

MARKET IMPERFECTION AND FAILED GOVERNANCE: THE CASE OF MUSIC PERFORMING RIGHTS

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Introduction

ASCAP (American Society of Composers, Authors, and Publishers) and BMI (Broadcast Music Inc.) are the two major U.S. performance rights organizations (PROs) empowered with the authority to license the music performance rights of their songwriter, composer, and publisher membership base. The two provide an administrative service to prospective users who otherwise might need to deal directly with each writer to avoid copyright infringement. To do this, each PRO makes music catalog available to most licensees through blanket fee arrangements that offer to users bundled rights to perform all songs in the catalog without regard to the users' need for something much less. That practice, and the resulting governance structure that has evolved in the market, has attracted considerable attention at the Justice Department and in law reviews (Cirace, 1978; Clark, 1980; Sobel, 1983; Fujitani, 1984; Hillman, 1998). More generally, it presents a number of interesting issues to scholars interested in public administration and the economics of organization and transaction

Complainants have alleged that alternative licenses (which are obligatorily offered) are priced in a fashion that discourages their use and therefore unduly preserves the market position of the blanket license. Furthermore, disgruntled users have also long contended that blanket licenses have been extended into domains where they are unnecessary, such as movie theaters. Since 1934, the business practices of the two

organizations have acquired the attention of antitrust officials concerned about unlawful tie-in.

Performing rights issues have appeared twice in the Second Circuit and once in the U.S. Supreme Court. Between them, the two performing rights organizations (PROs) have negotiated four consent decrees with the Antitrust Division of the U.S. Department of Justice. As terms of these Decrees, the prices and practices of ASCAP and BMI have been placed under the control of two distinct administrative Rate Courts that operate under the aegis of the Federal Court of the Southern District of New York.

The Supreme Court determined that blanket licensing is administratively more efficient than a system of direct licensing where radio and tv programmers acquire performance rights directly from copyright owners. However, there is no price competition in the sale of blanket licenses. Consequently, ASCAP and BMI can strategically use each other's fees as starting points to argue for increases in their next round of contract negotiations.

For a number of complicating institutional reasons, real competition among the two organizations for affiliated writers and publishers is seriously attenuated as well. Because the music catalog of each PRO forms the basis of its license contracts, courts have upheld the right of a PRO to disallow the movement of existing catalog without its consent. More importantly, fees charged to a licensee in any medium do not vary with respect to usage or catalog size during the length of a contract. Therefore, neither PRO has any way of collecting additional money that would be needed to pay royalties for new material. This reduces the incentive to acquire it.

As found by the Second Circuit Court (discussed below), the most effective way of disciplining the market for blanket licenses is to require that each organization offer a system of smaller licenses that are specific to individual programs. Per the language of ASCAP's later Consent Decree, program and blanket licenses must be offered with amounts and terms that provide to users a "genuine choice". While no clear standards for "genuine choice" have ever been established, a subsequent administrative formula for determining these amounts at ASCAP is economically inefficient. From an economic perspective, it overprices the program alternative and overprotects ASCAP's right to license music through blanket arrangements.

The paper concludes with a series of suggestions to resolve the matter. Most specifically, the program license arrangement should be modified to comply with accepted standards of economic efficiency. Blankets should be more directly tied to music usage and licensing on a per piece basis should be instituted for certain uses. Merger should be considered. Finally, the Consent Decrees should be vacated and ASCAP and BMI should be placed under the authority of the Copyright Office .

The Nature of the Performance Right

Copyright for musical performances is now federally protected in the U.S. by the Copyright Act of 1976. This Act, which actually became effective on January 1, 1978, replaced the existing state and common law statutory structure with a comprehensive federal system of copyright. To comply with international practice established in the Berne International Copyright Convention, all audio or visual works completed in the U.S. after enactment were copyrighted for 50 years after the creator's death. Works-for-hire were protected until the earlier of 75 years after publication, or 100 years after creation. The Sonny Bono Copyright Term Extension Law of 1998 extended each of these terms by twenty years.¹

Section 106 of the new act granted five exclusive rights to composers, writers, and artists who create tangible copies of original work. (Registration is not needed to secure copyright.) Presented concisely, these rights include:

¹ Works copyrighted before 1978 had been legally protected under the 1909 Copyright Act for a period of 28 years after death. This license could then be renewed for an additional 28. The 1976 law extended the renewal period for works completed between 1964 and 1977 to 47. Renewal to a second license was made automatic, but works that had fallen into the public domain before 1964 remained public.

- a. The right to reproduce the copyrighted work,
- b. The right to prepare derivative works based on the copyrighted work,
- c. The right to distribute copies or phonorecords of the copyrighted work
- d. The right to perform the copyrighted work in public
- e. The right to display the copyrighted work publicly

Each right is subject to qualifications and exemptions established elsewhere in the U.S.

Code or in common law.

Section 106(d) entails the right of performance that is the main topic of this paper.

Section 101 established that this right has two relevant dimensions:

The right to perform or display [the work] at a place open to the public or at any place where a substantial number of persons outside of a normal circle of a family and its social acquaintances is gathered.

The right to transmit or otherwise a communicate a performance or display of the work to a place specified by clause (1) or to the public, by means of any device or process, whether the members of the public capable of receiving the performance ... receive it in the same place or in separate places and at the same time or at different times.

Writer performance rights should not be confused with the rights to physically reproduce the words and music (1006a) and distribute the resulting composition (106c), which together compose the mechanical right or, when applied to video applications, the synchronization right. Writer copyright in original songs and musical compositions should not be confused with rights in the sound recordings made by artists and owned by the recording labels.

There are two kinds of performance rights. *Grand* or *dramatic* rights pertain to music compositions that are performed as part of a larger theatrical production, a

dramatic excerpt, or concert presentation thereof. *Small* or *non-dramatic* rights pertain to the larger category of compositions (including popular songs) that are performed independently of a story. Small rights would include individual show tunes that are performed without the show.

Performing Rights and Licensing

The performing rights organizations are empowered to act as agents for collecting royalties due for small performance rights. After composing a song that can be catalogued, a writer will enlist one of the PROs to act as her collecting agent. Dual affiliation of an individual is not permitted, but different members of a writing team may split affiliations. Once affiliated, a writer will enlist the services of a PRO-affiliated music publisher, to whom she passes the copyright. A publisher markets songs to record labels, administers the copyright, collects mechanical royalties, and sometimes edits the song. For their respective efforts, publishers and writers enjoy a 50/50 split of collected royalties, which the PROs gather from music-using licensees.

Music licensees of ASCAP and BMI principally include the three full time television networks (ABC, CBS, and NBC), 1200 affiliated and independent local tv stations, 11000 local cable operators, 150 cable programmers, 11500 local commercial radio stations, and 2000 noncommercial radio broadcasters. Other license groups include internet radio stations, colleges and universities, TV superstations subject to compulsory licenses, the Public Broadcasting System, the Univision Network, satellite subscription services, web sites, symphony orchestras, concert presenters, and thousands of general

license establishments for eating and drinking, commercial business, and general amusement.

The most recent available breakdown (ASCAP, 1998) of collection moneys and royalty payouts shows that ASCAP collected \$508.3 million and distributed \$424.5 million in 1998. Domestic license fees accounted for \$371.3 million of these revenues.² The respective breakdown of this domestic aggregate over television and cable, radio, general, and symphonic and concert performances was \$165.8, \$133.1, \$68.0, and \$4.3 million. The remainder of this paper will be concerned with the two broadcast categories.

The performing rights organizations license music to broadcasters in two ways. Each performing rights organization offers blanket licenses that empower the licensee to perform publicly any music in its catalog at any time. Much like a blanket, a program license limits this freedom to particular times of the program day.³ Both licenses have the advantage of pricing incremental usage at zero, which is economically efficient.

Alternatively, stations and show producers sometimes license performing rights directly with the writer when works are contracted for hire. *Direct licensing* entails contracts between stations and writers for performance rights of musical works. These have been practical with themes on local station news and talk shows that represent the only music usage on the program. *Source licensing* entails contracts between studio producers and writers for music that is integrated in a program or movie soundtrack.

² Remaining amounts were \$130.6 million for royalties in transfer from foreign collections, \$5.2 million for interest on investments, and \$1.3 million for membership dues.

³ Program music so covered would include *feature music* that is the primary focus of audience attention, *theme music* that is used to open and close programs, and *background music* that is used to complement screen action. Commercial music that is covered by a mini-blanket includes *advertising jingles*, *public service announcements*, and *promotional music* to help pitch other station or network programs.

Copyright is passed to the producer of the show, enabling all user stations to use the material without infringement.

Blanket Licensing and Consent Decrees

Copyright in performance was extended to music in 1897. Since music use at the time was exclusively live performance, legal copyrights were difficult to enforce nonetheless. A system of *direct licenses*, where prospective users would obtain usage rights from copyright holders, was evidently difficult. Additionally, individual composers and publishers had no way to police performance halls for copyright violations.

To protect their copyrights in performed music, several prominent songwriters established the ASCAP in 1914. The purpose was to protect against violations of small performance copyrights and to compensate writers and publishers for public performances of their artistic property. The society instituted a system of *blanket licenses* that enabled music halls to perform, without infringement, the entire ASCAP catalog for a period of time. When instituted, blanket licenses were economic because they reduced transaction costs and provided a perfect insurance policy against unwitting infringement in spontaneous music performances. ASCAP distributed blanket revenues to its members based on a performance monitoring system. Collected revenues grew tremendously in the 1920s as music made its way to radio stations that ASCAP subsequently licensed.

A second PRO, SESAC, was formed in 1930. Relatively small and for-profit, SESAC has always operated without Justice Department and court involvement. During a

tough negotiation with ASCAP, the radio industry in 1940 established BMI for the immediate purpose of licensing alternative content to enable a radio boycott of ASCAP. To this day, ASCAP, BMI, and SESAC license the copyrights of their writer and publisher affiliates in a market that is relatively non-competitive.

By 1934, ASCAP licensed 80% of radio music and entered into its first antitrust suit with the U.S. Department of Justice, which was dropped in the next year. In 1941, the Department sued both BMI and ASCAP. Consent decrees (cite these) quickly followed that specified, among other things, that PRO licensing was non-exclusive and that performance rights could be acquired through direct negotiation with the copyright holder.

After 1929, cinema usage of music moved from spontaneously played theater instruments to pre-recorded movie soundtracks. Nonetheless, ASCAP retained licensing responsibility for the performance rights of the soundtracks. In 1948, 164 theater owners successfully prosecuted an antitrust suit in District Court that disallowed an ASCAP practice which required members to license works to theaters at pooled rates (thereby negating the non-exclusive arrangements of the Consent Decree). *Alden Rochelle Inc. v. ASCAP*, 80 F. Supp. 888. The ASCAP Consent Decree was subsequently modified in 1950 to disallow to ASCAP the right to split-license performance rights in movie theaters (IV(E), V(C)).⁴ This led to the first prominent example of *source licensing*, whereby the

⁴ This means that synchronization and performance rights must be negotiated together. Since synchronization rights are not practically negotiated at the theater, source licensing must result. While not legally constrained by the Decree, source licensing was a practical outcome for music controlled by other performing rights organizations.

movie producer obtained performance rights for his soundtrack and conveyed those rights to theater users.

The Decree also re-required license non-exclusivity (IV(A-B), VI), banned discrimination to “similarly situated” licensees (IV(C)), and restricted the length of each license to five years or less (IV(D)). Section VII specified that ASCAP must offer to broadcasters a per program license based on a flat dollar amount or percentage of program revenue. Regarding the setting of alternative fees, ASCAP may not “deprive the licensees or prospective licensees of a genuine choice from among such various types of licenses” (VIII). The District Court in Southern New York was established as a hearing body for disputes regarding licensee fees (IX).⁵ Mention 60 days. BMI in 1966. By committing to Consent Decrees, the government committed to the most restrictive legal course for controlling the two PROs. Only the signatories to a Consent Decree (i.e., the Department of Justice and the PROs) may petition for an interpretation. Furthermore, the Rate Court does not have the authority to add new music licenses that may otherwise be reasonable.⁶ “A consent decree, though it is a judicial decree, is principally an agreement between the parties”⁷ and must be interpreted consistently with “plain meaning” or “explicit language”⁸ and “not by reference to what might satisfy the

⁵ A Ninth Circuit Court ruled that ASCAP’s blanket license was not a restraint of trade since the license was non-exclusive and because the applicants had the right to appeal fees to the District Court. *K91, Inc. v Gershwin Publishing Company*, 372 F. 2d 1 (9th Cir. 1967).

⁶*U.S. v. ASCAP (Application of Shenandoah Valley Broadcasting, Inc.)* 208 F. Supp. 896 (S.D.N.Y. 1962); 331 F. 2d 117 (2d Cir. 1964).

⁷*S.E.C. v. Levine*, 881 F. 2d 1165, 1178 (2d Cir. 1989)

⁸ *U.S. v. Atlantic Refining Co.*, 360 U.S. 19, 22-23 (Sup. Ct. 1959), *Suarez v. Ward*, 896 F.2d 28, 30 (2d Cir. 1990), *Berger v. Heckler*, 771 F. 2d 1556, 1568 (2d Cir. 1985)

purposes of one of the parties to it”.⁹ The matter contrasts with the U.K., where copyright law provides that all Performing Right Society licensees may directly appeal both entire licensing schemes and individual licenses to an oversight tribunal, and Germany, where the Patent Office has special arbitration procedures to resolve licensing disputes between the PRO (GEMA) and its users. (Fujitani, 1984)

Performing Rights and Television

In the early years of television in the late 1940s and early 1950s, music use was much like it had been on radio -- spontaneous use of copyrighted material on popular variety shows of the time. A blanket arrangement here was as useful as it was to radio. However, the number of tv shows that used music in this spontaneous manner declined with the advent of pre-recorded programs. As in movies, synchronization rights for music soundtracks were licensed at production. The same arrangement for performance rights was evidently possible. Television networks and stations would then come to challenge the blanket in a more aggressive manner than their radio predecessors. When the District Court held, and the Circuit Court affirmed, that ASCAP was under no obligation to offer any license, however reasonable, that was not required by the Consent Decree, the gauntlet for antitrust action was thrown.¹⁰

In 1979, the Supreme Court heard a BMI appeal of a Circuit Court decision that held that the blanket arrangement was per se illegal. *CBS, Inc. v. ASCAP*, 562

⁹ *Firefighters Local Union No. 1784 v. Stotts*, 467 U.S. 561, 574 (Sup. Ct., 1984).

¹⁰U.S. v. ASCAP (Application of Shendandoah Valley Broadcasting, Inc.), 208 F. Supp. 896 (S.D.N.Y. 1962); 331 F. 2d 117 (2d Cir.1964).

F. 2d 130 (2d Cir. 1977). The Court reversed the lower court and ruled that blanket licenses were properly examined under a rule of reason that must consider the savings in transactions costs. *BMI v. CBS*, 441 U.S. 1 (1979). Five years later, the Circuit Court heard an appeal of a District Court decision that ruled that ASCAP's blanket license was an unreasonable restraint of trade. *Buffalo Broadcasting Co. v. ASCAP*, 546 F. Supp. 274 (S.D.N.Y. 1982). Influenced by a law review article by Sobel (1983), the Second Circuit found that blanket arrangements do not restrain trade if alternative means of acquiring performance rights are "realistically available" and therefore reversed the decision. *Buffalo Broadcasting Co. v. ASCAP*, 744 F. 2d 917 (2d Cir. 1984).

The Court ruled that the "the only valid test of whether the program license is 'too costly' to be a realistic alternative is whether the price for such a license ... is higher than the *value* [emphasis mine] of the rights obtained" 744 F. 2d at 927. Judge Newman then affirmed that a previous arrangement between blanket and program licensing was reasonable *because the revenue streams under the two alternative domains could be expected to be the same*. From an economist's perspective, the decision is problematic because it fails to consider *underlying costs*.

Two Rate Court decisions in 1993 attempted to refine the standards of reasonable pricing. In a District Court case involving ASCAP, Capital Cities/ABC, and CBS, Judge William Conner ruled that there are no clear economic principles for determining blanket rates and that previous agreements were necessary benchmarks for setting subsequent fees. *U.S. v. ASCAP*, 831 F. Supp. 137 (S.D.N.Y. 1993). However, present fees must be tempered by the recognition of changing circumstances. Of primary importance, blanket

fees should be tied to music usage. A station's revenues can also be considered in order to adjust fees for inflation and changes in audience size that attract more advertising

In an administrative hearing in the same year involving ASCAP and Buffalo Broadcasting Company, Hearing Magistrate Michael Dolinger again found that applicable formulas based on economic principles were absent and applied – with reasonable modification – fees from prior blanket licenses that were negotiated by the two parties at arms length some years before. *U.S. v. ASCAP*, 1993 Copyright Decisions 26,335, 1993 WL 60687 (S.D. N.Y. Mar. 1, 1993). Having estimated that the average television station uses music in 75% of its programming, he then set the program fee ceiling at 133% of the blanket to ensure revenue equality between program and blanket revenues. He then affixed a 7% increment to compensate for the costs of additional monitoring in the final license period and finally added a 10% increment to cover off-program usage.¹¹ But for the 10% increment, a subsequent District Court affirmed the legal validity of Magistrate Dolinger's approach. *U.S. v. ASCAP*, 157 F.R.D. 173 (S.D.N.Y. 1994).

ASCAP acknowledged that additional administrative costs would be minimal for stations with computerized play lists (in second decision, p. 21). CHECK THIS OUT

¹¹ His 7% is quite generous, as he had determined that the related administrative expenses of program licenses amounted to 4.6% of the blanket base during the interim period 1973- . His 10% increment for off-program usage was overruled by the District Court, which found that he had no authority in the Consent Decree to set this fee.

Economic Perspectives

The nature of the performance right, the market for licenses, and the encompassing governance structure present a fascinating constellation of issues, and a formidable lineup of inefficiencies, to researchers involved in the economics of transactions and organizations.

1. *Compared with direct licenses, the blanket mechanism economizes considerably on the necessary number of transaction costs, particularly when music is used spontaneously.*

In the events leading up to the Supreme Court decision *BMI v. CBS*, the defendant networks made the case that a blanket license could be reasonably replaced by a system of direct licenses where licensees and songwriters would individually contract with one another. In this context, the Supreme Court reached its 1979 decision that found that the blanket license reduced the number of transactions between user and copyright holder and was therefore a distinct good not found in a market of direct licenses.

The benefits of the blanket mechanism are particularly pronounced in cases involving spontaneous use, where instantaneous transactions between user and copyright holder are impossible. Spontaneous use prevailed in live music performances in vaudeville halls, early radio programs, and early television.

2. *An overwhelming amount of television music is on pre-recorded soundtrack and not spontaneous.*

According to Northam (2000), minutes of airplay can be categorized as commercial (54.0%), background (41.4%), theme (3.2%), and feature performances (1.4%). Only the latter category would be amenable to spontaneous use.

More than spontaneously used music, it would be quite feasible to negotiate for combined synchronization and performance rights on any soundtrack much in the manner of studio movies. Indeed, all synchronization is so licensed now. Where necessary, remaining material on particular programs could reasonably be licensed in a “mini-blanket” arrangement.

3. *ASCAP and BMI do not economically compete to sell blanket licenses.*

The two organizations share material only on jointly authored works that involve cross-affiliations. For all intents and purposes, any music license therefore needs music from each. Two distinct licenses must then be purchased. Consequently, ASCAP and BMI do not need to price-compete with one another to sell blanket licenses. Rather, each may use its rival’s most recent arrangement as a starting point for its own negotiating position.

4. *ASCAP and BMI have limited ability to compete for affiliates.*

At present, blanket license fees for tv networks are flat rate. Local television and radio fees are based on a percentage-of-revenue that remains fixed for the duration of the license contract. For major stations, these percentages are negotiated on a groupwide

basis by the Radio Music Licensing Committee and the All-Television Music Licensing Committee.¹²

Amounts due from a particular station or group are not now adjusted for quarterly or annual changes in catalog size or in station usage. Therefore, neither PRO can capture additional licensing revenue to cover new music acquisitions. Consequently, each PRO can pay royalties for new material only by drawing down amounts paid to other incumbents.¹³ Affiliates of either PRO are then locked in a zero-sum game with one another and prospective new members.

Competition for affiliates is additionally diminished for yet another reason. Writer membership terms in ASCAP and BMI respectively span five and two years. When contracts expire, a writer may switch affiliations. However, because a PRO's music catalog forms the underlying foundation for licensee contracts, the courts have upheld the right for PROs to retain existing catalog.

5. Tying blanket fees to music usage would enhance competition. In the present administrative context, it would be difficult to achieve.

If licenses were adjusted for quarter-to-quarter changes in usage, the amounts due from each PRO would reasonably change in appropriate directions if market share were

¹²License fees for each radio station are obtained by multiplying the negotiated percentage rate by the adjusted advertising revenue for the particular station. Television fees are determined for the TMLC group as a whole by multiplying the negotiated percentage rate by the total advertising revenue of the group. This aggregate is assigned back to each television station by an industry determined procedure.

¹³The ASCAP system specifically apportions royalty pots to different affiliates based on their respective shares of total performance credits measured in each quarter. The total pot does not change with overall usage. BMI rewards performances with established payments and bonuses that may vary from quarter-to-quarter. The bonus pot is apportioned over different performances but does not change with overall usage.

to shift. Unless overall usage or station revenues increased, the combined amount paid to the PROs would not change. This would present a highly competitive framework in which aggressive acquisition of new affiliates would be rewarded in very short order.

In fact, usage-based pricing is now highly impractical to implement. First, ASCAP and BMI licenses are not synchronous and do not come up for renewal at the same time. Therefore, there is no clear point in time where the respective market share of each can be determined. More importantly, the two organizations now operate under two different Rate Courts. Even if license contracts were coterminous, there is now no appointed legal authority that could bring the two rates into a formula that ties respective license revenues to corresponding market share.

Third, usage measures would have to aggregate over different types of music and assign weights to each. Weights for television would have to be defined for feature, background, theme, commercial, or promotional. Each matter involves some arbitrary judgment and each advocate could be expected to produce a weighting scheme favorable to its particular market position. Adjudicating between them would be a Solomonic task requiring tremendous amounts of arbitrary judgments. More complications may arise if usages are aggregated over different stations.

6. Competition in the market for affiliates is somewhat reduced because the two organizations appeal to different niches.

ASCAP attempts to “follow the dollar” and establish radio performance credits in direct proportion to station revenues, while performance credits in the BMI Royalty

Payment Book increase less than proportionately with station revenues. Additionally, ASCAP does not bonus performances for cumulative play history, while BMI does. These differentials imply that BMI would appeal more to oldies and small-station writers (i.e., country). ASCAP would appeal more to the contemporary, urban crowd.

The resulting market outcome therefore is segmented. Competition in segmented markets is weaker than head-to-head competition.

7. Royalty payments to songwriters are arbitrary judgments.

ASCAP and BMI compensate their affiliates based on universal censuses or samples of broadcast airtime based on program information submitted by each station.¹⁴ Each PRO rewards sampled performances based on broadcast type, music use, and time of day, among others. The relative weights assigned to different music uses are based upon organizational judgments of the relative worth of different types of music -- feature, background, theme, advertising, and promotional.

Compared with soundtrack, theme, and commercial material, feature material on radio or television represents the most prestigious material in a catalog and attracts the highest royalties. It is not surprising that soundtrack and commercial writers, who contribute over 90% of television minutes, are troubled by payment disparities at both PROs (e.g., Hurdle, 1999; Mendelsohn, 2000). The ratio of most valued to least valued

¹⁴ Performances on TV networks, syndicated shows, and cable programs are surveyed based on censuses of cue sheets that list all music in a program. Respective usage on local television and radio stations are monitored through samples of cue sheets and program logs. ASCAP and BMI will sometimes examine off-the-air tapes to confirm general compliance.

music is 1 to 1 in the U.K., 3 to 1 in France, 4.5 to 1 in Germany, and 33.3 to 1 at ASCAP. (Holden, 2000)

8. Compared with blanket licenses, program licenses impose no great additional transaction burden upon ASCAP.

Under blanket licensing, ASCAP and BMI bear the cost of measuring and translating music use directly from station-provided materials and off-the-air tapes. Under present tv program licensing, stations report music use to Music Reports, Inc. (MRI), a clearinghouse contractor that collates station data to present to each PRO in electronic cue sheets that list all music performances in a program in the order of appearance. The costs of reporting and consolidation are born by the reporting stations and appropriately internalized. It is not clear how program licensing imposes additional costs upon ASCAP and BMI.

To some degree, blanket licenses may present additional benefits to the licensees. Most significantly, blanket licenses eliminates the need for additional insurance to protect against accidental violation of copyright (called errors and omissions). However, these additional values are internalized on the user side and again do not reflect additional costs imposed upon ASCAP and BMI. Therefore, they should not affect the price differential between a blanket and a per-program system.

9. From an economic perspective, the program license is overpriced.

Price differentials between substitute products (such as blanket and program licenses) are efficient if they are grounded in underlying cost differences. Such a

correspondence would give applicants the right incentives to choose between alternate license arrangements.

A graphic illustration is helpful to the analysis. For illustration, we assume that audience viewing and program revenues differ across television stations in the same proportions. Programs can then be ranked for the representative station in ascending order. Assuming that license fees are assigned to each program in proportion to its revenue, Curve L1 represents the relationship between the program fee aggregate and the percentage of licensed programs (designated X).

At 100% licensing, the blanket license and a full menu of program licenses would embody the exact attributes of one another and would therefore be perfect substitutes. As a matter of economic efficiency, the difference between L1 and the blanket fee should correspond to the *incremental fixed cost*, if any, that ASCAP or BMI carries in order to accommodate the per program structure. It would be for the court to determine the magnitude of this amount.

If a station licenses X programs, remaining programs $100 - X$ must be cleared at the source. For each program, program producers and local stations collectively bear the costs of additional data reporting (to MRI), payments to writers, and the additional costs of negotiation of all relevant rights.¹⁵ Assuming a fixed amount for each, source-license payments for performance rights would be directly proportional to $100 - X$. Curve L2 represents the combined costs of clearing $100 - X$ programs.

¹⁵ Sobel (1983, p. 48) contends negotiation costs will increase substantially under source licensing. Under blanket licenses, he argues that synchronization rights are now “loss-leaders” that are granted pro forma in order to position the writer to receive performance royalties from the blanket license. These negotiations may get tougher when performance and synchronization rights are bundled together in a source license.

Curve L3 is the sum of the costs for program-licensed and cleared programs. Point X_o represents the optimal license configuration that minimizes license costs. Some level of clearing is optimal if L3 falls below the blanket fee level.

The difference between the blanket amount and actual program payments represents a reduction in payments to ASCAP. Based on ASCAP's most recent data, roughly 85% of this payment would have gone to ASCAP affiliates, who would be compensated through source fees instead. However, the remaining 15% represents a contribution to ASCAP overhead that must be recovered in some fashion. An additional rider can then be reasonably added on to each program license to restore ASCAP's lost overhead.¹⁶

In contrast to this economic model, Magistrate Dolinger's present approach attempts to ensure that the resulting revenue streams of the blanket and program systems are equal for the representative station. Such an approach basically eliminates, for the average station, the financial incentive to adopt a program license and partially explains why program licensing is now so infrequent. In October, 1998, ASCAP and BMI program licenses attracted 185 and 130 local stations of a total of 1100 (Holden, 1998).

Implicitly, such a regime protects not only ASCAP's need to recover its overhead but of its apparent right to pay television writers through the blanket mechanism. Yet these writers are particularly dissatisfied with ASCAP's present regime.

¹⁶Sobel (1983, p. 48) makes the point that monitoring costs for other affiliates will increase since scale economies in enforcement may be lost. Additionally, the PROs resemble in some respects telephone and electric utilities that have the obligation to provide additional service at short notice if competitive options fail for some reason. The PROs then are "carriers of last resort" that ensure that any composition can be licensed. If these arguments are convincing, users of "partial bypass" (i.e., source licensing) may reasonably maintain contributions to PRO overheads..

10. *The program licenses embed many piecewise distortions.*

Under the present regime, the requisite payment to ASCAP and BMI for a program license does not change with the amount of music that is actually used on the show. If music from both catalogs is used, payments are due to both. With no means of avoiding double payments, a show that uses twenty ASCAP compositions will make roughly half the payment of a show that uses one ASCAP and one BMI. In a similar fashion, a show that source- or directly licenses 90% of its music will save no license amount if it cannot entirely cut out one PRO catalog. (Brainin, 1999)

11. *The efficiency of the program licensing system can be improved if per- piece licensing can be implemented.*

At present, ASCAP and BMI rely upon universal census to monitor performances on all network and syndicated television shows. Since all performances are now accounted, per piece licensing can be implemented costlessly.

The organizations must rely upon sample surveys for performances on local radio and television. There are two new technologies that can assist piece monitoring. First, under the Broadcast Data System (BDS), receivers can capture analog or digital radio transmissions and compare these signals with digital imprints of sound recordings that must be entered beforehand in local or central data bases. Manual comparisons are possible for those signals that cannot be matched, as would be the case for live television. Music use can be tallied automatically or monitored for all material that is data-based in the system.

The BDS was first introduced in 1998 as the basis for music monitoring at SESAC to assign blanket fees to respective performances. The reports have been picked up at ASCAP and BMI for the same purpose. However, the resulting count can be used as the basis for per-use licenses. This should be encouraged as another competitive alternative.¹⁷ Per-use fees can be administratively set based on average per use payment in present radio arrangements.

Alternatively, watermarking codes can be embedded in a master tape. The code is inaudible and travels through all media. The codes can display time of performance, the International Standard Works code, country of origin, publisher name, year of creation, and serial number. Once gathered, performance information can be made available for any copyright matter. Evidently, watermarking codes would enable per-use fees on all new audio and video material. However, it is not practically applicable for live performances.

*12. Significant scale economies in litigation, collection, and administration costs could be achieved if ASCAP and BMI were merged.*¹⁸

Based on most recent data, ASCAP and BMI respectively retain 15.5% and 18% of their license revenues to meet their operating overhead. Much of this overhead includes costs of negotiation, litigation, enforcing licenses, collection, and administration that are duplicate efforts. If this overhead is totally duplicate, the overhead ratio could

¹⁷ At present, BDS receivers are now located only in the largest listening areas. Blanket and program licenses remain as viable strategies in the remaining ones.

¹⁸ Based on the most recent web site data, for every dollar paid out to affiliates, ASCAP retains 18.2 cents. The corresponding BMI number is 22.0 cents. ASCAP earns extra credit for avoiding “discretionary voluntary payments, arbitrary payment changes, or short term special deals” that it feels smack of management favoritism.

fall to % if the two organizations were combined. This would compare favorably with the 10% target that the Performing Right Society of the U.K. has established for itself (Hutchinson, 1998)

In every other nation (except Brazil), one organization handles performing rights and one handles mechanical. The two are combined in Germany's GEMA and operate under one alliance in the U.K.

Conclusion

In 1999, the U.S. Department of Justice addressed a letter to BMI's Rate Court authority in fee matters. Concerned about the anti-competitive consequences of blanket licensing, the Department suggested that other reasonable regimes included "per channel licensing", a blanket license with a credit for directly licensed works, a "per programming period" license, and a "pay for play" blanket license under which the music user obtains blanket coverage but only pays for music that is actually performed. The court disregarded the letter as beyond the bounds of the Consent Decree.

The Consent Decree structure, with its requisite judicial restraint, has not been a suitable mechanism for handling the many contentious relationships between the PROs, their licensees, and their affiliates. This would suggest that legislative action is needed to empower the Copyright Office with full administrative authority to resolve a market and administrative system gone thoroughly amok.¹⁹ Ripe for administering the performance

¹⁹ For similar arguments, see Cirace, 1978; Clark, 1980; Fujitani, 1984; Hillman, 1998.

copyright, the Office now sets compulsory mechanical fees for second-use recordings and performance compensation for jukeboxes, satellite services, distant television signals, and digital sound recordings in qualifying noninteractive uses.

As has been the case recently with the FCC, a legislative act can empower the Office with additional responsibilities to monitor and enforce the music performance right. The Office could be granted the authority to establish regulations that would enact their assigned authority. Pursuant to normal procedure, the Office may from time to time issue notices of inquiry to establish basic facts and expand their understanding of a particular situation. At other points, the Office may issue Notices of Proposed Rulemaking that invite comments immediately related to a proposed regulation. Disaffected parties can challenge regulations in Federal Court.

There are two key gains to be had. First, the PROs, their affiliates, their users, and the Department of Justice would all be on equal levels before the Copyright Office. This opens the process to more direct participation by licensees and affiliates in shaping the rules under which they live. Second, compared with the Rate Courts that have operated under the Consent Decrees, the Copyright Office has considerably more legal authority to examine new matter and adopt subsequent rules to meet changing circumstances. This authority would be ingrained in their Congressional mandate and can be so augmented on appropriate occasion.

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Matters involving trademark damages have included the Kardashians/BOLDFACE Licensing, Oprah Winfrey/Harpo Productions, Madonna/Material Girl, CompUSA, Steve Madden Shoes, Kohl's Department Stores, *The New York Observer*, and Avon Cosmetics. Matters in publicity right damages have involved Zooey Deschanel, Arnold Schwarzenegger, Rosa Parks, Diane Keaton, Michelle Pfeiffer, Yogi Berra, Melina Kanakaredes, Woody Allen, and Sandra Bullock.

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The only present means of comparison is for those writer teams who have split affiliations. Using this strategy, Passman (1997, p. 233) finds that ASCAP generally outpays BMI.

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Of 1100 television stations, 185 choose an ASCAP PPL and 130 choose a BMI PPL (10/98) Author = Mark Holden, Film Music, 10/98.