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Before the
COPYRIGHT OFFICE
LIBRARY OF CONGRESS
Washington, D.C.

APR 17 2001

GENERAL COUNSEL
OF COPYRIGHT

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

**MEMORANDUM IN SUPPORT OF
RIAA PETITION TO ESTABLISH TERMS
GOVERNING THE RIAA COLLECTIVE**

The Recording Industry Association of America, Inc. ("RIAA") submits this Memorandum in support of the "RIAA Petition To Establish Terms Governing the RIAA Collective" (the "Petition"). The Petition requests that the Librarian of Congress ("Librarian") adopt certain terms governing the RIAA collective. The Petition further requests that the Copyright Office suspend the Copyright Arbitration Royalty Panel ("CARP") initiated by Copyright Office Order dated February 13, 2001, pending consideration of RIAA's Petition.

BACKGROUND

Section 114(d) of the Copyright Act, 17 U.S.C. § 114(d), affords certain subscription audio services a compulsory license to transmit sound recordings digitally, provided that they pay a reasonable royalty and comply with various statutory conditions. Section 114(f)(1) of the Act, 17 U.S.C. § 114(f)(1), directs the Librarian to initiate voluntary negotiations for the purpose of determining reasonable Section 114 royalty

rates and terms. If the parties are unable to agree, the Librarian must convene a Copyright Arbitration Royalty Panel ("CARP"). See 17 U.S.C. § 114(f)(2).

On June 2, 1997, the Librarian initiated a CARP proceeding to determine rates and terms for the Section 114(d) compulsory license. See *Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings*, 62 Fed. Reg. 29,742 (June 2, 1997). RIAA, Digital Cable Radio Associates, now known as Music Choice, DMX Music, Inc. ("DMX"), and Muzak, L.P. ("Muzak") (collectively, "the parties") were the only parties to participate in that proceeding. In November 2000, RIAA formed SoundExchange, an unincorporated division of RIAA. More than 2000 sound recording copyright owners, representing more than 90 percent of the sound recordings legitimately sold in the United States, are members of SoundExchange. Sound Exchange is responsible for administering statutory licenses. Music Choice, DMX and Muzak (the "Services") are subscription digital audio services that perform sound recordings pursuant to Section 114(d) of the Copyright Act.

In a report released November 12, 1997, the CARP adopted a rate and various terms for the Section 114 compulsory license. See *In re Determination of Statutory License Terms and Rates for Certain Digital Subscription Transmissions of Sound Recordings*, Report of the Copyright Arbitration Panel, No. 96-5-CARP-DSTRA (Nov. 12, 1997) (unpublished) ("CARP Report"). Neither the Services nor RIAA proposed, and the CARP did not adopt, any terms that would govern the operation of the RIAA collective that would receive and distribute royalties to be paid by the Services.

On review of the CARP Report, the Librarian specifically designated RIAA as the agent to receive Section 114 royalty payments and statements of account. He then

adopted *ab initio* various terms governing the collective. See *Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings*, 63 Fed. Reg. 25394, 25412-13 (1998) (“Librarian’s Order”).

The United States Court of Appeals for the District of Columbia Circuit subsequently reversed the Librarian’s Order insofar as it adopted terms governing the RIAA collective. See *Recording Industry Association of America v. Librarian of Congress*, 176 F.3d 528 (D.C. Cir. 1999). The court concluded that “there is no evidence in the record to support the terms imposed on RIAA.” *Id.* at 535. Accordingly, the court remanded the proceeding for further consideration of the terms in 37 C.F.R. §§260.2(d), 260.3(d), 260.6(b) and 260.7. *Id.* at 536. By Order dated February 13, 2001, the Copyright Office initiated this CARP proceeding to address the issues raised by the court’s remand.

DISCUSSION

The Librarian originally adopted four sets of terms governing the RIAA collective – (1) 37 C.F.R. 260.2(d), which would have required the collective, when distributing royalties, to value all performances the same without regard to the circumstances surrounding the performances; (2) 37 C.F.R. § 260.3, which specified terms for the collective’s distribution of royalty payments; (3) 37 C.F.R. § 260.6, which specified the manner in which interested parties may audit the collective; and (4) 37 C.F.R. § 260.7, which specified the procedures for RIAA’s dealing with unknown copyright owners.

RIAA does not believe it is necessary or appropriate for the CARP to adopt any terms governing the RIAA collective, i.e. SoundExchange. As the agent designated by the Librarian to receive Section 114 royalties for all sound recording copyright owners,

RIAA has a fiduciary responsibility to all such copyright owners – regardless of whether they are members of SoundExchange. RIAA has consistently and publicly acknowledged that responsibility. No one has ever demonstrated why normal principles of fiduciary law are insufficient to address whatever concerns prompted the Librarian’s initial adoption of terms restricting SoundExchange. Nevertheless, in order to avoid costly and time-consuming CARP proceedings, RIAA and the other parties have agreed to the terms set forth in the Petition.

Without waiving the foregoing position, RIAA believes that if any terms are to be imposed on the operation of SoundExchange, the terms in Attachment A to the Petition should be adopted. The following discusses the differences between the original and the proposed terms, and the reasons for those differences.

1. **Section 260.2(d) – Equal Valuation**

The Petition deletes Section 260.2(d) of the original terms, which required SoundExchange to value all performances equally for purposes of royalty distribution. Terms concerning the distribution methodology are set forth in proposed Section 260.3(e), which is discussed below.

2. **Section 260.3 – Terms for Making Payment of Royalties**

The Petition makes several changes in the original Section 260.3 in addition to certain non-substantive word changes. First, the original Section 260.3(c) required SoundExchange to distribute royalties to “the parties entitled to receive such payments according to the provisions set forth at 17 U.S.C. 114(g).” The governing provision, however, is Section 114(g)(2) of the Copyright Act. And that provision deals specifically with the sound recording copyright owners’ allocations to recording artists. Thus, the

Copyright Office's original rule does not specifically require SoundExchange to distribute royalties to sound recording copyright owners. The proposed rule clarifies that SoundExchange must distribute the royalties it receives from the services to the eligible copyright owners (both members and non-members of SoundExchange).

Section 114(g)(2) of the Copyright Act also provides that it is the responsibility of the copyright owner to allocate the royalties it receives to featured and non-featured artists in the percentages prescribed by Section 114(g)(2). See 17 U.S.C. § 114(g)(2) ("copyright owner of the exclusive right under section 106(6) . . . shall allocate to recording artists" the royalties that the copyright owner receives). The proposed Section 260.3(c) makes clear that each of the sound recording copyright owners, and not SoundExchange, will be responsible for allocating the royalties it receives to featured and non-featured artists in accordance with Section 114(g)(2) of the Copyright Act. Of course, the copyright owners would retain the option of authorizing RIAA to distribute any royalties on their behalf to the artists.

Second, proposed Section 260.3(d) clarifies that SoundExchange may deduct its reasonable costs before distributing royalties to the sound recording copyright owners. *See* S. Rep. No. 104-128, at 31 (1995) ("Senate DPRA Report") (The term "receipts" in Section 114(g)(2) "means the licensing fees received by the copyright owner of the sound recording. Thus, if a collecting society or other organization acts on behalf of the copyright owner of the sound recording in licensing and/or collecting royalties, 'receipts' shall constitute the moneys the copyright owner receives from the collecting agency and, therefore, would exclude administrative fees either deducted by or paid to the

collective”). The proposed Section 260.3(d) also is amended to track the language in Section 260.7 concerning the nature of the administrative fees that may be deducted.

Third, the Petition adds a new Section 260.3(e). This term sets forth certain limitations on the manner in which SoundExchange may distribute royalties to *non-members* of SoundExchange. It does not impose any limitations on the distribution methodology for *members* of SoundExchange, since the basis of the Librarian’s concern in adopting terms that govern the collective has been to regulate the RIAA’s treatment of non-members – and not to restrict the ability of the collective’s members to agree on particular distribution methodologies or other collective practices. *See* Respondent’s Br. at 16-17, 46-51 in *RIAA v. Librarian* (filed January 19, 1999).

Proposed Section 260.3(e) directs SoundExchange to treat all performances equally on a service-by-service basis for purposes of determining the share of royalties to be distributed to nonmembers. For example, assume that DMX made 1,000,000 separate performances of sound recordings; that SoundExchange received \$200,000 in net royalties for those performances; and that 100,000 of those performances were of sound recordings owned by a copyright owner who is not a member of SoundExchange. In that case, the non-member would receive \$20,000 from SoundExchange, *i.e.*, \$200,000 x (100,000 performances/ 1,000,000 performances). Nothing in the proposed terms would restrict the manner in which SoundExchange distributed the remaining DMX royalties to its members.

Proposed Section 260.3(e) further provides that SoundExchange may adopt a different methodology for distributing royalties to non-members as long as that methodology weighs each performance according to its relative value. SoundExchange

could consider any factor that reasonably relates to relative value, including without limitation the actual or estimated number of persons who listened to each performance by the service.

Proposed Section 260.3(e) also imposes certain notification requirements on the collective. Specifically, SoundExchange must notify the Copyright Office of: (1) the methodology for distributing royalty payments to nonmembers, and any amendment, thereto, within 60 days after adoption; and (2) any written complaint that SoundExchange receives from a nonmember concerning the distribution of royalty payments, within 60 days of receiving that complaint; and (3) the final disposition by SoundExchange of any such complaint, within 60 days of disposition. These notification requirements will help the Office to determine whether RIAA is in compliance with the proposed terms and whether the Office should renew its designation of the collective under Section 260.3(f).

Proposed Section 260.3(e) also states that nothing in the Office's Part 260 rules shall deprive any persons from pursuing any remedies they might have under law against the collective.

Finally, the proposed terms insert the language from the former Section 260.3(e), designating the RIAA collective to receive royalty payments and statements of account, into a new Section 260.3(f). In determining whether to make a new designation, the Copyright Office may consider any written complaints against SoundExchange – as long as SoundExchange receives timely notice of, and an opportunity to respond to, any such complaints. The proposed Section 260.3(f) also makes clear that membership in SoundExchange is open to all sound recording copyright owners on a nondiscriminatory basis.

3. Section 260.6 – Verification of Royalty Payments

Proposed Section 260.6 specifies the procedures by which “interested parties” may audit the royalty payments made by SoundExchange. The proposed Section 260.6 is identical to the original Section 260.6, except that: (1) it contains certain non-substantive language changes; (2) it defines “interested party” as including only (a) sound recording copyright owners who are non-members of SoundExchange and (b) those recording artists who are entitled to receive a share of the copyright owners’ receipts pursuant to Section 114(g)(2) of the Copyright Act, or their designated agents. Nothing in proposed Section 260.6 applies to sound recording owners who are members of SoundExchange; those copyright owners will follow the audit procedures to which they agree in becoming members of SoundExchange.

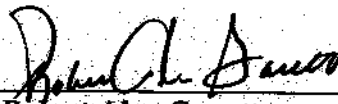
4. Section 260.7 – Unknown Copyright Owners

Aside from certain non-substantive language changes, proposed Section 260.7 makes no changes in the original Section 260.7. This provision specifies the procedures for dealing with the royalties of copyright owners who cannot be located within a three-year period.

CONCLUSION

RIAA urges the Librarian to adopt the terms set forth in the Petition and to suspend the CARP proceedings.

Respectfully submitted,

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April 17, 2001