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Organization: Netflix, Inc.

These comments are submitted by Netflix, Inc. ("Netflix") in response to the Copyright Office's Music Licensing Study: Notice and Request for Public Comment published on March 17, 2014, 78 Fed. Reg. 14739 (the "Notice").

Basis for Comments

Netflix is primarily engaged in the distribution of audio-visual programming content, including movies and television shows, to viewers via the Internet. Netflix spends hundreds of millions of dollars annually to compensate creators and copyright owners for the acquisition of that programming.

Music – whether of a theme, background or sometimes feature nature – typically is embedded in that programming at the time of its production by producers and long before it reaches the distribution channels provided by Netflix (as well as by broadcast, cable and satellite television and movie program services, sometimes – with Netflix – collectively referred to herein as "Services"). Consistent with long-standing industry practice, and as a result of a historical anomaly described in more detail below, U.S. producers of audio-visual content secure all licenses for music-related copyrights (and, in fact, for all other copyrighted elements of the programming) necessary to allow for the Services' lawful exhibition of the programming, *with one solitary exception*: the right to publicly perform, by non-theatrical means, the musical works (i.e., compositions) embodied in the programming. As a result, the burden of securing licenses for this non-theatrical public performance of musical works is typically placed on the "downstream" entities transmitting the content to viewers, i.e., the Services. And those Services, including Netflix, typically have had little choice but to secure licenses to publicly perform

musical works in the United States from the three U.S. performing rights organizations ("PROs") referenced in the Notice: ASCAP, BMI and SESAC.

In light of the foregoing, Netflix's comments are limited to those Subjects of Inquiry set forth in the Notice that relate to musical work performance rights licensing. In brief, Netflix favors elimination of the distinction between licensing the public performance of musical works for theatrical and for non-theatrical exhibitors, and supports the licensing, at the time of production, of all public performance rights in musical works, regardless of the means of delivery or venue of exhibition. Should that distinction persist, however, Netflix believes the ASCAP and BMI consent decrees, particularly the provisions for effective compulsory blanket licensing on request and rate oversight by federal "Rate Courts" under those decrees, play a critical role in reducing transaction costs for users like Netflix and, to some degree, minimizing the potential for misuse of market dominance. To that end, Netflix believes certain provisions of those decrees, particularly those enabling users to secure compulsory blanket licenses on request, should be extended to SESAC and, in the event of future reductions in the PROs' repertoires, to other dominant musical work copyright holders, and that additional modifications to the decrees themselves, including the adoption of an identical rate setting authority for all three PROs and mandated transparency in both the administration and negotiation of PRO licensing, are warranted.

We provide more detail below, in response to the specific Subjects of Inquiry pertinent to musical work performance rights licensing:

Subject #5: "Please assess the effectiveness of the current process for licensing the public performances of musical works."

As noted above, there is a distinct difference between how the public performances of musical works in audio-visual content are licensed for exhibition of such programming in movie theatres and how they are licensed for purposes of exhibition of such content in every other venue and by any other means (whether via broadcast television, satellite, Internet, etc.). This dichotomy has arisen in the wake of the theatrical exhibitors' anti-trust challenge to ASCAP in *Alden Rochelle, Inc. v. ASCAP*, 80 F.Supp. 888 (1948), which led to the inclusion of certain injunctive provisions in the ASCAP consent decree that prohibit ASCAP from licensing movie theatres for musical work performances associated with audio-visual content they exhibit. ASCAP Second Amended Final Judgment § IV(E) ("ASCAP is hereby enjoined and restrained from … [g]ranting to, enforcing against, collecting any monies from, or negotiating with any motion picture theatre exhibitor concerning the right of public performance for music synchronized with motion pictures"). Television at that time was in its infancy and – unlike the pre-recorded film content then-exhibited in theatres – featured primarily live programming; broadcasters did not predict that television would shortly mimic film by airing pre-recorded programming, including films, and failed to recognize the importance of, or timely advocate for, similar treatment.

As a consequence of this injunction, and based on long-standing industry practice, songwriters and music publishers typically negotiate with movie producers – in the same transaction and before production of a film is completed – regarding the value of *both* the synchronization rights and *theatrical* public performing rights (as well as, in the case of score music written specifically for a film, the compensation for the writer's time and effort). The transaction costs associated with obtaining theatrical performing rights in this fashion are negligible, since it is merely one incremental aspect of a negotiation that is *already* taking place

for purposes of obtaining necessary sync rights. And because the negotiations occur at the time of production, they are conducted in a price-competitive market; if the licensor seeks a price deemed excessive by the producer, the producer is able to obtain price quotes from any number of alternative music writers and/or publishers before the music is embedded in the film.

Critically, however, this injunctive provision in ASCAP's consent decree only applies to movie theatre exhibitors; and as a consequence of this historical anomaly, writers and publishers overwhelmingly do *not* negotiate with producers of audio-visual content regarding (and do not grant to such producers) the right to publicly perform anywhere else (or by any other exhibition means) the musical works embedded in audio-visual content – even for the exact same feature film that is initially released theatrically and later exhibited via any form of television or Internet streaming.

Accordingly, and uniquely for musical work performances, audio-visual content producers and/or licensors invariably exclude from the otherwise comprehensive copyright representations and warranties made to downstream exhibitors like Netflix the right to publicly perform the musical compositions embodied in such content. Such downstream exhibitors are then left to obtain these performing rights in a market that is devoid of price competition, as the music is already embedded in the content they receive and such exhibitors typically lack the right and/or ability to remove or replace the music. Instead, these exhibitors customarily take blanket licenses from the three PROs in a process that is far more inefficient and far less effective than the process whereby the identical rights are licensed seamlessly (and in a price-competitive manner) for theatrical exhibition.

Not surprisingly, these negotiations are expensive and time-consuming, and, for users, exactly what works are being licensed is far from transparent. The lack of control over the music

contained in the movies and television shows that Netflix (and other Services) distribute, combined with Netflix's (and other Services') lack of knowledge regarding how much of that music falls within the mutually-exclusive respective repertoires of ASCAP, BMI and SESAC, ensures an inefficient and one-sided market. Indeed, Netflix is frequently subject to claims by each PRO regarding PRO market shares (i.e., shares of works performed through Netflix) – which typically add up to well more than 100% – but has no way of accurately assessing those claims, including because the PROs do not make available any meaningful information identifying the size or the make-up of their individual repertoires. This lack of transparency, coupled with Netflix's (and other Services') inability to control or shift the share of musical works embedded in their programming, creates a significant imbalance of power in the PROs' favor.

This is not to suggest that the ASCAP and BMI consent decrees do not provide certain meaningful protections to users. In light of the current industry practice, where licensing of non-theatrical public performance rights does not occur in a competitive market, the consent decrees, particularly the provisions enabling effective compulsory blanket licensing on request and rate oversight by the Rate Courts, are vitally necessary for non-theatrical exhibitors of audio-visual content, and, for the most part, effective. Without these licensing options, Netflix (and other Services), which have no practical way to determine who owns which publishing rights associated with the movies and TV programs they distribute, would face, in the best case scenario, dramatically increased transaction costs and inefficiencies associated with reaching licensing arrangements with hundreds if not thousands of copyright owners in musical works. In the worst case scenario, where the public performance rights are severely fragmented across those thousands of copyright owners, Netflix and other Services might not be able to distribute

certain licensed movies and television shows for which they could not secure a license for performance of musical works on reasonable terms. For these reasons, and because a blanket license to repertoire is only as good as the scope of the musical works it is comprised of, Netflix supports the extension of certain provisions of those decrees, particularly those enabling users to secure compulsory blanket licenses on request, to SESAC and, in the event of publisher withdrawals from the PROs, to other dominant musical work copyright holders.

That said, the consent decrees, and their remedies, are not perfect. For example, while the goal of ASCAP/BMI Rate Court litigation is to arrive at a Court-determined rate that is equivalent to the outcome of negotiation in a competitive market between a willing buyer and a willing seller, both the substantial costs of litigation and the business uncertainties inherent in court-determined approximations of what is a competitive rate impose unnecessary risks and costs on all parties. And these costs and risks could be avoided entirely were the same musical work licensing practices applicable to theatrical performances of audio-visual content applied to all audio-visual content performances – i.e., by licensing, at the time of production, the public performance rights in musical works, regardless of the means of delivery or venue of exhibition. Netflix believes that changes in the Copyright Act (or PRO consent decrees) that would facilitate this outcome are warranted and would be beneficial to current users and potential market entrants, as well as to consumers.

In the event that relief in the form of elimination of the dichotomous licensing treatment applicable to movie theaters as compared to all other exhibitors of audio-visual content is not available, Netflix would support preservation of the existing consent decrees but propose certain changes in governing licensing practices that would effectively streamline the transaction costs of licensing through the PROs.

As noted above, the PROs are not competitive alternatives to one another for exhibitors like Netflix. One way to minimize transaction costs and inject more certainty into results would be to provide for all three PROs to be subject to the *same* rate-setting authority through which an overall industry-wide musical work performance rate for users can be determined (by negotiation or rate-setting litigation); and then the three PROs – who, unlike the downstream exhibitors, collectively have the data necessary to determine who owns what publishing rights – would be left to negotiate (or obtain a determination from this rate-setting body) as to what are their respective shares of the royalty pool. This consolidation of proceedings would by-definition lead to efficiencies compared to the existing structure; and there is precedent for this approach in copyright law. *See* 17 U.S.C. § 119 (establishing a consolidated statutory licensing scheme for retransmission of television programming by satellite providers). Further, greater transparency in the marketplace, both in terms of repertoire and market share, would benefit both copyright owners and copyright users. And simplifying the rate court structure could also save legal costs and speed up the licensing process, therefore leading to faster distribution of royalties to musical works copyright holders.

Subject #6: "Please assess the effectiveness of the royalty rate-setting process and standards applicable under the [ASCAP/BMI] consent decrees … as well as the impact, if any, of 17 USC section 114(i)" (the prohibition against considering the royalty rates for digital audio sound recording performances in ASCAP/BMI cases).

Given the world in which Netflix operates, including the lack of competition and choice noted above, the *process* of rate-setting under the ASCAP and BMI consent decrees – and the hypothetical competitive market standard for rate-setting applied in Rate Court cases – has

worked reasonably well. Rate Court cases have the virtues of being subject to the Federal Rules of Civil Procedure and Federal Rules of Evidence, which create the opportunity for all the litigants to fairly and predictably obtain discovery, present evidence and rely on precedent. Consequently, only a tiny fraction of license negotiations result in Rate Court litigation. (It is hard to know, however, whether this small number is the result of the deterrent effect of Rate Court for all parties, or stems from an unwillingness or inability on the part of users to take on the risk and costs of litigation, even if they believe the rates ASCAP or BMI are seeking do not fairly reflect the value of the musical works in the audio-visual content they distribute).

Further, as recommended above, one way in which the process could be improved would be to subject all three PROs – including SESAC – to the same rate-setting body (and to extend the effective compulsory license provisions of the ASCAP and BMI consent decrees to SESAC as well).

Regarding the Copyright Office's inquiry relating to the evidentiary bar embodied in 17 U.S.C. § 114(i), this prohibition should remain unchanged. This is a provision initially requested by the music publishing industry. Moreover, the only reason that the publishers now seek to excise this provision is that sound recording performance royalties have turned out to be higher than the publishers expected. But the reason for the "disparity" in rates is because the Copyright Royalty Board and its predecessor body (the Copyright Arbitration Royalty Panel) adopted arguments advanced by the record industry that there is no correlation between the value of sound recording and musical work performances given the fundamental differences between the recorded music and music publishing businesses. Accordingly, there is absolutely no warrant for a change in this provision.

Subject #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 discussed in detail above, Netflix believes that the ASCAP and BMI decrees are, for the most part, serving their intended purpose. Judge Cote's 136-page decision in the recent *Pandora v. ASCAP* case is but one example of how important the consent decrees are in constraining the market power of collectives the size of ASCAP and BMI; and the recent SESAC court decisions are indicative of the market power possessed by even a PRO as relatively small as SESAC. *In re Petition of Pandora Media Inc*., 12-cv-08035-DLC (S.D.N.Y. Mar. 18, 2014); *Meredith Corp. v. SESAC, LLC*, 09 Civ. 9177-PAE (S.D.N.Y. Mar. 8, 2014); *Radio Music Licensing Committee Inc. v. SESAC Inc. et al.*, 2:12-cv-05807-CDJ (E.D. Pa. Dec. 23, 2013). The consolidation in the publishing industry (with three publishers now controlling well over 60% of the market), coupled with the evidence detailed by Judge Cote in the *Pandora* decision of coordinated and arguably collusive behavior in the industry, reaffirms the need for the consent decree constraints applicable, at a minimum, to all PROs (including those constraints enabling effective compulsory licensing on request and rate oversight by the Rate Courts) and, in the event of withdrawal by publishers from the PROs, to other dominant musical work copyright holders, too.

Netflix's additional suggestions on how the current consent decrees could be improved are set forth in detail above, in response to Subject #5.

Subject #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 music licensing marketplace would be materially improved for both copyright owners and users if the government mandated transparency in both the administration and negotiation of licensing by the PROs. Judge Cote's decision in the *Pandora* case underscores the degree to which publishers have sought to take advantage of this lack of transparency (to users) regarding ownership of publishing rights. Any number of provisions could be adopted within the context of legislation or modification of the ASCAP and BMI consent decrees to address this problem.

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Netflix welcomes the opportunity to submit comments and to participate in the Copyright Office's initiative.

Respectfully submitted,

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