The issue is how to apply this requirement in a manner that is fair to both users and rights owners.

The relevant parts of section 3 of the *Broadcasting Act* read as follows:

> 3. (1) It is hereby declared as the broadcasting policy for Canada that
>
> ...
>
> (b) the Canadian broadcasting system, operating primarily in the English and French languages ... provides, through its programming, a public service essential to the maintenance and enhancement of national identity and cultural sovereignty:
>
> (c) English and French language broadcasting, while sharing common aspects, operate under different conditions and may have different requirements:
>
> ...
>
> (k) a range of broadcasting services in English and in French shall be extended to all Canadians as resources become available:

C. **Comment faut-il tenir compte de la politique canadienne en matière de radiodiffusion?**

Le sous-alinéa 68(2)(*a*)(ii) de la *Loi* stipule que le tarif ne peut avoir «pour effet, en raison d'exigences differentes concernant la langue et le contenu imposées par le cadre de la politique canadienne de radiodiffusion etabli a l'article 3 de la *Loi sur la radiodiffusion*, de désavantager sur le plan financier certains utilisateurs assujettis a cette loi». Le dossier de la présente affaire revele que le repertoire admissible représente environ les trois quarts du temps d'antenne des stations de langue française, par opposition a la moitie pour les stations de langue anglaise. N'eût ete l'exigence du sous-alinéa 68(2)(*a*)(ii), on aurait pu soutenir que les premières stations devraient verser des redevances passablement plus élevées que les secondes. Reste a déterminer comment cette exigence peut être satisfaite d'une façon qui soit équitable tant pour les utilisateurs que pour les titulaires de droits.

Les passages pertinents de l'article 3 de la *Loi sur la radiodiffusion* prevoient ce qui suit :

> 3. (1) Il est déclaré que, dans le cadre de la politique canadienne de radiodiffusion :
>
> ...
>
> b) le système canadien de radiodiffusion, ... offre, par sa programmation essentiellement en français et en anglais, un service public essentiel pour le maintien et la valorisation de l'identité nationale et de la souveraineté culturelle;
>
> c) les radiodiffusions de langues française et anglaise, malgré certains points communs, different quant a leurs conditions d'exploitation et, éventuellement, quant a leurs besoins;
>
> ...
>
> k) une gamme de services de radiodiffusion en français et en anglais doit être progressivement offerte a tous les Canadiens, au fur et a mesure de la disponibilité des moyens;

...

(2) It is further declared that the Canadian broadcasting system constitutes a single system...

CAB argued that the only way to address subparagraph 68(2)(a)(ii) of the *Act* is to discount any incremental use of the eligible repertoire due to the different application of Canadian broadcasting policy to French- and English-language stations. Put another way. CAB would have the Board letting stations use the eligible repertoire for free when they use more than other stations in order to comply with that policy. For this. CAB relies on two propositions. First, French-language broadcasters cannot suffer financial disadvantage simply because of the linguistic requirements of the Broadcasting *Act*. Second, the solution cannot lie in all stations paying at the same rate based on the whole industry's use of the eligible repertoire, as *this* would result in English-language stations paying a tariff which reflects a level of use higher than theirs.

CAB's interpretation is incorrect. The *Act* does not require that the Board ignore or discount the impact of the regulatory environment on use patterns. Instead, it mandates that users not be put at a *greater* financial disadvantage *than others* because of requirements of Canada's broadcasting policy. This is achieved if all users in a given group share equally the financial burden imposed as a result of the policy. as long as imposing that burden is fair. The cost of the equalization exercise required by this provision can be imposed on the indusuy, especially where the very policy that the Board is asked *to* consider treats all memben of that industry as part of a 'single system'.

CAB's interpretation is also dangerous. Subparagraph 68(2)(a)(ii) of *the Act* speaks not only of linguistic, but also of content requirements. Pushed to its logical conclusion.

...

(2) Il est déclaré en outre que le systeme canadien de radiodiffusion constitue un systeme unique...

L'ACR soutient que la seule façon d'aborder le sous-alinéa 68(2)(a)(ii) de la *Loi* est de ne pas tenir compte de la part d'utilisation du repertoire admissible découlant de l'application différente de la politique canadienne en matière de radiodiffusion aux stations de langue française et de langue anglaise. Autrement dit. l'ACR voudrait que la Commission permette aux stations tenus d'utiliser une partie plus grande du repenoire admissible pour se conformer a cette politique, de le faire gratuitement. Cene prétention se fonde sur deux propositions. La premiere veut que les radiodiffuseurs de langue française ne puissent être désavantagés sur le plan financier uniquement a cause des exigences de la *Loi sur la radiodiffusion* en matiere de langue. La seconde est que le taux des redevances ne saurait être fonde sur l'utilisation du répertoire admissible par l'ensemble de l'industrie. car les stations de langue anglaise se trouveraient a payer plus que leur niveau propre d'utilisation.

L'ACR se trompe. La *Loi* n'exige pas que la Commission ignore ou ne tienne pas compte de l'impact du contexte réglementaire sur le niveau d'utilisation. Elle exige plutdt que certains utilisateurs ne soient pas désavantagés *par rapport a d'autres* a cause des exigences de la politique canadienne en matiere de radiodiffusion. On y arrive si tous les utilisateun faisant partie d'un groupe donné supportent également le fardeau découlant de cette politique. en autant que le fardeau soit équitable. Le coût attribuable à cet exercice d'égalisation peut être imposé a l'ensemble de l'industrie, d'autant plus que la politique même dont la Commission doit tenir compte déclare que tous ses membres constituent un «système unique..

L'interprétation mise de l'avant par l'ACR compone par ailleurs des risques évidents. Le sous-alinéa 68(2)(a)(ii) de la *Loi* traite non seulement de langue. mais aussi de contenu. La

CAB's approach would require that the Board provide commercial radio stations with a rebate on account of that part of the eligible repertoire they play not as a maner of choice. but to comply with Canadian content requirements. The regime does not require that rights owners subsidize the radio industry on account of regulatory requirements; in fact. to do so would be unfair. especially given the provisions made in the *Act* to cushion the impact of the new royalties.

Consequently, the appropriate way to take into account the Canadian broadcasting policy in this instance is to charge all radio stations the same price, irrespective of the mount of eligible sound recordings used by each individual station, except for two exceptions which will be outlined later.

D. How much should radio stations pay for their use of the property represented eligible repertoire?

The *Act* requires the Board to fix an 'equitable remuneration' for the use of recorded music by radio stations, for the benefit of makers and performers. If. as stated earlier. the tariff is to be fair and equitable to both rights holden and users, fixing the tariff calls for an examination of the value rights holden provide and the benefit users derive from it.

SOGEDAM did not offer any particular rationale for its proposed rate of five per cent. In its final argument, it also supported *NRCC's* approach and conclusions. Consequently. the following analysis deals only with the arguments put forward by NRCC and by CAB.

1. The aoproach favoured bv NRCC

In developing the models which it offers as support for its proposals, NRCC relied on a number of assumptions. First, the price for neighbouring rights should be that to which a

demarche de l'ACR pourrait mener a l'octroi de rabais pour tenir compte de la part du répertoire admissible que les stations utilisent non pas volontairement. mais pour se conformer aux exigences de contenu canadien. Le regime n'exige pas que les titulaires de droiu subventionnent l'industrie de la radio au motif que cette dernière doit répondre a certaines exigences de nature réglementaire; il serait plutôt injuste d'agir ainsi. surtout si l'on tient compte des mesures que la *Loi* prévoit deja pour réduire l'impact des nouvelles redevances.

Par conséquent, la façon de tenir compte de la politique canadienne en matiere de radiodiffusion dans l'espèce est de faire payer le mime prix a toutes les stations de radio, *sans* egard aux niveaux individuels d'utilisation d'enregistrements admissibles, sous réserve de deux exceptions sur lesquelles nous reviendrons plus tard.

D. Combim les stations de radio devraient-elles payer pour l'usage qu'elles font du répertoire admissible dûment représenté?

La *Loi* exige que la Commission établisse «une rémunération équitable» pour l'utilisation de musique enregistrée par les stations de radio, pour le bénéfice des productem et artistes-interprets. Pour etablir un tarif qui, c o m e on l'a deja annoncé, soitjute et équitable tant pour les titulaires de droits que pour les utilisateun. il faut se pencher sur la valeur de l'apport des titulaires de droits et sur l'avantage que les utilisateun en tirent.

La SOGEDAM n'a rien avancé a l'appui du taux de cinq pour cent qu'elle propose. Dans son argumentation finale. elle a soutenu la demarche et les conclusions de la SCGDV. L'analyse qui suit porte donc uniquement sur les prétentions mises de l'avant par la SCGDV et par l'ACR.

1. La démarche aue propose la SCGDV

Pour mettre au point les modèles qu'elle offre au soutien de ses propositions, la SCGDV a retenu un certain nombre de postulats. Premierement. le prix payé pour les droits voisins devrait itre celui willing seller and a willing buyer would agree. Second, commercial stations make little use of live music or public domain recordings. Third. royalties should account for the rights of both makers and performers. Fourth, equitable remuneration should provide a fair return to rights holden for their investment of talent and financial resources. and should reflect the value that broadcasters, as commercial enterprises. derive from making use of sound recordings to earn revenue.

With respect to rights holden' financial commitments, NRCC insisted especially on the costs incurred in producing and promoting an album and on the risks involved in developing a recording artist. NRCC's witnesses also testified that the industry's primary business is to earn revenue from its copyrights. not only to generate record sales.

On the issue of the value radio stations derive from their use of sound recordings, NRCC relied on a number of assertions which it says support the view that advertising revenues of radio stations are dependent on those recordings. This. it says, provides an indication of the essential value of the use of sound recordings to the industry. The "facts" NRCC relied upon include the following. First. music fotmat stations account for the vast majority of radio listening in Canada. Second, music is the engine that drives mast commercial radio stations: a majority of people give music as the main reason for listening to radio; mast say they would listen less if radio did not play sound recordings. Third, advertisers pay for audiences. and music draws audiences. Fourth, performers provide stations with more value than composers do: stations are star driven and want to be associated with known artists. Fifth, music represents 78.4 per cent of total broadcast time and 88.2 per cent of *total* program time. Sixth. the royalties of the Society of Composers.

qui serait autrement etabli de gré a gré. Deuxiemement. les stations de radio commerciale diffusent peu ou pas de musique en direct ou d'enregistrements faisant partie du domaine public. Troisiemement. les redevances devraient tenir compte tant des droits des producteurs que de ceux des artistes-interprètes. Quatrièmement, une remuneration équitable demit offrir aux titulaires de hits un rendement équitable pour leur apport en talent et en ressources financiers et demit refleter le bénéfice que les radiodiffuseurs. en tant qu'entités commerciales. tirent de l'utilisation d'enregistrements sonores pour gagner des revenus.

Lorsqu'elle parle des engagements financiers des titulaires de hits. la SCGDV insiste avant tout sur les coûts de production et de promotion d'un album et les risques qu'implique le developpement des artistes. Ses témoins ont aussi souligné que l'industrie du disque cherche avant tout a dériver des bénéfices de ses droits d'auteur. et non seulement a générer des ventes d'albums.

Quant aux avantages que les stations de radio tirent de l'utilisation d'enregistrements sonores. la SCGDV s'est fondée sur certaines affirmations qui. selon elle. tendent a prouver que les recettes publicitaires des stations sont directement fonction de cene utilisation. Selon elle. cela indique a quel point l'industrie a besoin de ces enregistrements. A l'appui, elle invoque, entre autres. les «faits» suivants. Premierement. les Canadiens écoutent avant tout les stations de format musical. Deuxiemement. la musique est le moteur de la plupart des stations de radio commerciale; la majorité des personnes interrogées disent écouter la radio avant tout pour la musique et la plupart affirment qu'elles réduiraient leur écoute s'il y avait moins d'enregistrements sonores. Troisièmement, les annonceurs achètent des auditoires, et c'est la musique qui les attire. Quatrièmement, l'apport des artistes-interprètes a plus de valeur pow les stations que celui des compositeurs; les stations dependent des vedettes et cherchent a être identifiées a des artistes-

Authors and Music Publishers of Canada (SOCAN) represent about 10 per cent of program expenses.

NRCC then examined a number of pricing models to support the assertion that authors. perfomen and makers should receive between 18 and 23 per cent of commercial radio stations' advertising revenues. and that the combined value of rights in sound recordings is. at a minimum. 12 per cent. NRCC concluded that. after adjustments to account for the use of non eligible sound recordings and the blanket character of the regime, radio stations should pay 6.06 per cent of their advertising revenues for their use of sound recordings of musical works.

NRCC looked at a number of possible approaches to determine the appropriate royalties. Congruent with its starting proposition on valuation, it offered proxies that all refer to situations where the level of payment for the use of sound recordings is based on mutual agreement between a willing seller and a willing buyer. Each of them is commented upon in turn.

NRCC first noted that music stations spend 29 per cent of their revenues on programming. compared to 49 per cent for low music use stations. Based on this comparison, NRCC argued that suppliers of sound recordings should be able to claim 20 per cent of music stations' revenues. CAB objected to the use of this comparison. Scarcity creates value: talk programming is almost always acquired on an exclusive basis. while music is available to all stations. Moreover, the approach relies on two false assumptions. The first is that the value of an input can be determined by the value of possible, but more costly, substitutes. The second is that all inputs make an equal

interprets connus. Cinquièmement. la musique représente 78.4 pour cent du temps d'antenne total et 88.2 pour cent du temps de programmation. Sixièmement, les redevances versées a la Societe canadienne des auteurs. compositeurs et éditeurs de musique *(SOCAN)* représentent approximativement 10 pour cent des dépenses de programmation.

La SCGDV a ensuite examine un certain nombre de méthodes d'évaluation qui. selon elle. tendent a soutenir la proposition voulant qu'ensemble, les auteurs. artistes-interprets et producteun devraient recevoir entre 18 et 23 pour cent des recenes publicitaires des stations de radio commerciale. et que la valeur combinée des droits voisins est d'au moins 12 pour cent. Après avoir ajuste cette valeur pur tenir compte des enregistrementsnon admissible et du caractère général du régime. la SCGDV en vient a la conclusion que les stations devraient verser 6.06 pour cent de leurs recettes publicitaires pour l'utilisation qu'elles font des enregistrements sonores d'œuvres musicales.

La SCGDV a examine plusieun façons d'etablir un montant appropric de redevances. Conformément a sa position de depart concemant l'évaluation des droits. les analogies qu'elle a mises de l'avant portent sur des marchés dans lesquels le prix payé pour l'utilisation de l'enregistrement sonore est etabli de gré a gré. Chacun de ces modèles fera maintenant l'objet de commentaires.

La SCGDV souligne d'abord que les stations de format musical dépensent 29 pour cent de leurs revenus pour la programmation, par rapport au 49 pour cent dépensé par les stations qui utilisent peu de musique. La SCGDV emploie cette comparaison pour soutenir que les fournisseurs d'enregistrements sonores devraient pouvoir réclamer 20 pour cent des revenus des stations de format musical. L'ACR s'oppose a l'emploi de cette comparaison. La rareté d'un bien en augmente la valeur; la programmation verbale s'achète presque toujours sur une base exclusive alors que toutes les stations ont accès a la même musique. Qui plus est. cette demarche repose sur contribution to the generation of revenue. The Board agrees with CAB. if only because the notion that the value of non-exclusive recorded music would be close to the value of talk and information programming, if negotiated in a market situation, is unsustainable. Any comparison with television programming costs must also be set aside for the same reason.

deux premisses également fausses. La premiere est que la valeur d'un intrant peut être etablie a partir de substituts possibles mais plus coûteux. La seconde veut que tous les intrants contribuent egalement a générer des revenus. La Commission partage le point de vue de l'ACR, ne serait-ce que parce que l'on ne peut prétendre serieusement que dans un marché libre, la musique enregistrée accessible a tous se vendrait plus ou moins au même prix que la programmation park ou l'information. Pour les mêmes motifs, il faut rejeter toute comparaison avec les coûts de la programmation televisuelle.

NRCC then offered two approaches which yield similar results. Performers and makers receive 15 per cent or more of the retail price of compilation CDs or *cassettes* on account of the use of pre-recorded performances. while those who supply recorded music *to* discjockeys. restaurants and others pay 15 per cent of their *gross* revenues for a blanket licence to reproduce AVLA's repertoire. NRCC believes that these are particularly relevant comparisons, because they are examples of a commercial exploitation of recorded performances. in a market where there is a willing seller and a willing buyer. CAB objected to these approaches for reasons which need not be repeated here. The Board rejects these proxies; its task is to value the right to broadcast. not the right to reproduce.

La SCGDV a enswte mis de l'avant deux méthodes donnant des résultats similaires. Les artistes-interpets et les productem perçoivent 15 pour cent ou plus du prix de vente au detail des disques CD et cassettes représentant des compilations de chansons pré-enregistrées. Quant a ceux qui fournissent de la musique enregistrée aux *disc-jockeys*, aux restaurateurs et a d'autres, ils versent 15 pour cent de leurs recettes brutes pour la licence générale leur permettant de reproduire le repenoire de l'AVLA. La SCGDV croit qu'il s'agit la de comparaisons particulièrement pertinentes, s'agissant d'exemples de l'exploitation commerciale de prestations enregistrées, dans un marche où les transactions se font de gré a gré. L'ACR s'y oppose pour des motifs qu'il n'y a pas lieu de commenter. Pour sa part. la Commission rejette ces comparaisons au motif qu'elles concement le droit de reproduire et non celui de diffuser.

Subsidiarily, and even though it did not support using SOCAN's Tariff I.A as a proxy, NRCC commented on the relative value of neighbouring rights and authors' rights, coming to the conclusion that, all other things being equal NRCC's royalties should be higher than SOCAN's. In support of this propasition. *NRCC* provided evidence tending to show that making a sound recording costs approximately 4.5 *times* what it costs to make a song. The Board agrees with CAB that the cost of making a recording is of little help in establishing the value of a right to play it. Furthermore. the Board is far from convinced that such cost can be established or that

Subsidiairement, et bien qu'elle s'oppose a l'établissement d'un lien entre le tarif de droits voisins et celui de la *SOCAN*, la SCGDV s'est livrée a une comparaison à l'égard de la valeur relative des deux droits dans le marché du disque pour conclure que toutes choses égales, la SCGDV devrait recevoir davantage que la SOCAN dans le marché de la radiodiffusion. Elle fonde cene prétention sur une preuve tendant a etablir qu'il en coûte environ 4.5 fois plus pour produire un enregistrement sonore que pour écrire une chanson. Tout comme l'ACR. la Commission croit qu'on ne peut établir la valeur à accorder pour la diffusion d'un enregistrement sonore a the methodology NRCC used in this case was the right one. Finally, SOCAN's own *tariff* has never been based on the cost of creating a song.

partir de ce qu'il en coûte pour le produire. Qui plus est. la Commission n'est pas du tout convaincue qu'il soit possible d'etablir ce coût ou encore. que la façon dont la SCGDV s'y est prise soit la bonne. Enfin. le tarif de la SOCAN n'a jamais ete fonction de ce qu'il en coûte pour écrire une chanson.

NRCC also filed evidence tending to establish that royalties paid to performers and makers of sound recordings in free market transactions are approximately 2.5 times higher than royalties paid to authors. This issue is discussed later in *these* reasons.

La SCGDV a aussi cherche a etablir que les redevances versées aux artists-interprets et productem d'enregistrements sonores darts des transactions libres etaient environ 2.5 fois plus élevées que cells versées aux auteurs. Nous revenons sur cette question un peu plus loin.

2. The approach favoured by CAB

2. La demarche aue propose l'ACR

CAB supports the view that SOCAN's tariff represents the most *useful* starting point. In both cases, royalties are payable on account of the same rights flowing from the use of the same input. Although separate and distinct, the fact situations are as close as the Board will ever find. Finally, authors' rights were also originally decided by this Board and recently extended as the result of an agreement.

Pour sa part, I'ACR soutient que le tarif de la *SOCAN* reprbente le point de depart le plus utile. Dans les deux cas, les redevances sont versées pour les mêmes droits suite a I'utilisation du même produit. Même s'il s'agit de situations differentes. la Commission ne peut espérer trouver meilleure comparaison. Enfin. c'est la Commission qui a évalué les droits d'auteur a I'origine. et c s derniers ont ete récemment reconduits suite a une entente.

Having said this. CAB would reduce the rate to 0.7 per cent for several reasons. all of which ought to be rejected.

Cela dit. I'ACR réduirait le taux a 0.7 pour cent. invoquant divers motifs que la Commission rejette.

The importance of the represented repertoire

L'utilisation du repenoire *représenté*

CAB claims that not all of the eligible repertoire is properly before the Board in these proceedings. This has already been addressed and rejected.

L'ACR prétend qu'une partie du repertoire admissible n'est pas dûment représentée dans la présente affaire. Cet argument a deja été examiné et rejeie.

Neighbouring rights are intrinsically less valuable than copyright

De par leur nature, les droits voisins valent moins que *les droits d'auteur*

This argument is based on two assumptions. both of which the Board rejects.

L'argument se fonde sur deux prémisses que la Commission rejette.

Thus, CAB relies on the fact that the Rome Convention and the *Act* protect neighbouring rights less than authors' rights, even though some experts, including its own. recognize that there is

Ainsi. l'ACR se fonde sur le fait que la Convention de Rome et la *Loi* accordent moins de droits aux titulaires des droits voisins qu'aux titulaires des droits d'auteur. Pourtant. certains no formal hierarchy between them. The argument ignores a number of realities. First. the *Act* does not prioritize traditional copyright rights over neighbouring rights. To the contrary, the Act includes in its definition of copyright all exclusive rights granted to performers. makers of sound recordings and broadcasters. Second. section 19 rights do not differ substantially from those enjoyed by SOCAN: in both cases, there is no right to prohibit use. and the price for use is set by the Board. Third, the fact that authors enjoy more rights than performers. makers and broadcasters does not mean that their rights are more valuable; each right should be valued on its own merits, using proper valuation methodologies. Fourth, the fact that a performer retains the right to prevent certain uses of his or her performance even where the author consents to the use of the work is incompatible with the prioritization of authors' rights over those of performen.

CAB also argues that quite apart from any formal hierarchy, neighbouring rights are generally valued at a lower level than authors' rights. Both CAB and NRCC presented expert evidence on the relative rates being paid in other countries. CAB's expert concluded that commercial and public broadcasters paid, in aggregate. less for neighbouring rights than for authors' rights. although the picture is significantly altered in favour of neighbouring rights if one only looks at commercial stations. NRCC's expert witness. for his part, tended to conclude that commercial radio stations pay more for the neighbouring rights. The evidence in this respect was disappointing. The Board was unable to determine the relative extent of the eligible repertoire or the relative level of use covered by these tariffs. Given the *great* difficulty of making meaningful comparisons with the Canadian situation, it would be inappropriate to rely on them in setting the Canadian rate. More importantly. *any such* comparisons are necessarily influenced by local market considerations and must be treated with great caution.

experts, dont le sien. admettent qu'il n'existe pas de hiérarchie formelle entre les deux categories de droits. L'ACR méconnaît trop facilement un certain nombre de réalités. Premierement. la *Loi* n'établit pas d'ordre de priorite entre le droit d'auteur et les droits voisins. Au contraire, la definition de droit d'auteur inclut tous les droits exclusifs des artistes-interpretes. producteun d'enregistrements sonores et radiodiffuseurs. Deuxiemement. les droits énumérés a I'article 19 de la *Loi* ressemblent fortement a ceux dont jouit la *SOCAN* : dans un cas c o m e dans l'autre, on ne peut interdire I'usage et le prix *est* etabli par la Commission. Troisiemement. ce n'est pas parce que les auteurs ont plus de droits que les artistes-. interprètes, producteun ou radiodiffuseurs que la valeur des uns est supérieure a la valeur des autres: cham demit être évalué a sajute valeur et selon une méthode d'évaluation appropriée. Quatriemement. le fait que l'artiste-interprète puisse interdire qu'on utilise sa prestation lonque l'auteur consent a l'utilisation de son œuvre est incompatible avec la notion même de hiérarchie.

L'ACR soutient par ailleurs que. mis a part toute hiérarchie formelle, les droits voisins valent généralement moins que les droits d'auteur. Tant I'ACR que la SCGDV ont offert le temoignage d'experts sur les prix payés à l'étranger pour ces droits. L'expert de I'ACR affirme que les radiodiffuseurs commerciaux et publics confondus paient moins pour les droits voisins, bien que le rapport soit plutôt en faveur de ces demiers si l'on tient compte uniquement des stations commerciales. Pour sa part. l'expert de la SCGDV soutient que les stations de radio commerciale paient davantage pour les droits voisins. Cela dit. la preuve sur cene question a été décevante. Ainsi, il n'a pas ete possible d'etablir l'importance relative des répertoires admissible ni de I'usage qui en est fait. Compte tenu qu'il est pratiquement impossible d'etablir des comparaisons valables avec le marché canadien. il n'y a pas lieu d'utiliser ces données dans I'etablissement du taux canadien. De toute facon. les comparaisons de ce genre doivent être traitées avec beaucoup de précaution, car elles sont nécessairement affectées par les conditions locales des marchés en cause.

Performen and makers derive greater value than copyright owners from air play

CAB argued at length that a fair and equitable tariff should take into account the numerous benefits performers and makers derive from the air play their sound recordings receive. This is not a novel argument.

Radio does contribute to the sale of records. It has been and remains a very important vehicle for the promotion of records sales. This being said, radio does not play records to promote their sale. but to support its business, which is to attract listeners and sell advertising spots. As the Board stated in the past with respect to performing rights for musical works. this is but one case of a symbiotic relationship between different industries with no direct bearing on the price.

Radio *stations contribute* to *the* record *indusuy in several other ways*

As in the past with respect to performing rights for musical works. CAB also asked the Board to take into account the various contributions, both direct and indirect. made by radio stations to the record industry. These include on-air promotion of performers, monetary contributions to local talent development. as well as CRTC's imposed talent development requirements and 'significant benefit" payments required in connection with station ownership transfers.

These arguments remain unconvincing. If anything, Pariiament's decision to introduce neighbouring rights may be a reason for reassessing those practices. As for CRTC policies, they serve a different purpose. Copyright protection is granted as a means of ensuring remuneration for the use of all qualifying recordings, while CRTC policies are in response to objectives of the *Broadcasting Act* and concern the creation of new material by Canadians. To discount the remuneration of rights holders because of them would be both improper and unfair.

Artistes-interprètes et producteurs bénéficient davantage du temps d'antenne que *les titulaires de droits* d'auteur

L'ACR a soutenu avec insistance qu'un tarif jute et équitable doit tenir compte des nombreux avantages que les artistes-interprets et productem tirent du temps d'antenne consacré a leun enregistrements sonores. Cette pretention n'a rien de nouveau.

Certes. la radio contribue a la vente de disques. Elle a ete et demeure un véhicule promotionnel important. Cela dit. I'industrie ne diffuse pas les disques dans ce but. mais afin d'exploiter son entreprise, qui consiste a vendre des auditoires aux annonceurs. Comme la Commission I'a dit par le passe dans le contexte de l'exécution pubiique d'œuvres musicales. il s'agit la d'un cas parmi d'autres de rapport symbiotique entre deux industries. sans lien direct avec le prix.

Les stations de radio *contribuent* a *l'industrie du* disque de *plusieun autres façons*

Comme elle l'a fait par le passé a l'égard des droits d'exécution publique d'œuvres musicales, l'ACR a aussi demande a la Commission de tenir compte des diverses contributions directes et indirectes des stations de radio a l'industrie du disque. Cela comprend la promotion en ondes des artistes-interpretes. les contributions financières au developpement du talent local. ainsi que celles découlant des exigences imposées par le CRTC en matiere de developpement des talents canadiens et du «critère relatif aux avantages» lorsqu'il y a transfert de propriété.

Ces arguments demeurent peu convaincants. On pourrait même prétendre que l'introduction des droits voisins demit motiver un réexamen de ces pratiques. Quant aux politiques du CRTC, leur objet est différent. La protection du droit d'auteur vise la rémunération pour l'utilisation de tous les enregistrements admissibles: les politiques du CRTC répondent aux objets de la *Loi sur la radiodiffusion* et visent avant tout la création d'œuvres et d'enregistrements canadiens. Réduire la rémunération des titulaires de droits en raison de celles-ci serait a la fois inopportun et injuste.

3. The approach favoured by the Board

Several reasons lead the Board to conclude that the best *starting* point is SOCAN's present tariff.

First, SOCAN's tariff applies, more often than not, to the use of recorded musical works, while neighbouring rights tariffs apply to the use of recorded performances of the same works. Therefore, they involve a similar use and a similar right in a similar market.

Second, SOCAN's tariff has been in place for a long time; even though it constitutes a regulated price, it is one that the Board simply cannot ignore. As the Board stated in another, similar context:

> ... there is less need to use a proxy when an existing price, even an administered price, *can* be used as a starting point. This is especially true where information is available to determine whether or not the existing price is appropriate, and whether or not any adjustments ought to be made to account for changes in circumstances.[11]

Third, even though SOCAN still maintains that the current rate is too low while *CAB* still argues that it is too high, they have agreed to maintain the *status* goo for five *years*. For whatever the reasons, the 3.2 per cent rate remains the going rate, and we need not speculate as to its correctness for our purposes.

Fourth, all other proxies offered by NRCC are deficient in some ways, and certainly much weaker than SOCAN's tariff.

Fifth, SOCAN'S licence is a blanket licence. Therefore, using SOCAN's rate as a starting point avoids the difficulty of having to determine which value, if any, ought to be attributed to the blanket character of the regime.

3. La demarche aue retient la Commission

Pour plusieurs motifs, la Commission croit que le tarif de la *SOCAN* constitue le meilleur point de départ.

Premièrement, le tarif de la SOCAN vise principalement l'utilisation d'œuvres musicales enregistrées, et les droiu voisins portent *sur* l'utilisation de prestations enregistrées de ces mêmes œuvres. On traite donc d'un usage similaire dans un marché similaire.

Deuxiemement, ce tarif est en place depuis un bon moment. Il s'agit d'un prix réglementé, mais que la Commission ne peuc tout de même pas ignorer. Comme elle l'a deja dit, dans un contexte different mais similaire :

> ... le besoin de recourir a un prix analogue se fait moins sentir s'il existe un prix, même réglementé, pouvant servir de point de depart. Ceci est d'autant plus vrai si l'on dispose de renseignements permettant de determiner si ce prix convient toujours et s'il doit être rajusté pour tenir compte de l'évolution de la situation.[12]

Troisiemement, le tarif actuel vaut pour cinq ans, suite a une entente, malgré le fait que la SOCAN continue de soutenir qu'il est trop bas et que l'ACR pretende le contraire. Peu importe leurs motifs, le taux de 3,2 pour cent est le taw en vigueur, et il n'est pas nécessaire pour nos fins de mettre en doute son bien-fondé.

Quatrièmement, les comparaisons effectuées par la SCGDV comportent touts certaines faiblesses, et sont de toute maniere beaucoup moins valables que la comparaison avec le tarif de la *SOCAN.*

Cinquièmement, la licence de la SOCAN est une licence générale. En utilisant le taw de la SOCAN comme point de depart, on evite d'avoir à attribuer une valeur distincte, si valeur il y a, au caractère general du régime.

The only issue remaining, therefore, is whether 3.2 per cent is too much, enough or not enough to compensate fairly and equitably performers and makers of sound recordings. As stated earlier, the case put forward by CAB in favour of a reduced rate is not sustainable. Consequently, the only options left are to maintain a one-on-one relationship between the neighbouring rights and the authors' rights or to adjust the rate upwards.

Cela etant, reste a determiner si le taux de 3.2 pour cent suffit a compenser de façon juste et équitable les artistes-interprètes et les producteurs ou s'il faut ajuster ce taux a la hausse ou a la baisse. Comme on a deja conclu que la preuve et l'argumentation mises de l'avant par l'ACR ne sauraient justifier une reduction, les seules possibilités qui s'offrent sont de maintenir la parité entre les deux tarifs ou d'ajuster le taux a la hausse.

NRCC filed evidence tending to establish that royalties paid to performers and makers of sound recordings in free market transactions are approximately 2.5 times higher than royalties paid to authors.[13] Establishing this sort of comparison requires making the assumption that if performers do better than composers in a free market, they should be able to do as well in the other, regulated market. That assumption is not supported by the record of these proceedings. The evidence that performers may provide radio stations with more value than authors is far from conclusive. What the Board was offered in this *respect* was a series of anecdotal, impressionistic statements *that* often pulled either way.

Par sa preuve, la SCGDV a cherche a etablir que les redevances versées de gré a gré aux artistes-interprètes et producteurs dans le marche de la production des enregistrements sonores sont environ 2.5 fois plus élevées que celles versées aux auteurs.[13] Ce genre de comparaison se fonde sur la prémisse que les artistes-interprètes, gagnant davantage que les compositeurs dans un marche libre, devraient pouvoir faire aussi bien dans un marché réglementé. Or, le dossier de la présente affaire ne permet pas de tirer une telle conclusion. La preuve voulant que l'apport des artistes-interprètes aux stations de radio est plus important que celui des auteurs est loin d'être concluante. Les témoignages offerts a ce sujet constituent tout au plus des anecdotes ou des impressions et pourraient dans certains cas servir tout aussi bien a établir le contraire.

For example, Ms. Smith and Ms. Kondruk, who are experienced advertising executives, testified to the effect that music is very personal to people, that radio is a niche medium, that advertisers pay for audiences, who in turn are drawn by music format. Such statements, in so far as they establish anything useful, are hardly helpful to NRCC, who wishes to show the importance of individual performers by contrast to the overall music format. In the same vein, their assertion that stations advertise themselves using the music format and the artist's image does not mean that the artist's image has higher promotional value than the music format: the image is but a tool to help identify the format.

Ainsi, selon mesdames Smith et Kondruk, deux agents de publicité d'expérience, la musique est quelque chose de personnel et la radio est un organe de diffusion spécialisé; les annonceurs paient pour un auditoire attiré par le format musical. De telles affirmations, pour autant qu'elles prouvent quoi que ce soit, n'aident en rien la SCGDV, qui tente de démontrer l'importance des artistes-interprètes et non du format musical. Dans le même ordre d'idées, l'affirmation selon laquelle les stations utilisent le format musical et l'image des artistes-interprètes pour faire leur propre promotion ne signifie pas que les artistes-interprètes ont une valeur promotionnelle plus grande que le format musical; de fait, l'image sert également a identifier le format.

For their part. Messrs. Lefebvre and Stein-Sack. who have long worked in the area of records sales and distribution. offered the view that while a record starts with a song. the magic (in the form of a symbiosis between the song, the performance and the production) must be there for the record to sell, adding that the songwriter is the most fragile, least visible and least compensated contributor in the whole process of production and *sales* of records. Again. such impressionist statements, which in any event go to the relative contributions of participants in the records market, are of little help in determining the relative value of recordings to radio stations.

Pour leur part, messieurs Lefebvre et Stein-Sack. qui travaillent depuis longtemps dans le domaine de la vente et de la distribution d'enregistrements sonores affirment que, s'il est vrai de dire que sans chansons. il n'y a pas d'enregistrement qui vaille. la magie (cette symbiose entre la chanson. la prestation et la production) doit être là pour que le disque se vende. Et ils ajoutent que le compositeur est. de tous les collaborateurs dans le processus de production et de vente d'un enregistrement. le plus fragile. le moins visible et le moins bien rémunéré. Encore ici. ce genre d'affirmations. qui portent en outre sur la contribution relative des participants dans le marché du disque. ne sont guère utiles pour etablir la valeur relative des enregistrements sonores dans le marché de la radiodiffusion.

In the end, it was probably Mr. Reynolds. president of Universal Music Canada, who best stated the conundrum. when he expressed the view that establishing the relative value of the authors' and performers' contribution in a successful recording "is the classic chicken and egg situation. I don't think you *can* extricate the two and say. this *is* more important than that."[14]

En definitive. c'est *sans* doute M. Reynolds. président d'*Universal Music Canada,* qui a le miew formule le dilemme. À son avis, tenter de determiner l'importance relative des compositeurs et des artistes-interprètes au succès d'un enregistrement. [TRADUCTION] «c'est s'engager dans le debat classique de la poule et de l'oeuf. Je ne crois pas qu'on puisse les isoler et pouvoir dire : celui-ci est plus important que celui-là.»[14]

The Board prefers deciding on the basis that there is no reason to believe that the use of sound recordings on radio stations has any greater value than the use of the underlying works. Several reasons point to this solution. First, nothing requires the Board to look *to* the market (and especially a different market) for guidance: it is within its discretion to decide that this approach is reasonable.[15] Second, these are similar uses of the same recordings by the same broadcasters. Third. it *can* be readily argued that a pre-recorded performance is worth no more *to* broadcasters than a pre-recorded work: in both cases *one* is dealing with something *that* has *already* been fixed. Fourth, it matters not that *one* party was paid more than the other for making the fixation in the first place; we are dealing with two different markets and two different rights: the right to make the recording and the right to communicate it.

La Commission estime qu'il n'y a pas de raison de croire qu'à la radio les enregistrements sonores ont une valeur supérieure aux œuvres enregistrées, et ce pour plusieurs motifs. D'abord, rien n'oblige la Commission a se guider sur les prix du marché, surtout s'il s'agit d'un marché different: son pouvoir d'appréciation lui permet d'adopter toute autre démarche raisonnable.[15] Deuxièmement, il s'agit des mêmes utilisations. des mêmes enregistrements et des mêmes radiodiffuseurs. Troisièmement, on peut facilement soutenir qu'une prestation pré-enregistrée n'apporte ni plus, ni moins au radiodiffuseur qu'une œuvre pré-enregistrée : dans un cas comme dans l'autre. il s'agit de quelque chose qui a deja ete fixé. Quatrièmement, il importe peu qu'un des participants ait reçu davantage qu'un autre pour la fixation de l'enregistrement; nous sommes en présence de marchés distincts et de droits différents a savoir, le droit de faire l'enregistrement et celui de le communiquer.

4. The tariff rate

For the foregoing reasons, the Board concludes that most commercial radio stations should pay 45 per cent of what they pay to *SOCAN*, or 1.44 per cent of their advertising revenues, for the neighbouring rights.

All participants agree that stations that qualify as low music use stations for the purposes of the SOCAN tariff should pay 43.75 per cent of the royalties payable by other stations. Consequently. the rate for low music use stations (as defied by the participants) is set at 0.63 per cent.

On the other hand, participants disagree on the need for an even lower rate for all-talk stations. NRCC opposes the concept on the basis that SOCAN's tariff does not allow for it, that CAB has offered no evidence as to the number of stations that might be in this category and that the concept lacks sufficient clarity to be workable. For the following reasons, the Board grants CAB's request. First, the Board is satisfied that stations which do not use any eligible sound recordings other than production music should pay little neighbouring right royalties. if any. Second, this approach *makes* sense in this context, while it may not in SOCAN's tariff, given the nature of the respective repertoires. Third. the number of stations that will fall in that category is probably very small. Consequently, there is little risk involved in trying *the* formula. Having said *this*, the rate is set on a monthly. rather than yearly basis so as to better harmonize with the structure of the tariff. as will be outlined later.

5. The ability of the industry to pay the tariff

The tariff as certified by the Board would yield royalties of 11.29 million dollars per year[15] over the period of the tariff (1998 to 2002), if the 1997 figures on advertising revenues (the only

4. Le taux

La Commission en vient donc a la conclusion que le taux payable par la plupart des stations de radio commerciale pour les droits voisins devrait être fixé a 1.44 pour cent de leurs recettes publicitaires. soit 45 pour cent du taw de la *SOCAN.*

Tous s'entendent pour dire que les stations ayant droit au statut de petit utilisateur pour les fins du tarif de la SOCAN dement payer 43.75 pour cent de ce que versent les autres stations. Le taw pour ces stations. tel que les parties l'ont defini. est donc fixé a 0.63 pour cent.

Par contre. les participants ne s'entendent pas sur le besoin d'accorder un taw encore plus avantageux pour les stations de radio parlée. La SCGDV s'y oppose pour plusieurs motifs. Le tarif de la SOCAN ne prevoit pas de mesure semblable; l'ACR n'a pas etabli le nombre de stations qui pourraient bénéficier de la mesure; enfii le concept est trop vague pour être fonctionnel. La Commission fait droit a la demande de l'ACR pour les motifs suivants. Premièrement, la Commission est convaincue que les stations n'utilisant pas d'enregistrements sonores admissibles a part la musique de production devraient verser peu ou pas de redevances. Deuxièmement, vu la composition des repertoires concernés, la mesure se justifie en matiere de droits voisins même si elle n'est pas nécessairement indiquée dans le cas de la *SOCAN.* Troisièmement, comme très peu de stations pourront vraisemblablement s'en prevaloir. le fait d'expérimenter la formule comporte peu de risques. Cela dit, afin d'harmoniser davantage la mesure avec la structure tarifaire dont il sera question plus loin. ces stations seront assujetties a une redevance mensuelle et non annuelle.

5. La capacité de l'industrie de payer le tarif

Le tarif que la Commission homologue entraînerait le versement de 11.29 millions de dollars par année.[15] pendant la durée du tarif (1998 a 2002). en utilisant et tenant constantes les figures available at the time of the hearing) were used and remained constant over that period. Yet the application of subparagraph 68.1(1)(a)(i) of the *Act*. stipulating that commercial radio stations shall only pay $100 on their first 1.25 million dollars of annual advertising revenues. would reduce that amount to 5.68 million dollars. In addition. the phasing in of the regime over three years, would further reduce that amount to 1.89 million dollars in 1998 and to 3.78 million dollars in 1999.

The evidence provided by NRCC. and especially Exhibit NRCC-29. clearly established that the industry could have absorbed the full tariff, absent any special statutory provisions. Indeed. neither CAB nor its witnesses took issue with the validity or quality of NRCC's evidence on this point, Instead, CAB argued that NRCC's tariff as filed would deprive the industry of its recent hard-won profit margins. and would thereby deny it the investment capital needed to convert to digital technology and meet the competitive challenge posed by other major media.

The industry as a whole has come out of difficult years. Profit margins have grown and would have allowed the industry to absorb all of the tariff. Only small stations would have been put in difficulty: since Parliament has already addressed the issue, there is no need for the Board to do so. In the end, the fact that all stations will pay only $100 on account of their first 1.25 million dollars in advertising revenues, the level of the rate as set by the Board and the fact that there will not be a graduated tariff all combine to confirm that commercial radio stations will be able to afford the price they now have to pay for the neighbouring rights.

recettes publicitaires réalisées par l'industrie en 1997 (seules données disponibles lors de l'audience). Toutefois. l'application du sous-alinéa 68.1(1)(a)(i). qui prevoit le paiement de seulement 100 $ par les stations de radio commerciale sur la partie de leurs recettes publicitaires ne dépassant pas 1.25 million de dollars, réduit ces redevances a 5.68 millions de dollars et les mesures transitoires prévues a la *Loi* les ramènent a 1.89 million de dollars en 1998 et a 3.78 millions de dollars en 1999

La preuve déposée par la SCGDV. et tout particulièrement la pièce NRCC-29, demontre clairement que l'industrie aurait eu les moyens d'aquitter le plein tarif sans egard aux dispositions spéciales de la *Loi*. D'ailleurs. ni l'ACR ni ses temoins n'ont remis en question la validite ou la qualite de la preuve de la SCGDV a cet égard. L'ACR a plutôt soutenu que le projet tel qu'il a ete déposé annulerait les récentes marges bénéficiaires de l'industrie, gagnées de haute lutte, la privant ainsi du capital de placement dont elle a besoin pour passer a la technologie numerique et pour faire face aux défis concurrentiels posés par les autres médias d'importance.

L'industrie a connu récemment des années difficiles. Toutefois. ses marges bénéficiaires ont augmente et lui auraient permis d'acquitter le plein tarif. Seules les petites stations auraient connu des difficultés; or. comme le Parlement a déjà prévu des mesures a cet égard, la Commission n'a pas a s'en préoccuper. En bout de piste. le fait que toutes les stations ne versent que 100 $ sur la partie de leurs recettes publicitaires ne dépassant pas 1.25 million de dollars et que le tarif homologué ne soit pas un tarif gradué ne font que confirmer que les stations de radio commerciale auront bel et bien les moyens d'acquitter les redevances qu'elle devront payer a l'avenir pour les droits voisins.

VI. ISSUES RELATED TO THE COLLECTION AND STRUCTURE OF THE TARIFF

A. Who should collect the royalties?

NRCC wishes to collect all royalties payable under the tariff. SOGEDAM asks to receive the share attributable to its repertoire. Dealing with the issue of allocation raises two issues. What is the meaning of the single payment requirement set out in subparagraph 68(2)(a)(iii) of the *Act*? Can the Board direct users to pay SOGEDAM its share of the remuneration right?

1. The single payment requirement

In the Board's view, the arguments in favour of interpreting the single payment requirement as directing the Board to identify a single entity that will collect royalties on account of all the repertoire entitled to remuneration are overwhelming.

Thus, the requirement exists first and foremost for the benefit of uses. Interpreting the single payment requirement in this way is congruent with this benefit.

Second, this interpretation gives meaning to subparagraph 68(2)(a)(iii) of the *Act*. If the single payment requirement were to mean anything less, then subsection 19(2) of the *Act*, which already limits to one the payment to be made on account of any given recording, would have been sufficient.

Requiring that users make only one payment for the whole repertoire does not contradict the right of collectives to each file tariff proposals. The ability to ask for a tariff can readily be distinguished from the ability to act as collecting agent, as the home taping regime clearly demonstrates. Neither is it incompatible with a tariff that creates different structures for different parts of the repertoire. The Board could easily certify a tariff which has, say, a different price

VI. QUESTIONS LIÉES À LA PERCEPTION DES REDEVANCES ET À LA STRUCTURE TARIFAIRE

A. Qui devrait percevoir les redevances?

La SCGDV désire percevoir toutes les redevances exigibles en vertu du *tarif*. La SOGEDAM demande de percevoir la part qui revient a ses membres. Pour décider de la repanition, il faut trancher deux questions. Qu'entend-on par versement unique au sous-alinéa 68(2)*(a)*(iii) de la *Loi*? La Commission peut-elle ordonner aux utilisateurs de verser a la SOGEDAM sa pan du droit a rémunération?

1. L'exigence du versement unique

La Commission croit que l'exigence du versement unique l'oblige a désigner une seule entite responsable de la perception des redevances pour l'ensemble du repertoire ayant droit a rémunération et trouve les arguments au soutien de cette interpretation particulièrement convaincants.

Ainsi, si cette exigence existe, c'est d'abord et avant tout pour le bénéfice des utilisateurs. L'interpretation retenue par la Commission confiie cet avantage.

Deuxièmement, cette interpretation donne un sens au sous-alinéa 68(2)(a)(iii) de la *Loi*. Le paragraphe 19(2) de la *Loi*, en limitant à un seul le versement devant être effectué a l'égard de toute utilisation donnée d'un enregistrement donné, aurait suffi si l'obligation du versement unique devait signifier moins.

Permettre aux utilisateurs d'effectuer un seul paiement pour tout le répertoire ne prive pas chaque societe du droit de deposer un projet de tarif. Comme le régime de la copie privée le démontre clairement, on peut facilement etablir une distinction entre le droit de proposer un tarif et celui d'agir à titre de societe de perception. Cette interprétation n'écarte pas non plus la possibilité d'établir des structures tarifaires differentes pour differences parties du répenoire.

formula for SOGEDAM's repertoire than for NRCC's and still require that radio stations only pay at one designated place.

Consequently, the Board concludes that the single payment requirement entitles users to pay to a single collecting agent. Given that NRCC brings with it, through the makers it represents, all of the eligible repertoire that is properly before this Board, it is only logical to have it act as that collecting agent.

There are also practical reasons for selecting NRCC as the sole collecting agent for all royalties. First, NRCC controls all of the makers' rights in the repertoire entitled to remuneration. Second, this is the most efficient and practical way of dealing with the situation. NRCC is better placed than SOGEDAM to distribute royalties to all interested rights holders. Third, even in so far as French rights holders are concerned, SOGEDAM (who represents only some of the performers) has less at stake than NRCC, who represents all makers. Fourth, NRCC is likely to be better organized to manage the tariff for all concerned, including the monitoring of stations across the country, and the creation of appropriate databases for distribution purposes.

The Board is conscious that *NRCC* may be in a position to use its *status* as the only authorized collective in an attempt to force SOGEDAM to accept certain distribution practices which are the very reason why SOGEDAM was *created* in the first place. Unfortunately, the Board is there, first and foremost, to regulate the balance of market power between users and rights owners, and not, unless the *Act* says otherwise, between rights owners. SOGEDAM should direct any complaints it may have in this respect to the Commissioner of Competition.

Ainsi, la Commission pourrait fort bien homologuer une formule tarifaire pour le repertoire de la SOGEDAM et une autre pour celui de la SCGDV tout en ordonnant aux stations de radio de verser la totalite des redevances a une seule personne.

La Commission en vient donc a la conclusion que l'exigence du versement unique donne aux utilisateurs le droit de verser les redevances a un seul agent de perception. Compte tenu que la SCGDV, grâce aux producteurs qu'elle représente, fait apport de tout le repertoire admissible dont la Commission est saisie, il est tout a fait logique de la désigner pour agir a ce titre.

Des motifs pratiques amenent aussi la Commission a désigner la SCGDV comme agent de perception unique. Premièrement, elle fait apport des droits de tous les producteurs ayant droit a la rémunération. Deuxièmement, il s'agit de la façon la plus efficace et la plus pratique de régler la situation. La SCGDV est plus en mesure que la SOGEDAM de répartir les redevances parmi tous les intéressés. Troisiemement, même a l'égard des titulaires français, l'enjeu pour la SOGEDAM, qui ne représente qu'une partie des artistes-interprètes, est moindre que pour la SCGDV, qui représente tous les producteurs. Quatriemement, la SCGDV paraît mieux équipée pour gerer le tarif pour le bénéfice de tous les intéressés, qu'il s'agisse de la vérification des stations a travers le Canada ou de la mise sur pied de bases de données pour fins de distribution.

La Commission est consciente du fait que la SCGDV pourrait utiliser son statut d'unique agent de perception pour tenter d'amener la SOGEDAM à accepter certaines règles de distribution qui sont a l'origine même de la création de cette dernière. La Commission existe d'abord et avant tout pour maintenir l'équilibre économique entre utilisateurs et titulaires de droits: à moins que la *Loi* ne prévoie le contraire, elle ne se mêle pas des différends entre titulaires. Si la SOGEDAM devait se sentir lésée à cet égard, elle devra s'adresser au Commissaire de la concurrence.

2. Can the Board direct users to pay SOGEDAM its share of the remuneration right?

Given the interpretation the Board makes of the single payment requirement. it is obviously impossible for it to direct users to pay SOGEDAM its share of the remuneration right in the recordings onto which its members' performances are embedded.

This interpretation is supported by subsection 19(3), according to which the division of royalties between performers and makers takes place once the royalties have been paid. The need for such a division, and the fact that it *occurs* after collection, applies to all equitable remuneration. whether or not it is subject to the *SOCAN* regime and whether or not the Board is involved in setting a tariff. If the division of royalties must occur after the payment is made, that division cannot occur before.

This interpretation means that SOGEDAM's members cannot collect their remuneration right directly from the users through their society of choice. This is merely a facet of the economy of the statute, and is no worse than requiring the maker of a sound recording of a dramatic work to claim his share of the royalties from the performer if they were paid to the performer. or vice versa.

B. Can the Board determine the share SOGEDAM should receive?

SOGEDAM also would like that the Board set its share of the royalties. The Board is of the view that it cannot decide how co-creditors are to apportion the royalties among themselves.

Generally speaking, when the *Act* requires that the Board apportion royalties between collectives representing different groups of right owners. this is done expressly.[17] This is not the case here.

2. La Commission peut-elle ordonner aux utilisateurs de verser a la SOGEDAM sa part du droit a rémunération?

L'interprétation que la Commission retient du principe du versement unique rend impossible d'exiger que les utilisateurs versent a la SOGEDAM sa quote-part du droit a remuneration.

Cette conclusion est soutenue par la version anglaise du paragraphe 19(3), qui prevoit la repartition des redevances entre artistes-interprètes et producteurs après qu'elles aient ete versées. L'exigence de partage et le fait qu'il intervienne après la perception sont des conditions s'appliquant a toute rémunération équitable, assujettie ou non au régime de la SOCAN et sans egard au fait que la Commission soit appelée a etablir le tarif. Si le partage survient après la perception, il ne peut intervenir avant.

Par conséquent, les membres de la SOGEDAM ne peuvent percevoir leur droit a rémunération directement des utilisateurs par le truchement de la societe qu'ils ont choisie. Il s'agit la tout simplement d'une conséquence logique de l'économie du régime, qui n'est en rien plus choquante que l'exigence imposée au producteur de l'enregistrement sonore d'une œuvre dramatique de réclamer sa part des redevances auprès de l'artiste-interprète lorsque ce dernier les a perçues, et vice-versa.

B. La Commission peut-elle établir la quote-part de la SOGEDAM?

La SOGEDAM demande aussi à la Commission d'établir sa quote-part des redevances. La Commission croit qu'elle ne peut décider a la place des co-créanciers la façon dont ils entendent répartir le produit des redevances entre eux.

Règle générale, lorsque la *Loi* exige que la Commission répartisse les redevances entre sociétés représentant différents groupes d'ayants droit. elle le prévoit de façon expresse.[17] Elle ne

Furthermore. in regimes such as private copying. where such an apportionment is required, the *Act* does not establish in advance the shares attributable to the various colleges of rights owners: each group is entitled to claim the full value of its contribution, however established. By contrast. the neighbouring rights regime expressly provides for a single remuneration to be shared equally between performers and makers.

Moreover. nothing in the *Act* would allow the reader to infer a power of the Board to determine SOGEDAM's share of royalties as a necessary incident to setting the neighbouring rights tariff. As the regime is structured, the Board sets the royalties to be paid for the use of all sound recordings that are entitled to remuneration. Once this is done, the *Act* mandates equal sharing of the royalties between performers and maken. It is only once that split has occurred that the Board would come in if it were to determine SOGEDAM's share. that is. to determine how, as between those sharing in the performer's share, the entitlement to half the royalties should be divided. This is one step too far removed.

Finally, the Federal Court of Appeal has already ruled that the Board should not get involved in the allocation of liability between codebtors: [11]

> the apportionment of the sums *payable ... between those who are,* by law. ... *obliged to pay them* does not involve the determination of a royalty or of a term or condition relating to a royalty. *The sums that the various participants ... may owe to each other* are not royalties even though they are payable as a consequence of the payment of *the* royalties by one of them. The Board, therefore, was right in deciding that it lacked the jurisdiction to make that apportionment. [our emphasis]

One need only to substitute the word 'share' for "pay" to make this statement applicable to the issue at hand. That decision precludes the Board From getting into any division exercise that is not essential to the operation of the regime.

l'a pas fait dans ce cas-ci. Par ailleun. les regimes, tel celui de la copie privée. qui prevoient ce genre de répartition, ne fixent pas a l'avance les parts attribuables aux divers colleges d'ayants droit. chacun etant autorisé a réclamer la pleine valeur de son appon. peu importe la façon dont cette valeur est déterminée. Par contre. le régime des droits voisins prévoit expressément la repartition par moitie de la rémunération unique entre artistes-interprets et producteun.

Quiplus est. rien dans la *Loi* ne permet de conclure que la Commission a le pouvoir de fixer la quotepart de la SOGEDAM en tant qu'accessoire nécessaire a l'etablissement du tarif des droits voisins. Tel que *structure.* le régime exige que la Commission determine les redevances qui seront versées pour l'utilisation de tous les enregistrements sonores ayant droit a remuneration. Une fois cette étape franchie, la *Loi* stipule le partage par moitié des redevances. C'est donc après ce partage que la Commission interviendrait si elle était appelée a etablir la quotepart de la SOGEDAM. autrement dit pour répartir entre les artistes-interprets la moitie des redevances qui leur revient. À ce stade. le mandat de la Commission est deja épuisé.

Enfin. la Cour d'appel fédérale a deja exhorté la Commission de ne pas se mêler de la répartition de la responsabilité entre co-débiteurs : [11]

> la repartition des sommes *payables... entre les personnes qui sont,* en droit, *solidairement tenues de les payer* ne compone pas la détermination d'un droit ou d'une modalité y afférente. *Les sommes que les différentes personnes intéressées... peuvent se devoir mutuellement ne* sont *pas* des droits mtme si elles sont payables en raison du paiement des droits par l'une d'elles. La Commission a donc eu raison de statuer qu'elle n'avait pas compétence pour faire cette répartition. [l'italique est de nous]

Qu'on parle de répartition de créances ou de répartition de dettes, le principe reste le même. Cene décision empêche la Commission de s'engager dans tout exercice de repartition non essentiel au fonctionnement du regime.

Consequently, it will be for SOGEDAM to claim its members' share from NRCC. as co-creditors of the royalties collected by NRCC.

Par conséquent, il faudra que la SOGEDAM s'adresse a la SCGDV pour réclamer la pan qui revient a ses membres a titre de co-&ancien des redevances que cene derniere aura perçues.

C. Tariff Structure

C. La structure tarifaire

The following comments may help in understanding the tariff wording.

Les commentaires qui suivent permettront de mieux comprendre le libelle du tarif.

1. Phasing in

1. Durée de la période de transition

Given the nature of the tariff approved by the Board. there is no need to examine NRCC's proposal that the tariff be phased-in over five years instead of three.

La nature du tarif que la Commission homologue fait en sone qu'il n'est pas nécessaire de debame de la proposition visant a prolonger la période de transition a cinq ans.

2. A graduated tariff

2. Un tarif graduel

NRCC put forward several arguments in favour of a graduated tariff. Profit margins tend to increase rapidly with advertising revenues, so the structure is more sensitive to the financial circumstances of stations at various levels of revenue. Convenely, a flat rate would create an unnecessary burden to smaller. less profitable stations. Ability to pay is reflected in the entire tariff; all stations pay at the same rate for the same level of revenues.

La SCGDV a mis de l'avant plusieun arguments au soutien d'un tarif graduel. Généralement parlant, les marges bénéficiaires des stations augmentent rapidement en fonction de leun recettes publicitaires: cene structure répondrait donc davantage aux besoins financiers des stations selon leur taille. Réciproquement, un taux fie imposerait aux stations plus petites, et moins profitables. un fardeau excessif. Un tarif gradueI tient compte de la capacite de payer et chaque station paie le mÔme taw pow une tranche donnée de revenus.

CAB is opposed to the proposal on a number of grounds. First. if, as NRCC seems to accept, the value of sound recordings as a percentage of revenue is constant for all stations regardless of size, a graduated tariff imposes on certain stations. tariff obligations which exceed the value of the repenoire. Second, a flat rate tariff is the only way that equity can be assured to all participants. and is consistent with SOCAN's Tariff I.A. Third, all CAB stations support a flat rate tariff.

L'ACR s'oppose a cette proposition pour plusieun motifs. Premierement. si, c o m e la SCGDV semble convenir, la valew de l'enregistrement sonore. mesurée en pourcentage des recettes, est constante sans égard à la taille de la station. un tarif graduel impose a certaines d'entre elles des obligations tarifaires dépassant la valeur du répertoire pour celles-ci. Deuxièmement, un taw fixe est le seul qui soit équitable pour tous les participants et s'harmonise avec le tarif I.A de la SOCAN. Troisiemement. toutes les stations membres de l'ACR demandent un tarif à taw fixe.

The Board agrees with CAB's reasons for rejecting a graduated tariff. and adds the following.

La Commission est d'accord avec les motifs mis de l'avant par I'ACR pour rejeter une structure tarifaire graduelle. Elle ajoute ce qui suit.

First, cross-subsidization may be justified to avoid the predictable negative response to a tariff by those who have to pay it and the undesirable impact that this may have on well established public policies. Such was the case with the retransmission of distant radio and television signals, where the risk of signal dropping and the need to ensure the provision of similar television services in all regions of the country were significant factors in requiring all systems to pay the same price irrespective of the number of distant signals *carried.* It is not the case here.

Premierement, l'inter-financement se justifie lorsqu'il sen a prévenir les réactions negatives prévisibles de la part de cew qui sont appelés a payer un tarif ou encore, a eviter les conséquences néfastes qu'il peut avoir sur des politiques publiques existantes. C'est pourquoi la Commission a agi c o m e elle I'a fait en matiere de retransmission de signaw eloignes de radio et de television; le risque d'abandon de certains signaw et le besoin de s'assurer que touts les regions du pays bénéficient d'un service télévisuel similaire ont ete des facteurs importants dans la décision d'exiger que tous les systemes paient le même prix sans egard au nombre de signaw éloignés offerts. Ces risques n'existent pas dans la présente affaire.

Second, cross-subsidization may also be justified to ease the financial burden of less profitable entities. However, if smaller stations truly require a break, it need not be at the expense of larger stations. More importantly, in the present instance, Parliament has already taken care of the problem for stations with revenues below 1.25 million dollars.

Deuxièmement, l'inter-financement peut aussi servir a alléger le fardeau financier incombant a des entreprises moins profitables. Cela dit, si les stations plus petites ont veritablement besoin d'un rabais, cela ne veut pas dire que les stations de plus grande envergure devraient en faire les frais. Et surtout, dans l'espèce, le Parlement a déjà réglé le probleme pour les stations dont les recenes n'excèdent pas 1.25 million de dollars.

Third, NRCC's proposed cross-subsidization is justified only because of the high price demanded for its repertoire. With the lower tariff that the Board certifies, the need to find ways to reduce the burden on smaller stations is simply not there.

Troisiemement, l'inter-financement que propose la SCGDV est rendu nécessaire uniquement par le prix qu'elle demande pour l'utilisation de son repertoire. Le tarif que la Commission homologue élimine tout besoin de réduire le fardeau des stations plus petites.

Fourth, adopting similar tariff structures for musical works and sound recordings will facilitate comparisons between the two tariffs.

Quatrièmement, l'adoption de structures similaires pow les tarifs applicables aux œuvres musicales et a w enregistrements sonores rendra plus faciles les comparaisons entre les deux tarifs.

CAB is also correct in saying *that* NRCC's proposal, as filed, runs contrary to Parliament's intent that all stations pay only $100 on their first 1.25 million dollars of advertising revenues. NRCC applied its proposed average rate to all revenues, including those covered by the special rate, and then devised a grid that would generate the same total royalties. As a result, the industry ends up paying more than the average rate on revenues not covered by the special rate, which

L'ACR a aussi raison de prétendre que la proposition de la SCGDV, telle qu'elle *est* formulée, va a l'encontre de la mesure législative permettant a touts les stations de verser uniquement 100 $ sur la partie de leurs recettes publiatairesne dépassant pas 1.25 million de dollars. Pour dériver sa grille tarifaire, la SCGDV s'est servie du taux moyen qu'elle propose pour ensuite l'appliquer a l'ensemble des recettes de l'industrie, plutôt qu'a la partie excédant les 1.25

alone ought to be used in establishing the return offered by the tariff irrespective of the formula used.

million de dollars par station. Cela fait en sone que l'industrie dans son ensemble se trouve a verser davantage que le taux moyen sur les retenes non visées par le tarif spécial. Seules ces dernieres devraient servir a etablir le rendement du tarif. et cela qu'il s'agisse d'un tarif a taw fixe ou d'un tarif graduel.

3. Duration of the tariff

For many reasons, the Board concludes that the tariff should be set for five years instead of three. First. given the relationship the Board establishes with SOCAN's rate of 3.2 per cent, and the fact that CAB and SOCAN have agreed to maintain that rate for the next five years, there would be no point in reopening the neighbouring rights tariffs before then. Second. a five-year tariff keeps open the possibility of a joint hearing when the two tariffs expire in 2002. Third. five years should allow the market to adjust to the new reality: it would also allow the Board to make more useful observations on its real impact before embarking on a revision: better databases could also be put in place during that time. No one's interest would be served by putting this tariff back on the front burner after only a few months of its approval.

3. La durée du tarif

Pour plusieun motifs. la Commission croit que le tarif devrait être homologue pour cinq années plutôt que trois. Premierement, vu le rapport que la Commission etablit entre le tarif de la SOCAN et celui des droits voisins. il n'y a pas lieu de rouvrir ce dernier avant l'expiration du premier. Or, l'ACR et la SOCAN ont convenu d'une période de cinq ans. Deuxièmement. un tarif de cette durée permet, si la Commission lejuge nécessaire, d'entendre en même temps les deux tarifs lorsqu'ils viendront a échéance en l'an 2002. Troisiemement. cette période de temps devrait permettre au marché de s'ajuster a la mesure. tout en permettant à la Commission de se livrer a des observations plus utiles sur son impact réel avant de procéder a un réexamen: elle pourra aussi servir a mettre au point de meilleures bases de données. Enfii, personne n'a intérêt a réactiver le débat sur ce tarif quelques mois a peine après son homologation.

4. General structure of the tariff

The proposed statement NRCC filed was largely based on the Retransmission tariff. The Board has preferred following the model set out in SOCAN's Tariff 17 (Transmission of Pay, Specialty and Other Cable Services). In some cases. however, provisions are closer to the Retransmission tariff (ss. 12 and 13) or are added to deal with needs that are specific to the neighbouring rights regime (s. 4).

4. La structure générale du tarif

Le projet de tarif de la SCGDV reflétait dans une large mesure la structure du tarif de la retransmission. La Commission a préféré s'inspirer du tarif 17 de la SOCAN (Transmission de services par câble, y compris les services de télévision payante et les services spécialisés). Toutefois. quelques dispositions se rapprochent davantage du premier tarif (aa. 12 et 13) ou traitent de questions se soulevant uniquement dans le cadre du régime des droits voisins (a. 4).

5. Qualifying for a lower rate

The definitions used are those proposed by participants. Thus. qualifying for the low-use rate

5. Comment etablir si on se qualifie pour un taux plus bas

Les définitions retenues sont cells mises de l'avant par les participants. Par conséquent, le is entirely a function of so qualifying for the purposes of SOCAN's tariff. and all-talk stations are defined using language proposed by CAB.

As in SOCAN's tariff. a station must. as a condition of the tariff. keep and make available complete recordings of its last 90 broadcast days in order to qualify for a lower rate. The imponance of the benefit stations derive from these measures justify making it such a requirement.

6. A monthly tariff

As indicated in section 3 and other provisions of the tariff, royalties are to be calculated and paid monthly. This presents several advantages. First. it means that all calculations can be made on the basis of the reference month, the definition of which reflects SOCAN's tariff structure. Second. it avoids the need to estimate royalties and make corrections. Third, this allows a station to move from one format to another without having to take into account considerations that may be linked to the fact that the tariff is partly on a monthly basis, and partly on a yearly one.

For the same reasons. the rate for all-talk stations is set at $100 per month.

7. Taking into account the special provisions of subsection 68.1(1) of the *Act*

The tariff structure *takes* no account of the special provisions contained in subsection 68.1(1) of the *Act*. Instead. reference is made to it in section 4 of the tariff. These provisions apply "notwithstanding the tariffs approved by the Board". It is therefore appropriate that the tariff reflect what the Board would have considered fair and equitable absent those provisions.

It is also not necessary to specify how the stations are to take advantage of subparagraph 68.1(1)(a)(i) of the *Act*. Stations pay $100 on

statut tie station a faible utilisation est relié directement a celui qui prévaut aux fins du tarif de la *SOCAN*, et la definition de station de radio parlée reprend la formulation mise de l'avant par l'ACR.

Comme c'est le cas pour la SOCAN. la station se réclamant d'un taux plus bas est tenue. comme condition du tarif. de conserver et de mettre a la disposition de la SCGDV l'enregistrement complet de ses 90 dernieres journées de radiodiffusion. L'avantage que tirent les stations qui se prevalent de ce tarif justifie cene mesure.

6. Un tarif mensuel

L'article 3 et certaines autres dispositions du tarif établissent que les redevances sont calculées et versées a chaque mois sans egard au taux applicable. Cene facon de procéder comporte plusieurs avantages. Tous les calculs peuvent être effectués en utilisant le même mois de référence qui sert au tarif de la *SOCAN*. On n'a pas ainsi a estimer les redevances ou a procéder a des ajustements. Enfin, la station qui changerait sa formule de programmation en cours d'année n'aura pas a tenir compte des incidences découlant d'un tarif fondé partiellement sur une base mensuelle, et partiellement sur une base annuelle.

Pour ces mêmes motifs, le taux pour les stations de radio parlée est etabli à 100 $ par mois.

7. La prise en compte des dispositions spéciales du paragraphe 68.1(1) de la *Loi*

La structure tarifaire ne *tient* aucun compte des dispositions spéciales du paragraphe 68.1(1) de la *Loi*. On s'est contenté d'y référer dans l'article 4 du tarif. Ces dispositions s'appliquent «par dérogation aux tarifs homologués par la Commission». Il convient donc que le tarif reflète ce que la Commission aurait considéré être juste et équitable n'eût été de ces dispositions.

Il n'est pas non plus nécessaire de spécifier la façon dont les stations peuvent se prévaloir du sous-alinéa 68.1(1)(a)(i) de la *Loi*. Le texte their first 1.25 million dollars of advertising revenues. In the Board's view, this means that the payment obligations imposed in the tariff only come into operation once a station's revenues exceed that sum. Moreover, trying to build in the exception into the tariff would have made it unduly complicated. By contrast, if the exception is applied the way the Board thinks it ought to be, the structure is simple, as are the rules. Stations will simply have to take note of the point in the year where they cross the revenue threshold and conduct themselves accordingly. The fact that this will mean that NRCC will receive little during the first few months of the year is a direct result of clearly expressed parliamentary intent.

stipule que les stations ne versent que 100 $ sur la partie de leurs recettes publicitaires n'excédant pas 1.25 million de dollars. La Commission est d'avis que l'obligation de paiement imposée par le tarif entre en jeu uniquement lorsque les recettes d'une station dépassent ce seuil. Par ailleurs, tenter de prévoir un mécanisme qui prenne en compte cette disposition aurait rendu le tarif inutilement compliqué. Si l'exception opère ainsi que la Commission le croit, la structure tarifaire est simple, tout comme ses règles d'application. Les stations n'ont qu'à surveiller le moment à partir duquel elles dépassent le seuil et à se gouverner en conséquence. Le fait que les revenus de la SCGDV seront conséquemment très faibles durant les premiers mois de l'année découle directement de choix clairement exprimés par le législateur.

8. Reporting requirements

The reporting requirements are more or less on line with what the participants agreed to. The following issues are worth mentioning.

A) The requirement to provide play lists is included in the tariff, even though this is done voluntarily in the case of SOCAN. The difficulties NRCC experienced in getting information from some stations (who may not be members of CAB) amply justify making this a compulsory aspect of the regime.

The number of days for which stations must provide the information is set at 14, as is customary with SOCAN, rather than the 21 asked by NRCC. The provision is drafted so as to allow NRCC to select individual days (rather than one or more blocks of days) if it so wishes. The Board strongly expects that NRCC will cooperate with SOCAN so as to minimize the reporting burden of radio stations, and will entertain a request for a more formal form of cooperation if needed.

8. Les exigences de rapport

Les exigences de rapport reflètent, pour l'essentiel, l'accord des parties. Il y a lieu de noter des points suivants.

A) L'obligation de fournir les listes de diffusion est incorporée au tarif bien que la mesure soit volontaire dans le cas de la *SOCAN*. Les difficultés auxquelles la SCGDV a eu à faire face dans sa cueillette d'information auprès de certaines stations (qui ne sont pas nécessairement membres de l'ACR) justifient amplement la décision de rendre cet aspect du régime obligatoire.

La SCGDV pourra exiger de chaque station des renseignements à l'égard de 14 jours, comme c'est la pratique à la SOCAN, plutôt que les 21 demandés. Le libellé permet à la SCGDV, si elle le désire, d'opter pour des journées individuelles plutôt que pour un ou plusieurs blocs de journées. La Commission s'attend fortement à ce que la SCGDV collabore avec la SOCAN afin de faciliter la tâche des stations, et prendra en considération toute demande visant à rendre plus formelle cette exigence de collaboration si le besoin s'en faisait sentir.

There is no need to deal with CAB's request that the tariff reflect the value to NRCC of being provided with play lists. Given the blanket nature of the regime. collecting this sort of information is necessary. As stations derive benefits from such regime, it is only normal that they should carry parr of the burden of its efficient operation.

Il n'est pas nécessaire de traiter de la demande de l'ACR voulant que le tarif tienne compte de la valeur monétaire que la fourniture des listes de diffusion représente pour la SCGDV. Ce genre de renseignements est essentiel au bon fonctionnement d'un régime qui s'apparente a une licence générale. Les stations tirent des bénéfices d'un tel regime; il est donc normal qu'elles supportent une partie du fardeau nécessaire a son bon fonctionnement.

B) The tariff does not specify the number of audits NRCC can conduct in a given year. Such a limit has never been imposed on SOCAN. who appears not to have abused of this right. The Board is confident that NRCC will behave in the same fashion.

B) Le tarif n'impose pas de limite au nombre de verifications awquelles la SCGDV peut se livrer dans une année donnée. La Commission n'a jamais impose de limite de ce genre a la *SOCAN.* qui ne semble pas avoir abuse de ce droit. La Commission est conflante que la SCGDV agira de même.

C) Stations will be required to pay for an audit if royalties are under-reported by 10 per cent of any audited month. NRCC was proposing five per cent and CAB 20 per cent. Ten per cent seems a reasonable compromise.

C) Les stations devront payer les coûts de verification si les redevances ont ete sous-estimées de plus de 10 pour cent pour un mois quelconque. La SCGDV demandait cinq pour cent et l'ACR 20. Dix pour cent nous semble un compromis raisonnable.

D) The Board was surprised by the amount of controversy surrounding the confidentiality provisions. CAB expressed misgivings about allowing access to station financial information to persons other than NRCC. such as royalty claimants or other collectives for the purposes of establishing entitlements to payment- It asked that as much as possible, aggregate figures, as opposed to station specific data. be used for those purposes. The Board trusts *that* the provision included in the tariff will address the reasonable concerns of CAB in this respect.

D) La Commission s'etonne que les dispositions portant sur le traitement confidentiel aient soulevé autant de controverse. L'ACR s'est dite inquiete de devoir permettre l'accès aw données financières des stations a des penonnes autres que la SCGDV. notamment aux titulaires de droits et aux autres sociétés de gestion collective, pour effectuer la distribution. Elle a demandé que seules les données concernant l'ensemble des stations soient fournies a ces fins. La Commission est convaincue que la disposition incorporée au tarif suffit à répondre aux préoccupations raisonnables de l'ACR à cet égard.

CAB also stated that play list information was sensitive competitive information for broadcasters. NRCC ended up conceding that point. The provision included in the tariff draws no distinction between the two types of information.

L'ACR a aussi demandé que les radiodiffuseurs traitent les listes de diffusion c o m e renseignements concurrentiels de nature delicate. La SCGDV a finalement concédé ce point. Le tarif ne fait pas de distinction entre les deux types de renseignements.

E) All stations. including those whose royalty payment will only be $100 per year. will be required to comply with the tariffs reporting requirement. Only in this way can NRCC and. through it. the Board keep abreast of the use being made of the eligible repenoire by all of the industry.

9. Interest on late payments

The Board used the (simpler) formulation found in SOCAN's Tariff 17 instead of the one used in the retransmission tariff. Given that the tariff as structured does not require interim payments and adjustments, there is no need to be more specific.

10. Transitional provisions

The tariff contains. as did the 1990-1992 Retransmission tariff and SOCAN's Tariff 17 for 1990 to 1995. certain transitional provisions made necessary because the tariff takes effect on January 1. 1998 even though they were approved much later. A table sets out interest factors or multipliers to be used on sums owed in a given month. These were derived by using the Bank of Canada rates. Interest is not compounded. The amount owed for any given month is the amount calculated in accordance with the tariff multiplied by the factor set out for that month. The Board hopes that this will greatly simplify the stations' calculations and NRCC's verifications.

E) Toutes les stations. y compris celles qui ne versent que 100 $ par année. sont tenus aux exigences de rapport du tarif. Cette mesure est nécessaire afin de renseigner la SCGDV et éventuellement la Commission sur l'utilisation que l'ensemble de l'industrie fait du repertoire admissible.

9. Intérêts sur paiements tardifs

La Commission a retenu la formule simplifiée qu'on retrouve dans le tarif 17 de la SOCAN plutôt que celle utilisée dans le tarif de la retransmission. Il n'est pas nécessaire d'être plus précis, compte tenu que la structure tarifaire evite les versements intérimaires et les ajustements.

10. Dispositions transitoires

Tout c o m e le tarif pour la retransmission de 1990-1992 et le tarif 17 de la SOCAN de 1990 a 1995. le présent tarif comporte des dispositions transitoires qui sont nécessaires parce qu'il prend effet le 1er janvier 1998 et ce. mtme s'il a ete homologue beaucoup plus tard. Un tableau fournit les facteurs d'intérêts qui seront appliqués aux sommes dues pour les usages effectués durant un mois donné. Ces facteurs ont ete établis en utilisant le taux d'escompte de la Banque du Canada. L'intérêt n'a pas été composé. Le montant dû par rapport aux usages effectués dans un mois donné est le montant des redevances etabli conformément au tarif. multiplié par le facteur fourni pour le mois en question. La Commission est d'avis que ces mesures simplifieront de beaucoup les calculs et vérifications auxquels les stations et la SCGDV devront se livrer.

Le secrétaire de la Commission,

Claude Majeau
Secretary to the Board

ENDNOTES

1. Paragraph 68(2)*(a)*.Paragraph 68(2)*(b)*, which provides that the Board may also 'take into account any factor that it considers appropriate', adds nothing to the Board's already wide discretionary powers. See, for example. *SOCAN* v. *Canadian Association of Broadcasters* (C.A.), [1999] F.C.J. 389: *Réseaux Premier Choir Inc.* v. *Canadian Cable Television Assn.* [1997], 80 C.P.R. (3d) 208 (F.C.A.): *FWS Joint Sports Claimant* v. *Canada (Copyright Board)* (C.A.) [1992] 1 F.C. 487.

2. Subsection 68.1(3). See *Regulations Defining 'Advertising Revenues"*, SOR/98-447, Canada *Gazette* Part II, Vol. 132, No.19, p. 2589.

3. Subsection 68.1(5). Only the last expression has been defined. See *Definition of 'Wireless Transmission System" Regulations*, SOR/98-307. *Canada Gazette* Part II, Vol. 132. No. 12, p. 1817.

4. Section 20(2). See *Limitation of the Right to Remuneration of Certain Rome Convention Countries Statement.* SOR/99-143, *Canada Gazette* Part II, Vol. 133. No. 8, p. 1020.

5. 'Named" performers are represented in France by ADAMI, with which NRCC was negotiating a reciprocal agreement at the time of the hearing.

6. Mention should be made here of three issues which are of great importance to the participants but of little relevance, if any, to these proceedings. First, makers have agreed not to claw back royalties paid to performers through contract terms or otherwise. Second. AFM. ArtistI and APRS have agreed that non-members will be allowed to use the services of one of the societies by signing an agency agreement (in the case of AFM or

NOTES

1. Alinéa 68(2)*(a)*. L'alinea 68(2)*(b)*, qui stipule que la Commission peut aussi «tenir compte de tout facteur qu'elle estime indique, n'ajoute rien au pouvoir d'appréciation, deja fort large, dont la Commission dispose. Voir, par exemple, les arrêts *SOCAN* c. *Association canadienne des radiodiffuseurs* (C.A.), [1999] A.C.F. 389; *Réseaux Premier Choix Inc.* c. *Association canadienne de television par câble*, [1997] A.C.F. 78; *FWS Joint Sports Claimant c. Canada (Commission du droit d'auteur)* (C.A.). [1992] 1 C.F. 487.

2. Paragraphe 68.1(3). Voir le *Reglement sur la definition de retenes publicitaires*, DORS/98-447. *Gazene du Canada* Partie II. vol. 132. n° 19. p. 2589.

3. Paragraphe 68.1(5). Seule la derniere expression a ete définie. Voir le *Règlement sur la definition de «système de transmission par ondes radioélectriques»*, DORS/98-307, *Gazene du Canada* Partie II. vol. 132. n° 12, p. 1817.

4. Article 20(2). Voir la *Déclaration limitant le droit à rémunération équitable pour certains pays parties à la Convention* de Rome. DORS/99-143, *Gazene du Canada* Partie II, vol. 133. n° 8, p. 1020.

5. C'est l'ADAMI qui agit en France pour le compte des autres artistes-interprètes. A l'époque ou se sont tenus les audiences, la SCGDV était à négocier un accord de réciprocité avec cette société.

6. Il faudrait mentionner en passant trois questions qui sont d'une importance capitale pour les participants mais sans grand rapport avec la présente affaire. Premierement. les producteurs ont accepte de ne pas chercher a s'approprier les redevances versées aux artistes-interprets, que ce soit par contrat ou autrement. Deuxiemement. l'AFM, ArtistI et l'APRS ont convenu que d'autres personnes que leurs membres pourront avoir recours à

APRS) or an assignment agreement (in the case of Artisti) without having to become members of the "parent union". Third, members of AFM and ACTRA can be represented by another of the performers' collectives that are members of *NRCC*, thereby allowing them to be represented by one entity for the purposes of collective bargaining while asking another to administer their performing rights. The relationship between Artisti and UDA is such that the issue does not arise for members of UDA.

7. On issues of agency, see generally GHL Fridman, The Law *of Agency* (7th ed.) 1996 Butterworths.

8. The rules applicable in Quebec may be different, since article 2186 of the *Civil Code of* Quebec provides that "A contract of association is a contract by which the parties agree to pursue a common goal other than the making of pecuniary profits *to* be shared between the members of the association."

9. *See* J.-L Baudouin, *Les Obligations*, (4e éd), paragraph 864; GHL Fridman, The *Law* of *Contracts* (2d ed.) pp. 168-170.

10. Persons whose rights are represented here through a joint creditor are not "orphans" as this word is sometimes used in the context of section 76 of the *Act*, since their rights are indeed represented. The only true orphans are persons having rights in *sound* recordings for which neither the maker nor the performer is represented and in that case, no royalties are payable.

11. SOGEDAM's claim was limited *to* the French repertoire: it did not attempt to demonstrate the use made of sound recordings embedding performances of its 31 or so *Canadian* members.

leurs services de gestion de droits, soit par mandat (pour l'AFM ou l'APRS), soit par cession (pour Artisti) sans qu'il soit nécessaire d'adhérer au «syndicat» affilie. Troisiemement, les membres de l'AFM et de l'ACTRA pourront demander a une autre societe membre de la SCGDV qui gere les droits d'artistes-interprètes de gerer leur droit a rémunération; de la sorte, un membre pourra appartenir a une societe par les fins de négociations collectives et a une autre pour la gestion de ses droits voisins. La nature des liens existant entre Artisti et l'UDA fait en sorte que la question ne se souleve pas par rapport a cette dernière.

7. Sur les règles du mandat en *common law*, on peut consulter GHL Fridman, The *Law of Agency* (7e ed.) 1996 Butterworths.

8. Le droit québécois pourrait être different a cet égard. L'article 2186 du Code *civil du Québec* prévoit en effet que «Le contrat d'association *est* celui par lequel les parties conviennent de poursuivre un but commun autre que la réalisation de bénéfices pécuniaires a partager entre les membres de l'association.»

9. Voir J.-L. Baudouin, *Les Obligations*, (4e éd), paragraphe 864; GHL Fridman, *The Law of Contracts* (2d ed.) p. 168-170.

10. Le titulaire représenté par un co-créancier n'est pas un «orphelin» au sens où on l'entend habituellement lorsqu'on se réfère a l'article 76 de la *Loi*, puisque ses droits sont en fait représentés. Les seuls véritables orphelins sont les titulaires de droit dans un enregistrement sonore pour lequel ni le producteur, ni l'artiste-interprète n'est représenté et pour lequel aucune redevance n'est exigible.

11. La SOGEDAM s'est limitée a réclamer une quote-part a l'égard du repertoire français; elle n'a pas tente d'etablir l'usage fait des enregistrements sonores constitués de prestations de ses quelque 31 membres canadiens.

Jaffe Rebuttal Exh.6

DMCA
Section 104 Report

U.S. Copyright Office
August 2001

A Report of the Register of Copyrights
Pursuant to §104 of the Digital Millennium Copyright Act

DIGITAL MILLENNIUM COPYRIGHT ACT OF 1998, § 104

Pub. L. No. 105-304, 112 Stat. 2860, 2876

SEC. 104. EVALUATION OF IMPACT OF COPYRIGHT LAW AND AMENDMENTS ON ELECTRONIC COMMERCE AND TECHNOLOGICAL DEVELOPMENT.

(a) EVALUATION BY THE REGISTER OF COPYRIGHTS AND THE ASSISTANT SECRETARY FOR COMMUNICATIONS AND INFORMATION.–The Register of Copyrights and Assistant Secretary for Communications and Information of the Department of Commerce shall jointly evaluate–

(1) the effects of the amendments made by this title and the development of electronic commerce and associated technology on the operation of sections 109 and 117 of title 17, United States Code; and

(2) the relationship between existing and emergent technology and the operation of sections 109 and 117 of title 17, United States Code.

(b) REPORT TO CONGRESS.–The Register of Copyrights and the Assistant Secretary for Communications and Information of the Department of Commerce shall, not later than 24 months after the date of the enactment of this Act, submit to the Congress a joint report on the evaluation conducted under subsection (a), including any legislative recommendations the Register and the Assistant Secretary may have.

DMCA
Section 104 Report
U.S. Copyright Office
August 2001

A Report of the
Register of Copyrights
Pursuant to §104 of the Digital
Millennium Copyright Act

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The Register of Copyrights
of the
United States of America

Library of Congress
Department 17
Washington, D.C. 20540

(202) 707-8350

August 29,2001

Dear Mr. President:

I am pleased to present the Copyright Office's "DMCA Section 104 Report."

As required under section 104 of Public Law No. 105-304, the Report evaluates the effects of title I of the Digital Millennium Copyright Act of 1998 and the development of electronic commerce and associated technology on the operation of sections 109 and 117 of title 17, U.S.C. It also evaluates the relationship between existing and emergent technology and the operation of those sections.

Respectfully,

Marybeth Peters

Marybeth Peters
Register of Copyrights

Enclosure

The Honorable Richard B. Cheney
President
United States Senate
Washington, D.C. 20510

The Register of Copyrights
of the
United States of America

brary of Congress
epartment 17
'ashington, D.C. 20540

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Register of Copyrights

Enclosure

The Honorable J. Dennis Hastert
Speaker
United States House of Representatives
Washington, D.C. 20515

ACKNOWLEDGMENTS

This report is the result of the expertise, skills and dedication of many people. I was fortunate to be able to draw on many talented staff, and I am grateful to all of them. However, I especially thank and acknowledge the efforts of two officials of the Office. The first is Jesse Feder, Acting Associate Register for Policy and International Affairs, who served as the project manager and who was also a primary drafter of the report; the second is David O. Carson, General Counsel of the Copyright Office, whose wise counsel and sound advice was present throughout the process. Also, worthy of special praise are the others who drafted the report; they are Marla Poor, Attorney Advisor, Office of Policy and International Affairs, Steven Tepp, Policy Planning Advisor, Office of Policy and International Affairs, and Robert Kasunic, Senior Attorney-Advisor, Office of the Copyright General Counsel. Their efforts went well beyond writing sections of the report and they played important roles in the review process.

Others in the Office assisted the "report team" in numerous ways, including sharing their insight and advice. These individuals are Robert Dizard, Staff Director and Chief Operating Officer of the Copyright Office, Tanya Sandros, Senior Attorney, Office of the Copyright General Counsel; William Roberts Senior Attorney-Advisor for Compulsory Licenses, Office of the Copyright General Counsel; and Sayuri Rajapakse, Attorney-Advisor, Office of Policy and International Affairs. I also thank Kelly Lacey, our intern from Georgetown University Law Center, for her first-rate substantive help.

Numerous and important contributions were made by many others in the Copyright Office. I thank Marylyn Martin of the Register's Office, for her assistance in organizing our public hearing; Shirada Harrison of the Office of Policy and International Affairs, and Guy Echols and Sandra Jones of the General Counsel's Office for their assistance in completing the final document; Helen Hester-Ossa, Teresa McCall and Charles Gibbons of the Information and Reference Division for their excellent assistance in the design and layout of the Report and in getting it printed; Denise Prince of the General Counsel's Office for her assistance in getting it delivered to Congress; and Ed Rogers and George Thuronyi, our webmasters, for their expert contributions both during the study and in getting our Report out to the public via the Internet. Special thanks also to Xue Fei Li of our Automation Group for her technical assistance in receiving comments from the public by email.

Finally, just prior to completing the process, I asked June Besek, Director of Studies and Director of the International Program of the Kernochan Center for Law, Media and the Arts at Columbia Law School, to review the penultimate draft text. I appreciate her exceptional efforts (she had less than 48 hour) and her invaluable suggestions and comments.

Marybeth Peters
Register of Copyrights

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EXECUTIVE SUMMARY

INTRODUCTION

The Digital Millennium Copyright Act of 1998 (DMCA) was the foundation of an effort by Congress to implement United States treaty obligations and to move the nation's copyright law into the digital age. But as Congress recognized, the only thing that remains constant is change. The enactment of the DMCA was only the beginning of an ongoing evaluation by Congress on the relationship between technological change and U.S. copyright law. This Report of the Register of Copyrights was mandated in the DMCA to assist Congress in that continuing process.

Our mandate was to evaluate "the effects of the amendments made by [title I of the DMCA] and the development of electronic commerce and associated technology on the operation of sections 109 and 117 of title 17, United States Code; and the relationship between existing and emergent technology and the operation of sections 109 and 117. . . ." Specifically, this Report focuses on three proposals that were put forward during our consultations with the public: creation of a "digital first sale doctrine;" creation of an exemption for the making of certain temporary incidental copies; and the expansion of the archival copying exemption for computer programs in section 117 of the Act.

Part I of this Report describes the circumstances leading up to the enactment of the DMCA and the genesis of this study. Part I also examines the historical basis of sections 109 and

117 of the Act. Part II discusses the wide range of views expressed in the public comments and testimony. This input from the public, academia, libraries, copyright organizations and copyright owners formed the core information considered by the Office in its evaluation and recommendations. Part III evaluates the effect of title I of the DMCA and the development of electronic commerce and associated technology on the operations of sections 109 and 117 in light of the information received and states our conclusions and recommendations regarding the advisability of statutory change.

I. BACKGROUND

A. THE DIGITAL MILLENNIUM COPYRIGHT ACT

The World Intellectual Property Organization (WIPO) treaties were the impetus for the U.S. legislation. In order to facilitate the development of electronic commerce in the digital age, Congress implemented the WIPO treaties by enacting legislation to address those treaty obligations that were not adequately addressed under existing U.S. law. Legal prohibitions against circumvention of technological protection measures employed by copyright owners to protect their works, and against the removal or alteration of copyright management information, were required in order to implement U.S. treaty obligations.

The congressional determination to promote electronic commerce and the distribution of digital works by providing copyright owners with legal tools to prevent widespread piracy was tempered with concern for maintaining the integrity of the statutory limitations on the exclusive rights of copyright owners. In addition to the provisions adopted by Congress in 1998, there were other proposals – including amendments to sections 109 and 117, that were not adopted, but were the subjects of a number of studies mandated by the DMCA. Section 104 of the DMCA requires the Register of Copyrights and the Assistant Secretary for Communications and Information to report on the effects of the DMCA on the operation of sections 109 and 117 and the relationship between existing and emergent technology on the operation of sections 109 and 117 of title 17 of the United States Code.

The inclusion of section 109 in the study has a clear relationship to the digital first sale proposal contained in a bill introduced in 1997 by Congressmen Rick Boucher and Tom Campbell. The reasons for including section 117 in the study are less obvious. While there is no legislative history explaining why section 117 is included in the study, it appears that the reference was intended to include within the scope of the study a proposed exemption for incidental copies found in the Boucher-Campbell bill, which would have been codified in section 117 of the Copyright Act.

B. SECTION 109(a) AND THE FIRST SALE DOCTRINE

The common-law roots of the first sale doctrine allowed the owner of a particular copy of a work to dispose of that copy. This judicial doctrine was grounded in the common-law principle that restraints on the alienation of tangible property are to be avoided in the absence of clear congressional intent to abrogate this principle. This doctrine appears in section 109 of the Copyright Act of 1976. Section 109(a) specified that this notwithstanding a copyright owner's exclusive distribution right under section 106 the owner of a particular copy or phonorecord that was lawfully made under title 17 is entitled to sell or further dispose of the possession of that copy or phonorecord.

C. SECTION 117 COMPUTER PROGRAM EXEMPTIONS

Section 117 of the Copyright Act of 1976 was enacted in the Computer Software Copyright Amendments of 1980 in response to the recommendations of the National Commission on New Technological Uses of Copyrighted Works' (CONTU). Section 117 permits the owner of a copy of a computer program to make an additional copy of the program for purely archival purposes if all archival copies are destroyed in the event that continued possession of the computer program should cease to be rightful, or where the making of such a copy is an essential step in the utilization of the computer program in conjunction with a machine and that it is used in no other manner.

II. VIEWS OF THE PUBLIC

Section II of the report summarizes the views received fiom the public through comments, reply comments and hearing testimony. The summaries are grouped into three categories: views concerning section 109, views concerning section 117, and views on other miscellaneous issues.

A. VIEWS CONCERNING SECTION 109

Most of the comments dealt with section 109 whether of not they addressed section 117. While there was a broad range of views on the effect of the DMCA on the first sale doctrine, most of the commenters believed that the anticircumvention provisions of 17 U.S.C. section 1201 allowed copyright owners to restrict the operation of section 109. Of particular concern to many commenters was the Content Scrambling System (CSS) and the "region coding" used to protect motion pictures on Digital Versatile Disks (DVDs). They argued that use of CSS forces a consumer to make two purchases in order to view a motion picture on DVD: the DVD and the authorized decryption device. In the view of these commenters, this system reduces or eliminates the value of and market for DVDs by interfering with their free alienability on the market. A similar argument was advanced for the region coding on DVDs in that the geographic market for resale is restricted by this technological protection measure.

Another concern expressed by a number of commenters was the growing use of non-negotiable licenses accompanying copyrighted works that are written to restrict or eliminate statutorily permitted uses, including uses permitted under section 109. In some cases, these license restrictions are enforced through technological measures. It was argued that these licensing practices and the prohibition on circumvention frustrate the goals of the first sale doctrine by allowing copyright owners to maintain control on works beyond the first sale of a particular copy. These commenters stated that this interference with the operation of the first sale doctrine has the capacity to inhibit the function of traditional library operations, such as interlibrary loan, preservation, and use of donated copies of works.

Other commenters rebutted these claims, arguing that over-restrictive technological protection measures or licenses would not survive in the marketplace, since competition would be a limiting principle. It was also argued that the effect of licensing terms on the first sale doctrine is beyond the scope of this study.

Commenters generally viewed section 1202 of the DMCA, which prohibits the alteration or removal of copyright management information, as having no impact of the operation of the first sale doctrine.

The greatest area of contention in the comments was the question of whether to expand the first sale doctrine to permit digital transmission of lawfully made copies of works. Although some proponents argued that such transmissions are already permitted by the current language of section 109, most thought that clarification of this conclusion by Congress would be advisable since the absence of express statutory language could lead to uncertainty.

The proponents of revising section 109 argued that the transmission of a work that was subsequently deleted from the sender's computer is the digital equivalent of giving, lending, or selling a book. Allowing consumers to transfer the copy of the work efficiently by means of online transmission would foster the principles of the first sale doctrine. These principles have promoted economic growth and creativity in the analog world and should be extended to the digital environment. Proponents of this argument sought amendment to section 109 to allow a person to forward a work over the Internet and then delete that work from his computer.

Others opposed such an amendment for a number of reasons. Opponents pointed out that the first sale doctrine is a limitation on the distribution right of copyright owners and has never implicated the reproduction right which is, in their view, a "cornerstone" of copyright protection. In addition, the impact of the doctrine on copyright owners was also limited in the off-line world by a number of factors, including geography and the gradual degradation of books and analog works. The absence of such limitations would have an adverse effect on the market for digital works. Opponents also believed that proposals that depend on the user deleting his copy would be unverifiable, leading to virtually undetectable cheating. Given the expanding market for digital works without a digital first sale doctrine, opponents questioned the consumer demand for such a change in the law.

B. Views Concerning Section 117

The comments related to section 117 fell into two main categories: those addressing the status of temporary copies in RAM and those concerning the scope of the archival exemption.

Many commenters advocated a blanket exemption for temporary copies that are incidental to the operation of a device in the course of use of a work when that use is lawful under title 17. Such an exemption was originally proposed in the Boucher-Campbell bill as an amendment to section 117.

Other commenters vigorously opposed any exemption for incidental copies at this time. They argued that such an exemption would dramatically expand the scope of section 117 in contrast to the carefully calibrated adjustment made to section 117 in the DMCA to address the problems experienced by independent computer service organizations at issue in ***MAI Systems Corp. v. Peak Computer, Inc.*** These commenters stated that Congress' narrow adjustment to section 117 in the DMCA reaffirmed the conclusion that temporary copies in random access memory (RAM) are copies that are subject to the copyright owner's exclusive reproduction right. Further change would undercut the reproduction right in all works and endanger international treaty obligations.

There was disagreement on the economic value of temporary copies. Proponents of an amendment argued that temporary buffer copies are necessary to carry out streaming of performances of works on the Internet and have no value apart from that performance. They argued that the limitations under other sections of the Copyright Act, including sections 107 and 512, were insufficient to sustain the operation of businesses that stream audio performances to the public.

Opponents, on the other hand, argued that these copies are within the scope of the copyright owner's exclusive rights and do possess value. Particular emphasis was placed on the value of temporary copies of computer programs. It was also argued that as streaming performances become more common, these temporary copies will increase in value because of the adverse effect of the performances on the market for purchases of copies of these works. Opponents believed it would be premature to change the law because of the absence of specific evidence of harm and the high potential for adverse unintended consequences. It was noted that when Congress was presented with concrete evidence of harm to independent service organizations after the *MAI v.* Peak decision, Congress took steps to remedy the situation. Similarly, section 512 of the DMCA created limitations on the remedies available against Internet service providers for incidental copying that is essential to the operation of the Internet.

The other major concern involving section 117 concerned the scope of the archival exemption. Proponents of amending section 117 raised two primary points. First, they argued that the policy behind the archival exemption needs to be updated to encompass all digital works rather than just computer programs. Since computers are vulnerable to crashes, viruses, and other failures, downloaded music, electronic books and other works face the same risks that precipitated the exemption for computer programs. Some argued that all digital media is susceptible to accidental deletion or corruption. Consumers should be permitted to protect their investments in works.

Proponents of expansion of the archival exemption offered another argument – section 117 does not comport with reality. Systematic backup practices do not fit the structure of section 117, which is limited to making a copy of an individual program at the time the consumer obtains it. It was argued that such a discrepancy between the law and commonly accepted practices undermines the integrity of the law. Such a fundamental mismatch creates the perception that the law need not be literally followed, thereby creating a slippery slope.

Opponents of an expansion of the archival exemption countered that the justification behind section 117 no longer exists. Most software is distributed on CD-ROM, which is far more robust than floppy disks. Consumers need merely retain the original CD as a backup, since it is a simple operation to reinstall software that is compromised. In addition, these opponents argued that there is currently an inaccurate public perception of the scope of the backup copy exception. These commenters argue that many invoke the archival exception as a shield to commercial piracy.

Opponents of an amendment to section 117 asserted that even if there is a mismatch between actual backup practices and the current exception, no one has been harmed by it. Commenters noted that no one has been sued as a result of backing up material outside the scope of section 117, and no one has stopped performing backups. It was also argued that if a particular activity does not fall within the terms of section 117, it may nevertheless be privileged under the fair use doctrine.

C. Views Concerning Other Miscellaneous Issues

There were assorted other comments and testimony on a range of issues. There were concerns raised about the potential adverse effects of sections 1201 and 1202 on the traditional concepts of first sale, fair use, and the archival and preservation exemptions. It was argued that these prohibitions are likely to diminish, if not eliminate, otherwise lawful uses. It was asserted that copyright management information may also have the capacity to reveal user information in a manner that would chill legitimate uses of copyrighted works.

Another prevalent concern was that licenses are being used increasingly by copyright owners to undermine the first sale doctrine and restrict other user privileges under the copyright law. These commenters argue that this trend is displacing the uniformity of federal copyright law with a wide variation of contract terms that must be evaluated and interpreted. This poses a particular challenge to large institutions, such as universities and libraries, in determining legal and acceptable use in any given work. A number of commenters argued that federal copyright law should preempt such license terms.

Other commenters argued that Congress did not intend copyright law broadly to preempt contract provisions. They argue that the freedom to contract serves the interests on both copyright owners and the public by allowing greater flexibility in determining pricing, terms and conditions of use, and other options.

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III. EVALUATION AND RECOMMENDATIONS

We are not persuaded that title I of the DMCA has had a significant effect on the operation of sections 109 and 117 of title 17. The adverse effects that section 1201, for example, is alleged to have had on these sections cannot accurately be ascribed to section 1201. The causal relationship between the problems identified and section 1201 are currently either minimal or easily attributable to other factors such as the increasing use of license terms. Accordingly, none of our legislative recommendations are based on the effects of section 1201 on the operation of sections 109 and 117.

A. THE EFFECT OF TITLE I OF THE DMCA ON THE OPERATION OF SECTIONS 109 AND 117

The arguments raised concerning the adverse effects of the CSS technological protection measure on the operation of section 109 are flawed. The first sale doctrine is primarily a limitation on copyright owner's distribution right. Section 109 does not guarantee the existence of secondary markets for works. There are many factors which could affect the resale market for works, none of which could be said to interfere with the operation of section 109. The need for a particular device on which to view the work is not a novel concept and does not constitute an effect on section 109. VHS videocassettes for example, must be played on VHS VCRs.

A plausible argument can be made that section 1201 may have a negative effect on the operation of the first sale doctrine in the context of works tethered to a particular device. In the case of tethered works, even if the work is on removable media, the content cannot be accessed on any device other than the one on which it was originally made. This process effectively prevents disposition of the work. However, the practice of tethering a copy of a work to a particular hardware device does not appear to be widespread at this time, at least outside the context of electronic books. Given the relative infancy of digital rights management, it is premature to consider any legislative change at this time. Should this practice become widespread, it could have serious consequences for the operation of the first sale doctrine, although the ultimate effect on consumers is unclear.

We also find that the use of technological measures that prevent the copying of a work potentially could have a negative effect on the operation of section 117. To the extent that a technological measure prohibits access to a copyrighted work, the prohibition on the circumvention of measures that protect access in section 1201(a)(1) may have an adverse impact on the operation of the archival exception in section 117. Again, however, the current impact of such a concern appears to be minimal, since licenses generally define the scope of permissible archiving of software, and the use of CD-ROM reduces the need to make backup copies.

Given the minimal adverse impact at the present time, we conclude that no legislative change is warranted to mitigate any effect of section 1201 on section 117.

B. THE EFFECT OF ELECTRONIC COMMERCE AND TECHNOLOGICAL CHANGE ON SECTIONS 109 AND 117

There is no dispute that section 109 applies to works in digital form. Physical copies of works in a digital format, such as CDs or DVDs, are subject to section 109 in the same way as physical copies in analog form. Similarly, a lawfully made tangible copy of a digitally downloaded work, such as a work downloaded to a floppy disk, Zip™ disk, or CD-RW, is clearly subject to section 109. The question we address here is whether the transmission of a work to another person falls within – or should fall within – the scope of section 109.

1. *The First Sale Doctrine in the Digital World*

a Evaluation of Arguments Concerning First Sale

The first sale doctrine is primarily a limitation on the copyright owner's exclusive right of distribution. It does not limit the exclusive right of reproduction. While disposition of a work downloaded to a floppy disk would only implicate the distribution right, the transmission of a work from one person to another over the internet results in a reproduction on the recipient's mputer, even if the sender subsequently deletes the original copy of the work. This activity therefore entails an exercise of an exclusive right that is not covered by section 109.

Proponents of expansion of the scope of section 109 to include the transmission and deletion of a digital file argue that this activity is essentially identical to the transfer of a physical copy and that the similarities outweigh the differences. While it is true that there are similarities, we find the analogy to the physical world to be flawed and unconvincing.

Physical copies degrade with time and use; digital information does not. Works in digital format can be reproduced flawlessly, and disseminated to nearly any point on the globe instantly and at negligible cost. Digital transmissions can adversely effect the market for the original to a much greater degree than transfers of physical copies. Additionally, unless a "forward-and-delete" technology is employed to automatically delete the sender's copy, the deletion of a work requires an additional affirmative act on the part of the sender subsequent to the transmission. This act is difficult to prove or disprove, as is a person's claim to have transmitted only a single copy, thereby raising complex evidentiary concerns. There were conflicting views on whether effective forward and delete technologies exist today. Even if they do, it is not clear that the market will bear the cost of an expensive technological measure.

The underlying policy of the first sale doctrine as adopted by the courts was to give effect to the common law rule against restraints on the alienation of tangible property. The tangible nature of a copy is a defining element of the first sale doctrine and critical to its rationale. The digital transmission of a work does not implicate the alienability of a physical artifact. When a work is transmitted, the sender is exercising control over the intangible work through its reproduction rather than common law dominion over an item of tangible personal property. Unlike the physical distribution of digital works on a tangible medium, such as a floppy disk, the transmission of works interferes with the copyright owner's control over the intangible work and the exclusive right of reproduction. The benefits to further expansion simply do not outweigh the likelihood of increased harm.

Digital communications technology enables authors and publishers to develop new business models, with a more flexible array of products that can be tailored and priced to meet the needs of different consumers. We are concerned that these proposals for a digital first sale doctrine endeavor to fit the exploitation of works online into a distribution model – the sale of copies – that was developed within the confines of pre-digital technology. If the sale model is to continue as the dominant method of distribution, it should be the choice of the market, not due to legislative fiat.

We also examined how other countries are addressing the applicability of the first sale – or exhaustion – doctrine to digital transmissions. We found that other countries are addressing digital transmissions under the communication to the public right and are not applying the principle of exhaustion, or any other analog thereof, to digital transmissions.

b. Recommendation Concerning the Digital First Sale Doctrine

We recommend no change to section 109 at this time. Although speculative concerns have been raised, there was no convincing evidence of present-day problems. In order to recommend a change in the law, there should be a demonstrated need for the change that outweighs the negative aspects of the proposal. The Copyright Office does not believe that this is the case with the proposal to expand the scope of section 109 to include digital transmissions. The time may come when Congress may wish to address these concerns should they materialize.

The fact that we do not recommend adopting a "digital first sale" provision at this time does not mean that the issues raised by libraries are not potentially valid concerns. Similarly, our conclusion that certain issues are beyond the scope of the present study does not reflect our judgment on the merits of those issues.

The library community has raised concerns about how the current marketing of works in digital form affects libraries with regard to five specifically enumerated categories: interlibrary loans, off-site accessibility, archiving/preservation, availability of works, and use of donated copies. Most of these issues arise from terms and conditions of use, and costs of license agreements. One arises because, when the library has only online access to the work, it lacks a physical copy of the copyrighted work that can be transferred. These issues arise from existing business models and are therefore subject to market forces. We are in the early stages of electronic commerce. We hope and expect that the marketplace will respond to the various concerns of customers in the library community. However, these issues may require further consideration at some point in the future. Libraries serve a vital function in society, and we will continue to work with the library and publishing communities on ways to ensure the continuation of library functions that are critical to our national interest.

2. *The Legal Status of Temporary Copies*

a. RAM Reproductions as "Copies" under the Copyright Act

All of the familiar activities that one performs on a computer, from the execution of a computer program to browsing the World Wide Web, necessarily involve copies stored in integrated circuits known as RAM. This information can remain in memory until the power is switched off or the information is overwritten. These reproductions generally persist only for as long as the particular activity takes place.

The legal status of RAM reproductions has arisen in this study almost exclusively in the context of streaming audio delivery, including webcasting. In order to render the packets of audio information in an audio "stream" smoothly, in spite of inconsistencies in the rate of delivery, packets of audio information are saved in a portion of RAM called a buffer until they are ready to be rendered.

Based on an the text of the Copyright Act – including the definition of "copies" in section 101 – and its legislative history, we conclude that the making of temporary copies of a work in RAM implicates the reproduction right so long as the reproduction persists long enough to be perceived, copied, or communicated.

Every court that has addressed the issue of reproductions in RAM has expressly or impliedly found such reproductions to be copies within the scope of the reproduction right. The seminal case on this subject, *MAI. Sys. Corp. v. Peak Computer, Inc.*, found that the loading of copyrighted software into RAM creates a "copy" of that software. At least nine other courts have followed MAI v. *Peak* in holding RAM reproductions to be "copies" and several other cases have held that loading a computer program into a computer entails making a copy, without mentioning RAM specifically.

b. Evaluation of Arguments Concerning Temporary Incidental Copy Exceptions

In the course of this study, arguments were advanced in support of a blanket exemption for incidental copies similar to that proposed in the Boucher-Campbell bill. Most of the arguments advanced on such a proposal focused exclusively on the specific issue of buffer copies made in the course of audio streaming, rather than the broader issue of incidental copying generally. This focus suggests that legislation tailored to address the specific problems raised in the context of audio streaming should be examined. This focus is particularly appropriate since there was no compelling evidence presented in support of a blanket exemption for incidental copies and there was evidence that such an exemption could lead to unintended adverse consequences for copyright owners.

There was compelling evidence presented, however, on the uncertainty surrounding temporary buffer copies made in RAM in the come of rendering a digital musical stream. Specifically, webcasters asserted that the unknown legal status of buffer copies exposes webcasters to demands for additional royalty payments from the owner of the sound recording, as well as potential infringement liability.

The buffer copies identified by the webcasting industry exist for only a short period of time and consist of small portions of the work. Webcasters argue that these reproductions are incidental to the licensed performance of the work and should not be subject to an additional license for a reproduction that is only a means to an authorized end. Buffer copies implicate the reproduction right, thus potentially resulting in liability. There is, therefore, a legitimate concern on the part of webcasters and other streaming music services as to their potential liability.

We believe that there is a strong case that the making of a buffer copy in the course of streaming is a fair use. Fair use is a defense that may limit any of the copyright owner's exclusive rights, including the reproduction right implicated in temporary copies. In order to assess whether a particular use of the works at issue is a fair use, section 107 requires the consideration and balancing of four mandatory, but nonexclusive, factors on a case-by-case basis.

In examining the first factor – the purpose and character of the use – it appears that the making of buffer copies is commercial and not transformative. However, the use does not supersede or supplant the market for the original works. Buffer copies are a means to a noninfiinging and socially beneficial end – the licensed performance of these works. There is no commercial exploitation intended or made of the buffer copy in itself. The first factor weighs in favor of fair use.

The second factor – the nature of the copyrighted work – weighs against a finding of fair use because musical works are generally creative. The third factor – the amount and substantiality of the portion used in relation to the copyrighted work as a whole – would also be likely to weigh against fair use since, in aggregate, an entire musical work is copied in the RAM buffer. Since this is necessary in order to carry out a licensed performance of the work, however, the factor should be of little weight.

In analyzing the fourth factor – the effect of the use on the actual or potential market for the work – the effect appears to be minimal or nonexistent. This factor strongly weighs in favor of fair use.

Two of the four statutory factors weigh in favor of fair use, but fair use is also an "equitable rule of reason." In the case of temporary buffer copies, we believe that the equities unquestionably favor the user. The sole purpose for making the buffer copies is to permit an activity that is licensed by the copyright owner and for which the copyright owner receives a performance royalty. In essence, copyright owners appear to be seeking to be paid twice for the same activity. Additionally, it is technologically necessary to make buffer copies in order to carry out a digital performance of music over the Internet. Finally, the buffer copies exist for too short a period of time to be exploited in any way other than as a narrowly tailored means to enable the authorized performance of the work. On balance, therefore, the equities weigh heavily in favor of fair use.

c. Recommendation Concerning Temporary Incidental Copies

Representatives of the webcasting industry expressed concern that the case-by-case fair use defense is too uncertain a basis for making rational business decisions. We agree. While we recommend against the adoption of a general exemption from the reproduction right to render noninfiinging all temporary copies that are incidental to lawful uses, a more carefully tailored approach is desirable.

We recommend 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.

The economic value of licensed streaming is in the public performances of the musical work and the sound recording, both of which are paid for. The buffer copies have no independent economic significance. They are made solely to enable the performance of these works. The uncertainty of the present law potentially allows those who administer the reproduction right in musical works to prevent webcasting from taking place – to the detriment of other copyright owners, webcasters and consumers alike – or to extract an additional payment that is not justified by the economic value of the copies at issue. Congressional action is desirable to remove the uncertainty and to allow the activity that Congress sought to encourage through the adoption of the section 114 webcasting compulsory license to take place.

Although we believe that the fair use defense probably does apply to temporary buffer copies, this approach is fraught with uncertain application in the courts. This uncertainty, coupled with the apparent willingness of some copyright owners to assert claims based on the making of buffer copies, argues for statutory change. We believe that the narrowly tailored scope of our recommendation will minimize, if not eliminate, concerns expressed by copyright owners about potential unanticipated consequences.

Given our recommendations concerning temporary copies that are incidental to digital performances of sound recordings and musical works, fairness requires that we acknowledge the symmetrical difficulty that is faced in the online music industry: digital performances that are incidental to digital music downloads. Just as webcasters appear to be facing demands for royalty payments for incidental exercise of the reproduction right in the course of licensed public performances, it appears that companies that sell licensed digital downloads of music are facing demands for public performance royalties for a technical "performance" of the underlying musical work that allegedly occurs in the course of transmitting it from the vendor's server to the consumer's computer.

Although we recognize that it is an unsettled point of law that is subject to debate, we do not endorse the proposition that a digital download constitutes a public performance even when no contemporaneous performance takes place. If a court were to find that such a download can be considered a public performance within the language of the Copyright Act, we believe the that arguments concerning fair use and the making of buffer copies are applicable to this performance issue as well. It is our view that no liability should result from a technical "performance" that takes place in the c o m e of a download.

3. *Archival Exemption*

a. Evaluation of Arguments Concerning the Scope of Section 117(a)(2)

Currently the archival exemption under section 117(a)(2) is limited to computer programs. This section allows the owner of a copy of a computer program to make or authorize the making of an additional copy of the program "for archival purposes," provided that "all archival copies are destroyed in the event that continued possession of the computer program should cease to be rightful." A number of arguments were advanced in the course of this study for an expansion of this archival exemption in order to cover the kind of routine backups that are performed on computers and to allow consumers to archive material in digital format other than computer programs.

Commenters asserted that consumers need to backup works in digital form because they are vulnerable. That was CONTU's rationale for recommending that Congress create an exemption to permit archival copies of computer programs. In both cases, the vulnerability stems from the digital nature of the works. It would be perfectly consistent with the rationale of CONTU's recommendations and Congress*enactment of section 117 to extend the archival exemption to protect against the vulnerabilities that may afflict all works in digital format.

Evidence was presented to us noting that the archival exemption under section 117 does not permit the prevailing practices and procedures most people and businesses follow for backing up data on a computer hard drive. There is a fundamental mismatch between accepted, prudent practices among most system administrators and other users, on the one hand, and section 117 on the other. As a consequence, few adhere to the law.

While there is no question that this mismatch exists, nobody was able to identify any actual harm to consumers as a result of the limited scope of the archival exemption. Additionally, it was argued that the need to make archival copies of computer programs has diminished, because almost all software sold in the United States is distributed on CD-ROM, which itself serves as an archival copy in the event of hard drive problems or upgrades.

b. Recommendations Concerning the Archival Exemption

Although there has been a complete absence of any demonstrated harm to the prospective beneficiaries of an expanded archival exemption, and although we believe that a strong case could be made that most common archival activities by computer users would qualify as fair use, we have identified a potential concern – the interplay between sections 107 and 109. It appears that the language of the Copyright Act could lead a court to conclude that copies lawfully made under the fair use doctrine may be freely distributed under section 109.

Section 109 permits "the owner of a particular copy or phonorecord lawfully made" under title 17 to distribute that copy without the copyright owner's permission. To the extent that section 107 permits a user to make a backup copy of a work stored on a hard drive, that copy is lawfully made and the user owns it. Section 109, on its face, appears to permit the user to sell or otherwise dispose of the possession of that backup copy. The legislative history can be read to support either view.

We conclude that a statutory change is desirable, and recommend that Congress amend the copyright law in one of two ways.

Given the uncertain state of authority on the issue, we cannot conclude with a satisfactory level of certainty that a court will not, in the future, find a backup copy made by virtue of section 107 to be eligible for distribution under section 109. We believe that such a result is contrary to the intent of Congress and would have the capacity to do serious damage to the copyright owner's market. We therefore recommend that Congress either (1) amend section 109 to ensure that fair use copies are not subject to the first sale doctrine or (2) create a new archival exemption that provides expressly that backup copies may not be distributed. We express no preference as between the *two* options, and note that they are not mutually exclusive.

The first option would entail amending section 109(a) to state that only copies lawfully made ***and lawfully distributed*** are subject to the first sale doctrine. This proposed change would not preclude the distribution of copies made pursuant to the fair use doctrine since the exclusive right of distribution is equally subject to the fair use doctrine. It would, however, require that a separate fair use analysis be applied to the distribution of that copy.

The second option entails creating a new exemption for making backups of lawful copies of material in digital form, and amending section 117 to delete references to archival copies. The new exemption should follow the general contours of section 117(a)(2) and (b), and include the following elements: it should pennit the making of one or more backup copies of a work. The copy fiom which the backup copies are made must be in digital form on a medium that is subject to accidental erasure, damage, or destruction in the ordinary course of its use. It should stipulate that the copies may be made and used solely for archival purposes or for use in lieu of the original copy. It should also specify that, notwithstanding the provisions of section 109, the archival copy may not be transferred except as part of a lawful transfer of all rights in the work. Finally, it should specify that the archival copies may not be used in any manner in the event that continued possession of the work ceases to be rightful.

4. *Contract Preemption*

The question of contract preemption was raised by a number commenters who argued that the Copyright Act should be amended to insure that contract provisions that ovemde consumer privileges in the copyright law, or are otherwise unreasonable, are not enforceable. Although the general issue of contract preemption is outside the scope of this Report, we do note that this issue is complex and of increasing practical importance, and thus legislative action appears to be premature. On the one hand, copyright law has long coexisted with contract law. On the other hand, the movement at the state level toward resolving questions as to the enforceability of non-negotiated contracts coupled with legally-protected technological measures that give right holders the technological capability of imposing contractual provisions unilaterally, increases the possibility that right holders, rather than Congress, will determine the landscape of consumer privileges in the future. Although market forces may well prevent nght holders from unreasonably limiting consumer privileges, it is possible that at some point in the future a case could be made for statutory change.

INTRODUCTION

The Digital Millennium Copyright Act of 1998 (DMCA) was the most substantial revision of the nation's copyright law since the general revision enacted in 1976. What began as a more modest (though critically important) effort to implement two new treaties that addressed issues of copyright in the digital age became a far more comprehensive legislative preject to address a range of issues, digital and non-digital. The debates, both inside and outside the Congress, that were generated by this legislation led to myriad proposals – some of which were enacted and some of which were not. As Representative Howard Coble, Chairman of the House Judiciary Subcommittee on Courts and Intellectual Property and one of the bill's chief sponsors in the House, stated when he brought the measure to the floor, the DMCA "is only the beginning of Congress' evaluation of the impact of the digital age on copyrighted works."[1]

The DMCA directed the Register of Copyrights to prepare this Report as part of Congress' continuing evaluation of the impact of the digital age on copyrighted works. It is the fourth such undertaking mandated by Congress in the DMCA. In 1999, the Copyright Office released a report on digital distance education, which included recommendations that are embodied in S. 487 in this Congress?[2] In 2000, the Copyright Office and the National Telecommunications and Information Administration of the Department of Commerce (NTIA) released a joint report on the effect of the prohibition on circumventing access control

[1] 144 Cong. Rec. H7092 (daily ed. Aug. 4, 1998) (statement of Rep. Coble).

[2] Copyright Office, Copyright Office Report on Copyright and Digital Distance Education (1999). The results of this study were presented to Congress on May 25, 1999 and are available at: www.loc.gov/copyright/docs/de_rprt.pdf. The text of S.487 is available at: thomas.loc.gov/cgi-bin/query/z?c107:S.487:.

technologies in section 1201(a)(1)(A) of title 17, and an exception to that prohibition in section 1201(g), on encryption research.[3] Also in 2000, the Office completed a rulemaking required under section 1201(a)(1)(C) concerning an exemption from the section 1201(a)(1)(A) prohibition for noninfringing uses with respect to certain classes of works.

The focus of this Report is an evaluation of "the effects of the amendments made by [title I of the DMCA] and the development of electronic commerce and associated technology on the operation of sections 109 and 117 of title 17, United States Code; and the relationship between existing and emergent technology and the operation of sections 109 and 117 . . . ."[4] It is an outgrowth of proposals that were made contemporaneously with the consideration of the DMCA, but were not adopted in the law. Specifically, this Report focuses on two proposals that were characterized as vital to the continued growth of electronic commerce by their proponents: creation of a digital first sale doctrine to permit certain retransmissions of downloaded copies of works in digital form; and an exemption for certain digital reproductions that are incidental to the use of a copyrighted work in conjunction with a machine. One additional issue that was raised during the preparation of the Report, and appears to fall within the scope set forth by Congress in section 104 of the DMCA, is the appropriate breadth and formulation of the exception for making archival copies of computer programs in section 117.

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[3] The results of that joint Copyright Office and NTIA study were presented to Congress in May 2000 and are available at: www.loc.gov/copyright/reports/studies/dmca_report.html.

[4] DMCA, Pub. L. No. 105-304, § 104(a), 112 Stat. 2860, 2876 (1998).

The DMCA contemplated that, like the report on encryption research, the present effort would be a joint report of the Copyright Office and NTIA. In March 2001, however, NTIA released its own report. This Report, consequently, is exclusively the work of the Copyright Office. All of the views expressed and the recommendations made are, necessarily, solely those of the Register of Copyrights.

I. BACKGROUND

A. THE DIGITAL MILLENNIUM COPYRIGHT ACT

The DMCA was "designed to facilitate the robust development and world-wide expansion of electronic commerce, communications, research, development, and education in the digital age."[5] The DMCA grew out of legislation introduced to implement the provisions of two treaties concluded in Geneva, Switzerland in December 1996. These two treaties – which are sometimes referred to as the "Internet Treaties" – updated international copyright norms to account for the advent of digital networks. Title I of the DMCA implements the treaties, "thereby bringing the U.S. copyright law squarely into the digital age and setting a marker for other nations who must also implement these treaties."[6] Congress crafted title I to "protect property rights in the digital world."[7]

1. The WIPO Treaties

On December 20, 1996, at the conclusion of a three-week Diplomatic Conference held in Geneva, Switzerland, headquarters of the World Intellectual Property Organization (WIPO), delegations from 127 countries and the European Commission agreed on the text of two new treaties on copyright and neighboring rights: the WIPO Copyright Treaty (WCT) and the WIPO

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[5] S. Rep. No. 105-190, at 1-2 (1998).

[6] Id. at 2.

[7] Staff of House Committee on the Judiciary, 105' Cong., Section-by-Section Analysis of H.R. 2281 as Passed by the United States House of Representatives on August 4, 1998, at 2 (Comm. Print 1998) (Serial No. 6) (hereinafter House Manager's Statement). As the Senate Judiciary Committee noted, "[due to the ease with which digital works can be copied and distributed worldwide virtually instantaneously, copyright owners will hesitate to make their works readily available on the Internet without reasonable assurance that they will be protected against massive piracy. Legislation implementing the treaties provides this protection and creates the legal platform for launching the global digital on-line marketplace for copyrighted works." S. Rep. No. 105-190, at 8 (1998).

Performances and Phonograms Treaty (WPPT). The Diplomatic Conference was the culmination of a process that began formally in 1991 when a "Committee of Experts" was convened at WIPO to discuss a possible protocol to the Berne Convention for the Protection of Literary and Artistic Works (Berne)[8].

Berne is the principal multilateral agreement for protecting copyrights internationally. Berne establishes minimum levels of protection that all member countries must grant to authors, and requires member countries to grant national treatment to authors from other member countries. The last general revision of Berne took place in 1971. Technological and legal developments during the intervening two decades made updating Berne an imperative in the international copyright community.

In addition, the United States sought to introduce the subject of improved protection for sound recordings into the early Berne Protocol discussions. Rather than incorporating the subject of protection for sound recordings in the Berne Protocol, it was placed on a parallel track that had as its goal the creation of a separate "new instrument" for the protection of performers and producers — reflecting the civil law tradition of protecting performers and producers of sound recordings under the separate rubric of neighboring rights (or related rights, as they are sometimes called), rather than copyright.

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[8] Berne Convention for the Protection of Literary and Artistic Works (Paris Act 1971).

In 1993, at the urging of the United States, the Committees of Experts on the Berne Protocol and the New Instrument began considering the possible need for new international norms to address the effects on copyright owners of digital technologies and the rapid growth of digital networks?[9] The emergence and widespread use of these technologies exposed copyright owners to substantial risks of massive global piracy, while at the same time holding out the promise of new markets, new distribution channels and new means of licensing copyrighted works. In addition, digital technology created greater possibilities to use technological means to foil would-be infringers.

A central component of the "digital agenda" in the Berne Protocol and New Instrument discussions was to include in any new treaty a measure against the circumvention of technological measures employed by right holders to protect their rights. By 1993 it was widely recognized that, while use of technological measures to protect works was likely to become a critical element in a digital network environment, those measures were vulnerable to tampering. Widespread availability and use of devices or software for circumventing technological measures would imperil the right holder's reproduction right and, ultimately, could serve to dissuade right holders from making their works available in digital form.

Proposals up to and including the documents prepared for the 1996 Diplomatic Conference focused on prohibiting the making and selling of devices, or provision of services,

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[9] *E.g.*, WIPO. Questions Concerning a Possible Protocol to the Berne Convention — Part III, New Items. WIPO Doc. No. BCP/CE/III/2-III at ¶¶74-75 (March 12.1993).

for the purpose of circumvention. The obligation adopted by the Diplomatic Conference and set forth in Article 11 of the WCT and Article 18 of the WPPT is somewhat less precise. Rather than specifying the particular means of achieving the desired result —the prevention of circumvention of technological protection measures — the treaties require Contracting Parties to put in place adequate and effective legal measures for achieving that result.[10] Contracting Parties are afforded a degree of flexibility in determining precisely how to implement this obligation within their respective legal systems, provided that the implementation is adequate and effective against circumvention.

2. implementation of the WIPO Treaties in the DMCA

The Administration proposed and Congress adopted a minimalist approach in implementing the WCT and the WPPT in U.S. law.[11] In this context, "minimalist" was understood to mean that any provision of the treaty that was already implemented in U.S. law would not be addressed in new legislation. As to treaty obligations that were not adequately

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[10] Article 11 of the WCT states:

> Contracting Parties shall provide adequate legal protection and effective legal remedies against the circumvention of effective technological measures that are used by authors in connection with the exercise of their rights under this Treaty or the Berne Convention and that restrict acts, in respect of their works, which are not authorized by the authors concerned or permitted by law.

Article 18 of the WPPT states:

> Contracting Parties shall provide adequate legal protection and effective legal remedies against the circumvention of effective technological measures that are used by performers or producers of phonograms in connection with the exercise of their rights under this Treaty and that restrict acts, in respect of their performances or phonograms, which are not authorized by the performers or the producers of phonograms concerned or permitted by law.

[11] The U.S. took the same approach in implementing the Berne Convention in *1988*. See H.R. Rep. No. 100-609, at 20 (1988).

addressed in existing U.S. law, new measures would have to be adopted in implementing legislation in order to satisfy these obligations.

Protection against circumvention was determined not to be adequately covered by U.S. law. Certain specific instances of circumvention were prohibited by federal law, such as unauthorized decryption of encrypted satellite signals and trafficking in the means to do so,[12] but coverage was not comprehensive. To the extent that circumvention requires reproduction of the work that is protected by a technological measure, an act of circumvention can constitute copyright infringement. In addition, some instances of providing devices that circumvent technological measures could constitute contributory copyright infringement, but those circumstances would be extremely narrow — confined essentially to those instances where the device used to circumvent has no substantial noninfringing uses.[13] Consequently, new legislation was deemed necessary to implement the anticircumvention obligation in Article 11 of the WCT and Article 18 of the WPPT.[14]

a. *Section 1201 - Anticircumvention*

A principal means of addressing the risk of infringement in the digital age was to encourage copyright owners to help themselves by using technological measures to protect works

[12] 47 U.S.C. § 605.

[13] See *Sony Corp. v. Universal City Studios, Inc.*, 464 U.S. 417, 442 (1984) (manufacture of a staple article of commerce such as a copying device is not contributory infringement if it is "merely. . . capable of substantial noninfringing uses").

[14] H.R. 2281, 105th Cong., 1st Sess. (1997); S. 1146, 105th Cong., 1st Sess. (1997).

in digital form. Section 1201 of the DMCA reinforces those technological measures through legal sanctions against those who circumvent them. Not only does section 1201 prohibit the manufacture and distribution of devices, and the rendering of services, for the purpose of circumventing technological measures that protect against unauthorized access to works, or unauthorized exercise of the rights of the copyright owner, it also addresses the conduct of circumventing a technological measure that protects access.

It was determined early in the legislative drafting process that a prohibition on the ***devices and services*** that enable circumvention (the original focus of the treaty proposals) would be a critical element in treaty implementation, notwithstanding the fact that the treaty obligation was formulated broadly enough to include, potentially, national laws directed at the *act* of circumventing technological protection measures. Since the act of circumvention frequently entails copyright infiingement, or is immediately followed by an act of infringement, a legal prohibition focusing exclusively on the act of circumvention would add little to existing protections under copyright, and would suffer from the same practical difficulties in enforcement." Whether under copyright or under a specific prohibition on circumvention, a copyright owner's only recourse would be to detect individual violations by users of copyrighted works and bring a multitude of actions against the violators unfortunate enough to get caught. From a practical standpoint this outcome was viewed as an expensive, inefficient, and ultimately ineffective means of combating on-line infringement. By contrast, a prohibition on the

[15] *Cf.* S. Rep. No. 105-190, at 12 (1998) ("The copyright law has long forbidden copyright infringements, so no new prohibition [on circumvention of copy control technologies] was necessary.")).

manufacture, import or sale of devices, or rendering of services, for the circumvention of technological measures can prevent infringement by keeping the tools that enable circumvention out of the hands of individual users.

In addition to ensuring that protection against circumvention would be adequate and effective as required by the treaties, the drafters of the implementing legislation sought to protect the countervailing interest of users in their continuing ability to engage in noninfringing uses of copyrighted works. The principal means of accomplishing this goal was to divide technological protection measures into two categories — measures that control access to a work and measures that control the exercise of exclusive rights with respect to a work — and to treat these categories differently.

Fair use and other exceptions and limitations to a copyright owner's exclusive rights are defenses to copyright infringement — that is, the unauthorized exercise of the copyright owner's exclusive rights. Technological measures that control or prevent the exercise of those exclusive rights (often referred to by the shorthand phrase "copy control measures") thus have a direct relationship to fair use and other copyright exceptions. Activity that may be permitted under these exceptions could, nonetheless, result in liability under a prohibition on circumvention that included copy control measures. For this reason, the implementing legislation proposed by the Administration did not (and the DMCA does not) prohibit the conduct of circumventing of copy control measures.

By contrast, fair use and other copyright exceptions are not defenses to gaining unauthorized access to a copyrighted work Quoting a manuscript may be a fair use; breaking into a desk drawer and stealing it is not.[16] Circumventing access control measures was, therefore, prohibited in the Administration's proposed implementing legislation.

As to both types of technological measures, trafficking in circumvention tools — devices and services that enable circumvention — was prohibited under the Administration proposal if those tools meet at least one of three statutory criteria relating to the purpose for which the tool is designed, the predominant commercially significant use of the tool and the purpose for which the tool is marketed. This basic structure was retained throughout the legislative process and has been enacted into law as part of the DMCA.[17]

b. *Section 1202 - Copyright Management Information*

In addition to the anticircumvention provisions of title I, Congress also found that U.S. law did not adequately meet the requirements of the WIPO treaties that require contracting states to prohibit the removal or alteration of copyright management information (CMI).[18] As a

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[16] See H.R.Rep. No. 105-551, pt. 1, at 17 (1998) ("The act of circumventing a technological protection measure put in place by a copyright owner to control access to a copyrighted work is the electronic equivalent of breaking into a locked room in order to obtain a copy of a book.") (House Judiciary Committee).

[17] 17 U.S.C. § 1201

[18] Article 12 of the WCT provides in relevant part

> Contracting Parties shall provide adequate and effective legal remedies against any person knowingly performing any of the following acts knowing, or with respect to civil remedies having reasonable grounds to know, that it will induce, enable, facilitate or conceal an infringement of any right covered by this Treaty or the Berne Convention:
>
> (i) to remove or alter any electronic rights management information without

consequence, Congress enacted a new section as part of title I of the DMCA implementing the obligation to protect the integrity of CMI.[19] The scope of protection for this section is set out in two separate paragraphs, the first addressing false CMI[20] and the second prohibiting the removal or alteration of CMI. Subsection (a) prohibits the knowing provision or distribution of false CMI, if done with the intent to induce, enable, facilitate or conceal infringement. Subsection (b) bars the intentional removal or alteration of CMI without the authority of the copyright owner, as well as the dissemination of CMI or copies of works, knowing that the CMI has been removed or altered without authority. These provisions of the DMCA differ from other copyright provisions in title 17 in that they require that the act be done with knowledge or, with respect to civil remedies, with reasonable grounds to know that it will induce, enable, facilitate or conceal an infringement.

The implementation of these provisions to protect the integrity of CMI in U.S. law go beyond the minimum requirements in the two WIPO treaties?' The law does not, however,

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> authority;
>
> (ii) to distribute, import for distribution, broadcast or communicate to the public, without authority, works or copies of works knowing that electronic rights management information has been removed or altered without authority.

Article 19 of the WPPT contains nearly identical language.

[19] 17 U.S.C. § 1202.

[20] Provision of false CMI is not prohibited under the WIPO treaties. A prohibition on false CMI was, however, proposed in an Administration white paper in 1995, and introduced in Congress that same year. Information Infrastructure task force, Intellectual Property and the National Information Infrastructure: The Report of the Working Group on Intellectual Property Rights 235-36 (1995); H.R. 2441, 104th Cong., 1st Sess. § 4 (1995); S. 1284, 104th Cong., 1st Sess. § 4 (1995). It appears these proposals carried over into the Administration proposal for treaty implementation and, ultimately, into the DMCA as enacted.

[21] See supra note 20.

address the liability of persons who manufacture devices or provide services and it does not mandate the use of CMI or any particular type of CMI. It "merely protects the integrity of CMI if a party chooses to use it in connection with a copyrighted work."[22]

c. *Origin of the Present Report*

During the legislative process leading to the enactment of the DMCA, there were concerns raised about the adverse effects of these new protections on traditional noninfringing uses of copyrighted works that were privileged under limitations of the exclusive rights in the Copyright Act. In particular, concerns about the future viability of, *inter alia,* fair use and the first sale doctrine, and about liability for temporary incidental copies, were raised by segments of the public and Members of Congress.

One remedial method of addressing these concerns was the incorporation of a triennial rulemaking proceeding to be conducted by the Copyright Office.[23] This rulemaking process was created to examine whether section 1201(a)(1) has had or is likely to have any adverse effect on noninfringing uses of copyrighted works. It was intended to operate as a recurring means of monitoring the effect of section 1201(a)(1) on the market. Congress provided the Librarian of Congress with the regulatory authority to exempt "particular classes of works" for which users of copyrighted works were adversely affected in their ability to make noninfringing uses. On

[22] House Manager's Statement, *supra* note 7 at 20.

[23] *Id.* § 1201(a)(1)(C).

October 27,2000, the results of the first rulemaking proceeding were published in the Federal Register.[24]

Another response to the concerns about the continued applicability of the first sale doctrine in section 109 of the Copyright Act and the temporary reproductions that are incidental to lawful uses of works on digital equipment was a bill proposed by Representative Rick Boucher and Representative Tom Campbell (the "Boucher-Campbell bill").[25] One of the changes suggested in this bill was a modification of section 109 to make the first sale privilege apply expressly to digital transmissions of copyrighted works.[26] Another section of the bill proposed amending section 117 of the Copyright Act to allow reproductions of digital works that were incidental to the operation of a device and that did not affect the normal exploitation of the work.[27] At that time, based on the evidence available to it, Congress did not adopt this proposal.

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[24] 65 Fed. Reg. 64.556 (October 27,2000). Exemption to Prohibition on Circumvention of Copyright Protection Systems for Access Control Technologies. Final rule.

[25] H.R.3048. 105th Cong.. 1st Sess. (1997).

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SEC. 4. FIRST SALE.

Section 109 of title 17, United States Code. is amended by adding the following new subsection at the end thereof:

'(f) The authorization for use set forth in subsection (a) applies where the owner of a particular copy or phonorecord in a digital format lawfully made under this title, or any person authorized by such owner, performs, displays or distributes the work by means of transmission to a single recipient if that person erases or destroys his or her copy or phonorecord at substantially the same time. The reproduction of the work, to the extent necessary for such performance, display, distribution, is not an infringement.

[27]

SEC. 6. LIMITATIONS ON EXCLUSIVE RIGHTS.

(a) TITLE- The title of section 117 of title 17, United States Code, is amended to read as follows:

Instead Congress chose to have the Copyright Office and NTIA jointly conduct a study. In setting the parameters of this Report, however, the legislative history demonstrates that the scope of the Report was not intended to comprehend the full sweep of the proposals made in the Boucher-Campbell bill.[28]

'Sec. Limitations on exclusive rights: Computer programs and digital copies';

(b) DIGITAL COPIES–Section 117 of title 17, United States Code, is amended by inserting '(a)' before 'Notwithstanding' and inserting the following as a new subsection (b):

'(b) Notwithstanding the provisions of section 106, it is not an infringement to make a copy of a work in a digital format if such copying–

'(1) is incidental to the operation of a device in the course of the use of a work otherwise lawful under this title; and

'(2) does not conflict with the normal exploitation of the work and does not unreasonably prejudice the legitimate interests of the author.'

[28] The Boucher-Campbell bill also included proposals on the following:

expanding fair use to include uses by analog or digital transmission in connection with teaching, research, and other specified activities. The proposal was not acted on;

expanding the rights of libraries and archives to reproduce and distribute copies or phonorecords to authorize three copies or phonorecords to be reproduced or distributed for preservation. security, or replacement purposes, and to permit such copies to be in digital form. This proposal, with some modifications, was enacted as section 404 of the DMCA;

revising limitations on exclusive rights to provide for certain distance education activities. The DMCA directed the Register of Copyrights to study the issue of promoting distance education through digital technologies and provide recommendations to Congress. Copyright Office, "Report on Copyright and Digital Distance Education" *(1999)*. Based in large part on recommendations made in the Copyright Office's Study, this proposal has now been taken up in S. 487, which passed the Senate and is currently pending in the House;

preemption of terms in non-negotiated licenses that abrogate or restrict the limitations on exclusive rights in chapter 1 of the Copyright Act. This proposal was not acted on. See discussions *infra* at 69-71 and 162-164;

copyright protection and management systems. These provisions were proposed as an alternative to the anticircumvention and CMI provisions of the DMCA. The DMCA version prevailed and was enacted.

In an amendment to H.R. 2281 offered by Representative Rick White and adopted by the House Commerce Committee, what was to become the joint study by the Copyright Office and NTIA was introduced into the DMCA. Section 205 of the House Commerce Committee proposal called for a broad evaluation of the copyright law and electronic commerce "to ensure that neither the copyright law nor electronic commerce inhibits the development of the other."[29]

By the time the bill reached the House floor on August 4, 1998, the language regarding the joint study by the Copyright Office and NTIA had been pared back to focus on an evaluation of "the impact of this title and the development of electronic commerce on the operation of sections 109 and 117 of title 17, and the relationship between existing and emerging technology

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[29] Id. § 6 H.R. Rep.No. 105-551, pt. 2, at (1998) at 18.

SEC. 205. EVALUATION OF IMPACT OF COPYRIGHT LAW AND AMENDMENTS ON ELECTRONIC COMMERCE AND TECHNOLOGICAL DEVELOPMENT.

(a) FINDINGS–In order to maintain strong protection for intellectual property and promote the development of electronic commerce and the technologies to support that commerce, the Congress must have accurate and current information on the effects of intellectual property protection on electronic commerce and technology. The emergence of digital technology and the proliferation of copyrighted works in digital media, along with the amendments to copyright law contained in this Act, make it appropriate for the Congress to review these issues to ensure that neither copyright law nor electronic commerce inhibits the development of the other.

(b) EVALUATION BY SECRETARY OF COMMERCE–The Secretary of Commerce, in consultation with the Assistant Secretary of Commerce for Communications and Information and the Register of Copyrights, shall evaluate–

(1) the effects of this Act and the amendments made by this Act on the development of electronic commerce and associated technology; and

(2) the relationship between existing and emergent technology and existing copyright law.

(c) REPORT TO CONGRESS–The Secretary of Commerce shall, not later than 1 year after the date of the enactment of this Act, submit to the Congress a report on the evaluation conducted under subsection (b), including any legislative recommendations the Secretary may have.

on the operation of those provisions."[30] This change makes it clear that Congress was not seeking a broad review of copyright and electronic commerce issues, but focused instead on two particular sections of the Copyright Act.

In explaining the reasons for examining section 109, the House Manager's Statement stated that:

> [t]he first sale doctrine does not readily apply in the digital networked environment because the owner of a particular digital copy usually does not sell or otherwise dispose of the possession of that copy. Rather, "disposition" of a digital copy by its owner normally entails reproduction and transmission of that reproduction to another person. The original copy may then be retained or destroyed. The appropriate application of this doctrine to the digital environment merits further evaluation and this section therefore calls for such an evaluation and report."[31]

The reference to section 109 in the bill plainly refers back to the digital first sale proposal in the Boucher-Campbell bill. Although there is no similar legislative history explaining why section 117 is included in the Report, the most likely explanation is that it is an oblique reference to the proposed exception for incidental copies in section 6 of the Boucher-Campbell bill – particularly given the absence of any contemporaneous discussions concerning the scope of the computer program exemptions in section 117 (apart from title III of the DMCA). The Boucher-Campbell proposal on incidental copies would have been codified in section 117 of the Copyright Act.

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[30] House Manager's Statement, *supra* note 7. at 24. The conference committee made no substantive changes to the language of this section, which was ultimately enacted as section 104 of the DMCA.

[31] *Id.*

As ultimately enacted, section 104 of the DMCA requires the Copyright Office and NTIA jointly to evaluate:

> (1) the effects of the amendments made by this title and the development of electronic commerce and associated technology on the operation of sections 109 and 117 of title 17, United States Code; and
>
> (2) the relationship between existing and emergent technology and the operation of sections 109 and 117 of title 17, United States Code.

B. SECTION 109 AND THE FIRST SALE DOCTRINE

Section 109 of the Copyright Act restates the principle commonly referred to as the "first sale doctrine." Under the first sale doctrine a copyright owner does not retain the legal right to control the resale or other distribution of copies or phonorecords of a work that have already been lawfully sold. The first sentence of section 109(a) of the Copyright Act provides:

> Notwithstanding the provisions of section 106(3), the owner of a particular copy or phonorecord lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord.

It is this provision of the copyright law that permits sales of used books and CDs, lending of books and other copyrighted materials by libraries, and rentals of videocassettes, among other activities, without the need to obtain the permission of copyright owners or make royalty payments.

1. History of the First Sale Doctrine

The first sale doctrine was initially a judicial doctrine. In *Bobbs-Merrill Co. v. Straus*,[32] the U.S. Supreme Court held that a copyright owner's exclusive right to "vend" did not permit it to impose a price limitation on the retail sale of books in the absence of any agreement as to the future sale price. In its interpretation of the reach of the vending right, the Court expressed doubt that Congress intended to abrogate the common-law principle that restraints on the alienation of tangible property are to be avoided. It posed and answered a series of rhetorical questions:

> What does the statute mean in granting 'the sole right of vending the same'? Was it intended to create a right which would permit the holder of the copyright to fasten, by notice in a book or upon one of the articles mentioned within the statute, a restriction upon the subsequent alienation of the subject-matter of copyright after the owner had parted with the title to one who had acquired full dominion over it and had given a satisfactory price for it? It is not denied that one who has sold a copyrighted article, without restriction, has parted with all right to control the sale of it. The purchaser of a book, once sold by authority of the owner of the copyright, may sell it again, although he could not publish a new edition of it?'

The Court drew a sharp distinction between the reproduction right and the right to vend. It noted, as a matter of statutory construction, that the reproduction right was the "main purpose" of the copyright law, and the right to vend existed to give effect to the reproduction right.[34] Since a grant of control to the copyright owner over resales would not further this main purpose of

[32] 210 U.S. 339 (1908).

[33] *Id.* at 349-50.

[34] *Id.* at 350-51.

protecting the reproduction right, the Court was unwilling to read the statute as providing such a grant:[35]

> In our view the copyright statutes, while protecting the owner of the copyright in his right to multiply and sell his production, do not create the right to impose . . . a limitation at which the book shall be sold at retail by future purchasers, with whom there is no privity of contract. This conclusion is reached in view of the language of the statute, read in the light of its main purpose to secure the right of multiplying copies of the work. . . . True, the statute also secures, to make this right of multiplication effectual, the sole right to vend copies of the book. . . . To add to the right of exclusive sale the authority to control all future retail sales . . . would give a right not included in the terms of the statute, and, in our view, extend its operation, by construction, beyond its meaning, when interpreted with a view to ascertaining the legislative intent in its enactment.[36]

The parties in *Bobbs-Merrill* also raised, and the Court of Appeals addressed, antitrust concerns. Although the Supreme Court did not address these concerns, it was undoubtedly aware of them,[37] and competition policy is viewed as one of the underlying bases for the first sale doctrine.[38]

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[35] *Id.*

[36] *Id.*

[37] "This conclusion renders it unnecessary to discuss other questions noticed in the opinion in the Circuit Court of Appeals, or to examine into the validity of the publisher's agreements. alleged to be in violation of the acts to restrain combinations creating a monopoly or directly tending to the restraint of trade." *Id.*

[38] See MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT §8.12[A] [hereinafter NIMMER].

2. Legislative History of Section 109

The year following the *Bobbs-Merrill* decision, Congress codified the first sale doctrine in the Copyright Act of 1909.[39] Section 109(a) of the Copyright Act of 1976 carried forward the existing federal policy of terminating a copyright owner's distribution right as to a particular lawfully-made copy or phonorecord of a work after the first sale of that copy. The House Report explains:

> Section 109(a) restates and confirms the principle that, where the copyright owner has transferred ownership of a particular copy or phonorecord of a work, the person to whom the copy or phonorecord is transferred is entitled to dispose of it by sale, rental, or any other means. Under this principle, which has been established by the court decisions and section 27 of the present law, the copyright owner's exclusive right of public distribution would have no effect upon anyone who owns "a particular copy or phonorecord lawfully made under this title" and who wishes to transfer it to someone else or to destroy it.[40]

Section 109 creates a two-prong test for eligibility for the privileges[41] under section 109. First, the person must be the owner of the copy[42] at issue. This applies to ownership of the

[39] Section 27 of the 1909 Copyright Act provided

> The copyright is distinct from the property in the material object copyrighted, and the sale or conveyance, by gift or otherwise, of the material object shall not of itself constitute a transfer of the copyright, nor shall the assignment of the copyright constitute a transfer of the title to the material object; ***but nothing in this title shall be deemed to forbid, prevent, or restrict the transfer of any copy of a copyrighted work the possession of which has been lawfully obtained.***

17 U.S.C. § 27 (1977) (emphasis added).

[40] H.R. Rep. No. 94-1476, at 79 (1976) ["1976 House Report"].

[41] Many of the commenters referred to the first sale doctrine as a "right." This is an inartful term to describe the doctrine. Rights are guaranteed to individuals and are generally enforceable in court. The first sale doctrine is not an enforceable right from the standpoint of the owner of a copy – that is, there is no independent remedy if a person is effectively denied the benefits of section 109 through technological or contractual means. The first sale doctrine is a limitation to the scope of copyright; specifically it is a limitation to the distribution right of copyright owners.

[42] For convenience, the term "copy" will be used with the understanding that it incorporates phonorecords as well.

tangible item (e.g., a book, photograph, videocassette, CD, floppy disc, etc.) in which a copyrighted work is fixed.[43] While ownership may be obtained by virtue of a sale, this prong is also satisfied if ownership is obtained by virtue of gift, bequest, or other transfer of title.[44] It does not apply to mere possession, regardless of whether that possession is legitimate, such as by rental, or illegitimate, such as by theft.[45] Nor does it refer to ownership of the copyright or of any of the exclusive rights.[46]

Second, that copy must have been lawfully made. Ownership of a copy that is not authorized by either the copyright owner or the law, even if the owner is unaware of the piratical nature of the copy, does not permit the owner to avail himself of section 109.[47] Nothing in the statute limits the manner in which the making of the copy may be accomplished, so long as the resulting copy is lawful.

The statute does not distinguish between analog and digital copies. Consequently, it does not matter whether the work is embodied in an analog videocassette or a digital DVD – the copyright owner's distribution right with respect to that particular copy is extinguished once

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[43] Nimmer, *supra* note 38, at § 8.12[B][1].

[44] *Id.*

[45] *Id.*

[46] *Id.*

[47] Nimmer, *supra* note 38, at § 8.12[B][4].

ownership of the copy has been transferred, and the new owner is entitled to dispose of that copy as he desires.

3. Subsequent Amendments to Section 109

Congress has seen fit on three occasions to limit the effect of the first sale doctrine. In the Record Rental Amendment of 1984,[48] Congress amended section 109 to allow copyright owners of sound recordings and the musical works embodied therein to retain the exclusive right to dispose of a particular phonorecord by rental, lease or lending for purposes of direct or indirect commercial advantage, even after a lawful first sale of that phonorecord. The purpose of the amendment was to prevent the displacement of record sales by "rentals" that were, in fact, thinly-disguised opportunities for consumers to make personal copies of records without buying them.[49] In essence the so-called "rental right" serves to guard against infringement of the reproduction right. Congress extended the same concept to computer programs in the Computer Software Rental Amendments Act of 1990.[50] Both provisions have been incorporated into multilateral agreements and are now widely-accepted international standards.[51]

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[48] Pub. L. No. 98-450, 98 Stat. 1727 (1984).

[49] H.R. Rep. No. 98-987, at 2 (1983).

[50] Title VII of the Judicial Improvements Act of 1990, Pub. L. No. 101-650, 104 Stat. 5089.5134 (1990). Both the Record Rental Amendment and the Computer Software Rental Amendments Act are codified at 17 U.S.C. § 109(b).

[51] Agreement on Trade-Related Aspects of Intellectual Property Rights ("TRIPS"). Articles 11 and 14.4 (1994); WIPO Copyright Treaty, Article 7 (1996); WIPO Performances and Phonograms Treaty, Articles 9 and 13 *(1996)*.

Congress also limited the effect of the first sale doctrine when, in the course of implementing U.S. obligations under the TRIPS agreement in 1994, it extended copyright protection to certain preexisting works of foreign origin that had previously fallen into the public domain in the United States. Under section 109(a), as amended by the Uruguay Round Agreements Act,[52] copies embodying certain restored copyrights may not be sold or otherwise disposed of without the authorization of the copyright owner more than twelve months after the person in possession of the copies receives actual or constructive notice that the copyright owner intends to enforce his rights in the restored work.

By the same token, Congress has, on one occasion, expanded the first sale doctrine to cover not only the distribution right, but the public performance and public display rights as well.[53] Although legislatively sunsetted on October 1, 1995, section 109(e) permitted the public performance or display of an electronic videogame intended for use in coin-operated equipment.[54]

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[52] Pub. L. No. 103-465, 108 Stat. 4809, 4981 (1994).

[53] Section 109(c) also permits public display in limited circumstances: "Notwithstanding the provisions of section 106(5), the owner of a particular copy lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to display that copy publicly, either directly or by the projection of no more than one image at a time, to viewers present at the place where the copy is located." This provision permits, *among* other things, the display of a painting in a museum or public art gallery by the purchaser of the painting.

[54] Pub. L. No. 101-650, § 804(c), 104 Stat. 5089, 5136 (1990) was enacted as part of the Computer Software Rental Amendments of 1990 in order to overturn the result in *Red Baron-Franklin Park Inc. v. Taito Corp.*, 883 F.2d 275 (4th Cir. 1989), *cert. denied*, 493 U.S. 1058 (1990), a case which held that a copyright owner could prevent the purchaser of gray market circuit boards containing a copyrighted videogame from performing the videogame in a video arcade.

C. SECTION 117 COMPUTER PROGRAM EXEMPTIONS

Section 117 of the Copyright Act limits the exclusive rights of copyright owners by allowing the lawful owner of a copy of a computer program to make or authorize the making of another copy or adaptation of that program only for archival purposes or if it is necessary as an essential step in the utilization of the program in conjunction with a machine.[55]

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[55] In its entirety, section 117 reads as follows:

§ 117. Limitations on exclusive rights: Computer programs

(a) Making of Additional Copy or Adaptation by Owner of Copy.-Notwithstanding the provisions of section 106, it is not an infringement for the owner of a copy of a computer program to make or authorize the making of another copy or adaptation of that computer program provided

(1) that such a new copy or adaptation is created as an essential step in the utilization of the computer program in conjunction with a machine and that it is used in no other manner, or

(2) that such new copy or adaptation is for archival purposes only and that all archival copies are destroyed in the event that continued possession of the computer program should cease to be rightful.

(b) Lease. Sale, or Other Transfer of Additional Copy or Adaptation.-Any exact copies prepared in accordance with the provisions of this section may be leased, sold, or otherwise transferred, along with the copy from which such copies were prepared, only as part of the lease. sale, or other transfer of all rights in the program. Adaptations so prepared may be transferred only with the authorization of the copyright owner.

(c) Machine Maintenance or Repair.-Notwithstanding the provisions of section 106, it is not an infringement for the owner or lessee of a machine to make or authorize the making of a copy of a computer program if such copy is made solely by virtue of the activation of a machine that lawfully contains an authorized copy of the computer program, for purposes only of maintenance or repair of that machine, if-

(1) such new copy is used in no other manner and is destroyed immediately after the maintenance or repair is completed; and

(2) with respect to any computer program or part thereof that is not necessary for that machine to be activated, such program or part thereof is not accessed or used other than to make such new copy by virtue of the activation of the machine.

(d) Definitions.-For purposes of this section-

(1) the "maintenance" of a machine is the servicing of the machine in order to make it work in accordance with its original specifications and any changes to those specifications authorized for that machine; and

In addition, pursuant to an amendment contained in title III of the DMCA,[56] section 117 permits the owner or lessee of a machine to make or authorize the making of a temporary copy of a computer program if such copy is made solely by virtue of the activation of a machine that lawfully contains an authorized copy of the computer program, for purposes of maintenance or repair of that machine. The exemption only permits a copy that is made automatically when a computer is activated, and only if the computer already lawfully contains an authorized copy of the program. The new copy cannot be used in any other manner and must be destroyed immediately after the maintenance or repair is completed.

1. Legislative History of Section 117

a. *Recommendations of CONTU*

The transformation of section 117 into its current form dealing with computer programs began in the 1970s. When the 1976 Act took effect on January 1, 1978, Congress' approach to problems relating to computer uses of copyright works was still "not sufficiently developed for a definitive legislative solution."[57] Congress enacted what was commonly referred to as a "moratorium" provision in section 117, which preserved the status quo on December 31, 1977 (i.e., the day before the 1976 Copyright Act became effective) as to use of copyrighted works in conjunction with computers and similar information systems.[58]

> (2) the "repair" of a machine is the restoring of the machine to the state of working in accordance with its original specifications and any changes to those specifications authorized for that machine.

[56] Computer Maintenance Competition Assurance Act, Pub. L. No. 105-304, 112 Stat. 2860, 2886 (1998). codified at 17 U.S.C. § 117.

[57] 1976 House Report, *supra* note 40, at 116.

[58] *Id.* at 19. Former section 117 provided

Notwithstanding the provisions of sections 106 through 116 and 118, this title does not afford to

Congress stated at that time that it would look to the National Commission on New Technological Uses of Copyrighted Works (CONTU) to "recommend definitive copyright provisions to deal with the situation."[59] CONTU was created in 1974[60] to assist the President and Congress in developing a national policy for both protecting the rights of copyright owners and ensuring public access to copyrighted works when they are used in computer and machine duplication systems, bearing in mind the public and consumer interest.

Between CONTU's inception in 1974 and the issuance of its final report on July 31, 1978, the 1976 Copyright Act was enacted and became effective![61] The final report recommended that section 117 as enacted in 1976 be repealed in its entirety to ensure that the generally applicable copyright rules set forth in the 1976 Copyright Act apply to all computer uses of copyrighted works.[62] In addition, CONTU proposed that the Act be amended: (1) to define "computer program";[63] (2) to ensure that rightful possessors of copies of computer programs may use or adapt these copies for their use, because "placement of a work into a

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the owner of copyright in a work any greater or lesser rights with respect to the use of the work in conjunction with automatic systems capable of storing, processing, retrieving, or transferring information, or in conjunction with any similar device, machine or process, than those afforded to works under the law, whether title 17 or the common law or statutes of a State, in effect on December 31, 1977, as held applicable and construed by a court in action brought under this title.

[59] 1976 House Report, *supra* note 40, at 116.

[60] Pub. L. No. 93-573, 88 Stat. 1873 (1974).

[61] Final Report of the National Commission on New Technological Uses of Copyrighted Works 3-4 (1979) [hereinafter CONTU Report]. Although the report was issued in 1978, it was published in 1979.

[62] Id. at 12-13.

[63] Congress had already made it clear in legislative history that computer programs, to the extent that they embody a programmer's original expression, were protected under copyright within the category of "literary works." 1976 House Report, *supra* note 40, at 54.

computer is the preparation of a copy;"[64] and (3) to permit rightful possessors of computer programs to make archival (backup) copies of programs to "guard against destruction or damage by mechanical or electrical failure."[65]

b. *The 1980 Computer Software Copyright Amendments*

Congress adopted CONTU's recommendations in the Computer Software Copyright Amendments of 1980 with few changes.[66] The House Report accompanying the 1980 amendments did not explain the intent of the legislation, other than to "implement the recommendations of the [CONTU] Commission with respect to clarifying the law of copyright of computer software."[67] In the absence of a substantive discussion in the committee report, some courts have treated the CONTU Report as the legislative history of the 1980 amendments to the Copyright Act.[68] Other courts have expressed scepticism regarding the use of a report by an independent commission as evidence of congressional intent.[69]

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[64] CONTU Report, *supra* note 61, at 13.

[65] *Id.*

[66] Pub. L. No. 96-517, 94 *Stat.* 3015.3028 (1980). Congress changed "rightful possessor" to "owner."

[67] H.R. Rep No. 96-1307, pt. I (1980).

[68] *See, e.g., Apple Computer. Inc. v. Formula Int'l, Inc.*, 725 F.2d 521.525 (9th Cir. 1984) (employing CONTU Report as legislative history of the 1980 amendments); *Apple Computer, Inc. v. Franklin Computer Cop.*, 714 F.2d 1240, 1247-48, 1252 (3d Cir. 1983) (same).

[69] *See, e.g., Lotus Dev. Cop. v. Borland Int'l. Inc.*, 788 F. Supp. 78.93 (D. Mass. 1992), *rev'd on other grounds*, 49 F.3d 807 (1st Cir. 1995), *aff'd by an equally divided Court*, 116 *S. Ct.* 804 (1996).

As enacted in 1980, section 117 permits the owner of a copy of a computer program to make an additional copy of the program for archival purposes[70], or where the making of such a copy is "an essential step in the utilization of the computer program in conjunction with a . machine and . . . is used in no other manner. . . ."[71]

c. *The Computer Maintenance Competition Assurance Act of 1998*

Section 117 was further amended by title III of the DMCA, the Computer Maintenance Competition Assurance Act of 1998. The amendment was intended to "provide a minor, yet important, clarification in section 117 of the Copyright Act to ensure that the lawful owner or lessee of a computer machine may authorize an independent service provider, a person unaffiliated with either the owner or lessee of the machine, to activate the machine for the sole purpose of servicing its hardware components."[72] Title III was prompted by the outcome in *MAI Systems Corp. v. Peak Computer, Inc.*[73] and other cases that had held an independent service organization liable for copyright infringement by virtue of loading operating system software into a computer's RAM when a technician switched the computer on in order to repair or maintain it. Rather than addressing the general question of temporary copies as proposed in some contemporaneous bills,[74] title III of the DMCA narrowly overturned the outcome of *MAI v. Peak*

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[70] "Archival purposes." in this context, was intended to mean the backing up of copies by users, not for the purposes of, for example, expanding a library's archival collection.

[71] 17 U.S.C. § 117(a)(1).

[72] 144 Cong. Rec. S11890 (daily ed. Oct. 8, 1998) (statement by Sen. Leahy).

[73] 991 F.2d 511, *cert. dismissed*, 114 S. Ct. 671 (1994).

[74] See discussion of the Boucher-Campbell bill, *supra* at 15.

with respect to independent service organizations, leaving the underlying holding with respect to temporary copies intact.

2. Judicial Interpretation of Section 117

Courts have interpreted the section 117 exceptions narrowly. For example, in *Sega Enterprises Ltd. v. Accolade, Inc.*,[75] the Ninth Circuit held that copying a computer program into memory in order to disassemble it was a use that "went far beyond that contemplated by CONTU and authorized by section 117."[76] Regarding the archival exemption, one court has held that section 117 does not excuse the making of purported backup copies of a videogame embodied in ROM, because that particular storage medium is not vulnerable to "damage by mechanical or electrical failure."[77]

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[75] 977 F.2d 1510 (9th Cir. 1992).

[76] *Id.* at 1520.

[77] *Atari, Inc. v. J S & A Group, Inc.*, 597 F. Supp. 5, 9-10 (N.D. Ill. 1983).

II. VIEWS OF THE PUBLIC

A. SOLICITATION OF PUBLIC COMMENTS

In order to focus the issues involved in this Report, and to provide information and assistance to the Copyright Office and NTIA, the two agencies sought both written comments and oral testimony from the public. This process of public consultation commenced with the publication of a Notice of Inquiry in the Federal Register on June 5, 2000.[78]

The Notice of Inquiry sought comments and reply comments in connection with the effects of the amendments made by title I of the DMCA and the development of electronic commerce on the operation of sections 109 and 117 of title 17, United States Code, and the relationship between existing and emerging technology and the operation of such sections.[79]

In response to the Notice of Inquiry, we received thirty initial comments and sixteen reply comments.[80] Of those thirty initial comments, twenty-one dealt with section 109 and twelve dealt with section 117. Of the sixteen replies (to the initial comments), thirteen dealt with section 109 and eight dealt with section 117.

[78] 65 Fed Reg 35.673 (June 5, 2000).

[79] *Id.* For a more complete statement of the background and purpose of the inquiry, see the Notice of Inquiry which is available on the Copyright Office's website at: www.loc.gov/copyright/fedreg/65fr35673.html.

[80] The comments and replies have been posted on the Office's website; see www.loc.gov/copyright/reports/studies/dmca/comments/ and www.loc.gov/copyright/reports/studies/dmca/reply/, respectively.

On October 24,2000, the two agencies published a notice of public hearing in the Federal Register.[11] At this public hearing, held at the Copyright Office on November 29,2000, the two agencies inquired into points made in the written comments and focused on a series of specific questions. The information received fiom the written comments, as well as fiom the testimony of witnesses at the November 2000 public hearing, is summarized here.[12]

B. VIEWS CONCERNING SECTION 109[13]

1. The Effect of Section 1201 Prohibitions on the Operation of the First Sale Doctrine

There was a dramatic range of opinions in the many comments addressing this question. Most commenters believed that the anticircumvention provisions of 17 U.S.C. § 1201 provided copyright owners with the ability to restrict the operation of the first sale doctrine. A few of these commenters did not elaborate on this assertion. Those who did expressed many different views on precisely how the rule against the circumvention of technological protection measures restricts the operation of the first sale doctrine, and how severe that effect is.

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[11] 65 Fed Reg 63,626 (October 24, 2000).

[12] Summaries of testimony are available on the Copyright Office website at www.loc.gov/copyright/reports/studies/dmca/testimony/hearings.html; a full transcript of the public hearing is available at www.loc.gov/copyright/reports/studies/dmca/testimony/transcript.pdf.

[13] In referring to the comments and hearing materials, we will use the following abbreviations: C-Comment, R-Reply Comment, WST-Written Summary of Testimony, T + speaker-Hearing Transcript. Citations to page numbers in the hearing transcript are to the PDF version of the transcript on the Copyright Office website: www.loc.gov/copyright/reports/studies/dmca/testimony/transcript.pdf.

Among those who believed that section 1201 limits first sale, the majority of comments focused on one of two practical concerns surrounding the market for DVDs. The first addressed the proprietary encryption scheme known as the Content Scrambling System"[84] (CSS) that is used on commercial DVDs, and the requirement that manufacturers be licensed to produce DVD players. The second addressed the practice known as region coding.[85]

Most commercially released motion pictures on DVD, as noted by many commenters, are encrypted using CSS. Some commenters noted further that the only devices that are authorized to decrypt DVDs are DVD players that have been manufactured under a license from the consortium (which includes the major motion picture studios) that owns the rights to CSS.[86] As a result, the commenters complained, they are required to make two purchases in order to view a single DVD (i.e., the DVD and the player).[87] Certain commenters suggested that the practice of requiring a licensed player in order to view a DVD amounts to a violation of antitrust law.[88]

But for the anticircumvention law, it would be permissible for a person to use an unauthorized decryption program to view DVDs on devices other than authorized players, such

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[84] CSS is the technological protection measure adopted by the motion picture industry and consumer electronics manufacturers to provide security to copyrighted content of DVDs and to prevent unauthorized copying of that content. Motion Picture Association of America website: www.mpaa.org/Press, visited on May 1,2001.

[85] See discussion *infra*, at 36.

[86] C-Arromdee, at 1.

[87] C-Taylor, at 1.

[88] C-National Association of Recording Merchandisers, Inc. (NARM) and the Video Software Dealers Association, Inc. (VSDA), at 29-30.

as personal computers, if necessary. Such a program was found in violation of section 1201 in a highly publicized court case.[89] Some commenters discussed the case in great detail in their comments.[90]

The implication of the complaint about the CSS encryption code is that by enabling copyright owners to compel users to purchase a licensed DVD player, the value of a DVD is reduced. It is, argued some commenters, a requirement that each subsequent owner of a DVD obtain a new authorization to view the contents of that work?' That, in turn, means that the value of the first sale doctrine as applied to DVDs is reduced or eliminated. Thus, as applied to the market for DVDs, these commenters argued that the operation of the first sale doctrine has been obstructed by the rules against circumvention of technological protection measures.[92]

The concerns about region coding of DVDs are similar in nature. Region coding is a technological means of preventing DVDs manufactured for sale in one region of the world from playing on a DVD player that is manufactured for sale in a different region of the world. The result is that a DVD purchased in Asia cannot be viewed on a licensed DVD player purchased in the United States?' Were unauthorized circumvention permissible, region coding could be

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[89] *See Universal City Studios. et al. v. Reimerdes,* 82 F. Supp. 2d 211 (S.D.N.Y 2000). The case is presently on appeal to the Second Circuit. *Universal City Studios. et al. v. Corley*, docket #00-9 185.

[90] C-Thau and Taylor, at 4 *et seq.*

[91] *E.g.*, C-Taylor. at I.

[92] *E.g.*, C-Arromdee, at 1.

[93] Some DVD players can be switched fiom one region setting to another, but the user may only switch a few times before being permanently locked into a region.

defeated. These cornenters argued that region coding reduces the value of the first sale doctrine by limiting the market for resale of a DVD. And because the anticircumvention rules prevent users from defeating region coding, these commenters argued that those rules are interfering with the operation of the first sale doctrine.[94]

Others who believe that prohibitions on circumvention of technological protection measures have restricted the operation of the first sale doctrine were more general in their comments. One representative sample is a comment which noted that access controls that permit access on only a single device are likely to interfere with the exercise of the first sale doctrine?' This comment also addressed other situations, noting that access controls sometimes limit the amount of a work that is viewable at any time. While acknowledging that this serves a reasonable anti-piracy purpose, the comment also noted that such a practice makes it less likely that the user will exercise the first sale privilege. This is because in order to obtain a complete tangible copy of the work the user will have to separately print out numerous small portions.% This comment also observed that while files that require a password to gain access may not be limited to one device, transfer of the password, or "key," may be restricted in a way that prevents transfer of a file in a usable form?'

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[94] *E.g.*, C-LXNY, at 1.

[95] C-Computer Professionals for Social Responsibility (CPSR). at 2.

[96] Id.at3.5.

[97] Id. at 4.

That final point was echoed by a number of commenters. Their concern was that the non-negotiable licenses which are offered to users of copyrighted works are written to reduce or eliminate the availability of statutorily permitted uses, including uses permitted under section 109.[98] These terms may be enforced through technological protection measures. Thus, they argued, the rules against circumvention of such measures hamper the operation of the first sale doctrine.[99] This concern was particularly evident among users of computer software, who decried so-called shrinkwrap and click-wrap licenses.[100] A few commenters delved into a discussion of the relative merits of the Uniform Computer Information Transactions Act[101] (UCITA) – legislation that is currently being considered in numerous state legislatures, that would validate the enforceability of shrinkwrap and click-wrap licenses.[102]

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[98] *E.g.*, C-American Library Association, American Association of Law Libraries, Association of Research Libraries, Medical Library Association, and Special Libraries Association (Library Ass'ns), at 5-7.

[99] *Id.*

[100] Shrinkwrap and click-wrap licenses are terms used to describe the non-negotiable licensing terms that are sometimes placed on consumer packaging of copyrighted works, particularly software, in lieu of a simple sale of that copy of the work. The names derive fiom the practice of demonstrating users' assent to the tenns by virtue of their tearing open the plastic shrinkwrap packaging or clicking an "agree" button with a mouse.

[101] The Uniform Computer Information Transactions Act (UCITA), according to the National Conference of Commissioners on Uniform State Laws, represents the first comprehensive uniform computer information licensing law. This act uses the accepted and familiar principles of contract law, setting the rules for creating electronic contracts and the use of electronic signatures for contract adoption – thereby making computer information transactions as well-grounded in the law as traditional transactions. National Conference of Commissioners on Uniform State Laws website: www.nccusl.org/uniformact_factsheets/uniformacts-fs-ucita.htm, visited on May 2, 2001.

[102] *E.g.*, C-Lyons, at 3-5; R-Software and Information Industry Association (SIIA), at 10-11.

Similar concerns were also raised in the submission of the library associations.[103] They expressed concern that rules against circumvention give copyright owners the ability to maintain a running control on access to and copying of their works.[104] This, they argued, frustrates the goal of the first sale doctrine, by extending the rights of the copyright owner beyond the first sale of a particular copy.[105] As tangible examples of how this interference in the operation of the first sale doctrine might inhibit the functioning of a library, they gave several examples including interlibrary loan programs, preservation, and accepting donations of works.[106] All of these, they argued, have become difficult or impossible as a result of the intersection of licensing terms, technological measures and restrictions on circumvention.[107]

Other commenters had varying explanations for their belief that anticircumvention rules have hampered the first sale doctrine. For example, one commenter argued that anticircumvention rules limit the user's ability to make copies, which effectively precludes users from benefitting from the first sale doctrine.[108]

A few commenters stated that the rules against circumvention have little or no effect on the first sale doctrine. One commenter, for example, opined that such rules are irrelevant

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[103] C-Library Ass'ns. at 4-7.

[104] *Id.*

[105] *Id.*

[106] *Id.* at 10-19.

[107] *Id.*

[108] C-Van De Walker, at 2.

because they are essentially unenforceable.[109] Others argued that it is simply too soon in the evolution of this field to know.[110] They noted, however, that with time that condition may change.

A significant number of commenters expressed the view that prohibitions on circumvention of technological protection measures, particularly in the online environment, have had no effect on the operation of the first sale doctrine because the first sale doctrine is inapplicable to digital transmissions.[111] Several of these comments sought to respond to the concerns previously mentioned. For example, one commenter argued that concerns about copyright owners locking up works behind technological protection measures are without merit, because doing so would be a doomed business strategy.[112] That commenter also argued that the licensing of DVD players in no way disadvantaged consumers.[113] Further, that commenter asserted that analysis of the effect of licensing terms is beyond the scope of this Report.[114]

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[109] C-Stanford Linear Accelerator Center (SLAC), at 1.

[110] C-Digital Media Association (DiMA), at 7-9; C-Anthony, at 1.

[111] *E.g.*, R-Reed Elsevier Inc., at 5-8.

[112] R-Time Warner Inc. at 1-2.

[113] *Id.* at 2.

[114] *Id.* at 4.

2. The Effect of Section 1202 Prohibitions on the Operation of the First Sale Doctrine

The overwhelming number of commenters that expressed a view on this issue stated that there has not been any effect on the operation of the first sale doctrine as a result of the protections for copyright management information.[115] However, the library associations argued that when combined with technological protection measures and licensing limitations, copyright management information can give the copyright owner the ability to monitor and prohibit uses that are permissible under the law.[116] They were also concerned that such technology can give the copyright owner access to personal information about users, such as 'cookies',[117] that chills use of the work.[118] One commenter argued that protections for copyright management information limit the utility of the first sale doctrine because they prevent the owner of the copy from removing what he referred to as the "packaging" of the work.[119]

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[115] See, *e.g.*, C-SLAC, at 1; C-McGown, at 1; C-DiMA, at 9.

[116] C-Library Ass'ns, at 7-10.

[117] A 'Cookie" is information that is stored by Internet browsing software on a user's hard drive in response to an automated request by a web server. A subsequent automated request by a web server can instruct the browsing software to transmit that information back to the server.

[118] C-Library Ass'ns. at 7-10.

[119] C-Thomason, at 1.

3. The Effect of the Development of Electronic Commerce and Associated Technology on the Operation of the First Sale Doctrine.

One commenter simply found that the development of electronic commerce and associated technology has had no effect on the first sale doctrine.[120] Another believed that it was too soon to tell what the effect will be.[121]

The library associations argued that with the increase in distribution of copyrighted works online, it is less likely that a user will purchase a copy. Rather, they foresee that the user will be licensed to access a work online.[122] One result of this change, they argued, is that the first sale doctrine will not apply to online access.[123] They also argued that it permits copyright owners to create a price structure wherein entities that cannot afford the best version of the work must settle for a less expensive and less desirable version.[124]

Other commenters took that sentiment further, arguing that particularly in the e-commerce sphere, technology can now be used by copyright owners to circumvent constitutional and legislative limitations on the distribution right to the point of copyright misuse and/or antitrust violations.[125]

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[120] C-McGown, at 1.

[121] C-DiMA, at 9-11.

[122] C-Library Ass'ns, at 10-19.

[123] *Id.*

[124] *Id.*

[125] See C-NARM/NSDA, at 29-30, 37.

One copyright owner commented that new technology has made infringement of copyright easier and that a change in the existing level of protection for copyrighted works (such as expanded first sale privilege) could be disastrous for copyright owners.[126]

4. The Relationship Between Existing and Emergent Technology, on One Hand, and the First Sale Doctrine, on the Other

Relatively few commenters addressed this issue directly. Of those who did, most commenters believed that there is no relationship between existing and emergent technology and the first sale doctrine.[127] Some argued that technology is being used to defeat the first sale doctrine, as discussed above.[128] Another commenter noted that the first sale doctrine applies to tangible copies, not to the streaming or downloading of works.[129]

5. The Extent to Which the First Sale Doctrine Is Related To, or Premised On, Particular Media or Methods of Distribution

Many comments indicated that the first sale doctrine is not premised on any particular media or methods of distribution.[130] Some noted that the first sale doctrine is premised on older

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126 R-Time Warner Inc., at 1.

127 *E.g.*, C-McGown, at 1; C-Library Ass'ns, at 19.

128 C-Library Ass'ns, at 10-19.

129 C-Time Warner Inc., at 2-3.

130 *E.g.*, C-McGown, at 1; C-Taylor, at 5.

technology which provided greater impediments to the transfer of works than modem technology.[131] Others observed that the first sale doctrine is based on tangible copies.[132]

6. The Extent, if Any, to Which the Emergence of New Technologies Alters the Technological Premises upon Which the First Sale Doctrine Is Established

As with the previous issues, many of the commenters indicated that new technology does not alter the technological premises upon which the first sale doctrine is established. One commenter stated that new technology has made copyright laws obsolete and ineffective because of the impossibility of enforcement.[133] Several cornenters noted that while new technology has not altered the premises of the first sale doctrine, the legislative codification of that doctrine may need to be periodically updated to continue the proper application of the first sale doctrine to new technology.

7. The Need, if Any, to Expand the First Sale Doctrine to Apply to Digital Transmissions

The comments on this issue were both voluminous and passionate. They can be divided into two starkly contrasting groups: those arguing that section 109 should be amended to permit the digital transmission of works that were lawfully acquired (including the reproduction of the work as a part of the transmission process) and those opposing modification of section 109.

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[131] C-SIIA, at 6; C-SLAC at 2.

[132] C-Time Warner Inc., at 3; C-Anthony, at 2-3.

[133] C-SLAC, at 2-3.

Some of the commenters argued that digital transmissions are already permitted by the existing language of section 109.[134] This is because in obtaining the "source" copy, a user receives a transmission and upon completion of that transmission, there exists a copy of the work in tangible form. They dismissed concerns about additional copies being made when the first purchaser transmits the work to a second as being incidental to the transmission process. A legislative change that they seek is to amend section 1201 to allow circumvention of technological protection measures which prevent the operation of the first sale doctrine.[135]

Other commenters argued that the current language of section 109 could be read to apply to digital transmissions (although some conceded that a "formalistic" reading of section 109 does not), but sought legislative clarification to codify this conclusion.[136] Many commenters referred to the Boucher-Campbell bill[137] as a model for the changes they would like to see made to section 109.[138]

The commenters supporting changes to section 109 argued that copyright law has always been interpreted to be technology neutral, and that in order to be faithful to that tradition, the first sale doctrine should be updated to apply to digital transmissions.[139] They noted that the policy

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[134] C-NARM/NSDA, at 36-37.

[135] *Id.*

[136] R-Library Ass'ns, at 1-2.

[137] H.R. 3048, 105th Cong., 1st Sess. (1997).

[138] *E.g.*, C-Digital Future Coalition (DFC), at 3.

[139] *Id.*

behind the first sale doctrine was to prevent restraints on the alienability of property in order to promote the continual flow of property in society.[140] They argued further that the first sale doctrine has, for nearly a century, promoted economic growth and creativity, and should be extended into the digital environment.[141] In anticipation of counter-arguments that such an extension would be an invitation to infringement, they argued that technological protection measures and copyright management information can be used in concert to guarantee that when a user transmits the work, the "source" copy is deleted.[142] They also asserted that this technology exists now. Additionally, some argued that without a clear application of the first sale doctrine to digital transmissions, circumvention technology will gain in popularity.[143]

The library associations sought specific amendments to section 109 to address the concerns unique to libraries relating to interlibrary loans, preservation/archiving, accepting donated works, and other activities.[144]

There were a few other views supporting such a change as well. One commenter argued that while the copyright law is no longer relevant and the expansion of section 109 is not technologically necessary, the principles of copyright law should apply evenly.[145] Another

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[140] C-NARM /VSDA, at 9.

[141] C-Home Recording Rights Coalition (HRRC), at 2-3.

[142] *Id.* at 5.

[143] R-DiMA, at 6-7.

[144] C-Library Ass'ns, at 11-19.

[145] C-SLAC, at 3.

commented that first sale principles should also apply to the transmission of encryption "keys" so as to prevent technological protection measures from inhibiting exercise of the first sale right while still providing protection against infringement.[146]

Those who opposed the amendment of section 109 argued that the requested changes do not merely update the long-standing first sale doctrine to accommodate new technology, but expand the first sale doctrine well beyond its previous scope.[147] To date, the first sale doctrine has, with limited exceptions,[148] always been a limitation on only the distribution right. Commenters from the copyright industries noted that in order to transfer a copy of a work from one person to another by digital transmission it is necessary for copies to be made, thus implicating the reproduction right.[149] They asserted too that the transfer may also involve a performance of the work, implicating the public performance right or for sound recordings, the digital audio transmission right.[150]

Those opposed to amending section 109 also argued that a change along the lines proposed in the Boucher-Campbell bill would open the door to widespread unauthorized copying

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[146] C-Thau and Taylor, at 6.

[147] C-SIIA, at 3.

[148] See § 109(c) (limiting the public display right) and § 109(e) (limiting the public performance and public display rights). These provisions are discussed *supra*, at 25.

[149] R-American Film Marketing Association, Association of American Publishers, Business Software Alliance, Motion Picture Association of America, National Music Publishers' Association, and Recording Industry Association of America (Copyright Industry Orgs.), at 2.

[150] *Id.* at 5.

of works which, in turn, would destroy the market for those works."[151] They argued that this result could occur because the technology to require simultaneous destruction of the "source'*copy remains ineffective and prohibitively expensive.[152] Moreover, at least one copyright owner representative questioned the existence of any demand in the marketplace for the simultaneous destruction (also called "forward and delete',) technology.[153] Opponents also argued that in the context of traditional technology, the effect of the first sale doctrine on the marketplace for unused copies was limited by geography and the gradual degradation of books and analog tapes.[154] The absence of such limitations in the context of digital technology would cause an expanded first sale doctrine to have a far greater effect on the market."[155] They also noted that copyright owners' concerns raised in the context of this Report were precisely the same concerns that persuaded the Congress not to enact the Boucher-Campbell bill in the 105th Congress, and that nothing has changed that should alter Congress' judgment.[156]

8. The Effect of the Absence of a Digital First Sale Doctrine on the Marketplace for Works in Digital Form

For those who seek an amendment to section 109 to include digital transmissions explicitly in the first sale doctrine, the absence of express statutory language is a source of

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[151] *E.g.*, R-Time Warner Inc., at 1.

[152] R-Copyright Industry Orgs., at 3 4.

[153] T-National Music Publishers' Association (NMPA), Mann, at 157-58.

[154] R-SIIA, at 6.

[155] *Id.*

[156] R-NMPA, at 2-3.

uncertainty, reduced utility and/or a chilling effect on users in the marketplace, which is reducing the demand for copyrighted works.[157]

To those who oppose such an amendment, the current law provides an environment in which copyright owners are willing to offer their works in a digital form.[158] This, they argued, enhances the market for such works by providing them to consumers in the media they desire most. To counter claims that the absence of a clear application of the first sale doctrine to digital transmissions is harming the marketplace, one commenter quoted a 1997 U.S. Department of Commerce study asserting that "electronic shopping and mail order houses sold $22.9 billion in computer hardware, software, and supplies . . . more than any other types of retail businesses."[159] Another noted that according to Jupiter Communications, digital downloads will be a $1.5 billion commercial market by 2006.[160]

C. VIEWS CONCERNING SECTION 117

The public comments related to section 117 fell broadly into two categories: comments concerning the status of temporary copies in RAM and comments concerning the scope of the archival exemption.

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[157] C-Library Ass'ns, at 25-26; C-DiMA, at 13.

[158] *E.g.*, C-Time Warner Inc., at 3.

[159] R-SIIA, at 5.

[160] R-Broadcast Music, Inc. (BMI), at 6-7.

1. Exemption for Temporary Buffer Copies in Random Access Memory (RAM)

a. Legal Status of Temporary Copies and Need for an Exception.

Most of the comments received on "section 117" related not to the computer program exemptions provided in that section, but to the question whether an exemption for temporary incidental copies should be enacted. One group of commenters requested an exemption from the exclusive right of reproduction for certain kinds of temporary copies.[161] Another group of commenters, mostly comprised of copyright owners, did not believe there is any need or basis for an exemption for these temporary copies.[162]

Many of the commenters who support an amendment to create a general exception from the reproduction right for temporary incidental copies supported the exemption proposed in the Boucher-Campbell bill.[163] This bill included an exemption for digital copies that are incidental to the operation of a device in the course of use of a work when that use is lawful under title 17, U.S. Code. Because this exemption was originally proposed as an amendment to section 117, we discuss it in the context of section 117.[164]

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[161] *See generally* comments by Computer & Communications Industry Association (CCIA), DFC, HRRC, DiMA (suggesting similar but different wording), Blue Spike, Launch; *see also* R-Library Ass'ns, at 15-16.

[162] *See generally* comments by NARM and VSDA, Digital Commerce Coalition (DCC), Business Software Alliance (BSA). BMI. Copyright Industry Orgs.. Reed Elsevier. Inc. (REI).

[163] H.R.3048, 105th Cong., (1997); see discussion *supra* at 15.

[164] See discussion of the nexus between the temporary incidental copy issue and section 117 *supra* at 18.

The proponents of a temporary incidental copy exception argued that court decisions like *MAI Systems Corp. v. Peak Computer, Inc.*[165] and its progeny, have had the effect of invalidating the usefulness of the exemptions under section 117.[166] *MAI v. Peak* held that the loading of software into a computer's random access memory (RAM) in violation of a license agreement was an infringement because it entailed making a copy.[167] The exemption in section 117 applies to "the owner of a copy of a computer program."[168] The court in *MAI v. Peak* concluded that since the software was licensed by the copyright owner, the defendant, a third-party independent service oganization, was not an "owner" of the software and did not qualify for the exemptions under section 117.[169] The commenters argued that because most software today is acquired by license rather than purchase, few users of computer software would qualify for the exemption under section 117. Therefore, they contended, it is of little use.[170]

Other commenters generally opposed any exemption for temporary incidental copies at this time."' Many of them opposed the Boucher-Campbell bill, arguing that the proposed

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[165] 991 F.2d 511 (9" Cir. 1993), *cert. dismissed,* 114 S. Ct. 671 (1994).

[166] The DFC argues, for instance, that the practical force of the section 117 exemptions has been deprived by recent case law. citing *MAI v. Peak* and subsequent decisions that hold that every temporary RAM copying of a computer program, incidental to its use on a hardware platform, constitutes a fonn of "reproduction". C-DFC, at 3. CCIA said that the existing 117 has "in essence . . . been repealed" by *MAI v. Peak* and decisions like it. C-CCIA, at 2.

[167] *See* discussion of *MAI v. Peak infra* at 118.

[168] 17 U.S.C. § 117(a)(1).

[169] 991 F.2d 511,518 n. 5 (9th Cir. 1993).

[170] This argument appears to be less relevant to the proposal for a general exemption for temporary incidental copies, than to the question whether the existing exemptions under section 117 should apply only to "owners" of copies or to "rightful possessors" including licensees.

[171] *See generally* comments by the Copyright Industry Orgs., NMPA, and SIIA; T-BMI, Berenson, at 167.

exemption is not justified by technological developments, would dramatically expand the scope of section 117, and would drastically cut back on the exclusive reproduction right for all works.[172] In their view, the *MAI v.* Peak decision stands for two propositions relevant to section 117, both of which buttress, rather than weaken or "repeal" that statutory provision and the objectives for which it was enacted.[173] First, the Ninth Circuit's holding in MAI *v. Peak* has been followed in a number of other federal court decisions."[174] The copyright owners also argued that if the Ninth Circuit had reached the opposite conclusion – that such copying of a computer program into memory was not a reproduction falling within the scope of the reproduction right – enactment of what is now section 117(a)(1) would not have been necessary.[175] Second, the copyright owners argued that proponents of the Boucher-Campbell bill called on Congress in 1998 to overturn *MAI v. Peak* by adopting an exception for incidental copies, but that Congress did the opposite by passing title III of the DMCA, endorsing and reaffirming the conclusions of CONTU and the Ninth Circuit regarding temporary copies.[176] The copyright owners, joined by other commenters, argued that the DMCA embraced the general principle that temporary copies in RAM are copies that are subject to the copyright owner's exclusive reproduction right, and made only those carefully calibrated adjustments to the principle necessary to address the problems experienced by independent providers of computer maintenance and repair services.[177]

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[172] R-Copyright Industry Orgs., at 9.

[173] *Id.*

[174] See *infra* at 119.

[175] R-Copyright Industry Orgs., at 9; see *infra* at 113.

[176] *Id.*

[177] R-Copyright Industry Orgs.. at 10.

The copyright owners were also concerned that an exception for incidental copies would undercut the reproduction right in all works, and would raise significant questions about U.S. compliance with its international obligations.[178]

b. *The Economic Value of Temporary Copies*

Commenters were divided on the question whether temporary copies have economic value. The point of view of the commenters appeared to be strongly influenced by the context in which the particular temporary copy is made. Some commenters who discussed temporary copies that are incidental to an authorized transmission placed little or no economic value on the copies. The small temporary buffer memory copies that are used in today's webcasting technology, argued one commenter, have no intrinsic or economic value apart from the performance.[179] This commenter, representing an alliance of companies that develop and deploy technologies to perform, promote and market music and video content on the web and through other digital networks, noted that this webcasting technology demonstrates why section 117 needs to be updated for the digital age. He said that it should provide that the temporary buffers necessary to enable an authorized performance of copyrighted material are exempt from any claim of copyright infringement.[180]

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[178] WST-Copyright Industry Orgs.

[179] C-DiMA, at 19.

[180] *Id.*

Other commenters argued that the temporary copy has significant economic value.[181] These commenters referred to the holding in *MAI v.* Peak, and its subsequent confirmation by Congress in title III of the DMCA, as an implicit recognition that the copies have economic value since Congress deemed them worthy of protection.[182] Indeed, one commenter from a trade association that represents software and electronic commerce developers asserted that in the digital world it is possible that the full commercial value of the work is contained in that temporary copy. For example, customers are becoming less interested in possessing a permanent copy of software, and more interested in having that copy available to them as they need it.[183]

c. Promotion of Electronic Commerce

Some commenters asserted that the promotion and growth of electronic commerce requires a general exception for temporary incidental copies to cover all forms of digital content, not just computer software.[184]

Opposing that view was one commenter who noted that there is every indication from the marketplace to suggest that electronic commerce and the Internet continue to grow vigorously, and that in the two years since the enactment of the DMCA that growth has accelerated.[185] The commenter concluded that the evidence is simply not there to support the thesis that exemptions

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[181] See *generally* comments by Copyright Industry Orgs., BSA.

[182] R-Copyright Industry Orgs., at 9; T-BSA, Simon, at 105.

[183] T-BSA, Simon, at 138.

[184] C-DiMA, at 15; WST-HRRC; R-Library Ass'ns. at 14.

[185] T-BSA, Simon, at 105.

must be expanded to meet the demands of electronic commerce.[186] Copyright industries did not believe any changes to section 117 were necessary at this time in order to facilitate the continued growth of electronic commerce and the advance of technology for conducting electronic transactions in copyrighted materials. They professed to be unaware of any significant impediments to electronic commerce which have arisen as a result of section 117 in its current form.

d. *Changed Circumstances since Enactment of the DMCA*

A representative of the copyright industry associations observed that when Congress has dealt with the question of temporary copies, it has done so in response to real problems.[187] He noted that Congress responded in 1998 to real problems that were presented to it by independent service organizations that had been sued and were being held liable for creating temporary copies in RAM in the course of maintaining or repairing computers.[188] Congress, he also noted, took the same approach when it was presented with evidence that there was at least a credible threat of liability for online service providers, for making temporary copies in the course of carrying out functions that are at the core of the Internet.[189]

Several commenters spoke directly to this issue by addressing what has changed in the past two years that would require an exemption from the reproduction right for certain temporary

[186] *Id.*

[187] T-Copyright Industry Orgs., Metalitz, at 249.

[188] *Id:* see *supra*, at 30.

[189] T-Copyright Industry Orgs., Metalitz at 249; see *infra*, note 201.

copies and what additional experience has been gained over the past two years that may persuade Congress to rethink these issues. One commenter remarked that the test that should be considered is whether something has happened to the marketplace that would justify further changes in law.[190] He noted that Congress found no compelling evidence in 1998 that changes were merited, and having reviewed the submissions and marketplace developments, he found that there is no justification to come to a different conclusion today.[191]

Still another commenter argued that an amendment to section 117 to exempt temporary copies of works that are made as part of the operation of the machine or device is not necessary and would be inappropriate because no one can provide any evidence of harm.[192] This commenter asserted that no concrete examples had been proffered of situations where copyright owners have filed suit or otherwise made inappropriate claims based on such temporary copies or where webcasters have been hampered by any alleged threats. He was not aware of any record company that has claimed infringement or threatened litigation based on the making of temporary copies. To the contrary, he provided examples of webcasters and other internet music services being licensed by copyright owners with all the permissions they need to operate their business. Need for legislative action on this point, he said, has not been demonstrated and none should be taken where the likelihood of unintended consequences is high.[193]

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190 T-BSA, Simon, at 105.

191 *Id.*

192 T-RIAA, Sherman, at 305.

193 *Id.*

Other commenters, however, argued the problem was not theoretical. One webcaster noted that there are music publishers that are seeking mechanical royalties for temporary copies made in RAM buffers when music is streamed on the Internet, even though the performance to which the copy is incidental is fully licensed."[194] He noted that his company had not been sued but certainly had been threatened, and the threat of suit had been used against it in negotiations over license agreements."[195] The commenter said the threat of litigation, particularly to a growing company like his, is enough to cause problems, and is enough to make such a company agree to licenses that are, perhaps, unfair."[196] He also noted that it is not in anyone's interest to resolve a perceived ambiguity through litigation; this is a clear example of an instance in which legislative action could effectively resolve any uncertainty.[197]

e. Applicability of the Fair Use Doctrine to Temporary Copies

Suggestions were made in the comments that the fair use doctrine, rather than a separate exemption for temporary incidental copies, could address some of the concerns that were raised about such copies. Since certain commenters proposed that language be added to section 117 that would permit the making of temporary copies when such copies are "incidental to the operation of a device . . ." and do "not conflict with the normal exploitation of the work and do not unreasonably prejudice the legitimate interests of the author," one commenter suggested instead that the fair use doctrine be used rather than expanding section 117 with such broad

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[194] T-Launch, Goldberg, at 311.

[195] Launch has since been sued, but over issues unrelated to buffer copies.

[196] T-Launch. Goldberg, at 311.

[197] WST-Launch.

language. This commenter argued that this language is too broad and use of it may be dangerous by allowing acts well above and beyond any reasonable fair use.[198]

One of the commenters advocating an exemption for temporary incidental copies also recognized that fair use may address some of the concerns that were expressed. This commenter took the position that between the archival exemption set out in section 117 and the fair use doctrine, certain types of copies should already be determined not to be infringing under the law, including temporary copies of recorded content made in the course of playback through buffering, caching, or other means.[199] Library associations said that while they believe that the copying rights at issue already exist under fair use, making them explicit could help to eliminate some of the uncertainty that is currently preventing these rights from being fully and consistently exercised.[200]

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[198] R-SIIA, at 3.4; WST-SIIA; T-SIIA, Kupferschmid, at 132.

[199] WST-HRRC. The copies that HRRC asserts should already be determined not to be infringing under the law (because the copies fall under the archival exemption set out in section 117 or the fair use doctrine) are back-up or archival copies of works or phonorecords of content lawfully acquired through digital downloading; temporary copies of recorded content made in the course of playback through buffering. caching, or other means; and temporary copies that are stored through the technical process of Internet webcasting.

[200] R-Library Ass'ns, at 14.

f. *Liability for Making Temporary Copies under Section 512*[201]

The copyright industries questioned why the limitations on liability set out in section 512 cannot be used by the webcasters to address their problems regarding threats of litigation and noted that there have not been significant legal conflicts over incidental copying.[202] The copyright industries asserted that Congress, in enacting the DMCA, addressed and resolved some of the potential flash points. For instance, they asserted that, in what is now section 512, Congress carefully fashioned limitations on remedies that apply to infringements – including, notably "incidental copying" – that may occur in the course of activities that are essential to the smooth functioning of the Internet such as linking, storing, caching or providing conduit services, rather than creating broad exemptions to exclusive rights.[203]

Other commenters disagreed. One noted that the section 512 provisions are helpful to those who qualify as Internet service providers within the meaning of section 512 but that many webcasters are not Internet service providers and do not qualify for relief from liability under

[201] 17 U.S.C. § 512. Under section 512, a party that qualifies as a "service provider" may be eligible for one or more of four limitations on monetary liability for copyright infringement deriving from specified activities. For purposes of the first limitation, relating to transitory communications, "service provider" is defined in section 512(k)(1)(A) as "an entity offering the transmission, routing, or providing of connections for digital online communications, between or among points specified by a user, of material of the user's choosing, without modification to the content of the material as sent or received." For purposes of the other three limitations relating to system caching, hosting, and information location tools, "service provider" is more broadly defined in section 512(k)(1)(B) as "a provider of online services or network access, or the operator of facilities therefor."

In addition, to be eligible for any of the limitations, a service provider must meet two overall conditions: (1) it must adopt and reasonably implement a policy of terminating in appropriate circumstances the accounts of subscribers who are repeat infringers; and (2) it must accommodate and not interfere with "standard technical measures" as defined in section 512(i).

[202] T-Copyright Industry Orgs., Metalitz, at 247.

[203] R-Copyright Industry Orgs., at 10-11.

section 512.[204] Another commenter agreed that section 512 can be extremely helpful for intermediaries, but asserted that it does not solve the particular problem for Internet webcasters and Internet broadcasters who are the originators of the transmissions.[205]

2. Scope of the Archival Exemption

a. *Expansion of the Archival Exemption to Works Other than Computer Programs*

Although most comments received on section 117 related to an exemption for temporary copies, a number of commenters discussed the scope of section 117's archival exemption. One commented that it supports amending section 117 to allow owners of any digitally-acquired content (i.e., not just computer programs) the right to make an archival or backup copy;[206] that consumers may wish to make removable archive copies of downloaded music and video to protect their downloads against losses; and that despite the convenience of digital downloading, media collections on hard drives are vulnerable.[207] This commenter noted, for example, that when a consumer wants to upgrade to a new computer or a more capacious hard disk drive, there is no lawful means to transfer the consumer's media collection onto new equipment.

This point was echoed by other commenters who said that section 117 is too narrow and, in addition to computer programs, should apply to other works due to the fact that CDs can erode

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[204] T-DFC. Jaszi, at 273-74.

[205] T-DiMA, Greenstein, at 274.

[206] The copyright industry organizations pointed out in reply comments that DiMA believes this narrow exception to section 117(a)(2) should be expanded to cover any "content that [consumers] lawfully acquire through digital downloading." R-Copyright Industry Orgs., at 12.

[207] T-DiMA, Greenstein, at 238-39.

and DVDs can also develop similar problems.[208] Another commenter representing the library associations said that more categories of works are now being published in digital formats and that section 117 should be updated to clarify that the rights apply to all rightfully possessed digital media.[209] The library associations went on to say that all digital content is prone to deletion, corruption, and loss due to system crashes and that consumers must be permitted to protect their investments; thus it is critical to recognize that archival copying rights are as important today to the growth of digital publishing as they were to the growth of the computer software industry in the 1980s.[210]

On the other side was a trade association for the software and information industries. This association suggested that an expansion of section 117 to other copyrighted works is senseless because it is being used so sparingly today for computer software and the justification for the provision no longer exists.[211]

This same trade association expressed the view that the public perception of the scope of the section 117 backup copy exception may be distorted, and that persons engaged in piracy of software and other content assert they can justify their actions by relying on section 117. That commenter contended, for example, that persons attempting to auction off their so-called backup

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[208] C-Antony, at 4-5.

[209] R-Library Ass'ns, at 11. "Many types of works that were formerly distributed in print and analog formats are now being distributed only in digital format." *Id.* at 14.

[210] *Id.* at IS.

[211] R-SIIA, at 9.

copies of computer software or who make pirated software available on websites, ftp sites or chat rooms, do so under the guise of the section 117 backup copy exception.[212]

A trade association representing publishers of video and computer games stated that section 117 is used, not as a legitimate defense to infringement, but as an enticement to engage in piracy.[213] It asserted that, despite the diminishing need for an archival copy exception to protect any legitimate interest of users of computer programs, and the lack of any judicial precedent for expanding the scope of section 117(a)(2), the Internet is replete with sites purporting to offer "backup copies" of videogames containing computer programs, or the means for making them?" It contended that many of these sites specifically refer to section 117 as providing a legal basis for their operations; for example, one website offering such 'backup copies' reassures users that "under the copyright laws of the U.S.,you are entitled to own a backup of any software you have paid for," while another proclaims: "All the games, music cd's, and computer software that you will find on this page for sale are copied because it is perfectly legal by Section 117 of the US Copyright Law, to own these cd's and use them as long as you have the original program, game, or music cd."[215] In fact, according to this commenter, these sites are not actually offering "backup copies" or even copies that they rightfully own, and in any event they offer works other than computer programs. The commenter asserted that such sites "refer to section 117(a)(2) only

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212 C-SIIA, at 34.

213 C-Interactive Digital Software Association (IDSA). at 5.

214 *Id.*

215 *Id.*

to provide a patina of legitimacy to their operations, and to foster a false sense among users that a patently illicit transaction – a download of pirate product – might in fact somehow be lawful.

The same commenter recommended that the language of section 117(a)(2) be narrowed to make it clear that the provision does not allow a free-standing market in so-called "backup copies," and that it only covers the copying of computer programs to the extent required to prevent loss of use of the program when the original is damaged or destroyed due to electrical or mechanical failures. It asserted that such a statutory adjustment would not only accurately reflect the changes wrought by two decades of technological advancement, but would also promote legitimate electronic commerce. Perhaps most importantly, such an adjustment would eliminate much of the confusion created in the minds of some users by those who justify their piratical activities by reference to a supposed "right" to make "back up copies" of entertainment software products.[216]

b. *Clarification of the Archival Copy Exemption for Computer Programs*

One commenter noted that section 117 does not comport with normal practices and procedures that people use for archiving information on computers?" He asserted that while most businesses, and many individuals, perform periodic backups of everything on their hard

[216] *Id.* at 6.

[217] WST-Hollaar.

drive, section 117 prescribes a different style of archiving: making a copy of an individual program at the time the consumer obtains it.[218]

In this case, the commenter advised, the archival copy will not only contain copied data, but also copied commercial software that happened to be installed on the hard drive. Not only is the program copied but also data that came along with the program, even though section 117 does not give permission to copy that data.[219]

if the use of a particular program ceases to be rightful (primarily because the user has obtained a new version of the program – perhaps an upgraded version) the user no longer has the right to use it, but rather has the right to use the new program. The user most likely will not go back, find the CD-ROM that includes the archived data and programs and try to attempt in some way to delete the programs from the CD. Section 117, noted the commenter, does not match the reality of how file archives are made today.[220]

Another commenter agreed and said multiple backup copies are needed; programs that perform backups have no knowledge of the license status of the computer files being backed up and there is no commonly used file system that stores such status with the files, so that there is no way (within common practice) for backup programs to ascertain that status.[221] He also explained

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[218] *Id.*

[219] *Id.* at 93-95.

[220] *Id.*

[221] C-LXNY, at 1.

that periodic backups are made according to schedules, and to enable recovery. For example, backups may be made daily, weekly, monthly, yearly. Each tape (of the "full backup" type) would contain a copy. Although tapes are generally recycled, there are often legitimate reasons to preserve tapes.[222]

In response to the question whether there is any evidence of actual harm resulting from this mismatch between section 117 and the way system administrators or others actually backup network systems, most commenters were not aware of any harm that had resulted in this mismatch.[223] One commenter expressed concern that when the law is so far out of step with reality that it is seldom, if ever, observed, respect for the legal system diminishes and the rule of law suffers."

However, one commenter did not agree that archiving backup copies necessarily amounted to a violation of section 117. He pointed out that it would be necessary to look at section 107, stating that if the activity does not fall within the specific terms of section 117, then it may be permissible under the fair use doctrine.[225] Another commenter agreed that there was a mismatch, but questioned what the practical effect of this mismatch is. No one has been sued for backing up material that may fall outside the scope of Section 117. The commenter noted that the mission of the Report is to respond to real problems. He referred to the comment submitted

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[222] *Id.*

[223] *Id.* at 129.

[224] *Id.* at 95.

[225] T-SIIA, Kupferschmid, at 148.

by the Interactive Digital Software Association, which reported that one of the easiest ways to find pirated videogames online is to search for the term "section 117," since many websites offering pirated products refer, incorrectly, to that provision as legitimizing their conduct.[226]

D. VIEWS ON MISCELLANEOUS TOPICS

A number of public comments that we received addressed issues that are not directly related to section 109 or section 117. These miscellaneous views are summarized below.

1. Effect of Technological Protection Measures and Rights Management Information on Access to Works, Fair Use, and Other Noninfringing Uses.

There were many comments relating to the effects on noninfringing uses of works of technological protection measures used by copyright owners to protect their works from unauthorized access or copying. The library associations argued that it is not in the public interest to introduce legal and technological measures that diminish, if not eliminate, otherwise lawful uses.[227] The public, they asserted, now must face licensing barriers (contractual restrictions) and legal barriers (criminal penalties for circumvention) to both private and public lending and use.[228] They fear that it will remain illegal for a library or a user to circumvent technical protection measures in order to use the underlying works in ways that have traditionally been permitted under the first sale doctrine, fair use and exemptions for preservation.[229]

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226 T-Copyright Industry Orgs., Metalitz, at 249.

227 T-Library Ass'ns, Petersen, at 23.

228 C-Library Ass'ns, at 4.

229 *Id.* at 2.

The DMCA was criticized by another commenter because he said it prohibits circumvention of access control devices without requiring that the devices serve only their primary purpose.[230] This commenter believes the DMCA should not allow access control devices to act as a single entry point to a technology, thereby creating an artificially privileged group of technology providers in the market.[231]

Another commenter reached the opposite conclusion based on the premise that technological protection measures are largely ineffective. This commenter noted that despite the current illegality of circumventing technological protection measures, these measures are routinely defeated, concluding that, in practice, the law has not had a significant effect on controlling copying and distribution of digital works.[232]

Some commenters expressed concern with the effects on a user's ability to use copyrighted material under the fair use provisions when anticircumvention devices are employed. More broadly, one commenter opined that the pendulum has swung too far in the interest of copyright owners and has begun to trample the needs and rights of the copyright users.[233] The library associations noted that many librarians are reluctant to make fair use judgment calls due to accountability imposed by CMI technologies and criminal sanctions; where uncertainty about

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[230] C-Fischer, at 1-2.

[231] *Id.*

[232] C-SLAC, at 1-5.

[233] C-Beard, at 1-3.

permissible use exists, liability concerns may lead librarians to forego uses that are actually permitted under license and law.[234]

Another comment regarding the anti-circumvention provisions of the DMCA related to the implementation of the Secure Digital Music Initiative (SDMI) and similar technologies that could deprive educators and researchers of access to music.[235] The commenter noted that access to music under traditional notions of fair use has always been a part of our nation's cultural and legal history.[236]

2. Privacy

The library associations expressed concern for privacy rights and noted that, with copyright management information, content owners have the ability to track ongoing use of works in digital form, and to monitor who is looking at a work and exactly what the users are doing with it despite Congress' efforts to protect privacy in the DMCA.[237] They went on to say that although the DMCA's definition of CMI specifically excludes any personally identifying information about a user of a work or a copy,[238] the way CMI technologies are actually implemented may result in the compilation and tracking of usage information.[239]

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234 C-Library Ass'ns, at 8.

235 C-Future of Music Coalition, at 3.

236 *Id.*

237 C-Library Ass'ns, at 8.

238 17 U.S.C.§ 1202(c).

239 C-Library Ass'ns, at 8.

Another commenter noted a threat to the right to privacy since copyright holders may invade the privacy of citizens attempting to communicate privately with one another on the grounds that "violations" or "infringements" may be occurring.[240] This may lead government, said the commenter, to routine monitoring of its own citizens' communications in order to prevent the transmission of "unlicensed" information."'

3. Contract Preemption and Licensing

Many comments raised in both written and oral testimony related to contract preemption and licensing issues. The library associations argued that the first-sale doctrine is being undermined by contract and restrictive licensing which results in uncertainty about the application of the first sale doctrine for copies of works in digital form.[242] They noted the trend towards the displacement of provisions of the uniform federal law — the Copyright Act — with licenses or contracts for digital information. The library associations asserted that college and university administrators, faculty, and students who previously turned to a single source of law and experience for determining legal and acceptable use must now evaluate and interpret thousands of licenses.[243]

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[240] C-Darr, at 2.

[241] *Id.*

[242] T-Library Ass'ns. Neal, at 16.

[243] *Id.* T-Library Ass'ns., Petersen, at 23.

Another commenter argued that the case law is in disarray concerning the effectiveness of contractual terms contained in so-called "shrink-wrap" and "click-through" licenses'" that ovemde consumer privileges codified in the Copyright Act. This commenter proposed that section 301 of the Copyright Act[245] be amended to provide a clear statement of the supremacy of federal copyright law provisions providing for consumer privileges over state contract rules.[246] The library associations agreed with this view. Publishers responded to this line of argumentation by characterizing it as a licensing issue, not a first-sale issue.[247] The publishers noted that Congress did not intend copyright law broadly to preempt contract provisions, citing the example of section 108(f)(4) which provides that despite the privileges otherwise provided to libraries and archives under section 108, nothing in the section is to affect any contractual obligations assumed at any time by a library or archives when it obtained a copy of a work in its collections. These privileges for libraries, according to the publishers, were written to take account of the fact that contractual licensing was going to be the primary way in which copyright owners were going exploit the rights provided to them under the law.[248] Another commenter pointed out that it is a long accepted principle of American jurisprudence that parties should be free to form contracts as they see fit.[249]

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[244] See *supra*, note 100.

[245] 17 U.S.C. § 301. Section 301 establishes the scope of federal preemption under the Copyright Act. See *infra*, at 162.

[246] C-DFC. at 3; T-DFC. Jaszi, at 228.

[247] T-AAP. Adler, at 31.32.

[248] *Id.*

[249] R-DCC, at 4.

Some commenters discussed UCITA in this context and noted ~~that~~, as with the Uniform Commercial Code and other uniform state laws, UCITA is intended to help facilitate electronic commerce.[250] Concern was expressed that UCITA ignores the supremacy of federal law, and, again, recommendations were made to amend section 301. The library associations believe that ambiguity in the law harms libraries and has a stifling impact on library activities. As an example, they stated that it is unclear whether a librarian, on behalf of a patron, can secure and provide interlibrary loan copies or interlibrary loan delivery of works in this environment.[251]

4. Open Source Software

One commenter was concerned that amendments to section 109 may jeopardize the ability of open source and free software licensors to ensure that third-party transferees receive the entire product whose distribution was authorized by the licensor, including the software license rights.[252] Open source or free software licenses grant users the right to: (1) have the source code; (2) freely copy the software; (3) modify and make derivative works of the software; and (4) transfer or distribute the software in its original form or as a derivative work, without paying copyright license fees.[253] The entire open source model is premised on the enforceability of those license provisions.

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[250] R-DCC, at 1; see *supra*, note 38 and accompanying text.

[251] T-Library Ass'ns, Neal, at 55.

[252] T-Red Hat, Kunze, at 256, 257.

[253] WST-Red Hat.

5. Other DMCA Concerns

Several commenters expressed opposition to the DMCA for a variety of reasons. One commented that his right to communicate freely under the First Amendment was threatened by the DMCA because it broadened the definition and scope of copyright. This, in turn, resulted in frivolous cease and desist letters being sent to those attempting to exercise fair use and other exceptions.[254]

Another commenter expressed concern that the DMCA shifted the balance of power away from consumers and gave undue leverage to corporations.[255] This commenter believes that the DMCA has hampered progress and the rights of citizens by, for example, taking down websites without due process and condoning corporate behavior that does not support fair use.[256]

Concern was expressed over the distribution of monies relating to the digital performance right in sound recordings.[257] This commenter noted that the royalties should not be distributed in the "same unfair and inaccurate way" as monies are distributed under the current formula of the Audio Home Recording Act.

[254] C-Darr, at 1.

[255] C-Jones, at 1.

[256] *Id.*

[257] C-Future of Music Coalition, at 2.

III. EVALUATION AND RECOMMENDATIONS

A. THE EFFECT OF TITLE I OF THE DMCA ON THE OPERATION OF SECTIONS 109 AND 117

We are not persuaded that title I of the DMCA has had a significant effect on the operation of sections 109 and 117 of title 17, apart from some isolated factual contexts that are discussed below. Many of the public comments received by us alleged that 17 U.S.C. § 1201, as enacted in title I of the DMCA,[258] is affecting the operation of sections 109 and 117[259] (while a significant number of others argued that it is not[260]). However, either the concerns raised cannot be accurately described as being "effects on the operation of" one of those sections, or if there is an effect on the operation of one of those sections, that effect can just as easily be ascribed to other factors (such as the existence of license terms) as to section 1201. Consequently, none of the legislative recommendations made in this Report are based on effects of section 1201 on the operation of sections 109 and 117.

1. The Effect of Section 1201 on the Operation of the First Sale Doctrine

a. DVD *Encryption*

Several commenters argued that section 1201's protection of CSS for DVDs against circumvention affects consumers' exercise of the first sale doctrine by enforcing technological limitations on the way DVDs can be used.[261] These commenters asserted that because CSS is

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[258] No commenters indicated that any other provision of title I of the DMCA affected the operation of sections 109 and 117, and we are not aware of any issues relating to whether other provisions have an effect on those sections of the Copyright Act.

[259] See C-Fischer, C-DFC, C-NARM/VSDA.

[260] See C-Copyright Industry Orgs., C-Time Warner Inc.

[261] See C-Arromdee, C-Thau and Taylor.

proprietary technology that is licensed to device manufacturers under restrictive terms, the use of CSS limits the potential playback devices for DVDs, which, in turn, limits the potential market for resale of DVDs. Second, they argued that because licensed playback devices enforce region codes,[262] DVDs purchased in one region of the world cannot be as easily resold in other regions, again limiting the potential resale market.

This argument is without merit. The first sale doctrine codified in section 109 limits an author's distribution right so that subsequent disposition of a particular copy by its owner is not an infringement of copyright. The first sale doctrine does not guarantee the existence of a secondary market or a certain price for copies of copyrighted works. If fewer people may wish to purchase a used DVD, or if they would pay less for it due to CSS, that would not equate to interference with the operation of section 109. Many circumstances in the marketplace may affect the resale market for copies of works – improvements in technology, introduction of new formats, and the quality and cultural durability of the content of the work. None of these factors can properly be said to interfere with the operation of section 109, even though they could reduce the resale market for a work or even render it nonexistent.[263]

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[262] Each DVD bears an embedded region code corresponding to the region of the world where the particular DVD is authorized to be sold. Licensed DVD players will only play DVDs that are coded for the region where the player is sold. Region coding is used to prevent gray market importation of DVDs from one region to another.

[263] To the extent that there is a concern that region coding may limit the number of purchasers outside North America who are willing to buy region 1 DVDs (i.e., DVDs coded for sale within North America), that concern has nothing to do with section 1201. Section 1201 of title 17, United States Code, has no effect outside the United States. Consequently, a purchaser in Hong Kong could modify a region 6 player so that it could play a region 1 DVD without fear of any repercussions under section 1201 (although there may or may not be consequences under Hong Kong law). Moreover, resale outside the U.S. has nothing to do with section 109, which only governs resale within the United States.

Equally without merit is the argument – essentially a corollary to the guaranteed resale market argument – that the first sale doctrine gives consumers a right to use a DVD on any electronic device. In fact, virtually all devices capable of playing a DVD that are sold in the U.S. are compliant with CSS, so there is no real effect on the resale market as a result of the application of CSS technology. Further, this argument has nothing whatever to do with the privilege under section 109 to dispose of a copy of a work. Moreover, taken one step further, that argument would lead to the absurd result of requiring that consumers be able to play Beta videocassettes on VHS players, or VHS videocassettes on personal computers.

b. *Tethering Works to a Device*

A plausible argument can be made that section 1201 may have a negative effect on the operation of the first sale doctrine in the context of tethered copies – copies that are encrypted with a key that uses a unique feature of a particular device, such as a CPU identification number, to ensure that they cannot be used on *any* other device.[264] Even if a tethered copy is downloaded directly on to a removable medium such as a Zip™ disk or CD-RW, the content cannot be accessed on any device other than the device on which it was made. Disposition of the copy becomes a useless exercise, since the recipient will always receive nothing more than a useless piece of plastic. The only way of accessing the content on another device would be to circumvent the tethering technology, which would violate section 1201.

[264] See C-CPSR, at 4-5.

The practice of using technological measures to tether a copy of a work to a particular hardware device does not appear to be widespread at the present time, at least outside the context of electronic books. We understand through informal discussions with industry that this technique is – or at least can be – employed in some cases with electronic books using digital rights management (DRM) technology. Given that DRM is in its relative infancy, and the use of DRM to tether works is not widespread, it is premature to consider any legislative change to mitigate the effect of tethered works on the first sale doctrine. Nevertheless, we recognize that if the practice of tethering were to become widespread, it could have serious consequences for the operation of the first sale doctrine, although the ultimate effect on consumers of such a development remains unclear.

2. The Effect of Section 1201 on the Operation of Section 117

The use of technological measures that prevent copying of a work could have a negative effect on users' ability to make archival copies that are permitted under section 117. If, and to the extent that, such anti-copying measures can also be considered to be access control measures that are protected against circumvention by section 1201,[265] section 1201 could be said to have an adverse impact on the operation of section 117 in this context. For several reasons, however, the actual impact on consumers appears to be minimal.

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[265] Section 1201 does not prohibit the circumvention of technological protection measures that only prevent copying. Thus, a user could lawfully circumvent the measures to create an archival copy. However, to the extent that copy controls also function as access controls, the circumvention of which is prohibited by section 1201, the circumvention of those measures is prohibited. Moreover, because section 1201 also prohibits the creation and distribution of circumvention tools, those consumers who lack the ability to circumvent technological protection measures would be unable to circumvent those measures even when such circumvention would not be unlawful.

First, since the overwhelming majority of computer programs sold in the United States are sold pursuant to a license, and section 117 applies only to "owners," the terms of the license agreement generally determine whether a user has the right to make an archival copy.[266] In cases where the license does not pennit the creation of an archival copy, even absent technological protection measures, the copying is prohibited. Thus, in such cases it is the license that is impairing the operation of section 117.

Second, at the present time most software is sold without copy protection. Where the license permits or does not preclude the creation of an archival copy (or in the relatively few cases where the transaction was an outright sale) the user may make an archival copy as contemplated in section 117.

Third, as of last year approximately ninety-eight percent of computer software sold in the United States was sold on CD-ROM.[267] This means that even where consumers are prevented from making an archival copy, they are still able to reinstall the work in the event of computer malfunction. In essence, the CD-ROM itself acts as the archival copy. In that case, even if consumers are prevented from making archival copies as contemplated in section 117, their software investment is protected fiom system malfunctions, thus fulfilling the purpose of the

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[266] *Our* (admittedly unscientific) review of sixteen license agreements for software used by the Copyright Office found that fourteen of them permitted the user to *make* a backup copy and one was silent. Only one of the sixteen licenses prohibited the user fiom making a backup copy, requiring the user either to use the original media as the backup copy or to replace the original media for a twenty-five dollar fee.

[267] R-SIIA, at 9.

archival exemption as articulated by CONTU.[268] Accordingly, we conclude that the evidence at this time of an effect of title I of the DMCA on the operation of section 117 is not substantial, and no legislative change is warranted.

B. THE EFFECT OF ELECTRONIC COMMERCE AND TECHNOLOGICAL CHANGE ON SECTIONS 109 AND 117

We have made no attempt in preparing this study to separate out the impact of electronic commerce on sections 109 and 117 from the impact of technological change. Such an effort would probably have been futile since, as the language of section 104 suggests, by grouping the two issues together, the issues are inextricably intertwined. In its essence, electronic commerce is commerce carried out through new technologies. This study is an outgrowth of the intersection between new technology and the new business models that it makes possible. Our evaluation is of the impact of that intersection on the specified provisions of the Copyright Act.

1. The First Sale Doctrine in the Digital World

a. *Application of Existing Law to Digital Content*

The application of section 109 to digital content is not a question of whether the provision applies to works in digital form — it does. Physical copies of works in a digital format, such as CDs or DVDs, are subject to section 109 in the same way as physical copies of works in analog form. Likewise, a lawfully made tangible copy of a digitally downloaded work, such as an image file downloaded directly to a floppy disk, is subject to section 109. The question we address here

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[268] See *supra*, at 29.

is whether the conduct of transmitting the work digitally,[269] so that another person receives a copy of the work, falls within the scope of the defense.[270]

Section 109 limits a copyright owner's exclusive right of distribution. It does not, by its terms, serve as a defense to a claim of infringement of any of the other exclusive rights?" The transmissions that are the focus of proposals for a "digital first sale doctrine"[272] result in reproductions of the works involved. The ultimate product of one of these digital transmissions is a new copy in the possession of a new person. Unlike the traditional circumstances of a first sale transfer, the recipient obtains a new copy, not the same one with which the sender began. Indeed, absent human or technological intervention, the sender retains the source copy. This copying implicates the copyright owner's reproduction right as well as the distribution right.

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[269] The transmissions discussed in this section are not broadcasts, but transmissions that, like point-to-point transmissions, involve the selection of specific recipients by the sender.

[270] Some commenters were confused between the proposal to apply the first sale doctrine to otherwise unauthorized digital transmissions of copyrighted works by lawful owners of copies of such works and the notion that a lawful copy created as a result of an authorized digital transmission is a lawful copy for purposes of section 109. The former would expand the scope of section 109 and will be discussed below. The latter is well within the current language of the statute. Regardless of whether a copy is created as a result of the nearly instantaneous transmission of digital information through broadband computer connections or as a result of months of painstaking labor of a cloistered monk working with a quill by candlelight, so long as that copy is lawfully made, it satisfies the second prong of eligibility for the section 109 defenses.

[271] 17 U.S.C. § 109(a). In limited circumstances the public display right is covered as well. 17 U.S.C. § 109(c). See supra, note 53.

[272] The term "digital first sale doctrine" is used here to denote a proposed copyright exception that would permit the transmission of a work from one person to another, generally via the Internet, provided the sender's copy is destroyed or disabled (whether voluntarily or automatically by virtue of a technological measure). We use the term because it has been used frequently in discourse about the subject. It is, however, a misnomer since the proposal relates not to works in digital form generally (which are, of course, already subject to section 109), but to transmissions of such works.

Section 109 provides no defense to infringements of the reproduction right. Therefore, when the owner of a lawful copy of a copyrighted work digitally transmits that work in a way that exercises the reproduction right without authorization, section 109 does not provide a defense to infringement.

Some commenters suggested that this reading of section 109 is unduly formalistic. The language of the statute, however, must be given effect. Section 109 is quite specific about the rights that are covered, and does not support a reading that would find additional rights to be covered by implication. Where Congress intended to immunize an activity, such as fair use, from infringement of any of the exclusive rights, it did so expressly.[273] It simply cannot be presumed that where Congress did enumerate specific rights, it somehow intended other rights to be included as well. In addition, our reading of section 109 is entirely consistent with the judicial origin of the first sale doctrine in the *Bobbs-Merrill* decision. The Supreme Court drew a sharp distinction between the two rights, creating an exception to the vending (i.e., distribution) right only to the extent that it didn't interfere with the reproduction right.[274] We therefore conclude that section 109 does not apply to digital transmission of works.

b. *Evaluation of Arguments Concerning Expansion of Section 109*

A number of commenters proposed that section 109 be expanded to apply expressly to the reproduction, public performance and public display rights to the extent necessary to permit the

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[273] *E.g.*, 17 U.S.C.§ 107 ("Notwithstanding the provisions of sections 106 and 106A, the fair use of a copyrighted work . . . is not an infringement of copyright.").

[274] *Bobbs-Merrill*, 210 U.S. at 350-51. See discussion *supra*, at 20-21.

digital transmission of a work by the owner of a lawful copy of that work, so long as that copy is destroyed. This section will review the arguments for and against such a digital first sale doctrine.

i. Analogy to the physical world

Arguments in support of a digital first sale doctrine generally proceed from an analogy to the circulation of physical goods. Whether couched as a means of achieving technological neutrality,[275] meeting consumer expectations that were formed in the off-line world,[276] or eliminating barriers to competition between e-commerce and traditional commerce,[277] an underlying basis for the argument in favor of a digital first sale doctrine is that the transmission and deletion of a digital file is essentially the same as the transfer of a physical copy.

To be sure, there is an important similarity between physical transfer, on one hand, and transmission and deletion, on the other. At the completion of each process the transferor no longer has the copy (at least in usable form) and the transferee does. Some of the proposals would enhance this similarity by requiring the use of technological measures (in some cases

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[275] *E.g.*, C-Anthony, at 3.

[276] *E.g.*, R-DiMA, at 6 (arguing that without a digital first sale doctrine, consumers are being short-changed when they purchase copyrighted works online because they don't get what they expect and, consequently, will become disenchanted with the medium, decreasing legitimate demand and increasing online infringement).

The opponents of a digital first sale doctrine counter that the proposal would sharply reduce the supply of works available online because copyright owners would lack confidence that their works will be protected from piracy. In addition, they point out that there is tremendous demand for copyrighted works online, even though section 109 has not been expanded. R-SIIA, R-BMI. They view this as evidence that revision of section 109 is not a prerequisite to having robust growth in e-commerce in copyrighted works.

[277] C-HRRC, at 5-6.

referred to as "move" or "forward-and-delete"technology) that will disable access to or delete entirely the source file upon transfer of a copy of that file. Assuming the technology is effective, these proposals would ensure that the single act of sending the work to a recipient results in a copy of the work being retained by the recipient alone. They differ from the Boucher-Campbell bill, which required an additional affirmative act: the subsequent deletion of the work by the sender.

Implicit in any argument by analogy is the assertion that the similarities outweigh the differences. Whether or not the analogy outlined above is compelling from a policy perspective depends upon whether the differences between the circulation of physical copies and electronic "transfers" are more significant than the similarities.

Physical copies of works degrade with time and use, making used copies less desirable than new ones. Digital information does not degrade, and can be reproduced perfectly on a recipient's computer. The "used"[278] copy is just as desirable as (in fact, is indistinguishable from) a new copy of the same work. Time, space, effort and cost no longer act as barriers to the movement of copies, since digital copies can be transmitted nearly instantaneously anywhere in the world with minimal effort and negligible cost. The need to transport physical copies of works, which acts as a natural brake on the effect of resales on the copyright owner's market, no

[278] The "used" copy refers to the copy on the recipient's computer. In fact, it is not "used" in any sense of the word since it was initially created on the recipient's computer as the end result of the transmission process.

longer exists in the realm of digital transmissions. The ability of such "used" copies to compete for market share with new copies is thus far greater in the digital world.[279]

Even the "lending" of a fairly small number of copies of a work by digital transmission could substitute for a large number of purchases. For example, one could devise an aggregation site on the Internet that stores (or, in a peer-to-peer model, points to) multiple copies of an electronic book. A user can "borrow" a copy of the book for as long as he is actually reading it. Once the book is "closed," it is "returned" into circulation. Unlike a typical lending library, where the book, once lent to a patron, is out of circulation for days or weeks at a time, the electronic book in this scenario is available to other readers at any moment that it is not actually being read. Since, at any given time, only a limited number of readers will actually be reading the book, a small number of copies can supply the demand of a much larger audience. The effect of this activity on the copyright owner's market for the work is far greater than the effect of the analogous activity in the non-digital world.

In addition, unless a "forward-and-delete" technology is employed, transfer of a copy by transmission requires an additional affirmative act by the sender. In applying a digital first sale doctrine as a defense to infringement it would be difficult to prove or disprove whether that act had taken place, thereby complicating enforcement.[280] This carries with it a greatly increased risk

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[279] T-SIIA, Kupferschmid, at 85.

[280] These differences have already been noted by the Register on a prior occasion. Marybeth Peters, *The Spring 1996 Horace S. Manges Lecture – The National Information Infrastructure: A Copyright Office Perspective*, 20 Colum. V.L.A. Journal 341, 355 (Spring, 1996).

of infringement in a medium where piracy risks are already orders of magnitude greater than in the physical world. Removing, even in limited circumstances, the legal limitations on retransmission of works, coupled with the lack of inherent technological limitations on rapid duplication and dissemination, will make it too easy for unauthorized copies to be made and distributed, seriously harming the market for those works.[281]

Even the use of "forward-and-delete" technology, as advocated by some commenters,[282] is not a silver bullet. Technological measures can be hacked; they are expensive; and they often encounter resistence in the marketplace. In order to achieve a result that occurs automatically in the physical world, a publisher would have to pay for an expensive (and less than 100 percent reliable) technology and pass that cost along to the consumer, while at the same time potentially making the product less desirable in the marketplace. The ability of the market to correct this imbalance would be inhibited because copyright owners would need to apply these measures or face the risk of unauthorized copying under the guise of the first sale doctrine. In addition, technological measures may inadvertently impede legitimate uses of the work, harming consumers. Further, no one has offered evidence that this technology is viable at this time.

One copyright industry representative observed in oral testimony that there had been no "hue and cry, not even so much as a suggestion, that consumers are looking for products that will

[281] *Accord* R-Time Warner Inc., at 2-3.

[282] *E.g.*, R-DiMA, at 5.

function under the forward-and-delete model."[283] To the contrary, the Napster phenomenon was cited as evidence that consumers wish to retain, not destroy, the digital copy from which the work is transmitted."' We encountered nothing in the course of preparing this Report that would refute this observation.

Each of these differences between circulation of tangible and intangible copies is directly relevant to the balance between copyright owners and users in section 109. In weighing the detrimental effect of a digital first sale doctrine on copyright owners' markets against the furtherance of the policies behind the first sale doctrine it must be acknowledged that the detrimental effect increases significantly in the online environment. "The ultimate question is whether an equivalent to the first sale doctrine should be crafted to apply in the digital environment. The answer must turn on a determination that such a new exception *is* needed to further the policies behind the first sale doctrine, and that it can be implemented without greater detriment to the copyright owner's market."[285] We turn now to an evaluation of the policies behind the first sale doctrine.

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[283] T-NMPA, Mann, at 157.

[284] *Id.* at 157-58.

[285] Peters, *supra*, note 280, at 355-56 (emphasis in original).

ii. Policies behind the first sale doctrine

"The first sale doctrine was originally adopted by the courts to give effect to the early common law rule against restraints on the alienation of tangible property."[286] As discussed above, it appears to have been motivated as well by competition concerns – specifically, the ability of publishers to use their vending or distribution right to control not only the initial sales of books, but the aftermarket for resales.[287]

The tangible nature of the copy is not a mere relic of a bygone technology. It is a defining element of the first sale doctrine and critical to its rationale. This is because the first sale doctrine is an outgrowth of the distinction between ownership of intangible intellectual property (the copyright) and ownership of tangible personal property (the copy).[288]

The distribution right can be conceptualized as an extension of the copyright owner's exclusive rights to include an interest in the tangible copies. Under common-law principles, the owner of the physical artifact – the copy – has complete dominion over it, and may dispose of possession or ownership of it as he sees fit. The distribution right, nonetheless, enables the

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[286] S. Rep. No. 162.98" Cong., 1"Sess. 4 (1983). The legislative history of section 109 and of section 27 of the 1909 law. the first codification of the first sale doctrine, is quite brief. Despite its brevity, it focuses on one important and relevant concept. Repeatedly, the congressional reports refer to the ability of the owner of a *material* copy to dispose of that copy as he sees fit. H.R Rep. No. 2222.60" Cong., 2nd Sess. 19 (1909); H.R 28 192.60" Cong., 2" Sess. 26 (1909); H.R. Rep. No. 94-1476, 94th Cong., 2nd Sess. 79 (1976).

[287] See *supra*, at 21.

[288] "Ownership of a copyright, or of any of the exclusive rights under a copyright, is distinct from ownership of any material object in which the work is embodied. Transfer of ownership of any material object, including the copy or phonorecord in which the work is first fixed, does not of itself convey any rights in the copyrighted work embodied in the object; nor, in the absence of an agreement, does transfer of ownership of a copyright or of any exclusive rights under a copyright convey property rights in any material object." 17 U.S.C. § 202.

copyright owner to prevent alienation of the copy – up to a point. That point is when ownership of a lawfully made copy is transferred to another person – *i.e.*, first sale. The first sale doctrine upholds the distinction between ownership of the copyright and ownership of the material object by confining the effect of the distribution right's encroachment on that distinction.

The underlying connection between the two concepts is apparent in the 1909 Copyright Act. Both the first sale doctrine and the doctrine that ownership of copyright is distinct from ownership of a material object are found in section 27.[289] Notwithstanding their codification in separate sections of the 1976 Act, their origin as part of the same provision of the 1909 Act demonstrates that the concepts are two sides of the same coin.

Digital transmission of a work does not implicate the alienability of a physical artifact. When a work is transmitted, the sender is not exercising common-law dominion over an item of personal property; he is exercising the central copyright right of reproduction with respect to the intangible work. Conversely, the copyright owner's reproduction right does not interfere at all with the ability of the owner of the physical copy to dispose of ownership or possession of that copy, since the first sale doctrine applies fully with respect to the tangible object (e.g., the user's hard drive) in which the work is embodied.

Because the underlying purpose of the first sale doctrine is to ensure the free circulation of tangible copies, it simply cannot be said that a transformation of section 109 to cover digital

[289] The text of section 27 is quoted, *supra*, note 39.

transmissions furthers that purpose. The concerns that animate the first sale doctrine do not apply to the transmission of works in digital form.[290]

A number of the comments we received express the view that a digital first sale doctrine would further the purposes of section 109. We note that none of those comments are supported by a historically sound formulation of what those purposes are. For example, one commenter argued that the first sale doctrine is based on a calculation of incentives to create.[291] This view is not supported by the legislative history of section 109. Moreover, as is discussed below, the potential harm to the market and increased risk of infringement that would result from an expansion of section 109 could substantially reduce the incentive to create.[292] Thus, this argument is both historically unsound and unpersuasive as a practical matter.

Another commenter suggested that the original purpose of the first sale doctrine was "to Promote the Progress of science and Useful *Arts* [sic]."[293] This observation does not advance the argument. It is a given that the "Progress of Science and useful Arts"[294] is the policy

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[290] "The first sale doctrine was developed to avoid restraints on the alienation of physical property, and to prevent publishers from controlling not only initial sales of books, but the after-market for resales. These concerns do not apply to transmissions of works on the [Internet]." Peters, *supra*, note *280*, at 355-56 (emphasis in original).

[291] C-DiMA, at 5-6 ("Copyright law secures to the copyright owner the exclusive rights of first distribution to provide an incentive for the creation and dissemination of copyrighted works. Once the copyright holder has been compensated for the initial distribution of the work. no further incentive is required, so the copyright owner should not be able to extract further profits from that particular copy of the work").

[292] See *infra*, at *97-99.*

[293] C-DFC. at 2 ("Historically, the 'first sale' doctrine has contributed to the achievement of that goal by providing a means for the broad secondary dissemination of works of imagination and information.") (quoting without citation, U.S. Const. *Art.* I, sec. 8).

[294] U.S. Const. Art. I sec. 8.

undergirding the *entire* Copyright Act. However, particular provisions of the law may have more precise purposes, as is the case here.

The library associations made the claim that the first sale doctrine is based on a right of access[295] – a right not found in the legislative history of section 109. In support of this argument, they cited to section 109(d)[296] as a demonstration that section 109 applies "according to the scope of the interest that has been transferred, rather than according to the object of that interest."[297] We understand this argument to suggest that because the lease of a tangible object is not activity to which section 109 applies, the fact that a work is embodied in a tangible object must not be the test for the application of section 109. Instead, this argument appears to suggest, the scope of the interest conveyed (ownership versus rental) is the determinative factor for the application of section 109. This interpretation is fundamentally flawed. Section 109 is conditioned on both ownership (as opposed to mere possession) and the requirement that such ownership be of a particular physical copy. The failure to satisfy either requirement will preclude the distribution of the copy pursuant to section 109.

The library associations supported their conclusion regarding the first sale doctrine being a proxy for a right of access by proceeding from the premise that the requirement of a particular physical copy should be jettisoned from the doctrine. To support that premise, the library

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[295] R-Library Ass'ns, at 3-7.

[296] 17 U.S.C.§ 109(d) (stipulating that the privileges of this section apply only to ownership of copies, not mere possession).

[297] *Id.* at 3.

associations claim that the requirement of a particular physical copy "was an efficient proxy for distinguishing the copyright owner's exclusive rights in his work from the right to access and use that work . . . ."[298] The argument is circular.

There is nothing to support the thesis that the first sale doctrine is a stand-in for a right of access to copyrighted works. Apart from the reference to section 109(d) discussed above, no authority was marshaled in support of this proposition. Neither the statutory text nor the legislative history of section 109 (or section 27 of the 1909 law) support the proposition. To the contrary, however, the Supreme Court's decision in *Bobbs-Merrill* and the legislative history of the 1909 Act do refer directly to alienability of tangible property.[299]

A number of the comments also made reference to socially desirable activities, such as library lending, that are furthered by the existing first sale doctrine, and argue that similarly desirable activities would be furthered by a digital first sale doctrine. Asserting that a digital first sale doctrine would have beneficial effects is not the same as arguing that it would further the purposes of the existing first sale doctrine, since there is no sound basis for asserting that those effects are related to the purpose of the first sale doctrine. This argument relates not to underlying purpose, but to a balancing of the impact of copyright rights and exceptions. Even assuming the accuracy of the assertion that a digital first sale doctrine would result in socially desirable activities, the fact that a particular limitation on a copyright owner's exclusive rights

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[298] *Id.* at 3-4.

[299] *See supra* at 20-24.

will promote a public good is not, in itself, a sufficient basis for curtailing copyright protection. The social benefit must be balanced against the harm to the copyright owner's legitimate interests, and thus to the incentive to create. As discussed above, the extension, by analogy, of the first sale doctrine to the online environment has a significantly greater negative impact on copyright owners' legitimate interests than does the traditional first sale doctrine in the realm of tangible copies.

iii. Development of new business models

Reasoning by analogy always carries with it the risk of becoming captive to the analogy. Assumptions that are implicit in one situation can carry over to the analogous situation even though those assumptions no longer apply. This appears to be the case with the analogy between distribution of tangible copies and online transmissions of works.

Proposals for a digital first sale doctrine endeavor to fit the exploitation of works online within a distribution model that was developed within the confines of pre-digital technology. Digital communications technology enables authors and publishers to develop new business models, with a more flexible array of products that can be tailored and priced to meet the needs of different consumers.[300] Requiring that transmissions of digital files be treated just the same as the sale of tangible copies artificially forces authors and publishers into a distribution model based on outright sale of copies of the work. The sale model was dictated by the technological necessity of manufacturing and parting company with physical copies in order to exploit a work –

[300] Jane C. Ginsburg, *From Having Copies to Experiencing Works: the Development of an Access Right in U.S. Copyright Law* 10 (2000) (available online at papers.ssrn.com/paper.taf?abstract_id=222493).

neither of which apply to online distribution. If the sale model continues to be the dominant method of distribution, it should be the choice of the market, not due to legislative fiat.

iv. International considerations

In evaluating the arguments put forward to support a digital first sale doctrine, it is instructive to inquire how the international community is addressing the application of exhaustion of rights[301] to the online transmissions of works. The 1996 WIPO treaties[302] set international norms for the treatment of copyright and related rights in the internet environment. The treaties addressed both the circulation of physical goods and the transmission of works.

[301] "Exhaustion" is the term that is often used in international agreements to refer to the termination of a copyright owner's distribution right with respect to a particular copy after that copy has been sold with the copyright owner's authorization — i.e., the first sale doctrine. The distribution right is said to "exhaust" after the first sale.

[302] See *supra*, at 5.

The WCT and the WPPT provide an exclusive distribution right[303] with respect to tangible copies of works while, with respect to intangible copies (that is, transmissions), providing a separate exclusive right of making available to the public, that was conceived as a

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[303] WCT, art. 6:

(1) Authors of literary and artistic works shall enjoy the exclusive nght of authorizing the making available to the public of the original and copies of their works through the sale or other transfer of ownership.

(2) Nothing in this Treaty shall affect the freedom of Contracting Parties to determine the conditions, if any, under which the exhaustion of the right in paragraph (1) applies after the first sale or other transfer of ownership of the original or a copy of the work with the authorization of the owner.'

+Agreed Statement concerning Articles 6 and 7: As used in these Articles. the expressions "copies" and "original and copies," being subject to the right of distribution and the right of rental under the said Articles, refer exclusively to fixed copies that can be put into circulation as tangible objects.

WPPT. art. 8:

(1) Performers shall enjoy the exclusive right of authorizing the making available to the public of the original and copies of their performances fixed in phonograms through the sale or other transfer of ownership.

(2) Nothing in this Treaty shall affect the freedom of Contracting Parties to determine the conditions, if any, under which the exhaustion of the right in paragraph (1) applies after the first sale or other transfer of ownership of the original or a copy of the fixed performance with the authorization of the performer.+

'Agreed statement concerning Articles 2(e), 8, 9, 12, and 13: As used in these Articles, the expressions "copies" and "original and copies," being subject to the right of distribution and the right of rental under the said Articles, refer exclusively to fixed copies that can be put into circulation as tangible objects.;

WPPT, *art.* 12:

(1) Producers of phonograms shall enjoy the exclusive right of authorizing the making available to the public of the original and copies of their performances fixed in phonograms through the sale or other transfer of ownership.

(2) Nothing in this Treaty shall affect the freedom of Contracting Parties to determine the conditions. if any, under which the exhaustion of the right in paragraph (1) applies after the first sale or other transfer of ownership of the original or a copy of the phonogram with the authorization of the producer of the phonogram.•

•Agreed statement concerning Articles 2(e), 8, 9, 12, and 13: As used in these Articles. the expressions "copies" and "original and copies," being subject to the right of distribution and the nght ot rental under the said Articles, refer exclusively to fixed copies that can be put into circulation as tangible objects.

subset of a general right of communication to the public.[304] The treaties permit members to limit the distribution right with an exhaustion principle,[305] but there is no requirement to do so. There is no provision in either treaty regarding exhaustion of the making available or communication rights. This is hardly surprising since exhaustion is a concept that has heretofore only applied to the right to distribute tangible copies.

Those countries that have implemented protection for online transmissions have largely done so through the right of communication to the public and thus provide no equivalent of the first sale limitation to such rights. We are not aware of any country other than the United States that has implemented the making available right through application of a combination of the distribution, reproduction, public performance and public display rights. In a sense, the only reason the issue of first sale arises in the U.S. is because we chose to implement the making

[304] WCT, *art.* 8:

Without prejudice to the provisions of Articles 11(1)(ii), 11*bis*(1)(i) and (ii), 11*ter*(1)(ii) and 14*bis*(1) of the Berne Convention, authors of literary and artistic works shall enjoy the exclusive right of authorizing any communication to the public of their works, by wire or wireless means, including the making available to the public of their works in such a way that members of the public may access these works from a place and at a time individually chosen by them.

WPPT, art. 10:

Performers shall enjoy the exclusive right of authorizing the making available to the public of their performances fixed in phonograms, by wire or wireless means, in such a way that members of the public may access them from a place and at a time individually chosen by them;

WPPT, art. 14:

Producers of phonograms shall enjoy the exclusive right of authorizing the making available to the public of their phonograms, by wire or wireless means, in such a way that members of the public may access them from a place and at a time individually chosen by them

[305] WCT, art 6(2); WPPT, art. 8(2), art. 12(2).

available right through, *inter alia,* the distribution right. Elsewhere, online transmissions are considered communications to the public, and the first sale doctrine simply does not apply.

An important example of this is the European Union's Information Society Directive.[306] This directive, which, among other things, implements the WIPO treaties, provides for a distribution right[307] that is limited by the exhaustion principle, and a separate making available right that is not. The exhaustion principle in the Directive is expressly limited to circulation of tangible copies:

> Copyright protection under this Directive includes the exclusive right to control distribution of the work incorporated in a tangible article. The first sale in the Community of the original of a work or copies thereof by the rightholder or with his consent exhausts the right to control resale of that object in the Community.[308]

The Directive goes further, stating in clear terms that exhaustion does not apply to online transmissions:

> The question of exhaustion does not arise in the case of services and on-line services in particular. This also applies with regard to a material copy of a work or other subject-matter made by a user of such a service with the consent of the rightholder. Therefore, the same applies to rental and lending of the original and copies of works or other subject-matter which are services by nature. Unlike CD-

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[306] Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001, on the harmonisation of certain aspects of copyright and related rights in the information society (OJ L 167/10 2001) ("Information Society Directive").

[307] Information Society Directive, art. 4:

1. Member States shall provide for authors, in respect of the original of their works or of copies thereof, the exclusive right to authorise or prohibit any form of distribution to the public by sale or otherwise.

2. The distribution right shall not be exhausted within the Community in respect of the original or copies of the work, except where the first sale or other transfer of ownership in the Community of that object is made by the rightholder or with his consent.

[308] Information Society Directive, art. 28.

> ROM or CD-I, where the intellectual property is incorporated in a material medium, namely an item of goods, every on-line service is in fact an act which should be subject to authorisation where the copyright or related right so provides.[309]

The decision of the EU not to create an exception to the nght of communication to the public that is similar to the doctrine of exhaustion of the right of distribution represents an informed policy decision that such an expansion is not appropriate. We are not aware of a public outcry in any of the EU countries in opposition to this decision.

The analogy that some in the U.S. have made between the downstream distribution of a tangible copy of a work and an online transmission is attractive because of the broad application of the right of distribution in U.S. copyright law. As both activities implicate the distribution right, the distinction between the distribution of physical objects and intangible transmissions may at first blush seem small. They are, however, distinct acts with distinct characteristics that ought not necessarily be treated similarly. When viewed through an international lens this distinction becomes clearer.

c. *Recommendations*

Based on the foregoing discussion, and for the reasons set forth below, we recommend no change to section 109 at this time. Although there is a great deal of speculation about what may happen in the future, we heard no convincing evidence of present-day problems. However, legitimate concerns have been raised about what may develop as the market and technology evolve. These concerns are particularly acute in the context of the potential impact on library

[309] Information Society Directive, art. 29.

operations. The time may come when Congress may wish to consider further how to address these concerns.

i. No change to section 109

In order to recommend a change in the law, there should be a demonstrated need for the change that outweighs any negative aspects of the proposal. We do not believe that this is the case with the proposal to expand the scope of section 109 to include a digital first sale doctrine.

Much of the rhetorical force behind the digital first sale proposal stems from the analogy to circulation of goods in the physical realm. On examining the nature of digital transmissions compared to the nature of transfers of material objects, we do not find this analogy compelling for several reasons.

The analogy ultimately rests on the fiction that a transmission of a work is the same as a transfer of a physical copy. In order to get around the fact that a transmission results in two copies, the analogy requires one of two things to happen: either a voluntary deletion of the sender's copy or its automatic deletion by technological means. Both are unworkable at this time.

Relying on voluntary deletion is an open invitation to virtually undetectable cheating, and there is no reason to believe there would be general compliance with such a requirement. If the burden were placed on the copyright owner to demonstrate that there was no simultaneous deletion of the copy from which the transmission was made, it would erect what would probably be an impossible evidentiary burden. If the burden of establishing the defense were placed on the defendant, and had to be met by demonstrating simultaneous deletion, the defendant would have a similarly impossible evidentiary burden. If the defendant were merely required to demonstrate the absence of a copy of the work on his hard drive, then the simultaneous deletion principle would, as a practical matter, disappear, and section 109 would become a defense that could be asserted whenever a copy was deleted at any time after it had been transmitted one or more times or copied for retention on another medium. The recent phenomenon of the popularity of using Napster to obtain unauthorized copies of works strongly suggests that some members of the public will infringe copyright when the likelihood of detection and punishment is low.

Relying on a "forward-and-delete" technology is not workable either. At present such technology does not appear to be available. Even assuming that it is developed in the future, the technology would have to be robust, persistent, and fairly easy to use. As such, it would likely be expensive – an expense that would have to be borne by the copyright owner or passed on to the consumer. Even so, the technology would probably not be 100 percent effective. Conditioning a curtailment of the copyright owners' rights on the employment of an expensive technology would give the copyright owner every incentive *not* to use it. In the alternative, it would be damaging to the market to expand section 109 in anticipation of the application of technological protection measures, thus giving the copyright owner a choice between significantly increased expenses, significantly increased exposure to online infringement, or not offering works online.

Asserting, by analogy, that an online digital transmission is the same as a transfer of a material object ignores the many differences between the two events. Digital transmission has a much greater effect on the market for copies provided by the copyright owners. It is also accompanied by a greatly increased risk of piracy.

The risk that expansion of section 109 will lead to increased digital infringement weighs heavily against such an expansion. Copyright piracy in the online world is not a matter of speculation — it is, unfortunately, an established fact of life. It appears likely that expanding section 109 would encourage infringement of the reproduction right, either in the mistaken belief that the provision allows a user to retain a copy of a work after it has been transmitted one or more times, or in the belief that the defense can be asserted in bad faith to defeat, or at least complicate, an infringement lawsuit. And unlike Napster, the activity would not rely on a central server, so both the infringing activity and the evidence of infringement would be decentralized and therefore difficult to detect and

Twice since the enactment of the current Copyright Act, Congress has stepped in to *narrow* the scope of the first sale doctrine to safeguard the reproduction right.[311] In both cases there was anecdotal evidence of abuses in the marketplace, combined with conditions that created the opportunity for widespread abuse. The same conditions apply to the proposals to

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[310] See I. Trotter Hardy, Project Looking Forward: Sketching the Future of Copyright in a Networked World 262-63 (Copyright Office, 1998) (analyzing the difficulties involved in preventing, identifying, and remedying decentralized infringement) (available online at www.loc.gov/copyright/docs/thardy.pdf).

[311] See discussion *supra*, at 24-25.

create a digital first sale doctrine. Again, the striking popularity of Napster is a strong indication that many people will infringe copyright if the means to do so is at their disposal. And the more convenient the means, the greater the likelihood of infringements. The risk to the copyright owners' reproduction right is simply too great.

We do not ignore the claim that an expansion of section 109 would further the pro-competitive goals of the first sale doctrine. To the extent that section 109 does not permit the transmission of copyrighted works, the right holders retain the exclusive right to restrict or prohibit such activity, thereby barring resales that compete with sales of new copies. Of come, a lawfully made and owned copy of a work on a floppy disk, Zip™ disk, CD-ROM or similar removable storage medium can easily be transferred by physical transfer of the item and that activity is within the current reach of section 109. In the final analysis, the concerns about expanding first sale to limit the reproduction right, harm to the market as a result of the ease of distribution, and the lessened deterrent effect of the law that could promote piracy, outweigh the pro-competitive gains that might be realized from the creation of a digital first sale doctrine. In addition, there does not appear to be any evidence that the kind of price-fixing behavior that prompted the Supreme Court to establish the first sale doctrine is occurring. Should such behavior become widespread, and should antitrust law fail to afford an appropriate remedy, this conclusion may have to be revisited.

Implicit in several of the submissions that addressed the first sale issue is a belief that the analogy of transmissions to physical transfer is so compelling that consumer expectations about transferability of downloaded material have become deeply-rooted. It is said that failure of the law to live up to this expectation will damage commerce in such material. We are aware of no empirical (or even anecdotal) evidence for this proposition, so any assessment of claims concerning consumer expectations and their effect on e-commerce is necessarily conjectural. However, it can be said with confidence that e-commerce and the market for works online has grown quite substantially despite the absence of an expanded section 109. In addition, judging from consumer trends today, there appears to be little or no evidence of desire on the part of consumers to engage in the kind of conduct — transmission and simultaneous deletion — that would be covered in a digital first sale doctrine.

in any event, these issues of consumer expectations and the growth of electronic commerce are precisely what should be left to the marketplace to determine. Straight-jacketing copyright owners into a distribution model that developed around a different technology at a different time is a formula for stifling innovative, market-driven approaches to meeting consumer demand for digital content. If, as has been asserted, the current tenns by which copyright owners offer their products are unacceptable to consumers, consumers will stop buying them under those terms and competitors will step into the breach. Such self-correcting market forces should be given an opportunity to address these types of concerns before Congress alters the balance of rights and exceptions in the Copyright Act.

ii. Further consideration of ways to address library issues related to the first sale doctrine

The fact that we did not recommend adopting a "digital first sale" provision at this time does not mean that the issues raised by libraries are not potentially valid concerns. Similarly, our conclusion that certain issues are beyond the scope of the present study does not reflect our judgment on the merits of those issues.

The library community has raised concerns about how the current marketing of works in digital form affects libraries with regard to five specifically enumerated categories: interlibrary loans, off-site accessibility, archiving/preservation, availability of works, and use of donated copies.[312] In each case, the concern is that licensing terms for use of the works will effectively prohibit the desired activity.[313]

Concerning interlibrary lending, library associations suggest that the Copyright Act should reaffirm and strengthen rules on interlibrary loan especially for acquired digital works."[314] They state that licenses often prohibit the loaning of works in digital form. As mentioned elsewhere, the issue of licenses is beyond the scope of this study.

It should be noted that many interlibrary loans are not in fact loans – the temporary lending of a particular copy of a work – but delivery of copies. The "lending" institution

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[312] C-Library Ass'ns, at 11-19.

[313] *Id.*

[314] *Id.* at 11-13, 23.

reproduces the copyrighted work and sends the reproduction to the "borrowing" library. This copy is given by the borrowing library to its patron, who becomes the owner of that copy. Clearly this activity of libraries is outside of the scope of section 109. As to the library patron, to the extent that such a reproduction and distribution is authorized by section 108,[315] the copy becomes his property and is therefore subject to section 109.

Library concerns about offsite accessibility relate chiefly to licenses that limit access to a particular work to a specific location (e.g., a single building or computer). This means that such works are not available for use offsite, including in a classroom. Libraries seek the ability to make all works in their collections available for classroom use.[316] These are contract issues that are not within the mandate for this study.

Library associations raised a related concern about licensing terms which limit the number of users of a work at any given time, the hours of the day during which works may be used, or other similar limitations.[317] Less restrictive licenses are often available, but at a higher price. As with restrictions on offsite availability of works, these limitations have the effect of reducing the general availability of those works that are subject to the limitations. The library associations believe that these restrictions create substantial burdens to research.[318] This is also a

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[315] Section 108 was updated in the Digital Millennium Copyright Act of 1998; as updated, section 108 makes it clear that digital copies may not be given to patrons. Copies given to patrons must be in analog form – e.g., photocopies.

[316] C-Library Ass'ns, at 11-13, 23.

[317] *Id.* at 17.

[318] *Id.*

contract issue that is not within the mandate of the study. However, we do note that the difficulty identified by the library associations is not new, and is not unique to the digital world. Libraries have always had make difficult trade-offs between greater availability of particular works (through the purchase of more copies) and other priorities.

Concern was also raised about works that libraries can only offer by means of online access. The terms of use of a work that is accessed in this way are typically set forth in a subscription agreement. Online access is achieved by loading the work into the RAM of a computer while it is being accessed; it does not involve the making of a permanent copy. Here there is no section 109 issue – at the end of the online session the library owns no physical copy that can be transferred.

Preservation and archiving are identified as potential problems because many licenses prohibit copying for such purposes (or for any purpose) and because prohibitions on copying are enforced by technological means.[319] The library associations propose creating a national system of digital repositories, where specific libraries or institutions would be designated as custodians of specific parts of our nation's digital history and assisted in their efforts to preserve these works.[320] While these issues are beyond the scope of this study, we acknowledge that they are legitimate concerns that have been recognized as such.[321] In fact, they are being addressed. For

[319] C-Library Ass'ns, at 14.

[320] *Id.* at 23.

[321] Committee on Intellectual Property Rights and the Emerging Information Infrastructure, The Digital Dilemma 209-10 (2000).

example, the Librarian of Congress, James H. Billington, has appointed a national advisory committee to assist the Library of Congress in the development of a National Digital Information Infrastructure and Preservation Program to ensure the long-term availability of digital materials. That committee held its first meeting on May 1, 2001.

The focus of library concerns regarding donated copies is their ability to use donated CD-ROMs. Libraries are not able to use CD-ROMs donated to them because the donors are not owners of the CD-ROMs, only licensees, and thus lack the legal authority to transfer the copy of the work they possess.[322] Since the license agreement prevents the transfer, the issue is beyond the scope of this study.

Most of these issues arise from terms and conditions of use, and costs of license agreements. One arises because, when the library has only online access to the work, it lacks a physical copy of the copyrighted work that can be transferred.[323] These issues arise from existing business models and are therefore subject to market forces. We are in the early stages of electronic commerce. We hope and expect that the marketplace will respond to the various concerns of customers in the library community. However, these issues may require further consideration at some point in the future. Libraries serve a vital function in society, and we will continue to work with the library and publishing communities on ways to ensure the continuation of library functions that are critical to our national interest.

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322 C-Library Ass'ns. at 18-19.

323 See Ginsburg supra note 300, at 10.

2. The Legal Status of Temporary Copies

a. *Relevance to* this *Report*

As was discussed above, this Report is a direct outgrowth of Congressional concern at the time of the enactment of the DMCA about the copyright treatment of digital reproduction and transmission.[324] Specifically, the scope of the study and Report mandated by Congress in section 104 of the DMCA can be traced to some of the proposed amendments to sections 109 and 117 of title 17 made in the Boucher-Campbell bill.[325] One of these proposals was an amendment to section 117 that would allow temporary copies to be made if these copies were "incidental to the operation of a device in the course of the use of a work otherwise lawful under this title."[326] While this proposal was not adopted by Congress, section 117 was one of the provisions of title 17 that we were instructed to examine in this Report. The only context in which section 117 arose in the Boucher-Campbell bill was with respect to incidental copying.

This Report necessarily requires consideration and evaluation of temporary incidental copies made in the course of use on a computer or computer network, such as the Internet. In addition to the congressional concerns leading to the creation of this Report, the comments and testimony received in the course of our study illustrate the importance of clarifying the lawful scope of temporary copies in the current market. In order to understand the issues raised by the transmission of digital works over the Internet, it is appropriate to clarify the current state of the

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[324] *See* discussion *supra*, at 18.

[325] H.R 3048, 105th Congress, 1st Session, November 13.1997. See discussion *supra*, at 15 & ff.

[326] *Id.* at Sec. 6(b)(1).

law on this issue. This section will discuss the origins of the section 117 exemption for temporary copies and examine its purpose in relation to new developments related to temporary buffer copies.

b. *RAM Reproductions as "Copies" under the Copyright Act*

i. Technical background

All instructions and data that are operated on by a computer are stored in integrated circuits known as RAM. Unlike flash memory, read-only memory (ROM)[327] and magnetic storage devices such as disk and tape drives, RAM is volatile: when power is switched off, all information stored in RAM is erased. Conversely, as long as the power remains on, information stored in RAM can be retrieved and reproduced unless it is overwritten by other information.

All of the familiar activities that one performs on a computer —e.g., execution of a computer program. retrieval and display of information, browsing the World-Wide Web — necessarily entail making reproductions in RAM. These reproductions generally are made automatically, and transparently to the user—i.e., without the user being aware that copies are being made. The copies usually persist for as long as the activity takes place?" For example, the instructions that comprise a computer program generally remain in RAM for as long as the

[327] This term includes all variants of ROM, such as programmable read-only memory (PROM). erasable programmable read-only memory (EPROM). electrically erasable programmable read-only memory (EEPROM) and so on.

[328] In many instances, as a technical matter, the information will remain in RAM even after it is no longer in use. For example, when a computer program terminates, the operating system takes note of the fact that the memory occupied by the program is now available for other use. The content of that memory, however, is unchanged until it is overwritten with new information, or the power is turned off.

program is running. Likewise, the data that express text and images remain in RAM for as long as the text and images are displayed. As the packets of binary information comprising works traverse computer networks, temporary copies (in RAM and on disk) are made as they move from point to point along the way from source to destination.

Although it is theoretically possible that information could be stored in RAM for such a short period of time that it could not be retrieved, displayed, copied or communicated, this is unlikely to happen in practice. A device that is capable of storing, but not retrieving, displaying, copying or communicating information would have no practical purpose, and there would be no engineering justification for making such a device.

The issue of the legal status of RAM reproductions has arisen in this study almost exclusively in the particular factual context of streaming audio.[329] In order to render[330] the packets of audio information in an audio "stream" smoothly, the rendering software maintains a "buffer" – a portion of memory set aside to store audio information until it has been rendered. Inconsistencies in the rate at which audio packets are delivered over the Internet are thus evened out, so that the software can render the information at a constant rate. As information is rendered, it is discarded and new information is put into the buffer as it is received.

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[329] "Streaming audio" is the digital transmission of sound – often sound recordings of musical compositions – as a series of packets of audio information that are reassembled and rendered on the recipient's computer as they are received.

[330] In this context "render" means the process by which the digital representation of sounds and/or images is converted back into those sounds and/or images.

ii. Statutory analysis

Section 106(1) of the Copyright Act grants a copyright owner the exclusive right "to reproduce the copyrighted work in copies" and to authorize others to do so. Reproducing a work in RAM therefore falls within the scope of a copyright owner's exclusive reproduction right if it results in a "copy."

The starting point for determining whether reproductions in RAM are copies for copyright purposes is the text of the statute. "Copies" are defined in the Copyright Act as:

> material objects, other than phonorecords, in which a work is fixed by any method now known or later developed, and from which the work can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device.[331]

There is no question that RAM chips are "material objects." They are electronic integrated circuits, etched and deposited on a wafer of semiconducting material (such as silicon), which are capable of storing binary information in the form of electrical impulses. A work stored in RAM can be "perceived, reproduced, or otherwise communicated" with the aid of a computer. The key issue, therefore, is whether a reproduction in RAM is "fixed."

The Copyright Act defines "fixed" as follows:

> A work is "fixed" in a tangible medium of expression when its embodiment in a copy or phonorecord . . . is sufficiently permanent or stable to permit it to be perceived, reproduced, or otherwise communicated for a period of more than transitory duration.[332]

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[331] 17 U.S.C. § 101.

[332] *Id.*

As to the element of duration, the definition of "fixed" does not require that a copy be permanent or that it last for any specified period of time.[333] For a work to be fixed, is must only be "*sufficiently* permanent or *stable* to permit it to be perceived [or] reproduced . . . for a period of more than transitory duration."[334] Although the embodiment of a work in RAM is not permanent, since loss of power results in erasure of the work, typically it is "sufficiently . . . stable" to be "perceived [or] reproduced" for an indefinite period of time — i.e., for as long as the power remains on and the memory locations storing the work are not overwritten with other information. As one court has observed, the conclusion that RAM copies are fixed

> is actually confirmed rather than refuted by [the] argument that the RAM representation of the program is not "fixed" because it disappears from RAM the instant the computer is turned off. Thus one need only imagine a scenario where the computer, with the program loaded into RAM, is left on for extended periods of time, say months or years, or indeed left on for the life of the computer. In this event, the RAM version of the program is surely not ephemeral or transient; it is, instead, essentially permanent and thus plainly sufficiently fixed to constitute a copy under the Act.[335]

Based on the definitional language in the Copyright Act, RAM reproductions are generally "fixed" and thus constitute "copies" that are within the scope of the copyright owner's reproduction right. The definition of "fixed" leaves open the possibility, however, that certain RAM reproductions that exist for only a "period of . . . transitory duration" are not copies. The statute does not define "transitory duration" directly. Since permanence *is* not required for

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[333] *See Advanced Computer Services of Michigan, Inc. v. MAI Sys. Corp.*, 845 F. Supp. 356, 362-63 (E.D. Va. 1994).

[334] 17 U.S.C. § 101 (emphasis added).

[335] *Advanced Computer Services*, 845 F. Supp. at 363.

fixation, "transitory" must denote something shorter than "temporary." "Transitory" must also denote something less than "ephemeral," as that term is used in the Copyright Act, since the Act confirms that "ephemeral recordings" are fixed by providing a specific exemption for "ephemeral recordings" lasting up to six months.[336] Courts have not attempted to formulate a general rule defining how long a reproduction must endure to be "fixed," deciding instead on a case-by-case basis whether the particular reproduction at issue sufficed.[337]

Nonetheless, a general rule can be drawn from the language of the statute. In establishing the dividing line between those reproductions that *are* subject to the reproduction right and those that are not, we believe that Congress intended the copyright owner's exclusive right to extend to all reproductions from which economic value can be derived. The economic value derived from a reproduction lies in the ability to copy, perceive or communicate it. Unless a reproduction manifests itself so fleetingly that it cannot be copied, perceived or communicated, the making of that copy should fall within the scope of the copyright owner's exclusive rights. The dividing line, then, can be drawn between reproductions that exist for a sufficient period of time to be capable of being "perceived, reproduced, or otherwise communicated" and those that do not.[338]

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[336] 17 U.S.C. § 112.

[337] *See, e.g., MAI Sys. Corp. v. Peak Computer, Inc.*, 991 F.2d 511, 518 (9th Cir. 1993); *Advanced Computer Servs.*, 845 F. Supp. at 363.

[338] This view is consistent with the discussion of fixation in the legislative history of the Copyright Act. The legislative history is examined *infra* at 114-117.

It is also consistent with "a quite well-established position at the international level" that 'fixation means sufficient stability of form so that what is 'fixed' may be perceived, reproduced or otherwise communicated." Mihaly Ficsor. *Copyright for the Digital Era: The WIPO "Internet" Treaties*, 21 Colum./VLA J. L. and the Arts 197 (1997) ("Digital Era").

As a practical matter, as discussed above, this would cover the temporary copies that are made in RAM in the course of using works on computers and computer networks.

Drawing the line with reference to the ability to perceive, reproduce or otherwise communicate a work makes particular sense when one considers the manner in which one important category of digital works—computer programs—are utilized. Computer programs are exploited chiefly through exercise of the rights of reproduction and distribution. In order to utilize a program, it must be copied into RAM. To exercise the right to make that temporary copy in RAM is to realize the economic value of the program. That RAM copy need only exist long enough to communicate the instructions to the computer's processing unit in the proper sequence.

Exploitation of works on digital networks illustrates the same point. Digital networks permit a single disk copy of a work to meet the demands of many users by creating multiple RAM copies. These copies need exist only long enough to be perceived (e.g., displayed on the screen or played through speakers), reproduced or otherwise communicated (e.g., to a computer's processing unit) in order for their economic value to be realized. If the network is sufficiently reliable, users have no need to retain copies of the material. Commercial exploitation in a network environment can be said to be based on selling a right to perceive temporary reproductions of works.[339]

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[339] Other exclusive rights may be involved as well. A discussion of these additional rights is beyond the scope of this Report.

Apart from these policy considerations, attempting to draw a line based on duration may be impossible. The language of the Copyright Act rules out drawing the line between temporary and permanent copies, as discussed above. Even if this distinction were possible under the statute, the concept of permanence is not helpful in this context. Magnetic disks and tapes can be erased; printed works decompose over time, or can be destroyed deliberately or accidentally. Separating some temporary copies from others based on their duration poses similar difficulties. How temporary is temporary? Hours? Minutes? Seconds? Nanoseconds? The line would be difficult to draw, both in theory and as a matter of proof in litigation.

The conclusion that reproductions in RAM are "copies" is reinforced by the existence of another provision of the Copyright Act: section 117. The current version of section 117 was added in 1980 at the recommendation of CONTU. In relevant part, it provides:

> Notwithstanding the provisions of section 106, it is not an infringement for the owner of a copy of a computer program to make or authorize the making of another copy or adaptation of that computer program provided:
>
> (1) that such a new copy or adaptation is created as an essential step in the utilization of the computer program in conjunction with a machine and that it is used in no other manner. . . .[340]

The "new copy" that is "created as an essential step in the utilization of the computer program in conjunction with a machine" is the copy made in RAM when the program is executed. No such exemption would have been necessary if reproductions in RAM could not be copies. It would be

[340] 17 U.S.C. § 117.

unreasonable to interpret the definitions in section 101 in such a way that it would render section 117 superfluous.[341]

iii. Legislative history

The legislative history of the Copyright Act confirms that certain temporary reproductions implicate the reproduction right, but is ambiguous as to the precise dividing line between temporary reproductions that are considered "fixed" and those that are not. In discussing the definition of "fixed," the House Report that accompanied the Copyright Act of 1976 states that copies that exist only "momentarily" in RAM may not satisfy the fixation requirement.[342] According to the 1976 House Report, "the definition of 'fixation' would exclude from the concept purely evanescent or transient reproductions such as those projected briefly on a screen, shown electronically on a television or other cathode ray tube, or captured momentarily in the 'memory' of a computer."[343]

One interpretation of that statement is that Congress viewed all reproductions in the "memory" of a computer to exist only momentarily, and thus as incapable of meeting the fixation requirement.[344] If so, then the legislative history was based on an imperfect grasp of the relevant technology. As discussed above, reproductions in RAM can exist for long periods of time —i.e.,

[341] *See, e.g., Pennsylvania Dept. of Public Welfare v. Davenport,* 495 U.S. 552, 562 (1990) ("Our cases express a deep reluctance to interpret a statutory provision so as to render superfluous other provisions in the same enactment.").

[342] 1976 House Report, *supra* note 40, at 53.

[343] *Id.*

[344] *See* discussion *infra,* at 120-123.

for as long as the power remains on and no other information is stored in the memory locations occupied by the reproduction. In addition, RAM reproductions are qualitatively different from the other examples cited (projection on a screen, or display on a television or cathode ray tube). RAM reproductions are stored or embodied in the RAM chip. A projection on a screen or a display on a television or cathode ray tube is not stored or embodied in the screen or TV or display tube.[345] In any event, the premise that all RAM reproductions exist only momentarily is incorrect, and cannot support a conclusion that all RAM reproductions are unfixed.[346]

Another possible interpretation of the statement in the House Report concerning computer memory is that it applies not to all RAM reproductions, but only to those "reproductions . . . captured *momentarily*" in "computer memory."[347] This interpretation implies that any reproduction in computer memory that exists more than "momentarily" is fixed. This interpretation adheres more closely to the statutory text, since, as discussed above, the statute on its face contemplates that at least some temporary copies satisfy the fixation requirement?"

Consequently, it appears to be the better interpretation of the language in the 1976 House Report.

[345] See *infra*, note 369.

[346] *Accord* CONTU Report, supra note 61, at 22 n.111 ("Insofar as a contrary conclusion [that works in computer storage arc not fixed] is suggested in one report accompanying the new law. this should be regarded as incorrect and should not be followed since legislative history need not be perused in the construction of an unambiguous statute").

[347] 1976 House Report, *supra* note 22. at 53 (emphasis added).

[348] See discussion *supra*, at 109–1 14.

Stating that copies which exist only "momentarily" are not fixed (and copies that exist longer are fixed) still begs the question of precisely which RAM copies exist for too short a *time* to satisfy the fixation requirement, and which do not. The best guide in the legislative history for determining where Congress intended to draw the line between fixed and unfixed reproductions is elsewhere in the 1976 House Report, where it is stated that "fixation is sufficient if the work 'can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device.'"[349] This statement supports the distinction drawn above between RAM copies that exist long enough to be perceived, reproduced or otherwise communicated and those that do not.

The legislative history of a subsequent amendment to the Copyright Act also supports the conclusion that temporary copies in RAM may satisfy the fixation requirement. The current text of sections 117(a) and (b) was added in 1980 as part of a package of amendments recommended by CONTU. The House report accompanying the 1980 amendments did not explain the intent of the legislation, other than to implement CONTU's recommendations.[350] The CONTU Report sets forth its reasons for recommending the statutory additions, which Congress enacted with few changes?"

[349] 1976 House Report, *supra* note 35, at 52 (quoting 17 U.S.C. § 102(a)).

[350] Referring to the portion of the bill that added the section 101 definition of "computer program" and section 117, the House committee report stated only that it "embodie[d] the recommendations of the Commission on New Technological Uses of Copyrighted Works with respect to clarifying the law of copyright of computer programs." H.R. Rep. No. 1307 (Part 1), 96th Cong.. 2d Sess. 23 (1980).

[351] The status of the CONTU Report as legislative history is discussed supra, at 29.

CONTU clearly viewed reproductions in computer memory as "copies," implicating a copyright owner's exclusive rights under section 106.[352] In 1976 Congress considered the problems associated with computer uses of copyrighted works not to be sufficiently developed for a definitive legislative solution.[353] Congress enacted what was commonly referred to as a "moratorium" provision in section 117, which preserved the status quo on December 31, 1977 as to use of copyrighted works in conjunction with computers and similar information systems.[354] In recommending the repeal of that provision, CONTU stated:

> The 1976 Act, without change, makes it clear that the placement of any copyrighted work into a computer is the preparation of a copy and, therefore, a potential infringement of copyright. . . .
>
> Because the placement of a work into a computer is the preparation of a copy, the law should provide that persons in rightful possession of copies of programs be able to use them freely without fear of exposure to copyright liability. . . . One who rightfully possesses a copy of a program, therefore, should be provided with a legal right to copy it to that extent which will permit its use by that possessor. This would include the right to load it into a computer. . . .[355]

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[352] C O W Report, *supru* note 61, at 13. It is reasonable to assume that in 1978. when the CONTU Report was published. reference to "placement of a work into a computer" was understood to include reproduction in volatile memory. Although early generations of computers used non-volatile ferrite core memory, volatile solid-state memory was in wide use by the early 1970s.

[353] 1976 House Report, *supru* note 35. at 116.

[354] Pub. L. No. 94-553, 90 Stat. 2541 (1976); 1976 H o w Report, *supru* note 35, at 116. Former section 117 read as follows:

> Notwithstanding the provisions of sections 106 through 116 and 118, this title does not afford to the owner of copyright in a work any greater or lesser rights with respect to the use of the work in conjunction with automatic systems capable of storing, processing, retrieving, or transferring information, or in conjunction with any similar device. machine or process. than those afforded to works under the law. whether title 17 or the common law or statutes of a State, in effect on December 31, 1977. as held applicable and construed by a court in action brought under this title.

[355] CONTU Report, *supra* note 61, at 13.

iv. Judicial interpretation

Every court that has addressed the issue of reproductions in volatile RAM has expressly or impliedly found such reproductions to be copies within the scope of the reproduction right. We are aware of no cases that have reached the contrary conclusion.

The seminal case on the subject is ***MAI Sys. Corp. v. Peak Computer. Inc.***,[356] in which the defendant's loading of operating system and diagnostic software into computer memory in violation of a license agreement was held to be an infringement?" In reaching that conclusion, the Ninth Circuit examined the definitions in section 101 and found that "loading of copyrighted software into RAM creates a 'copy' of that software."[358] The court noted that, although it was aware of no prior cases holding that reproductions in RAM were copies, "it is generally accepted that the loading of software into a computer constitutes the creation of a copy under the Copyright Act."[359] After making note of evidence in the record that, once the software was loaded into RAM, the defendant was able to view the system error log in order to diagnose a problem with the computer, the court reasoned that this evidence demonstrated "that the representation created in the RAM is 'sufficiently permanent or stable to permit it to be perceived, reproduced, or otherwise communicated for a period of more than transitory

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[356] 991 F.2d 511 (9th Cir. 1993). *cert. dismissed,* 114 S. Ct. 671 (1994).

[357] *MAI v. Peak* has generated controversy on two fronts. As discussed *infra,* at 120, the holding regarding RAM copying has been consistently upheld by later courts, but criticized by a number of academic commentators. In addition, the implications of the case for competition in the computer repair industry led in 1998 to a specific legislative exemption for certain temporary copies in RAM. *See* discussion *infra,* at 30.

[358] *Id.* at 518.

[359] *Id.* at 519.

duration.'"[360] Consequently, the court affirmed the district court's conclusion that "a 'copying' for purposes of copyright law occurs when a computer program is transferred from a permanent storage device to a computer's RAM."[361]

At least nine other courts have followed *MAI v. Peak* in holding RAM reproductions to be "copies," although not all have ultimately found the defendant to be liable for infringement.[362] Even before *MAI v. Peak*, the Fifth Circuit had stated that "the act of loading a program from a medium of storage into a computer's memory creates a copy of the program."[363] The factual context suggests that the court was referring to RAM. Several other cases have also held that

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[360] *Id.*

Id.

[362] *See Stenograph L.L.C. v. Bossard Assocs.*, 144 F.3d 96, 101-02 (D.C. Cir. 1998) (holding that "a RAM reproduction constitutes a copy"); *DSC Communications Corp. v. DGI Technologies, Inc.*, 81 F.3d 597, 600 (5th Cir. 1996) (citing *MAI v. Peak*, holding that copy is made when software is loaded into computer's RAM; defendant is not enjoined from making such copies, however, because it is likely to prevail on its defense of copyright misuse); *Triad Sys. Corp. v. Southeastern Express Co.*, 64 F.3d 1330, 1335 (9th Cir.), *cert. denied*, 116 S. Ct. 1015 (1995) (loading of software into RAM is "copying" for purposes of the Copyright Act); *Intellectual Reserve, Inc. v. Utah Lighthouse Ministry, Inc.*, 75 F. Supp. 2d 1290, 1294 (D. Utah 1999); *Wilcom Pty. Ltd. v. Endless Visions*, 1998 U.S. Dist. LEXIS 20583, *9 (E.D. Mich Dec. 2, 1998) ("a temporary copy of the program's object code in. . . RAM . . . is sufficiently 'fixed in a tangible medium of expression' to constitute an infringing copy under the Copyright Act"); *In re Independent Sew. Orgs. Antitrust Litigation*, 23 F. Supp. 2d 1242, 1245 (D. Kan. 1998) ("use (and hence reproduction into random access memory ('RAM')) of diagnostic software . . . was not authorized by [plaintiff] and hence constituted infringement"); *Marobie-FL. Inc. v. National Assoc. of Fire Equip. Dists.*, 983 F. Supp. 1167, 1176-78 (N.D. Ill. 1997) (citing *MAI v. Peak*, finding RAM copies to be fixed as long as they are capable of being perceived); *Religious Tech. Center v. Netcom On-line Comm.*. 907 F. Supp 1361, 1368 (N.D. Cal. 1995) ("In the present case, there is no question after MAI that 'copies' were created . . . ."; preliminary injunction denied, however, because plaintiff did not demonstrate a substantial likelihood of success on the merits); *In re Independent Serv. Orgs. Litigation*, 910 F. Supp. 1537, 1541 (D. Kan. 1995) ("We agree with the court in [*MAI v. Peak*]. that transferring a computer program from a storage device to a computer's RAM constitutes a copy for purposes of copyright law."); *Advanced Computer Sews. of Mich.. Inc. v. MAI System Corp.*, 845 F. Supp. 356.363 (E.D.Va. 1994) (where "a copyrighted program is loaded into RAM and maintained there for minutes or longer, the RAM representation of the program is sufficiently 'fixed' to constitute a 'copy' under the Act"). Set also, *Ohio v. Perry*, 41 U.S.P.Q.2d (BNA) 1989 (Ohio App. 1997) (following *MAI v. Peak* in concluding that state charge of unauthorized use of property stemming from the unauthorized posting of software on a computer bulletin board service was preempted by the Copyright Act because the defendant's acts constituted copyright infringement).

[363] *Vault Corp. v. Quaid Software Ltd.*, 847 F.2d 255, 260 (5th Cir. 1988).

loading a computer program into a computer entails making a copy, Without mentioning RAM specifically.[364]

v. Commentary

In contrast to the apparent unanimity among courts that have considered the issue of RAM copying, legal scholars are divided on the question – which may account for the characterization of *MAI v. Peak* by at least one commenter as "controversial."[365] Although some academics have expressed support for the conclusion that the reproduction right can embrace RAM copies,[366] much commentary on the subject has criticized the holding of *MAI v. Peak*.[367]

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[364] *See, e.g., Sega Enterprises Ltd. v. MAPHIA*, 948 F. Supp. 923, 931-32 (N.D. Cal. 1996)(following *MAI v. Peak*); *NLFC, Inc. v. Devcom Mid-America, Inc.*, 45 F.3d 231,235 (7th Cir. 1995) ("Neither party disputes that loading software into a computer constitutes the creation of a copy under the Copyright Act"; nonetheless, court affirms summary judgment for defendant because of plaintiffs failure to establish copying as a factual matter); *Roeslin v. District of Columbia*, 921 F. Supp. 793.800 (D.D.C. 1995)("The placement of a copyrighted program into a computer, or the loading of a copyrighted program into a computer (which occurs every time [one] uses the program). constitutes 'copying' the program for purposes of the Copyright Act."); *Tricom, Inc. v. Electronic Data Sys. Corp.*. 902 F. Supp. 741,745 (E.D. Mich 1995)(loading software onto mainframe computer constitutes copying under the copyright law); *Hubco Data Prods. Corp. v. Management Assistance, Inc.*, 219 U.S.P.Q. (BNA) 450, 456 (D. Idaho 1983)(statutory definition of "copy" "makes clear that the input of a work into a computer results in the making of a copy, and hence that such unauthorized input infringes the copyright owner's reproduction right").

[365] C-DFC. at 3.

[366] *See. e.g.*, 1 William F. Patty, Copyright Law and Practice 171(1994); David Nimmer, *Brains and Other Paraphernalia of the Digital Age*, 10 Harv. J. of Law & Tech 1, 10-11 (1996); Jane C. Ginsburg, *Putting Cars on the "Information Superhighway": Authors. Exploiters, and Copyright in Cyberspace*, 95 Colum L. Rev. 1466, 1475-77 (1995); I. Trotter Hardy, *Symposium: Copyright Owners' Rights and Users' Privileges on the Internet: Computer RAM "Copies": A Hit or a Myth? Historical Perspectives on Caching as a Microcosm of Current Copyright Concerns*, 22 Dayton L. Rev. 423, 427-28, 456-60 (1997).

[367] *See, e.g.*, Mark A. Lemley, *Symposium: Copyright Owners' Rights and Users' Privileges on the Internet: Dealing with Overlapping Copyrights on the Internet.* 22 Dayton L. Rev. 547, 550-5 1 (1997); James Boyle. *Intellectual Property Policy Online: A Young Person's Guide*, 10 Harv. J. Law and Tech. 47.88-94 (1996); Fred H. Cate, *The Technological Transformation of Copyright Law*, 81 *Iowa* L. Rev. 1395. 1452-53; Niva Elkin-Koren, *Cyberlaw and Social Change: A Democratic Approach to Copyright Law in Cyberspace*, 14 Cardozo *Arts &* Ent. L.J. 215, 269-74 (1996); Pamela Samuelson, *Legally Speaking: The NII Intellectual Property Report.* Communications of the ACM, Dec. 1994, at 21.22 *("Legally Speaking")*; Jessica Litman, *The Herbert Tenzer Memorial Conference: Copyright in the Twenty-First Century: The Exclusive Right to Read*, 13 Cardozo Arts & Ent. L.J. 29, 42-43 (1994).

Just as webcasters appear to be facing demands for royalty payments for incidental exercise of the reproduction right in the course of licensed public performances, it appears that companies that sell digital downloads of music under either voluntary licenses from music publishers or the section 115 compulsory license, and voluntary licenses from record companies, are facing demands for public performance royalties for a technical "performance" of the underlying musical work that allegedly occurs in the course of transmitting it from the vendor's server to the consumer's PC.[440]

As with the issue of buffer copies made in the course of streaming, this appears to be an issue driven as much by the structure of the administration of copyright rights in the music industry as by technology. The issue simply would not seem to arise in other industries where the public performance and reproduction rights are exercised by the same entity.

We view this issue as the mirror image of the question regarding buffer copies. We recognize that the proposition that a digital download constitutes a public performance even when no contemporaneous performance takes place is an unsettled point of law that is subject to debate. However, to the extent that such a download can be considered a public performance, the performance is merely a technical by-product of the transmission process that has no value separate from the value of the download. If it is a public performance, then, we believe that arguments concerning fair use and the making of buffer copies apply to that performance.[441] In

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[440] T-BMI, Berenson, at 163-65.

[441] See discussion of the application of fair use to buffer copies, *supra*, at 133-141.

any case, for the reasons articulated above, it is our view that no liability should result under U.S. law from a technical "performance" that takes place in the course of a download.

3. Scope of Archival Exemption

Currently the archival exemption under section 117(a)(2) is limited to computer programs. This section allows the owner of a copy of a computer program to make or authorize the making of an additional copy of the program "for archival purposes," provided that "all archival copies are destroyed in the event that continued possession of the computer program should cease to be rightful."[442] A number of arguments were advanced in the course of the study for an expansion of this archival exception in order to cover the kind of routine backups that are performed on computers and to allow consumers to archive material in digital format other than computer programs. The arguments for and against such an expansion are discussed below.

a. *Arguments in Favor of Expanding the Archival Exemption*

i. General vulnerability of content in digital form

Commenters asserted that consumers need to back up works in digital form because they are vulnerable. CONTU recommended that Congress create an exemption to permit archival (backup) copies of computer programs because they are vulnerable to "destruction or damage by mechanical or electrical failure."[443] This vulnerability stems not fiom the fact that they are computer programs, but because they are stored in digital form. The rationale given by CONTU

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[442] 17 U.S.C. § 117(a)(2).

[443] CONTU Report, *supra* note 61 at 13.

for adopting an archival exemption for computer programs would apply equally to any work stored in digital format.[444]

It would be perfectly consistent with CONTU's recommendations and Congress' enactment of section 117 to extend the archival exemption to protect against technical vulnerabilities that afflict the present day use of digital files. The digital media collection on a hard drive is also vulnerable to technical failure such as hard disk crashes, virus infection, or file corruption.

ii. Mismatch between section 117 and current archival practices

Evidence has been presented noting that the archival exemption under section 117 does not permit the practices and procedures most people follow for backing up data on a computer hard drive. The commenters stated that an amendment to section 117 would be necessary for it to reflect the reality of how many computer users (and most business users) actually back up information.

Section 117 appears to have been written to address a particular style of archiving: the making of a copy of an individual program at the time the consumer obtains it. However, we were told that most businesses, and many individuals, perform periodic backups of everything on

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[444] It would have been well within CONTU's mandate (to make recommendations concerning "the reproduction and use of copyrighted works of authorship. . . . in conjunction with automatic systems capable of storing, processing, retrieving, and transferring information") to have proposed an archival exemption applicable to all works in digital form. CONTU Report, *supra* note 61, at 4. It did not do so, for reasons that were not articulated in the Report.

their disk (and not just one backup copy upon purchase of the computer program). This backup copy includes all installed computer programs, together with any related data files, various configuration files, and all of the user's own data, including any copyrighted works that have been downloaded. Section I 17 does not permit the copying of anything other than the computer programs.[445]

Section 117 requires the destruction of any archived copy once possession of the program ceases to be rightful. Possession – or at least use – of a program typically ceases to be rightful once the user acquires an upgraded version.[446] A literal reading of section 117 would require the user to go through all of the backup tapes, CD-Rs and other archival media, identify each of the files that constitute the earlier version of the computer program, and attempt to delete them. This is neither practical nor reasonable.

Based on the evidence presented during the course of preparing this Report, there is a fundamental mismatch between accepted, prudent practice among most system administrators and other users, on one hand, and section 117 on the other. As a consequence, few adhere to the letter of the law.

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[445] It was suggested by one commenter that even data files associated with a computer program could not be archived under section 117. WST-Hollaar.

[446] T-Hollaar, at 94, 150. For example, the Symantec License and Warranty for Norton SystemWorks™ provides that "YOU MAY NOT: ... use a previous version or copy of the Software after you have received a disk replacement set or an *upgraded* version as a replacement of the prior version, ...".

b. ***Arguments Against Expanding the Archival Exemption***

i. Lack of demonstrated harm

While the mismatch between section 117 and sound backup practices is indisputable, nobody was able to identify any instance where a consumer has suffered any harm as a result of the limited scope of the archival exemption. There are two principal ways that consumers could be harmed: by refraining, to their detriment, from activities because they do not fall within the scope of the exemption; and by being subject to legal claims from copyright owners for conduct that falls outside the scope of the exemption. Neither appears to be occurring.

It was pointed out several times during the course of this study that the backup copies that consumers make from their hard drives generally embody all files, including digital downloads. If this activity is so commonplace, it does not appear that consumers are risking their investment in digital media to conform their conduct to section 117. Nor has anyone provided any evidence that any consumer has ever faced litigation, or even the threat of litigation, for making a backup copy of a hard drive containing material that fell outside the scope of the archival exception under section 117. To the contrary, evidence was presented that consumers who back up their hard drives generally do so outside the parameters of section 117 with no repercussions whatsoever.

ii. Justification for section 117(a)(2) has diminished

The need to make backup copies of computer programs has diminished. It was pointed out in the comments that today section 117(a)(2) has little, if any, utility. Almost all the software sold in the United States is sold on CD-ROM.[447] The CD-ROM serves as the backup copy once a computer program is loaded from the CD-ROM to one's computer. CD-ROMs have an estimated failure rate of significantly less than 1%.

It has been argued that there would seem to be little point to expanding section 117(a)(2) to other copyrighted works when current law does not appear to be causing any real-world problems and the justification for the provision may no longer exist. While this may be the case today, we acknowledge that the sale of computer software as digital downloads is on the rise, and that may increase the need for an archival exemption.

iii. Bad faith use of the section 117 defense

It was brought to our attention during the course of this study that section 117 is being used by some members of the public to justify conduct that it does not permit because of the public's misunderstanding of the purpose of the section. We were told that persons engaged in software and content piracy are also using section 117 to justify their activities. For example, one of the commenters noted that people auction off their so-called backup copies of their computer software or make pirate software available on websites, ftp sites or chat rooms under the guise of the section 117 back-up copy exception.[448]

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[447] According to PC Data, in 1999, ninety-seven percent of all the software sold in the United States was sold on CD-ROM and in 2000, ninety-eight percent of all software was sold on CD-ROM. R-SIIA, at 9.

[448] C-SIIA, at 4.

c. ***Recommendations***

We recommend that Congress amend the copyright law in one of the two ways that we outline below. We acknowledge that persuasive arguments were presented on both sides of the question whether to expand the archival copy exemption that is currently in section 117(a)(2). On balance, after examining those arguments and taking into consideration the additional concerns that we discuss below, we conclude that a statutory change is desirable.

In support of a recommendation to revise the archival exemption, it has been demonstrated to our satisfaction that there is a fundamental mismatch between section 117 and current archival practices. Those practices – to which copyright owners have not objected – do not harm right holders, are necessary for consumers to protect their investment in digital materials, and should be permitted to continue.

In support of making no change to the scope of the exemption, there has been a complete absence of any demonstrated harm to the prospective beneficiaries of an expanded archival exemption.[449] Any dramatic expansion of a fairly modest copyright exemption carries with it the risk of causing unintended consequences. Moreover, we believe that a strong case can be made that most common archival activities by computer users[450] would qualify as fair use.

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[449] This factor is an element that distinguishes the archival exemption issue from the buffer copy issue discussed *supra*.

[450] We are assuming for purposes of this fair use analysis that the activity consists of backing up all or a portion of the contents of a hard drive on a removable medium for retention against the possibility of accidental destruction of that material *and for no other purpose*. Of course, this analysis would not apply to any infringing material on a hard drive.

The purpose of the use – backing up the material on a computer's hard drive – is merely to safeguard lawfully-obtained copies against accidental destruction. Although the use is not transformative, it probably would not be considered commercial either.[451] The use does not supplant the original because it does not entail a separate exploitation of the work – or any exploitation unless that original copy is damaged or destroyed. As with time-shifting, backing up is "a legitimate, essentially non-exploitative purpose." This factor appears to favor the user.

The second factor – nature of the work – would appear to favor copyright owners since many of the works being copied are clearly very creative in nature, and are thus subject to a more limited scope of fair use than informational works.[452] But this by no means precludes the conclusion that making backup copies is a fair use.[453]

The third factor – the amount and substantiality of the portion used – might also appear to weigh against a finding of fair use since the entire work is copied.[454] However, this too does not preclude a finding of fair use.[455] Here, since the purpose of the activity being engaged in is to protect one's legally obtained copy through archiving, copying the entire work is necessary.

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[451] *See Campbell*, 510 U.S. at 579 (discussing transformative use); *id.* at 584-85 (discussing commercial use).

[452] *Id.* at 586; *Diamond*, 745 F.2d 142, at 148 (2d Cir. 1984).

[453] For example, copying of entire motion pictures for time-shifting purposes was considered a fair use in *Sony*. Motion pictures generally fall at the creative end of the spectrum.

[454] *Infinity Broadcast Corp.*, 150 F.3d 104, at 109 (2d. Cir. 1998).

[455] Sony, 464 U.S. 417, 449-50 (1984).

The fourth factor – effect of the use on the market – weighs strongly in favor of fair use. The effect on the market for the copyrighted work will be nonexistent. The copies being made under this fair use analysis are being made for the sole purpose of safeguarding one's investment – a vulnerable investment due to susceptibility of digital media to accidental damage or destruction. The archival copies do not enter the market at any point and since they are copies of works for which the copyright owner has already been compensated, there is no harm to the owner in lost revenue. It is our conclusion that a strong case can be made that the use being made is fair.

If the analysis ended there, recommending no statutory change could be a viable option. Another element to consider, however, is the interplay between sections 107 and 109. It appears that the language of the Copyright Act could lead a court to conclude that, by operation of section 109, copies of works made lawfully under the fair use doctrine may be freely distributed.

Section 109 permits "the owner of a particular copy or phonorecord lawfully made" under title 17 to distribute that copy without the copyright owner's permission.[456] To the extent that section 107 permits a user to make backup copies of works stored on a hard drive, those backup copies are lawfully made and the user owns them. Section 109, on its face, appears to permit the

[456] 17 U.S.C. § 109(a).

user, as the owner of a lawfully made backup copy, to "sell or otherwise dispose of the possession" of that backup copy.[457]

Authority is unclear over the application of the first sale doctrine to lawfully made copies that have not been distributed with the copyright owner's consent. Section 109 is commonly understood to codify the "first sale doctrine," which implies that an actual sale, or at least an authorized distribution, must occur before the doctrine applies. However, the statutory text only requires that the copy be lawfully made, and makes no reference to a prior authorized sale or other distribution.[458]

The legislative history of section 109 can be read to support both views. In one sentence, the 1976 House Report suggests that an actual first sale is required to trigger section 109, which it asserts "restates and confirms the principle that, where the copyright owner has transferred ownership of a particular copy or phonorecord of a work, the person to whom the copy or phonorecord is transferred is entitled to dispose of it by sale, rentai, or any other means . . . ."[459] But this position is undercut by a passage on the same page, which asserts that "the disposition of a phonorecord legally made under the compulsory licensing provisions of Section 115 would not

[457] *Id.* Backup copies made pursuant to § 117(a)(2), though "lawfully made," are subject to the limitations on distribution contained in § 117(b) and the requirement in § 117(a)(2) that they be destroyed once possession of the original is no longer rightful. Since § 117 is both the more specific and the later enacted provision, these limitations would prevail over the general language of § 109(a) under basic canons of statutory interpretation.

[458] 17 U.S.C. § 109(a).

[459] 1976 H o w Report, *supra* note 40, at 79 (1976).

outside the scope of Section 109(a).[460] A leading copyright treatise concludes that "on balance, it would seem that the literal text of Section 109(a) should be followed, so that its immunity may be claimed by any 'owner of a particular copy or phonorecord lawfully made,' and not just by those who acquired such ownership via a prior transfer from the copyright owner."[461]

Given our view that, in the typical situation[462] the making of backup copies is probably a fair use, we see a [illegible] to copyright owners under current law that those backup copies could then be distributed without legal consequence. We believe that outcome would be fundamentally unfair[463] and notwithstanding the ambiguity of the 1976 House Report on this point, contrary to congressional intent. Nonetheless, we cannot overlook the possibility that a court would hold this way. When added into the balance, this element tips the scale in favor of statutory change.

We therefore recommend that Congress either (1) amend section 109(a) to ensure that fair use copies are not subject to the first sale doctrine; or (2) create a new archival exemption that provides expressly that backup copies may not be distributed. We express no preference as between the two options, and note that they are not mutually exclusive.

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[460] *Id.*

[461] Nimmer, *supra* note 21, at § 8.12[B][3][c].

[462] *See supra*, note 450.

[463] Apart from the obvious detrimental effect this outcome would have on the copyright owner's market, we note that the initial determination of fair use that permitted the making of the copy may have been premised on the fact that the copy was not made for distribution. *See infra*, note 468.

The first option would entail amending section 109(a) to state that only copies that have been lawfully made ***and lawfully distributed*** are subject to the first sale doctrine. We believe that this change would be consistent with what Congress intended in section 109.

As noted above, the text of section 109 does not refer to any previous transfer of a lawfully owned copy (although the condition that the person be an owner could be argued to presuppose a sale or other transfer of ownership from the copyright owner) and the 1976 House Report is ambiguous on the question whether a first sale must occur to trigger the application of section 109 to a particular copy. Section 109 was intended by Congress to "restate[] and confirm[]" a principle that had been "established by the court decisions and section 27" of the 1909 law. Section 27 refers not to "lawful copies" but to copies "the possession of which has been lawfully obtained." This language arguably requires a lawful sale or other distribution (otherwise the copy would be lawfully "made" not lawfully "obtained"q).[464] The seminal court decision on first sale, *Bobbs-Merrill Co. v. Straus*,[465] went even further, holding that the copyright owner parted with all right to control sale of a copy after it "had parted with the title to one who had acquired full dominion over it and had given a satisfactory price . . . ."[466] Given this chronology of the development of the first sale doctrine, it seems very unlikely that Congress intended a radical departure from the requirement of a "first sale" or other authorized distribution by the copyright owner. A likelier explanation for the particular wording in the statute is that it

[464] *See Platt & Munk Co. v. Republic Graphics, Inc.*, 513 F.2d 847 (2d Cir. 1963).

[465] 210 U.S. 339 (1908). The case is discussed *supra*, at 20.

[466] 210 U.S. at 350.

was drafted to avoid any potential conflict with the ability of a compulsory licensee's, or subsequent purchaser's, ability to sell phonorecords made under the section 115 compulsory license "to make and distribute phonorecords" of nondramatic musical works.[467]

We note that this proposed change to section 109 would not preclude the distribution of copies made pursuant to section 107 in all cases, since (like all of the exclusive rights in section 106) the distribution right is subject to the fair use doctrine. It would, however, require that a separate fair use analysis be applied to the distribution of that particular copy. The fair use copy could be transferred only in those cases where the distribution itself qualified as a fair use.[468]

The second option entails creating a new exemption for making backups of lawful copies of material in digital form, and amending section 117 to delete references to archival
The new exemption should follow the general contours of section 117(a)(2) and (b), and include the following elements: It should permit the making of one or more backup copies of a work.

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[467] 1976 House Report, *supra* note 40, at 79 ("[A]ny resale of an illegally 'pirated' phonorecord would be an infringement, but the disposition of a phonorecord legally made under the compulsory licensing provisions of section 115 would not."). Our proposal would also meet this concern since a phonorecord that is manufactured and sold under the section 115 license would be both lawfully made and lawfully distributed.

[468] In some cases, the making of a copy may be a fair use in large part because the copy is not disseminated to third parties. For example, in *Sony*, the Supreme Court held that it was a fair use for a private citizen to record a television program off-the-air for purposes of "time-shifting," which the Court described as "the practice of recording a program to view it once at a later time. and thereafter erasing it" 464 U.S. at 423. The personal nature of that use was critical to the Court's analysis. See, *e.g.*, 464 U.S. at 449 ("the District Court's findings plainly establish that time-shifting for private home use must be characterized as a noncommercial, nonprofit activity"). The fact that the making of a personal copy for purposes of time-shifting (and with the anticipation of subsequent destruction of the copy) is fair use should not *make* it lawful subsequently to sell, rent or give that "lawfully made" copy to a third party.

[469] We recommend this approach in order to preserve section 117's present character as a computer program exemption and at the same time ensure that computer programs and other materials in digital form are subject to the same rules concerning the making of backup copies.

The copy from which the backup copies are made must be in digital form on a medium that is subject to accidental erasure, damage or destruction in the ordinary course of its use. It should stipulate that the copies may be made and used solely for archival purposes or for use in lieu of the original copy. It should also specify that, notwithstanding the provisions of section 109, the archival copy may not be transferred except as part of a lawful transfer of all rights in the work. Finally, it should specify that the archival copies may not be used in any manner in the event that continued possession of the work ceases to be rightful.

Permitting the making of multiple copies is necessary because prudent backup practice requires it. For example, a typical approach to backing up would entail making both on-site and off-site copies of the entire contents of a hard drive on a regular basis, in addition to making incremental backups of just those files on the hard drive that have changed.

The requirement that the work be stored in digital form on a medium that is subject to accidental erasure, damage or destruction in the ordinary course of its use is intended to avoid claims like that faced by the court in *Atari, Inc. v. J S & A Group, Inc.*,[470] without unduly limiting the exemption to current technology.[471] The exemption would also not be limited, as the *Afari* court suggested, to damage or destruction by electrical or mechanical failure. Media that are subject to accidental erasure by human error would qualify as well. Digital media that are subject

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[470] 597 F. Supp. 5.9-10 (N.D. Ill. 1983) (rejecting assertion that making of 'backup' copies of a videogame embodied in ROM is permitted under section 1 17 because ROM is not vulnerable to "damage by mechanical or electrical failure," court holds device for copying videogames in ROM not to have substantial noninfringing uses under *Sony* analysis of contributory infringement)

[471] Currently, the exception would be limited primarily to backups made from copies on a hard drive, floppy disk. or other magnetic medium

to accidental destruction outside the ordinary course of use (e.g., by fire or other catastrophe), however, would not qualify, since there would no longer be a basis for treating them any differently from traditional hard-copy media for purposes of archiving.

The proposal that archival copies may be made and used solely for archival purposes or for use in lieu of the original copy is derived from section 117(a)(2). It has been modified in recognition of the fact that, in certain instances, the original copy is used as the backup, and the backup becomes the use copy.[472]

The requirement that archival copies not be transferable (except as part of a lawful transfer of all of the transferor's rights in the work) is derived fiom section 117(b). This takes care of the concern addressed above regarding the intersection of sections 107 and 109 in the context of backup copies.

The requirement that archival copies not be used in any manner in the event that continued possession of the work ceases to be rightful is a substitute for the requirement in section 117(a)(2) that any such backup copies be destroyed. Since backup copies frequently include many works on a single medium, and since erasure or destruction of individual files on such a medium is often impossible, the proposal would not require destruction. It would instead require that the archival copies not be used in any manner.

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[472] See Copyright Office, The Computer software Rental Amendments Act of 1990 The Nonprofit Library Lending Exemption to the "Rental Right" 77-78 (1994).

4. Contract Preemption

Several cornenters proposed that the Copyright Act should be amended to ensure that contractual provisions that override consumer privileges in the copyright law, or are otherwise unreasonable, are not enforceable![473] In essence, this is a request to amend section 301 of the Copyright Act, which governs the scope of federal preemption of state law (including state contract law). Section 301 states that

> all legal or equitable rights that are equivalent to any of the exclusive rights within the general scope of copyright as specified by section 106 in works of authorship that are fixed in a tangible medium of expression and come within the subject matter of copyright as specified by sections 102 and 103, . . . whether published or unpublished, are governed exclusively by this title. . . . [N]o person is entitled to any such right or equivalent right in any such work under the common law or statutes of any State.

There appears to be consensus among courts that enforcement of contracts is not prohibited as a general matter.[474] However, there is disagreement among courts respecting the degree to which the Copyright Act may preclude the enforcement of specific contractual provisions that would otherwise be enforceable under state law. At least one court has taken a nearly categorical approach to contract preemption, holding that rights created by contract are not "rights equivalent to any of the exclusive rights within the general scope of copyright."

> Rights "equivalent to copyright" are rights established by law – rights that restrict the options of persons who are strangers to the author. . . . A copyright is a right against the world. Contracts, by contrast, generally affect only their parties; strangers may do as they please, so contracts do not create "exclusive rights."[475]

[473] *See, e.g.*, C-DFC, at 4; T-Library Ass'ns, Neal, at 16; T-DiMA, Greenstein, at 239.

[474] *Architectronics, Inc. v. Control Systems, Inc.*, 935 F. Supp 425.441 (S.D.N.Y.1996); *see also Selby v. New Line Cinema Corp.*, 96 F. Supp. 2d 1053.1059 (C.D. Cal. 2000) (a majority of courts have found that breach of contract claims generally are not preempted).

[475] *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1454 (7th Cir. 1996).

Consequently, "a simple two-party contract . . . may be enforced."[476]

Other courts have found contract rights preempted to the extent that they essentially. restate one or more of the exclusive rights under section 106 of the Copyright Act (e.g., reproduction) with no "extra element."[477] No case, however, has applied preemption broadly enough to nullify contractual provisions that vary or ovemde exceptions and limitation in the Copyright Act.

Section 7 of the Boucher-Campbell bill would have amended section 301 to apply the broad scope of preemption of contract rights advocated by some of the commenters.[478] Unlike the proposals concerning the first sale doctrine and temporary copies, however, section 104 of the DMCA does not include any statutory reference that arguably brings this proposal within the scope of the Report. Consequently, we conclude that the issue of preemption of contractual provisions is outside the scope of the Report.

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[476] *Id.*

[477] *National Car Rental Sys. v. Computer Assocs. Int'l*, 991 F.2d 426,433 (8th Cir. 1993); *Frontline Test Equip. v. Greenleaf Software, Inc.*, 10 F. Supp. 2d 583.593 (W.D.Va. 1998).

[478]

SEC. 7. PREEMPTION.

Section 301(a) of title 17, United States Code, is amended by inserting the following at the end thereof:

"When a work is distributed to the public subject to non-negotiable license terms, such terms shall not be enforceable under the common law or statutes of any state to the extent that they–

"(1) limit the reproduction. adaptation, distribution, performance, or display, by means of transmission or otherwise, of material that is uncopyrightable under section 102(b) or otherwise; or

"(2) abrogate or restrict the limitations on exclusive rights specified in sections 107 through 114 and sections 117 and 118 of this title.".

H.R. 3048, 105th Cong., 1st Sess., § 7 *(1997)*.

We do note, however, that the issue is complex and of increasing practical importance, and as such, may be worthy of further consideration at some point in the future.[479] On one hand, copyright has long coexisted with contract law, providing a background of default provisions against which parties are generally free to order their own commercial dealings to suit their needs and the realities of the marketplace. On the other hand, movement at the state level toward resolving uncertainties that have existed about the enforceability of non-negotiated license agreements, coupled with legally-protected technological measures that give right holders the technical capability of imposing contractual provisions unilaterally, increases the likelihood that right holders, and not the copyright policies established by Congress, will determine the landscape of consumer privileges in the future. Although market forces may well prevent right holders from unreasonably limiting consumer privileges, it is possible that at some point in the future a case could be made for statutory change.

5. Miscellaneous Additional Issues Beyond the Scope of the Report

a. *Impact of Section 1201 on Fair Use and other Copyright Exceptions*

Several commenters expressed general opposition to the prohibitions on circumvention of technological protection measures contained in 17 U.S.C. § 1201, and noted their concerns about

[479] We note that in Australia the CLRC published an issues paper in June 2001 seeking information regarding the prevalence, effects and desirability of contracts that purport to override copyright exceptions granted under the *Copyright Act 1968*. In particular, the CLRC is investigating the extent to which such agreements occur in the online and offline environments and whether these agreements are and should be valid and enforceable. In all, the CLRC seeks views on nine issues. Details can be found on the CLRC website at www.law.gov.au/clrc.

the adverse impact that section 1201 may have on fair use and other copyright exceptions."[480] Given the express language of section 104, which requires an evaluation of the impact of, inter *alia*, section 1201 on the operation of two specific provisions of the copyright law – sections 109 and 117 – it seems unlikely that Congress intended this Report to delve into the general relationship between section 1201 and all of the other copyright exceptions and limitations. Moreover, the fact that Congress expressly directed us to evaluate this precise issue every three years as part of the rulemaking under section 1201(a)(1)(C), tends to support the conclusion that the impact of section 1201 on fair use and other copyright exceptions is outside the scope of this Report.

b. *Impact of Section 1201 on Users of DVDs*

Several sets of comments were focused on the litigation[481] concerning software tools for circumventing the CSS that is used to encrypt motion pictures distributed on DVD.[482] Some of these comments offered a point-by-point rebuttal of the plaintiffs' case; others expressed concern that section 1201 had an adverse effect on users of DVDs by limiting the playback of DVD movies to devices that are licensed by the consortium holding the rights to the CSS technology.

Only the courts have the authority to determine the outcome of the *Reimerdes* case; our mandate is to evaluate the impact of section 1201 on the operation of sections 109 and 117.

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[480] *See, e.g.*, C-NARM/VSDA, at 37. *See generally* C-Fischer; C-Darr; C-Jones; C-Klosowski; C-Love.

[481] *See supra*, note 89.

[482] *See, e.g.*, C-Arromdee; C-Thau and Taylor.

Although some of the comments tried to recast the DeCSS controversy as a first sale issue,[483] this effort reflected a misconception of the nature of the first sale doctrine.[484]

Apart from the foregoing issue, the general questions concerning the relationship between section 1201 and users of DVDs are outside the scope of this Report.

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[483] *See. e.g.*, C-LXNY, at I.

[484] See *supra*, at 14.

requesting to testify. his or her title and organization (if the submission is on behalf of an organization). mailing address, telephone number. telefax number (if any) and e-mail address. The message should also identify the document clearly as a request to testify. The one page summary of the intended testimony must be sent as a *MIME* attachment, and must be in a single file in either: (1) Microsoft Word Version 7.0 or earlier; (2) WordPerfect 7 or earlier; (3)Rich Text File (RTF) format; or (4) ASCII text file format.

2. If by regular mail or hand delivery: Send to Jesse M. Feder. Policy Planning Advisor, Office of Policy and International Affairs. U.S. Copyright Office. Copyright GC/I&R, P.O. Box *70400*. Southwest Station. Washington. DC 20024: and to Jeffrey E.M. Joyner. Senior Counsel, Office of Chief Counsel. National Telecommunications and Information Administration (NTIA), Room 4713. U.S. Department of Commerce. 14th Street and Constitution Avenue, *NW.*. Washington. DC 20230. Please include two copies of the one page summary of the intended testimony, each on a 3.5-inch write-protected diskette, labeled with the name of the person making the submission and, if applicable. his or her title and organization. Either the document itself or a cover letter must also identify the document clearly as a request to testify and include the name of the person making the submission. his or her title and organization (if the submission is on behalf of an organization), mailing address, telephone number, telefax number (if any) and e-mail address (if any). The document itself must be in a single file in either (1) Microsoft Word Version 7.0 or earlier: (2) WordPerfect Version 7 or earlier; (3) Rich Text File (RTF) format: or (4) ASCII text file format.

Background: On October 28, 1998, the DMCA was enacted into law (Pub. L. No. 105–304. 112 Stat. 2860). Section 104 of the DMCA directs the Register of Copyrights and the Assistant Secretary for Communications and Information of the Department of Commerce to submit to the Congress no later than 24 months after the date of enactment a report evaluating the effects of the amendments made by title 1 of the Act and the development of electronic commerce and associated technology on the operation of sections 109 and 117 of title 17. United States Code. and the relationship between existing and emerging technology and the operation of those sections.

The objective of title I of the DMCA was to revise U.S. law to comply with two World Intellectual Property Organization (WIPO) Treaties that were concluded in 1996 and to strengthen protection for copyrighted works in electronic formats. The DMCA establishes prohibitions on the act of circumventing technological measures that effectively control access to a work protected under the U.S. Copyright Act and the manufacture, importation, offering to the public, providing or otherwise trafficking in any technology. product, service, device, component or part thereof which is primarily designed or produced to circumvent a technological measure that effectively controls access to or unauthorized copying of a work protected by copyright. has only a limited commercially significant purpose or use other than circumvention of such measures, or is marketed for use in circumventing such measures. The DMCA also makes it illegal for a person to manufacture, import, offer to the public, provide. or otherwise traffic in any technology. product, service. device, component or part thereof which is primarily designed or produced to circumvent a technological measure that effectively protects a right of a copyright owner in a work protected by copyright, has only a limited commercially significant purpose or use other than circumvention of such measures, or is marketed for use in circumventing such measures. In addition the DMCA prohibits. among other actions. intentional removal or alteration of copyright management information and knowing addition of false copyright management information if these acts are done with intent to induce, enable, facilitate or conceal a copyright infringement. Each prohibition is subject to a number of statutory exceptions.

Section 109 of the Copyright Act, 17 U.S.C. 109, permits the owner of a particular copy or phonorecord lawfully made under title 17 to sell or otherwise dispose of possession of that copy or phonorecord without the authority of the copyright owner, notwithstanding the copyright owner's exclusive right of distribution under 17 U.S.C. 106(3). Commonly referred to as the "first sale doctrine." this provision permits *such* activities as the sale of used books. The first sale doctrine is subject to limitations that permit a copyright owner to prevent the unauthorized commercial rental of computer programs and sound recordings.

Section 117 of the Copyright Act. 17 U.S.C. 117. permits the owner of a copy of a computer program to make a copy or adaptation of the program for archival purposes or as an essential step in the utilization of the program in conjunction with a machine. In addition, pursuant to an amendment contained in title III of the DMCA. section 117 permits the owner or lessee of a machine to make a temporary copy of a computer program if such copy is made solely by virtue of the activation of a machine that lawfully contains an authorized copy of the computer program. for purposes of maintenance or repair of that machine.

Specific Questions: The principal purpose of the hearing is to inquire into points made in the written comments submitted in this proceeding, and not to raise new issues for the first time. Specifically. the public hearing will (and therefore the one page summary of intended testimony must) focus on the following questions:

- What are the policy justifications for or against an amendment to Section 109 to include digital transmissions, and what specific facts *can* you provide to support your position? What problems would an amendment to Section 109 address? What problems would an amendment to Section 109 not address? What problems would an amendment to Section 109 create? What problems would be averted by leaving this section unchanged? What would be the likely impact on authors and other copyright owners of an amendment to Section 109 modeled on Section 4 of H.R.3048, 105th Cong.. 1st Sess. (1997), and what is the basis for your assessment?
- Please explain in detail the impact an amendment to Section 109 to include digital transmissions would have on the following activities of libraries with respect to works in digital form: (1) Interlibrary lending: (2) use of works outside the physical confines of a library; (3) preservation and (4) receipt and use of donated materials. To what extent would an amendment to section 109 fail to have an impact on these activities? Please explain whether and how these activities should and can be accommodated by means other than amendment of Section 109?
- What are the policy justifications for or against an exemption to permit the making of temporary digital copies of works that *are* incidental to the operation of a device in the course of a lawful use of a work, and what specific facts *can* you provide to support how such an exemption could further or hinder electronic commerce and Internet growth? What problems would it address and what problems would a broad exemption not address? What problems would such an exemption create? How would your assessment differ if an exemption were limited to

temporary digital copies of works that are incidental to the operation of a device in the course of an authorized use of the work?

• What are the policy justifications for or against an expansion to the archival copy exception in section 117 to cover works other than computer programs, and what specific facts can you provide to support for your view? Would such an expansion of section 117 further or hinder electronic commerce and Internet growth? What problems would such a statutory change address and not address? What problems would such an expansion create?

• What are the policy justifications for or against expressly limiting the archival copy exception in section 117 to cover only those copies that are susceptible to destruction or damage by mechanical or electrical failure? What problems would such a statutory change address and not address? What problems would such a change create?

Marybeth Peters,

Register of Copyrights, United States Copyright Office.

Kathy D. Smith,

Chief Counsel, National Telecommunications and Information Administration.

[FR Doc. 00-27293 Filed 10-23-00; 8:45 am]

BILLING CODE 1410-30-P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

Notice of Solicitation of Public Interest

AGENCY: Executive Office of the President, Office of Management and Budget (OMB), Office of Federal Procurement Policy (OFPP).

ACTION: Notice of solicitation of public interest.

SUMMARY: OFPP is developing a new initiative to fundamentally examine the manner by which the Government develops and applies incentives to its contractual vehicles, and is seeking information and advice that would advance this effort.

COMMENTS DUE DATE: Comments and information regarding the proposed initiative must be received on or before December 26, 2000.

FOR FURTHER INFORMATION CONTACT: Comments and information should be sent to Stanley Kaufman, Deputy Associate Administrator, OMB, OFPP, 725 17th Street NW., Washington, DC 20503. He can be reached electronically at *skaufman@omb.eop.gov* or by phone at 202-395-6810.

SUPPLEMENTARY INFORMATION:

I. Background

Procurement reform initiatives such as the Federal Acquisition Streamlining Act of 1994, the Federal Acquisition Reform Act of 1996, the Information Technology Management Reform Act of 1996, and Performance-Based Service Contracting are significantly changing the way the Government acquires supplies and services, moving from a process-oriented, rules-based, risk avoidance culture to one emphasizing performance outcomes, business judgment, streamlined procedures, and risk management.

The rules-based culture constrained contracting officials' flexibility to serve as business advisors focusing on the overall business arrangements. While the cited acquisition reforms provided contracting officers increased flexibilities in negotiations and communication with contractors, research by the Army and studies by OFPP and industry found that innovative contracting methods are being used insufficiently, and effective incentives exist which are not being considered.

Consideration of incentives typically was limited to the fee portion of contracts to the detriment of other incentives that contractors would find more appropriate and meaningful, such as a consistent revenue flow and the promise of future business. In addition, incentives too often focused on the process of the work to be performed vs. the outcomes, thereby rewarding unnecessary and/or even counterproductive behavior. Furthermore, profit is not an effective incentive for non-profit entities such as universities and research laboratories. As a result, contractors often did not provide their best solutions and Government requirements were not fulfilled in as timely, quality-related, and cost-effective manner as possible.

II. The Project

OFPP is looking to develop a new contracting paradigm that will encourage acquisition officials to develop joint objectives with contractors and effectively incentivize both parties to create "win/win" business arrangements.

In pursuing this project, OFPP would like to pull together any experiences and literature regarding non-fee type incentives. Consultation with the private, non-profit, and public sectors is hereby sought. A review of current policy, regulatory and statutory guidance will be conducted to determine any barriers to achieving the project's objective and the need for any additional guidance to facilitate compliance.

Accordingly, OFPP is seeking ideas, recommendations, practices, lessons learned, etc. on what works in industry, the non-profit environment, and state and local governments. Such information tailored to specific industries (e.g., manufacturing, services, construction), subsets of industries (e.g., information technology, advisory and assistance services, environmental remediation), types of contractors (e.g., universities, small businesses) and types of endeavors (e.g., research and development) would be welcomed. We also would welcome any studies or literature that analyzes, assesses, or validates these practices, as well as information on relevant training courses and materials.

In examining this information and developing any policy initiative, we will consider approaches that would fundamentally restructure our contractual relationships to accommodate improving our business, arrangements, and so would welcome any appropriate recommendations as well as the identification of any impediments (legal, regulatory or policy). OFPP welcomes written comments and materials, and is willing to meet with individual companies, associations, and other organizations to hear their views and recommendations. OFPP is concurrently surveying Federal agencies to ascertain any ongoing innovative practices that could be used in this initiative.

We are also considering a public meeting to facilitate the exchange of information between the Government and general public to explore this issue if sufficient interest exists. Topics could include: developing alternative incentive strategies; providing recommendations; sharing best practices and lessons learned; reviewing existing literature; and identifying barriers and potential benefits and disadvantages for both agencies and contractors. Expressions of interest in such a meeting would be appreciated.

Kenneth J. Oscar,

Acting Deputy Administrator.

[FR Doc. 00-27117 Filed 10-23-00; 8:45 am]

BILLING CODE 3110-01-P

Appendix 5

Appendix 5

Joint Study on 17U.S.C. Sections 109 and 117
Required Pursuant to DMCA Section 104

Public Hearing
November 29,2000

Schedule of Witnesses

9:30-9:45 Introduction

Hon. Marybeth Peters, Register of Copyrights
Hon. Gregory L. Rohde, Assistant Secretary of Commerce for Communications and Information

9:45-11:00 Panel 1

James Neal and Rodney Peterson
American Association of Law Libraries, American Library Association, Association of Research Libraries, Medical Library Association, and Special Libraries Association

Allan Adler
Association of American Publishers

Bernard Sorkin
Time Warner Inc.

Fritz Attaway
Motion Picture Association of America

11:00-12:30 Panel 2

Keith Kupferschmidt
Software and Information Industry Association

Lee Hollaar

Scott Moskowitz
Blue Spike, Inc.

Emery Simon
Business Software Alliance

Nic Garnett
Intertrust Technologies Corporation

12:30-1:45 Lunch Break

1:45-3:10 Panel 3

Susan Mann
National Music Publishers' Association, Inc.

Marvin Berenson
Broadcast Music Inc.

Gary Klein
Home Recording Rights Coalition

Pamela Horovitz
National Association of Recording Merchandisers

John T. Mitchell (for Crossan Andersen)
Video Software Dealers Association

3:10-4:35 Panel 4

Professor Peter Jaszi
Digital Future Coalition
Seth Greenstein
Digital Media Association
Steven J. Metalitz
American Film Marketing Association, Association of American Publishers, Business Software Alliance, Interactive Digital Software Association, Motion Association of America, National Music Publishers' Association. and Recording Industry Association of America
Daniel Duncan
Digital Commerce Coalition
Carol Kunze
Red Hat, Inc.

4:35-6:00 Panel 5

Cary Sherman
Recording Industry Association of America, Inc.
David Goldberg
Launch Media, Inc.
David Beal
Sputnik7.com
David Pakman
myPlay Inc.
Bob Ohweiler
MusicMatch Inc.
Alex Alben
RealNetworks, Inc.
Robert Nelson (for Charles Jennings)
Supertracks, Inc.

6TH DOCUMENT of Level 1 printed in FULL format.

Jaffe Reburtal Exh.

COPYRIGHT ROYALTY TRIBUNAL
AGENCY: Copyright Royalty Tribunal.

37 CFR Part 306
1980 Adjustment of the Royalty Rate for Coin-Operated Phcnorecord Players

[Docket No. CRT 80-1]

46 FR 884

January 5, 1981

TION: Final rule

MMARY: The Copyright Royalty Tribuna? adopts the rule establishing the rate of yalty payments for the public performance of nondramatic musical works by in-operated phonorecord players.

FECTIVE DATE: February, 4, 1981
lopted December 10, 1980.

OR FURTHER INFORMATION CONTACT:

larence L. James. Ji., Chairman, Copyright Royalty Tribunal. (2021 653-5175.

EXT: SUPPLEMENTARY INFORMATION:

iduction

17 U.S.C. 804(a)1 provides that the Copyright Royalty Tribunal (Tribunal) hall publish a notice in the Federal Register on January 1, 1980 of the ommencement of proceedings concerning the adjustment of royalty rates for sin-operated phonorecord players as provided in section 116. It is further rovided that the Tribunal shall render its final decisions in this proceeding ithin one year from the date of such publication.

ackground and Chronology

?he Amusement and Music Operacore (AMOA) and the three principal music erforming rights societies -- American Society of Authors, Composers, and ublishers (ASCAP); Broadcast Music, Inc. (BMI); and SESAC, Inc. responded to he Tribunal's notice af January 2, 1980.

Cn February 13 in the officer of the Tribunal a meeting was held with all nterested parties to discuss the economic eurvey to be conducted by AMOA and to ake recommendations on the information to be solicited. The Tribunal and the erforming rights societies offered suggestions to be included in the survey ut were informed by AMOA that the questionnaire for the survey had already been ailed.

The Tribunal conducted public hearings to receive testimony on the stments of royalty rates as provided in section 116 on April 2, 3, 4, 21, 22. Rebuttal was heard on May 16 and 19, 1980. I addition to the materia? resented at these hearings, the Tribunal also received written statements and ocumentary evidence submitted in accordance with the rules of the Tribunal. roposed findings of fact and conclueions of law were submitted on September 16, 980 at the direction of the Tribunal.

At a public session on December 10, 1980 the Tribunal made its final etermination concerning the royalty rate adjustment for coin-operated honorecord players.

ummary of Evidentiary Positions of the Parties

The American Society of Composers, Authors and Publishers (ASCAP) and SESAC onsidered that by application of the standards an 17 U.S.C. Sec. 801(b)(1) a easonable compulsory license fee for the public performance of all copyrighted usical compositions by a jukebox is $70. n1 They also contended that because he royalty rate is to apply for at least a ten year period, the S70 fee should e subject to annual adjustments reflecting the increase in the cost of living s determined by the Consumer Price Index. n2 Moreover they *contend* that the nnual adjustments should commence for the 3982 calendar year. n3

n1 "Proposed Findings of Fact and Conclusions of Law Submitted by ASCAP and SESAC" September 16, 1980, p. 1.

n2 Ibid., p. 1.

n3 Ibid.. p. 1.

lthough ASCAP and SESAC contend that the record in thie proceeding eupports compulsory license rate expressed in dollars or as a percentage of the revenue of each jukebox, they conclude that "at this tame and on thas record, practical onsiderations and the stated preference of the jukebox operators * * * convince s that the more appropriate fee for all jukeboxes is a fee expressed in ollars." n4

n4 Ibid., p. 2.

These two performing rights societies stated that in order to apply the standards in Section 801(b) they felt compelled to determine a compulsory license fee similar to the fee which would be reached on the open marketplace if performing rights societies and jukebox operators were free to negotiate for Licenses absent a compulsory license. n5

n5 Ibid.. p. 2.

With that as a benchmark they concluded that the most useful approach in reaching a marketplace value was to use close marketplace analogies. n6 n6 Ibid., p. 2.

Three analogies were used: (a) general establishments, such as bars, grills, restaurants and taverns using mechanical music (i.e., music provided by non-live); (b) background music services; and (c) foreign jukebox operators. n7

n7 Ibid., p. 2.

ASCAP's direct case was presented through testimony of Robert R. Nathan, hairman of Robert R. Nathan Associates, Inc., and Dr. Paul Fagan, ASCAP's Chief conomist and Director of Special Programs.

Mr. Nathan testified that in our economy value is usually determined in the arketplace, and when a regulatory agency must set a rate it should do so based n the most likely parallel or similar economic circumstances relating to the oods or services in question. n8

n8 Ibid., p. 20.

Mr. Nathan discussed the four objectives in Sec. 801 which in his opinion the ribunal must apply in determining a reasonable compulsory license fee. He said hat the first objective, maximizing the availability of creative works to the ublic, means that the rate must be sufficient to maintain the Creator's ncentive to create the work and to encourage its exploitation. He added that he fee should not be so high as to reduce the demand for music, n9

n9 Ibid., p. 26.

The second objective, providing a fair return to the copyright owner and a air income to the copyright user, is one which would be met by free negotiation etween the parties. Mr. Nathan urged the tribunal to consider market experience n parallel areas, pointing out that a fair return to owners and fair income to sers does not guarantee every owner a maximum return or every user a profit.

n10 Ibid., pp. 20-21.

The third objective, Mr. Nathan testified, required the balancing of the elative contributions of the copyright owner and the copyright user. He pointed ut that marketplace value is the only effective measure of the relative reative contributions, capital investments, costs and risks of the copyright ser and owner. n11

n11 Ibid., p. 21.

Mr. Nathan testified that the fourth objective was to seek to minimize the isruptive impact on both the jukebox industry and the established license tructure of music performing rights. n12

n12 Ibid., p. 21.

Dr. Paul Fagan detailed the three marketplace analogies ASCAP proposed to the ribunal. The first analogy is to the license fees paid by establishments like restaurants, taverns, bars and grills which use tape recorders, record players or jukeboxes not subject to compulsory license. He testified the lowest such

;e for ASCAP alone is $70. When the fees for BMI and SESAC are added, the total .nimum fee paid by such establishments is $190. n13 Dr. Fagan stressed that iere would be an administrative savings if all three repertories were licensed : once, estimating the resulting total minimum license fee at $140. n14

.13 Ibid., p. 24.

n14 ibid., p. 24

The second analogy addressed by Dr. Fagan was to license fees paid by ickground music services. He said that ASCAP licensee about 700 background isic operators. The annual rate charged by ASCAP alone for locations similar to iose in which *jukeboxes* may be found is $27. This rate, however, was described s an interim fee subject to retroactive adjustment to 1971. a15 Assuming that he rates *were* adjusted only for inflation, he said that. it would be $52.08 in 980. n16

n15 Ibid., p. 25.

n16 Xbid., p. 25.

The third analogy testified to by Dr. Fagan was for license fee6 paid for ukeboxes abroad. He noted that the foreign analogy was particularly ppropriate. One, the licenses granted by foreign performing right societies are dentical in ecope to the American compulsory license. Two, the fees are either egotiated with industry groups or are subject to governmental approval. Three, oreign jukebox operators operate in the same way as their American ounterparts. Four, the rates here should be higher than abroad because income evels in foreign Countries are generally lower than those in the United States. 17

n17 Ibid., p. 26.

She average fee paid by jukeboxes in the nineteen countries ASCAP surveyed is 33 and the mean is $70.92. n18

n18 Ibid., p. 26.

Dr. Fagan further testified that the prcpoeed $70 fee is one that :oin-machine operators can afford, amounting to only 19 cents per day. n19

n19 Ibid., p. 28.

Broadcast Music, Inc. (BMI) through testimony by Edward W. Chapin, vice resident and general counsel underscored its agreement with ASCAP and SESAC in :he adoption of a royalty rate which would vary annually in accordance with the :onsumer Price Index. n20

n20 "Proposed Findings of Fact and Conclusions of Law submitted by BMI" September 16, 1980, p. 10.

BMI, based on prior congressional findings, has proposed a royalty rate of approximately $30 adjusted annually in accordance with the CPI. n21

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n21 Ibid., p. 12.

BMI's proposed royalty rate follows directly from the legislative history and statutory mandate requiring balancing of economic considerations. Therefore, applies historical changes in the CPI to the $19.70 base specifically recognized by Congress in 1975 as a reasonable fee. n22

n22 Ibid., pp. 12-13.

Application of the CPI from 1975 to the $19.73 base results in a royalty rate of approximately $30, adjusted annually. n23

n23 Ibid., p 13.

In BMI's view its proposal represents a compromise between maximizing the return to copyright owners, whose works presents the means by which the users gain their profits, and any economic considerations applicable to the copyright users. n24

n24 Ibid., p. 13.

BMI believes the $30 fee, although considerably smaller than many applicable state, local or foreign license fees, can be considered as providing a "fair return" to the copyright owner. Moreover, the $30 fee would amount to approximately 8 cents per day per jukebox -- equal to or less than the cost of one play per day -- thus it would not deny a "fair income" for the copyright user. n25

n25 Ibid., p. 14.

As a consequence, adoption of the proposed rate is likely to "maximize the availability of creative works," "reflect the relative roles of the copyright owner and the copyright user," and "minimize any disruptive impact on the industries involved." n26

n26 Ibid., p. 14.

The Amusement and Music Operators Association (AMOA) presented its case through the testimony of eleven witnesses and the submission of thirty exhibits, the principal one being Exhibit #10, the Peat, Marwick, Mitchell and Company (PMM&Co.) survey of the economic condition of the jukebox operators' business. n27

n27 "Proposed findings of Fact and Conclusions of Law submitted by AMOA," September 16, 1980, p. 5.

AMOA contends that there has been a marked increase in recent years in the numbers of amusement games that are in operation, especially in contrast to the decline in number of jukeboxes that are in operation and that many operators do not segregate their operating expenses for jukeboxes and games. n28

n28 Ibid., p. 6.

AMOA estimated that there are between 3000 and 5000 operators who operate between 251,000 and 308,000 jukeboxes in the country. n29 n29 Ibid., p. 15.

They introduced testimony which indicated that during the years 1975 through ¹⁷⁸ Rockola, Rowe and Seeburg produced between 38,000 and 42,000 jukeboxes lly, about one-half of which were for the U.S. market. n30

n30 Ibid., p. 16.

The PMM&Co survey indicates that on the average a typical operator operated 7 jukeboxes and 225 amusement games, and that jukeboxes and games *were* both perated in 65% of all locations with 65% *of* all jukeboxes operatrng in cities f 40,000 or less. n31

n31 Ibid., p. 16.

The AMOA produced testimony that new jukeboxes cost up to $2500 each, and ccessories nay add another $500. n32 fhey further indicated that the useful ife of a jukebox at the operators' preferred locations is about five years. n33

n32 Ibid., p. 17.

n33 Ibid., p. 17.

They also indicated that jukebox operators purchase phonorecords at an verage rate of 2 1/2 to 3 records per box per week, or about 130 to 150 record6 er box per year. n34

n34 Ibid., p. 17.

Although prices *per* play differ between operatore and between different areas opular pricing generally is two for a quarter or five for 50 cents which verages about 10 cents per play. n35

n35 Ibid., p. 21.

Several of AMOA's witnesses stressed that their boxes arc limited to an ncome based upon time. n36

n36 Ibid., p. 22.

The PMM&Co survey indicates that for the industry at large 18% of the boxes in Operation earned for the operators less than $300 per year, and that 475 earned less than $700 per year. For smaller operators *of fewer* than 40 machines, 13% of the boxes earned le66 than $300 per year, and 57% earned le66 than $600 per year. n37

n37 *Ibid.*, p. 24.

A report by professors Sequin and Malone of Notre Dame University indicates that over the 40 year period 1940 to 1980, while the Coneumtr Price Index increased 452%, the average price per play on jukeboxes increased 150%. n38

n38 Ibid., p. 25

AMOA reported statistics from the U.S. Department of Commerce on the jukebox inufacturing business which show a drop in total shipments and sales from a .gh of about 75,000 units in 1973 to about 38,000 units in 1975, and a intinuation at about that level through 1978. n39

n39 ibid., p. 26.

Jukebox operator witnesses offered testimony reflecting a continuing decline the numbers of jukeboxes that are in operation, citing two basic causes *for* ie decline. (1) the operators' inability to increase prices per play so as *to* eep up with the rate of inflation, and (2) the loss of jukebox locations due to ocio-economic changes such as urban redevelopment, and replacement of jukeboxes y other means of entertainment such as background music, radio, television, iscos and live entertainment. n40

n40 Ibid., p. 27.

The AMOA, citing evidence of the decline in the jukebox operating business, ecreasing revenues and margins of profit, and industrywide reduction in numbers ! locations and of jukeboxes in operation, argued strongly that the $8 royalty ee should be left unchanged. n41

n41 Ibid., p. 31.

egal Considerations

he Issue *of* Burden of Proof

AMOA has asserted that the performing rights organizations have the burden of roof in this proceeding. They cite as authority McCormick, On The Law *Of* vidence n42 and certain provision of the Administrative Procedure Act. n43

12 Pre-hearing **Brief**, AMOA p. 6.

n43 Memorandum in Support of AMOA Propoeed Finding of Facts and Conclusions of Law, pp. 7-8.

We find the McCormick rule is inapplicable in the circumstances of this proceeding. The Copyright Act of 1976 mandates review of the interim rate pursuant to Section 804(a)(1) In Section 804 Congrees clearly distinguishes between procedures appiicable to the 1980 royalty determination and the subsequent 10-year **review** proceedings, Section 804(a)(1) statee:

(O)n January 1, 1980, the Chairman of the Tribunal shall Cause to be published in the Federal Register notice of commencement of proceedings under this chapter * * *

17 U.S.C. Section 804(a)(1). Section 804(a)(2) states:

(D)uring the calendar years specified in the following schedule (i.e. every subsequent tenth year for jukebox) any owner or user of a copyrighted work *whose* royalty rates arc specified by this title, or by a rate established by the ibunal, may file a petition declaring that the petitioner requests an ljustment of the rate. (Italics added)

This proceeding commenced without any petition by an owner or user according 7 U.S.C. 804(a)(1). The Senate Report recognized the mandatory nature of proceedings: "This subsection requires that there be a review in 1980 of ion royalty rates, and it is mandatory for the CRT to commence such roceedings." n44 We conclude that none of the parties has the burden of showing iat the Tribunal should examine the fee. We find the statute requires the ribunal to do so.

n44 S. Rep. No. 94-473, 94th Cong. 1st. Sess. (1975) p. 156.

Further this proceeding differs from others which may occur in future years. roceedings in 1990 and each subsequent tenth calendar year will occur only if a opyright owner or jukebox operator petitions the Tribunal for an adjustment of ne rate. n45

n45 17 U.S.C. § 804(a)(2).

We therefore conclude, that while subsequent review proceedings may be nitiated only by petition of an interested party, the 1980 review ie mandatory. ince none of the partiee herein has inrtiated this royalty rate proceeding, ach party carries an equal burden of proof.

he Issue of the Annual Cost of Living

AMOA's position is that the Copyright Act does not permit an annual djustment for inflation under Section 116. They argue that the approach used by be CRT in Section 118 public broadcasting proceeding is not provided for under ection 116. They further argue that Section 118's reference to "rates and erms" for public broadcasting royalty provides the CRT with authority to adopt he annual cost of living approach, while Section 116's reference only to "rate" ts the Tribunal's flexibility. n46

n46 AMOA Reply Brief to Preheating Brief of BMI, pp. 5-6.

Both BMI and ASCAP/SESAC advocate the adoption of a royalty rate which would ary annually in accordance with the Consumer Price Index. n47 As both BMI and SCAP/SESAC point out, the Tribunal adopted this approach in its Section 118 ublic broadcasting proceeding.

n47 Proposed Findings of Facte and Conclusions of Law of BMI, p. 13, and roposed Findings of Facts and Conclusions of Law submitted by ASCAP and BMI, p. 11.

We find that the legislative history of Section 118 shows clearly that the ise of the word "terms" has nothing to do with cost of living adjustments. It states:

The Committee anticipates that the "terms" established by the Commission shall include provisions as to acceptable methods of payment of royalties by public broadcasting entities to copyright owners. For example, rhere the whereabouts of the copyright owner may not be readily known, the terms should, pecify the nature of the obligation of the public broadcasting entity to locate ie owner, or to set aside or Otherwise assure payment of appropriate royalties, ould he or she make a claim. n4B

n 48 H. Rep. NO. 94-1476, 94th Cong., 2nd Sess. 118 (1976).

AMOA further claims that the Tribunal is restricted in its application of the onsumer Price Index to the jukebox rate by criteria Specified in Section 801(b) 1)-(D) and that it is not so restricted under Section 118. n49

n 49 Memorandum in Support of AMOA Proposed Findings of Fact6 and Conclusions f Law, p. 11.

We find that AMOA's position is at odds with the legislative history of the ection. It states:

Similar considerations (to jukebox royalty standards) are noted in connection ith Commission review of rates and terms for public broadcasting in the iscussion of Section 118, above. n50

n 50 H. Rep. No. 94-1476, 94th tong., 2nd Sess. 118 (1976).

We conclude that there are no essential differences in the tribunal's uthority with reepect to Sections 116 and 118 which would permit the Tribunal o provide annual cost of living adjustments in one case and not the other. We ind that there is nothing in the statute or legislative history which could be onstruea to limit the application of annual cost of living adjustments.

In conclusicn, we find that the adoption of adjusted jukebox royalty rate hich varies annually with the Consumer Price Index is a proper exercise of ribunal authority.

b. Issue of the Performing Rights Societies Financial Data

AMOA sought to bring into issue in this proceeding the manner of how the erforming rights organizations distributed jukebox royalties to their ffiliates and members. AMOA argued that § 801(b)(1)(B) of the Copyright Act alled for an investigation of the performing rights organization6 distribution ethods. n51 AMOA further argued that performing rights organizations are not n "compliance" with the Copyright Act unless they distribute royalties among their affiliates and members in accordance with a requirement contained in ection 116(c)(5). n52

n 51 AMOA Brief an admissibility of certain exhibits

n 52 Id

Finally AMOA argued that there is no logical way the Tribunal can determine if a change should be made in the compensation chat i6 to be provided without calculation of the specific compensation to individuals. n53 Under AMOA's approach thi6 was the only way that the "fair return" standard of the Act could be met.

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46 FR 884

n 53 AMOA Pre-hearing Brief, Q. 9.

In summary AMOA's position in essence was asking the Tribunal to establish ·· value of individual musical works based on the time and expense incurred by songwriters for each one, together with a value inexplicably derived from .. placement of a work on a popularity chart. It then asks the Tribunal to ivestigate the internal distrrbution procedures of the performing rights :ganizations to establish the exact payout for each member or affiliate. A)mparison of the two calculation6 ·· the costs and the payout ·· would, ;cording to AMOA, produce the "fair return" calculations supposedly required by ie Copyright Act. n54

n 53 AMOA Pre-hearing Brief, pp. 7-9.

BMI argued that the language cited by AMOA "to afford the Copyright owner a air return for his creative work", reflects the broad goal of the legislation o insure that creators are fairly compensated through adoption of license fees stablishing a reasonable value for the use of the Copyright works. We agree. he language in the statute is not a directive authorizing the Tribunal to nvestigate individual members or affiliates collections from the performing ights organizations.

We find that there is no indication either in the statute or the legislative istory, that Congress intended the Tribunal to calculate rates or return for ach piece of music and then base royalty adjustments on these rates of return.

We *frnd* that the copyright Act in section 116(c)(4)(B) specifically provides hat royalty fees are to be distributed to the performing rights organizations. he section reads in pertinent part:

(4) The fee6 to be distributed shall be divided as follows:

* * *

(B) to the performing rights societies, the remainder of the fees to be .istributed in such pro rata shares as they shall by agreement stipulate among hemselves, or, if they fail to agree, the pro rata share to which such erforming rights societies prove entitlement.

The performing rights organizations are specifically referred to by name in he definition of "performing rights society" set out in section 116(e)(3) of .he Act. It is thus our opinion that the Act recognizes a practical necessity 'or individual creators of music to adequately protect their performing rights ind for users, such as the jukebox industry, to conveniently acquire performing :ights. We conclude, therefore, that the "fair return" to music copyright owners, i.e. the reasonable value of the performing right can be established on a collective basis.

We find nothing in the Copyright Act or its legislative history which indicates that the Tribunal was intended to regulate the internal operations of the performing rights societies. In our opinion the Tribunal's authority is strictly limited to setting applicable royalty fees and establishing the distribution to claimants.

In our opinion section 116(c)(5) establishes authority in the Tribunal to omulgate regulations permitting prospective claimants to enter establishments id sample jukeboxes to establish the basis of a claim. We find, however, that iis section does not require that pertorming rights organizations must blish that they have segregated jukebox royalties from royalties collected other sources, and therefore. since the Copyright Act doer not create ithority in the Tribunal to establish euch regulations, no such regulations ive beer. adopted.

etermination Of Royalty Rate

ie AMOA Case

The Tribunal finds that the case presented by the AMOA, including the dustry survey, has failed to provide reliabie data concerning the operating xpenses, revenues, or return on investment on jukebox operators.

The Tribunal convened a conference of the parties on February 13, 1980 in rder to permit the Tribunal and all of the parties to make suggestions oncerning the contents of a questionnaire which would be used by AMOA to survey he financial condition of jukebox operators. At that conference the epresentatives of AMOA stated that it was too late to revise the questionnaire.

We note the limited response rate to the questionnaire, estimated by Peat arwick to be approximately 14%. Dr. John Scarbrough, the Peat Marwick manager n charge of the survey, testified:

I wouldn't argue very hard if you wanted to say that it was not a good esponse. n55

n55 Transcript, April 4, 1980, p. 61.

ne record of this proceeding contains detailed testimony reciting the ocedures utilized in the preparation and distribution of the questionnaire, hich present significant questions as to the survey's methodology and bjectivity, as well as the nature and scope of the data provided.

We also note that the survey information is not consistent with other vidence in this record, such as 1979 Playmeter survey of the jukebox industry 56 and a survey of the industry published in the March 1978 issue of Replay. 57 we have reviewed the testimony of the AMOA witnesses -- five Jukebox perators, representatives or distributors of the three American jukebox anufactures, a "one-stop" distributor of records, and a trade association fficial. we find that this testimony does not provide a basis for forming any epresentative picture of the jukebox industry nor does it create a foundation or the industry's claim of economic hardship. The testimony does establish an ndustry practice to turn over 50% of the gross revenues from jukeboxes to the ocation owner.

n56 ASCAP Exhibit 8.

n57 BMI Rebuttal Exhibit A.

he BMI Case

BMI proposed that we determined the rate by applying the Consumer Price Index 1975 to a proposed jukebox royalty fee of $19.70 that had been mentioned in ngressional committee report. We have concluded that this approach is not in ccord with our statutory responsibilities in this proceeding.

he ASCAP/SESAC Case

In reaching our determination in this proceeding, we found the ASCAP/SESAC oncept cf basing the rate on marketplace analogies to be most attractive. We ave examined the three marketplace analogies urged upon us by ASCAP/SESAC -- he Licenses fees paid by general establishments using mechanical music, ackground music services, and foreign jukebox fees.

These analogies individually and collectively are subject to limitations and istinguishing features. We believe that certain of the distinctions set forth n the AMOA pleading have validity. n58 While acknowledging that our rate cannot e directly linked to marketplace parallels, we find that they serve as an ppropriate benchmark to be weighed together with the entire record and the tatutory criteria.

n58 AMOA Proposed Findings, p. 40-42.

'ribunal Rate

We find that a per box payment of $50 is a reasonable fee for the jukebox ndustry as a whole. We have phased in the rate to accord the jukebox industry n opportunity to adjust, since in our view the jukebox induetry has never reviously paid reasonable compensation for the use of copyrighted music. We ote that ASCAP/SESAC, in their proposed findings, concluded that an interim fee d be appropriate "to afford the coin machine industy an opportunity to adopt o compulsory licensing at marketplace rates." n59 Consequently, the adjustment of the jukebox rate on January 1, 1982 wrl? be limited to $25.

n59 ASCAP Findings, p. 3.

We are aware that some jukebox operators function on a narrow profit margrn, nd that certain jukeboxes produce modest revenues. The Tribunal is satisfied hat adequate attention has been given to the small operator, including the doption of an amendment to the proposed fee schedule that was proposed for the enefit of such operators.

Based on the Playmeter and Replay surveys and ocher evidence in this record, we believe that it would be reasonable for some operators to be paying more than $50. If the Tribunal had adopted a fee schedule based on such factors as per box revenue or the number of boxes owned by a particular operator, a higher payment by certain operators or for particular boxes might be warranted. The Tribunal has chosen to adopt a flat rate for all boxes -- the course urged upon us by all parties an this proceeding.

IC is not reasonable that the fees adopted in this proceeding should remain :changed until at least 1990. We have therefore made provision for a single ›st of living adjustment.

ıtory Criteria

We have reached our decision in full recognition of the application to this :oceeding of the criteria in 17 U.S.C. 801(b). We observe that the criteria ıre not drafted for specific applicatior.exclusively to the determination of ıe jukebox rate. The Tribunal has analyzed each of the criteria.

› Maximize the Availability of Works

The first statutory objective of our rate determination listed in Section ›1(b)(1) is "To maximize the availability of creative works to the public". We › not maintain that the jukebox rate is crucial to assuring the public cf the vailability of creative works. As has been observed in the pleadings, musical ›rks were created and exploited fer many years, during which, in our view, ongwriters and publishers were unjustly denied reasonable compensatron for a ommerical use of their works. We concur in the ASCAP/SESAC ficding that reaeonable payment for jukebox performances will add incrementally to the ncouragement of creation by songwriters and exploitation by music publishers, ad so maximize availability of musical works to the public." n60 We find othing in this record which would justify any reasonable Concern that the chedule we have adopted will deprive the public of access to music.

n60 ASCAP Findings, P. 4.

air Return to the Copyright Owner and Fair Income Eor the Copyright User

The second statutory criteria is "To afford the copyright owner a fair return his creative work and the copyright user a fair income under existing ..nomic conditions." we have previously discussed our conclusion that, within he limitations necessarily inherent in a flat industry rate, our schedule ffords the copytight owner a fair return. We reject the contention that :opyright owners are paid for jukebox performances by mechanical royalties lerived from record sales. We recognize that performing rights arc distinct from ·ecording rights. The Congress has detennined that copyright owners are entitled o be paid reasonable fees for both. The Tribunal also rejects the contention .hatno adjustment of the royalty fee should be made unless the copyright owners ıstablished their "need to receive" an increase.

We have above given our analysis of the testimony presented by the jukebox ndustry. We find nothing in that testimony which would warrant a conclusion 'hat our schedule will deprive the jukebox operator of a fair income under ıxisting economic conditions. In adopting the rate, we have given sympathetic :onsideration to the circumstances of emall Jukebox operators, and reflected in :he determination of our rate that certain boxes produce modest revenues.

ՙelative Contributions

46 FR 884

The third statutory criteria is "To reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk, and contribution to the opening of markets for creative expression and media for their communication." On the basis of the record in this proceeding we have no basis for concluding that jukebox operators and owners of establishments with jukeboxes make any unique or distinctive contribution concerning creativity, technology, capital investment, cost, risk, and the opening of new markers for creative expression and media for their communication. We find in this record no basis for a conclusion that the efforts of jukebox operators through the selection of records and their performance promote the dissemination of songs in any significant manner. We find that the owners of the establishments in which jukeboxes are located do not make a contribution in the areas encompassed in this statutory objective.

On the other hand, the contribution of the copyright owner whose works are performed under the compulsory license directly benefits the jukebox operator and location owner.

Disruption of the Industries

The fourth statutory criteria is "To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices." We find that a failure of this Tribunal to establish a reasonable fee for jukebox performance could snterfere with performing tights societies receiving reasonable fees from similar users of music, whose rates are not established in accordance with statutory provisions.

We cannot on the basis of the evidence presented by the jukebox industry find that our schedule will have a disruptive impact on the structure of the Jukebox industry or disturb generally prevailing industry practices. By introducing the fee schedule in two phasee, we have, in our view, adequately reflected in our decision the objective of this statutory criteria. The jukebox industry pays reasonable market prices for all other goods and services they require. We hold that they can pay the schedule we have adopted for the central commodity of their boxes without adverse impact.

Conclusion

On the basis of the marketplace analogies presented during the proceeding, taking the record as a whole, and with regard for the statutory criteria, the Tribunal has adjusted the royalty rate for coin-operated phonorecord players to $50 per machine. That rate takes account both of what is paid for music elsewhere under similar circumstances and, since it is a flat rate, of the Tribunal's concern for the smaller, less profitable operacore.

In order to ease the impact of a rate increase upon the jukebox industry and in recognition of the fact that royalty payments far jukeboxes have been in effect in the United States only since 1978, the Tribunal has elected to stagger the introduction of the rate. It will take effect on January 1, 1982, and for two years, from 1982 to 1984, the rate will be half ·· $25.

Because the $50 rate set as a result of this proceeding cannot be reviewed ntil 1990, the Tribunal feels that the copyright owners might not be fairly ompensated unless a provision is included to adjust for inflation. This djustment takes place on January 1, 1987, and as based upon the Consumer Price converrng the period February 1981 to August 1986.

Accordingly, pursuant to 17 U.S.C. 801(b)(1) and 804(e), 37 CFR Chapter III s hereby amended as follows:

By adding a new Part 306, to read as follows:

PART 306 -- ADJUSTMENT OF ROYALTY RATE FOR COIN OPERATED PHONORECORD PLAYERS

Sec.

36.1 General.

06.2 Definition of coin-operated phonorecord player.

06.3 Compulsory license fees for coin-operated phonorccord players.

06.0 Cost of living adjustment.

Authority: 17 U.S.C. 801(b)(1) and 804(e)

§ 306.1 General.

This Part 306 establishes the complusory license fees for coin-operated honorecord players beginning on January 1, 1982, in accordance with the isions of 17 U.S.C. 116 and 804(a).

§ 306.2 Definition of coin-operated phonorecord player.

As used in this Part, the term "coin-operated phonorecord player" shall have he same meaning as set forth in 17 U.S.C. 116(e)(1).

§ 306.3 Compulsory license fees for coin-operated phonorecord playerr.

(a) Commencing on January 1, 1982 the annual compulsory license fee for a coin-operated phonorecord player, as set forth in 17 U.S.C. 116(b)(1)(A), shall e $25.

(b) Commencing on January 1, 1984 the annual compulsory license fee for a oin-operated phonorecord player, as set forth in 17 U.S.C. 116(b)(1)(A), shall e $50, subject to adjustment in accordance with § 306.4 hereof.

(c) In accordance with 17 U.S.C. 116(b)(1)(A), if performances arc made Available on a particular phonoreeord player for the first time after July 1 of my year, the compulsory license fee for the remainder of that year shall be one alf of the annual rate of (a) or (b) above, subject to adjustment in accordance ith § 306.4 hereof.

§ 306.4 Cost of living adjustment.

(a) On August 1. 1986 the Copytight Royalty Tribunal (CRT) shall publish in [th]e Federal Register a notice of the change in the cost of living as determined [by th]e Consumer Price Index (all urban consumers, all items) from the first [Inde]x published subsequent to February 1, 1981 to the last Index published prior [t]o August 1, 1986.

(b) On the same date as the notices published pursuant to paragraph (a), the [CR]T shall publish in the Federal Register a revised schedule of the compulsory [l]icense fee which shall adjust the dollar amount set forth in § 306.3(b) [ac]cording to the change in the Cost of living determined a3 provided in [pa]ragraph (a). such compulsory license fee shall be fixed at the nearest dollar.

(c) The adjusted schedule for the compulsory license fee shall become [e]ffective on January 1, 1987.
[N]ote. ·· commissioners Brennan, Coultet and Burg concurred in the above opinion. [C]ommissioner Garcia disagreed with the conclusion reached and has filed a [s]eparate conclusion. Commissioner James has filed separate Findings of Facte, [C]onclusions and Opinion.

[C]larence L. James. Jr.,

Chairman, copyright Royalty Tribunal.

[S]eparatc Conclusion of Commissioner Garcia

It is my considered opinion and thus my conclusion that the royalty rate [i]ncrcase should have been 530.00 and 560.00.

• [Sepa]rate Findings of Facts, Conclusions and Opinion of Commissioner James

I cannot support the findings of facts, the conclusions reached from thoee [f]acts, and the specific rationale of the majority of the members of the [T]ribunal. In my opinion their determination of an equitable and reasonable [s]tatutory rate io unsupported by the record in this proceeding.

This is a proceeding to adjust the reasonable copyright royalty rate as [p]rovided for in section 116. The statutory authority which governs the Tribunal [i]n this adjustment, states that the rate shall be calculated to achieve certain [e]numerated objectives. They are as follows:

1. To maximize the availability of creative works to the public;

2. To afford the copyright owner a fair return for hi6 creative work and the [c]opyright user a fair income under existing economic conditions;

3. To reflect the relative roles of the copyright owner and the copyright [u]ser in the product made available to the public with respect to relative [c]reative contribution, technological contribution, capital investment, cost. [r]isk, and contribution to the opening of new markets of creative expression and [m]edia for their communication;

4. *To* minimize any disruptive impact OR the structure of the industries ıvolved and on generally prevailing industry practices.

The compulsory license fee rewires payment to copyright owners *for* use of · r property by others, preventing free negotiation in the marketplace as to . Thus, the issue before the Tribunal was value in the marketplace. The ı,.slative history of the Copyright Act and the record in this proceeding ıpports the proposition chat the Tribunal must determine a license fee ›mparable to the fee reached in the open marketplace by anaiogous music users. ɜcause performing tights societies and jukebox operators are not free to ɜgotiate, the only fair, logical and equitable approach *to* establishing a ›mpulsory license fee is on the basis of marketplace value.

It is therefore my opinion that to determine marketplace value. the Tribunal ın only rely on marketplace analogies. Eased on the record in this proceeding, : ıs clear that the marketplace guidelines of other analogous music users, rovide the only credible evidence ın the record *to* establish a "reasonable" ɜe. Negotiated fees by analogous music users, which are identical or similar, ısed cn this record ıs the *only* indicator of true market value. n1

n1 Tr. 4/2 p. 23, pp. 25-32, p. 57, pp. 73-74; Tr 4/3 p. 124

The above position is supported by ASCAP's expert economic witness, Robert E. athan. Mr. Nathan testified that, "In our economy, value is usually determined n the marketplace. When a regulatory agency must set a rate, it should do so astd on the most likely parallel or similar economic circumstances relating to he goods and services in question." n2

n2 Tr. 4/2 pp. 22-23.

In this record the only evidence of marketplace value was based on close arketplace analogies of other music users. n3 The evidence in the record rovided three such close marketplace analogies:

3 Tr. 4/2 p. 66; ASCAP/SESAC Pre-Hearing Statement pp. 10-12; Charlee T ın's letter to Chairman 5/12/80 with enclosure.

1. License fees paid by general establishments (on location rates);

2. License fees paid by background operators;

3. The licensing fee arrangement and foreign countries. n4

n4 Ibid.

The first analogy ie license fees paid by establishments which use tape ecordere, record playerr, or free jukeboxes. Evidence offered by ASCAP ndicated the minimum fee for such an establishment is $70. n5 Evidence offered y BMI indicated that the minimum fee is $60 per year. n6 SESAC cffered no vidence ın this regard. Further the evidence indicated that the maximum fee for SCAP for thie type of establishment ın $490, and for BMI $210. Combining the ıinimum for both ASCAP and BMI would result in an annual fee of $130. This vidence was uncontroverted or refuted by AMOA.

n5 Tr. 4/2 p. 66; ASCAP/SESAC Pre-Hearing Statement pp. 10-12.

n6 Charles T. Duncan's letter to Chairman 5/12/80 with enclosure.

The second analogy was license fees paid by background music service. Both n7 and BMI n8 indicated that the fees, charged under this category, have the subject of litigation since 1971 and consequently have been frozen ince that tine. Because current ASCAP and BMI fees do not reflect the rate of nflation since 1971, it was not possible to ascertain the marketplace value or ackground music. n9

n7 Tr. 4/2 pp. 63-64.

n8 Charles T. Duncan's letter to Chainnan 5/12/80 *with* enclosure.

n9 ASCAP/SESAC Pre-Hearing Statement pp. 13-14; Proposed Findings of Facte nd Conclusions *of* Law submitted by ASCAP and SESAC p. 2S, and Charles T. uncan's letter to Chairman 5/12/80 with enclosure.

The third analogy is licenee fees paid for jukeboxes abroad. n10 In my pinion, any consideration of foreign fees by the Tribunal must be excluded. oreign fees reflect different licensing systems and cultural values. Further. he foreign fees are applied based on various criteria. In essence, the foreign ees involve such a diversity of circumstances as to be of little or no robative value.

n10 ASCAPISESAC Pre-Hearing Statement p. 15; Tr. 4/2 p. 66; Findings of Facts nd Conclusions of Law submitted by ASCAP and SESAC pp. 25-26.

In essence, the majority reached a conclusion on the premise tnat a true arket value rate would result in too large an increase in fees. The majority as set on course by what they deemed *were* the gurding standards of the etatutc hich referred to minimizing the disruptive impact *on* the economic structure of he industries involved. It was the majority view and opinion that a large ease in fees would be oppressive to the industry and would "impact on emall ators." n11 In my opinion the majority misconceived the evidence in the ecord when this standard wae applied. First, it is apparent that the standard as applied only to jukebox operations. There apparently woz no consideration iven to significant disruption in existing market prices for performing rights ocieties, fees paid by other analogous music users. The majority, in eeeence, ppears to have reached a eonclueion based on an ability to pay theory. n12

n11 Tr. 12/10 pp. 4-5.

n12 Determination of Royalty Rate by majority, supra.

The real economic impact of increased fees on jukebox operators cannot be letermined *from* this record. n13 Economic data supplied by AMOA was of questionable reliability and validity and could not be used as a basis for any rate determination. n14 In addition, the record simply does not support AMOA testimony that jukebox operator6 are destitute or will go out of bufiness if fees art increased.

n13 Findings of Facts and Conclusions of Law submitted by ASCAP and SESAC, p. ?.

n14 AMOA Survey; Tr. 4/3 p. 36; pp. 51-53; and Findings of Facts and ›nclusions of Law submitted by ASCAP and SESAC. pp. 33-46.

In fact, the evidence is clear and convincing to the contrary. The reccrd in ›is proceeding shows that coin machine operators pay fair market price €or all . and services they use. n15 Further it has been established in the record jukebox operators have traditionally shared one half of the gross revenue .th a joint venture partner who neither contributes to the venture nor takes ›y risk. n16 This arrangement is neither bargained, nor negotiated, but :aditionally given away. How is it that jukebox operators can claim destitution : inability to pay a fair and reasonable rate, when for years over one half of ›eir revenue has been given away? Even the small operator, the concern of the ijority, split revenue 50-50 with the establishment owner. Is it appropriate ›r jukebox operators to come before this Tribunal and claim economic hardship? 17 In my opinion it would be far better to reanalyze or reevaluate the :aditional practice of givrng away one half of the revenue than to seek :onomic redress from this Tribunal.

n15 Tr. 4/21 p. 135 Tr. 4/2 pp. 24-25, 108-109.

n16 Tr. 4/4 p. 120; Tr. 4/21, p. 98, 138; Tr. 4/12 pp. 50-80

n17 Tr. 5/19 pp. 52 54; ASCAP Exh. R-4 pp. 47-51; R-22 pp. 16-17; Tr. 5/19 p. 49-52.

The rate established by the majority is not reasonable. Nor does it afford he copyright owner a fair return for his creative work. There is no evidence in he record to support the rate, no logic behind it and no equity in it.

In my opinion the record it replete with evidence that the minimum reasonable arketplace value fee should be $130, not $25 or $50. I find that the record is oid of any valsd argument that once a reaeonable rate is established there hould be a discount because of economic hardship. There is simply no probative vrdence in the record that jukebox operator6 should not and can not pay rates ' "arable to those paid by other analogous music users for the same product.

n18 ASCAP Exh. R-4, pp. 47-51; Tr. 4/21 pp. 72-74, 98, 102-4, 134 and 138; r. 4/22 pp. 73-76 and 99.

In conclusion, there is substantial evrdence in the record to show that ukebox operators have the ability to pay a fair, equitable and reasonable rate. hey already give one half of their revenues away. Further, I find $130, as a inimum, is a reasonable fee bared on market value, and that it meets each of he standards of 17 U.S.C. 801(b). n19

n19 Findings of Facts and Conclusions of Law submitted by ASCAP and SESAC, p. 3-11.

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