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Copyright Office
Library of Congress
c/o Jacqueline C. Charlesworth
General Counsel and Associate Register of Copyrights
Washington, D.C.

Electronically Submitted

RE: RESPONSE TO MUSIC LICENSING STUDY: NOTICE AND REQUEST FOR COMMENT
Docket No. 2014-03

Ladies & Gentlemen:

I am writing in reply to the Request for Public Comment on the effectiveness of the current methods for licensing musical works and sound recordings.

INTERESTS OF RESPONDENT

I believe I can be helpful in this inquiry by virtue of a perspective that is both unique and common in studies of this type. During the course of my 35-year association with the music business, I have experience as:

- an *attorney* for recording artists, songwriters, music publishers, record companies, and technology companies in drafting and negotiating music and recording licenses (Law Offices of Milton A. "Mickey" Rudin and private practice),
- an *expert witness* for record companies and a PRO (Sony-BMG, Warner Music Group, ASCAP);
- an author of a popular *legal treatise* on music licensing (*Kohn On Music Licensing*);
- the founder of a *music service provider* (EMusic, Inc.) who sought and obtained hundreds of thousands of licenses for the digital delivery of musical works and sound recordings; and
- the founder of a company (RoyaltyShare, Inc.) that assists record companies and music publishers in tracking hundreds of millions of download and streaming delivery transactions for purposes of accurately *accounting* royalty shares to their respective artists and songwriters.

My experience is *unique* because my background gives me vantage point from which I can express genuine empathy for the challenges faced by each of participating constituencies: record companies (and the recording artists they serve), music publishers (and the songwriters they serve), and music service providers (and the listening public they serve).

Yet, my perspective is *common* to this inquiry in that, like many of the other participants, my time has been one of the costs inherent in the process of music licensing. And since the costs of music licensing is a function of its complexity, I and others like me have benefited from such complexity.

Today, I am retired and I have no connection with the music industry other than:

- a minority shareholder interest in RoyaltyShare, Inc. a venture-backed company I founded in 2006 and from which I retired in 2013;

- a copyright interest in *Kohn On Music Licensing* (4th Ed., Wolters Kluwer), an 1,800-page legal treatise on the licensing of musical works and sound recordings[1]; and

- a personal interest in seeing that the Copyright protections afforded by Congress, pursuant to the U.S. Constitution, serves both the creators of the works protected and the public for whose ultimate benefit that protection is granted.

To be clear, I have prepared this response without consulting anyone else. I am its sole author, solely responsible for its content, and no one else has made any contribution to this response whatsoever. Nor has anyone contributed money that was intended to fund its preparation or otherwise influence the views expressed herein.

The remainder of this comment will summarize (a) the problem underlying the complexity of music licensing, (b) the consequences of such problem, (c) a solution to the problem, and (d) an explication of such solution in the context of answers to many of the twenty-four specific questions raised by this inquiry.

[1] Hereinafter referred to as, "*KOML*." The book has been cited by the U.S. Supreme Court in *Eldred v. Ashcroft*, 57 U.S. 186 (2003), the Second Circuit Court of Appeals in *Woods v. Bourne*, 60 F.3d 978 (2d Cir. 1995) and *Boosey & Hawkes v. Buena Vista Home Video*, 145 F.3d 481 (2d Cir. 1988), and other courts, including Fred Ahlert Music Corp. v. Warner/Chappell Music, 958 F.Supp. 170 (S.D.N.Y. 1997), and *Bridgeport Music v. Dimension Films*, 410 F.3d 792 (6th Cir. 2005). The book was first published in 1992 concurrent with my co-author's retirement as vice president of licensing for the music publisher, Warner/Chappell Music. The 4th Edition, released in 2010, contains in its new first chapter an exploration of some of the authors' other views on music licensing.

THE PROBLEM

Implicit in the background provided in the Notice for Public Comments is the multi-headed cause of many of the challenges presented by music licensing in the digital age:

a. the three-sided market (i.e., record companies, music publishers, and music service providers) in which only two sides are ever at one time at the same table in negotiation with each other regarding the same product (i.e., a sound recording embodying a musical work); which is

b. complicated by the fact that one side of the market (i.e., music publishers) is institutionally split by the historical divisibility of rights (i.e., the right of public performance and the right of reproduction), which is

c. further complicated, on the performance rights side, by the existence of multiple PROs, two of which are subject to separate consent decrees, and many music publishers who desire the right to license public performances directly to music service providers (bypassing the PROs), which is

d. further complicated, on the reproduction side, by a handful of collection agencies and administrators who represent only a fraction of popular musical works and by thousands of individual music publishers who elect to license reproductions directly; which is

e. further complicated, by the fact that the reproduction rights to many of these musical works are split among multiple co-owners on a non-exclusive administration basis; which is

f. finally complicated by the fact that many of these licenses are not available on a worldwide basis in an age in which territorial licensing has become technologically obsolete.

THE CONSEQUENCE

The consequence of this modern-day Hydra is that music licensing (at least with respect to digital delivery and transmission) is characterized by unnecessarily high *transaction costs.*

A portion of these transaction costs are borne by those seeking to use and enjoy recordings of musical works (i.e., music service providers and their customers) and the rest is borne by the creators of these works, the recording artists and songwriters whose royalty earnings are adversely affected by these costs.

The beneficiaries of these elevated transaction costs are the middlemen who are the recipient of such costs in payment for their services: record companies, music publishers, collection societies, PROs, collection agencies, IT departments, technology providers, accountants and auditors, and lawyers (not to mention authors and publishers of books on music licensing).

Of course, transaction costs are not inherently bad—they are necessary to the operation of every market. But when a legal infrastructure inspires rather than discourages inefficiencies in the operation of a market, it behooves those who enact the laws and those who administer them to change the laws and regulations in way that will reduce such inefficiencies.

THE RATIONALE FOR STATUTORY LICENSES

Fortunately, as Hercules found a way to defeat his multi-headed foe, mechanisms exist that can reduce the transaction costs arising from the state of affairs described above. The paradigm is embodied in the form of the statutory licensing provisions of Section 115 (with respect to reproduction licensing of musical works) and Section 114 (with respect to the licensing of certain kinds of digital audio transmissions, and associated ephemeral reproduction, of sound recordings) of the Copyright Act.

Granted, the statutory licenses have their costs: namely, the reduced freedom of contract suffered by the owners of the musical works and sound recordings. (The freedom of contract is reduced, but not always eliminated; for example, the Section 115 statutory license does not compel the licensing of the "first use" of the musical work). Yet, as we know, the ultimate purpose of copyright protection is to provide an incentive for the creation of works of authorship by means of compensating creators for their use. Without that incentive, the public at large would suffer an in efficient, underproduction of such goods.

Accordingly, the statutory licenses are justified to the extent transaction costs arising from a purely *voluntary* license regime threatens to overwhelm the means of compensation and, therefore, the incentive of copyright.

It is submitted that the statutory licenses under Sections 115 and 114 are justified by the benefit they afford: the significant reduction in transaction costs of licensing musical works and sound recordings for the respective uses they cover. Certainly, while millions of dollars and management resources have been devoted to establishing terms and rates under statutory provisions, such costs pale in comparison to the transaction costs that would be incurred in their absence.

The hypothesis of reduced transaction costs arising from statutory licensing could be criticized as one that suffers a lack of sufficient hard data. Perhaps econometric studies can be contrived to support it and others to refute it. (Certainly, numerous law review articles, written by those whose living depends on transaction costs, have lead such criticism). But, here, we may learn from Aristotle who taught that precision is not to be sought in all discussions; it will be adequate if we look for precision just so far as the nature of the subject admits. This has always been true of controversies in copyright, such as the duration of copyright (from the days of Lord Mansfield to *Eldred v. Ashcroft*), applications of the idea/expression dichotomy (e.g., *Nichols v Universal Pictures*), and copyright's applicability to computer software interfaces (e.g, *Lotus v. Borland*, *Oracle v. Google*).

It is fair, therefore, to reason from useful thought experiments. Imagine, for example, the market operating without the compulsory provisions. Start with the simple situation of a recording artist seeking to license a previously recorded musical work for use in a new sound recording—whether for embodiment

in physical copies to be distributed or digital copies to be transmitted for permanent delivery or transitory performance. The owner of the musical work would have a number of potential pricing models from which to choose: cents per copy, percentage of revenue, or both, or neither, and the model may vary, of course, depending upon the use.

Whatever the business model chosen for each use, the ultimate *rate* may depend upon an independent variable: the value of the song (or the importance of the use) relative to the recording in which the song is embodied—similar to the factors a music publisher considers in issuing a voluntary synch license.[2] Thus, regardless of the model, the owner of the musical work would be justified in charging a higher rate if the contribution of the song to the value of the recording is relatively higher than the contribution made by the recording artist.

Of course, if high costs of negotiating the appropriate models and individual rates don't impede the consummation of a license, certainly the copyright owner's outright refusal to license will. Such refusal may come at the hands of any one of multiple co-owners, for any reason, or no reason. And even if all co-owners would otherwise agree to license, contractual rights of consent in favor of each of multiple songwriters or recording artists could block such issuance. At first blush, that might seem to be the owner's prerogative, but as Professor Nimmer put it, the scope of an owner's rights in Blackacre have never been the same as the owner of the copyright in *Black Beauty*. The monopoly conferred by copyright is a limited grant which sole interest lies in the general benefits derived by the public from the labors of authors.

Under the compulsory license, no one beyond the first licensee can be denied a license and the fee for the license will be the same statutory rate for the reproduction license, regardless of the value of the relative contributions of the musical work and the performer to the sound recording. Of course, while the *rate* is the same, the ultimate revenue to the song owner will likely be different. But what justifies restricting the copyright owner's freedom of contract? It could only be that, by reducing transaction costs, the public will benefit from the availability of a greater variety of recordings (within legitimate limits that protect artistic integrity[3]) of existing musical works—which is the ultimate purpose of incentivizing creators in the first place.

The problem is compounded, of course, in a case where a new music service provider is seeking a license to millions of existing recordings for a use not covered by the terms of many of these negotiated, voluntary licenses (e.g., a mechanical license to record and exploit the recording for all uses except interactive streaming, or a mechanical license that does not permit the sound recording owner to pass-through or sublicense the musical work to music service providers at all). In a world without statutory licenses, the specific terms of each of these millions of voluntary licenses—and underlying songwriter agreements—

[2] See, *KOML* (4th Ed.), Chapter 15, pp. 1085-1140.

[3] The statutory license has provisions that would require a voluntary license from the owner of the musical work where the new recording would change the basic melody or fundamental character of the musical work. Section 115(a)(2).

would have to be consulted as a condition to release of the recordings, works that are not owned by those who could block their release.

This happens to be one of the acute problems currently faced by the film & TV industry: thousands of motion pictures and television programs are not currently available to the public for download or transmission over the Internet, because the synch licenses for musical works used in these films—negotiated decades before the advent of services like Netflix—require renegotiation. For a single film to be cleared for release, a satisfactory deal has to be reached with respect to every musical work and every sound recording used in the film before it be exploited for the new use. A single co-owner of a split copyright, or songwriter with approval rights could hold up the digital exploitation of the entire film, even after thousands of dollars of music clearance efforts have already been expended.

Thus, any one of the owners or co-owners of the musical works and sound recordings used in the film, and perhaps any one of the songwriters and recording artists who created such works, have substantial power over the exploitation of a copyrighted work in which they have no ownership interest whatsoever. Yet, under a scenario when one person (perhaps someone who cannot even be located) can block the exploitation of the larger work and all the works associated with it, everyone loses: no revenue to the film owner, no revenue to the music publishers, no revenue to the record companies, no revenue to the recording artist, no revenue to the songwriter, no revenue to the motion picture service provider and, most importantly, no *availability* to the public—the raison d'etre of copyright.

A SOLUTION

While the reduction of transaction costs was not the original purpose of the statutory license under the 1909 Act[4], the benefit of reduced transaction costs has since become, in my view, an excellent rationale not only to maintain it, but to significantly expand its scope—both under Section 115 and Section 114.

The question this inquiry needs to address, in my view, is not whether to extend the statutory license provisions of Sections 115 and 114, but how.

At the highest level, my comments below recommend a Herculean attack on the multi-headed negotiation that currently stultifies the entire music licensing process for the use of audio recordings of musical works in the digital realm. The basic terms, which are incorporated in the answers to specific questions below, are summarized as follows:

1. Section 115 and Section 114 should be redrafted to contain parallel provisions assuring consistency in licensing the digital delivery and transmission of a single work that contains a sound recording and a musical work. Alternatively, these provisions could be combined for that purpose.

[4] A history of the origin of the statutory license under Section 115 (and its predecessor under the 1909 Act) is set forth in Chapter 13 of *KOML* (4th Edition) at pp. 732-773 and the development of statutory license under Section 114 is set forth in Chapter 23 at pp. 1465-1504.

2. Section 115 should be amended to make clear it covers all forms of digital audio deliveries and transmissions, including digital phonorecord deliveries, tethered downloads, interactive streaming, and the like.
3. Section 114 should be expanded so that its compulsory provisions cover all forms of digital audio deliveries and transmissions, *including* interactive digital audio transmissions and digital phonorecord deliveries.
4. Section 106(6) be expanded to provide sound recording owners with the exclusive right of public performance *by any means*.
5. Current provisions of Section 114 concerning statutory license revenue flowing through agents such as SoundExchange should be maintained on the grounds that public performance of digital audio transmissions was a new right. By the same token, should Section 106(6) be expanded to include all forms of public performances of sound recordings, such performances should be subject to a Section 114 compulsory license and administered through agents such as SoundExchange. But when expanding compulsory license to all interactive digital audio transmissions and digital phonorecord deliveries, statutory license revenue would flow directly to the owners of the sound recordings.
6. Section 114 licenses should be available on a blanket basis with notice provisions that parallel similar provisions under Section 115.
7. Section 115 should be amended to compel a *blanket* license.
8. Licenses under Sections 115 and 114 should include any necessary reproduction licenses *and* public performance licenses.
9. The statutory rate for the licenses necessary under a revised Section 115/114 would be a separate rates for the musical work and sound recording, but each of those rates should be set by a single rate setting body. Though considered and established together, these rates should be separate, because if the underlying musical work is in the public domain, a payment would not be required for the use; if the sound recording is in the public domain, a payment need only be made for the underlying copyrighted musical work. In any event, how the royalties are divided between the musical work and sound recording should not be a concern of the music service provider; the allocation should be decided by the rate setting body.
10. In addition, the rate setting body should not only establish how revenues generated should be split between the musical work and the sound recording, but also (a) between the reproduction and public performance aspects of the use (e.g., what share is allocated to the PRO for the particular use), and (c) between the kind of use (e.g., what share is allocated to SoundExchange or other agent for the particular use).
11. A digital clearing organization or musical recording rights registry ("Rights Registry"), separate from the rate setting body, should be established to maintain a central database of all rightsholder, sound recording and musical work metadata, administer the blanket licenses under both Sections 115 and 114, collect revenues generated from such licenses, allocate such revenue among rightsholders in accordance with the statutory scheme, and distribute such revenue to the appropriate rightsholders depending upon the use—on the publishing side, to music publishers, PROs, administrators and collection agencies; on the recording side, to record companies and SoundExchange.

12. The Rights Registry should be a private non-profit body operating with a Board and charter similar to those of ASCAP and SoundExchange, containing representatives of rightsholders from the music publishing, sound recording, reproduction rights, public performance rights, and music service provider constituencies.
13. As a condition to the license, music service providers would be required to (a) comply with specific reporting requirements sufficient to allow the Rights Registry to perform accurate allocations and distributions, and (b) allow real-time access to transactions as they occur for purposes of (i) auditing and (ii) the provision of real-time analytics to the rightsholders.

COMMENTS ON SPECIFIC SUBJECTS

Musical Works

1. Please assess the current need for and effectiveness of Section 115 statutory license for the reproduction and distribution of musical works

The section above entitled, the *Rationale for Statutory Licenses* is incorporated herein by this reference. It is submitted that the Section 115 statutory license is fully justified by the substantial reduction in transaction costs it effects. That reduction is in the public interest, because it increases the availability of the greatest variety of musical recordings to the listening public, which is one of the primary public interests served by the monetary incentive afforded creators under copyright law.

Section 115 has been effective, but only to a point. While the compulsory provision has served the music publishing and record industries well for decades, its effectiveness has fallen down with the advent of a new kind of music reproduction licensee entering into the mix: digital music service providers, who, in the absence of a form of blanket license from a single or limited number of sources, have had to engage in an expensive effort to identify copyright owners and negotiate licenses on a song-by-song basis.

This has reduced the field of potential music service providers to those with the financial ability to bear the upfront transaction costs. The reduced competition has slowed innovation and the consumer adoption of these services. Without sufficient consumer adoption, the scale necessary for a profitable operation is impeded and the prospects for revenue flowing through to creators of musical works and sound recordings are reduced. It is no coincidence that as consumers shifted their demand from physical goods to digital deliveries, the music industry revenues have decline dramatically—from their peak in 1999 to less than half of that amount today.

2. Please assess the effectiveness of the royalty ratesetting process and standards under Section 115.

The ratesetting process for permanent digital phonorecord deliveries, tethered downloads, and on-demand stream will never be effective in the absence of consideration of rates for the use of (a) the

sound recordings in which such musical works are embodied and for (b) the public performance aspects of the use, neither of which are at the table during the Section 115 ratesetting process.

3. Would the music marketplace benefit if the Section 115 license were updated to permit licensing of musical works on a blanket basis by one or more collective licensing entities, rather than on a song-by-song basis?

Yes.

If so, what would be the key elements of such a system?

The section above entitled, *A Solution*, is incorporated herein by this reference. The following elements may also be helpful:

A statutory license for musical works under a blanket basis would entail at least the elements of (i) scope, (ii) notice, (iii) rate, (iv) payments/collections, and (v) distributions. (These elements could serve as a model for an enhanced parallel regime for statutory licenses for sound recordings).

1. Scope.
    a. Section 115(a)(1)'s current requirement of "first use" should be maintained. The copyright owner's freedom of contract should be inviolable until he or she first licenses the work for distribution or delivery.
    b. Section 115(a)(2)'s prohibition against the modification of the basic melody or fundamental character of the work should also be maintained. The musical copyright owner may be compelled to give up freedom of contract for the public interest, but not his or her artistic integrity. (With respect to a parallel sound recording license, a similar restriction that would prohibit digital sampling of sound recordings without obtaining a voluntary license. However, the sound-a-like exception should be maintained).
    c. To the extent the rates will vary among the different forms of exploitation (i.e., distribution of phonorecords, or transmissions of digital files on a permanent, tethered, or transitory basis), these forms should be distinguished by definition.
    d. The license should include the privilege of reproduction *and* performance.
    e. The license, or a parallel license, should include the right to use the sound recordings in which the musical works are embodied (discussed below).

2. Notice.
    a. Pass-through licenses, at least insofar as they apply to digital transmission, should be eliminated. The music publishers should have a direct relationship with music service providers, albeit through an intermediary licensing/collection organization, such as the Rights Registry.
    b. A music service provider applying for a blanket license should be enabled to submit one notice to the Rights Registry, specifying its intention to obtain a statutory *blanket* license to the entire repertoire of musical works that have been previously distributed or made

digitally available and its agreement to the terms of such license (whether it is listed in the Rights Registry or not). (Similarly, under Section 114, the music service provider would submit a separate notice specifying its intention to obtain a statutory blanket license to the entire repertoire of sound recordings that have been previously distributed or made digitally available and its agreement to the terms of such license).

c. Notice will entitle the music service provider to, among other things, a delivery of the rightsholder, musical work and sound recording metadata for the sole purpose of properly accounting for transactions.

3. Rate.

a. Rates would be set by a statutory body comprised of individuals with music industry experience, nominated by rightsholders and music service providers, and selected from this pool by the Copyright Office ("Rate Board"). Requiring nomination to be made by the music industry stakeholders would assure that only those with music industry or music service provider experience could be appointed to the Rate Board.

b. The Rate Board would set the rate for use of musical works and the rate for the use of sound recordings. The relative value between those two would be subject to some debate; perhaps it would first established by the statute or regulation, subject to revision by the Board. But rates for the use of sound recordings can no longer be set without rates for the use of musical works in mind. This must be done together under the auspices of the same statutory framework.

c. Rates, in each case, would include the fees for making reproductions and public performances.

d. Rates would be set as a percentage of revenues, subject to appropriate floors. A percentage of revenue is the only fair basis for allocating the value of the relative contributions; the rate regime can always include a safeguard with appropriate minimums to address the risk of non-revenue generating services. Rates based on a percentage of revenues has worked well for the PROs and the broadcast industry since the early 1930's when they were introduced, which was just before recorded music began to be broadcast.[5] By contrast, penny rates established by the CRB with respect to webcasting of sound recordings have not taken into account the infancy of the webcast industry and the need to attract a critical mass of customers before sound recording owners could receive full value for the use of their works.

e. Rates should not be confused with Allocations.

- While separate rates will be established between musical works and sound recordings, the Rate Board would set the Allocations between the between the reproduction use and the performance use, depending upon the kind of use.
- Allocations should reflect the divisibility of copyright according to the nature of the use. For example, physical distribution of phonorecords and permanent downloads might have no element of value accorded the public performance

[5] For the history of this, see Chapter 1 of Kohn On Music Licensing (4th Edition, 2010) at pp. 7-20.

right. On-demand streams, tethered downloads, and webcasts may have more value, or all value, accorded to the public performance element, depending upon the circumstances.

- Allocations should be invisible to the music service provider, as long as it is providing the detailed transaction data for the respective uses required under the license for proper revenue allocation and distribution.

f. Rates will be reviewed by the Rate Board both periodically and upon application for a specific rate review by any rightsholder or music service provider (in the manner of a rate hearing).

g. Consideration should be given to an appellate review board, appointed in the same manner as the Rate Board, or appeals to the federal courts (at least to assure due process).

4. Payments/Collections

a. Music service providers would make payments and provide reports to a Rights Registry or digital clearing organization to be established for this purpose.

b. Consideration should be given to the establishment of two or more digital clearing organizations who would compete for rightsholders, much the way the PRO's compete today—to ensure better service through some competition or threat of competition. This may involve some duplication of effort, but the inefficiencies should be outweighed by the efficiencies gained by a competitive environment.

c. Music service providers would agree to comply with strict transaction reporting requirements with detail sufficient for accurate accounting down to the appropriate rightsholders for the transactions engaged in. The efforts of DDEX could be leveraged to this effect, but neither the government nor the Rate Board should legislate precisely how the Rights Registry chooses to format its metadata or reporting requirements.

d. Music service providers would be required provide transparent access to transaction data in real-time to an independent validation service, working on behalf of the digital clearing organization, the musical works owners, and the sound recording owners, for both audit purposes and *real-time* transaction analytics.

e. Payments and reports would be required as frequently as the technology allows (e.g., monthly, weekly, daily[6]), as determined by the Rate Board.

5. Distributions to Rightsholders

a. Musical work rightsholders include:

- owners of musical work (e.g., music publishers, songwriters)
- Music publishing collection agencies (e.g., Harry Fox Agency) and administrators, working on behalf of music publishers or musical work copyright owners;
- PROs (ASCAP, BMI, SESAC),

[6] The Barnes & Noble e-book service provides sales reports and invoicing to their book publisher licensors on a daily basis.

b. Sound Recording rightsholders include:
   - Owners of sound recordings (e.g., record companies)
   - SoundExchange and other such agencies

c. Rightsholders would be entitled to distributions for licensing revenues allocated to them.
   - This means, for example, that the PRO's role in respect to the blanket licenses for these digital uses would be reduced to the collection of its allocation from the Rights Registry and the distribution of those funds down to their respective rightsholders (i.e., music publishers and songwriters members), but the PRO's would not administer licenses to music service providers or collect funds, which would be done by the Rights Registry or competing digital clearing organizations. It would be the Rights Registry's responsibility to allocate revenues between reproduction use and public performance use in accordance with the statute, regulations, or decisions by the Rate Board.
   - On the sound recordings side, SoundExchange, too, would collect its allocation from the Rights Registry for allocations or revenue to certain types of digital audio transmissions currently described in Section 114, and distribute funds to its constituents (record companies, recording artists), but not administer licenses or collect funds from music service providers, which would be done by the Rights Registry to administer the allocation process. It would be the Rights Registry's responsibility to allocate revenues between reproduction use and public performance use in accordance with the statute, regulations, or decisions by the Rate Board.

4. For uses under the Section 115 statutory license that also require a public performance license, could the licensing process be facilitated by enabling the licensing of performance rights along with reproduction and distribution rights in a unified manner?

Yes.

***5.* Please assess the effectiveness of the current process for licensing the public performances of musical works.**

The process of licensing public performances of musical works in traditional markets, such as radio and television broadcasting, and retransmissions in commercial business establishment has been excellent with the rate review process safe-guarding fairness in licensing.

However, in the digital market, rate court proceedings have morphed from the nature of a fairness hearing for proposed rates to an actual rate setting process—something which the courts are not equipped to do, especially without jurisdiction over rate setting for mechanical reproductions of musical works and transmissions of sound recordings.

Moreover, certain music publishers are attempting to pull their digital rights from the PROs in an effort to gain more leverage to raise the rates charged for public performances of their musical works

in the digital realm. The effort is symptomatic of the problem created by separate rate processes for reproductions and performances, and sound recordings and musical works.

6. ***Please assess the effectiveness of the royalty ratesetting process and standards applicable under the consent decrees governing ASCAP and BMI, as well as the impact, if any, of 17 U.S.C. 114(i), which provides that "[l]icense fees payable for the public performance of sound recordings under Section 106(6) shall not be taken into account in any administrative, judicial, or other governmental proceeding to set or adjust the royalties payable to copyright owners of musical works for the public performance of their works."***

   The answer to question 5 above is incorporated by this reference.

   The language quoted in the question from Section 114 is also symptomatic of the problem created when rates are set by separate rate setting regimes for musical works and sound recordings, as well as separate regimes for setting rates for reproductions and performance uses.

   Music service providers should be charged a pair of rates (considered and established together) for their intended uses of musical works and sound recordings and then not be involved in the business of how the royalties they pay get allocated among the rightsholders, including the allocation between reproduction and public performance use.

7. ***Are the consent decrees serving their intended purpose? Are the concerns that motivated the entry of these decrees still present given modern market conditions and legal developments? Are there alternatives that might be adopted?***

   As noted in answers to questions 5 and 6 above, rather than being used as a protection in individual cases against unfair performance fee demands, the consent decrees are turning the federal courts into a rate setting body, which it is unequipped to do, since it is not involved in the setting of rates for sound recordings or reproductions of musical works.

Sound Recordings

8. ***Please assess the current need for and effectiveness of the Section 112 and Section 114 statutory licensing process.***

   The section above entitled, the *Rationale for Statutory Licenses* is incorporated herein by this reference. It is submitted that the *need* for the Section 114 statutory license parallels the need for Section 115, except in the case of 114, it does not cover enough.

   The ability of sound recording owners to use a *voluntary* license for interactive streaming and permanent download services, while owners of musical works are otherwise constrained by the compulsory provisions of Section 115 has created an imbalance in the allocation of revenues from music service providers. See response to Question 19 below.

For this reason, Section 114 should be expanded such that its compulsory provisions cover all forms of digital audio deliveries and transmissions of sound recordings, including interactive digital audio transmissions and digital phonorecord deliveries (while Section 115 should be clarified to do the same with respect to musical works).

The elements of an expanded Section 114 statutory license regime for these uses would parallel the elements of a revised Section 115 license as recommended in the answer to question 3 above.

9. Please assess the effectiveness of the royalty ratesetting process and standards applicable to the various types of services subject to statutory licensing under Section 114.

The Copyright Royalty Board (CRB) have taken actions that have resulted in an unnecessarily complex set of individual rate regimes for the various uses contemplated by Section 114 by various kinds of defined transmitters. Many of these separate regimes, the result of voluntary industry settlements, is said to have been spawned by a rate regime set by the CRB that has been criticized as not properly reflecting the economics of a growing transmission industry. Some have suggested that these difficulties resulted from the fact that too few of the CRB's members have appeared to have sufficient music industry experience when they embarked upon the rate setting process.

For this reason, it is recommended that that nominations for the new Rate Board, discussed above, be made by music industry and music service provider stakeholders themselves. Members would be selected by an independent organization, such as the Copyright Office, but only from among the slate of industry nominees.

10. Do any recent developments suggest that the music marketplace might benefit by extending federal copyright protection to pre-1972 sound recordings?

Yes, because the public performance of pre-1972 sound recordings by digital audio transmission does not appear to be an exclusive right of the copyright owner under common law or any state statute.

In this regard, there should be some surprise at the second clause of the following sentence included at footnote 12 of the Notice to which this comment responds:

> "Thus, a person wishing to digitally perform a pre-1972 sound recording cannot rely on the Section 112 and 114 statutory license *and must instead obtain a license directly from the owner of the sound recording copyright*." [Emphasis added]

When Section 106 was amended to provide the owner of sound recordings the exclusive right of public performance by means of digital audio transmission (17. U.S.C. Sec. 106(6)), it was a new right that had not existed under federal or, to my knowledge, under common law copyright or the statute of any state.

That this is an entirely new right would seem to be supported by the fact that, under Section 114, payments of the recording artists' shares were to be made directly to them via one or more non-profit

rights agents, rather than passing through the record companies and paid out in accordance with the artists' recording agreements.

When Section 106 was amended to add this new limited performance right, Congress could not have amended state statutory or common law rights to pre-71 recordings. While sound recordings became protected under applicable state laws until 2067, it does not mean that the state laws or the common law automatically recognized a public performance right in sound recordings.

Moreover, that existing common or state statutory law did not cover such a performance right is evidenced by the fact that no sound recording owner ever claimed it (at least successfully) was so covered in the over 40 years since passage of the 1972 Act. Moreover, it does not appear that any pre-1972 sound recording owner has claimed that its exclusive common law or statutory rights in such recordings ever included a public performance right by means of digital audio transmission since the enactment Section 106(7).

At least not until a lawsuit making such claim was filed on April 17, 2014, less than a month after the Notice containing footnote 12 was filed in the Federal Register.

The complaint in that lawsuit, *Capitol Records LLC v. Pandora Media, Inc.*, 651195/2014, New York State Supreme Court, New York County (Manhattan) cites neither a statutory provision nor a case citation under New York statutory or common law supporting a such public performance right, whether by means of digital audio transmission or otherwise, in pre-1972 sound recordings.

The lawsuit, apparently, is attempting to persuade the New York State courts to add such a performance right to the common law. Whether this is good policy is now in the hands of the New York Supreme Court, notwithstanding the opinion apparently expressed by the Copyright Office in footnote 12.

Are there reasons to continue to withhold such protection?

No. On the contrary, there is now good reason to extend such protection if only to eliminate litigation in 50 states to change the common law or potentially inconsistent legislative efforts to do the same.

Should pre-1972 sound recordings be included within the Section 112 and 114 statutory licenses?

Yes, as those compulsory provisions are expanded to include interactive services and digital phonorecord deliveries as recommended herein.

11. Is the distinction between interactive and noninteractive services adequately defined for purposes of eligibility for the Section 114 license?

No. Given the above recommendation to add interactive streaming and digital phonorecord deliveries to the compulsory provisions of Section 114 (not to mention the controversy about the correct categorization of the *Pandora* service), definitions under Section 114 should be reconsidered.

Platform Parity

12. What is the impact of the varying ratesetting standards applicable to the Section 112, 114, and 115 statutory licenses, including across different music delivery platforms.

As discussed further in the response to Question 19 below (incorporated herein by this reference), because some kinds of works (i.e., musical works) and their uses (e.g., digital phonorecord delivery, on-demand streams) are subject to *compulsory* licensing and other kinds of works (i.e., sound recordings) and their uses (e.g., digital phonorecord deliveries, on-demand streams) are subject to *voluntary* licensing, the ratesetting standards have caused an inequitable division of revenues between creators and distributors of musical works and sound recordings. The sections above entitled, *The Problem*, *The Consequences*, and *The Solution* are also incorporated herein by this reference.

Do these differences make sense?

No.

13. How do differences in the applicability of the sound recording public performance right impact music licensing?

While owners of musical works are disadvantaged by the compulsory provisions of Section 115, owners of sound recordings have been disadvantaged by the lack of a general public performance right under Section 106. The addition of Section 106(6) to add a public performance right by means of digital audio transmissions has partially remedied this disadvantage.

In any revision of the Copyright Act, Section 106(6) should be expanded to cover all public performances of sound recordings. As flowing from a new right, distributions of public performance revenues should be made in accordance with the regime established under Section 114 for statutory digital audio transmissions (e.g., through SoundExchange and similar agents).

But when expanding compulsory license to all interactive digital audio transmissions and digital phonorecord deliveries for sound recordings, the statutory license revenue would flow to the owners of the sound recordings, not through SoundExchange or other agents. This is because the DPDs are an existing reproduction right, unlike the new right created with the enactment of Section 106(6).

Changes in Music Licensing Practices

14. How prevalent is direct licensing by musical work owners in lieu of licensing through a common agent or PRO? How does direct licensing impact the music marketplace, including the major record labels and music publishers, smaller entities, individual creators, and licensees?

No response.

15. Could the government play a role in encouraging the development of alternative licensing models, such as micro-licensing platforms? If so, how and for what types of uses?

The government should play a role in revising the statutory provisions and promulgating appropriate regulations under those provisions, but should otherwise do nothing to either encourage alternative licensing models or specific technology platforms.

As suggested in the answer to question 22 below, the federal government, working with the Rights Registry, could play a role in maintaining and making publicly available all rightsholder and repertoire metadata regarding the identity of rights holders and the musical works and sound recordings with which they are associated (e.g., as creators, authors, owners, etc.). This may be coupled with a claims and dispute resolution process.

16. In general, what innovations have been or are being developed by copyright owners and users to make the process of music licensing more effective?

No response.

17. Would the music marketplace benefit from modifying the scope of the existing statutory licenses?

Yes.

The costs of the statutory licenses—the reduced freedom of contract suffered by the owners of the musical works and sound recordings—are greatly outweighed by the benefits they afford: the significant reduction in transaction costs of licensing musical works and sound recordings for the respective uses they cover.

For the reasons set forth above (in sections entitled *The Problem*, *The Consequences*, *The Rationale for Statutory Licenses*, and *A Solution,* which are incorporated herein by this reference), these benefits will increase significantly by expanding the scope of the existing statutory licenses, under Sections 115 and 114, to include both reproductions and public performances and all forms of digital deliveries and transmissions.

The ultimate purpose of copyright protection is to provide an incentive for the creation of works of authorship by means of compensating creators for their use. Without that incentive, the public at large would suffer an in efficient, underproduction of such goods. The expansion of the statutory licenses recommended here will significantly reduce the transaction costs of music licensing and thereby increase the effectiveness of the incentive of copyright.

Revenues and Investment

18. How have developments in the music marketplace affected the income of songwriters, composers, and recording artists?

If each household in the United States (over 100 million) paid $10 per month, $12 billion would be generated, a number that greatly exceeds the combined revenue of music publisher and record companies from digital music service providers (and perhaps all other music revenue sources) in the United States. It is estimated that subscription music services—such as *Spotify*, *Beats*, etc.—have only a few million paying subscribers combined, a small fraction of that necessary to maximize the income of songwriters, composers and recording artists.

To the extent elevated transaction costs in music licensing have impeded the creation of new, innovative subscription music services and the adoption of such services by consumers, it behooves the government to take action to reduce those transaction costs by effective legislation.

19. Are revenues attributable to the performance and sale of music fairly divided between creators and distributors of musical works and sound recordings?

No. The National Music Publishers Association, in recent public statements, has made a convincing case that musical works are inadequately compensated for their use in digital deliveries and transmission as compared to sound recordings—although I have no opinion on the extent to which such relative compensation is inadequate.

The solutions recommended above would provide a mechanism to remedy this misallocation: making sure that when rates are set, the appropriate *allocations* (whatever that may be) are being made by the same body within the same statutory framework at the same time.

All I have to say about the specific allocation between musical works and sound recordings is this: the proper allocation will be a function of precision desired and the transaction costs involved in achieving such precision.

There are two ways to get to an allocation while minimizing transaction costs: (1) an efficient means of analyzing the data and calculating a more precise allocation or (2) a rule of thumb to be applied equally to all transactions until such means is acquired.

The nature of the problem was summarized in the section above entitled, The Rationale for Statutory Licenses. The only way to do a precise allocation is on a recording by recording basis, the allocation between the recording and the underlying musical work being a function of the value of the song (or the importance of the use) relative to the recording in which the song is embodied (e.g., recording of a popular musical work by Bob Kohn v. recording of an unknown song by Lady Gaga). This is a very expensive allocation to calculate, if it can be done objectively at all, especially when performed over millions of recordings and billions of transactions.

Accordingly, the industry must for the time being rely on a rule of thumb influenced by allocations we see in a free market. When sound recordings are synch licensed for use in motion pictures, generally (though not always), the fee charged for the recording is often the same the same the fee charged for the recordings. Sound recording owners might contend that, under such circumstances, the recording is being undervalued, because there are more close substitutes for the recording (e.g., Frank Sinatra's rendition v. Tony Bennett's rendition of the same musical work). Of course, many musical works also have close substitutes, depending upon the use.

Sound recording owners might also contend that making a new recording of an existing musical work requires significant financing, risks not undertaken by the owner of the musical work. However, over time, such recording cost are sunk costs. An argument can be made, therefore, that the allocation to the sound recording during the first few years following its release should be higher than it is during the remainder of the copyright term. At some point certainly, the owner of the sound recording is taking no more risk in issuing a digital license than the owner of the musical work.

At the end of the day, it is fair to say that owners of sound recordings, because of the *voluntary* nature of their licenses, as opposed to the *compulsory* nature of the music publisher licenses, are probably getting an allocation of revenue from digital deliveries and transmissions more than what they would get on a level playing field. This may compensate for the sound recording owners not having a general public performance right and revenues from terrestrial broadcasts, but that has been partially remedied by their exclusive right in public performance by digital audio transmissions, especially their voluntary licensing of interactive streams.

To this discussion, I add one anecdotal example:

In December, 1997, I co-founded Emusic.com (initially named Goodnoise), which in July, 1998 became the first company to sell a digital music MP3 file for 99 cents per track. Our standard deal with our independent record company licensors at the time (who numbered over 1,000 by 2001) was that we paid them 50 percent after deduction of two costs: the 8.5 cent mechanical license fee and the 1 cent fee we paid for the required MP3 patent licenses. We agreed with the Harry Fox Agency and the music publishers to pay the mechanical license fee directly to them instead of passing them through the record companies.[7]

Thus, for every 99 cents we collected, we paid 9.1 cents (adjusted from 8.5 for comparison purposes) directly to the music publisher and 44.45 cents to the record company. In other words, about 9.1% was allocated to the musical work, about 45% allocated to the sound recording, and about 45% allocated to the music service provider.

[7] This increased our transaction costs, but we didn't wish to take on the risk that the record companies would be unable accurately pass through the mechanical fee to publishers. To the extent they didn't, we would be open to lawsuits for infringement from potentially thousands of music publishers, since we were the ones making reproductions. Thereupon, Emusic became the first company to submit a "bulk" mechanical license request to the Harry Fox Agency (in the form of a spreadsheet containing a request for 32,000 licenses.

When, five years later, Apple established the iTunes store in April, 2003, they also charged consumers 99 cents per track. Under their arrangement with major record companies, they paid 70 cents per track under which the record companies passed through the 9.1 cent mechanical fee[8] to music publishers. Thus, the allocation was about 61.5 percent to the record company, 9.1 percent to the music publisher, and 29% to the service provider.

Accordingly, the record companies experienced a 45% increase in allocation over the existing model while the music publishers saw no increase whatsoever. Moreover, the music publishers had no direct relationship with iTunes for audit or any other purposes at the time.

Clearly, the record company's *voluntary* license, together with its ability to pass-through an existing mechanical license, put them to great advantage in negotiating a fee allocation relative to music publishers who were at a disadvantage under the Section 115 *compulsory* license provisions.

The way to remedy this misallocation of resources is not to eliminate the Section 115 statutory license, which would only increase transaction costs, but to include digital phonorecord deliveries of sound recordings under a form of statutory license akin to Sections 115 or 114. At the same time, owners of sound recordings should be given a general public performance right under Section 106(6).

20. In what ways are investment decisions by creators, music publishers, and record labels, including the investment in the development of new projects and talent, impacted by music licensing issues?

The existing legal and business infrastructure for music licensing has significantly and necessarily increased the transaction costs of making recorded musical works available to the public. This could only have the effect of reducing the consumption of such works, causing lower revenues and fewer investment funds available to develop and promote new songwriters and recording artists.

21. How do licensing concerns impact the ability to invest in new distribution models?

The high transaction costs of music licensing vary by distribution model, encouraging some and impeding the development of others. For example, to engage in terrestrial broadcasting of musical sound recordings, one need only obtain a public performance license for the use of musical works from the PROs, which is based on a percentage of revenues, rather than a pennies per play model, and available on a blanket basis. No licenses for the use of the sound recordings are necessary. This has enabled a robust and competitive environment for terrestrial radio.

By contrast, interactive streaming services require a whole gamut of licenses for musical works, sound recordings, reproductions, and performances—on a penny per play model as well as the requirement of large advance payments—and they must be licensed on a song-by-song, recording-by-recording basis. These circumstances have not only put such services at a competitive disadvantage to terrestrial radio, but have made it difficult for startup companies with innovative distribution models or

[8] Under pre-1978 recording contracts, the mechanical fees may be subject to control-composition clauses, which reduces even further the share of the musical works in the digital delivery.

technology to enter the market and compete with companies who may be less nimble, but which can otherwise afford to make the upfront investments required.

Data Standards

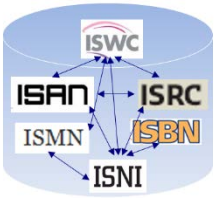
22. Are there ways the federal government could encourage the adoption of universal standards for the identification of musical works and sound recordings to facilitate the music licensing process?

The Rights Registry recommended herein, which would be responsible for establishing reporting requirements, would be in the best position to recommend specific standards for metadata and reports, pursuant to recommendations developed by both the rightsholders and the service providers. The federal government should not otherwise be engaged in the standards process, except insofar as encouraging a general principle of *transparency*, especially with respect to metadata, and the resolution of disputes between rightsholders and service providers on issues of date standards.

Currently, repertoire metadata is considered by collection agency, PROs, and rightsholders as a form of "family jewels," an important means of self-preservation. Even lists that merely identify rightssholders (e.g., names of songwriters, composers and music publishers in the IPI database) not connected to repertoire metadata is considered proprietary information of the collection agencies.

The truth of the matter is, without transparency of rightholder and repertoire metadata, moneys will never be allocated accurately to recording artists and songwriters—impeding, of course, the overriding purpose of the copyright law.

Accordingly, it is recommend that the federal government require each licensee and licensor to contribute to the Rights Registry (and/or the Copyright Office) all rightsholder (e.g., songwriter, recording artist, music publisher, record company ID) and repertoire (musical work and sound recording) metadata in their possession or under their control. The Rights Registry (and/or the Copyright Office) should make available access to this metadata online, and establish a claims and dispute resolution process to assure to the maximum extent possible that revenue is flowing to the appropriate owners, songwriters and recording artists. Establishing an infrastructure for the defining and enforcement of property rights is one of the essential roles of government in a free society.



Other Issues

23. Please supply or identify data or economic studies that measure or quantify the effect of technological or other developments on the music licensing marketplace, including the revenues attributable to the consumption of music in different formats and through different distribution channels, and the income earned by copyright owners.

No response.

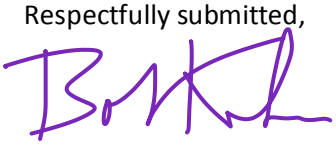
24. Please identify any pertinent issues not referenced above that the Copyright Office should consider in conducting its study.

I reserve the privilege of amending or supplementing these comments as appropriate and as the Copyright Office will accept.

The Copyright Office should be commended for asking an important set of focused questions and for giving members of the public an opportunity to contribute our thoughts on these important issues. In the end, it is hoped that the Copyright Office will contribute greatly to the efficiency of the music licensing process.

The challenges are great, but not insuperable, and progress will be made if we bear in mind that the U.S. Constitution refers to securing rights to Authors, not their intermediaries, and that such rights are secured to promote the *public interest* in encouraging the works of their creation.

Respectfully submitted,



Bob Kohn