6

Before the
Copyright Office of the Library of Congress
Washington, D.C. 20024

In the Matter of	)	
	)	Docket No. RM 2000-7
Mechanical and Digital Phonorecord	)	
Delivery Compulsory License	)	

REPLY COMMENTS OF NAPSTER, INC.

I. Introduction.

Napster, Inc. ("Napster") has followed with interest the above captioned proceeding and the Copyright Office of the Library of Congress' ("Copyright Office") Notice of Inquiry ("Notice"). In a prior letter to the Copyright Office, Napster argued that the United States Congress ("Congress") is the proper forum to resolve the issues raised by the Recording Industry Association of America ("RIAA") in its Petition for Rulemaking and to Convene Copyright Arbitration Royalty Panel if Necessary, *In the Matter of Application of the Mechanical Compulsory License to Certain Digital Music Services* ("RIAA Petition") filed with the Copyright Office. More specifically, Napster stated that Congress, and not the Copyright Office, should determine the proper application of the mechanical compulsory license system for musical works to certain types of online digital music services.

Napster still believes that Congress is the proper forum to resolve these issues. Beyond the reasons raised in its letter, Napster notes that other commentors, including the RIAA[1], MP3.com[2], the Digital Media Association ("DiMA")[3], and the National Music Publishers' Association ("NMPA")[4], have taken the position at various times that the Copyright Office may not have the jurisdiction to undertake the action encouraged in the RIAA Petition or that Congress actually is the proper forum to resolve some of the issues attendant to online music distribution.

Nevertheless, Napster submits that if the Copyright Office does initiate a rulemaking on these issues, the Copyright Office should define incidental digital phonorecord deliveries ("iDPDs") to include Limited Downloads within the scope of the definition and that, further, the Copyright Office should make clear that the term Limited Downloads extends beyond the limited download business model that RIAA members have to date advocated. Rather, Limited Downloads should be interpreted to include a broad but predictable range of music sampling or promotional services and peer-to-peer business models.

If the Copyright Office determines, however, that Limited Downloads are not iDPDs, Napster suggests in the alternative that Limited Downloads are a subclass of

---

1 *See* Memorandum of NMPA, SGA, and the RIAA Regarding Disposition of the Digital Phonorecord Delivery Rate Adjustment Proceeding (July 21, 1998), at 2 (submitted to the Copyright Office in *In the Matter of DPD Rate Adjustment Proceeding*, No. 96-4).

2 *See* Comments of MP3.com, In *the Matter of Mechanical and Digital Phonorecord Delivery Compulsory License*, Docket No. RM 2000-7, at 7 (April 23, 2001) (MP3.com Comments).

3 *See* Comments of the Digital Media Association, *In the Matter of Mechanical and Digital Phonorecord Delivery Compulsory License*, Docket No. RM 2000-7, at 3 (April 23, 2001) (DiMA Comments).

4 *See* Comments of the National Music Publishers' Association, *In the Matter of Mechanical and Digital Phonorecord Delivery Compulsory License*, Docket No. RM 2000-7, at 1, 4-10 (April 23, 2001) (NMPA Comments).

digital phonorecord deliveries ("DPDs") and that the Copyright Office, pursuant to Section 115(c)(3)(D), should consider this as part of its rulemaking and undertake to set a lower rate for Limited Downloads than for DPDs. If the Copyright Office conducts a rulemaking to define iDPDs as they relate to Limited Downloads, Napster supports the use of a CARP proceeding to set the rates for iDPDs.

If it is determined that the Copyright Office has jurisdiction, Napster agrees that the Copyright Office should streamline the procedure for obtaining a mechanical compulsory license for not only iDPDs, but DPDs, as well. This will better take into account the nature of the online music distribution services that will require such licenses.[5] Finally, should it be determined that the Copyright Office has the authority in this instance to create a safe harbor under Section 115 and issue interim rules, it should not be exercised in the absence of notice and an expedited public comment period.[6]

Napster wishes to make clear that its Reply Comments in this proceeding are made with reference to the musical works copyrights contained in Limited Downloads and in no way are meant to reflect Napster's stance in regards to sound recording licenses. More specifically, Napster reiterates its prior stance that the current licensing scheme for sound recordings is inefficient and anticompetitive, thereby requiring the development of a federal legislative solution in the form of a sound recording compulsory license.[7]

II. Napster Background.

Napster, which has created an Internet community of music fans, has been the fastest-growing application in the history of the Internet. Shawn Fanning, then an 18-year-old freshman at Northeastern University, invented the Napster software in 1999. The company and its approximately 90 employees are based in Redwood City, California.

The Napster software is a revolutionary technology based on person-to-person file sharing. The Napster application enables users to locate and share music files (in MP3 and WMA formats) from one convenient, easy-to-use interface. The files are not stored on a central computer, they are stored on the hard drives of each of the millions of Napster users. Users download the music files from other users' computers. Napster also provides community members with a vehicle to identify new artists and a forum to communicate their interests and tastes with one another via instant messaging, chat rooms, and Hot List user bookmarks.

---

[5] *See* MP3.com Comments, at 8.

[6] *See* Comments of the Recording Industry Association of America, *In the Matter of Mechanical and Digital Phonorecord Delivery Compulsory License*, Docket No. RM 2000-7, at 17-21 (April 23, 2001) (RIAA Comments); MP3.com Comments, at 10-11.

[7] *See* Testimony of Hank Barry, Interim CEO, Napster, Inc., "Online Entertainment: Coming Soon to a Digital Device Near You?" United States Senate, Committee on the Judiciary, April 3, 2001, at 10. Attached as Appendix B.

Users have installed the Napster application more than 80 million times. The service has experienced peak use of more than 1.8 million people simultaneously and approximately 8 million unique IP addresses in one day.

On February 20, 2001, Napster unveiled the business model for its new membership-based service. The New Napster Service, which the company plans to release this summer, will allow Napster to provide compensation to all rights holders involved. More specifically, Napster's new, modified service will be a Limited Download service that allows the company to: (1) track songs that are exchanged using the New Napster Service, thereby providing Napster with information necessary to compensate rights holders; (2) limit users' ability to transfer files to another device, in essence tethering the files to users' computers; and (3) limit the sound quality through fidelity limitations.

III. The Current State of the Industry and Relevant Licensing Mechanisms.

Despite the many benefits that Napster and the emerging online music distribution industry promises, and the high consumer demand to receive music online, the industry's future viability is far from secure. Instead, the industry's development has been slowed by recording industry business and legal tactics aimed at curtailing competitive online music distributors' abilities to compete effectively against the established offline major recording companies. In terms of licensing, not one publicly traded and operating company has successfully obtained licenses from the major recording companies and all music publishers. Many online music companies, such as Riffage.com and MusicMaker.com, ceased operations. Many other companies have been forced to lay off a significant percentage of their employees.

Jim Griffin, Founder and CEO of Cherry Lane Digital, authored a white paper on these issues entitled "At Impasse: Technology, Popular Demand, and Today's Corporate Regime," in which he described the uphill battle that new online music distribution companies face. According to Griffin, the five major recording companies control roughly 85% of the market for prerecorded music.[8] Further, these companies' music publishing arms control a high percentage of the music publishing market as well. Griffin noted that the major recording companies' high market concentration allows them to operate in a coordinated manner that results in non-competitive anti-consumer behavior.[9] In the online world, this coordinated behavior has manifested itself in the aforementioned actions against competing online music distribution companies that, according to Griffin, require a legislative solution.[10]

The competing online music distribution companies, including the major recording companies, also are hampered by the incredibly complex and inefficient music licensing procedures that often involve multiple licensors for any particular work. As

---

[8] *See* Jim Griffin, At Impasse: Technology, Popular Demand, and Today's Copyright Regime, April 2001, at 5.

[9] *Id.* at 7.

[10] *Id.* at 4.

Napster's Interim CEO, Hank Barry, stated before the Senate Judiciary Committee, each work on a CD usually constitutes two separate copyrights. The first copyright is in the sound recording, or the artist's performance, which the recording company (usually) owns. The second copyright is in the musical composition being performed.[11] The complexity arises from the fact that the musical composition and the sound recording frequently are owned by separate companies or individuals. For example, at the Senate Judiciary Committee hearing, Mr. Barry noted that on one specific Holmes Brothers gospel CD, there are thirteen sound recordings and eight separate music publishers.[12] With approximately 3,000 recording companies and over 25,000 independent music publishers in the United States alone, the prospect of negotiating the sound recording and musical composition rights for all works to enable online distribution is a virtually impossible task.[13]

The RIAA Petition seeks to have the Copyright Office resolve certain inefficiencies associated with securing the publishing licenses for the online delivery or distribution of non-dramatic musical works through the establishment of a more efficient licensing process.[14] The RIAA stated in its petition that the lack of clarity regarding such licensing issues was "the primary obstacle to the launch of digital services."[15] Napster believes that the lack of clarity and the lack of a streamlined process for obtaining all forms of licenses, including publishing licenses, is a major obstacle to launching consumer friendly services. The current licensing procedures, for both musical compositions and sound recordings, have led to a paralysis within the nascent online music distribution market that is seriously hindering the industry's ability to grow and meet the staggering consumer demand for online music services. Napster believes a streamlining of procedure and a determination that iDPDs include Limited Downloads would help alleviate some of these licensing concerns as they relate to musical works, and thus facilitate the growth of the online music distribution industry.[16]

---

[11] *See* Testimony of Hank Barry, Interim CEO, Napster, Inc., "Online Entertainment: Coming Soon to a Digital Device Near You?" United States Senate, Committee on the Judiciary, April 3, 2001, at 6.

[12] *See* Oral Statement of Hank Barry, Interim CEO, Napster, Inc., "Online Entertainment: Coming Soon to a Digital Device Near You?" United States Senate, Committee on the Judiciary, April 3, 2001.

[13] *See* Testimony of Hank Barry, Interim CEO, Napster, Inc., "Online Entertainment: Coming Soon to a Digital Device Near You?" United States Senate, Committee on the Judiciary, April 3, 2001, at 7.

[14] *See* Petition for Rulemaking and to Convene Copyright Arbitration Royalty Panel if Necessary, *In the Matter of Application of the Mechanical Compulsory License to Certain Digital Music Services* (November 22, 2000) ("RIAA Petition").

[15] *See* RIAA Petition, at 11.

[16] It is important to note that regardless of the Copyright Office's ultimate determination, this proceeding will not help alleviate licensing concerns related to sound recordings.

IV. The United States Congress is the Proper Forum to Determine the Scope of the Mechanical Compulsory License for Musical Compositions.

The RIAA argues that a rulemaking is necessary to determine whether Section 115 of the Copyright Act, which established a mechanical compulsory license for DPDs, applies to On-Demand Streams and Limited Downloads.[17] It is Napster's opinion that Congress, and not the Copyright Office, is the proper forum for resolving such policy issues raised by the advent of innovations in the digital delivery of musical works.

First, by the RIAA's own admission, the Copyright Act is not clear as to whether Section 115 applies to these situations.[18] The RIAA also concedes that there are important policy questions regarding mechanical compulsory licenses for certain digital musical services that must be examined.[19] Given the important policy issues involved, combined with the uncertainty regarding Section 115's application to online music services, Congressional action is necessary.

Further, in a prior Copyright Office proceeding, the RIAA took the position that the Copyright Office did not have the authority to determine if streaming media activities were DPDs within the meaning of Section 115.[20] Now, the RIAA argues that the Copyright Office has the requisite authority to initiate the rulemaking proceeding pursuant to Section 702 of the Copyright Act, which states: "The Register of Copyrights is authorized to establish regulations not inconsistent with law for the administration of the functions and duties *made the responsibility* of the Register under this title."[21] While Section 115 provides the Register with a number of responsibilities, Congress did not confer upon the Register in Section 115 the responsibility to define iDPDs, or to determine which online music distribution business models involve the use of DPDs or iDPDs. The RIAA also is misplaced in its reliance on the *Satellite Broadcasting*[22] and *Cablevision*[23] cases to support the Copyright Office's authority to initiate a rulemaking proceeding, as those cases: (1) did not involve the possibility of wide ranging agency action, as is contemplated here, and (2) involved Section 111 of the Copyright Act, as opposed to Section 115 and mechanical compulsory licenses.

---

17 *See* 17 U.S.C. 115.

18 *See* RIAA Petition, at 3, 9, 11-14.

19 *See* RIAA Petition, at 11-14.

20 *See* Memorandum of NMPA, SGA, and the RIAA Regarding Disposition of the Digital Phonorecord Delivery Rate Adjustment Proceeding (July 21, 1998), at 2 (submitted to the Copyright Office in *In the Matter of DPD Rate Adjustment Proceeding*, No. 96-4).

21 *See* 17 U.S.C. § 702 (emphasis added).

22 *Satellite Broadcasting and Communications Association v. Oman*, 17 F.3d 344, 347 (11th Cir. 1994).

23 *Cablevision Systems Development Co. v. Motion Picture Association of America, Inc.*, 836 F.2d 599, 608-609 (D.C. Cir. 1988).

The RIAA also notes that resolution of these issues will impact "thousands" of companies.[24] Further, the online music marketplace has changed substantially since Congress amended Section 115 to include DPDs and iDPDs, including the recent advent of vertically integrated content development and distribution companies. In such situations, Congress is the proper forum, as the Copyright Office stated, to "balance the specific concerns of the interested parties and enact a legal regime that addresses those concerns."[25] Napster's Interim CEO Hank Barry echoed these concerns in his recent testimony before the Senate Judiciary Committee on April 3, 2001.[26] At that time, Mr. Barry noted that the complexities surrounding the licensing of music for online distribution that result from the many potential licensors for any given work warranted Congressional intervention in the form of a compulsory license system.[27]

Congress already has begun to explore these issues in the form of two separate Senate Judiciary Committee hearings[28] and a May 17th hearing before the House Judiciary Committee. Further, DiMA and MP3.com both noted that Congress actually is the proper forum to resolve some of the issues related to online music distribution services.[29] Accordingly, Napster urges Congress to continue its examination of these issues and determine the proper application of the mechanical compulsory license to Limited Downloads.[30]

V. Should the Copyright Office Initiate a Rulemaking, It Should Determine that Limited Downloads are iDPDs and that Limited Downloads are Defined to Include Peer-to-Peer Limited Download Business Models.

Napster recognizes that the Copyright Office may choose to undertake such a proceeding and, as such, offers the following arguments related thereto.

---

[24] *See* RIAA Petition, at 13.

[25] *See* Notice of Inquiry, *In the Matter of Mechanical and Digital Phonorecord Delivery Compulsory License*, 66 FR 14099 (March 9, 2001), Docket No. RM 2000-7, at 14099.

[26] *See* Testimony of Hank Barry, Interim CEO, Napster, Inc., "Online Entertainment: Coming Soon to a Digital Device Near You?" United States Senate, Committee on the Judiciary, April 3, 2001.

[27] *See id.* at 10.

[28] Napster Interim CEO Hank Barry testified before the Senate Judiciary Committee on July 11, 2000, and April 3, 2001, on a number of issues related to the emerging online music distribution market. Mr. Barry's testimony for the July 11, 2000, hearing is attached as Appendix A.

[29] *See* MP3.com Comments, at 7; DiMA Comments, at 3.

[30] It also is important to note that at the recent House Judiciary Committee hearing on online music distribution, Representative Cannon questioned whether the Copyright Office had the requisite authority to initiate a rulemaking proceeding. *See* Comments of Representative Chris Cannon, "Oversight Hearing on Music on the Internet," United States House of Representatives, Committee on the Judiciary, May 17, 2001.

Definition of Limited Downloads

Napster's service involves the exchange of online music files via digital downloads. The New Napster Service, set to launch this summer, will be a Limited Download service that will permit Napster users to: (1) track songs that are exchanged using the New Napster Service, thereby providing Napster with information necessary to compensate rights holders; (2) limit users' ability to transfer files to another device, in essence tethering the files to users' computers; and (3) control the sound quality through fidelity limitations.

Any Copyright Office proceeding involving Limited Downloads should adopt a definition for Limited Downloads that takes into account the many online music services being offered. More specifically, the Copyright Office should not limit the services that qualify as Limited Downloads merely to those that fit within the RIAA's proposed definition.[31] A more flexible approach might prove to be the most prudent. For example, the Copyright Office might want to consider a definition for Limited Downloads along the lines of: "a commercial on-demand transmission of a use-limited download (*e.g.*, available for listening for a limited number of times or a time certain, or limited by the file's sound fidelity or by a user's ability to transfer the file downloaded to another device) to a local storage device (*e.g.*, the hard drive of a user's computer) using technology that causes the downloaded file to be available for such limited uses without regard to the architecture of the service through which the transmission occurred." The Copyright Office should not define Limited Downloads, or for that matter iDPDs or DPDs, in a manner that prevents peer-to-peer file sharing companies that facilitate the transfer of Limited Downloads from being able to avail themselves of Section 115 simply because the music files are transferred via a peer-to-peer architecture.[32] Simply put, the Copyright Office should take care to ensure that all business models that facilitate the delivery of downloads meetings an objective definition for Limited Downloads will be able to avail themselves of the mechanical compulsory license for iDPDs.

---

[31] *See* RIAA Petition, at 1 (The RIAA defined the term Limited Download to include "an on-demand transmission of a time-limited or other use-limited (*i.e.*, non-permanent) download to a local storage device (*e.g.*, the hard drive of the user's computer), using technology that causes the downloaded file to be available for listening only either during a limited time (*e.g.*, a time certain or a time tied to ongoing subscription payments) or for a limited number of times.").

[32] There is no reason to think that Section 115 currently would not apply to Napster-like peer-to-peer services that enable their users to share music files, assuming that the Napster-like service complies with Section 115's requirements. More specifically, according to one noted copyright law commentator, a company may obtain a compulsory license on behalf of another. As such, there would not seem to be any reason why a peer-to-peer company would not be able to obtain a compulsory license that allows its users to share music files. *See Nimmer on Copyright*, Ch. 8, Sec. 8.04 (J)(1) (2001).

Limited Downloads as iDPDs

The RIAA takes the position that it is necessary to clarify whether the mechanical compulsory license embodied in 17 U.S.C. § 115 applies to Limited Downloads[33], and that valid arguments exist to support the notion that Limited Downloads are iDPDs.[34] For example, a DPD is defined as:

> "each individual delivery of a phonorecord by digital transmission of a sound recording which results in a specifically identifiable reproduction by or for any transmission recipient of a phonorecord of that sound recording..."[35]

This definition accurately describes the process by which a sound recording embodied in a phonorecord is digitally transmitted as a file via the Internet to a user's computer (*i.e.,* a download) and where no restrictions are placed on how that file can subsequently be used. It is clear, however, that a Limited Download does not provide consumers with the same benefits obtained through ownership of a physical phonorecord or a download that is not use-limited in any manner. As such, a Limited Download is an iDPD, as opposed to a general DPD -- the arguable equivalent of a physical phonorecord.

If the Copyright Office finds, however, that Limited Downloads are not iDPDs, Napster argues in the alternative that Limited Downloads are a subclass of DPDs. Pursuant to Section 115(c)(3)(D), the Copyright Office has the authority to set "rates and terms" for DPDs and iDPDs.[36] Napster argues that the reference to "rates and terms" suggests that the Copyright Office may set multiple rates and terms for various categories of DPDs and iDPDs. Therefore, if the Copyright Office determines that Limited Downloads are not iDPDs, it should conclude that Limited Downloads are a subset of DPDs subject to a lower rate than general DPDs due to the limitations inherent in such downloads.

Streamline DPD and iDPD Mechanism

Merely defining iDPDs without streamlining the procedures surrounding DPD and iDPD mechanical compulsory licenses to take into account the nature of the online music distribution market would not further the development of the online music distribution market.[37] As MP3.com notes in its Comments, the current procedures for

---

33 *See* RIAA Petition, at 3, 9-10; RIAA Comments, at 1.

34 *See* RIAA Petition, at 9-10; RIAA Comments, at 15-16. (The RIAA also argues that Limited Downloads may be phonorecords distributed by acts or practices in the nature of rental, lease, or lending pursuant to 17 U.S.C. § 115(c)(4). Napster does not support this view, as it assumes that all Limited Downloads are limited in use based on the time period or number of times during which a consumer may access that Limited Download. As described in more detail above, such a narrow definition of Limited Downloads does not take into account other online music download services that may limit consumer use in a different manner.).

35 *See* 17 U.S.C. § 115(d).

36 *See* 17 U.S.C. § 115(c)(3)(D).

37 *See* MP3.com Comments, at 8.

obtaining a mechanical compulsory license are not able to handle the enormous demands of music distribution companies. In particular, Napster agrees that the procedure for obtaining an iDPD mechanical compulsory license should not include the current burdensome mechanical compulsory license notice requirements.[38] Napster also believes the procedures for general DPDs should be streamlined as they apply to online music distribution services.

CARP Proceeding

Napster agrees with DiMA and the RIAA's Comments that, should the Copyright Office determine that Limited Downloads are iDPDs, the Copyright Office should initiate a CARP proceeding to establish the applicable iDPD royalty rate.[39] If the Copyright Office should determine that Limited Downloads are not iDPDs, the Copyright Office should then initiate a CARP proceeding to establish an applicable lower rate for Limited Downloads as a subclass of DPDs pursuant to its authority to set rates and terms for DPDs.[40]

VI. The Copyright Office Should Not Issue Interim Rules Without Allowing for Prior Notice and an Expedited Public Comment Period.

Napster believes that, notwithstanding its skepticism concerning the Copyright Office's jurisdiction to pursue the rulemaking advocated by the RIAA, the law and prudence dictate that any interim rules and safe harbor only be developed and promulgated in an open and public environment. Napster disagrees with the RIAA and MP3.com that the Copyright Office should issue interim rules to govern digital music service in relation to Section 115 while the Copyright Office conducts a rulemaking proceeding without first allowing for notice and expedited public comment on the interim rules.[41] Napster does not think that the current situation rises to a level that warrants the issuance of such rules without opportunity for notice and public comment and the benefits attendant to this notice and comment procedure.

Section 553 of the Administrative Procedures Act ("APA") requires that federal agencies issue rules after complying with the APA's prior notice and public comment provisions.[42] The public comment facet associated with federal agency rulemaking proceedings is extremely valuable. For example:

> Public input provides valuable information to rulemaking agencies at low cost to the agencies. Rules adopted with public participation are likely to be more

---

38 *See id.* at 8-9.

39 *See* RIAA Comments, at 4; DiMA Comments, at 6-7.

40 *See* 17 U.S.C. § 115(c)(3)(D).

41 *See* RIAA Comments, at 17-21; MP3.com Comments, at 10-11.

42 *See* 5 U.S.C. § 553.

> effective and less costly to administer than rules written without such participation. They contain fewer mistakes. They are more likely to deal with unexpected and unique applications or exceptional situations, and...serve fundamental democratic purposes.[43]

The APA's "good cause" exception allows agencies to dispense with the prior notice and public comment requirements when the agency "for good cause finds...that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest."[44] Court decisions and the APA's legislative history indicate, however, that the good cause exception is to be construed narrowly[45] in order to avoid providing agencies with an escape clause from the notice and comment requirements Congress prescribed.[46] Further, an agency must demonstrate that exigent circumstances exist in order to avail itself of the APA's good cause exception as "only in compelling situations will a court subordinate the values embodied in public participation."[47]

The current situation does not meet the APA's good cause exception. There undoubtedly exists consumer demand for online music distribution services, as evidenced by Napster's huge popularity, and there has been considerable criticism of the recording industry for not taking steps to meet this growing demand.[48] The lack of notice and public comment prior to the issuance of any Copyright Office interim or final rules threatens actually to hinder the online music distribution industry's development and remove any public benefit the rules otherwise would have created. More specifically, the lack of public comments could result in the Copyright Office issuing rules that do not adequately address the unique concerns of the many companies that would be impacted. The interim rules could, in effect, provide a competitive advantage to a handful of online music distribution companies and, as such, prevent competition in this nascent industry.

Further, the RIAA noted that these issues are particularly "apt for a rulemaking proceeding, where all interested parties can file comments on the issue and a rule can be issued *after consideration of these comments.*"[49]

---

43 *See* Michael Asimow, *Interim-Final Rules: Making Haste Slowly,* 51 Admin. L. Rev. 703, 707-708 (Summer 1999) (Asimow).

44 *See* 5 U.S.C. § 553(b)(3)(B).

45 *See* Asimow, at 718; *See also*, S. Doc. No. 79-404, at 200, 258 (1946) ("A true and supported or supportable finding of necessity or emergency must be made and published.").

46 *See, e.g., United States v. Garner*, 767 F.2d 104, 120 (5th Cir. 1985).

47 *See* Asimow, at 719.

48 *See, e.g.,* Statement of Don Henley, "Online Entertainment: Coming Soon to a Digital Device Near You?" United States Senate, Committee on the Judiciary, April 3, 2001 ("The record industry has fiddled on the sidelines while the digital revolution went on without them.").

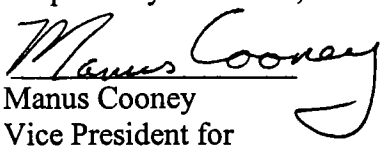
49 *See* RIAA Petition, at 13 (emphasis added).

VII. Conclusion.

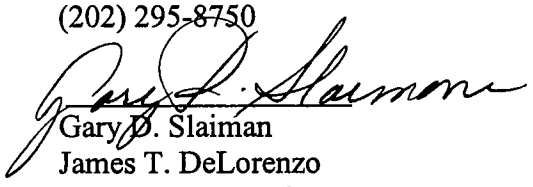
Napster wishes to note that the chief advocates for Copyright Office action are the trade association for the five major recording labels -- the RIAA -- and MP3.com, a soon-to-be major label controlled online music company. All other commentors have taken the position that many of the reforms sought by this small but powerful group of companies should be left to Congress to resolve. As such, the Copyright Office should not accept the RIAA's invitation to facilitate its members' apparent plans to vertically integrate the distribution of online music via a rule making of questionable credibility and propriety.

If, notwithstanding counsel to the contrary, it is determined that the Copyright Office may proceed, Napster would urge that any and all rules -- including any interim rules -- be vetted through a public notice and comment period, and that they be crafted in a manner so as to facilitate the deployment of various online music services, regardless of whether they are controlled by the existing major recording labels. Specifically, Napster submits that if the Copyright Office does initiate a rulemaking on these issues, the Copyright Office should define iDPDs to include within the definition's scope Limited Downloads. Further, the Copyright Office should make clear that the term Limited Downloads extends beyond the limited download business model that RIAA members have to date advocated. Rather, Limited Downloads should be interpreted to include a broad but predictable range of music sampling or promotional services without regard to the services' respective architectures.

Respectfully submitted,



Manus Cooney
Vice President for
Corporate and Public Policy Development
Napster, Inc.
3000 K Street, N.W., Suite 125
Washington, D.C. 20007
(202) 295-8750



Gary J. Slaiman
James T. DeLorenzo
SWIDLER BERLIN SHEREFF FRIEDMAN, LLP
3000 K Street, N.W., Suite 300
Washington, D.C. 20007
(202) 424-7707
Counsel for Napster, Inc.

May 23, 2001

Appendix A

Testimony of Hank Barry
Chief Executive Officer
Napster, Inc.
Before the Senate Judiciary Committee
Remarks Prepared for Delivery
July 11, 2000

Good morning and thank you for inviting me to appear before you today. I am Hank Barry, Chief Executive Officer of Napster, Inc., and I represent the Company and members of the Napster community. I would like to recognize Shawn Fanning, the inventor of Napster, who is sitting behind me.

This Committee is at the center of the great Constitutional debates of our country and the protection of the rights we cherish as Americans. In the coming years, your Committee will continue its important oversight of the legal issues in the Internet world, and I greatly value the opportunity to contribute to that endeavor.

Let me begin with a general point on which everyone in this room can agree: Americans love music, and Americans are listening to and making music like never before.

Record sales and music radio listening are up; school bands, choirs and drum and bugle corps are back.

Napster's success reflects that love of music. As of this morning, after less than a year, without any advertising or promotion, Napster has attracted nearly 20 million users. Over half of them are over 30 years of age and they are evenly split between men and women. In the evenings, we consistently have about 500,000 people using the service simultaneously. By comparison, that is about one third of the number of people using America Online at the same time.

I would like to talk with you today about Napster's technology, Napster's impact, and Napster's future.

Andy Grove, the Chairman of Intel, recently said "the whole Internet could be rearchitected by Napster-like technology." Let me try to place his observation in some historical context.

As you know, the Internet began as a redundant communication network among scientists involved in defense research. They needed to reliably share information that was distributed all over the system. The commercial use of the Internet for media purposes abandoned this structure. Instead, Internet companies adopted the broadcasting

model, with large centralized computers "serving" information to the consumer's PC as if it were a television receiver. Serving, not sharing, became the dominant approach.

Shawn Fanning began a revolution that is returning the Internet to its roots. Napster is an application that allows users to learn about others' tastes and share their MP3 files. If users choose to share files - and they are not required to - the application makes a list of those files, and sends the list and only the list to become part of the central Napster directory. The Napster directory, then, is a temporary and ever-changing list of all the files that members of the community are willing to share.

Users can search that list, comment on the files on others' computers, see what other people like, and chat about all this.

They do this all for no money, expecting nothing in return, on a person-to-person basis. That's it.

Napster does not copy files. It does not provide the technology for copying files. Napster does not make MP3 files. It does not transfer files. Napster simply facilitates communication among people interested in music. It is a return to the original information sharing approach of the Internet, allowing for a depth and a scale of information that is truly revolutionary.

Napster is helping, not hurting, the recording and music publishing industry and artists. A chorus of studies shows that Napster users buy more records as a result of using Napster and that sampling music before buying is the most important reason people use Napster.

Users who transfer more than 20 files soon delete over 95% of those files. In the last 6 months record sales are up more than 8% from the previous year -- an increase of more than one billion dollars a year. Like other advances in technology, what Napster shows is that more access to music leads to more interest in music.

Lawsuits against Napster contend that our 20 million users, the recording and music publishing industry's best customers, are guilty of copyright infringement. We strongly disagree. Copyright is not absolute. It has limits.

Companies that hold copyrights on behalf of creators, and which control distribution of creative works, have a strong inclination to change the copyright laws from a balanced vehicle for public enrichment to an unbalanced engine of control. Copyright holders traditionally are reluctant to allow new technologies to emerge.

This Committee's hearing records are replete with examples of new technologies struggling to survive as copyright holders argue that these new technologies will impede their ability to be compensated for copyrighted works. You and the courts have allowed -- over their objections -- technological advances like radio, the cassette player, cable

television, and the VCR -- advances which proved to be a financial boon to these same concerned copyright holders.

Napster can work with the recording and music publishing industries. We remain enthusiastic about creating a market-based solution that will benefit consumers, artists, and the traditional recording and music publishing companies. Since my first day on the job, I have been reaching out to the major recording and music publishing labels.

In conclusion, we should not brand as thieves the 20 million Americans that enjoy the Napster service. Instead, we should let history be our guide.

Americans love music. Every time a new technology makes it easier for listeners to discover, enjoy and share music, the recording and music publishing industry benefits. Thank you for your time and attention today.

Testimony of Hank Barry
Chief Executive Officer
Napster, Inc.
Before the Senate Judiciary Committee

Introduction

Good morning and thank you for the opportunity to appear before you today to discuss music and the Internet. I am Hank Barry, Chief Executive Officer of Napster, Inc., and I am here today on the Company's behalf and on behalf of the members of the Napster community.

I am honored to be here today. Both through your jurisdiction and your historical concerns, this Judiciary Committee has been at the center of the great Constitutional debates of our country and the protection of the rights we cherish as Americans. In the coming years, your Committee will continue its important oversight of the laws that govern how we handle delicate copyright issues in the Internet world, and I sincerely value the opportunity to contribute to that endeavor.

Napster is a revolutionary technology based on person-to-person, non-commercial file sharing. It was invented in 1999 by Shawn Fanning, then a college freshman, who is seated behind me today. In less than a year, without any advertising or promotion, Napster has attracted millions of users of all ages and backgrounds, while gathering praise from Internet experts for its technology and contributions to the on-line community. As Andy Grove, former Chairman of Intel, recently stated, "The whole Internet could be re-architected by Napster-like technology."

We at Napster respect and believe in the copyright laws and the values – both public and private – that they are designed to promote. We believe that copyright can

successfully take into account new technologies and innovations, and that Napster and its millions of users throughout all fifty states are operating in compliance with the law. The core issue is not copyright, although the recording and music publishing industry, struggling to overcome its late entry into the Internet economy, is attempting to paint it as such in court. The real issue concerns business models.

My remarks today will address these technology, copyright and business issues.

The Technology

Two key elements of context are essential to understanding Napster's technology. The first is the current architecture of most Internet information. The second is the technology related to music that is not part of Napster, but which is the enabling foundation that allows Napster and similar architectures to exist.

Congressional support for DARPA was central to the beginning of the Internet. Essentially, the Internet was set up as a redundant communication network among scientists, many of whom were doing defense related work. Using the Internet, they could share that information via a system that would continue to allow communication even in the event a great portion of the physical infrastructure were destroyed.

We have only begun to explore the potential of the Internet for person-to-person communication. With notable exceptions like e-mail, instant messaging and chat rooms, the Internet has largely been used to create an experience for users that is similar to television. We have taken the broadcast tower and replaced it with large computers that

"serve" information to the consumer – and we have relegated the personal computer, which is increasingly powerful, to little more than a receiver of text, pictures and sound from the "broadcasting tower" web site. This "client/server" architecture tracks the broadcasting model, but it does not in my opinion take advantage of the fundamentally interactive nature of the Internet.

Concurrently with the adoption of this client/server architecture, developments in computer technology have greatly affected the way millions of people listen to music. Napster contains none of this technology, but without it the Napster community could not exist.

In the early 1980s, Sony and Phillips promulgated the "Red Book" standard for making compact discs. As the recording and consumer electronics companies (and some companies were both) adopted this standard, we moved from a world where analog recordings were published on analog media, such as vinyl records and cassettes, to a world where music is represented by ones and zeros. Since their inception, both the Microsoft Windows and Apple Macintosh operating systems have supported the copying of any digital file, regardless of type. This effectively allowed people to copy CDs onto the hard drives of their computers. However, since the files for a song on a CD were on the order of 40 to 50 megabytes of data per song, this was not at all practical at that time.

In 1987, the Motion Picture Experts Group, an industry standards group that included representatives of the recording and music publishing industry, promulgated the MP3 standard for taking these large digital files and compressing them into smaller files (approximately 3 to 4 megabytes per song). These smaller files could more easily be stored on a computer, processed by a computer and transferred between computers over

the Internet. The file is decompressed for listening by "player" software, but because of the compression, the sound quality is not as good as that of a CD.

About four years ago, newly available software applications combined the steps of copying the file from the CD and compressing the file into the MP3 standard format. At the same time, the average speed of an Internet connection increased. People found that if they had a relatively fast Internet connection, the smaller MP3 file format allowed them to effectively transfer digital versions of sound recordings. They did this via e-mail, so-called FTP file transfer software and many other means. This usage was promoted as an important feature by all the leading Internet service providers.

In sum, the ability to listen to music digitally depends on the ability to copy audio files into a computer, compress them into the MP3 format and transfer them over the Internet. Napster does none of these things. So why all the fuss about Napster?

Napster is an application that allows users to learn about others' musical tastes and share their MP3 files. If they choose to share files – and they are not required to – the application makes a list of the files designated by the user and sends the list to become part of the central Napster directory. The Napster directory is a list of all the files that members of the community are willing to share. Users can search that list, comment on the files on others' computers, see what other people like and chat about all this. If they want to and if the other person is then online, they can share the files designated as "shareable." This is accomplished by a file transfer from one person's computer directly to another's. They do this for no money, expecting nothing in return, on a person-to-person basis.

That's it. Napster is an Internet directory service. Napster does not copy files. It does not provide the technology for copying files. Napster does not compress files. It does not transfer files. Napster simply facilitates communication.

Napster is a throwback to the original structure of the Internet I described above. Rather than build large servers, Napster relies on communication between the personal computers of the members of the Napster community. The information is distributed all across the Internet, allowing for a depth and a scale of information that is truly revolutionary.

The Napster method of person-to-person, non-commercial file sharing is a new tool, a new way of sharing information. All new tools change the way we do things, and that often upsets the established order. In the case of Napster, the established order is the recording and music publishing industry. When presented with this new tool, the industry reacted by attempting to crush Napster, as it has tried to do with other technologies in the past. As it has before, the industry has sought refuge in the copyright laws.

Napster Respects and Believes in the Copyright Laws

Napster believes in copyright and its benefits to society. Napster believes that copyright law can work well in the new Internet environment, and foster innovation and technological advances like file sharing, so long as we do not lose sight of what the copyright law is truly meant to protect.

Copyright is a tool of public policy; it does not vindicate a private right. The copyright laws are meant to find the balance between the "embarrassment of a monopoly" – to use Jefferson's term – that we offer to authors in order to encourage their production of works, and the public interest that otherwise would not allow such a monopoly to occur. Copyright is therefore an incentive we as a society grant so that we may have better access to more original expression. In the end, the copyright laws are for the benefit of the public as a whole, not the individual copyright owners. The balance requires that these rights be limited so that we as a society can share, grow and build upon one another's creativity. But that balance is always at risk in the struggle between copyright absolutists and those who think more limited protections are appropriate.

Companies that hold copyrights on behalf of creators, and which control distribution of creative works, have a strong inclination to extend copyright into a complete monopoly control over the creative work – to change the copyright laws from a balanced vehicle for public enrichment to an unbalanced engine of control. As a result, copyright holders traditionally are reluctant to allow new technologies to emerge. This Committee's hearing records are replete with examples of new technologies struggling to survive as copyright holders argue that these new technologies will impede their ability to be compensated for copyrighted works.

Faced with these innovations and the copyright holders' protests against them, Congress has repeatedly maintained the correct balance, whether by only granting a limited term for copyright, by codifying the fair use doctrine, or most recently, by recognizing the right of individuals to make digital or analog copies of musical works for noncommercial purposes.

As a result of decisions made by Congress and the courts, technological advances like radio, the cassette recorder, cable television and the VCR have survived copyright holders' attacks and, in the end, proved to be a financial boon to these same concerned copyright holders. The fact that this is true can be demonstrated by the statement made by Jack Valenti, the President of the Motion Picture Association of America, in the context of the Sony Betamax litigation. At that time he testified before Congress that the VCR was to the movie industry "as the Boston Strangler is to a woman alone." Sixteen years after Valenti's statement, the movie industry is thriving as never before. U.S. box office receipts in 1999 reached $7.5 billion, their highest level ever. All of this in spite of an 85.1% VCR penetration rate in U.S. households. By all accounts, the VCR has enormously helped the movie industry, and now accounts for more than half of the industry's revenues.

It is my firm belief that the consumers who use Napster are *not* committing copyright violations. Let me clarify that point. Nobody, not even the recording and music publishing industry, is saying that Napster is committing direct copyright infringement. Instead, they are saying that the millions of people who use Napster, the hundreds of thousands of citizens in every state, are copyright infringers. It is the fundamental premise of their suit against Napster that, by engaging in the very conduct – music sharing – that the recording and music publishing industry has known about and encouraged for many years, your employees, your colleagues, your friends, your family members and your constituents are violating the law. We disagree, and believe that the vast majority of Napster users appropriately operate in a non-commercial manner within the bounds of the copyright laws. Napster's view on this issue is based on a review of

the copyright statutes, court decisions and the expert opinions of copyright scholars. In that regard, I would refer you to our brief on this subject in opposition to the current preliminary injunction sought by the recording industry plaintiffs.

After years of uncertainty surrounding the copying of records for non-commercial use, in Section 1008 of the Copyright Act, Congress sought to clarify that consumers could make copies for noncommercial use without fear of violating copyright laws. Today these same people are flocking to Napster. The music industry should embrace these users for who they are, the industry's most loyal consumers of music.

Further, even if one were to assume that some Napster users were violating copyright law, Napster would still not be liable for any copyright infringement pursuant to the landmark Sony Betamax decision. The Betamax case recognized that Sony's offering of the Betamax VCR did not constitute copyright infringement because the Betamax was capable of non-infringing uses, such as copying for time-shifting purposes. Napster allows similar uses. For example, Napster users often transfer an MP3 file onto their hard drive as a complement to a CD they already own. Further, studies show that Napster users share songs as a way to sample music before purchasing it, including music that the user would not normally consider buying. Finally, Napster provides a critical link between new artists and the public. Too much creative talent fails to get through the recording and music publishing industry filter. Lack of recording contracts and radio play should not deny creators from finding an audience. Napster is a great way for fans to find the music of artists they read about or hear play at a local club.

Technological Change Will Impact the Distribution of Music

The Internet revolution of which Napster is a part challenges many companies. Often, existing methods of distributing goods and services are at risk of being supplanted by new, more efficient and vibrant Internet-based distribution systems. As a result, businesses try with varying levels of success to adapt to the new environment the Internet economy is still in the process of creating. These existing companies take one of two approaches. Some embrace the new economy and mold themselves into Internet-friendly companies. For example, UPS, FedEx and WAL-MART are all examples of companies with significant pre-Internet market share that are actively adapting to the new Internet environment. Others, however, seek to exploit their position in the existing market to dominate the development of this vibrant new market space. In other words, these companies attempt to protect themselves by keeping down innovative Internet technologies.

That is exactly what is happening here. The recording and music publishing industry has known of the technology for creating and distributing MP3 files for years. Yet they have chosen not to take any actions to stop or even slow this widespread proliferation. Indeed, the recording and music publishing industry actively encouraged this proliferation by forming partnerships with and investing in companies that direct consumers to MP3-encoding software that will enable them to transfer music files over the Internet. They did this because they knew that rather than hurting their sales, as they now claim, MP3s on the Internet in fact help their sales. The recording and music publishing industry's goal in attempting to crush Napster appears to be to retain control

over the flow of competing unsigned artists' music into the marketplace, and the means of and business model of distributing music over the Internet.

Despite all this, we at Napster remain enthusiastic about the possibility of working with the recording and music publishing industry to create a market-based solution that will benefit consumers, artists, Napster and the traditional recording and music publishing companies alike. Before my arrival, Napster's attempts to negotiate with the industry were at first seemingly welcomed, but then, while talks were still continuing and without notice, the recording companies sued. Nevertheless, since my first day on the job, I have been reaching out to the major recording labels. Ironically, all this is occurring in an environment of steadily increasing record sales.

Recording industry statistics show that the music business is booming. For example, according to the RIAA, U.S. CD sales increased 11% in 1999 to a dollar value of $12.8 billion, and are up 8% for the first quarter of 2000 compared to the same time period last year. These figures discredit a study commissioned by the RIAA in the litigation that attempted to show that sales of CDs near certain colleges from 1997 to 2000 had gone down. That report focused on declining sales at these selected stores over that time period, but failed to take into account the fact that Napster did not even exist until late 1999, and that big box and online retailers probably played the most significant role in any declining sales that may have occurred at these selected college stores.

In fact, numerous studies show that Napster users are more likely to buy CDs after using the Napster directory service. For example, a recent study showed that 28.3% of users who have transferred files using Napster have increased their CD purchases, as

opposed to only 8.1% whose purchases have decreased. In addition, a Pew Foundation report found that people are going out and purchasing music they first sample online. Further, more than half of all users use Napster to sample songs before purchasing them, and 42% of these samplers actually purchase more CDs as a result. In fact, one study of college-aged users showed that over 95% of all files that are shared between those Napster users are soon erased, supporting the view that Napster is a sampling and listening experience, and not a permanent copying experience that could displace conventional CD sales. The excitement that Napster creates for new and established artists is helping to drive increased sales, reaping even greater profits for the recording and music publishing industry.

Further, far from hurting the creative community, Napster is offering thousands of artists a new and effective distribution system for their work. Last year, the major recording labels released only 2,600 albums. In contrast, in the past four months Napster has signed over 17,000 artists to participate in its new artist program, more than 7,500 of whom reside in the states represented by members of the Judiciary Committee. Through this program and Napster-run chat rooms that allow users to discuss new artists and songs, Napster provides independent artists an inexpensive, alternative method of promotion. In one case, a student at the University of Florida posted his songs on Napster. The ensuing buzz resulted in increased sales of his CD on his own web site, which allowed him to partially fund his college tuition.

In an industry where a few large companies operate as the gatekeepers to the American listening public, artists clearly see Napster as a revolutionary way to gain access to those who would not otherwise have a chance to appreciate their work. Jim

Guerinot, an industry veteran who currently owns the Time Bomb recording label and is personal manager for The Offspring, a multi-platinum-selling rock band, has said: "It is the band's and their manager's opinion that allowing fans of The Offspring to hear their music on Napster will make fans more, not less, likely to purchase the group's records, T-shirts and other merchandise, and attend live performances by the band....The Offspring view Napster as a vital and necessary means to promote music and foster a better relationship with fans."

In conclusion, we should let history be our guide. Every time a new technology makes it easier for listeners to discover, enjoy and share music, the recording and music publishing industry ends up benefiting. In the end, artists, the industry and new technologists will create a solution that benefits consumers, artists, Napster and the recording and music publishing industry. Until that time, however, we believe it would be rash to construe or change existing laws in such a manner as to destroy Napster. To do so would brand as thieves the millions of music lovers throughout the United States who have come together to share and enjoy music on Napster and the Napster community will disappear. I hope you in Congress will watch closely these developments and I thank you for your time.

Appendix B

TESTIMONY

OF

HANK BARRY

INTERIM CEO

NAPSTER

HEARING BEFORE THE SENATE COMMITTEE ON THE

JUDICIARY

UNITED STATES SENATE

ON

ONLINE ENTERTAINMENT: COMING SOON TO A

DIGITAL DEVICE NEAR YOU

TUESDAY, APRIL 3, 2001

Mr. Chairman and members of the Committee, thank you for inviting me to appear before you today. I am happy to be here on behalf of Napster and all the members of the Napster community. As I did last time I was here, I would like to take a moment to acknowledge Shawn Fanning, the founder of Napster, who is sitting behind me today. He was 19 then. He is 20 now – and despite his advanced years, he is not yet over the hill.

I think no one in this room - even those with whom we have disagreed vigorously - would contest that accessing music over the Internet is something that tens of millions of people, young and old, love to do. Over half of Napster's users are over 25, and they come from all walks of life. The question before us today – from all of our very different perspectives and responsibilities -- is what does it take to make music on the Internet a fair and profitable business.

To realize this goal, I believe it will take an Act of Congress – a change to the laws to provide a compulsory license for the transmission of music over the Internet. And today I will tell you why I strongly believe such a change is necessary, an important step for the Internet, and why it will be good for artists, listeners and businesses.

Negotiation History

When I last testified before this Committee last July, I did not believe this issue required a legislative solution. I believed that Napster should find a private contractual solution

that the rights holders and the people who use Napster could all support. We said "let the marketplace work."

Since that time the Napster community has continued to grow. We then had 20 million members; we have grown to more than 60 million members today, even as we aggressively comply with the District Court's injunction.

Since people who use Napster buy more music than others and are very willing to pay for music over the Internet, I believed there was a basis for making an agreement with the record and music publishing companies. We built our business model around this idea: that the people using Napster want artists and songwriters to be paid, and that peer-to-peer Internet technology is the most efficient and convenient way ever devised to make music accessible.

I have tried for the last 9 months to make an agreement under which Napster can get a license from the record companies and the music publishers. I believed that any such agreement would serve as a precedent for other agreements and could serve as the basis for payments by the people using Napster to recording artists and songwriters. We were able to reach agreement with Bertelsmann on a business model for a new service and license terms for the sound recordings and the musical compositions they control. Yet I cannot today report that any other such agreement has been reached with a major label.

Perhaps I should not have been surprised at this result. Although the World Wide Web portion of the Internet has been around for 7 years, and billions of investor dollars have been spent founding and attempting to grow technology companies and consumer companies that would help all of us access music over the Internet, to this date no service has been able to provide a comprehensive offering of music on the Internet that is licensed by the major recording and publishing companies.

For the record companies, the promise of music over the Internet has always been "coming real soon now". Every time this Committee holds a hearing on these issues, new promises of imminent progress are made. Just last July, Fred Ehrlich from Sony told this Committee "we are in active conversations" with both eMusic and mp3.com. But, once again, these have turned out to be empty statements.

The DMCA was supposed to solve many of these problems. As Chairman Hatch said in the last hearing of this Committee on this issue:

"In short, it was believed that a stable, predictable legal environment would encourage the deployment of business models which would make properly licensed content more widely available. Sadly, this has not yet occurred to any great extent in the music industry, and the DMCA is nearly two years old."

Look at the facts. Where are the Internet businesses with clear and complete recording and music publishing licenses? There are none. Where are the emerging digital media companies with negotiated agreements with all rightsholders? There are none.

And of course these companies argue that this is Napster's fault. That argument might be granted some validity if there were even one fully-licensed business with anything approaching a comprehensive consumer offer. But there are none.

We might all well ask - why is this so complicated? Why can't the record companies and music publishing companies just issue licenses to eMusic, Liquid Audio, Listen.com, Yahoo, MSN and Napster, and everyone else, so consumers can pay money and have access to music over the Internet, while ensuring that artists and songwriters are paid? Why have the record and publishing companies continually said they are going to license, and then not followed through?

Well, one obstacle may have been a lack of will -- the record companies have stated repeatedly that they believe that licenses of sales over the Internet will cut into physical goods sales and generally damage, not increase, their business. This fear, of course, has not been founded in reality to date. CD sales are stronger than other retail, even in the face of uncertain economic times. Internet music has increased interest in music as a whole. Like the VCR, the cassette, and every other major innovation, Internet music has been greeted by a chorus of doom from existing distributors. But let's assume that the

will is there to license music over the Internet – certainly all of the record and publishing companies represented on this panel now say they want to move forward in this area.

Even if we assume that everyone agrees that licensing music for the Internet would be a good thing, my experience is that it is an almost impossibly complicated thing. And unfortunately I have to explain how complicated it is by going over the rights structure in this industry. So if you will let me do that . . .

Industry Overview

This background description here is for those of you who are not copyright lawyers. Bob Kohn of eMusic wrote a great book on this if you want further information.

As the members of this Committee know, when you buy a CD or tape, you are really getting copies of two separate works. The first is the sound recording that the artist and producers and musicians made in the studio. The second is the musical composition, the song that is being played. By law, each copy of the CD is also considered a reproduction of that musical composition. The complex part about this is that the sound recording and the musical composition that is sung on the sound recording (the "song" – the music) are almost always owned by different companies, even where, as in many cases, the recording artist is the same person who wrote the song.

Now if you are trying to make music available to the public on the Internet, whether for download or streaming or even for broadcast, and if you need a private contractual

agreement to do that, then you have to negotiate with both sets of rightsholders – the record companies and the music publishers. First you have to go to the record companies (and if you want the good stuff, like polkas and Lithuanian folk songs, you have to go to many record companies - there are over 3,000 record companies in the US alone).

And when you have negotiated each of those 3,000 separate agreements, you are only half way there – because then you have to go and negotiate with all of the music publishers – and there are over 25,000 independent music publishers in the US alone. Mr. Murphy's organization represents many of them, but I believe Mr. Roberts from MP3.com would tell you that anything less than an overall comprehensive license to all compositions doesn't do you much good, because the likelihood is that rights you have and the rights you need will not match at all. And even one failure to match can bring down the whole structure.

This is further complicated by the fact that several of the largest music publishers, controlling millions of songs, are owned by the record labels, but the music publishing catalogs they control bear no relation to the sound recordings they control – they are not the same songs. For a final complication - the music publishers have two separate rights, the right to make a mechanical copy of the song and the public performance right, that may both be implicated in this type of licensing. And each of those rights is administered for them by a different rights organization.

Now, as you know Senator, that is a simplified statement of the rights structures in this industry.

Compulsory Licenses

So, what can Congress do to simplify this in a way that will work?

Well, here – at the center of the matter – I find myself in surprising agreement with a perceptive recent analysis by the RIAA.

Vivendi Universal and the National Association of Music Publishers are in a dispute based on the fact that Universal made musical compositions available online without getting the publishers' permission. The RIAA has gone to the Copyright Office seeking guidance as to whether Section 115 of the Copyright Act applies in such circumstances. The RIAA articulates a compelling case for the need for compulsory licenses. The RIAA says that two fundamental problems limit access to music on the Internet: first, that independent sequential negotiations with all rights holders (like those I described a minute ago) are practically impossible in any reasonable time frame. Second, they say that the laws regarding rights are unclear.

It's an argument I would like to examine with you in some detail.

So let me quote now from the RIAA's Petition. I have attached the entire Petition to my testimony.

The RIAA said: "To the extent that On-Demand streams and Limited Downloads make use of musical works, it is right and proper that songwriters and music publishers receive a reasonable royalty, as appropriate and as provided under existing law. RIAA's member companies are ready and willing to pay reasonable applicable royalties for the services they operate or authorize."

[so far so good]

A few paragraphs down, they continue.

"To be compelling to consumers, it is believed that a service must offer tens or hundreds of thousands of songs, in which rights may be owned by hundreds or thousands of publishers. No service provider is eager to embark on individual negotiations with all those publishers unless it is necessary."

[well - that's my experience too. Continuing...]

"The music industry is unique among owners and users of copyrighted works in that reproduction and distribution of musical works has been subject to a compulsory license since 1909. In the nearly a century that the mechanical compulsory license has existed, it has become the foundation of business practices that are deeply ingrained in the industry and have been embraced by the copyright owners whose works are subject to it."

"... the availability of a compulsory license has ensured that necessary rights can be obtained, when needed, at a known price, and pursuant to established procedures. Recognizing that the business practices founded upon the compulsory license extend to On-Demand streams would avoid the need for individual negotiations on a scale that is unprecedented in the industry and thus facilitate the launch of On-Demand Streaming services..."

"The lack of clarity as to the issues described above has become the primary obstacle to the launch of digital services designed to meet ever-increasing consumer demand.... Representatives of the RIAA and its members have negotiated with representatives of music publishers concerning the licensing of services that would offer On Demand Streams and Limited Downloads. However, in large part because of the uncertainty as to the fundamental questions of law addressed above, these negotiations have not yet successfully resolved the matter."

In short, the RIAA's position is that Internet music is a mess because everyone involved asserts complex and varying rights, that there are too many potential licensors for "independent sequential negotiations", and that the best way for the market to move forward quickly and fairly may be a compulsory license for musical compositions.

That is the official position of the RIAA – and I endorse this principle. But I endorse it not just for musical compositions – but for sound recordings as well. Not just for music publishers, but also for record companies.

Do they Work? Examples of Compulsory Licenses

As the RIAA says, compulsory licenses have a long history of success, allowing for the widespread implementation of a new technology while ensuring that rights holders are compensated. Congress has repeatedly used such licenses as a way of advancing public policy goals in the context of new and frequently inefficient marketplaces. Compulsory licenses have encouraged beneficial new technologies, and responded effectively to particular market failures – including excessive contracting costs and anticompetitive market structures.

Let's look at some examples:

In 1909, Congress created a right against the reproduction of musical compositions in mechanical forms (*i.e.*, piano rolls), but limited this right through the creation of a mechanical compulsory license for musical works. The legislative history behind the mechanical compulsory license reveals that Congress enacted this provision, not only to compensate composers, but to prevent the Aeolian Company, which had acquired mechanical reproduetion rights from all of the nation's leading music publishers, from limiting the dissemination of the music to the public through the creation of a monopolistic environment. Thanks to this, once a song has been recorded by anybody, it may be recorded by anyone else, without a further license from the music publisher, if the person making the new recording notifies the publisher and pays a statutorily mandated royalty based on the number of copes made. That's where "cover" songs come from –

and only those of us who have heard different versions of "Louie Louie" can appreciate what that compulsory license has meant for American music.

Years later, Congress again enacted several additional compulsory license, this time related to consumers' ability to access broadcast transmissions via cable and satellite systems. In 1976, Congress passed a compulsory license for cable television systems that retransmit copyrighted works. Pursuant to the compulsory license provision, copyright owners are entitled to be paid prescribed royalty fees for a cable television company's secondary transmission of the copyrighted work embodied in television and radio broadcasts.

Then, in 1988, Congress passed the Satellite Home Viewer Act of 1988 (SHVA), which created a compulsory license system for satellite carriers that retransmit television broadcasts that operates similar to the cable compulsory license. Congress acted again in 1999 when it expanded the SHVA's scope to include local-into-local retransmission.

Congress recognized the ability of these then cutting edge technologies to further disseminate to the public television and radio content, and the need to ensure that rights holders remained adequately compensated. Congress understood, however, the inefficiencies inherent in forcing cable or satellite providers to negotiate individual licensing agreements, thereby resulting in the use of a compulsory license system.

Interestingly enough, considering the current controversy, Congress' next foray into compulsory licenses applied specifically to music. The Digital Performance Rights in Sound Recordings Act of 1995 created a limited performance right for sound recordings, subject to a compulsory license for certain digital audio deliveries of sound recordings. The compulsory license originally applied, in general, to non-interactive satellite and cable audio digital deliveries. The Digital Millennium Copyright Act amended the original law to explicitly include non-interactive webcasting of sound recordings within the compulsory license's scope.

At the time, Congress reasoned that these new technologies promised to encourage the widespread dissemination of this music to the public. Once again, Congress enacted the compulsory license mechanism as a means to ensure that artists and other rights holders were compensated, while not hindering the continued development and deployment of these digital delivery systems.

Finally, I think we can all agree that AM and FM radio have been good for recorded music. The benefits of radio have flowed from the effective compulsory license created by performing rights societies, such as ASCAP and BMI. They enforce songwriters' and music publishers' performance rights through a court created process that removes the need to negotiate with individual rights holders. While Congress did not create this procedure, it has implicitly endorsed it by recognizing these performing rights societies in recent legislation. Further, Congress repeatedly has refused requests to outlaw the use of these blanket licenses.

In all of these cases of compulsory licensing, creators benefit from, but do not completely control, the distribution of their product. A balance is struck – a balance that is at the heart of all intellectual property law. Remember, intellectual property is not the same as real property or personal property – copyright is a limited right. Copyright is not based on a private right of the individual, it is a creation of and a tool of public policy. It requires a constant balance between the public's interest in promoting creative expression and the public's interest having access to those works. This is a balance that has often proven impossible to find without the help of the Congress.

Important Elements of Any Licensing Regime for Internet Music

Let me offer a few specific elements that I think are important for a fair and equitable compulsory license law.

Any such solution has to apply to the entire catalog of the applicable rightsowner, whether record company or music publisher. Too often companies have entered into licensing arrangements that contain a clause saying that the subject matter of the license will be decided "later, when the rightsholders can determine what rights the rightsholder owns and can license." This process, which is generally know a "rights clearances" is often used to transform what looks like a real license into an empty shell.

Any such solution should also offer licensees both the sound recording rights and the musical composition rights. As we have seen above, it makes no sense for a licensee to have a sound recording license, and then have to begin negotiating with all the publishers.

Any technology requirements for copyright management and security have to be general enough so that they are capable of being fulfilled by many vendors. Private licensing regimes have been recently reported which would violate this basic principle of neutrality, by linking access to rights to the use of particular software – even as there are interlocking financial arrangements between the rightsholders and the software companies. ASCAP cannot tell a radio station what brand of transmitter to use; and no such new technological extensions of market power should be a part of any new licensing.

The licensing terms under any compulsory licensing system must be the same for all. I am particularly concerned here about a point Senator Hatch made at our hearing last July, that he was concerned that the major record companies would make cross-licensing arrangements among each other that would have economic terms that would ensure that the Internet services the record companies operate would have greater profits than any other licensed services.

Benefits to All Artists

We must be careful to construct a structure that will allow all recording artists, songwriters, record companies and publishers, not just the few large entities, to

participate and profit from music on the Internet. I believe that the great strength of American music is as much in choral, gospel and inspirational music bands, as it is in the latest Top 40 hits. Certainly a 10 minute walk through the shared files of Napster users suggests the same. We all listen to everything. And so all independent labels and publishers should participate as well.

Finally, I think we should adopt a direct Internet rights payment to artists. There is certainly precedent for this in the so-called "writer's share" of public performance (radio and television) payments that are made by ASCAP and BMI. As you know, a portion of those payments goes directly to the songwriter. We can do the same and give artists a direct benefit from these new technologies.

Conclusion

Senator, this is a moment of tremendous opportunity. For many years, our nation and this Committee heard wonderful promises of an emerging digital music era, where people could have convenient access to the entire catalog of recorded music over the Internet at the touch of a button.

Well, as often happens, history arrived ahead of time.

And it is a uniquely American story.

A young man with no standing, no credentials, no connections, and no plan for placating the powerful, sat down outside Boston and created an entirely new system.

Within 18 months, we were no longer debating whether there would be music on the Internet, but debating the best way to make sure that it continues. More than 60 million users have started a new stage in our national love affair with music. Napster users are nearly 50% more likely to say they are listening to more music now than six months ago, compared to others on line. All of us are finding new music - and music we'd forgotten how much we loved.

The question before this Committee is a matter of policy. How to make this new world of Internet music work. The next step should not be shutting it down, but making it work for everyone. The Congress has effectively promoted new technologies in the past, while ensuring that creators benefit; it is essential that we do so again today.

Thank you.

5038429