
EQUALIZING WEBCASTING LICENSING SCHEMES: THE INTERNET RADIO FAIRNESS ACT AND THE FUTURE OF INTERNET RADIO

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INTRODUCTION

“[D]igital is saving music,” one music industry power-player recently claimed.¹ At first glance, this appears to be true. In 2013, the revenue from digital music was \$5.9 billion, an increase of 4.3% over the previous year. Digital consumption is a fast growing source of revenue for record labels resulting from mass consumer utilization of digital services as a primary music source.² As of 2013, there were over five hundred digital music companies³

· Production Editor, *CommLaw Conspectus: Journal of Communications Law and Technology Policy*. J.D., The Catholic University of America, Columbus School of Law, 2014; B.A., Vanderbilt University, 2006. Many thanks to Professor Megan La Belle for her comments; to the extraordinary editors of *CommLaw Conspectus*; and to my friends and family for their unwavering support. This paper is dedicated to John Maher.

¹ Richard Smirke, *IFPI Digital Music Report 2013: Global Recorded Music Revenues Climb for First Time Since 1999*, BILLBOARD.BIZ (Feb. 26, 2013), <http://commcns.org/1w9RJtr> (quoting Edgar Berger, President and CEO, International, Sony Music Entertainment) (internal quotation marks omitted).

² INT’L FED’N OF THE PHONOGRAPHIC INDUS., DIGITAL MUSIC REPORT 2014, at 6 (2014), available at <http://commcns.org/11Ntskq>; see also Press Release, Strategy Analytics, Global Digital Music Sales to Top \$8.6 Billion in 2012: Streaming Revenues Up 40% Compared to 8.5% for Downloads (Aug. 15, 2012), available at <http://commcns.org/TNM25V>. Digital streaming services have become widely used for listening to music and news. See, e.g., Glenn Peoples, *Business Matters: Nearly A Third of Consumers Using Streaming Services: Report*, BILLBOARD.BIZ (July 9, 2012, 5:27 PM), <http://commcns.org/1pbI7MO> (“Nearly a third of consumers in 25 countries around the world now use a music streaming service.”); *Online Radio Audience Jumps 30 Percent in Past Year: Study*, BILLBOARD.BIZ (Apr. 10, 2012, 4:26 PM), <http://commcns.org/1jSOYaF> (“[O]nline weekly radio audience is now at

offering downloading and streaming services.⁴ Amid the myriad of evolving business models in digital services, musical content creators, copyright owners, and others with vested copyright interests have struggled to navigate an ever-changing licensing landscape. While the explosive growth of new digital music delivery methods benefits the public by exposing listeners to a greater breadth of musical content, it remains unclear how these technological advancements will affect content-creator compensation and, also, whether digital consumption can fully replace the decline of the traditional radio delivery method.⁵ One critical and complex question arising out of the Internet radio expansion⁶ is whether the current royalty-payment scheme adequately applies to these new methods of delivery and satisfies the interested parties, particularly as the traditional record industry model of terrestrial radio⁷ and brick-and-mortar sales continues to decline.⁸

The important issue as to whether the compulsory royalty rate for Internet radio broadcasters is equitable in relation to other digital payment models arose

an estimated 76 million Americans. The figure represents a more than 30% increase from a year ago and is 29% of the U.S. population.”).

³ INT’L FED’N OF THE PHONOGRAPHIC INDUS., DIGITAL MUSIC REPORT 2013, at 6 (2013), available at <http://commcns.org/1pbIcJH>.

⁴ For an interesting discussion of downloading and streaming, see WILLIAM W. FISHER III, PROMISES TO KEEP: TECHNOLOGY, LAW, AND THE FUTURE OF ENTERTAINMENT 17–18 (2004). Downloading is defined as the “transmission over the Internet of a digital copy of an audio or video recording, followed by storage of that file on the recipient’s computer, enabling the material to be replayed repeatedly on demand.” *Id.* at 17. Methods of streaming include interactive and noninteractive streaming. Interactive streaming occurs “[a]t the request of the recipient [and involves] transmission over the Internet of a digital copy of an audio or video recording, which is then ‘played’ but not stored.” *Id.* Interactive streaming enables users to request specific music and artists “on-demand,” but does not allow those users to store the music. *Id.* Noninteractive streaming involves the same process as that of interactive streaming, however, the specific music played does not occur at the request of the recipient. *Id.* at 17–18.

⁵ See, e.g., Glenn Peoples, *Business Matters: Download Sales Off to Terrible Start in 2014*, BILLBOARD.BIZ (Jan. 23, 2014), <http://commcns.org/1mgTvSw> (“The cycle is clearly evident: the growth of streaming services negatively impacts digital purchases and puts additional pressure on the music business to generate new revenue by growing streaming services.”); Erin Griffitch, *Can Traditional Radio and Pandora Live Together in Harmony? Terrestrial Broadcaster Hope So*, ADWEEK (Oct. 6, 2011), <http://commcns.org/S9nMJW> (“Terrestrial radio isn’t going anywhere, according . . . to terrestrial radio execs.”).

⁶ See discussion *infra* Part I.A–C.

⁷ “Terrestrial radio” is identified as “the traditional broadcast radio that has been available as AM and FM stations. Licensed radio stations utilize the electromagnetic spectrum to transmit an analog signal containing content on a specified frequency, with specified power source within a specific geographic region.” 1 ENTERTAINMENT LAW: LEGAL CONCEPTS AND BUSINESS PRACTICES § 1:59 (3d ed. 2013).

⁸ See Matthew Perpetua, *Digital Sales Eclipse Physical Sales for the First Time*, ROLLING STONE (Jan. 6, 2012), <http://commcns.org/1on0MFp> (“According to data released by Nielsen SoundScan, digital sales were up by 8.4 percent from 2010, while physical album sales declined by 5 percent.”).

with the recently proposed Internet Radio Fairness Act of 2012 (“IRFA”).⁹ Although the proposed legislation did not pass in 2012,¹⁰ an examination of the IRFA will help guide future rate proposals. The IRFA highlights a debate over whether the current digital music licensing system disproportionately favors specific business models at the expense of online broadcasting companies and, in the long run, consumers.¹¹

With major technology companies entering the Internet radio market,¹² the royalty disparity between webcasters and other digital music models needs to be settled.¹³ Given that consumers expect access to digital-content on multiple devices for a one-time fee,¹⁴ common sense dictates that copyright owners face an increasingly uphill battle to secure more favorable royalty rates. Inevitably, these countervailing interests threaten the music industry’s traditional business model. These interests challenge all parties involved to satisfy an increasingly insatiable consumer desire for unbridled access to a broad library of digital music, while adequately compensating content creators and owners.

This paper centers on the debate regarding compensation to content owners and the alleged disparate royalty rates paid out to copyright owners among varying digital delivery methods. Part I of this paper provides an overview of webcasting, defining and broadly delineating the varying models. Part II discusses the background of copyright law and the history of the webcasting licensing scheme. Part III provides an overview of digital music licensing schemes and the disparate treatment of various digital music deliveries. Part IV examines the recently proposed IRFA, the debate surrounding its proposal, and the implications of some of the Act’s proposals becoming law. Finally, Part V proposes that the webcasting licensing controversy may best be resolved through the adoption of the willing buyer and willing seller (“WBWS”) stan-

⁹ The Internet Radio Fairness Act of 2012, S. 3609, 112th Cong. (2012); The Internet Radio Fairness Act of 2012, H.R. 6480, 112th Cong. (2012).

¹⁰ Rick Marshall, *The Quest for “Parity”: An Examination of the Internet Radio Fairness Act*, J. COPYRIGHT SOCIETY OF THE U.S.A. 445, 463 (Sept. 9, 2013) (unpublished manuscript), available at <http://commcns.org/1h6dINM>.

¹¹ 158 Cong. Rec. S6628, S6628 (daily ed. Sept. 12, 2012) (statement of Sen. Wyden) (introducing the Internet Radio Fairness Act of 2012, S. 3609 and stating that “Consumers and rightsholders are increasingly seeking innovative, new models that can better promote music and compensate artists”).

¹² One such technology company is Apple, which entered the Internet radio market with iTunes Radio. See *iTunes Radio—Hear Where Your Music Takes You*, APPLE, <http://commcns.org/1nqg9gM> (last visited Mar. 22, 2014).

¹³ Senator Wyden recognized the royalty-rate disparity in his introduction remarks for IRFA. See 158 Cong. Rec. at S6628 (statement of Sen. Wyden) (lauding IRFA as treating Internet radio, “for purposes of establishing royalty rates, in the same way that satellite and cable radio are treated”).

¹⁴ *Publishers Must Realign with Consumer Expectations for Digital Media*, YOUGov (Jan. 5, 2011), <http://commcns.org/1kFpAW2>.

dard,¹⁵ as that would be the most appropriate and workable solution amenable to all parties involved.

I. OVERVIEW OF WEBCASTING

A. Defining Webcasting

Webcasting, otherwise known as Internet radio, involves noninteractive digital audio transmissions broadcast over the Internet to a consumer.¹⁶ The listener selects a genre or a station, and then the webcaster streams specific songs for the chosen genre or station.¹⁷ The webcaster transmits a digital audio or video file over the Internet to the end-user, who listens to or views the file without keeping permanent copies of the webcast transmission.¹⁸

B. Types of Digital Music Services

Internet-music services are provided by a range of companies¹⁹ and operate under a subscription or advertising business model.²⁰ For instance, some webcasters, like Pandora, utilize a statutory webcasting scheme.²¹ Others, like Sirius XM Radio, offer paid, subscription-only music services.²² Still, other companies simulcast²³ through the Internet, like Clear Channel,²⁴ which is

¹⁵ See *infra* Part IV.C.

¹⁶ Karen Fessler, *Webcasting Royalty Rates*, 18 BERKELEY TECH. L.J. 399, 399 n.4 (2003).

¹⁷ See, e.g., Pandora Media, Inc., Annual Report (Form 10-K), at 3 (Mar. 16, 2012) [hereinafter Pandora 2012 Form 10-K].

¹⁸ AL KOHN & BOB KOHN, KOHN ON MUSIC LICENSING 1481, 1516 (4th ed. 2010). For clarification, neither the term “Internet radio” nor “webcasting” refers to interactive digital services. However, as demonstrated herein, an industry standard definition of “webcasting” is lacking, leading some to lump both interactive and noninteractive services under the webcasting definition. Considering interactive and noninteractive services are subject to different royalty rates, this is problematic. *Id.*

¹⁹ Some of the companies include Pandora, Spotify, iTunes, Amazon, Google, Rhapsody, Slacker, Rdio, and MOG. Don Sears, *Why the Online Music Industry Is a Mess*, CNNMONEY (Aug. 30, 2012), <http://comcnns.org/1raenlu>. In addition to the assortment of companies in the Internet-music industry, a plethora of services exist, such as those identified by Harry Fox Agency (“HFA”). HFA’s Digital Definitions page describes the wide variety of digital services in existence and exemplifies the absence of an industry standard as to what exactly “webcasting” encompasses. *Digital Definitions*, HARRY FOX AGENCY, <http://comcnns.org/TNMu4f> (last visited Feb. 28, 2014). These differing types of service contribute to royalty rate confusion among types of digital delivery methods.

²⁰ Sears, *supra* note 19.

²¹ See discussion *infra* Part II.C–D.

²² Sirius XM Radio Inc., Annual Report (Form 10-K), at 1 (Feb. 6, 2013).

²³ For a definition of “simulcasts,” see the CARP’s report. *In re* Rate Setting for Digital Performance Right in Sound Recordings and Ephemeral Recordings, Docket No. 2000-9 DTRA 1 & 2, at 82 (Copyright Arb. Royalty Panel Feb. 20, 2002) [hereinafter CARP Re-

available on the Internet through iHeartRadio.²⁵ Public institutions, such as National Public Radio (“NPR”), provide noncommercial services through not only traditional, terrestrial means, but also through their websites.²⁶ All of these services represent a mere cross-section of the numerous digital services offered.

One of the benefits of the variety of Internet radio services is that users are able to participate in more personalized radio experiences. For instance, services like Last.fm,²⁷ Pandora, iHeartRadio and Slacker,²⁸ create automatic, customized playlists for listeners from a single reference point—an artist, genre, decade or theme. Users have some control over their listening experiences and can skip to the next song in a playlist created for them by an algorithm or by the company’s staff.²⁹

C. Who Listens to Webcasting?

Today, more Americans still listen to terrestrial radio than Internet radio. According to a February 2012 study, approximately 241 million people in the United States listen to radio each week.³⁰ A growing percentage of Americans (about 39% or an estimated 103 million) listen to Internet radio every month, accounting for roughly one out of every three Americans.³¹ Self-reported data indicates that, in 2012, Internet radio listeners tuned-in for approximately 9.5 hours per week.³² Only 13% of those that listen to Internet radio do not listen to

port] (defining simulcast as “services which simultaneously stream (retransmit) their over-the-air broadcasts via the internet”).

²⁴ Press Release, Clear Channel, Clear Channel Extends Reach of Iconic Radio Brands via XM Satellite Radio (June 8, 2011), <http://commcns.org/1jnD4B6>.

²⁵ *Id.*

²⁶ *Ways to Listen to NPR*, NPR, <http://commcns.org/1h6dYMC> (last visited Mar. 22, 2014).

²⁷ Last.fm is a music recommendation service through which users subscribe and download “The Scrobbler”—an algorithm that helps users discover more music based on the songs you play. *About*, LAST.FM, <http://commcns.org/S9nXVR> (last visited Mar. 3, 2014). In addition, Last.fm allows users to tag tracks and join discussions with other Last.fm subscribers. *Id.*

²⁸ Slacker is a music customization service that allows users to access a music library containing 10 million licensed tracks and over 200 stations. *About Slacker*, SLACKER, <http://commcns.org/1kiqJmP> (last visited Mar. 3, 2014).

²⁹ *See, e.g., About Pandora*, PANDORA, <http://commcns.org/RtSmxp> (last visited Mar. 3, 2014) (utilizing an algorithm); *About Slacker*, *supra* note 28 (using staff to create the stations for listeners).

³⁰ ARBITRON & EDISON MEDIA RESEARCH, THE INFINITE DIAL 2012: NAVIGATING DIGITAL PLATFORMS 10 (Apr. 12, 2013), <http://commcns.org/1pbIM0O> (for comparison and growth purposes).

³¹ *Id.* at 19.

³² *Id.* at 21.

over-the-air, traditional radio.³³

Importantly, this listener data merely estimates the number of consumers tuning into webcasting and is not entirely accurate, due to limited collection methods and an absence of a central database tracking Internet radio data. Regardless, the upward trajectory is clear: based upon similarly reported data in 2003, Internet radio is soaring in popularity.³⁴ In 2012, Pandora constituted 5.6% of the Internet radio market in the U.S., and, in 2013, it grew to constitute 8% of the market.³⁵ Young adults are the key demographic, as evidenced by a study led by the NPD Group, which found that digital listenership of free on-line radio is most popular among young adults ages 18 to 25.³⁶

Furthermore, research indicates that an important impetus behind the popularity of streaming and Internet radio services is the consumer's ability to listen to music free of charge and the easy discoverability of new music and artists.³⁷ These are the benefits of noninteractive streaming services offered by Internet radio providers, which are unlike on-demand services that require users to choose the specific artists or songs to whom or to which they prefer listening.³⁸ Webcaster-provided content curation enables listeners to enjoy the music passively; music is selected for the user based upon a broad genre or a station, and the webcaster selects other artists similar to the initial genre or artist selected by the consumer.³⁹

D. Internet Radio Listening Devices

At the inception of Internet radio, listeners could only access online radio stations through their desktop personal computers.⁴⁰ Since then, webcasting has also become available on mobile devices.⁴¹ Joe Kennedy, former chief executive officer and president of Pandora, envisioned Internet radio further expanding away from pure personal computer engagement. Kennedy explained that Pandora is “penetrating areas where people traditionally listen to radio, with 60

³³ *Id.* at 22.

³⁴ *Id.* at 12–13 (using a chart to show that, in 2003, 17% of those surveyed reported listening to Internet radio, while, in 2013, 45% of those surveyed reported listening to Internet radio).

³⁵ DIGITAL MUSIC REPORT 2013, *supra* note 3, at 17.

³⁶ Press Release, NPD Grp., Online Radio Is the Fastest Growing Music Listening Option (Apr. 3, 2012), *available at* <http://commens.org/1mufkzY>.

³⁷ DIGITAL MUSIC REPORT 2013, *supra* note 3, at 9.

³⁸ FISHER, *supra* note 4, at 18.

³⁹ *See About Pandora*, *supra* note 29 (describing Pandora's content-curation algorithm). *But see We Are Beats Music*, BEATS MUSIC, <http://commens.org/1tGQHmr> (last visited Mar. 3, 2014) (discussing the role of staff in creating music stations).

⁴⁰ DIGITAL MUSIC REPORT 2014, *supra* note 2, at 16.

⁴¹ *Id.* (“Underpinning . . . [the music industry's transformation into a global digital business] is the global shift of music consumption to smartphone-based mobile platforms.”).

brands of car supporting Pandora radio,” but Pandora is “also now accessing the living room with 650 home consumer products now supporting Pandora.”⁴² Listening to music on the go has become a “core activity” for smartphone and tablet users⁴³—perhaps one reason why Apple and Beats Music, among others, have entered the Internet radio market.⁴⁴ Consumers see music as important to the mobile experience.⁴⁵ Smartphones are the third most popular device for listening to music and are used more often than MP3 players.⁴⁶ In Pandora’s fiscal year ended January 31, 2013, mobile-phone and connected-device users accounted for 77% of the total listener hours.⁴⁷ Tablet owners also heavily use their devices to listen to music. A study in June 2012 found that 51% of tablet owners used their tablets to listen to music, compared with 42% who used them to read books.⁴⁸ Despite this wide-range of diverse services offered to consumers, digital services and sales, such as permanent digital downloads,⁴⁹ fail to compensate for the steep decline in physical, brick-and-mortar purchases that generate crucial royalty income for copyright owners.⁵⁰ The inability of digital sales and webcasting to replace lost revenue for content creators should ultimately play into the calculation of royalties for digital services.

⁴² DIGITAL MUSIC REPORT 2013, *supra* note 3, at 17 (internal quotation marks omitted).

⁴³ *Id.* at 23.

⁴⁴ *See, e.g.*, Apple, Inc., Annual Report (Form 10-K), at 3 (Oct. 30, 2013) [hereinafter Apple, Inc. 2013 Form 10-K] (describing the ability of users to utilize iTunes Radio, the free Internet streaming service introduced September 2013, on a variety of Apple devices, such as iOS devices, Mac and Windows personal computers, and Apple TV); Press Release, Beats Music, Beats Music Is Here (Jan. 11, 2014), <http://commcns.org/InN11Wr> (highlighting the importance of mobile devices by advertising Beats Music’s Internet radio service as allowing up “to five family members across 10 devices” to use the service).

⁴⁵ *See* ACCENTURE, THE 2013 ACCENTURE CONSUMER ELECTRONICS PRODUCTS & SERVICES USAGE REPORT 26 (2013), *available at* <http://commcns.org/1k9MUqm> (reporting that 30% of tablet users and 31% of smartphone users consider important the “[a]bility to use your preferred streaming music service”).

⁴⁶ DIGITAL MUSIC REPORT 2013, *supra* note 3, at 23.

⁴⁷ Pandora Media, Inc., Annual Report (Form 10-K), at 15–16 (Mar. 18, 2013) [hereinafter Pandora 2013 Form 10-K].

⁴⁸ ONLINE PUBLISHERS ASS’N, A PORTRAIT OF TODAY’S TABLET USER WAVE II, at 19 (2012), *available at* <http://commcns.org/1raeLjQ>.

⁴⁹ A permanent digital download is defined as each delivery of a “phonorecord by digital transmission of a sound recording (embodying a musical composition) resulting in a reproduction made by or for the recipient which may be retained and played by the recipient on a permanent basis. PDDs are sometimes referred to as full downloads or untethered downloads.” *Digital Definitions*, *supra* note 19.

⁵⁰ Ed Christman, *What’s Behind the Digital Download’s Decline and Can Streaming Save the Day?*, BILLBOARD.BIZ (Jan. 10, 2014), <http://commcns.org/1mug0oM>; *see* Perpetua, *supra* note 8.

II. STATUTORY BACKGROUND OF COPYRIGHT LAW IN A MUSICAL CONTEXT

A. The Basics of Copyright Law

Before describing the Internet Radio Fairness Act and its proposed Internet radio royalty standards, an overview of the basics of copyright law is essential. Today, under the Copyright Act of 1976, the payment of music-licensing royalties may involve two copyrights: the copyright for the musical work,⁵¹ and the copyright for the sound recording.⁵² The term “musical works” includes the compositions, while a “sound recording” is a work that results “from the fixation of a series of musical, spoken, or other sounds.”⁵³ A striking delineation between these two copyrights is that musical works may be “fixed” in more than one sound recording. For instance, “Over the Rainbow,”⁵⁴ the musical ballad made famous by Judy Garland in *The Wizard of Oz*, has been recorded countless times by different artists.⁵⁵ Each time a recording of “Over the Rainbow” is performed or a copy of a sound recording is sold, the original composers of the composition receive a royalty payment for their copyright ownership in the song, while the recording artist or record label of each individual recording receives compensation for its individual sound recording only, depending upon the format in which the recording is performed.⁵⁶

Notably, the rights granted to songs versus sound recordings under the Copyright Act differ. The copyright owner in a musical composition—unlike the owner of a sound recording⁵⁷—possesses an additional exclusive right of

⁵¹ 17 U.S.C. § 102 (2012).

⁵² *Id.*; see also 17 U.S.C. § 101 (2012) (defining “sound recordings”).

⁵³ 17 U.S.C. § 101; U.S. COPYRIGHT OFFICE, CIRCULAR 50, COPYRIGHT REGISTRATION FOR MUSICAL COMPOSITIONS 1 (2012), available at <http://commens.org/1k9N0OD> (“Musical works include both original compositions and original arrangements or other new versions of earlier compositions to which new copyrightable authorship has been added.”).

⁵⁴ The underlying musical work of “Over the Rainbow” includes music by Harold Arlen and lyrics by E.Y. Harburg. See *Harold Arlen Biography: We’re Off to See the Wizard*, OFFICIAL HAROLD ARLEN WEBSITE, <http://commens.org/1jSRduy> (last visited Mar. 5, 2014); see also *Harold Arlen Detailed Song List*, SONGWRITERS HALL FAME, <http://commens.org/S9oc39> (last visited Mar. 5, 2014).

⁵⁵ Search Results for “Over the Rainbow,” ALLMUSIC, <http://www.allmusic.com> (search “over the rainbow”; then follow “Songs” hyperlink to filter search results) (last visited Mar. 23, 2014).

⁵⁶ See 17 U.S.C. § 114(a)–(b) (2012); 17 U.S.C. § 106 (2012) (granting the sound recording owner fewer rights under the Copyright Act than the owner of the musical work). See generally IRS, TRAINING 3153-101, MARKET SEGMENT SPECIALIZATION PROGRAM ON ENTERTAINMENT: MUSIC INDUSTRY (1994), available at <http://commens.org/1mgURgg> (identifying the compensation schemes in the music industry).

⁵⁷ Compare 17 U.S.C. § 106(4) (granting the exclusive public performance right to the copyright owner of musical works), with 17 U.S.C. § 114(a) (“The exclusive rights of the

public performance under section 106(4).⁵⁸ “the owner of copyright . . . has the exclusive rights to do and to authorize . . . in the case of . . . musical . . . works . . . to perform the copyrighted work publicly”⁵⁹ In other words, the copyright laws grant the composer (*i.e.*, the owner of the musical work) the exclusive right to authorize the public performance, while the performer (*i.e.*, the owner of the sound recording) has not been granted that right.⁶⁰ The varying rights bestowed upon copyright owners in differing types of creative works exemplify the highly detailed scheme embodying Congress’s judgment as to the appropriate balance between intellectual property protection granted to copyright owners, and public access to users and consumers of such works.

B. Compulsory Licensing

While copyright owners receive exclusive rights of their copyrighted works, some limitations are imposed.⁶¹ One set of limitations or exceptions occurs through “compulsory licenses,” which enable a user to pay a fee to a copyright owner for use of the copyrighted content that would ordinarily violate one of the copyright owner’s exclusive rights granted under the Copyright Act,⁶² resulting in an implicit contract between the user and copyright owner. The user pays the copyright owner a fee set by the government and, in return, must abide by regulations set by the Copyright Office.⁶³ This compulsory license enables the content owner to prevent activities infringing on his or her exclusive rights, but compels the owner to grant others permission to engage in activities subject to these compulsory licensing terms.⁶⁴ Compulsory licensing is an important and beneficial instrument for multiple reasons: It cuts down on costly, drawn-out negotiations with recalcitrant copyright owners,⁶⁵ and trans-

owner of copyright in a sound recording . . . do not include any right of [public] performance under section 106(4).”), and 17 U.S.C. § 106(6) (“[T]he owner of copyright . . . has the exclusive rights to . . . in the case of sound recordings, to perform the copyrighted work publicly by means of a digital audio transmission.”).

⁵⁸ See 17 U.S.C. § 114(a).

⁵⁹ 17 U.S.C. § 106(4).

⁶⁰ Shourin Sen, *The Denial of a General Performance Right in Sound Recordings: A Policy That Facilitates Our Democratic Civil Society?*, 21 HARV. J.L. & TECH. 233, 234 & n.4 (2007).

⁶¹ See, e.g., 17 U.S.C. § 110(1) (2012) (stating that a copyright owner cannot prohibit the performance or display of a work in an educational setting).

⁶² FISHER, *supra* note 4, at 41.

⁶³ U.S. COPYRIGHT OFFICE, CIRCULAR 73, COMPULSORY LICENSE FOR MAKING AND DISTRIBUTING PHONORECORDS 1 (2011), available at <http://commcns.org/1jVdFV7> (“The Copyright Office’s regulations set out in detail the procedures that must be followed to operate under a compulsory license.”); see also FISHER, *supra* note 4, at 41.

⁶⁴ FISHER, *supra* note 4, at 41.

⁶⁵ *Id.*

actional costs are reduced.⁶⁶ While compulsory licensing can also exist for mechanical rights, in this paper, the focus primarily centers on the compulsory licensing of sound recordings in digital transmissions under section 115 of the Copyright Act.

C. Digital Performance Right in Sound Recordings Act⁶⁷

Another type of exclusion from the rights granted to copyright owners appears in the form of the “public performance” right. While the public performance right continues to be excluded with regard to sound recordings performed in the terrestrial radio format,⁶⁸ the right garnered some recognition in other formats beginning in the early 1990s. Starting in the mid-1990s, the “public performance” right’s applicability to other technological mediums was addressed by Congress through the Digital Performance Right in Sound Recordings Act of 1995 (“DPRA”). At that time, terrestrial radio was no longer the sole format for broadcast radio.⁶⁹ The 1990s saw a shift, championed by entrepreneurs, from music consumption via the purchase of physical products to digital consumption of music services, where consumers pay for access to digital libraries of recorded music.⁷⁰ Such services involved webcasting, which

⁶⁶ ROBERT P. MERGES, CATO, NO. 508, COMPULSORY LICENSING VS. THE THREE “GOLDEN OLDIES”: PROPERTY RIGHTS, CONTRACTS, AND MARKETS 1 (2004), available at <http://commens.org/S9ogjr> (“From its inception in the U.S. in the early 20th century, compulsory licensing has been seen as a means of making intellectual works available by reducing some of the transaction costs associated with obtaining permission to use copyrighted material.”).

⁶⁷ See generally Digital Performance Right in Sound Recordings Act of 1995, Pub. L. No. 104-39, 109 Stat. 336 (1995) (codified as amended in scattered sections of 17 U.S.C.).

⁶⁸ See 17 U.S.C. § 106(6) (“[T]he owner of copyright under this title has the exclusive rights to do and to authorize . . . in the case of sound recordings, to perform the copyrighted work publicly by means of a *digital audio transmission*.”) This impliedly means that only *digital audio transmissions*, not *terrestrial broadcasts* are covered. For a more in-depth discussion regarding the lack of a terrestrial public performance right in sound recordings, see Laura E. Johannes, *Hitting the Right Notes: The Need for a General Public Performance Right in Sound Recordings to Create Harmony in American Copyright Law*, 35 WASH. U. J.L. & POL’Y 445, 455 (2011).

⁶⁹ H.R. REP. NO. 104-274, at 12–13 (1995). The House Report on DPRA stated: [A] small number of services have begun to make digital transmissions of recordings available to subscribers. Trends within the music industry, as well as the telecommunications and information services industries, suggest that digital transmission of sound recordings is likely to become a very important outlet for the performance of recorded music in the near future. Some digital transmission services . . . will be interactive services that enable a member of the public to receive, on request, a digital transmission of the particular recording that person wants to hear.

Id. at 12.

⁷⁰ KEVIN PARKS, MUSIC AND COPYRIGHT IN AMERICA: TOWARD THE CELESTIAL JUKEBOX 166 (ABA Publishing 2012).

advantageously provided clearer transmission of content in relation to physical products, required less power to air broadcasts over the Internet, and allowed digital broadcasters to offer highly specialized music formats, including specific genres, artists, and even songs.⁷¹

Even though these advances in content-delivery methods benefitted consumers, the industry met such developments with skepticism. Music industry stalwarts, like the Recording Industry Association of America (“RIAA”),⁷² worried that such developments would result in a “home-taping” situation, enabling listeners to record content streams on-demand and store it on their home computer’s hard-drive.⁷³ The fear was that such copying could result in a near-perfect, digital copy embodying clear, crisp sound and would undercut the need for brick-and-mortar store purchases of physical records.⁷⁴

In 1991, the Copyright Office released a study acknowledging that a “digital audio transmission” right would affect the music industry and made a formal recommendation to implement a performance royalty in order to offset lost brick-and-mortar sales.⁷⁵ Subsequently, in 1993, both houses of Congress introduced performance right legislation addressing this very problem.⁷⁶ Then, copyright owners and broadcasters began meeting privately regarding the performance right.⁷⁷ Terrestrial radio broadcasters claimed that they still served a

⁷¹ *Id.*

⁷² The RIAA is a trade organization operating to support the record labels. *See Who We Are*, RECORDING INDUSTRY ASS’N AM., <http://commcns.org/1k9NaWe> (last visited Mar. 6, 2013).

⁷³ PARKS, *supra* note 70, at 166. Congress appears to have recognized this concern, because the House noted the home-taping dilemma in its report on the DPRA. *See* H.R. REP. NO. 104-274, at 21 (1995).

⁷⁴ *See* Eric Leach, *Everything You Always Wanted to Know About Digital Performance Rights But Were Afraid to Ask*, 48 J. COPYRIGHT SOC’Y U.S.A. 191, 219 (2000) (“[T]he very real possibility of making digital copies of digital transmission meant that music listeners would no longer need to purchase an original recording at a music store. Indeed, this fear of record store replacement was one of the principal motivations for the [DPRA].”). *See* Kristine J. Hoffman, Comment, *Fair Use or Fair Game? The Internet, MP3, and Copyright Law*, 11 ALB. L.J. SCI. & TECH. 153, 159 (2000) (describing the RIAA’s pursuit to protect its members’ copyright interests against emerging digital technologies like the sharing of MP3s via the Internet). The RIAA’s fears of digital copies supplanting sales seem to have been realized with the creation of Napster, the Internet service that facilitated the transmission of MP3 files between and among its users. *A&M Records, Inc. v. Napster*, 239 F.3d 1004, 1010–11 (9th Cir. 2001) (discussing Napster’s service).

⁷⁵ *Hearings Before the H. Subcomm. on Courts and Intellectual Property of the H. Comm. on the Judiciary on H.R. 1506 Digital Performance Right in Sound Recordings Act of 1995*, 104th Cong. 164, 188 (1995) (statement of Hon. Marybeth Peters, Register of Copyrights).

⁷⁶ *See generally* Digital Performance Right in Sound Recordings Act of 1993, H.R. 2576, 103d Cong. (1993) (House of Representative’s version of the bill); Performance Rights in Sound Recordings Act of 1993, S. 1421, 103d Cong. (1993) (Senate’s version of the bill).

⁷⁷ PARKS, *supra* note 70, at 166.

promotional function for artists and, thus, should not owe artists a performance royalty.⁷⁸ Congress agreed with terrestrial radio broadcasters and refused to grant Internet broadcasters the same leeway—most likely because the digital transmissions were high quality and made consumers less likely to buy physical compact discs.⁷⁹ Congress believed that Internet broadcasting posed a greater threat, because it could exceed the broadcasters' claimed boundary of mere "promotion" and supplant music sales with webcasts.⁸⁰ Out of these discussions, in 1995, emerged the DPRA.⁸¹

The DPRA⁸² further expanded the copyright holder's rights by granting an additional right to the sound recording copyright owner: the right of digital audio transmission.⁸³ The right of sound recordings specifies that no one may "perform [a] copyrighted work publicly by means of a digital audio transmission" without permission from the copyright owner.⁸⁴ This means that sound recording copyright owners are entitled to royalties when their music is played via Internet radio, satellite radio, or cable radio stations.

Importantly, the digital transmission right granted was significantly enhanced in two ways. First, the right does not extend to "eligible nonsubscription transmissions," which primarily referred to the retransmission of AM/FM radio broadcasts over the Internet.⁸⁵ Second, the DPRA implemented a compulsory blanket license for "noninteractive subscription transmissions."⁸⁶ Thus,

⁷⁸ Johannes, *supra* note 68, at 455, 463–64.

⁷⁹ *Id.* at 454–55, 455 n.58.

⁸⁰ See Leach, *supra* note 74, at 216–19 (describing the difference between analog and digital transmissions and the resulting implications of the higher quality of digital transmissions).

⁸¹ See generally Digital Performance Right in Sound Recordings Act of 1995, Pub. L. No. 104-39, 109 Stat. 336, (1995). See Jane C. Ginsburg, *Copyright Legislation for the Digital Millennium*, 23 COLUM.-VLA J. L. & ARTS 137, 167 (1999).

⁸² Digital Performance Right in Sound Recordings Act of 1995 § 2, 109 Stat. at 336.

⁸³ 17 U.S.C. § 106(6) (2012).

⁸⁴ *Id.*

⁸⁵ 17 U.S.C. § 114(j)(6) (2012). More specifically, the subsection states:

An "eligible nonsubscription transmission" is a noninteractive nonsubscription digital audio transmission not exempt under subsection (d)(1) that is made as part of a service that provides audio programming consisting, in whole or in part, of performances of sound recordings, including retransmissions of broadcast transmissions, if the primary purpose of the service is to provide to the public such audio or other entertainment programming, and the primary purpose of the service is not to sell, advertise, or promote particular products or services other than sound recordings, live concerts, or other music-related events.

Id.

⁸⁶ See Public Performance of Sound Recordings: Definition of Service, 65 Fed. Reg. 33,266, 33,266 (May 23, 2000) ("Among the limitations on the performance was the creation of a . . . compulsory license for nonexempt, noninteractive, digital subscription transmissions . . ."); see also 17 U.S.C. § 114(d)(2)–(3), (f) (imposing the compulsory license for nonexempt, noninteractive, digital subscription transmissions). The statute defines a "nonsubscription" transmission as "any transmission that is not a subscription transmis-

any service under this definition can, so long as it complies with the licensing terms, play any sound recording without seeking permission from the copyright owner at a royalty rate set by the then-called Copyright Arbitration Royalty Panel (“CARP”), an *ad hoc* body that set rates for the various compulsory licenses under the Copyright Act.⁸⁷ The Act provided, however, that the CARP would only step in if copyright owners and noninteractive subscription services failed to reach voluntary rate agreements under the compulsory license.⁸⁸ In the absence of such an agreement, CARP set the compulsory rate using the standard set in section 801(b)(1) of the Copyright Act.⁸⁹

D. The Digital Millennium Copyright Act of 1998 (“DMCA”)⁹⁰

Following the DPRA’s passage, a dispute arose regarding the licensing obtained by webcasters for their streaming of sound recordings.⁹¹ Webcasters maintained that they were exempt from section 106(6).⁹² The recording industry argued to the contrary, claiming that webcasters were not exempt from section 106(6) and that webcasters needed the sound recording copyright owners’ consent prior to Internet transmission.⁹³ The crux of the dispute was whether webcasters needed direct licensing from the sound recording owners.⁹⁴ The dispute was between nonsubscription webcasters (who claimed an exemption from section 106(6))⁹⁵ and the recording industry (who asserted that the exemption was inapplicable).⁹⁶ Important to the dispute was the fact that traditional radio broadcasting and other “analog” transmissions were exempt from these provisions under the DPRA, because the webcasters believed that Congress intended to exempt the streaming activities.⁹⁷

sion.” *Id.* § 114(j)(9). A “subscription” transmission is any “transmission that is controlled and limited to particular recipients, and for which consideration is required to be paid or otherwise given by or on behalf of the recipient to receive the transmission or a package of transmissions including the transmission.” *Id.* § 114(j)(14); *see also id.* § 114(j)(15) (“A ‘transmission’ is either an initial transmission or a retransmission.”).

⁸⁷ Digital Performance Right in Sound Recordings Act of 1995 § 3, 109 Stat. at 341–42.

⁸⁸ *Id.*

⁸⁹ 17 U.S.C. § 801(b)(1) (2012).

⁹⁰ *See generally* Digital Millennium Copyright Act, Pub. L. No. 105-304, 112 Stat. 2860 (1998) (codified, as amended, in scattered sections of 17 U.S.C.).

⁹¹ CARP Report, *supra* note 23, at 8.

⁹² *Id.*

⁹³ *Id.*

⁹⁴ Terry Hart, *A Brief History of Webcaster Royalties*, COPYHYPE (Nov. 28, 2012), <http://commens.org/11NtYyQ>.

⁹⁵ In its current form, § 106(6) provides that the owner of the sound recording copyright has the exclusive right to “perform the copyrighted work publicly by means of a digital audio transmission.” 17 U.S.C. § 106(6) (2012).

⁹⁶ Hart, *supra* note 94; *see also* CARP Report, *supra* note 23, at 8.

⁹⁷ *See* 17 U.S.C. § 106(6). If retransmitted or “simulcast” over the Internet, traditional

In 1998, Congress settled the escalating contention by passing the Digital Millennium Copyright Act of 1998,⁹⁸ a controversial and expansive piece of legislation that has shaped the current digital-licensing regime.⁹⁹ The DMCA added eligible nonsubscription services to the types of webcasting services subject to the compulsory licensing provision.¹⁰⁰ Further, the DMCA altered the standard that the CARP must apply when determining royalty rates for these compulsory licenses.¹⁰¹ Instead of the section 801(b)(1) standard, the CARP would, for the webcaster compulsory license rates, “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” (known as the WBWS standard).¹⁰² However, the DMCA maintained the existing section 801(b)(1) standard for preexisting subscription services and preexisting satellite radio services, including SiriusXM Radio.¹⁰³

The DMCA settled the dispute over whether webcasting is subject to the section 106(6) digital performance right and whether webcasters who transmit sound recordings on an interactive basis, as defined by section 114(j) of the Copyright Act, must secure consent from individual owners of such recordings and negotiate fees.¹⁰⁴ When webcasters provide non-interactive services, then

radio broadcasting signals lose their exemption and fall within the Section 114 license. *Bonneville Int’l Corp. v. Peters*, 347 F.3d 485, 498 (3d Cir. 2003); *see also* 17 U.S.C. § 106(6) (giving exclusive public-performance rights to sound recorders). The *Bonneville* court quoted the Senate’s report for the following proposition: “The classic example of [an exempt transmission under Section 114(d)(1)(A)] is a transmission to the general public by a free *over-the-air* broadcast station, such as a traditional radio or television station” *Bonneville Int’l Corp.*, 347 F.3d at 498 (quoting S. REP. NO. 104-128, at 19 (1995)) (internal quotation marks omitted) (alteration in original).

⁹⁸ CARP Report, *supra* note 23, at 8. *See generally* Digital Millennium Copyright Act, Pub. L. No. 105-304, 112 Stat. 2860 (1998) (codified at 17 U.S.C. §§ 1201-1205 (2006)).

⁹⁹ Allen Bargfrede & Cecily Mak, *The State of Digital Law*, BERKLEE COLLEGE MUSIC (last visited Mar. 5, 2014), <http://commcns.org/1w9TYgh>.

¹⁰⁰ Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings and Ephemeral Recordings, 67 Fed. Reg. 45,240, 45,240 (July 8, 2002).

¹⁰¹ CARP Report, *supra* note 23, at 9.

¹⁰² *Id.* at 19 (internal quotation marks omitted). Note the difference between the WBWS standard and the 801(b)(1) standard. *Compare* 17 U.S.C. § 114 (f)(2)(B) (2012) (“In establishing rates . . . [for] eligible nonsubscription services and new subscription services, the Copyright Royalty Judges 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 a willing seller.*”), *with* 17 U.S.C. § 801(b)(1) (2012) (requiring the Copyright Royalty Judges to: maximize the work’s public availability; give the copyright owner a fair return and the copyright user a fair income; reflect the relative roles of the copyright owner and copyright user; and minimize any disruptive impact on prevailing industry practices).

¹⁰³ Digital Millennium Copyright Act § 405(a)(2), 112 Stat. at 2895. More specifically, the DMCA stated, “In establishing rates and terms for *preexisting subscription services* and *preexisting satellite digital audio radio services*, in addition to the objectives set forth in *section 801(b)(1)*” *Id.* (emphasis added).

¹⁰⁴ CARP Report, *supra* note 23, at 8–9.

those providers are eligible for compulsory licensing.¹⁰⁵ For that reason, Congress created a new compulsory license in section 114(d)(2) and (f)(2) for “eligible nonsubscription transmissions,” including webcasters’ non-interactive transmissions of sound recordings.¹⁰⁶ The webcaster must comply with several requirements, in addition to those for subscription services, to be eligible for the compulsory license.¹⁰⁷ Of the webcaster royalties, 50% would be distributed to copyright owners and 50% would be distributed to performers.¹⁰⁸

Thus, the performance of a musical work through a digital audio transmission requires the webcaster to obtain three licenses: a license for the public performance of the musical composition, which is generally obtained from a PRO;¹⁰⁹ a license for the public performance of the sound recording for digital audio transmissions;¹¹⁰ and a license for the creation of ephemeral copies of the sound recording used in the transmission process.¹¹¹

E. The Webcaster Settlement Acts of 2008¹¹² and 2009¹¹³

The development of the webcasting royalty scheme did not end with the DMCA, but was further complicated when CARP convened the first rate-setting proceedings for statutory webcasting in 2002 for the time periods of 1998–2000 and 2001–2002,¹¹⁴ and then again in 2005 for the time period of

¹⁰⁵ *Id.* at 8.

¹⁰⁶ *Id.*

¹⁰⁷ *Id.* at 8–9.

¹⁰⁸ *Id.* at 9.

¹⁰⁹ *Id.* at 5 n.6.

¹¹⁰ 17 U.S.C. § 114(a) (2012) (“The exclusive rights of the owner of copyright in a sound recording are limited to the rights specified by clauses (1), (2), (3) and (6) of section 106”); *see also* 17 U.S.C. § 106(6) (2012) (“[T]he owner of copyright . . . has the exclusive rights to do and to authorize . . . in the case of sound recordings, to perform the copyrighted work publicly by means of a digital audio transmission.”).

¹¹¹ 17 U.S.C. § 112(a)(1) (2012). Section 112(a)(1) provides that a webcaster making a digital broadcast transmission of a performance of a sound recording on a nonsubscription basis may make a single copy or phonorecord of a particular program if: (1) the copy is retained and used solely by the webcaster for its own broadcasts within its local service area; (2) no further copies are made; and (3) the copy or phonorecord is destroyed within six months after the first public transmission, unless preserved exclusively for archival purposes. *Id.*

¹¹² *See generally* Webcaster Settlement Act of 2008, Pub. L. No. 110-435, 122 Stat. 4974 (codified as amended at 17 U.S.C. § 114).

¹¹³ *See generally* Webcaster Settlement Act of 2009, Pub. L. No. 111-36, 123 Stat. 1926 (codified as amended at 17 U.S.C. § 114).

¹¹⁴ CARP Report, *supra* note 23, at 1–2 (“[T]his [CARP] . . . has been empanelled to set compulsory license fees for eligible nonsubscription digital audio transmissions of sound recordings as provided for in § 114 of the . . . [DMCA], as well as for the making of ephemeral copies . . . as provided for in § 112 of the DMCA.”).

2006–2010.¹¹⁵ In 2004, amidst all of the rate-setting proceedings, Congress passed the Copyright Royalty and Distribution Reform Act of 2004 (“CRDRA”), which replaced the CARP with a permanent panel of judges, refined the arbitration procedures to establish licensing rates, and required periodic adjustments to those rates for digital services subject to compulsory licensing.¹¹⁶ The permanent, three-person panel of judges was the Copyright Royalty Board (“CRB”).¹¹⁷ The CRB (formerly the CARP) had a legislative mandate to set royalty rates for compulsory licenses.¹¹⁸

Then, in 2008, Congress passed the Webcaster Settlement Act of 2008 (“WSA”)¹¹⁹—which was extended in 2009¹²⁰—to encourage settlements of royalty disputes for statutory webcasting rates. The WSA permitted SoundExchange,¹²¹ the principal administrator of statutory licenses under sections 112 and 114 of the Copyright Act, and webcasters to negotiate settlements of ongoing disputes arising out of the royalty rates that were set by the Judges for the 2006–2010 time period, and also permitted SoundExchange to negotiate royalty rates for the 2011–2015 time period.¹²²

Congress recognized that certain webcasting business models warranted or might even require experimental settlement agreements, because if those settlements were classified as precedent-setting in royalty-rate proceedings, then

¹¹⁵ Digital Performance Right in Sound Recordings and Ephemeral Recordings, 72 Fed. Reg. 24,084, 24,084 (May 1, 2007).

¹¹⁶ The Copyright Royalty and Distribution Reform Act of 2004, Pub. L. No. 108-419, § 3, 118 Stat. 2341, 2341–42, 2357–58, 2365 (2004) [hereinafter CRDRA].

¹¹⁷ *Id.* § 3, 118 Stat. at 2341. The CRDRA phased out the CARP system that had been part of the Copyright Office since 1993. CRDRA replaced CARP (which itself replaced the Copyright Royalty Tribunal in 1993) with the Copyright Royalty Board. The Copyright Royalty Judges are appointed for six-year terms with an opportunity for reappointment. However, the first three judges serve two-, four- and six-year terms, so as to stagger terms and avoid replacement of all three judges at one time. *Id.* § 3, 118 Stat. at 2345.

¹¹⁸ CARP Report, *supra* note 23, at 7–8.

¹¹⁹ *See generally* Webcaster Settlement Act of 2008, Pub. L. No. 110-435, 122 Stat. 4974 (codified as amended at 17 U.S.C. § 114).

¹²⁰ Webcaster Settlement Act of 2009, Pub. L. No. 111-36, § 2, 123 Stat. 1926, 1926 (codified as amended at 17 U.S.C. § 114).

¹²¹ *Exclusive Interview with SoundExchange President Mike Huppe*, SOUNDEXCHANGE, <http://commcns.org/11Nu6hR> (last visited Mar. 24, 2014) (“SoundExchange is a non-profit performance right organization that collects statutory royalties from satellite radio (such as SIRIUS XM), Internet radio (like Pandora), cable TV music channels and similar platforms for streaming sound recordings. The Copyright Royalty Board, which is appointed by The U.S. Library of Congress, has entrusted SoundExchange as the sole entity in the United States to collect and distribute these digital performance royalties on behalf of featured and non-featured recording artists, master rights owners (usually record labels), and independent artists who record and own their masters.”).

¹²² *About Digital Royalties*, SOUNDEXCHANGE, <http://commcns.org/11Nu6hR> (last visited Mar. 24, 2014).

parties might not enter into settlements in the first place.¹²³ Notably, any commercial webcaster may choose the terms of this agreement over the terms of the March 2007 CRB decision¹²⁴ meaning companies can choose the terms by which they abide.

The ability to choose between the WSA versus the CRB terms compounds the already-complex determination of webcasting royalty rates. For instance, between the broad categories of “commercial webcaster” and “noncommercial webcaster,” a company can usually easily identify under which category it falls.¹²⁵ However, a webcaster must then further determine where it fits within each broad category. For instance, under the commercial webcaster grouping, there are eight subcategories from which to determine where a company fits: (1) commercial webcasters following the CRB rates; (2) commercial webcasters following the WSA rates; (3) broadcasters; (4) small broadcasters; (5) pureplay broadcasters; (6) small pureplay webcasters; (7) small webcasters; and (8) microcasters.¹²⁶ Noncommercial webcaster classification is no easier. Under the noncommercial webcaster grouping, there are five subcategories.¹²⁷

According to the pureplay settlement, every pureplay webcaster must make a \$25,000 minimum payment on an annual basis, which serves as a deposit against the overall royalty payments for the year, should the overall payment exceed \$25,000.¹²⁸ In order to calculate the royalty payments for pureplay, webcasters are divided into three groups. Large webcasters, who are defined as entities with at least \$1.25 million in annual revenues,¹²⁹ must pay the greater of 25% of total revenues or a “per performance” rate that is about half of that

¹²³ This concern resulted from the fact that relatively few meaningful settlements occurred prior to previous statutory webcasting proceedings.

¹²⁴ Webcaster Settlement Act of 2009 § 2.

¹²⁵ See *Commercial Webcaster*, SOUNDEXCHANGE, <http://commcns.org/1gvKyqB> (last visited Mar. 28, 2014) (“Webcasters which are neither tax-exempt under Section 501 of the Internal Revenue Code (e.g. churches, schools, etc.) nor owned by a governmental entity are ‘commercial’ webcasters.”); *Noncommercial Webcaster*, SOUNDEXCHANGE, <http://commcns.org/1jnDHdT> (“Services which are owned by a governmental entity for public purposes or owned by a tax-exempt service under Section 501 of the Internal Revenue Code (e.g., churches, schools, etc.) must operate as ‘noncommercial’ webcasters. . . . (The ‘noncommercial’ status of a webcaster is not based on an absence of advertisements or commercials on the web site or within the programming.)”).

¹²⁶ *Commercial Webcaster*, *supra* note 125.

¹²⁷ *Noncommercial Webcaster*, *supra* note 125 (describing the five noncommercial webcasting categories: (1) noncommercial webcasters following the CRB rates; (2) noncommercial webcasters following the WSA rates; (3) noncommercial microcasters; (4) noncommercial educational webcasters; and (5) specific webcasters industry organizations classify under public radio).

¹²⁸ See KOHN & KOHN, *supra* note 18, at 1524–27 (discussing the royalty rates set for various webcasting services in much greater detail).

¹²⁹ See *id.* at 1526.

established by the March 2007 CRB decision.¹³⁰ For example, the settlement set the 2013 rate at \$0.00120 per song per listener, while the March 2007 CRB decision set the rate at \$0.0018 per song per listener.¹³¹ In addition, large webcasters must submit census filings of playlist reports.¹³² These monthly filings contain information regarding every song played as opposed to quarterly reports of songs played during two seven-day periods during each quarter.¹³³ These reports must be retained for at least a three-year period.¹³⁴

Small webcasters, another category of webcasters, are defined as entities having fewer than \$1.25 million in annual revenues and with less than the maximum allowable “aggregate tuning hours” (“ATH”) in the year, which ranges from 8 million to 10 million ATH.¹³⁵ Small webcasters must pay the greater of a percentage of revenue, calculated as follows, for the 2009–2015 period: 12% of the first \$250,000 in revenue and a higher rate of 14% for revenue in excess of \$250,000, or, in the alternative, 7% of expenses.¹³⁶ In addition, these small webcasters must also submit census filings of playlist reports, which consist of information about every song played.¹³⁷ However, small webcasters can pay a proxy fee in exchange for relaxed reporting requirements.¹³⁸ Pureplay webcasters, such as Pandora, who offer subscription services in addition to a pure music stream must pay a rate identical to that paid by broadcasters participating in the SoundExchange/NAB deal.¹³⁹ SoundExchange pitched a “discounted rate structure” to content owners as an experiment, asserting that the original rates themselves were fair.¹⁴⁰

Since the implementation of these rate structures, Pandora and other webcasters have continuously complained that the royalty rates are too high and envision heavy users as ultimately bearing the majority of increased, associated costs from advertising and other methods to increase revenues.¹⁴¹ In or-

¹³⁰ *See id.* at 1524–25.

¹³¹ *See id.* at 1524–26.

¹³² *See id.*

¹³³ *See id.* at 1526.

¹³⁴ 37 C.F.R. § 370.3(h) (2012).

¹³⁵ *See* KOHN & KOHN, *supra* note 18, at 1526–27.

¹³⁶ *See id.* at 1527.

¹³⁷ *See id.* at 1527–28.

¹³⁸ *See id.* at 1521–22.

¹³⁹ *See id.* at 1524–26.

¹⁴⁰ *See* Press Release, SoundExchange, SoundExchange and “PurePlay” Webcasters Reach Unprecedented Experimental Rate Agreement (July 7, 2009), *available at* <http://commens.org/1iljyp4> (according to SoundExchange, “Time will tell if revenue sharing is the right move for both the recording community and webcasters . . . but we’re willing to take the risk in the hope that artists, rights holders and webcasters can all benefit”).

¹⁴¹ *See* Eric Egelman, *Pandora CEO Pushes Congress for Lower Royalties*, BLOOMBERG (Nov. 28, 2012), <http://commens.org/1on1UZf> (stating that the company’s royalty burden is currently impermissibly calculated and too high).

der to reduce substantially the overall royalty burden of both the recording and publishing royalties, some companies like Pandora have creatively shaped their business models to qualify for lower royalty calculations for musical works,¹⁴² in addition to pushing for the IRFA legislation aimed at recording royalties. Ultimately, these efforts on behalf of webcasters like Pandora demonstrate that these companies will pursue multiple creative means to reduce royalty burdens, in the hope that either on the publishing side or the recording side, the royalty burden will be lessened.

III. AN OVERVIEW OF THE PANDORA WEBCASTING MODEL

While a number of webcasters exist in the United States, Pandora remains one of the leading webcasters with approximately 175 million registered users.¹⁴³ In a one year period, Pandora nearly doubled the amount of content streamed; users streamed 14.01 billion hours of content for the fiscal year ending January 31, 2013,¹⁴⁴ significantly more than the 8.2 billion hours of content streamed in 2012.¹⁴⁵

As a pureplay webcaster,¹⁴⁶ Pandora falls under the compulsive royalty burden of \$0.12 per song played, heavily relying upon advertising revenue to meet this burden.¹⁴⁷ Currently, Pandora offers two models to its subscribers: an ad-supported service provided free of charge, and a subscription-based service called Pandora One.¹⁴⁸ The free service enables listeners to access content libraries and up to 100 personalized playlist stations interrupted by periodic advertisements.¹⁴⁹ The institution of a listening cap of 320 hours per month on desktop and personal computers serves as one major drawback for those who heavily use its service.¹⁵⁰ However, Pandora reports that very few listeners exceed this cap.¹⁵¹ For those listeners that do exceed the cap, Pandora reserves the

¹⁴² Glenn Peoples, *Pandora Buys Terrestrial Radio Station in North Dakota, Aims for Lower ASCAP Royalties*, BILLBOARD.BIZ (July 11, 2013), <http://commcns.org/1rafn9c>.

¹⁴³ Pandora 2013 Form 10-K, *supra* note 47, at 2 (defining registered users are defined as “the total number of accounts that have been created for our service at period end”).

¹⁴⁴ *Id.*

¹⁴⁵ *Id.* at 3.

¹⁴⁶ *Id.* at 3–5. Unlike traditional radio stations that broadcast the same content to all listeners at the same time, Pandora’s content is broadcast to each individual listener based upon an algorithm, called “The Music Genome Project.” *Id.* The algorithm assembles user data to create playlists, which “predict listener music preference, play music content suited to the tastes of each individual listener and introduce listeners to music they will love.” *Id.*

¹⁴⁷ *Id.* at 9.

¹⁴⁸ *Id.* at 3.

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ *Id.*

right through its terms of service to charge a \$0.99 fee.¹⁵²

Listeners accessing Pandora's free service through devices other than a personal computer have access to unlimited playing time of music and other content, like stand-up comedy.¹⁵³ A large majority of Pandora users access the service through their tablets or mobile devices.¹⁵⁴ As more and more listeners opt to stream Pandora music through their mobile devices,¹⁵⁵ Pandora is instituting a listening cap on those mobile users¹⁵⁶ because registered users carry their mobile devices on their person and will have substantially more access to Pandora on their phones. The shift in the user listening methods radically alters the amount of time one can access the service. For instance, user time is naturally limited in the traditional listening method on a desktop or laptop computer, as users periodically step away from their computers, or leave their computers at the end of a workday.

In addition to the free service provided by Pandora, listeners have the option of subscribing to Pandora One, a subscription service through which subscribers pay either \$3.99 for a one-month subscription or \$36.00 for a one-year subscription.¹⁵⁷ The advantages of paying for Pandora One include the elimination of ads, unlimited listening time, and higher quality audio streams.¹⁵⁸ Approximately 13% of Pandora's total revenue in fiscal year 2012 was achieved through this subscription service.¹⁵⁹ Pandora hopes to persuade more users to join its subscription service; however, not many users have converted from the paid service.¹⁶⁰

Nevertheless, as more companies enter the Internet-radio market,¹⁶¹ Pandora will likely find it increasingly difficult to convince users to pay for Pandora One when many webcasters provide free, ad-supported services. If a substantial majority of Pandora's registered users continue to utilize the free service and Pandora cannot increase the percentage of paid subscribers, Pandora will most likely need to secure a lower royalty burden in order to achieve profitability. This is where Pandora really has the opportunity to justify a reduced roy-

¹⁵² *Id.*

¹⁵³ *Id.* at 6.

¹⁵⁴ *Id.* at 2 (noting that approximately 140 million registered users accessed Pandora services through their tablets or mobile devices in 2013).

¹⁵⁵ Andy Fixmer, *Pandora Says 40-Hour Mobile Cap Cuts Music Content Costs*, BLOOMBERG (May 7, 2013), <http://commens.org/1kirzjo>.

¹⁵⁶ *Id.* (noting that Pandora instituted a 40-hour listening cap on its mobile users in order to reduce its royalty burden.).

¹⁵⁷ *Id.*

¹⁵⁸ *See Pandora One*, PANDORA, <http://commens.org/1oBg8nh> (last visited Jan. 27, 2014) (discussing the benefits of upgrading to Pandora One).

¹⁵⁹ Pandora 2013 Form 10-K, *supra* note 47, at 3.

¹⁶⁰ *Id.*

¹⁶¹ Glenn Peoples, *Business Matters: Pandora Pauses, But Internet Radio on the Rise*, BILLBOARD.BIZ (Feb. 7, 2014), <http://commens.org/1oBg9aX>.

alty burden: if Pandora can demonstrate that it acts more than a mere host of copyrighted content and, instead, provides a valuable service that significantly impacts or enhances the user experience of that copyrighted content,¹⁶² then Pandora has a stronger argument to reduce the sound recording royalties paid.

Without a reduced royalty structure, Pandora will likely continue posting financial deficits. Pandora currently has an accumulated deficit of \$139.6 million due to its inability to generate sufficient revenues as the number of listening hours increases and the royalties paid for content acquisition also continue increasing.¹⁶³ Pandora explicitly acknowledges that at the current webcasting royalty rates, the advertising revenue generated may not be enough to offset content royalty expenses even with the relatively low subscription rate of Pandora One.¹⁶⁴ Approximately 88% of Pandora's revenue comes from advertising sales, but these advertising agreements are short term and are generally terminable at any time by the advertiser.¹⁶⁵ Particularly, as Pandora listenership shifts to mobile devices, Pandora must continue capturing a majority of its revenues through advertising and continue increasing its listener base in the mobile platform if it plans to continue its current business model.¹⁶⁶

Pandora recently initiated an experiment with its current business model to reduce its royalty burden regarding performance royalties. In its desperation to lessen its royalty burden, Pandora sought to substantially reduce its performance licensing fees by making a very bold move: Pandora strategically purchased a terrestrial radio station in South Dakota.¹⁶⁷ Pandora purchased a small station that only has a listenership of 108,000 people in the spring of 2013, an interesting move considering over 70 million people listen to Pandora each month.¹⁶⁸ By acquiring this small terrestrial station, Pandora attempts to take advantage of reduced performance royalty fees¹⁶⁹ available to broadcast radio stations.¹⁷⁰ While the small station acquisition directly relates to *performance* royalties issues and *not* sound recording royalties that are the subject of the

¹⁶² See Pandora 2013 Form 10-K, *supra* note 47, at 4 (stating that Pandora's delivery platform provides users the ability to research song lyrics, to read the history of the artists they listen to, to view photos of the artists, and to buy albums and songs via Amazon or iTunes).

¹⁶³ *Id.* at 14.

¹⁶⁴ *Id.*

¹⁶⁵ *Id.* at 4, 15.

¹⁶⁶ *Id.* at 14.

¹⁶⁷ *Pandora Buys Terrestrial Radio Station in North Dakota*, *supra* note 142.

¹⁶⁸ *Id.*

¹⁶⁹ Again, "performance royalty fees" refers to the royalties paid out to songwriters and publishers. This is distinguished from the sound recording royalties, which are subject of the IRFA.

¹⁷⁰ *Pandora Buys Terrestrial Radio Station in North Dakota*, *supra* note 142. The strategic purchase is a way for Pandora to qualify for Radio Music Licensing Committee agreements regarding royalties and public performances of musical works from the PROs.

IRFA, Pandora's move exemplifies the varying methods and experiments webcasters will consider in order to decrease their overall royalty burdens. This importantly demonstrates that reduced royalties are sought from both the musical recording owners (the PROs and songwriters) as well as the sound recording owners. This could have a substantially negative impact on the livelihood of musical content creation and have negative implications for the sustainability of the music industry.

IV. THE INTERNET RADIO FAIRNESS ACT OF 2012

As a result of Pandora's purported royalty woes, the company hired Washington lobbyists in 2012 to assist it in securing recalculated sound recording royalty rates for webcasters.¹⁷¹ Pandora lobbied for the passage of a bill that would change how the CRB determines webcasters' statutory royalty rates for the digital performances of sound recordings by using the 801(b)(1) Standard.¹⁷² The culmination of Pandora's efforts resulted in the proposal of the IRFA in the fall of 2012.¹⁷³

While the IRFA ultimately failed to pass, it would have altered federal law by changing the DMCA standard currently applied by CRJs to establish compulsory licensing royalty rates for the public performance of sound recordings by noninteractive digital audio services.¹⁷⁴ The current standard established rates and terms based upon the willing buyer/willing seller standard.¹⁷⁵ In determining the applicable royalty rates, the IRFA would have required CRJs to make the following considerations: (1) the public's interest in both the creation of new sound recordings of musical works and in fostering online and other digital performances of sound recordings; (2) the income necessary to provide a reasonable return on all relevant investments, including investments in prior periods for which returns have not been earned; (3) the value of any promotional benefit or other non-monetary benefit conferred on the copyright owner by the performance (*i.e.*, radio promotional benefits that terrestrial radio claims); and (4) the contributions made by the digital audio transmission service to the content and value of its programming.¹⁷⁶

In addition, the IRFA would have authorized a \$500.00 minimum, annual administrative fee *on top of* the royalty rates paid.¹⁷⁷ The burden of proof would have been placed on sound recording copyright owners to establish that fees

¹⁷¹ See, e.g., Egelman, *supra* note 141.

¹⁷² 17 U.S.C. § 801(b)(1) (2012); see *supra* notes 112–14 and accompanying text.

¹⁷³ See generally Internet Radio Fairness Act, S. 3609, 112th Cong. (2012).

¹⁷⁴ *Id.*

¹⁷⁵ *Id.*

¹⁷⁶ *Id.* § 2(C)–(D).

¹⁷⁷ *Id.* § 3(a)(2)(A)(i)(II).

and terms they seek satisfy the requirements instituted by the IRFA and do not exceed the fees to which most copyright owners and users would agree under competitive market circumstances.¹⁷⁸

The IRFA sought to establish licensing fee structures, aimed at fostering competition among the licensors of sound recording performances and between sound recording performances and other programming.¹⁷⁹ Further, CRJs would have been prohibited from disfavoring a percentage of revenue-based fees and taking into account the rates and terms in licenses for interactive services or the determinations rendered by CRJs prior to the enactment of this Act.¹⁸⁰ This would eliminate any attempts to examine royalty rates across digital service types and examine whether or not the rates are appropriate based upon the market.

The IRFA would also have allowed particular transmitting organizations entitled to transmit a performance to the public to make more than one copy or phonorecord embodying a performance or display of a work for its own transmissions, archival preservation, or security.¹⁸¹ Currently, *no more than one copy* can be made for such purposes.¹⁸² By allowing more than one copy to be made, the exclusive rights of the content owners are further restricted.

Furthermore, the IRFA would have required common agents or collectives representing copyright owners of sound recording to make available a comprehensive, centralized list of copyright licensing information via the Internet.¹⁸³ The list's aim was to facilitate licensing and to provide greater transparency to the public and companies.¹⁸⁴ A centralized list could absolutely be helpful in the facilitating of licensing, but would be a costly undertaking due to massive songwriter catalogs as well as the vagueness of the statute's language. In addition, many of the collectives, like PROs, already have their own databases,¹⁸⁵ so why add another one to the mix? With multiple rights owners in songs and sound recordings, it could be problematic in determining which party amongst those rights owners bears the burden of providing the copyright information.

Finally, the evidentiary, procedural, and judicial review standards would

¹⁷⁸ *Id.* § 3(a)(3)(B) (“‘Competitive market circumstances’ are circumstances in which a licensee enters into a license for the noninteractive performance of sound recordings with a licensor that does not possess market power resulting from the aggregation of copyrights, either by a licensing collective or individual copyright owners.”).

¹⁷⁹ *Id.* § 3.

¹⁸⁰ *Id.*

¹⁸¹ *Id.*

¹⁸² *Id.*

¹⁸³ *Id.* § 5.

¹⁸⁴ *Id.*

¹⁸⁵ *See, e.g.*, ACE Database, ASCAP, <http://commcns.org/1hrtZr1> (last visited Apr. 11, 2014).

have been revised under the IRFA for CRJ proceedings and determinations.¹⁸⁶ In those proceedings which determine the terms and rates of royalty payments for digital performances of sound recordings, participants are required during voluntary negotiations to disclose: previous license agreements entered into by the participant, its members, or participant-represented licensors or licensees during a specified preceding five-year period; or other documents relied upon in rate-setting proceedings.¹⁸⁷ The Librarian of Congress would have been required to submit recommendations to Congress on how the federal government can facilitate, and possibly establish, a global music registry that is sustainably financed and consistent with the World Intellectual Property Organization (“WIPO”) obligations.¹⁸⁸

A. The IRFA’s Supporters

The IRFA addressed laws that its supporters claim disadvantaged the Internet radio compared to other digital services.¹⁸⁹ Supporters of the bill, such as Senator Ron Wyden, voiced concern that barriers to innovation in digital broadcasting hamper the abilities of webcasters and Internet radio businesses to start up, create competition, and create jobs in the digital music marketplace.¹⁹⁰ Legislators backing the IRFA were concerned with musicians’ and songwriters’ abilities to market themselves, obtain exposure to audiences, and their abilities to receive adequate compensation for their music.¹⁹¹ According to these legislators, IRFA would have addressed those concerns.¹⁹²

In addition to the claim that the IRFA would assist content creators and the music industry as a whole, supporters claimed the IRFA would have benefitted consumers by providing more avenues for broader digital music access and would have also provided those consumers with “diverse music choices.”¹⁹³ Senator Wyden claimed that the IRFA would end discrimination against Internet radio by treating it the same as satellite and cable radio.¹⁹⁴

Supporters also believed that the WBWS standard could not apply because “there is no functioning market for these licenses and . . . judges are left with

¹⁸⁶ S. 3609 § 6.

¹⁸⁷ *Id.*

¹⁸⁸ *Id.* § 7.

¹⁸⁹ Senator Ron Wyden, Summary of the Internet Radio Fairness Act of 2012 (Sept. 21, 2012), available at <http://commcns.org/1nN24Ws>.

¹⁹⁰ *Id.*; see also Gregory A. Barnes, *A Common Sense Approach to Internet Radio Royalties* (Nov. 7, 2012, 9:35 AM), <http://commcns.org/1jVeiy6>.

¹⁹¹ Summary of the Internet Radio Fairness Act of 2012, *supra* note 189.

¹⁹² *Id.*

¹⁹³ *Id.*

¹⁹⁴ *Id.*

very little information to make reasonable conclusions.”¹⁹⁵ Senator Wyden specifically asserted that the current rate setting for Internet Radio has directly led to webcasters paying five times the amount of royalties as other digital music formats like satellite and cable.¹⁹⁶ Through implementation of the IRFA, supporters believed that the CRJs could establish royalty rates based upon a broader set of factors delineated under the 801(b)(1) standard.¹⁹⁷

The IRFA has garnered support from a group of Internet radio service providers, broadcast radio companies, and others concerned about the Internet radio industry’s future.¹⁹⁸ Some of these stakeholders formed the Internet Radio Fairness Coalition (“IRFC” or “Coalition”) in October 2012 “to advocate for legislation that would establish an equitable royalty rate setting standard for Internet radio.”¹⁹⁹ The IRFC claimed that the current standard that determines how webcasting should pay the recording industry, is out of balance and grossly unfair.²⁰⁰ In the digital marketplace, the current system of determining how licensing rates are paid is ancient and out of step with the current realities of the digital music business.²⁰¹ The Coalition supported the IRFA for a number of reasons, as iterated by other supporters. It claimed that digital music consumers would have a greater variety of music choices.²⁰² The IRFA would enable artists to earn incrementally greater royalty payments as Internet radio continues its growth.²⁰³ Artists, IRFC claimed, would have a better connection with fans through marketing, merchandising, and tours.²⁰⁴ The IRFA could establish a “sustainable digital marketplace” to act as a basis for digital music entrepreneurs to create new and innovative methods and services for delivering digital music content to the listeners.²⁰⁵ Finally, IRFC claimed that the IRFA

¹⁹⁵ *Id.*

¹⁹⁶ *Id.*

¹⁹⁷ *Id.*

¹⁹⁸ See, e.g., *DiMA Welcomes House Subcommittee Hearing on Internet Radio Fairness Act*, DIGITAL MEDIA ASS’N, <http://commcns.org/1nN2a0c> (last visited Feb. 3, 2014); see Eric Savitz, *Pandora Asks Users to Lobby Congress on Royalty Rates*, FORBES (Sept. 24, 2012), available at <http://commcns.org/NOT1wz>.

¹⁹⁹ *Internet Radio Fairness Coalition Launches*, RADIO MAG. (Oct. 26, 2012), <http://commcns.org/1gvKOpC> (last visited Mar. 1, 2014).

²⁰⁰ *Internet Radio Fairness Coalition Launches to Help Accelerate Growth and Innovation in Internet Radio to Benefit Artists, Consumers and the Recording Artists*, PR NEWSWIRE (Oct. 25, 2012), <http://commcns.org/1ilk6eB>.

²⁰¹ *Rising Tides Envisioning Fair Internet Radio*, FUTURE MUSIC COALITION, <http://commcns.org/1muinYU> (last visited Mar. 1, 2014).

²⁰² Summary of the Internet Radio Fairness Act of 2012, *supra* note 189.

²⁰³ Jason Cherkis, *Pandora Goes after Artist Royalties in Big Risk*, HUFF POST (Dec. 4, 2012), <http://commcns.org/1oBgxpE>.

²⁰⁴ Press Release, Internet Radio Fairness Coalition, The IRFA: Good for Consumers, Artists, and the Recording Industry 1, available at <http://commcns.org/1muiCmC> (last visited May 26, 2014).

²⁰⁵ Kenneth J. Thompson, *The Internet Radio Fairness Act and Atlanta’s Local Artists*,

would result in greater revenues for record labels, the primary deliverers of digital music content on the Internet.²⁰⁶

Additionally, the IRFC claimed that the IRFA would have enabled artists to make more money through the accelerating growth and innovation of Internet radio.²⁰⁷ The Coalition argued that “the *more* the sector grows, the *more* their music is played, and the *more* opportunities they will have to reach their audiences, who are spending more time than ever looking for music online.”²⁰⁸ However, this belief rests on the assumption that this Internet radio growth will occur quickly and, therefore, afford copyright owners the opportunity to earn more royalties at the 801(b)(1) Standard through broader digital radio consumption. There is no guarantee, however.

Some scholars contend that streaming does not completely destroy overall sales of music, as long as the number of digital music subscribers paying for music continues to “climb rapidly.”²⁰⁹ However, with the introduction of other nonsubscription radio services like iRadio, it is likely that consumers will discontinue their paid subscriptions and will, instead, opt for nonpaid deliveries. As one scholar posited, “There is a point at which there would be 100[%] cannibalization [of permanent digital downloading and brick-and-mortar sales], and we would make more money through subscription services . . . [w]e calculate that point at approximately 20 million worldwide subscribers.”²¹⁰ Hopefully, this point is in the near future, as recent statistics indicate permanent downloads have begun sharply declining.²¹¹

One proponent asserted that the standards utilized in royalty rate settings should support sustainable growth and, in addition, the same standard should be applied to satellite, Internet radio, and cable royalty calculations.²¹² Presently, the amount of music played by listeners is suppressed and this, in turn, prevents artists and record labels from earning money.²¹³ The main and most controversial argument that the Coalition has made is as follows:

[R]ecord labels and their allies don’t seem to understand how to help de-

KENNETH J. THOMPSON (Feb. 11, 2013), <http://commcns.org/1w9Vwab>.

²⁰⁶ *Id.*

²⁰⁷ Press Release, Internet Radio Fairness Coalition, *supra* note 204, at 1.

²⁰⁸ *Id.* at 1 (emphasis in original).

²⁰⁹ Ben Sisario, *As Music Streaming Grows, Royalties Slow to a Trickle*, N.Y. TIMES, Jan. 29, 2013, at A3.

²¹⁰ *Id.* (quoting Cliff Burstein, whose company, Q Prime, manages major artists like Metallica) (internal quotation marks omitted).

²¹¹ Glenn Peoples, *The State of Streaming Music As Beats Music Launches*, BILLBOARD.BIZ (Jan. 21, 2014), <http://commcns.org/1nqJEMS> (“In all, U.S. consumers bought 76.6 million fewer tracks and 99,000 fewer digital albums [in 2013] . . . The silver lining: losses in digital sales were undoubtedly smaller than the gains in advertising-supported and subscription streaming revenues.”).

²¹² Summary of the Internet Radio Fairness Act of 2012, *supra* note 189.

²¹³ Press Release, Internet Radio Fairness Coalition, *supra* note 204.

velop a sustainable market, and without that expertise they have defaulted to simply pushing for rates that cause possible new entrants to decide against entering the market and existing players to either drop out or reduce their volume.²¹⁴

The Coalition concludes that the digital marketplace will ultimately collapse unless structures are implemented that facilitate the growth of a real, sustainable marketplace, and the parties should focus on the licensing-marketplace picture as a whole, because artists receive compensation based upon volume of plays.²¹⁵ The Coalition's argument lacks merit because new webcasting parties, like iTunes Radio and Beats Music, continue to enter the market.²¹⁶ However, the fact that Beats Music chose a subscription-only service arguably suggests that the company believes that the royalty burden is too high for it to be profitable.²¹⁷ On the other hand, Beats Music could simply be making smarter business decisions than other webcasters by charging customers a small monthly fee.

B. The Royalty Standard Comparison

While the IRFA addresses multiple aspects of Internet radio, most of the controversy has centered on the proposal to adopt the 801(b)(1) Standard, leaving the WBWS Standard behind. The 801(b)(1) Standard and the WBWS standard disparately treat the parties, ultimately resulting in wide variation between royalties paid to content owners depending upon the type of digital service provided.

1. *The 801(b)(1) Standard*²¹⁸

At the heart of the IRFA controversy lies the 801(b)(1) Standard, section 114(f) of the Copyright Act empowered the CRJs to set rates, absent voluntary

²¹⁴ *Id.*

²¹⁵ *Id.*

²¹⁶ *See, e.g.,* Apple, Inc. 2013 Form 10-K, *supra* note 44, at 3 (describing the ability of users to utilize iTunes Radio, the free Internet streaming service introduced September 2013, on a variety of Apple devices, including on iOS devices, Mac and Windows personal computers and Apple TV). Apple's entrance into the market with iTunes Radio occurred despite the IRFA, its proposal, or the subsequent fall in Pandora's stock following the failure of the IRFA. *See* Pandora 2012 Form 10-K, *supra* note 17, at 3 (providing data as of the end of the fiscal year, January 31, 2012).

²¹⁷ *We Are Beats Music*, *supra* note 39; *see also The State of Streaming Music As Beats Music Launches*, *supra* note 211 (observing that Beats Music is not a traditional, free, ad-supported webcaster like Pandora, which offers both free and subscription services; however, Beats Music has chosen to offer subscription services only).

²¹⁸ 17 U.S.C. § 801(b)(1) (2012).

agreements reached by the parties.²¹⁹ With rate-setting, the statutorily set objectives are:

(A) To maximize the availability of creative works to the public; (B) To afford the copyright owner a fair return for his or her 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; and (D) To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices.²²⁰

The CRJs may make determinations concerning the adjustment of compulsory license royalty rates.²²¹ In addition, the CRJs may make determinations concerning the adjustment of reasonable copyright royalty rates under various types of licenses.²²²

The CRJs may also make determinations concerning the adjustment of copyright royalty rates under licenses governing secondary transmissions, solely in accordance with certain statutory provisions.²²³ The Judges must weigh all relevant considerations and set out their conclusions in a form that permits adequate judicial review.²²⁴ Additionally, copyright royalty rate adjustment proceedings may be conducted every fifth calendar year, and the Judges may not conduct proceedings more frequently.²²⁵ During those calendar years, any owner or user of a copyrighted work whose royalty rates are specified or established by the Copyright Act may file a petition with the CRJs declaring a rate determination or adjustment.²²⁶ Additionally, no burden of proof on a party seeking rate adjustment exists.²²⁷

In addition, courts substantially defer to the ratemaking decisions of the CRB, because Congress expressly tasked it with balancing the conflicting statutory objectives enumerated in the Copyright Act.²²⁸ To the extent that the statutory objectives determine a range of reasonable royalty rates that would serve all the objectives adequately but to differing degrees, the Board is free to

²¹⁹ 17 U.S.C. § 114(f)(1)(B) (2012).

²²⁰ 17 U.S.C. § 801(b)(1).

²²¹ *Id.* § 801(b)(2).

²²² *Id.*

²²³ *Id.* § 801(b)(2)(A).

²²⁴ *Id.* § 801(b)(2)(B).

²²⁵ 17 U.S.C. § 114(f)(1)(A) (2012).

²²⁶ *Id.* § 114(f)(1)(C).

²²⁷ Paul Fakler, *Music Copyright Royalty Rate-Setting Litigation: Practice Before the Copyright Royalty Board and How It Differs from ASCAP and BMI Rate Court Litigation*, 33 LICENSING J. 1, 5 (2013), available at <http://commcns.org/1jSU3Qf>.

²²⁸ 17 U.S.C. § 801(b)(2).

choose among those rates.²²⁹ Courts are without authority to set aside the particular rate chosen by the Board, so long as that rate lies within a zone of reasonableness.²³⁰

2. *The Willing Buyer/Willing Seller Standard*²³¹

Webcasters are subject to a different standard as enacted under the DMCA: the WBWS standard.²³² The WBWS standard requires the judges to “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.”²²³³ A major concern of webcasters and the standard’s critics is that the standard is a theoretical determination, prohibiting the CRB from considering other royalty rates, relying instead upon theoretical markets for rate-setting.²³⁴ Ironically, however, the IRFA also set such prohibitions in its proposal. In addition, the royalty rate is pre-determined for a five-year period prior to the commencement of that period,²³⁵ resulting in predictability of rates and business costs.

Some scholars claim that the WBWS standard emerged as a result of powerful record industry conglomerates having the loudest voices at the bargaining table during the DMCA negotiations.²³⁶ At that time, it was unclear how big the webcasting industry would grow.²³⁷ As a result, the record industry secured desirable royalty rates for their content.²³⁸ The proof lies in the comparison of Pandora, which paid royalty rates set by the CRB under the WBWS standard, with SiriusXM, which paid much lower royalty rates under another standard. According to Pandora’s annual report, the webcasting giant paid approximately 50% of its gross revenues in royalties during fiscal year 2012 at a rate of \$0.12 per song played, and could pay around 70% in the first quarter of fiscal year 2013.²³⁹ However, following the recent CRB ruling in 2012, under the statutory

²²⁹ *Id.* § 801(b).

²³⁰ Kevin Gordon, *CRB: Open the Door on Web IV: The Future of Webcasting Royalty Rates*, COMMLAW BLOG (Jan. 3, 2014), <http://commcns.org/1muj4RQ>.

²³¹ 17 U.S.C. § 114(f)(2)(B); 17 U.S.C. § 112(e)(4) (2012).

²³² See discussion *supra* Part II.D; see also CARP Report, *supra* note 23, at 8.

²³³ 17 U.S.C. § 114(f)(2)(B); 17 U.S.C. § 112(e)(4).

²³⁴ Kurt Hanson, *Internet Radio Fairness Act Would Spur Innovation*, BILLBOARD.BIZ (Nov. 27, 2012), <http://commcns.org/1tGSWpP>; see 17 U.S.C. § 114(f)(2)(B); see also 17 U.S.C. § 112(e)(4).

²³⁵ Gordon, *supra* note 230.

²³⁶ See, e.g., Casey Rae-Hunter, *Better Mousetraps: Licensing, Access, and Innovation in the New Music Marketplace*, 7 J. BUS. & TECH. L. 35, 36 (2012).

²³⁷ Press Release, Representative Jason Chaffetz, Reps. Chaffetz and Polis Introduce Bipartisan Internet Radio Act (Sept. 21, 2012), <http://commcns.org/RtU5Te>.

²³⁸ Hanson, *supra* note 234.

²³⁹ Pandora 2012 Form 10-K, *supra* note 17, at 8, 123 (data as of the end of the fiscal

license covering the performance of sound recordings over SiriusXM's satellite digital audio radio service, and the making of ephemeral copies in support of such performances, for the five-year period starting January 1, 2013, SiriusXM will pay a royalty based on gross revenues of 9.5% for 2014, 10.0% for 2015, 10.5% for 2016, and 11% for 2017.²⁴⁰ While SiriusXM now pays an escalating rate that is higher, those royalty rates are still nowhere near those paid by Pandora, highlighting the extreme variation in royalty rates between types of digital services.

Royalty parity is a goal that should be reached, but not at the expense of the creators themselves and their abilities to adequately compensated. Content owners provide the *musical content*, the sole reason that consumers flock to webcasting websites. Webcasting services like Pandora merely add value through their curation of content and the technology playing that content. Without the musical content, only advertisements would remain on the webcasting sites. Consumers do not flock to webcasting sites for ads; those consumers seek the products of the content creators: the music. Without the provided content, nothing remains to attract users and webcasters cannot maintain a viable radio service.

Furthermore, the argument that webcasting providers are not viable companies in the long-term fails to persuade. Recently released reports of webcaster revenues and valuations show that these companies are thriving and will continue to do so.²⁴¹ Webcasters continue to enter the market. For instance, Apple entered the Internet radio market and has invested millions of dollars in its webcasting service, iTunes Radio.²⁴² If the webcasting business failed to be a profitable endeavor, why would large technology giants seek entrance into the Internet radio market? Simply put: the evidence strongly suggests that webcasting is a profitable endeavor on a long-term basis and can, therefore, support paying the content owners a fair royalty rate under the WBWS Standard.

V. PROPOSAL AND CONCLUSION

Ultimately, new webcasters entering the Internet radio marketplace should have the opportunity to thrive, but not at the expense of the copyright owners to which their success is dependent upon. While webcasters claim that the 801(b)(1) royalty standard could arguably allow Internet radio companies the chance to thrive by providing a more stable and predictive royalty calculation,

year, January 31, 2012).

²⁴⁰ Sirius XM Holdings Inc., Annual Report (Form 10-K), at 12 (Feb. 4, 2014).

²⁴¹ See Pandora 2012 Form 10-K, *supra* note 17, at 8–10.

²⁴² *iTunes Radio*, APPLE, <http://commens.org/11Nuxc5> (last visited Jan. 27, 2014).

this “stability” should not be at the expense of content creators that provide the very content attracting users to the webcasting services. The free-market standard embodied in the WBWS Standard allows copyright owners to obtain fair compensation for their creative contributions. While no perfect solution exists, the WBWS standard best achieves the most equitable compensation model for all parties involved until the legislature can reconsider the royalty rate structure in the next Copyright Act.