COPYRIGHT AT A CROSSROADS, AGAIN!:

THE COPYRIGHT MODERNIZATION ACT

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EXCERPTED

While extending compulsory licensing to new digital phonorecord deliveries (DPDs), the Digital Performance Rights in Sound Recordings Act of 1995 (DPRSRA) did not add corresponding statutory licenses in two other delivery technologies -- limited downloads and "on demand" streams – that some digital providers (such as Rhapsody and Yahoo!) now predominantly provide.[1] Like DPDs and CDs, these technologies now make music available at listener request and therefore compete implicitly with the choice-driven permanent download.

To accommodate the additional use rights for compositions in interactive streaming and limited download, the Recording Industry Association of America, Inc. ("RIAA"), the National Music Publishers' Association, Inc. ("NMPA") and The Harry Fox Agency, Inc. ("HFA") reached an interim agreement in 2001 by which the publishers agreed to allow labels to embed works in tracks sold to the competing services.[2] With an agreement to keep negotiating for a final deal, the record labels came to pay specified recoupable advances ($1,000,000 for the first

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[1] An "On-Demand Stream" is an on-demand, real-time transmission made using streaming technology, such as Real Audio or Windows Media Audio. A "Limited Download" is a download made using technology designed to cause the downloaded file to be available for listening only, either during a limited time or for a limited number of times.

[2] **S. Bonisteel "RIAA, Songwriters Clear Away Music-Subscription Hurdles", Oct. 9, 2001,at http://www.findarticles.com/p/articles/mi_m0NEW/is_2001_Oct_9/ai_78998791. The due royalty rate was to be determined from contracts between publishers and labels that would be eventually negotiated or arbitrated. In the interim, the RIAA agreed to pay HFA a nonrefundable advance payment of $1 million to cover the first two years, and an additional $62,500 for every month afterward. The advances were recoupable from due royalties and were then to be applied to any due licensing amounts.**

two years, $62,500 for each additional month) and, when eventually determined, suitable royalties retroactively to the beginning of 2001.

Due to differences in legal interpretation, the labels and publishers were not able to come to a final agreement to convey needed rights. As a legal matter, the transmission of any content from an originating server to a hard drive necessarily implicates ephemeral and incidental reproductions in the server, cache, and random access memory that have no indepedent values outside of enabling digital transmission. The question then is what value to assign to these particular reproductions.

Record labels here followed the recommendations of the Copyright Office, which contended that reproduction rights in interactive streaming qualify for fair use, if not a statutory exemption.[3] The Office's conclusion concurs with that of a European Union Directive, which had earlier exempted transient copies from the reach of the reproduction right,[4] and a number of consumer and technology advocates – such as Public Knowledge, the Electronic Frontier Foundation, and Consumer Electronics Association.

For their part, music publishers contended that the resulting interactive uses would enable full access to the work at any moment chosen by the user. With the buildout of wireless receiving devices, interactive streams will increasingly substitute for store sales and downloads; material will be stored on centralized servers instead of hard drives and portable devices. From the publishers' perspective, it is then appropriate to assign to the reproduction of an interactive stream a value that is congruent with its true worth as an economic substitute. The publisher's position is apparently upheld legally by a Ninth Circuit decision involving software copies made into random access memory during upload.[5]

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[3]U.S. Copyright Office, DMCA Section 104 Report (2001). *Id.*, xxiii-xxvii, 132-46.

[4]Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society, 2001 O.J. (L167) 10, par. 33, Art. 5(1). See also *Id.* at Art. 5(2)(d) (preservation of ephemeral recordings made by broadcasters permitted). Member States must implement the Directive in their national laws by December 22, 2002. *Id*. at Art. 13(1).

[5]MAI Systems Corp. v. Peak Computer, Inc. (9th Cir.), 991 F.2d 511 (1993). See also Apple Computer, Inc. v. Formula Int'l, Inc., 594 F. Supp. 617, 621 [224 USPQ 560] (C.D. Cal. 1984), (district court held that the copying of copyrighted software onto silicon chips and subsequent sale of those chips is not protected by fair use exemptions of 17 U.S.C. 117); *Vault Corp. v. Quaid Software Ltd*., 847 F.2d 255, 260] (5th Cir. 1988) ("the act of loading a program from a medium of storage into a computer's memory creates a copy of the program"); 2 *Nimmer on Copyright*, Section 8.08 at 8-105 (1983) ("Inputting a computer program entails the preparation of a copy."); *Final Report of the National Commission on the New Technological Uses of Copyrighted Works*, at 13 (1978) ("the placement of a work into a computer is the preparation of a copy").

The critical difference in interpretation led to a negotiating impasse between labels and publishers who came to see the relative value of temporary reproductions quite differently. From the label position, all streaming transmissions are merely performances, and thus entitled only to the lower royalty fees associated with this lesser activity. From the publisher position, the same transmissions rightfully implicate reproduction rights, and are then cued off of royalties charged for full downloads.

From an economic perspective, the publishers are correct. Downloading and interactive streaming are economic substitutes; consumers choose among substitute based on relative price ratios. To ensure that the relative price ratio is not distorted, it is then appropriate to affix license fees on competing activities in an equitable fashion. That is, copyright licenses should fix equal percentage fees on streaming and download revenues in the same amount; e.g., 14% of sound recording fees.[6] In fact, such a percentage parity had been advocated in Canada by CSI (i.e., CMRRA/SODRAC Inc), a combined society formed by the Anglo- and French-speaking mechanical collecting societies CMRRA and SODRAC in order to collect due publisher revenues from online music services in the country.

It is sometimes suggested that publishers are entitled to a smaller share of the interactive stream because the stream is less than a complete download, and indeed the Copyright Board of Canada apparently succumbed to this reasoning in March, 2007.[7] This disparity between compensations for downloads and streaming makes not economic sense. If the stream is imperfect, such a product infirmity – which is quite arguable on other grounds[8] -- will already be reflected in the price that music service providers charge to online users. Whether consumers prefer downloads or streaming, the price differential between the technologies reflect hedonic differences in the consumer value of the two services. If music publishers are charged the same percentage of download and service prices, their resulting revenue payments will then also have a suitable hedonic adjustment for differences in consumer tastes. There is then no point in distorting a symmetric balance by adjusting the price for streamed compositions further.

Indeed, some hypothetical numbers may illustrate how publishers may suffer greatly if denied the right to receive full parity for streaming services. By some forecasts, online music will account for 25% of industry revenues by the year 2010. If downloading and streaming evenly split the market, streaming will account for 12.5% of the industry total If streamed compositions are

[6] This is only illustrative. Some additional compensation must be allowed for free sound recordings offered as part of a promotion. The publisher here may yet be entitled to some compensation.

[7] The Board's decision and tariffs can be viewed at http://www.cb-cda.gc.ca/new-e.html

[8] Streaming services bear the positive attribute that no physical storage space will be consumed and that personal music collections can be reached from any device.

compensated at a royalty equal to half the percent revenue of downloading and physical records, publishers will lose 6.25% of the mechanical royalty base they might otherwise earn. .

This royalty loss could erode a substantial amount of the profit total. For example, a publisher that earns a 15% profit margin on revenues will suffer a 40% profit loss if total royalty revenues are reduced by 6%., and a 60% profit loss if the margin is 10% Losses will be mitigated if performance and synchronization revenues can be stabilized or increased,. However, it is entirely conceivable that some group of independent publishers will be forced into mergers or cease operations entirely if they are undercompensated from online music services.

The appropriate fee for compensation of the mechanical copyright would be about 13% of all online music revenues. The reasoning is as follows. The label now earns about 65 cents per licensed download track. Some 9.1 cents of this is the mechanical compensation for a fully licensed musical composition. Dividing appropriately, publishers now earn a 13% of label revenues collected on download services. They should earn a comparable amount from streaming.

Under the circumstances, it would be tragic if a sector of the publishing were eroded during a digital era that should greatly expand the appeal of the music catalogs they control. As copyright owners, music publishers would be the apparent losers if consumers were to shift to interactive streaming, a phenomenon that they would have every financial reason to resist. If the matter is not resolved now, a far greater impasse may occur in five years.

ABOUT THE AUTHOR

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In the technology sector, Dr. Einhorn worked at Bell Laboratories and the U.S. Department of Justice (Antitrust Division) and consulted to General Electric, AT&T, Argonne Labs, Telcordia, Pacific Gas and Electric, and the Federal Energy Regulatory Commission. He has advised parties and supported litigation in matters involving patent damages and related valuations in semiconductors, medical technologies, search engines, e-commerce, wireless systems, and proprietary and open source software.

Litigation support involving media economics and copyright damages has involved music, movies, television, advertising, branding, apparel, architecture, fine arts, video games, and photography. Matters have involved Universal Music, BMG, Sony Music Holdings, Disney Music, NBCUniversal, Paramount Pictures, DreamWorks, Burnett Productions, Rascal Flatts, P. Diddy, Nelly Furtado, Usher, 50 Cent, Madonna, and U2.

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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In media and intellectual property, he has consulted to inventors, publishers, songwriters, composers, cartoonists, sculptors, photographers, architects, artists, record labels, movie producers. and screenwriters. Dr. Einhorn has designed and applied innovative techniques related to damage estimation, valuation, licensing, and strategy in transactional and litigation matters involving patents, copyrights, trademarks, trade secrets, and publicity rights. He has testified, counseled, published articles, or lectured in music rights, fair use, data mining, royalties, damages, hyperlinking, file-sharing, and digital rights management.

Michael Einhorn received a B.A. from Dartmouth College and a Ph.D. in Economics from Yale University. He taught at Rutgers University and worked at the U.S. Department of Justice, Broadcast Music, Inc., and Bell Laboratories. He served as an Adjunct Professor of Communications and Media in the Graduate School of Business at Fordham University and a Research Fellow and Adjunct Professor at Columbia University. He is also a frequent lecturer in Continuing Legal Education programs.

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