

From Broadcast to Webcast: Copyright Law and Streaming Media

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Presented at the 30th annual
Telecommunications Policy Research Conference
Alexandria, VA

Revised September 15, 2002

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Abstract

This paper examines the copyright issues facing streaming media. The paper details the arcane requirements for digital performances, the controversy over how ephemeral RAM copies should be treated, and the current rulemaking on the statutory digital performance license. Streaming media face complex requirements detailing what constitutes a non-interactive transmission eligible for a statutory license under section 114 of the Copyright Act. Section 114 calls for a statutory license for the digital transmissions of sound recordings (digital performances) that meet certain strict eligibility requirements. In addition, section 112 provides for a statutory license for the ephemeral copies made in the course of those transmissions.

A Copyright Arbitration Royalty Panel (CARP) issued a report on February 20, 2002 recommending that different rates be adopted for Internet transmissions depending on whether the transmission is a simulcast by a terrestrial broadcaster or a "free standing" transmission. The fee was seven cents per 100 performances for simulcasts and fourteen cents per 100 performances for Internet-only transmissions. The Librarian of Congress rejected the rate for Internet-only transmissions and set the rate for all webcasts at seven cents per 100 performances (non-CPB non-commercial broadcasters who transmit webcasts will pay a rate of two cents per 100 performances).

An analysis of the rate reveals that the section 114 license is significantly more expensive than the corresponding license for the underlying musical work (a ratio of 3.5 to 1 compared to a ratio of 1 to 1 in other countries). The new rate favors radio stations and large, established webcast aggregators over small, independent webcasters who would be better served by a percentage-of-revenue metric. The current law's broadcasting exemption gives over-the-air radio a huge advantage over webcasting. However, in the long run, the high rate may give less popular recording artists an opportunity to gain attention and encourage new creative uses for streaming technology.

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“Curtain Call for Webcasts? Royalty Fees Killing Most Internet Radio Stations, Webcasters Head to Washington in Royalty Protest, Webcast Royalty Proposal Draws Fire From All Sides.” These were just a few of the headlines written this year as the Library of Congress sought to establish license fees for digital performances of sound recordings.¹ The Librarian of Congress was caught in a no-win situation. On one side were record labels seeking to exercise a new right, on the other side was a nascent industry with popular opinion on its side. At the heart of the debate is a revolutionary technology called “streaming” that allows anyone to create their own radio station on the Internet.

The Internet is the newest medium for the distribution of audio and visual content. With each new medium comes a new fight over the scope of copyright protection. Streaming content on the web is simply the latest battleground in the fight between content producers and distributors. Congress tried to implement a compromise; content producers (in this case the record companies) would be granted copyright protection for public performances of sound recordings but distributors would be able to take advantage of a statutory license to transmit those performances. This paper examines the myriad copyright issues facing streaming media. The paper details the arcane requirements for digital performances, the controversy over how

¹ Headlines in order: Washington Post, June 21, 2002; USA Today, July 21, 2002; Washington Post, May 8, 2002; Washington Post, Aug. 8, 2002.

ephemeral RAM copies should be treated, and the current rulemaking on the statutory digital performance license.

Section 114 of the Copyright Act calls for a statutory license for the digital transmissions of sound recordings (digital performances) that meet certain strict eligibility requirements. In addition, section 112 provides for a statutory license for the ephemeral copies made in the course of those transmissions. Streaming media face complex requirements detailing what constitutes a non-interactive transmission eligible for the statutory license under section 114.

A Copyright Arbitration Royalty Panel (CARP) issued a report on February 20, 2002 recommending that different rates be adopted for Internet transmissions depending on whether the transmission is a simulcast of a terrestrial broadcast signal or an Internet-only transmission. The fee was seven cents per 100 performances for simulcasts and fourteen cents per 100 performances for Internet-only transmissions. The Librarian of Congress rejected the rate for Internet-only transmissions and set the rate for all webcasts at seven cents per 100 performances (non-CPB non-commercial broadcasters that transmit webcasts will pay a rate of two cents per 100 performances).

This paper concludes that while the current statutory rate is too high, it may be a blessing in disguise. The rate is too high since it overvalues the sound recording performance right as compared to the musical composition performance right. In addition, by using a per-performance metric, the rate makes it extremely difficult for small, independent webcasters to survive. However, the high rate may ultimately help recording artists and the public. First, the rate makes it possible for unknown artists to

offer a lower rate as a way to gain airplay and attention. Second, the high rate encourages webcasters to develop new, creative uses for the medium rather than relying on music as a way to attract an audience. The biggest problem with the current law is that it continues to favor over-the-air radio over Internet streaming.

I. Introduction to streaming and the copyright issues

Streaming is distinguished from other forms of music distribution by the method and purpose of transmission. Standard music downloads consist of MP3 files or other file formats that are copied completely to the user's hard drive for later playback. The file cannot be played until it is fully downloaded. Streaming differs from this in two important respects. First, the music is performed while the file transfer is occurring. Second, when the transfer/performance is complete, no copy of the file remains on the user's hard drive. Thus, the streaming song is a public performance rather than a reproduction.² The streaming is similar to a terrestrial broadcast signal other than the method of transmission. Thus, streaming is often referred to as "webcasting."

Webcasts can take many forms. They range in length from seconds to hours. They can be performed "on demand" by selecting a program that is stored on a server or they can be continuous similar to tuning into a radio station where the user begins listening at a random point in the programming. One final distinction that some observers make is the original source of the content. A FCC-licensed, terrestrial radio station may simulcast its programming on the Internet. This is referred to by some as a radio

² However, in order to perform the song, part of the file is stored in a buffer. Theoretically, the buffer contains no more than a few seconds of the song at any one time and is continuously overwritten.

retransmission (RR). Programming that is only available on the Internet is referred to as an Internet-only (IO) transmission.³

Record companies, which hold the copyrights to most sound recordings, argue that digital performances of sound recordings (webcasting) reduces album sales. The concern is two-fold: (1) some users possess the technological skill to make copies of streaming songs,⁴ and (2) the webcasts may serve as substitutes for owning copies of particular songs. Because of the scarcity of radio frequencies, most FCC-licensed stations play a large enough variety of songs that a consumer would not consider listening to the radio to be a good substitute for owning the record to listen to on demand. On the Internet, the number of webcasts is unlimited, meaning that consumers can tune into very specific programs that feature a narrow range of artists and recordings. This is more likely to serve as substitute for owning the record, especially as wireless broadband Internet access becomes more prevalent, allowing users to listen to webcasts on portable devices. From the perspective of the copyright owners, the risk of substitution increases as the user gains more influence over the choice of songs performed. Interactive, on-demand performances pose the greatest risk to record sales while completely non-interactive and broad-based song selection poses the least significant risk.

³ The distinction is only valuable if there is a legal difference in the classification of an RR transmission as opposed to an IO transmission. This became a source of much controversy when the CARP proposed two different rates, one for RR and a higher rate for IO transmissions. This is discussed later in the paper.

⁴ "Ripping" software makes it possible to make a permanent copy of the streaming content onto the user's hard drive. Most consumers do not possess this software and are therefore unable to make perfect digital copies of the streaming content.

Even before the Internet and digital media created concerns of piracy, record labels and recording artists had argued that sound recordings should enjoy a performance right. The lack of a performance right for sound recordings is an anomaly in the law.⁵ When records are performed on the radio, the copyright owner in the musical composition earns a performance royalty but the copyright owner in the sound recording does not.

The Copyright Act grants copyright owners a bundle of five rights: reproduction, distribution, adaptation (derivative works), public performance, and public display.⁶ As will be discussed in detail in this paper, sound recordings do not enjoy a standard public performance right but rather a limited right controlling public performances of certain digital audio transmissions.⁷ For the purpose of this paper, the relevant definition of a public performance is:

to transmit or otherwise communicate a performance or display of the work...to the public, by means of any device or process, whether the members of the public capable of receiving the performance or display receive it in the same place or in separate places and at the same time or at different times.⁸

Webcasting implicates both the reproduction right and the public performance right.

To make matters more complex, the reproduction right is implicated in two different ways. First, the webcaster must make ephemeral copies of the songs on servers to facilitate streaming. Second, the act of streaming itself creates buffer copies of the song in a computer's RAM. To make matters even *more complex*, most music recordings

⁵ David Nimmer, *Ignoring the Public, Part I: On the Absurd Complexity of the Digital Audio Transmission Right*, 7 UCLA ENT. L. REV. 189 (2000).

⁶ 17 U.S.C. §106 (2000).

⁷ 17 U.S.C. §106(6).

contain two separate copyrights: the copyright in the underlying musical composition (the song) and the copyright in the performing artist's rendering of the composition (the sound recording).⁹

II. Musical composition rights

Songwriters have long enjoyed public performance rights. Any individual or business entity that publicly performs a song must get permission from the copyright owner (songwriter or composer). Public performances include radio and television broadcasts and performances in bars, restaurants, concert halls, etc. Because countless public performances occur everyday in countless locations, songwriters have formed performing rights organizations (PROs) such as ASCAP and BMI that administer their public performance rights and collect and distribute the resulting royalties. Most businesses that make frequent use of public performances (such as broadcast stations, bars, and concert halls) obtain a "blanket license" from each PRO which allows them to perform any song administered by that organization. It is important to note that a public performance of a song may take place as a live rendition of the song or by playing a sound recording of the song (on vinyl, cassette, compact disk, MP3 file, etc.). Public performance royalties make up a substantial share of the revenue earned by songwriters.

With the advent of webcasting, the PROs established experimental rates for permission to perform musical compositions via digital streaming on the World Wide

⁹ 17 U.S.C. §101

Web (web). For example, ASCAP has established a basic rate of about 1.6 percent of revenues or 0.048 cents per site visit.¹⁰ Similarly, BMI's basic fee is 1.75 percent of revenues or 0.012 cents per page impression.¹¹ The PROs take the position that almost every transmission of a song is a performance, even if the purpose of that transmission is to purchase a permanent copy of the song.¹²

Similarly, the National Music Publishers Association (NMPA) argues that every streaming transmission is also a reproduction and distribution and therefore requires a mechanical license.¹³ The NMPA negotiated an agreement with the RIAA that on-demand streaming and limited duration downloads do require a mechanical license, while streaming that qualifies for the section 114 statutory license does not.¹⁴ The Digital Music Association argues that the streaming process is the same in both instances and that therefore, a mechanical license should not be required for on-demand

⁹ Not all sound recordings contain an underlying copyrighted song. Some musical compositions are in the public domain. Other sound recordings (such as nature recordings) do not contain musical compositions at all.

¹⁰ Any site visit lasting more than one hour is counted as multiple visits based on the number of hours. ASCAP Experimental License Agreement, <http://www.ascap.org/weblicense/ascap.pdf> Accessed August 29, 2002.

¹¹ BMI Experimental License Agreement, <http://bmi.com/licensing/forms/internet01.pdf> Accessed August 29, 2002.

¹² In a joint statement ASCAP, BMI and NMPA/Harry Fox Agency took the position that only "pure downloads" that result in a permanent, *reproducible* copy of the song would not be considered a performance [emphasis added]. <http://www.ascap.org/legislative/jointstatement.html> accessed August 28, 2002. Because record labels are unlikely to authorize the sale of MP3 files that do not contain copy protection, almost no download would qualify as a "pure download" and hence all downloads would be considered a performance as well. No court has yet ruled on this issue.

¹³ Section 115 of the Copyright Act provides for a compulsory license to make mechanical copies of songs once the song has been released as a recording. Once a recorded version of a song is published, anyone can distribute their own recording of the song to the public as long as they pay the statutory rate. The compulsory license does NOT extend to making copies of the original recording of the song, nor does it extend to making copies of the lyrics or sheet music. 17 U.S.C. §115 (2000).

¹⁴ Agreement between NMPA, Harry Fox Agency and the RIAA, Section 8.1(a) (Oct. 9, 2001) <http://nmpa.org/pr/FinalRIAAgreement.pdf>

streaming either.¹⁵ One can see on the part of the NMPA a concern that on-demand streaming could become a substitute for purchasing a recording of the song. From the NMPA's perspective, if you can listen to the song on-demand, it is the equivalent of owning a copy of the song and therefore should be treated as such under the law.

In its report on the DMCA, the Register of Copyrights took the position that the creation of buffer copies in RAM during streaming is a fair use:

The sole purpose for making the buffer copies is to permit an activity that is licensed by the copyright owner and for which the copyright owner receives a performance royalty. In essence, copyright owners appear to be seeking to be paid twice for the same activity. Additionally, it is technologically necessary to make buffer copies in order to carry out a digital performance of music over the Internet. Finally, the buffer copies exist for too short a period of time to be exploited in any way other than as a narrowly tailored means to enable the authorized performance of the work. On balance, therefore, the equities weigh heavily in favor of fair use....The uncertainty of the present law potentially allows those who administer the reproduction right in musical works to prevent webcasting from taking place - to the detriment of other copyright owners, webcasters and consumers alike - or to extract an additional payment that is not justified by the economic value of the copies at issue.¹⁶

The Register of Copyrights recommended that Congress pass a law to exempt webcasters from liability when their streaming activities create temporary buffer copies.¹⁷

While the legal delineation of rights between the NMPA and PROs is unsettled, the settlement between the NMPA and RIAA essentially allows webcasters who offer non-interactive streaming to transmit musical compositions after securing a blanket

¹⁵ Effect of the RIAA/NMPA/HFA Agreement on Inquiry into Digital Phonorecord Deliveries, Comments filed by DiMA, <http://www.copyright.gov/carp/dpd/dpd001.pdf>

¹⁶ DMCA Section 104 Report, A Report of the Register of Copyrights, xxv-xxvi (2001).

¹⁷ *Id.* at 142-43.

license for the performance rights from the PROs. The performance rights to the sound recordings are much more complex.

III. Sound recording rights

Unlike the musical compositions they often contained, sound recordings were not protected by federal copyright law until 1971.¹⁸ At that time Congress declined to include a public performance right for sound recordings. Thus, radio stations pay a fee to perform the underlying song, but are not required to pay a fee to perform the sound recording of the song. This anomaly is usually attributed to the strength of the broadcasting lobby when the law was passed and justified by the belief that radio airplay benefits the record companies by promoting their sound recordings.¹⁹ Another factor was the concern among the PROs (primarily ASCAP and BMI) that Congress would direct the PROs to share their royalties with the record companies.²⁰ When Congress overhauled the copyright law in the 1976 Copyright Act, it still declined to grant sound recordings a performance right even though the Copyright Office had recommended including such a right.²¹ Meanwhile, the International Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations, better known as the Rome Convention, granted limited broadcast

¹⁸ Sound Recording Act of 1971, Pub. L. 92-140, 85 Stat. 391 (1971).

¹⁹ Kimberly L. Kraft, *The Webcasting Music Revolution Is Ready to Begin, as Soon as We Figure Out the Copyright Law: The Story of the Music Industry at War with Itself*, 24 HASTINGS COMM. & ENT. L.J. 1, 6 (2001).

²⁰ *Id.*

²¹ Nimmer, *supra* note 5 at 190.

performance rights to sound recordings in 1961.²² However the United States is not a member of the Rome Convention and so American performers do not receive royalties from countries that are signatories.

IV. Digital Performance Right in Sound Recordings Act of 1995

In 1995, Congress finally granted a limited performance right to sound recordings with the Digital Performance Right in Sound Recordings Act of 1995 (DPRA).²³ The right was limited to certain digital transmissions of sound recordings, primarily interactive and subscription transmissions. The digital performance right was later amended by the Digital Millennium Copyright Act (DMCA) in 1998 to expand the right to include some non-subscription transmissions.²⁴

It is no exaggeration to say that the DPRA is one of the most convoluted and unreadable laws ever passed. The law is a perfect example of interest-group policymaking that has been the hallmark of copyright legislation since the beginning of the 20th century, as described by Jessica Litman.²⁵ Congress simply acted as mediator between two commercial industries, the recording industry (which wanted a full performance right for sound recordings) and the existing distribution industries that publicly perform sound recordings (that wanted an exemption from any performance right). Congress responded by crafting a law that would exempt most preexisting uses of sound recordings:

²² International Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organisations (Rome Convention), Oct. 26, 1961 Available from WIPO at:

<http://www.wipo.int/clea/docs/en/wo/wo024en.htm>

²³ Pub. L. 104-39, 109 Stat. 336 (1995).

²⁴ Pub. L. 105-304, 112 Stat. 2860 (1998).

Notwithstanding the views of the Copyright Office and the Patent and Trademark Office that it is appropriate to create a comprehensive performance right for sound recordings, the Committee has sought to address the concerns of record producers and performers regarding the effects that new digital technology and distribution systems might have on their core business without upsetting the longstanding business and contractual relationships among record producers and performers, music composers and publishers and broadcasters that have served all of these industries well for decades. Accordingly, the Committee has chosen to create a carefully crafted and narrow performance right, applicable only to certain digital transmissions of sound recordings.²⁶

First, the public performance right only applied to digital audio transmissions of sound recordings. Therefore all analog audio performances are exempt as well as all performances (whether digital or analog) that do not include a transmission. "To 'transmit' a performance or display is to communicate it by any device or process whereby images or sounds are received beyond the place from which they are sent."²⁷ Nor does the performance right apply to audiovisual works (i.e. motion pictures and television programs).²⁸ The 1995 law also created an exemption for all non-subscription, non-interactive transmissions as well as certain retransmissions of non-subscription broadcast transmissions within 150 miles of the transmitter. Transmissions to business establishments are also exempt as well as retransmissions of licensed transmissions. Interactive transmissions and certain subscription transmissions do require a license.

²⁵ Jessica Litman, *Copyright Legislation and Technological Change*, 68 OREGON L.REV. 275 (1989).

²⁶ S. Rep. No. 104-128, at 13 (1995).

²⁷ 17 U.S.C. §101 (2000).

²⁸ This creates an interesting loophole whereby an audio-only webcast must obtain a license but a music video webcast does not have to obtain a license. Of course, the webcaster would need to obtain a license to perform the music video but none of those royalties would necessarily be allocated to the performers.

Non-interactive subscription transmissions are eligible for a statutory license if they meet certain requirements: The subscription transmission must not exceed the “sound recording performance complement” which basically says you cannot transmit more than three songs from the same album or four songs by the same artist within any three hour period. The purpose of this restriction as well as a restriction on informing listeners of when songs by particular artists would be played was to prevent users from being able to either record songs or use the webcast as a substitute for purchasing the sound recording.²⁹

Interactive services are not eligible for a statutory license and must negotiate directly with the record companies for the right to perform their sound recordings. An interactive service is defined in part as “one that enables a member of the public to receive a transmission of a program specially created for the recipient, or on request, a transmission of a particular sound recording...”³⁰ Record companies believed that interactive services pose the greatest threat to record sales. Thus, the DPRA created three categories of digital transmissions: (1) exempt transmissions, which do not require a license; (2) nonexempt transmissions that are eligible for a statutory license (primarily non-interactive subscription transmissions); and (3) nonexempt transmissions that are not eligible for a statutory license (primarily interactive transmissions).

²⁹ S. Rep. No. 104-128, at 24-25 (1995).

³⁰ 17 U.S.C. §114(j)(7).

Digital Performance Rights in Sound Recordings Act of 1995

Type of transmission	License required	Statutory license available
Analog transmission	No	N/a
Audiovisual transmission	No	N/a
Non-interactive, non-subscription transmission (including FCC radio stations)	No	N/a
Retransmissions of non-interactive, non-subscription <i>broadcast</i> transmissions (basically within 150 miles of the transmitter), <i>whether the retransmission is subscription or non-subscription in nature</i>	No	N/a
Transmissions to (or within) a business establishment	No	N/a
Subscription transmissions that (1) are not interactive, (2) do not exceed the sound recording complement, and (3) do not preannounce the time when songs will be played	Yes	Yes
Simultaneous retransmissions of eligible subscription transmissions	No	N/a
Interactive transmissions	Yes	No
Simultaneous retransmissions of interactive transmissions	No	N/a

The 1995 Act also put restrictions on the exclusive licensing agreements between copyright owners and interactive services. The purpose of these restrictions was to prevent the major record labels, which hold the rights to 90 percent of the popular sound recordings in the United States, from monopolizing the market for interactive digital performances.³¹

The most important aspect of the 1995 law was that all non-interactive, non-subscription digital audio transmissions were exempt from the new performance right for sound recordings. Both terrestrial radio stations that chose to simulcast on the Internet and Internet-only webcasters could perform sound recordings for free.³² At the time the law was written, webcasting was a nascent technology and Internet connection speeds were too slow to fully utilize the technology. By 1998, webcasting had

³¹ S. Rep. No. 104-128, at 25 (1995).

proliferated with hundreds of radio stations and webcasters streaming music on the Internet. As Congress prepared to pass the Digital Millennium Copyright Act, the RIAA successfully lobbied to insert language to the provisions of the DPRA to close the “loophole” that prevented them from licensing non-subscription webcast performances.

V. Digital Millennium Copyright Act of 1998

The DMCA modified the exemption in section 114(d)(1). Where the 1995 Act included one exemption for “a non-subscription transmission other than a retransmission” and separate exemption for “a non-subscription broadcast transmission,” the DMCA eliminated the first exemption. Thus nonbroadcast transmissions such as webcasts were no longer exempt from the performance right in sound recordings. The DMCA also extended the statutory license to cover eligible non-subscription transmissions (i.e. non-interactive webcasts) and specified conditions for three preexisting DBS/cable subscription music services (DMX, Music Choice, and DiSH network) as well as two preexisting mobile satellite digital audio services (CD Radio and American Mobile Radio).

All transmissions eligible for the statutory license must (1) be non-interactive, (2) not cause a receiving device to switch channels (unless the transmission is to a business establishment),³³ and (3) include copyright management information contained in the sound recording. The five preexisting subscription services cannot (1) exceed the sound

³² 17 U.S.C. §114(d)(1)(A)(i-iii).

³³ The purpose of this clause is to make sure webcasters cannot exceed the sound recording performance complement by switching listeners from one channel to another. The exception for businesses makes little sense since transmissions made to a business establishment are apparently exempt from licensing under section 114(d)(1)(C)(iv).

recording performance complement or (2) publish or announce song titles in advance. All other eligible transmissions (non-interactive, non-subscription transmissions and subscription transmissions made by new services) (1) cannot exceed the performance complement unless it is a third party retransmission of a broadcast transmission (as long as the broadcast station does not regularly exceed the performance complement), (2) cannot announce or publish song titles in advance (except for announcing the names of upcoming artists within an unspecified time period), (3) cannot repeat programs of less than three hours in length, archive programs less than five hours in length, or maintain archived programs of more than five hours in length for more than two weeks, transmit the same sound recording repeatedly with the same visual information (so that the song is associated with a particular advertisement or message without the copyright owner's consent), etc.³⁴ Ultimately, the purpose of these detailed provisions is to prevent users from being able to predict which artists or songs will be played at a given time so that the users cannot (1) record the transmission to avoid purchasing a copy of the phonorecord or (2) tune in the transmission as a substitute for purchasing the phonorecord.³⁵ One unique aspect of the DMCA amendment is that in order to be eligible for the statutory license for non-subscription transmissions, a website that streams music must do so for entertainment purposes rather than simply as a promotion for particular products or services. Thus, Ford Motor Company would not be able to use the statutory license to create a webcasting service as background music

³⁴ The remaining *six* conditions simply further attempt to prevent users from being able to use these transmissions as a substitute for purchase of the sound recordings.

for its corporate website. However, sites that promote or sell music-related products can still take advantage of the statutory license.

Digital Millennium Copyright Act of 1998

Type of transmission	License required	Statutory license available
Analog transmission	No	n/a
Audiovisual transmission	No	n/a
Non-interactive, non-subscription <i>over-the-air</i> broadcast transmission (only FCC licensed stations)	No	n/a
Retransmissions of non-interactive, non-subscription <i>broadcast</i> transmissions (basically within 150 miles of the transmitter), <i>whether the retransmission is subscription or non-subscription in nature</i>	No	n/a
Transmissions to (or within) a business establishment	No	n/a
Subscription transmissions that (1) are not interactive (2) do not exceed the sound recording complement and (3) do not preannounce the time when songs will be played	Yes	Yes IF: follow set limits on archiving and repeating programs, etc. Special rules apply for certain preexisting subscription services: DMX, DiSH, Music Choice, CD Radio, and American Mobile Radio
Simultaneous retransmissions of eligible subscription transmissions	No	n/a
Interactive transmissions	Yes	No
Simultaneous retransmissions of interactive transmissions	No	n/a
Non-subscription transmissions other than FCC-licensed <i>over-the-air</i> broadcast transmissions	Yes	Yes IF: (1) non-interactive, (2) does not exceed sound recording complement, (3) does not preannounce song titles in a manner that allows listeners to know when songs will be played, (4) includes copyright management information and anticopying technology where feasible, (5) follows set limits on archiving and repeating programs, (6) does not associate specific sound recordings with specific visual images in a manner that is likely to cause confusion, (7) is part of an entertainment offering to the public not associated with a nonmusic-related website.

After the DMCA was passed, broadcasters argued that simultaneous Internet streaming of radio programming was exempt from licensing under section 114(d)(1)(A),

³⁵ Jane C. Ginsburg, *Copyright Legislation for the "Digital Millennium"*, 23 COLUM.-VLA J.L. & ARTS 137, 167

which exempts broadcast transmissions. The RIAA argued that the exemption only applied to “over-the-air” transmissions and that Internet transmissions must be licensed, even if it is the identical programming and source. The Copyright Office issued a ruling that Internet transmissions by broadcast stations are not exempt from the licensing requirements.³⁶ The Copyright Office reasoned that Congress did not intend to exempt webcasting when the DPRA was passed in 1995 because Congress was unaware of webcasting at that time and that Congress did not change the broadcast exemption in 1998 even after specifically modifying the law to encompass webcasting. A broadcast transmission is defined as “a transmission made by a terrestrial broadcast station licensed *as such* by the Federal Communications Commission.”³⁷ The Copyright Office agreed with the RIAA and DiMA that the word “terrestrial” is meant to limit the exemption to over-the-air broadcasts and that inclusion of the words “as such” limits the exemption to the activities that are licensed by the FCC. In addition, Congress repeatedly used the phrase “over-the air” to identify the broadcasts it sought to exempt.³⁸ The Copyright Office also noted that its interpretation made the most sense since retransmissions of broadcast signals are only exempt under certain circumstances:

The Copyright Office believes that the narrowly drawn safe harbors for retransmissions of radio signals illustrate Congressional intent to distinguish between a traditional over-the-air broadcast transmission of an AM/FM radio signal and a retransmission of that signal.³⁹

(1999).

³⁶ Public Performance of Sound Recordings: Definition of a Service, 65 Fed. Reg. 77292 (Dec. 11, 2000).

³⁷ 17 U.S.C. 114(j)(3) [emphasis added].

³⁸ Public Performance of Sound Recordings: Definition of a Service, 65 Fed. Reg. at 77298 (Dec. 11, 2000).

³⁹ *Id.* at 77299.

In addition, the Copyright Office agreed with copyright owners that since the section 112 exemption does not allow broadcasters to make ephemeral recordings for Internet transmissions, it is unlikely that Congress intended to exempt those transmissions in Section 114.⁴⁰ The Copyright Office also noted that it would be illogical for Congress to grant broadcasters an exemption for streaming their terrestrial signals but require other parties to pay a license fee to stream the exact same signals. If the broadcasters were correct in their interpretation that the exemption covers all transmissions by a broadcaster, then broadcasters could create Internet-only, exempt transmissions while third-parties could not. It would also allow broadcasters to avoid the specific limits on pre-announcing songs and exceeding the sound recording performance complement. Therefore, the Copyright Office ruled that only the over-the-air transmissions by broadcasters are exempt from the licensing requirements of Section 114.

The broadcasters appealed the ruling and lost in *Bonneville v. Peters*.⁴¹ The court held that the ruling was reasonable and within the power of the Copyright Office to make. The court went even further and stated in dicta that it would have reached the same conclusion as the copyright office if forced to answer the question itself.⁴²

VI. Ephemeral recordings

In addition to the performance license required by section 114, webcasting entails the making of ephemeral copies of the sound recording and the musical composition.

⁴⁰ *Id.* at 77300.

⁴¹ *Bonneville Int'l Corp. v. Peters*, 153 F. Supp 2d 763 (E.D. Pa. 2001).

⁴² *Id.* at 784.

As noted earlier, the RIAA negotiated an agreement with NMPA to license the incidental reproductions related to on-demand streaming and temporary downloads of sound recordings containing musical compositions.⁴³ As part of the agreement, the NMPA agreed not to seek royalties for the copies of songs made during the course of webcasts that are eligible for the section 114(d)(2) statutory license.

There is still the matter of the ephemeral copy of the sound recording itself. Section 112 provides for a statutory license for eligible webcasters to make a copy of the sound recording to facilitate the licensed performance transmission.⁴⁴ Only those entitled to transmit a performance under section 114(d)(1)(C)(iv) – transmissions to a business establishment, and those entitled to transmit a performance under section 114(f) – subscription and non-subscription services that are eligible for a statutory license under 114, can take advantage of the statutory license for ephemeral recordings.

VII. CARP Report

The provisions of sections 112 and 114 direct the Copyright Office to form Copyright Arbitration Royalty Panels (CARP) if industry groups cannot negotiate acceptable royalty rates for the respective statutory licenses. The CARP proceeding for pre-existing subscription cable/satellite and satellite radio services uses the criteria detailed in section 801(b)(1) for establishing the statutory rate. The panel “may consider the rates and terms for comparable types of subscription digital audio transmission

⁴³ Agreement between NMPA, Harry Fox Agency and the RIAA, (Oct. 9, 2001) <http://nmpa.org/pr/FinalRIAAAgreement.pdf>

⁴⁴ 17 U.S.C. §112(e).

services and comparable circumstances under voluntary license agreements...”⁴⁵ The process is repeated every five years. The criteria under section 801(b)(1) are as follows:

- (A) To maximize the availability of creative works to the public;
- (B) To afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions;
- (C) To reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk, and contribution to the opening of new markets for creative expression and media for their communication;
- (D) To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices.

In a significant departure from these criteria, the CARP proceeding for new subscription services and eligible non-subscription services (such as non-subscription webcasts) establishes a more limited set of criteria for establishing rates. The panel “shall establish rates and terms that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and willing seller.”⁴⁶ Thus, the panel may not consider goals A through D listed above when setting the statutory rate. The rate setting procedure is repeated every two years.

In February 2002, a CARP issued its report recommending statutory rates for non-interactive, non-subscription, eligible transmissions (*i.e.* webcasts). The CARP distinguished between three types of webcasts targeted to the general public: (1) simultaneous retransmissions of over-the-air radio broadcasts, (2) all other Internet

⁴⁵ 17 U.S.C. §114(f)(1)(B).

⁴⁶ 17. U.S.C. §114(f)(2)(B).

transmissions, (3) and transmissions by non-CPB affiliated noncommercial broadcasters.⁴⁷

CARP section 114 analysis

The statute required that the panel establish “rates and terms that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller.”⁴⁸ One question was whether the RIAA should constitute a single seller (in which case the private agreements it reached with webcasters would be the appropriate benchmark) or whether the panel should envision an hypothetical market with multiple collective agencies, each able to license all sound recordings.⁴⁹ The panel chose a middle ground “where the buyers are DMCA-eligible services, the sellers are record companies, and the product being sold consists of blanket licenses for each record company’s repertory of sound recordings.”⁵⁰

The RIAA had entered into agreements with 26 separate webcasters and offered those agreements as a benchmark for the statutory rate. The RIAA proposed the following rates:

Type of service	Section 114 license	Section 112 license	Minimum fee
Business to consumer webcast (B2C)	0.4 cents per transmission per listener OR 15% of gross revenues	10% of section 114 license fee	\$5000
B2B webcast	0.5 cents per transmission per listener	10% of section 114 license fee	\$5000
“Listener-influenced” webcast	0.6 cents per transmission per listener	10% of section 114 license fee	\$5000

⁴⁷ CPB-affiliated broadcasters (i.e. NPR affiliated stations) had already negotiated a private license agreement with the RIAA.

⁴⁸ 17 U.S.C. §114(f)(2)(B).

⁴⁹ In the Matter of Rate Setting for Digital Performance Right in Sound Recordings and Ephemeral Recordings, Dkt. 2000-9 at 22 (Feb. 20, 2002) [hereinafter CARP Report].

⁵⁰ *Id.* at 24.

The webcasters countered with a fee based on what radio stations pay to perform the underlying musical works.⁵¹ They then raised this amount slightly since webcasters play an average of 15 songs per hour compared to an average of 11 songs per hour on the radio. They then discounted the rate based on the “promotional value” of streaming in helping record companies to sell their sound recordings. Ultimately the webcasters proposed a payment of 0.014 cents per song or 0.21 cents per hour per listener.⁵² In addition, webcasters argued there should be no distinction between the different types of webcasting services as long as they all met the requirements for the statutory license, and they argued that no minimum fee should be imposed.

In reaching its conclusion and applying the statutory factors the CARP concluded that it could not determine whether webcasting had a positive or negative effect on record sales. In an important aspect of its decision, the CARP determined that the license should be based on a per performance fee rather than set as a percentage of revenues. The panel noted that a per-performance metric is directly connected to the right being licensed and percentage of revenue is difficult to implement because of the difficulty in determining which revenues are related to the performance, and finally, a revenue metric would mean that copyright owners would not be fully compensated since many webcasters generate very little revenue.⁵³

⁵¹ This required taking the yearly fee for a sample of music-intensive radio stations and calculating an average fee per listening hour and then dividing that figure by the average number of songs played per hour to obtain a per song fee.

⁵² CARP Report *supra* note 49 at 30.

⁵³ *Id.* at 37.

Ultimately the panel rejected the webcasters theoretical model for determining royalty rates in part because it is based upon a dozen questionable assumptions, including different rights (song versus sound recording) and different technologies (radio versus Internet). The panel then looked at the 26 RIAA license agreements as a potential benchmark for the statutory rate.

The panel rejected 25 of the 26 agreements as benchmarks because the agreements reflected artificially high rates to influence the CARP proceeding and many of the companies were unable to sustain operations. Many of the webcasters who negotiated with the RIAA were in an unfair position due to ongoing litigation and negative publicity among other reasons.⁵⁴ The panel felt that the RIAA had only agreed to deals that were skewed highly in its favor to influence the rate set by the panel.

The CARP did pay credence to the agreement between Yahoo! and the RIAA. Yahoo is a webcast aggregator that streams hundreds of Internet-only (IO) channels and hundreds of broadcast radio retransmissions (RR). Since Yahoo was a large company with significant resources, the panel felt it would be on equal footing with the RIAA during the negotiations. However, the panel noted that Yahoo's interests in negotiating a license were not identical to the interests of other webcasters. The panel determined that because Yahoo was only concerned with the total license fee, it was willing to negotiate an artificially high rate and an artificially low RR rate in order to obtain an acceptable overall rate. The RIAA was more concerned with creating a high IO rate to influence the CARP proceeding, especially since at the time of the negotiation it was

unclear if radio stations would be forced to pay any license fee for their Internet transmissions.⁵⁵

The CARP did accept the premise that the marketplace would establish lower rates for radio retransmissions than Internet only transmissions because of the promotional value of radio broadcasts.⁵⁶ It then determined the IO rate should be the midpoint between the artificially high IO rate from the Yahoo agreement and the “blended rate” (the overall rate Yahoo paid when combining payments made under the IO and RR rates).⁵⁷ The midpoint was 0.14 cents per sound recording per listener. The panel used the same reasoning to raise the artificially low RR rate to 0.07 cents per sound recording per listener.⁵⁸ Later the panel noted that the lower rate for RR transmissions was also warranted because there was some evidence that record companies perceive less risk to record sales from typical radio retransmissions than the niche programming provided on most Internet-only transmissions (which typically focus on a narrow genre and are thus more likely to serve as a substitute for record purchases than broad-based radio playlists).⁵⁹

The panel rejected the RIAA’s claim that B2B webcasters (those that provide syndicated webcasting services for third parties) should pay a higher rate. The panel also rejected the RIAA’s contention that listener-influenced webcasts should pay a

⁵⁴ *Id.* at 59-60.

⁵⁵ *Id.* at 65-69.

⁵⁶ *Id.* at 74-75.

⁵⁷ *Id.* at 76. Analyzing this section of the CARP report is extremely difficult since much of the material has been redacted from the public version.

⁵⁸ *Id.* at 77.

⁵⁹ *Id.* at 84.

higher royalty rate. The panel noted that the RIAA claimed that these services are ineligible for a statutory license to begin with. The panel did not feel equipped to define the myriad of services that qualify for the statutory license but yet should be charged a higher royalty rate: “We conclude that so long as a service complies with, and is deemed eligible for the statutory license, it should not pay a separate rate based upon listener influence.”⁶⁰ The panel also reasoned that archived radio programming and other Internet programming by radio stations that is *not* a simulcast of the station’s over-the-air signal should be licensed at the IO rate (0.14 cents per sound recording per listener).

In setting a rate for noncommercial broadcasters that were not already covered by an agreement between the RIAA and NPR-affiliated stations, the panel accepted the RIAA’s argument that a prior CARP had granted non-commercial broadcasters a 2/3 discount from the commercial royalty rate for musical compositions. Therefore, the panel set a rate of 0.02 cents for simulcasts and 0.05 cents for archived programming and up to two side channels (1/3 the rate for commercial RR transmissions).⁶¹

CARP section 112(e) analysis

As noted earlier, streaming requires ephemeral copies of sound recordings. Each webcaster is allowed to make one exempt ephemeral copy, but any additional copies are subject to a statutory license as provided by section 112(e). Also as noted earlier, the Copyright Office believes ephemeral copies have no independent value and that

⁶⁰ *Id.* at 81.

⁶¹ *Id.* at 93.

Congress should amend the law to eliminate the license requirement. In looking at the 26 agreements between the RIAA and webcasters, the panel again looked most closely at the Yahoo agreement, which in this case was a flat fee that worked out to 8.8 percent of the total section 114 royalties. Because eight of the other agreements between the RIAA and webcasters had ephemeral license rates of approximately 10%, the panel decided to “round up” from the Yahoo agreement of 8.8% and set the license fee for ephemeral recordings at 9.0 percent.⁶² The panel also set a minimum fee of \$500 for combined section 112 and 114 licenses.

Final CARP Panel ruling on relevant webcast royalty rates

Type of service	Section 114 performance fee	Section 112 ephemeral copy
Simultaneous retransmission of a broadcast signal	0.07 cents per song per listener	9% of performance fee
All other Internet transmissions	0.14 cents per song per listener	9% of performance fee
Simultaneous retransmission of a non-profit, non-CPB broadcast signal	0.02 cents per song per listener	9% of performance fee
Archived programming and up to 2 side channels of a non-profit, non-CPB broadcast signal	0.05 cents per song per listener	9% of performance fee

VIII. Librarian of Congress’ Ruling

After the CARP panel issued its report, the Register of Copyrights recommended that the Librarian of Congress *reject* some of the rates set by the panel.⁶³ Predictably, the

⁶² *Id.* at 104. However the eight agreements were not used in setting the section 114 royalty rate because of the unfair bargaining position of the RIAA.

⁶³ In the Matter of Digital Performance Right in Sound Recordings and Ephemeral Recordings, (May 21, 2002). The Librarian issued his final rule in: Determination of Reasonable Rates and Terms for the Digital

RIAA argued that the rates were set too low and the webcasters argued that the rates were set too high. The webcasters also argued that the CARP panel was arbitrary in not establishing an alternative rate based on percentage of revenue. The Librarian noted that while the panel could have included an alternative fee structure, it was not obligated to do so.⁶⁴ The Librarian did indeed modify the rates, most importantly by reducing the standard Internet-only (IO) rate from 0.14 cents to 0.07 cents; the same rate used for radio retransmissions (simulcasts of over-the-air radio stations.).

The key decision of the Librarian (based on the Register's recommendation) was to reject the CARP panel's conclusion that simulcasts of radio signals should enjoy a lower rate than Internet-only transmissions. The panel had based its conclusion on the fact that the RIAA had negotiated separate rates with Yahoo for the two different types of webcasts. The Librarian concluded that the panel's conclusion was arbitrary based on the evidence:

The question, however, is whether the rates in the Yahoo! agreement represent distinct valuations of Internet-only transmissions and radio retransmissions. Ultimately, the Register concludes that they do not and, therefore, the Panel's reliance on these specific rates for IO transmissions and radio retransmissions as a tool for setting the statutory rates is arbitrary. The fundamental flaw in the Panel's analysis, though, is not its acceptance of the Yahoo! agreement as a starting point. Rather, it is the Panel's determination that the differential rate structure reflects a true distinction in value between Internet-only transmissions and radio retransmissions based upon the promotional value to the record companies and performers due to airplay of their music by local radio stations. The Panel reached this conclusion in spite of the fact that nothing in the record indicates that the parties considered the promotional value of radio retransmissions over the Internet when they negotiated these rates.⁶⁵

Performance of Sound Recordings and Ephemeral Recordings; Final Rule, 67 Fed. Reg. 45239 (July 8, 2002) [hereinafter Register's Report].

⁶⁴ *Id.* at 24250.

⁶⁵ *Id.* at 45252.

The Librarian noted that the CARP concluded that the distinction between RR and IO rates in the Yahoo Agreement was “developed to effectuate particular objectives of the parties, distinct and apart from establishing an actual valuation of the performances.”⁶⁶

The Librarian’s report notes that the CARP panel ignored its own conclusion that there was no determinate evidence that webcasting has a beneficial effect on record sales.

The Librarian then used the combined Yahoo payments to determine the cost of the performances, yielding a “blended” rate of 0.065 cents per performance.⁶⁷ In addition, Yahoo had paid an effective rate of 0.083 cents for the first 1.5 billion transmissions. The Librarian then felt comfortable in choosing 0.07 cents as a middle ground between the two rates. In addition, the Librarian ruled that the exemption for retransmissions of radio transmissions within 150 miles of the transmitter does *not* apply to Internet retransmissions.⁶⁸ This conclusion was based on the fact that Congress did not provide a section 112 exemption for the ephemeral recording required to make such a transmission. Because the Librarian had lowered the rate for all IO transmissions (including archived programs and side channels) to 0.07 cents, it similarly reduced the royalty rate for archived programs by non-commercial broadcasters to 0.02 cents.

⁶⁶ *Id.*

⁶⁷ *Id.* at 45255.

⁶⁸ *Id.* at 45256. Section 114(d)(1)(B) provides the exemption within 150 miles of the transmitter.

In terms of the section 112 license fees, the Librarian ruled that the Panel should not have given weight to the 25 voluntary agreements which it had discounted in setting the section 114 rates:

What causes concern, however, is the Panel's reliance, even to a small degree, on the ephemeral rates set forth in eight of the 25 voluntary agreements it had previously repudiated. Such action is arbitrary unless the Panel can offer a clear explanation for its actions. It did not do so and, in fact, it stated that its review of the 26 licenses "reveals an inconsistent, rather than a consistent, pattern."⁶⁹

Therefore the Librarian set the rate at 8.8 percent, based on the Yahoo agreement.

Librarian's final ruling on relevant webcast royalty rates

Type of service	Section 114 performance fee	Section 112 ephemeral copy
Simultaneous retransmission of a broadcast signal	0.07 cents per song per listener	8.8% of performance fee
All other Internet transmissions	0.07 cents per song per listener	8.8% of performance fee
Simultaneous retransmission of a non-profit, non-CPB broadcast signal	0.02 cents per song per listener	8.8% of performance fee
Archived programming and up to 2 side channels of a non-profit, non-CPB broadcast signal	0.02 cents per song per listener	8.8% of performance fee

Since the Librarian issued his final rule, both webcasters and the RIAA have announced they will appeal the decision to the Court of Appeals for the D.C. Circuit.⁷⁰ In the meantime a bill has been introduced in the House of Representatives to overturn the Librarian's ruling with respect to webcasters that would qualify as small businesses and to provide an exemption for ephemeral recordings used in the course of webcasting.⁷¹

⁶⁹ *Id.* at 45262.

⁷⁰ Amy Harmon, *Technology Briefing Internet: Royalty Rates Will Be Appealed*, N.Y. TIMES, Aug. 8, 2002 at C5.

⁷¹ Internet Radio Fairness Act, H.R. 5285, 107th Cong. (2002).

Still to be determined are the record-keeping requirements that webcasters will have to implement to make sure copyright owners are properly compensated. This will be another crucial issue as the interim requirements suggested by the Librarian are potentially burdensome and expensive to implement, especially for small, non-profit webcasters such as college radio stations.

IX. Analysis

While the RIAA has argued that its works are being undervalued, most of the protest and hyperbole has come from webcasters. Most webcasters earn little to no revenue from their transmissions and argue they will be forced to shut down operation because they cannot afford the royalty payments.⁷² Part of the challenge in setting industry-wide rates that reflect a “willing buyer-willing seller” standard is the huge disparity between different groups of buyers. Yahoo, RealNetworks, and other large webcasters distribute hundreds of channels and are owned by multi-billion dollar corporations. On the other side of the divide, thousands of small webcasters have almost no resources or financial backing. Clearly Yahoo can afford to pay a higher rate than an individual attempting to start a webcasting business out of her living room.

One of the controversies that has emerged since the CARP issued its report is the admission of Mark Cuban, former president of Broadcast.com, that Yahoo was willing to agree to a high royalty rate in part to drive smaller webcasters out of business. In a letter to the Radio and Internet Newsletter (RAIN), Cuban wrote:

⁷² Christopher Stern, *Curtain Call for Webcasts?* WASH. POST, June 21, 2002 at E1; Jefferson Graham, *Royalty Fees Killing Most Internet Radio Stations*, USA TODAY, July 21, 2002.

I, as Broadcast.com, didn't want percent-of-revenue pricing. Why? Because it meant every "Tom, Dick, and Harry" webcaster could come in and undercut our pricing because we had revenue and they didn't....As an extension to that, I also wanted there to be an advantage to aggregators. If there was a charge per song, it's obvious a lot of webcasters couldn't afford to stay in business on their own. THEREFORE, they would have to come to Broadcast.com to use our services....⁷³

This letter highlights the fact that the Yahoo deal, which formed the basis of the CARP rates and the Librarian's final rate determination, is an inappropriate benchmark and puts the thousands of small webcasters at a significant disadvantage.

Two other studies also suggest the current royalty rates are too high. A report issued by Jupiter Research concludes that under current revenue models, most webcasters cannot afford the royalty fees.⁷⁴ NetRadio would have paid more than \$725,000 in royalties, consuming more than forty percent of its revenues. A paper by Carol Ting and Steven Wildman at Michigan State University concludes that the distribution costs of Internet radio alone are higher than expected revenues.⁷⁵ Thus, webcasters were struggling to make a profit even before sound recording royalties were imposed. In addition, unlike over-the-air broadcasting, distribution costs for webcasters increase significantly as the size of the audience increases.⁷⁶

This is not to suggest that webcasters should be allowed to perform the sound recordings for free. Just as songwriters earn performance royalties, performing artists

⁷³ Mark Cuban, e-mail letter to RAIN, June 24, 2002 [emphasis in original]. Available online: <http://www.kurthanson.com/archive/news/062402/index.asp> Note: Cuban had left Broadcast.com before Yahoo reached its final agreement with the RIAA.

⁷⁴ Internet Radio: Post-CARP Survival Scenarios, MUS02-U06, Jupiter Research (2002). Executive summary on file with author.

⁷⁵ Carol Ting and Steven S. Wildman, The Economics of Internet Radio, Paper submitted to the Telecommunications Policy Research Conference, Sept. 2002.

⁷⁶ *Id.*

should earn royalties as well. What then should be the appropriate benchmark for the royalty rate? At the outset it is important to note that the CARP and Librarian were constrained by the specific rate-setting criteria established by Congress. Most CARPs are allowed to consider the criteria under section 801(b)(1) which allow the CARP to consider public policy objectives such as maximizing the availability of creative works and minimizing the disruptive impact on the structure of the involved industries.⁷⁷ However the rates for eligible non-subscription transmissions must be “rates and terms that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and willing seller.”⁷⁸ The CARP was not free to consider other policy objectives in setting the rates. Section 114(f)(2) includes two additional criteria to be used in determining the willing buyer/willing seller rates:

In determining such rates and terms, the copyright arbitration royalty panel shall base its decision on economic, competitive and programming information presented by the parties, including-

(i) whether use of the service may substitute for or may promote the sales of phonorecords or otherwise may interfere with or may enhance the sound recording copyright owner's other streams of revenue from its sound recordings; and

(ii) the relative roles of the copyright owner and the transmitting entity in the copyrighted work and the service made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, and risk.

These criteria do not add flexibility as they simply reflect the considerations that willing buyers and sellers will take into account in the normal course of their negotiations.

⁷⁷ 17 U.S.C. §801(b)(1).

⁷⁸ 17. U.S.C. §114(f)(2)(B).

It is useful to compare the royalties paid for the sound recording to the royalties paid for the underlying musical composition. In a prior proceeding for preexisting subscription services, the CARP recognized that the PRO license fees were useful in establishing a range of rates but the fees were not determinative of the marketplace value for the sound recording performance rights.⁷⁹ In the proceedings for non-subscription webcasts, the webcasters offered a theoretical model based on the license fees paid to the PROs. The CARP panel and the Librarian rejected that model for a number of reasons including. First, the theoretical model is based upon numerous assumptions, including that the performance rights in musical works and sound recordings are analogous, different delivery systems (over-the-air vs. Internet) are analogous, and that different royalty metrics (percentage of revenue vs. per-performance) can be converted into one another.⁸⁰ In addition, the panel rejected the notion that the market for musical works is analogous to the market for sound recordings.

Had the panel adopted a percentage-of-revenue model, it may have been more willing to use the PRO fees as a guide. Such was the case when a CARP set the royalties for pre-existing subscription services.⁸¹ However, since the PROs license the underlying compositions to broadcast stations on a percentage-of-revenue basis, attempting to convert that fee to a per-hour or per-listener fee is difficult. Indeed, the panel rejected

⁷⁹ Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings, Dkt. No. 96-5 CARP DSTR, 63 Fed. Reg. 25394, 25404 (May 8, 1998).

⁸⁰ CARP Report *supra* note 49 at 39-40.

⁸¹ Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings, Dkt. No. 96-5 CARP DSTR, 63 Fed. Reg. 25394, 25409-10 (May 8, 1998).

webcasters' attempt to make such a conversion, in part because the resulting metric did not accurately predict the actual fees paid by various radio stations.⁸²

However, both BMI and ASCAP do offer webcasters a blanket performance license for the underlying musical work based on listener hours as well. This allows us to attempt to make some comparisons. As a simple hypothetical example, assume a station averages 1000 listeners per hour. The total cost for the section 112 and 114 licenses would be \$11.42 compared to a fee of 48 cents for ASCAP performance royalties for the underlying songs. The BMI fee would be similar, leading to a total cost of approximately \$1.00 for the song performance licenses.⁸³

Type of license	Base rate	Cost for one hour of operation with 1000 listeners (15 songs)
ASCAP performance license for the song	1.615% of revenues <i>or</i> 0.048 cents per session (up to one hour)	48 cents (Note: this would be the cost even if only one song were performed)
BMI performance license for the song	1.605% for radio simulcasts 1.75% for IO webcasts <i>or</i> 0.012 cents per page impression	Unclear, but assumed to be approximately the same (or less) than ASCAP fee ⁸⁴
Section 114 license for the sound recording	0.07 cents per performance	\$10.50
Section 112 license for the ephemeral recording	8.8% of section 114 fee	92 cents

⁸² CARP Report *supra* note 49 at 42.

⁸³ SESAC, the third PRO, uses a fee structure based on number of page requests, but with a maximum fee of less than \$2000 per year. ASCAP historically has charged the highest rates of any of the three PROs. While BMI was unwilling to provide precise numbers, it is doubtful that they would be significantly higher than the fees charged by ASCAP. In comparing their webcasting fees based on revenues, BMI currently charges 0.135% more than ASCAP (1.75% compared to 1.615%).

⁸⁴ When contacted by the author, BMI was unwilling to clarify the page impression metric. Theoretically, the fee is based on the number of separate pages visited. Thus, if a user simply went to one page to select a webcast, that user might be able to listen to hundreds of songs but only register ONE page impression at 0.012 cents. For simplicity, this paper doubles the ASCAP fee and then rounds up to estimate the total song performance license fee.

It is important to note that the per song rate for BMI and ASCAP increases when listeners stay tuned for less than one hour. Even if the 1000 listeners only tuned in for one song, the webcaster would pay the same PRO fees, whereas the section 114 license would be reduced to 70 cents under the same conditions.

Even if we were to assume that the average listener tuned in for only 20 minutes, the ratio of the sound recording license to the musical composition license remains high. The listener would hear an average of five songs in a 20-minute span. The combined ASCAP/BMI/SESAC royalties would be approximately 0.1 cents per listener (the equivalent of 0.02 cents per song). The sound recording performance license would be 0.35 cents (0.07 cents per song). So under the current rates, webcasters are paying more than three times as much for the sound recording performance rights than the musical composition performance rights.

How does this compare with other nations that recognize both rights? The Rome Convention created a sound recording performance right for over-the-air broadcasts in 1961. In addition, the European Union's 1992 Copyright Directive created a similar right binding on EU members.⁸⁵ An analysis of the licensing fees in twelve nations reveals that the sound recording performance fee is typically smaller than the musical composition performance fee.⁸⁶ It is important to note that in each nation both license fees are based on a percentage-of-revenue. So the precise value of each right cannot easily be converted into a per-song metric. However, comparing the rates for each right

⁸⁵ Council Directive No. 92/100, Nov. 19, 1992 (European Commission).

can provide an indication of the relative value of each.⁸⁷ In his testimony, William Kempton concluded that the royalty rates for sound recordings “are no higher, and indeed, are generally set lower than the royalty rates for the musical composition.”⁸⁸ The Librarian’s decision to set the sound recording performance rate at 0.07 cents per performance compared to a musical composition performance rate of approximately 0.02 cents⁸⁹ creates a ratio of 3.5, compared to an average ratio of 0.5 to 1.0 for the equivalent rights in other countries. This suggests that the royalty rate may be higher than the true market value of the sound recording performance right. The CARP panel rejected Kempton’s analysis without explanation.⁹⁰

The panel also noted that “in determining the prices to which willing buyers and willing sellers would agree, the ‘true’ relative value – even if that could be precisely ascertained – is less important than the parties’ perception of that relative value.”⁹¹ Thus, the panel was caught in the circular logic of their mandate; to set the fee based upon what the marketplace would have determined on its own if no statutory fee were necessary. There is a particular flaw in the panel’s logic that the perceived value is more important than the true value. In a correctly functioning marketplace, the two

⁸⁶ In the Matter of Digital Performance Right in Sound Recordings and Ephemeral Recordings, Dkt. No. 2000-9, CARP DTRA 1&2, testimony of Paul William Kempton, Media Matrix Grp.

<http://www.digmedia.org/webcasting/CARP/KemptonTestimony.DOC>

⁸⁷ *Id.* at para. 11.

⁸⁸ *Id.* at para. 10.

⁸⁹ As noted above, the PROs use a “session” metric rather than a performance metric. Thus, the rate per song varies based on how long the listener tunes into the webcast. ASCAP’s fee of 0.048 cents per hour translates into a maximum of 0.048 cents per song (if the user only listens to one song) or as little as 0.0032 cents per song if the user listens to 15 songs within a one-hour time span. The 0.02 cents is based on a 20-minute transmission in which the user listens to five songs and includes payments to ASCAP, BMI, and SESAC.

⁹⁰ CARP Report *supra* note 49 at 41-42.

values should be the same. Instead we are left with a situation where the last remaining property holder can hold out for a higher rate.⁹² The panel was apparently blind to this discrepancy even though they dealt with an identical situation in evaluating the Yahoo agreement. The Yahoo agreement included one rate for IO transmissions and a different rate for RR transmissions. The panel noted that Yahoo was less concerned with the value of each individual rate and more concerned with the *total* payments it would have to pay. Similarly, webcasters are less concerned with the precise song performance rate and the sound recording performance rate and are more concerned with the *total* royalty fees they are forced to pay. It doesn't matter if those royalties are distributed equally between the songwriter and the recording artist or not. Since webcasters already knew the PRO fees they would have to pay to perform the song, they would be willing to pay any amount for the sound recording license fee *up to the combined value of both rights*. For example, if a webcaster is willing to pay up to 0.1 cents per performance and she has already agreed to pay 0.02 cents for the song performance right, then she will be willing to pay up to 0.08 cents for the sound recording performance right. This does not mean that she perceives the sound recording to be more valuable than the song. By setting the royalty fee in this manner, the Librarian is essentially preventing the PROs from raising their rates in the future, since the sound recording rate captures all of the additional value of a webcast performance.

⁹¹ *Id.* at 41.

⁹² If a property developer were buying a group of houses, the last seller can try to hold out for more money. The developer is likely to pay since that house represents the last hurdle before developing the property. Similarly, webcasters need the rights to both the song and the sound recording. Because the

Webcasters face an uphill battle with high distribution costs and the new royalty payments. It is unclear that webcasters can generate enough revenues to survive. Current advertising rates vary dramatically for webcasters but tend to range from a CPM of \$2 to \$10. Live365.com's rate card offers a variety of options. One purchase plan creates an effective CPM of \$2.33.⁹³ If the webcaster were able to sell one advertisement per song, 30% of the revenues would be allocated for the sound recording royalty. Given the nature of banner ads, it is difficult to determine the approximate inventory and revenues based on these rates. If the webcaster were able to charge a higher CPM and sell multiple ads per song, the statutory license would be a significant expense, but not necessarily insurmountable. Yet it seems clear that in the current market, such revenue projections are unrealistic.⁹⁴ The Jupiter Research report concludes that the only profitable content for webcasting in the near term is news/talk and sports since they are not governed by the statutory rate.⁹⁵

X. Conclusion

It is easy to sympathize with the Internet hobbyist who decides to share his or her music collection by webcasting. Many webcasters set up Internet radio stations for fun rather than profit. Economists can endlessly debate whether the specific royalty rates adopted by the Librarian are "fair" to recording artists or webcasters. There is something surreal about a law that requires an arbitration panel to establish rates that

royalty fees for the song have already been agreed upon, the RIAA has improved negotiating power as the last seller.

⁹³ Live365.com sales presentation. On file with author.

⁹⁴ See e.g. Emma Cowing, *Poor Performance of Internet Adverts Creates Buyer's Market*, THE SCOTSMAN, Dec. 4, 2001 at 5.

“would have been negotiated in the marketplace...” The obvious answer would be to let the marketplace set the rates. Of course, unequal market power makes that problematic to say the least. At the same time, to the extent that broadcasters and webcasters argue that the rates are higher than the true market value, nothing prevents them from negotiating with record companies for better rates. Indeed one record company has already made headlines by offering to waive the license fee for one year.⁹⁶ This will encourage webcasters to play those sound recordings. In a truly competitive market, other record companies would soon try to get their recordings played as well (assuming they believe such performances have value).

The normal justification for compulsory licenses is the high transaction costs of dealing with countless copyright owners. Yet most webcasts focus on a much narrower range of music. In addition, while there are thousands upon thousands of different copyright owners for the underlying songs, there are a relatively small number of copyright owners who control the sound recordings. Therefore the transaction costs are not insurmountable. A webcaster that plays folk music would only need to negotiate with labels offering that particular genre. This is one area where the market should be able to develop a clearinghouse on its own, just as there is a clearinghouse for book reproduction rights that still allows each publisher to set its own license rate. It is also important to remember that the statutory rate represents the *ceiling* in terms of costs. It

⁹⁵ Internet Radio, *supra* note 74.

⁹⁶ *Artemis Records to Waive Webcast Fees*, L.A. TIMES, July 30, 2002.

is very likely that webcasters would be able to negotiate cheaper rates by working directly with the record companies.

From a public policy perspective, other key questions emerge:

- Will the current structure and rates give over-the-air radio an unfair advantage over webcasting?
- Will the current structure and rates give webcasting aggregators an unfair advantage over small independent webcasters?
- Is there a reason we (as a society) should want to encourage the performance of sound recordings as compared to other types of content such as movies, plays, etc.?
- How will the current structure and rates affect the structure of the recording industry?

Will the current structure and rates give over-the-air radio an unfair advantage over webcasting? The answer to this question appears to be “yes.” Over-the-air radio currently enjoys two significant advantages over webcasting: portability and static distribution costs. Most radio listening takes place in automobiles. As 3G wireless technology matures, consumers will be able to listen to high quality webcasts on portable devices. Thus, webcasting may offer a reasonable substitute for radio. From this perspective, the sound recording license fee put webcasters at a significant disadvantage since radio stations do not have to pay the license fee. This may be a moot point since the distribution costs already give radio a huge advantage over webcasting. As noted above, webcast distribution costs increase as the audience grows, while radio distribution costs (already quite low) do not.⁹⁷ Webcasting does have one advantage over radio and that is its worldwide reach. Thus webcasts can be narrowly

⁹⁷ See Ting and Wildman, *supra* note 75.

tailored to reach a specific segment of the market that would be too small to target on a citywide basis. Advertisers are often willing to pay a premium to reach a more homogenous audience that fits the profile for the product being advertised. Whether this webcasting advantage over radio is enough to overcome the increased distribution and royalty costs remains to be seen, but it appears as though radio has the advantage for now – at least until portable Internet access becomes widespread.

Will the current structure and rates give webcasting aggregators an unfair advantage over small independent webcasters? As Mark Cuban noted in his letter to RAIN, the per performance royalty fee gives large aggregators with established revenues a huge advantage over small webcast start up companies.⁹⁸ Webcasters will have difficulty in attracting any advertising revenues until they have attracted a significant audience. As Cuban pointed out, this will force most webcasters to turn to a large aggregator to distribute their channels unless they are able to negotiate reduced royalty rates with copyright owners.

Is there a reason we (as a society) should want to encourage the performance of sound recordings as compared to other types of content such as movies, plays, etc.?

This broader social question reveals a fundamental anomaly in copyright law. While Congress has created statutory licenses for *retransmissions* of television programs, this is the first instance where it has created a statutory license for the initial transmission of content.⁹⁹ The only comparable compulsory license is for mechanical reproductions of

⁹⁸ See Cuban, *supra* note 73.

⁹⁹ The Copyright Act provides for compulsory licensing of cable retransmissions (§111) and satellite retransmissions (§§119 & 122).

musical compositions.¹⁰⁰ The mechanical license for songs was adopted to prevent monopolization of the market for piano rolls in the early 20th century. Since that time, it has encouraged the creation of “cover songs” of popular music.¹⁰¹ No other type of content can be transmitted on the Internet without the explicit permission of the copyright owner. Is there a reason why individuals should have special access to music on the Internet compared to newspaper stories, books, movies, or paintings?

This is not to suggest that music has no place in our cultural life. Music is a significant art form that has played a key role in culture since before recorded history. But recorded music is also a product and there is no reason why the producer should have to share that product any more than he or she wants to. Each individual is free to make his or her own music and share it at will. Indeed, with the compulsory license for songs, anyone can record someone else’s music and distribute that as well. What is important about copyright is that the law not prevent someone from commenting on the content that is put into the “marketplace of ideas.”¹⁰² That doesn’t mean the law needs to provide special access to streaming songs versus any other type of content. If the purpose of promoting webcasting is to provide competition for radio, then radio must be forced to pay the same license fees.

How will the current structure and rates affect the structure of the recording industry? If a recurring concern is that record companies control too many copyrights, then how does giving webcasters special access to their recordings reduce the continued

¹⁰⁰ 17 U.S.C. §115.

¹⁰¹ An interesting topic that will be saved for another paper.

relevance of the labels? By keeping the royalty rate artificially low, record companies have no effective way to engage in price discrimination. This perhaps puts lesser known artists at a disadvantage since they cannot effectively offer a lower “introductory” price. For example, if webcasters can perform popular recordings (in any genre of music) for a nominal fee, they have less incentive to perform unknown works, even if offered for free, since there is little cost savings compared to the popular recording. On the other hand, if popular recordings command a high performance fee then lesser known artists may be able to garner some airplay by offering a significantly lower fee. The worst case scenario is that popular recordings are also offered at a reduced rate, which is what the webcasters are asking for in the first place.

Assume the opposite: that most record labels refuse to negotiate reasonable fees, thus curtailing the amount of webcasting. Perhaps record labels would prefer that webcasting not develop as an industry. If record companies make it more difficult for the public to hear their roster of bands, then won't they be disserving the bands themselves? Wouldn't that lead some bands to decide that signing with a major label does more harm than good? Perhaps that would be the most effective way to reduce the importance of the record labels.

The risk, of course, is that record labels will engage in anti-competitive conduct, favoring affiliated webcasters over independent webcasters, and more significantly, maintaining the status quo whereby over-the-air radio is the primary means of

¹⁰² See, e.g. Matt Jackson, *Using Technology to Circumvent the Law: The DMCA's Push To Privatize Copyright*, 23 HASTINGS COMM/ENT L.J. 607, 615-19 (2001).

promoting records. Clearly the oligopolistic “big five” record labels have an advantage over smaller labels in getting radio airplay, especially as radio also becomes more oligopolistic with increased consolidation. This leads us back to the first, and most significant problem: radio currently enjoys an unfair advantage over webcasting since radio does not need to pay a license fee to perform sound recordings. Correcting this discrepancy should be a top priority for Congress.

It is easy to hate the “music industry” for its commodification of such an essential art form. The dominance of the major record labels and radio stations compels us to cheer for independent labels and webcasters. But if we hate the major labels, then why should we care if webcasters have easy access to their recordings? If we want radio (or webcasting) to be more than a promotional vehicle for “product,” then why not encourage webcasters to do more than play prerecorded music? An unintended consequence of the royalty rates may be that more webcasters turn to talk, debate, and find new creative uses for streaming that do not simply try to improve radio with more eclectic song lists but instead truly find new uses for a new medium. Perhaps in the end, we will say the Librarian’s decision is a blessing in disguise.