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## COMMENT

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### MUSIC PIRACY AND DIMINISHING REVENUES: HOW COMPULSORY LICENSING FOR INTERACTIVE WEBCASTERS CAN LEAD THE RECORDING INDUSTRY BACK TO PROMINENCE

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## INTRODUCTION

Since the late 1990s, record labels have suffered from consistently decreasing annual revenues as a result of the rampant music piracy characterizing the digital age. The traditional business model that music promoters and distributors have utilized for the past century no longer seems efficient in the age of the Internet. In 1999, overall music sales reached a peak of \$14.6 billion in total revenue.<sup>1</sup> By 2009, that number had fallen to only \$6.3 billion.<sup>2</sup> CD sales in the United States exceeded 785 million albums in 2000; but by 2008, total album sales had decreased by almost a third.<sup>3</sup> The year 2011 proved to be promising for record labels, as total album sales increased by 1.3 %, but the music industry's struggles are likely to continue as album sales dropped 4% in 2012.<sup>4</sup>

Despite the increased connectivity and access to information that digital technology provides us, the Internet has created a world where illegally shared, copied, and distributed music dominates the marketplace. The recording industry, however, continues to fail to adequately address the

<sup>1</sup> Tim Arango, *Digital Sales Exceed CDs at Atlantic*, N.Y. TIMES, Nov. 26, 2008, at B1.

<sup>2</sup> David Goldman, *Music's Lost Decade: Sales Cut in Half*, CNNMONEY (Feb. 3, 2010), [http://money.cnn.com/2010/02/02/news/companies/napster\\_music\\_industry/index.htm](http://money.cnn.com/2010/02/02/news/companies/napster_music_industry/index.htm).

<sup>3</sup> See Michael C. Yeh, Comment, *The Performance Rights Act: A Lack of Impact on a Transitioning Music Industry*, 15 MARQ. INTELL. PROP. L. REV. 217, 218 (2011) (explaining that this decline was mainly due to the proliferation of the Internet).

<sup>4</sup> Christopher Morris, *UMG, Adele Top 2012 Album Sales*, VARIETY (Jan. 4, 2013), <http://www.variety.com/article/VR1118064165/?cmpid=NLCDailyHeadlines> (“Overall album sales—which includes both albums and so-called ‘track equivalent’ digital albums—were off 1.8% compared to 2011. . . . CD sales shrank by 13.5% to 193 million and digital album downloads climbed 14% to almost 117.7 million, a record mark.”).

most significant problem facing the music industry—music piracy—and the resulting widespread harm to most music industry participants today.<sup>5</sup>

Record labels suffer the most devastating effects of music piracy as their profits continue to decline.<sup>6</sup> But decreasing annual revenues have also led to less funding and more one-sided record contracts for aspiring musicians.<sup>7</sup> Additionally, music consumers have been unable to experience and enjoy new and progressive forms of music delivery as Internet-based businesses and webcasters are stifled by rising costs and are forced to operate under a legal structure designed more for the mid-1900s than the 21st century.

Some reports estimate that as much as 95 % of music is downloaded illegally, for free, on a yearly basis.<sup>8</sup> The digital transmission of music, including peer-to-peer (P2P) file sharing services, most of which developed following the creation of the infamous Napster service,<sup>9</sup> allows infringers to create and distribute illegal copies of copyrighted music to the general public in a matter of seconds.<sup>10</sup> Illegal downloading of pirated music

<sup>5</sup> See *Who Music Theft Hurts*, RIAA, <http://www.riaa.com/physicalpiracy.php> (last visited May 6, 2013) (“One credible study by the Institute for Policy Innovation pegs the annual harm at \$12.5 billion dollars in losses to the U.S. economy as well as more than 70,000 lost jobs and \$2 billion in lost wages to American workers.”).

<sup>6</sup> While music piracy affects recording artists and labels throughout the world, this Comment is primarily concerned with the United States recording industry and the measures that can be taken on a domestic level.

<sup>7</sup> See Henry H. Perritt, Jr., *New Business Models for Music*, 18 VILL. SPORTS & ENT. L.J. 63, 83 (2011) (lamenting that labels are pushing their performing artists to accept so-called “360 deals,” which give record companies a share of revenue from endorsements, live performances, and merchandise sales—in addition to their standard share of revenue from record sales—despite the labels’ lack of expertise in these additional areas).

<sup>8</sup> INT’L FED’N OF THE PHONOGRAPHIC INDUS., DIGITAL MUSIC REPORT 2009: NEW BUSINESS MODELS FOR A CHANGING ENVIRONMENT 22 (2009), available at <http://www.ifpi.org/content/library/DMR2009.pdf>; see also Steven Masur, *Collective Rights Licensing for Internet Downloads and Streams: Would It Properly Compensate Rights Holders?*, 18 VILL. SPORTS & ENT. L.J. 39, 43 (2011) (stating that 90% or more of P2P file transfers violate U.S. copyright laws and threaten the viability of companies that depend on copyright protection); *Legal Downloads Swamped by Piracy*, BBC NEWS (Jan. 16, 2009, 6:02 PM), <http://news.bbc.co.uk/2/hi/technology/7832396.stm> (“[M]ore than 40 billion music files were illegally shared in 2008.”). But some commentators have argued that the overall negative effect of music piracy is not as detrimental as the music industry has propounded. See Catherine Rampell, *The Music Industry, Post-Napster*, N.Y. TIMES (Mar. 21, 2011), <http://economix.blogs.nytimes.com/2011/03/21/the-music-industry-post-napster> (citing a new study which claims that “Napster and its file-sharing descendants have not, in fact, reduced the entrance of new artists to the music market, even if piracy has made it harder to make a financial killing in the industry”).

<sup>9</sup> See Jared S. Welsh, Comment, *Pay What You Like—No, Really: Why Copyright Law Should Make Digital Music Free for Noncommercial Uses*, 58 EMORY L.J. 1495, 1514-17 (2009) (providing a detailed history of the rise and fall of Napster).

<sup>10</sup> See Perritt, *supra* note 7, at 75 (“P2P file sharing developed as an underground channel for unlicensed access to recorded music.”); Tyler Hardman, Note, *Webcasting and Interactivity: Problems*

continues to escalate despite the variety of legal downloading sites available today.<sup>11</sup>

In response, the major labels and recording industry executives have consistently clamored for legislative assistance to combat diminishing yearly revenues due to music piracy.<sup>12</sup> However, rather than adapt to new consumer preferences that are focused upon individualized customization and capitalize on the opportunities digital technology can provide, record labels have for the most part chosen to continue fighting to protect their outdated business models.<sup>13</sup> Instead of overhauling their traditional practices to establish modernized approaches that properly respond to new technologies and consumer habits, record labels continue to demand more oppressive royalty rates and higher shares of revenue from less powerful market participants.<sup>14</sup> Most recently, record labels have proposed legislation that primarily benefits their economic interests, without considering the rights or needs of other music industry participants.<sup>15</sup>

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*and Solutions*, 17 B.U. J. SCI. & TECH. L. 290, 291 (2011) (explaining that consumers can now access music “without ever stepping foot in a conventional retail store”).

<sup>11</sup> See Amy Duvall, Note, *Royalty Rate-Setting for Webcasters: A Royal(ty) Mess*, 15 MICH. TELECOMM. & TECH. L. REV. 267, 288 (2008) (identifying iTunes and MP3.com as examples of legal downloading sites).

<sup>12</sup> See Perritt, *supra* note 7, at 76 (explaining that EMI’s worldwide revenue was £2.08 billion in 2006 and fell to £1.75 billion in 2007); see also Yeh, *supra* note 3, at 218 (“Music sales are not creating the same profits as before, and rather than change or adapt, record labels are petitioning the legislature to create new modes of revenue.”).

<sup>13</sup> See Yeh, *supra*, note 3, at 226 (explaining that online social networking sites now provide smaller artists with opportunities for direct interaction with music listeners, which renders the traditional record label model and distribution advantages increasingly obsolete).

<sup>14</sup> See, e.g., Performance Rights Act, H.R. 848, 111th Cong. (2009) (proposing that terrestrial radio stations pay sound recording copyright owners royalties where they have never been required to before). *But see* Brian Day, *In Defense of Copyright: Record Labels, Creativity, and the Future of Music*, 21 SETON HALL J. SPORTS & ENT. L. 61, 74-75 (2011) (explaining that the vast resources and expertise of record labels contribute to performing artists’ success and financial security in numerous ways).

<sup>15</sup> For examples of such proposed legislation, see H.R. 848. These proposals ask Congress to amend the Copyright Act to require traditional terrestrial radio (AM/FM) stations to pay musicians, recording artists, and other sound recording copyright owners for the right to play songs on the air. However, it has been recognized for decades that radio airplay offers recording artists and record labels free marketing; radio station broadcasts successfully peak the interests of music listeners, which “compels them to go out and buy the song or album.” Yeh, *supra* note 3, at 224. For this reason, terrestrial radio stations have until now been exempt from having to pay recording artists and sound recording copyright owners any royalties for the public performance of such works. See also PROTECT IP Act of 2011, S. 968, 112th Cong. § 3 (2011) (providing for “enhancing enforcement against rogue websites operated and registered overseas”). Many of the more recent legislative proposals have been met with opposition and claims that the laws would violate certain fundamental rights and liberties. See Stop Online Piracy Act, H.R. 3261, 112th Cong. (2011) (proposing that Congress expand U.S. copyright law enforcement to combat online

This Comment suggests that Congress should amend the Copyright Act to ensure that promising new music-based technologies are able to survive. The establishment of a compulsory license<sup>16</sup> for interactive webcasters<sup>17</sup> will help ensure that sound recording copyright owners are properly compensated for their recordings and performances, while also guaranteeing that the public will be able to utilize these copyrighted works to their greatest benefit. As a result of the recording industry's failed efforts to combat music piracy over the past two decades, Congress must concern itself with the interests and future viability of the entire music industry. By expanding compulsory licensing to cover both noninteractive and interactive webcasters, the dual purposes<sup>18</sup> of copyright law envisioned in the Constitution<sup>19</sup> can best be achieved.

Through the establishment of compulsory licensing for interactive webcasters, music listeners will be able to consume copyrighted sound recordings in the most beneficial and preferred manner. A greater variety of music, in more easily consumable formats and through more accessible services, will then be made available to the public at affordable rates. Meanwhile, copyright owners will be better compensated as a result of the proliferation of personalized digital music services, and the resulting decrease in music piracy, as consumers recognize the value in the legal streaming of music. Market participants will no longer have to waste valuable resources on high-stakes litigation and lobbying efforts that often harm the reputation and public perception of the music industry. In the

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illegal trafficking in copyrighted intellectual property in ways that opponents claim will violate the First Amendment and cripple the Internet).

<sup>16</sup> Compulsory licensing provides a third party with the right to use copyrighted works without the copyright owner's permission so long as an established royalty fee is paid for such use. Also known as statutory licensing, compulsory licensing is primarily utilized in situations where high transaction costs prevent beneficial negotiations and agreements from taking place. See Andrew D. Stephenson, Comment, Webcaster II: *A Case Study of Business to Business Rate Setting by Formal Rulemaking*, 7 HASTINGS BUS. L.J. 393, 399 (2011) (explaining that transaction costs are lowered for both copyright owners and copyright users by the imposition of a statutory scheme for payment and collection of compulsory license rates).

<sup>17</sup> Webcasting is a means of distributing audio recordings to many simultaneous users using streaming media technology via the Internet. The term is used interchangeably with Internet radio, online broadcasting, and similar phrases throughout this Comment. See *Digital Definitions*, HARRY FOX AGENCY, <http://www.harryfox.com/public/DigitalDefinitions.jsp> (last visited May 6, 2013).

<sup>18</sup> The granting of copyrights is intended both to provide adequate compensation for authors of original works and to promote the progress of the arts for the benefit of the general public. See U.S. CONST. art. I, § 8, cl. 8 (describing the purposes of copyright law).

<sup>19</sup> See *id.*; see also Hardman, *supra* note 10, at 311 ("Protecting 'traditional record sales' . . . must stand in the shadow of the promotion of progress in the development of new technologies and forms of distribution." (footnote omitted)).

process, consumers will recognize the benefits and low costs of interactive webcasting, and the consumer base of these webcasting companies will grow under a more balanced statutory scheme. Copyright owners, webcasters, and consumers will all benefit from an increased demand for legally accessible music and the proliferation of more affordable services that are personalized and individually tailored to consumer preferences.

Part I of this Comment provides a discussion of the severe problems music piracy has generated for the recording industry over the past two decades and the many ways in which the recording industry has failed to combat the piracy epidemic. Part II outlines the advancement of music in the digital age, with a particular focus on the importance of streaming technology in the future. Part III chronicles the history of copyright protection for sound recordings, from the initial structure of the digital performance right to the current tripartite framework of the public performance right in sound recordings. Part IV provides further details of the noninteractive webcasting royalty proceedings, detailing the key shortcomings of the current rate structure and the issues that industry participants have been grappling with for the past two decades. Part V argues that compulsory licensing should be congressionally established for interactive webcasters and outlines the general structure that should be adopted. Lastly, Part VI provides a detailed discussion of the economic benefits an interactive webcasting compulsory license rate will have for the recording industry so long as Congress and the major record labels fully embrace streaming technology and interactive webcasting.

## I. THE MUSIC PIRACY EPIDEMIC

The vast majority of U.S. copyrights in sound recordings are owned by three major record companies.<sup>20</sup> This concentration stems from the common industry practice of sound recording artists assigning their intellectual property interests to these record labels through recording contract agreements. In exchange, the sound recording artists receive distribution services, guaranteed compensation, and other benefits that they might not otherwise

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<sup>20</sup> The three major record labels existing today are Universal Music Group, Sony Music Entertainment, and Warner Music Group. EMI Group, which was previously the fourth largest record label, was purchased by Universal Music Group in September 2012. *See Morris, supra* note 4 (explaining that Universal Music Group continued as the market leader in 2012, with a market share totaling more than 39% after the EMI purchase, and “Sony Music Entertainment captured 30.25% of the album market, [while] Warner Music Group took 19.15%”).

receive.<sup>21</sup> Because most of the profits received from album and song sales accrue to record labels after the assigning of such rights, music piracy primarily diminishes the annual revenues garnered by these large record labels. By diminishing the operating budgets of record labels, however, music piracy also limits the opportunities available to recording artists; consequently, the supply and diversity of music that can be made available to consumers diminishes as well.<sup>22</sup>

#### A. Failed Efforts to Combat Piracy

In the late 1990s and early 2000s, sound recording copyright owners attempted to combat the rise of P2P networks and the proliferation of illegal copying and distribution of digital music files through litigation efforts. The threat of Napster<sup>23</sup> in the late 1990s led to a series of copyright infringement suits against many of the large file sharing services that were created in Napster's wake. Sound recording copyright owners initially experienced great success in high-profile lawsuits during the early 2000s.<sup>24</sup> As a result, many of the largest and most successful P2P networks offering permanent download services were shut down.<sup>25</sup> But over time, young entrepreneurs and software developers recognized the shortcomings of prior centralized P2P services and created new file sharing services that are more streamlined for the user but more problematic for record labels and copyright

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<sup>21</sup> However, with the rise of the Internet and the decreasing costs of production, distribution, and marketing of musical recordings, thousands of artists have chosen to maintain the copyrights in their own sound recordings. See MUSICFIRST, THE RADIO DISTORTION HANDBOOK 11 (2009), available at <http://www.musicfirstcoalition.org/sites/default/files/Radio%20Distortion%20Handbook%201-18%20Final.pdf> (explaining that "many artists are . . . the sound recording copyright owners of their music"); see also Perritt, *supra* note 7, at 184-85 (estimating that the cost of producing an album has decreased drastically to about \$12,500). But see Day, *supra* note 14, at 78 ("Despite the rise in technological innovation, . . . it is estimated that the production cost of a pop-rock album is still over \$200,000 . . .").

<sup>22</sup> See Day, *supra*, note 12, at 100-02 (explaining that decreased profits for record labels due to music piracy will result in less investment in new artists and thus a declining quantity and quality of music available to the public).

<sup>23</sup> See Welsh, *supra* note 9, at 1514-17 (providing a detailed history of the rise and fall of Napster).

<sup>24</sup> See *Metro-Goldwyn-Mayer Studios Inc. v. Grokster, Ltd.*, 545 U.S. 913, 941 (2005) (holding that a distributor of P2P file sharing software was secondarily liable for the copyright infringement of end users under an inducement theory); *A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1021-24 (9th Cir. 2001) (holding that the P2P file sharing service could be held liable for contributory and vicarious infringement of sound recording copyrights).

<sup>25</sup> See, e.g., *GROKSTER*, <http://www.grokster.com> (last visited May 6, 2013) ("The United States Supreme Court unanimously confirmed that using this service to trade copyrighted material is illegal."); *LIMEWIRE*, <http://www.limewire.com> (last visited May 6, 2013) ("LimeWire is under a court order . . . to stop distributing the LimeWire software.").

owners.<sup>26</sup> It soon became apparent to sound recording copyright owners that obtaining a verdict against such companies for secondary copyright infringement was now much more uncertain and costly than ever before.<sup>27</sup>

As a result, record labels and other copyright owners used individual lawsuits to enforce their rights against the actual illegal downloaders and end users of these P2P services. The Recording Industry Association of America (RIAA), on behalf of sound recording copyright owners, sued more than 30,000 individuals who had illegally downloaded music over the Internet.<sup>28</sup> However, while many of these cases resulted in favorable verdicts for the record labels,<sup>29</sup> the labels abandoned this litigation strategy because of the high costs, the lack of a significant deterrent effect on the general public, and the judgment-proof status of many of the named defendants.<sup>30</sup>

Not only did these individual lawsuits fail to stem the tide of music piracy,<sup>31</sup> but also consumers rebelled and criticized the record labels for being greedy and unjust.<sup>32</sup> In response, while some consumers turned to alternative legal forms of music distribution, many were incentivized to further engage in acts of music piracy in defiance of the RIAA lawsuits.<sup>33</sup> Consequently, the RIAA ceased filing these suits against individuals.<sup>34</sup>

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<sup>26</sup> See, e.g., THE PIRATE BAY, <http://www.piratebay.se> (last visited May 6, 2013) (exemplifying new, more problematic sites). *The Pirate Bay* is a Swedish website that allows users to share electronic files through magnet links and .torrent files.

<sup>27</sup> See Welsh, *supra* note 9, at 1518-20 (discussing how and why the music industry transitioned from suing file sharing services to bringing claims against individual infringing end users).

<sup>28</sup> See Masur, *supra* note 8, at 44 (explaining that this legal strategy ultimately failed).

<sup>29</sup> See *Capital Records, Inc. v. Thomas-Rasset*, 799 F. Supp. 2d 999, 1012 (D. Minn. 2011) (reducing a previous \$1.5 million jury award to \$2250 per song downloaded), *vacated*, 692 F.3d 899 (8th Cir. 2012); *Sony BMG Music Entm't v. Tenenbaum*, No. 07cv11446-NG, 2009 WL 4723397, at \*2 (D. Mass. Dec. 7, 2009) (ordering the payment of \$675,000, which was later reduced to \$67,500 on due process grounds); see also Jon Healey et al., *Song Swappers Face the Music*, L.A. TIMES, Sept. 9, 2003, at A1 (discussing the first wave of 261 lawsuits filed against individual infringers).

<sup>30</sup> See Welsh, *supra* note 9, at 1519-20 (explaining that the backlash that resulted against the RIAA and copyright owners proved more costly than any benefits that could be obtained from these individual suits).

<sup>31</sup> For most consumers, the benefits of obtaining free music continued to outweigh the costs associated with the very low risk of being named a defendant in a copyright infringement suit.

<sup>32</sup> See David J. Moser, *File Sharing FAQ*, COPYRIGHT GURU (2007), [http://www.copyrightguru.com/file\\_sharing\\_faq.htm](http://www.copyrightguru.com/file_sharing_faq.htm) (explaining that "estimates indicate that the overall amount of file-sharing has not decreased and may have increased").

<sup>33</sup> See Masur, *supra* note 8, at 44 ("[P]ursuing infringers ha[s] led to a backlash and consumer criticism, while still not making a significant dent in the amount of piracy."). Why the current generation of music consumers does not view online music piracy as an immoral act, on par with the theft of physical chattels, is a question outside the realm of this Comment.

<sup>34</sup> See Sarah McBride & Ethan Smith, *Music Industry to Abandon Mass Suits*, WALL ST. J., Dec. 19, 2008, at B1 (explaining that the RIAA decided to pursue alternative enforcement strategies).



Nevertheless, the RIAA and record labels have continued to seek effective ways of curbing illegal file sharing. Record labels have begun to cooperate with Internet Service Providers (ISPs) in terminating the Internet accounts of individuals engaging in significant illegal file sharing.<sup>35</sup> Copyright owners have also attempted to protect their intellectual property interests through the use of digital rights management (DRM) and anti-circumvention measures.<sup>36</sup> The goal of both of these approaches was to rely upon the quasi-copyright protections established by the Digital Millennium Copyright Act of 1998 (DMCA) to ensure that sound recordings are properly protected from illegal use, copying, and distribution.<sup>37</sup>

For the most part, however, record labels and music publishers have abandoned these approaches. Not only could many of the technologies protecting digital files easily be circumvented, but also consumers began to refuse to pay for the higher costs associated with such protections and technologies.<sup>38</sup> Because companies were passing their costs on to end users for technologies that only benefited copyright owners, consumers responded by demanding DRM-free media.<sup>39</sup> Most damagingly, passionate consumers began to feel that they were morally permitted to illegally circumvent such protections and distribute DRM-free files to other users.<sup>40</sup>

#### B. *New and Innovative Ways to Combat Piracy*

Not all efforts to combat music piracy have failed. Industry participants can still obtain adequate compensation for the creation of musical works and sound recordings.<sup>41</sup> Recent innovative efforts by successful and popular

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<sup>35</sup> See Gary Myers & George Howard, *The Future of Music: Reconfiguring Public Performance Rights*, 17 J. INTEL. PROP. L. 207, 221-22 (2010) (detailing the many ways record labels and copyright owners have attempted to address and combat music piracy).

<sup>36</sup> See Welsh, *supra* note 9, at 1520 (discussing how these attempts to prevent copying of digital files ultimately failed).

<sup>37</sup> See generally 17 U.S.C. §§ 1201-02 (2006).

<sup>38</sup> See Welsh, *supra* note 9, at 1520 (explaining why the recording industry moved away from using DRM).

<sup>39</sup> See *id.* (calling DRM “virtually unworkable in practice”).

<sup>40</sup> See *Digital Rights Management: A Failure in the Developed World, a Danger to the Developing World*, ELECTRONIC FRONTIER FOUNDATION (Mar. 23, 2005), <https://www.eff.org/wp/digital-rights-management-failure-developed-world-danger-developing-world> (explaining that DRM technology “has been in wide deployment for a decade with no benefit to artists and with substantial cost to the public and to due process, free speech and other civil society fundamentals”).

<sup>41</sup> See Perritt, *supra* note 7, at 136-37 (explaining that the demand function for individual songs or albums of an artist depends upon price, quality, transaction costs of obtaining the music, identification and altruistic feelings toward the copyright owner, popularity, convenience of being

performance artists serve as an example of how embracing new forms of technology and recognizing changing consumer preferences can be an effective way to combat the music piracy epidemic.

Most notably, in an attempt to effectively use new distribution technologies, Radiohead, a band who retained the copyrights in their sound recordings instead of assigning them to a record label, chose to release their seventh album as a digital download through their website.<sup>42</sup> The album was offered free of charge, but the band invited fans to pay whatever they desired for the download.<sup>43</sup> The band utilized positive public relations and clever marketing to tailor the distribution of their music to consumer preferences and new forms of social media.<sup>44</sup>

While this form of distribution may not be possible for smaller bands lacking the large fan base and vast resources of Radiohead, record labels and artists should take notice. As technology further advances and the world becomes more connected through the Internet, such new and innovative ways of distributing music and providing consumers with more affordable options will become dominant.<sup>45</sup> After all, Radiohead not only enjoyed extensive positive publicity from this distribution choice, but also garnered payments from consumers that ranged up to \$212, received payment from two out of five downloaders, and overall averaged about \$2.26 per album download, which is more than they would have received under a standard recording contract.<sup>46</sup>

This Comment does not intend to suggest that the recording industry is behaving in an unmerited or illogical manner by attempting to protect its intellectual property. The music industry has faced an almost impossible task in recent years as illegal file sharing has become more convenient, cheaper, and seemingly morally acceptable. However, thousands of smaller artists have recognized the changing landscape of music and the new forms

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able to listen to the music, probability of obtaining corrupted files, and probability of facing a lawsuit).

<sup>42</sup> See Mark Binelli, *The Future According to Radiohead*, ROLLING STONE, Feb. 7, 2008, at 55 (detailing the unique approach to selling albums taken by the band).

<sup>43</sup> See *id.*

<sup>44</sup> See Greg Kot, *Radiohead's 'In Rainbows' Experiment Pays Off with 3 Million Sales*, CHI. TRIB. (Oct. 20, 2008), [http://leisureblogs.chicagotribune.com/turn\\_it\\_up/2008/10/radioheads-in-r.html](http://leisureblogs.chicagotribune.com/turn_it_up/2008/10/radioheads-in-r.html) (explaining that as a result of this promotional campaign, Radiohead's album topped the Billboard charts in early 2008 and achieved physical and digital sales of about three million albums combined).

<sup>45</sup> See Perritt, *supra* note 7, at 171-72 (noting that Nine Inch Nails, Beastie Boys, and David Byrne of Talking Heads all recently made certain songs available through a Creative Commons noncommercial attribution license that permits free use of the recordings, contingent upon any derivative works being made available under the same terms and conditions).

<sup>46</sup> Binelli, *supra* note 42, at 55.

of distribution that are available in the twenty-first century. Individual artists and bands are beginning to capitalize on unique opportunities to engage with consumers and music listeners in ways that promote positive publicity. Record labels should follow suit and recognize that by embracing new technologies and tailoring their marketing and distribution efforts to align with new consumer preferences, annual revenues can begin to rise again as music piracy is more effectively contained. Furthermore, record labels and copyright owners should recognize the benefits that streaming technology can provide the entire industry.

## II. THE MODERNIZATION OF MUSIC

For the past few decades, the distribution of music has drastically shifted from the traditional record label model that is dependent upon the sale of physical records, CDs, and albums to the transmission and delivery of digital music files and individual songs.<sup>47</sup> In fact, it is estimated that by 2020, Internet radio will almost equal weekly listenership of terrestrial radio stations.<sup>48</sup>

In 2012, digital album sales accounted for more than one in three albums, enjoying a 20% increase from 2010 to 2011, achieving a 14% increase from 2011 to 2012, and reaching a record 117.7 million consumer purchases.<sup>49</sup> Digital sales as a whole, which include not only album sales, but also individual song purchases and music videos, hit an all-time high of 1.66 billion in 2012, 3.1% higher than in 2011.<sup>50</sup> Internet webcasters now garner an audience of consumers that is estimated to exceed 100 million per month.<sup>51</sup>

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<sup>47</sup> See Charles Sykes, *Album Sales Are Looking Up*, USA TODAY, Jan. 5, 2012, at D3 (documenting how digital sales rose to 50.3% of all music sales, eclipsing physical sales for the first time); see also Myers & Howard, *supra* note 35, at 213-14 (arguing that there is the potential to increase the income of music industry participants by modernizing the royalty rate scheme and focusing on new revenue streams).

<sup>48</sup> See Brian Day, Note, *The Super Brawl: The History and Future of the Sound Recording Performance Right*, 16 MICH. TELECOMM. & TECH L. REV. 179, 200 (2009) (discussing industry projections and the role of Internet radio in the future).

<sup>49</sup> See Morris, *supra* note 4 (reporting changes in album sales).

<sup>50</sup> See Agence France-Presse, *Digital Music Commerce Hits New High in 2013 at 1.66 Billion Sales*, THE RAW STORY (Jan. 4, 2013), <http://www.rawstory.com/rs/2013/01/04/digital-music-commerce-hits-new-high-in-2013-at-1-66-billion-sales> (noting the growth of digital music sales).

<sup>51</sup> See Paul Resnikoff, *More Than 100 Million Americans Now Listen to Online Radio . . .*, DIGITAL MUSIC NEWS (Apr. 10, 2012), <http://www.digitalmusicnews.com/permalink/2012/120410radio> ("According to just-released survey data from Edison Research and Arbitron, 103 million Americans are now accessing online radio in some form, in any month." (emphasis omitted)). The rise of mobile technology and services has also provided a "tremendous growth opportunity for radio," as "45% of Internet radio users are listening on a mobile device—with 84% of them listening [up] to 1-3 hours per day." *Report: Internet Radio Ad Revenue Up 21%*, NET-

This growth has resulted in expansive opportunities for effective advertising as digital music webcasting grows in popularity.<sup>52</sup>

Meanwhile, in 2011, physical album sales fell 5% to 228 million,<sup>53</sup> and sales shrank an even greater percentage in 2012, dropping to 193 million.<sup>54</sup> Sales of CDs have declined each year for the past six years, with an overall net reduction of more than 60% compared to the peak years of the late 1990s.<sup>55</sup> Consumers are increasingly turning to online distribution services like iTunes<sup>56</sup> that allow them to purchase music in the form of individual digital songs. Thus, while the creation and advancement of streaming technology has contributed immensely to this drastic decrease in physical album sales over the past two decades,<sup>57</sup> the rise of digital album and song sales provides hope for the industry in the future.

### A. *The Rise of Streaming Technology*

In 1994, terrestrial radio stations began streaming content over the Internet.<sup>58</sup> Streaming is a unique form of digital technology where a user's computer receives "time- and location-sensitive streams" that are reassembled

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NEWSCHECK (Sept. 19, 2011), <http://www.netnewscheck.com/article/14074/report-internet-radio-ad-revenue-up-21>; see also Stephenson, *supra* note 16, at 397 (discussing the profitability of the modern music industry and commercial webcasting services).

<sup>52</sup> See Stephenson, *supra* note 16, at 397 (explaining that Internet radio broadcasters enjoyed \$500 million in advertising revenue in 2006); Ben Sisario, *Pandora and Spotify Rake in the Money and Then Send It Off in Royalties*, N.Y. TIMES (Aug. 24, 2012), <http://mediadecoder.blogs.nytimes.com/2012/08/24/pandora-and-spotify-rake-in-the-money-and-then-send-it-off-in-royalties> (noting that Pandora, which makes the majority of its revenue from advertisements, reported total revenue of \$81 million in the second quarter of 2012 alone).

<sup>53</sup> See Morris, *supra* note 4; see also Perritt, *supra* note 7, at 89-90 (providing detailed statistics of decreasing CD sales over the past decade).

<sup>54</sup> See Morris, *supra* note 4.

<sup>55</sup> Perritt, *supra* note 7, at 89-90.

<sup>56</sup> See generally ITUNES, <http://www.itunes.com> (last visited May 6, 2013). iTunes was created by Apple in 2001 and today is the largest music retailer in the United States. In the face of diminishing profits for record labels and the widespread piracy that is threatening to destroy the music industry, iTunes has been called "a beacon of hope" and has been credited with saving the music industry. See Jesse A. Bland, Note, *Biting the Hand That Feeds: Why the Attempt to Impose Additional Performance Fees on iTunes Is a Search for Dollars Without Sense*, 2 HARV. J. SPORTS & ENT. L. 157, 162-63 (2011) (attributing the expansive growth of digital music sales to iTunes).

<sup>57</sup> Streaming technology allows real-time playing of a song while a constant link is maintained between the server and end user. Most notably, streaming media does not allow a permanent copy of the file to be downloaded to the user's computer, and a song can only be heard again by connecting to the Internet and streaming the file again. See Bland, *supra* note 56, at 163-64 (distinguishing between permanent downloads and streaming media).

<sup>58</sup> See Hardman, *supra* note 10, at 303 (noting that these transmissions were initially of very poor quality).

using a specific program designed for different types of media.<sup>59</sup> Known as a “player,” this program collects and reconstructs a song in a “buffer,” which is a form of temporary RAM storage.<sup>60</sup> When a sufficient number of streams have been collected, providing the user with the initial seconds or minutes of a song, the song can be played even while the computer continues to receive additional streams to acquire the entire song in the temporary RAM storage.<sup>61</sup> However, unlike permanent downloads, which are saved to the user’s computer and can be quickly played again, “once [a] song is finished playing, the buffer is emptied,” and a copy is not retained on the user’s computer.<sup>62</sup>

The creation of software allowing for the compression of digital files while maintaining outstanding sound quality began the rapid proliferation of Internet streaming and webcasting.<sup>63</sup> As webcasting grew in popularity and the Internet became faster and more accessible, consumer preferences shifted, and music listeners demanded a greater variety of Internet radio services and increased customizability.<sup>64</sup> Today, online music services such as Pandora<sup>65</sup> provide consumers with the ability to listen to millions of songs for free.<sup>66</sup> These types of “noninteractive” webcasters allow users to create and manage personalized music stations that center around specified genres, bands, or even songs.

Another subset of webcasters provides consumers with “on-demand,” or fully customizable services, where users can select individual and specific

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<sup>59</sup> See Duvall, *supra* note 11, at 268 (detailing the process by which streaming technology operates in terms of sound recordings).

<sup>60</sup> *Id.* at 268-69.

<sup>61</sup> *Id.* Video content, as well as audio content, can be distributed through streaming technology.

<sup>62</sup> See *id.* at 269 (explaining the key difference between downloaded music files and streams).

<sup>63</sup> See Perritt, *supra* note 7, at 93-94 (“Digital recording technologies make it possible to produce perfect copies of recorded music cheaply and quickly. Compression algorithms embedded in software known as ‘codecs’ produce relatively small files that can be distributed in a few seconds via the Internet.”); see also Bland, *supra* note 56, at 175 (discussing how the first technology for streaming audio—RealAudio—was developed and released).

<sup>64</sup> See Hardman, *supra* note 10, at 303 (discussing the evolution of the Internet radio industry).

<sup>65</sup> See generally PANDORA RADIO, <http://www.pandora.com> (last visited May 6, 2013). Pandora is a free, ad-supported service allowing music listeners to create semi-customized music channels. It is also available for smartphones and other mobile devices, and additional content is available for a low monthly subscription fee.

<sup>66</sup> See Mary Ann Lane, *‘Interactive Services’ and the Future of Internet Radio Broadcasts*, 62 ALA. L. REV. 459, 459 (2011) (explaining that various webcasters provide consumers with instant access to “free” music); see also Perritt, *supra* note 7, at 71 (“Printed scores, broadcast radio, recording technologies, and audio amplification all changed the way music was made, distributed and consumed[,] . . . like the more recent proliferation of small computers linked to the Internet . . .”).

songs to be played at any time.<sup>67</sup> Under the current copyright regime, such “interactive” services are more costly to administer due to the higher royalty rates that must be negotiated directly with copyright owners.<sup>68</sup> As a result, many interactive webcasters have chosen not only to bring in revenue through advertising, but also to charge consumers subscription fees for access to, and use of, their multimillion-song databases.<sup>69</sup>

Nevertheless, whether music is offered to the public free of charge or for a low monthly fee, it has never been easier or more affordable for consumers to hear the music that they want to hear, when they want to hear it.<sup>70</sup> With the advent of iPods,<sup>71</sup> smart phones,<sup>72</sup> wireless internet,<sup>73</sup> 3G networks,<sup>74</sup> and cloud computing,<sup>75</sup> consumers can enjoy music almost anywhere and at any time.<sup>76</sup> As Internet access becomes more widespread and versatile, music consumers using services such as Pandora, Spotify,<sup>77</sup> or Grooveshark<sup>78</sup> “will

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<sup>67</sup> See Kevin Purdy, *Battle of the Streaming Music Services*, LIFEHACKER (Aug. 10, 2010), <http://lifehacker.com/5608715/battle-of-the-streaming-music-services> (comparing many of the most popular on-demand streaming music services).

<sup>68</sup> See generally 17 U.S.C. § 114 (2006) (outlining the tripartite structure of the digital public performance right).

<sup>69</sup> See RHAPSODY, <http://www.rhapsody.com> (last visited May 6, 2013) (“[A]ll the music [you want] all day everyday for \$10 a month.”); see also Matthew Johnson, *Understanding Royalty-Bearing Companies #2: Rhapsody*, SONGTRUST (Feb. 24, 2011), <http://blog.songtrust.com/industry-profiles/understanding-royalty-bearing-companies-2-rhapsody> (explaining the general structure and royalty payment scheme of Rhapsody).

<sup>70</sup> See Welsh, *supra* note 9, at 1525-26 (explaining that, despite the decreasing annual profits experienced by the music industry over the past decade, the rise of digital technology and distribution has increased demand from consumers).

<sup>71</sup> See Perritt, *supra* note 7, at 65 (explaining that the “iPod permit[s] consumers to listen to music all the time and this enormously increases the potential demand for music”).

<sup>72</sup> See Hardman, *supra* note 10, at 311 (explaining that smart phones enable a large percentage of the population to listen to music via webcasting, even where wireless networks are not available).

<sup>73</sup> See Day, *supra* note 14, at 102 (explaining that the government is urging Internet providers to drastically increase Internet speeds and access for American consumers by 2020).

<sup>74</sup> See Hardman, *supra* note 10, at 311 (noting that “3G networks are expanding every day, and still faster networks are currently in their beginning stages of development”).

<sup>75</sup> See Whitson Gordon, *Cloud Music Comparison: What’s the Best Service for Streaming Your Library Everywhere?*, LIFEHACKER (June 15, 2011), <http://lifehacker.com/5812138/cloud-music-comparison-whats-the-best-service-for-streaming-your-library-everywhere> (explaining that “a number of cloud music services allow you to stream your music to nearly everything—laptops, tablets, smartphones—with minimal effort or tech know-how”).

<sup>76</sup> See Welsh, *supra* note 9, at 1512-13 (explaining that the massive decrease in revenue for record labels is a result of the increasing amount of data that can be stored on computer hard drives and portable music players, such as the iPod, the dramatic increase in Internet speeds over the past decade, and the introduction of the MP3 file format that has greatly compressed digital files).

<sup>77</sup> See SPOTIFY, <http://www.spotify.com> (last visited May 6, 2013). Spotify is a Swedish streaming music service that allows users to search for music within a library of over 15 million

have little or no need to keep digital copies of the songs they want to hear.”<sup>79</sup>

### B. *The Current Potential of Streaming Services*

Consumers have recognized that streaming technology provides significant savings in cost and convenience when compared to traditional ownership of CDs or records.<sup>80</sup> As a result, executives of entertainment companies in various industries are beginning to place an increasing emphasis on streaming technology.<sup>81</sup>

As of 2008, nearly half of all Americans had listened to music on the Internet, with about one in every eight Americans listening to music online regularly.<sup>82</sup> In just four years, that number has grown to over 100 million people—about one in every three Americans—accessing online radio in some form each month.<sup>83</sup> The proliferation of webcasting services and their increased use by consumers can be attributed to the fact that digital transmission services do not suffer from the same geographical limitations that other forms of delivery must contend with.<sup>84</sup> There is seemingly no limit to

songs. Visual and audio advertising support the free version of Spotify, while a paid premium subscription allows higher bitrate streams and offline access to the service.

<sup>78</sup> See GROOVESHARK, <http://www.grooveshark.com> (last visited May 6, 2013). Grooveshark serves as an example of an almost pure “on-demand” service. Consumers themselves upload copies of songs from their own computers, allowing other users to search for and listen to specific songs, albums, or artists. Copyrighted sound recordings can be listened to repeatedly as long as a user is connected to the service. However, the company does not provide consumers with the ability to download or copy files from other computers in permanent form on their own computers. Users can only listen to songs by accessing the Internet.

<sup>79</sup> Hardman, *supra* note 10, at 304.

<sup>80</sup> See, e.g., *Netflix Users Stream More Than 2 Billion Hours*, WALL ST. J., Jan. 5, 2012, at B9 (explaining that Netflix has experienced greater success as it shifts more towards streaming content).

<sup>81</sup> See Christina Warren, *5 of the Best Streaming Media Services Compared*, MASHABLE (Feb. 14, 2011), <http://mashable.com/2011/02/14/streaming-media-comparison> (reviewing five different streaming media providers in the music, television, and motion picture industries).

<sup>82</sup> The percentage of teenage Americans and young adults who listen to music regularly online is most likely much higher due to their more pronounced acceptance and use of twenty-first century technologies. See Glenn Peoples, *Business Matters: Teens Listen to Music Most on YouTube, Pay for Music More Than Other Age Groups, Nielsen Study Says*, BILLBOARD (Aug. 14, 2012), <http://www.billboard.com/biz/articles/news/1084161/business-matters-teens-listen-to-music-most-on-youtube-pay-for-music-more> (“Teens are obviously more digitally adept than other age groups . . .”).

<sup>83</sup> See Resnikoff, *supra* note 51 (evaluating the usage of online radio).

<sup>84</sup> For a more detailed discussion of the various ways that webcasting improves the digital distribution of music in today’s world, see Kaitlin M. Pals, Note, *Facing the Music: Webcasting, Interactivity, and a Sensible Statutory Royalty Scheme for Sound Recording Transmissions*, 36 J. CORP. L. 677, 692 (2011).

the number of webcasts or level of customization that consumers can enjoy. Thus, if properly harnessed, webcasting can result in the promotion of a greater variety and quantity of music.

Furthermore, online services are now able to utilize technology that exposes consumers to additional music that they will potentially enjoy, based upon their demonstrated musical preferences.<sup>85</sup> Webcasting provides a unique way for the music industry to ensure customer satisfaction by allowing listeners to hear full songs before purchasing copyrighted works. In fact, many studies have shown that regular online music listeners are the most likely demographic to purchase physical CDs or digital albums, buying the works of artists that they hear for the first time on Internet radio stations or webcasting services.<sup>86</sup>

The music industry should recognize the benefits that webcasting can provide and adopt a new business model that fully embraces the evolution of technology and the preferences consumers display for interactive streaming services.<sup>87</sup> The history of sound recording copyright protection and public performance rights must be understood properly before innovative streaming technologies can be harnessed to combat music piracy and raise industry revenues. Only then can the congressional mistakes of the past be heeded and the survival and future growth of the recording industry be ensured.

### III. THE HISTORY OF THE SOUND RECORDING PUBLIC PERFORMANCE RIGHT

The Copyright Clause of the Constitution grants Congress the right to “promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.”<sup>88</sup> Though copyright protection is not granted exclusively to incentivize the production of unique and creative works for the benefit of society, many of the amendments and changes Congress has enacted in the Copyright Act since 1790 focused on the economic incentives

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<sup>85</sup> See *id.* at 692 n.136 (discussing the use of algorithms to match content to consumer preferences).

<sup>86</sup> See *id.* at 692-93 (citing various studies that display the positive effects that Internet radio has on CD sales).

<sup>87</sup> See Welsh, *supra* note 9, at 1522 (explaining that “new technologies have actually helped to increase the demand for recorded music by making its consumption more convenient and reducing search costs[,] . . . [yet] the industry continues to lose profits. . . . protecting its entrenched capital [and] defending its outdated methods in court rather than updating them”); see also Duvall, *supra* note 11, at 289 (“Just as the entertainment industry has been forced to adapt due to technological changes, so too should the music industry adjust to webcasting.”).

<sup>88</sup> U.S. CONST. art. I, § 8, cl. 8.



copyright protection can provide.<sup>89</sup> By properly incentivizing creators, Congress seeks to ensure that copyrighted material continues to be produced and made available to the public so that individuals can receive maximum benefit from their use.<sup>90</sup>

In 1897, Congress extended copyright protection to written musical compositions in order to ensure that proper compensation would continue to incentivize the production of such beneficial works for society.<sup>91</sup> The Copyright Act of 1909 granted authors certain property rights in their musical creations: the exclusive rights to reproduce, distribute, create derivative works, publicly perform, and publicly display these types of works.<sup>92</sup>

A recorded piece of music is comprised of two distinct copyrightable elements: the underlying musical work and the sound recording of that musical work.<sup>93</sup> The songwriter or composer of a song obtains copyright protection in the musical work, which consists of the lyrics and melody that is fixed in some tangible form.<sup>94</sup> This is the form of copyright that has been recognized since the Copyright Act of 1909. Conversely, sound recording copyrights are usually owned by the artist or record label and are distinct from the underlying musical work.<sup>95</sup> A sound recording is the actual performed version of a song, fixed in a tangible medium of expression, such as a compact disc, album, or digital file.<sup>96</sup>

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<sup>89</sup> See H.R. REP. NO. 60-2222, at 7 (1909) (explaining that the purpose of the passage of certain portions of the Copyright Act of 1909 was to ensure that “the composer [received] an adequate return for all use made of his composition”).

<sup>90</sup> See Pals, *supra* note 84, at 678 (explaining how Congress has struggled to balance the interests of creators and the public as technology has changed).

<sup>91</sup> See 17 U.S.C. § 102(a)(2) (2009).

<sup>92</sup> See *id.* § 106.

<sup>93</sup> See *id.* § 102(a)(2), (7).

<sup>94</sup> Though musical works are closely related to sound recordings, a detailed discussion of the copyright protections provided to songwriters and composers is outside the realm of this Comment. For more information, see DONALD S. PASSMAN, *ALL YOU NEED TO KNOW ABOUT THE MUSIC BUSINESS* 206-08 (6th ed. 2006) (explaining the common arrangements songwriters enter into with publishers).

<sup>95</sup> See AL KOHN & BOB KOHN, *KOHN ON MUSIC LICENSING* 1312-14 (3d ed. 2002) (explaining the distinct divide between musical work and sound recording copyrights in the performance and reproduction contexts). This division is not particularly helpful to consumers. See Duvall, *supra* note 11, at 271 (“This initial division of the two rights appears inefficient and influenced much more by the actual copyright holders than the copyright users.”).

<sup>96</sup> See Yeh, *supra* note 3, at 222 (explaining in further detail the difference between musical works and sound recordings).

### A. *Early History of Sound Recording Rights*

Congress did not amend the Copyright Act to recognize limited copyright protection for sound recordings of musical compositions until 1971.<sup>97</sup> For the first time, artists and record labels could license their works and receive compensation for the production of musical sound recordings.<sup>98</sup> The primary purpose of the Sound Recordings Act of 1971 (SRA), which was subsequently retained in the Copyright Act of 1976, was to ensure that unauthorized reproductions and distributions of sound recordings would be made illegal under federal law.<sup>99</sup>

Due to opposition from broadcasters and music publishers, however, the SRA and Copyright Act of 1976 did not recognize an exclusive right in the public performance of sound recordings.<sup>100</sup> The right was limited to only the distribution and reproduction of such sound recordings.<sup>101</sup> Thus, only composers and music publishers were given the right to receive royalties from public performances through a compulsory license established by Congress, while owners of the sound recordings did not receive any compensation for the public performance of their works.<sup>102</sup>

### B. *Digital Performance Right in Sound Recordings Act*

As the Internet became a central part of life, and the creation of streaming technology in the early 1990s provided music pirates with a new means of engaging in illegal reproduction and distribution, the recording industry recognized that the traditional music licensing structure did not adequately

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<sup>97</sup> See Sound Recording Act of 1971, Pub. L. No. 92-140, 85 Stat. 391 (1971) (establishing the right “[t]o reproduce and distribute to the public . . . sound recording[s]”).

<sup>98</sup> See M. WILLIAM KRASILOVSKY ET AL., THIS BUSINESS OF MUSIC: THE DEFINITIVE GUIDE TO THE MUSIC INDUSTRY 63-64 (Robert Nirkind et al. eds., 10th ed. 2007) (discussing the early history of federal copyright protection for sound recordings).

<sup>99</sup> See Lane, *supra* note 66, at 461 (explaining that piracy was the primary concern behind the SRA).

<sup>100</sup> See 17 U.S.C. § 114(a) (1976); see also *Performance Royalty: Hearings on S. 1111 Before the Subcomm. on Patents, Trademarks, and Copyrights of the S. Comm. on the Judiciary*, 94th Cong. 1-4 (1975) (statement of Sen. Hugh Scott, Member, S. Comm. on the Judiciary) (identifying the broadcasting industry’s opposition to performance royalty payments).

<sup>101</sup> See KOHN & KOHN, *supra* note 95, at 1296 (“Conspicuously absent from the list of works [in the Copyright Act] in which a copyright owner may exercise the exclusive right of public performance is the *sound recording*”).

<sup>102</sup> See Lane, *supra* note 66, at 462 (explaining that such public performance rights were omitted purposefully for sound recordings).

compensate or protect copyright owners of sound recordings.<sup>103</sup> The industry as a whole feared that online music piracy could have devastating effects on yearly revenues and profits for companies and artists offering musical works and sound recordings to consumers.<sup>104</sup>

The four major record companies at the time, along with other influential industry participants, adamantly urged Congress to address the threat that satellite and digital technologies posed to sound recording copyright owners due to the lack of a public performance right under the Copyright Act.<sup>105</sup> As a result, in 1995, Congress finally enacted the Digital Performance Right in Sound Recordings Act (DPRSRA), which granted copyright owners in sound recordings the exclusive right to “perform the copyrighted work publicly by means of a digital audio transmission.”<sup>106</sup>

By creating a new digital public performance right for sound recordings and broadening the compulsory license structure to address the proliferation of webcasting and online music downloading, the DPRSRA recognized and attempted to respond to the perceived threat that the Internet presented to the music industry.<sup>107</sup> The DPRSRA first established that all transmissions and broadcasts are public performances under the Copyright Act and then granted the copyright owner of a sound recording the exclusive right to perform the copyrighted work publicly by means of a digital-audio transmission.<sup>108</sup> Of particular importance to this Comment, the DPRSRA’s main structure distinguished between interactive and noninteractive services.<sup>109</sup>

The DPRSRA initially created three distinct categories to reflect the fact that certain types of musical services present copyright owners with more serious concerns and potential problems related to the protection of their exclusive bundle of property rights than other music services do.<sup>110</sup>

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<sup>103</sup> See Lane, *supra* note 66, at 462 (discussing the arguments made before Congress by various record labels in favor of amending copyright law protections); Day, *supra* note 48, at 184 (same).

<sup>104</sup> See S. REP. NO. 104-128, at 13 (1995) (“[T]he Committee has sought to address the concerns of record producers and performers regarding the effects that new digital technology and distribution systems might have on their core business . . .”).

<sup>105</sup> See *id.* at 11-12 (explaining that these new technologies threatened the viability of the record industry).

<sup>106</sup> Digital Performance Right in Sound Recordings Act of 1995, Pub L. No. 104-39, 109 Stat. 336 (1995) (codified as amended at 17 U.S.C. § 106(6) (2009)).

<sup>107</sup> See KOHN & KOHN, *supra* note 95, at 1295-96 (discussing the DPRSRA as a response to concerns that previous copyright laws could not be enforceable in a digital world).

<sup>108</sup> See 17 U.S.C. § 106(6) (2009); Digital Performance Right in Sound Recordings Act of 1995, § 3, 109 Stat. at 343-44.

<sup>109</sup> See *id.* (defining an “interactive service”).

<sup>110</sup> See H.R. REP. NO. 104-274, at 13 (1995) (explaining the reasoning behind the establishment of a tripartite system).

The first category focused on digital audio transmissions offered by interactive services. This category required authorization from and payment to the copyright owner for each sound recording offered to consumers.<sup>111</sup> The DPRSRA defined an “interactive service” as “one that enables a member of the public to receive, on request, a transmission of a particular sound recording chosen by or on behalf of the recipient.”<sup>112</sup> Congress and the music industry recognized, and continue to believe, that these interactive services present the greatest threat to music sales and yearly revenues.<sup>113</sup>

The second category subjected noninteractive, subscription-based services to a compulsory license.<sup>114</sup> At the time, Congress believed that subscription fees would primarily support Internet radio stations, and thus the compulsory license fee would result in extra revenue for the music industry.<sup>115</sup> However, in practice, online radio stations recognized the lucrative opportunities presented by Internet advertising and chose to offer services that were both noninteractive and nonsubscription-based and thus fall outside of the category subject to a compulsory license.<sup>116</sup>

Therefore, most services chose to structure their business models to fall within the third category of the DPRSRA. This category included services that were both noninteractive and nonsubscription. These services were exempted from paying the sound recording copyright owner for the use of the sound recording under the DPRSRA.<sup>117</sup> As a result, sound recording copyright owners were not compensated when their works were publicly performed on traditional radio broadcasts or on the majority of Internet radio stations existing at the time.

### C. DMCA Amendments

Three years later, Congress recognized its failure to properly address the dangers that Internet radio and webcasting presented to the music industry.<sup>118</sup> As a result, Congress more effectively addressed the concerns raised

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<sup>111</sup> See generally Digital Performance Right in Sound Recordings Act of 1995.

<sup>112</sup> *Id.* § 3, 109 Stat. at 343.

<sup>113</sup> See H.R. REP. NO. 104-274, at 14 (“Of all the new forms of digital transmission services, interactive services . . . pose the greatest threat to the livelihoods of those whose income depends upon revenues derived from traditional record sales.”).

<sup>114</sup> See § 3, 109 Stat. at 338.

<sup>115</sup> See KOHN & KOHN, *supra* note 95, at 1299-1300 (explaining that this belief was the “major blunder” of the DPRSRA).

<sup>116</sup> See H.R. REP. NO. 104-274, at 13-15 (explaining that nonsubscription broadcasts are exempt from the public performance right).

<sup>117</sup> See § 3, 109 Stat. at 336-37 (listing exempt transmissions).

<sup>118</sup> See generally Digital Millennium Copyright Act, Pub. L. No. 105-304, 112 Stat. 2860 (1998).

by Internet webcasting with the passage of the DMCA in 1998. While the DMCA was primarily intended to ensure that adequate compensation accrued to copyright owners of sound recordings, it also represented a conscious attempt to protect beneficial new technologies and forms of media consumption and distribution.<sup>119</sup>

The major change from the DPRSRA was the DMCA's extension of compulsory licensing to sound recordings provided through noninteractive, nonsubscription digital audio transmissions.<sup>120</sup> This amendment to the DPRSRA defined nonsubscription transmissions to encompass webcasting, which subjected Internet radio broadcasts to the same compulsory licensing scheme as subscription digital audio transmissions.<sup>121</sup> Thus, only traditional terrestrial radio stations were exempted from the payment of sound recording royalties to copyright owners.<sup>122</sup> Notably, in 2000, the Copyright Office ruled that even transmissions by terrestrial radio stations via the Internet were no longer exempt from the sound recording digital performance right.<sup>123</sup> Thus, the DMCA amendments subjected almost all digital transmissions of music to some form of a compensation requirement payable to sound recording copyright owners.<sup>124</sup>

Of particular importance, the DMCA continued to distinguish between "interactive" and "noninteractive" streaming transmissions.<sup>125</sup> In an effort to ensure that Internet radio stations would not displace high revenue physical album sales,<sup>126</sup> the DMCA required that interactive webcasters negotiate directly with sound recording copyright owners to obtain digital performance

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<sup>119</sup> See *Arista Records, LLC v. Launch Media, Inc.*, 578 F.3d 148, 154 (2d Cir. 2009) (explaining that the goal of the DMCA was "protecting sound recording copyright holders to promote sales, distribution, and development of new music, [while] . . . making development of new media and forms of distribution 'economically [f]easible'" (alteration in original) (quoting H.R. REP. NO. 104-274, at 14)).

<sup>120</sup> 17 U.S.C. § 114(f) (2009).

<sup>121</sup> See *id.* (including "eligible nonsubscription transmission services" under the public performance right); § 405, 112 Stat. at 2898 (1998).

<sup>122</sup> See Ira Hoffman, Note, *Pseudo-Interactivity: An Appropriate Rate Scheme for Customizable Internet Radio Services*, 32 CARDOZO L. REV. 1515, 1520 (2011) (explaining that traditional radio play was exempted because it provided free exposure for artists and sound recordings and was believed to actually increase record sales); see also Day, *supra* note 48, at 187 (explaining that fewer digital transmissions were excused from paying royalties following the passage of the DMCA).

<sup>123</sup> See Copyright Office Rulemaking, Public Performance of Sound Recordings: Definition of a Service, 65 Fed. Reg. 77,292 (Dec. 11, 2000) (upheld by the Third Circuit in *Bonneville Int'l Corp. v. Peters*, 347 F.3d 485, 490 (3d Cir. 2003)).

<sup>124</sup> See 17 U.S.C. § 114(d) (2009) (establishing the scope of exclusive rights in sound recordings).

<sup>125</sup> See *id.* § 114(d)(2)-(4) (outlining the distinction).

<sup>126</sup> See H.R. REP. NO. 104-274, at 13 (1995) (explaining the intricacies of the DMCA amendments); see also KOHN & KOHN, *supra* note 95, at 1329 ("[I]nteractive streams of musical works will tend to displace sales of CDs . . .").

licenses for their services.<sup>127</sup> However, noninteractive streaming services currently enjoy a congressionally established compulsory license, provided that the service complies with the Copyright Act's requirements.<sup>128</sup> Therefore, sound recording copyright holders are essentially required to grant a license to any qualifying noninteractive webcaster to stream sound recordings to the public for an established rate.<sup>129</sup>

### 1. Effects of the DMCA

Based upon the current tripartite structure of the DMCA, it is extremely advantageous for an Internet radio provider to qualify for the noninteractive webcasting compulsory license and forego the high transaction costs of negotiating directly with sound recording copyright owners for the right to offer music to consumers.<sup>130</sup> There are a few interactive webcasters, such as Rhapsody<sup>131</sup> and Spotify,<sup>132</sup> that have had relative success under the current digital performance right framework. However, the vast majority of popular

<sup>127</sup> See 17 U.S.C. § 114(d)(3)(A). Interactive services are generally not granted licenses through these voluntary negotiations for a period in excess of twelve months.

<sup>128</sup> See *id.* § 114(j)(13) (prohibiting noninteractive webcasters from transmitting more than three songs from the same album or four songs by the same artist in any three-hour period).

<sup>129</sup> See *id.* § 114(g)(2) (describing how an agent distributes license receipts).

<sup>130</sup> Transaction costs include negotiation costs associated with voluntary transactions between copyright owners and potential users, search costs associated with buyers and sellers finding each other in order to initiate negotiations, information costs associated with learning about products and the needs of certain businesses, decision costs associated with ensuring that one enters into the most beneficial bargains, policing costs associated with ensuring proper compliance with agreements, and enforcement costs associated with parties filing lawsuits to enforce their rights and contracts. See Stephenson, *supra* note 16, at 399-400 (explaining in detail the advantages of certain statutory license schemes in the context of copyright).

<sup>131</sup> See Janko Roettgers, *Rhapsody to Launch Music Subscriptions in 16 European Countries This Spring*, GIGAOM (Jan. 10, 2013), <http://gigaom.com/2013/01/10/rhapsody-europe-expansion> (“Rhapsody has been the longest-running music subscription service in the U.S., and has more than one million subscribers. The company was seemingly caught by surprise by Spotify’s quick ascent, but has in recent months fought back with a number of new apps and features.”).

<sup>132</sup> Rhapsody is the most popular interactive, or “on-demand,” service that currently exists. See *About Us*, RHAPSODY, <http://www.rhapsody.com/about/index.html> (last visited May 6, 2013) (“Rhapsody is the number-one premium subscription service, with more than one million members . . .”). It is an interactive webcasting service that charges consumers a monthly subscription fee for access to a music library containing over 16 million songs. *Id.* Spotify, however, has quickly gained a strong foothold and large user base in the United States since its launch in 2001. See *Spotify Reaches One Million Subscribers*, SPOTIFY (Mar. 8, 2011), <http://www.spotify.com/us/blog/archives/category/spotify> (describing the milestone of hitting one million subscribers); see also Robert Andrews, *Spotify’s Progress: Challenging Rhapsody but Freemium Gap Growing*, PAIDCONTENT (Dec. 6, 2012, 4:20 PM), <http://paidcontent.org/2012/12/06/spotify-progress-challenging-rhapsody-but-freemium-gap-growing> (“Whilst Spotify gives limited free nonmobile access to nonpayers, Rhapsody requires payment from the outset . . .”).

music services offered to the general public today are noninteractive,<sup>133</sup> due to the lower royalty rates owed to copyright owners and the presence of compulsory licensing for noninteractive webcasters. Creating a successful interactive webcasting service is not impossible under the current framework, but the increased costs associated with direct negotiations and the need to acquire streaming rights from a wide variety of copyright owners means that only a small number of entities are even capable of pursuing such a business plan.<sup>134</sup>

The definition of interactivity, however, is not limited to only the most clear-cut “on-demand” services that allow users to select specific songs to listen to at any time.<sup>135</sup> The DMCA amendments broadened the definition of an “interactive service” to include the phrase “enables a member of the public to receive a transmission of a program specially created for the recipient.”<sup>136</sup> Therefore, under this revised provision, interactive webcasting also includes a variety of services where the degree of choice offered to consumers, and a music listener’s ability to shape the service to his or her preferences, crosses a hazy line defining what is too much predictability or personalized control.<sup>137</sup>

Specifically, the legislative history of the DMCA makes clear that “audio-on-demand,” “pay-per-listen,” and “celestial jukebox” services all fall under

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<sup>133</sup> Pandora is the most dominant noninteractive webcaster in the market today. See Trefis Team, *Pandora Still Pricey, Even with 125 Million Users*, FORBES (Feb. 2, 2012, 1:20 PM), <http://www.forbes.com/sites/greatspeculations/2012/02/02/pandora-still-pricey-even-with-125-million-users/> (announcing that Pandora exceeded 125 million registered users). However, new noninteractive webcasting services, such as Turntable.fm, have begun to garner high praise for their innovative forms of music delivery. See Adrienne Jeffries, *What Is This Magical Turntable.fm Everyone’s Talking About?*, BETABEAT (June 10, 2011, 9:50 AM), <http://www.betabeat.com/2011/06/what-is-this-magical-turntable-fm-everyones-talking-about> (describing the appeal of Turntable.fm).

<sup>134</sup> For example, *Music Unlimited* is one of the more recent interactive webcasters to hit the market, providing over 10 million songs to consumers for a monthly subscription fee of \$9.99. See generally MUSIC UNLIMITED, <https://music.sonyentertainmentnetwork.com> (last visited May 6, 2013). Sony Entertainment, the entity offering this service, is one of the more powerful organizations within the entertainment industry and is one of the four major record labels. This interactive webcasting service can be provided to consumers at an affordable rate due to the company’s ownership of sound recording copyrights, extensive industry connections, attractive distribution capabilities, and powerful brand image.

<sup>135</sup> See Lane, *supra* note 66, at 466 (discussing the statutory classification of interactivity under the DMCA).

<sup>136</sup> 17 U.S.C. § 114(j)(7) (2009); see also Hoffman, *supra* note 122, at 1522 (“[T]he DMCA recognized that on-demand streaming was not the only type of transmission that could hurt record sales.”).

<sup>137</sup> See H.R. REP. NO. 105-796, at 87-88 (1998) (outlining the factors that may classify a service as interactive).

the category of interactive services.<sup>138</sup> For example, a service can qualify as interactive even if the consumer selects certain artists, rather than specific songs, that become the basis for a personalized webcast or stream.<sup>139</sup> Essentially, an interactive service can best be determined by looking at whether a user is “permitted to select particular sound recordings in a prerecorded or predetermined program.”<sup>140</sup> However, the DMCA’s legislative history does not clearly outline what kinds of services are not deemed interactive under § 114(j)(7) or where the line should be drawn.<sup>141</sup>

The definition of interactivity thus has been the subject of important litigation in recent years.<sup>142</sup> Determinations of interactivity are made today on a case-by-case basis. As a result, substantial and important resources are continually squandered as sound recording copyright holders and digital music providers attempt to find and stretch the boundaries of how much control users can be given in their consumption of music without crossing the line from noninteractive to interactive.<sup>143</sup> Meanwhile, sound recording copyright owners continue to challenge online music services through increasingly expensive litigation measures.<sup>144</sup> Even though noninteractive webcasters are still required to pay copyright owners and performance artists royalties under the noninteractive compulsory license rate, it is not surprising that record labels continue to fight innovative and successful noninteractive webcasters like Pandora because of the belief that Internet radio consumers “will choose to listen to webcasts and forego purchasing [CDs or digital albums].”<sup>145</sup> While these services will still provide copyright holders with some compensation, record labels have recognized that the

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<sup>138</sup> See H.R. REP. NO. 104-274, at 25 (1995).

<sup>139</sup> See H.R. REP. NO. 105796, at 87.

<sup>140</sup> *Id.* at 88.

<sup>141</sup> See Pals, *supra* note 84, at 684 (criticizing the way in which Congress has defined interactivity).

<sup>142</sup> See, e.g., *Arista Records, LLC v. Launch Media, Inc.*, 578 F.3d 148, 149-50 (2d Cir. 2009) (determining that a highly customizable webcasting service was noninteractive).

<sup>143</sup> See Hoffman, *supra* note 122, at 1516 n.10 (claiming that Pandora is an example of a digital audio transmission service that falls in the gray area between clear interactive and noninteractive services).

<sup>144</sup> See, e.g., Jonathan Stempel, *Digital Music Service Grooveshark Sued by EMI*, REUTERS (Jan. 5, 2012, 10:31 PM), <http://www.reuters.com/article/2012/01/06/us-grooveshark-emi-lawsuit-idUSTRE80501S20120106> (“Grooveshark has been sued by the large record company EMI Group Ltd, which accused the popular digital music service of paying no royalties since entering a licensing agreement to stream music nearly three years ago.”).

<sup>145</sup> Lane, *supra* note 67, at 471; see also Hardman, *supra* note 10, at 306 (predicting that webcasting services may be driven out of the market due to escalating litigation costs).



royalty fees from noninteractive webcasters are not enough to overcome the effects of piracy.<sup>146</sup>

## 2. The Uncertainty and Dangers Facing Webcasters

Under the case-by-case approach adopted by the Copyright Office and federal courts, it is uncertain whether services using algorithms will continue to be considered noninteractive under the three-tiered DMCA system.<sup>147</sup> Given the current lack of a compulsory licensing rate for interactive services, such individualized factual determinations and the uncertainty surrounding potential high-stakes litigation can inevitably lead to services having to shut their doors.<sup>148</sup>

If future courts interpret interactivity in a slightly different manner, many webcasters will be forced to pay higher rates to sound recording copyright owners and suffer the substantial transaction costs associated with direct negotiations.<sup>149</sup> Smaller webcasters with less bargaining power will suffer by being forced to negotiate directly with copyright holders in a manner that may be “prohibitively expensive or even impossible.”<sup>150</sup> High transaction costs are involved with direct negotiations, as users of copyrighted works must seek out the copyright owner, ensure that others do not have claims to such works, and initiate such transactions from a relatively weak bargaining position. Even worse, while copyright owners of musical works have utilized collective rights organizations such as the American Society of Composers, Authors, and Publishers (ASCAP) and Broadcast Music, Inc. (BMI) to ensure that beneficial market transactions occur as efficiently as possible,<sup>151</sup> sound recording copyright owners do not have such

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<sup>146</sup> See Masur, *supra* note 8, at 57-58 (explaining that many believe “that with the cloud of litigation eliminated, file-sharing networks would rapidly improve[,] . . . [and] the vast majority of file sharers would be willing to pay a reasonable fee for the freedom and peace of mind to download whatever they like using whatever software suits them” (footnote omitted)).

<sup>147</sup> See Hoffman, *supra* note 122, at 1530 (arguing that questionable services should be classified as interactive in future litigation).

<sup>148</sup> For example, in *Arista Records, LLC v. Launch Media, Inc.*, 578 F.3d 148 (2d Cir. 2009), the webcasting company that provided the LAUNCHcast service to consumers chose to cease making the service available even prior to the final court determination.

<sup>149</sup> See Hardman, *supra* note 10, at 305 (explaining that the current regime fosters uncertainty regarding whether Internet radio websites are safe from lawsuits, and arguing that this uncertainty can have potential chilling effects).

<sup>150</sup> Lane, *supra* note 66, at 473; see also Pals, *supra* note 84, at 687 (“For many webcasters, negotiating licenses from all sound recording copyright holders individually would be prohibitively expensive and difficult.”).

<sup>151</sup> See William Henslee, *What’s Wrong with U.S.?: Why the United States Should Have a Public Performance Right for Sound Recordings*, 13 VAND. J. ENT. & TECH. L. 739, 753 (2011) (explaining that collective rights organizations arose in response to the practical problems individual copyright

collective rights organizations in place to help streamline direct negotiations in the world of webcasting.<sup>152</sup>

As a result, future webcasting companies may stop pushing the boundaries of interactivity and simply pursue noninnovative, noninteractive webcasting forms. Internet radio broadcasters may face negotiating costs that are so high that they cannot provide highly customizable webcasting to online music listeners at affordable rates. Recording artists and record labels will inevitably suffer as legal personalized services become more expensive for consumers to access; music listeners will recognize the increased costs and turn to the many convenient and available forms of pirated music services available on the Internet today.<sup>153</sup> Thus, in order to ensure that the recording industry enjoys rising revenues and profits in the future, a solution is needed that effectively aligns the interests of sound recording owners, distributors, and users.

#### IV. THE DEVELOPMENT OF THE NONINTERACTIVE WEBCASTING ROYALTY RATE

In order to propose an efficient solution to the problems and uncertainty facing the music industry today, it is important to understand the mistakes that have been made in relation to the establishment of the compulsory licensing rate for eligible and qualifying noninteractive webcasters.

Since the first recognition of a limited sound recording performance right in 1995, webcasters have suffered from a severe imbalance in negotiating power between themselves and record labels.<sup>154</sup> Normally under the Copyright Act, individuals must directly negotiate with copyright owners to obtain licenses in such works. However, in several instances, the Copyright

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owners faced in policing use of their works and collecting the royalties that they were entitled to); *see also* *Broad. Music, Inc. v. Columbia Broad. Sys., Inc.*, 441 U.S. 1, 1 (1979) (holding that ASCAP and BMI do not violate antitrust laws, despite price fixing behavior, because of the superior efficiency such organizations provide).

<sup>152</sup> *See* Henslee, *supra* note 151, at 758 (explaining that the major collective rights organizations only collect and distribute royalties to songwriters and owners of publishing rights, not the performing artist); *see also* Hardman, *supra* note 10, at 296-97 (discussing the advantages of collective rights organizations and the benefits that they can provide from an economic standpoint). Since almost 85% of artists are represented by the three major record labels, there is, in some sense, a form of collective bargaining that occurs when services wish to acquire the rights to entire catalogues of music.

<sup>153</sup> *See also* Welsh, *supra* note 9, at 1508-09 (explaining that standard record label contracts often provide recording artists with little or no revenue from the sale of records and that consumers seek alternatives as a result).

<sup>154</sup> *See* Day, *supra* note 48, at 191 (describing the years following the passage of the DPRSRA as an "uphill battle" for both webcasters and copyright owners).

Act supersedes copyright law's reliance upon market mechanisms and private bargaining by establishing compulsory licenses.<sup>155</sup> Of particular relevance to this Comment is the compulsory license established under 17 U.S.C. § 114, which, as previously explained, only applies to certain operators of noninteractive digital transmission services.

Compulsory licensing, and the preemption of a copyright owner's control over the use of his or her work, is primarily justified on economic grounds. These licenses benefit owners and users by reducing the high transaction costs associated with private license bargaining. In fact, transaction costs can reach a level so high that beneficial and utility-increasing negotiations will not take place at all; this can result in market failures that have the potential to impoverish copyright owners, desired users, and consumers at the same time.<sup>156</sup> Ideally, a proper statutory licensing scheme will increase net revenues for both users and creators of copyrighted works, which will facilitate the circulation of these works to the public. The establishment of a satisfactory and workable royalty rate, however, is anything but easy, and often results in bitter disputes and lengthy legal proceedings.

Today, compulsory licenses for sound recordings under § 114 are administered by the Copyright Royalty Board (CRB), which is comprised of specialized judges that are appointed by the Library of Congress.<sup>157</sup> Yet the establishment of the current compulsory license for noninteractive webcasters may have been the longest and most bitterly battled of all the compulsory licenses established under the Copyright Act.

#### A. *Copyright Arbitration Royalty Panel Proceedings*

The DMCA amendments to § 114 of the Copyright Act initially attempted to establish the compulsory licensing rate by providing for a voluntary negotiation period within which copyright holders and webcasters

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<sup>155</sup> See 17 U.S.C. § 111(c) (2006) (establishing a statutory license in secondary transmissions by cable television systems); *id.* § 112(e) (establishing a statutory license for ephemeral recordings used to facilitate digital transmissions); *id.* § 115(a) (allowing for the reproduction and distribution of phonorecords of nondramatic musical works, including authorized digital phonorecord delivery of such musical works); *id.* § 118(b)(4) (permitting the use of certain copyrighted works by noncommercial broadcasting entities); *id.* § 119(a)(1) (allowing satellite retransmissions to the public for private viewing); *id.* § 122(a) (establishing a statutory license for satellite retransmissions of local television stations' broadcasts into the local markets).

<sup>156</sup> See Antonio Cordella, *Does Information Technology Always Lead to Lower Transaction Costs?*, Global Cooperation in the New Millennium 855 (The 9th European Conference on Information Systems, June 27, 2001), available at <http://is2.lse.ac.uk/asp/asp/asp/asp/20010024.pdf> ("IT is a powerful tool to support the economic system because it makes more information available so that the uncertainty faced is reduced and hence the transaction costs are lowered.").

<sup>157</sup> See 17 U.S.C. § 114(f) (2009) (describing the licensing process).

could set the binding rate through market mechanisms.<sup>158</sup> Only if these negotiations broke down would the Copyright Arbitration Royalty Panel (CARP) utilize its congressionally vested arbitration power 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 seller.”<sup>159</sup> CARPs were established in 1993 through the Copyright Royalty Tribunal Reform Act, which eliminated the Copyright Royalty Tribunal (CRT)—the body that had been in place to administer compulsory licenses since the 1976 Copyright Act.<sup>160</sup> Therefore, in 1999, when voluntary negotiations broke down between webcasters and the RIAA, which represented the major record labels and had been vested with the power to collectively bargain on behalf of sound recording copyright owners, CARP proceedings were utilized for the first time in relation to sound recordings.<sup>161</sup>

CARP established the compulsory license for certain digital sound recording transmissions in order to reduce the transaction costs associated with establishing acceptable rates, while shifting the costs of administering such statutory licenses to copyright owners and users.<sup>162</sup> Webcasters were required to pay royalties on a per-performance basis, at a rate of seven-hundredths of a cent per performance for commercial webcasters and a lower rate of two-hundredths of a cent per performance for noncommercial webcasters.<sup>163</sup> In other words, the webcaster was required to pay these amounts to the relevant sound recording copyright owner each and every time a song was played.<sup>164</sup>

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<sup>158</sup> See Day, *supra* note 48, at 188-91 (providing a detailed history of the compulsory licensing rate proceedings).

<sup>159</sup> 17 U.S.C. § 114(f)(2)(B); see also Duvall, *supra* note 11, at 272 (“The rates and terms set by the CARP were to distinguish among the different types of services and the degree to which the use of the service increased or decreased the purchases of physical phonorecords (CDs, tapes) by consumers.”).

<sup>160</sup> Copyright Royalty Tribunal Reform Act of 1993, Pub. L. No. 103-198, 107 Stat. 2304 (1993).

<sup>161</sup> See Day, *supra* note 48, at 188.

<sup>162</sup> See Robert P. Merges, *Compulsory Licensing vs. the Three “Golden Oldies”: Property Rights, Contracts, and Markets*, THE CATO INSTITUTE, Policy Analysis No. 508 (Jan. 15, 2004) 1, available at [http://www.cato.org/pub\\_display.php?pub\\_id=1366](http://www.cato.org/pub_display.php?pub_id=1366) (“Compulsory licensing seems to pay off big in the short term by reducing the need for individual buyers to locate, negotiate with, and pay individual sellers. Compulsory licensing supposedly addresses the ‘market failure’ of high transaction costs.”).

<sup>163</sup> See *In re Rate Setting for Digital Performance Right in Sound Recording & Ephemeral Recordings*, Docket No. 2000-9 CARP DTRA 1 & 2 (Feb. 20, 2002), available at [http://www.copyright.gov/carp/webcasting\\_rates.pdf](http://www.copyright.gov/carp/webcasting_rates.pdf) (upheld by the Librarian of Congress on review).

<sup>164</sup> These rates were heavily based upon the recent private agreement between the RIAA and Yahoo!, which was believed to represent a voluntary market transaction between a willing buyer and seller. For more information, see Duvall, *supra* note 11, at 274.

These rates, however, garnered extreme opposition and forced many smaller streaming services out of business.<sup>165</sup> Though the rates were based on a voluntary market transaction between Yahoo! and the RIAA, smaller webcasters did not have the same business structure, capabilities, or resources as Yahoo!, and thus they were subjected to royalty rates that they could not pay while still making a profit. As a result, a wide variety of webcasters began to lobby Congress for assistance, arguing that CARP's decision threatened the viability of the webcasting industry as a whole.<sup>166</sup>

Accordingly, Congress quickly passed the Small Webcaster Settlement Act of 2002, which authorized SoundExchange<sup>167</sup> to collectively bargain and enter into agreements with webcasters on behalf of all sound recording copyright owners and performers.<sup>168</sup> With additional time to negotiate, a compromise between SoundExchange and commercial webcasters was reached in December 2002.<sup>169</sup> An acceptable rate based upon a percentage of the webcaster's total revenue, rather than a per-performance structure, was established.<sup>170</sup>

Not only did this legislative compromise quell the objections of webcasters by creating a system based upon percentages of revenue, but also it satisfied recording artists because of the way in which royalty fees would be distributed.<sup>171</sup> As long as the statutory requirements were satisfied and a service remained noninteractive, the established royalties would be collected

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<sup>165</sup> See Day, *supra* note 48, at 188 (explaining that there was an extreme backlash after the CARP royalty rates were announced).

<sup>166</sup> See Duvall, *supra* note 11, at 275 (explaining that "[m]any webcasters staged a 'Day of Silence' to protest the new fees and accounting procedures").

<sup>167</sup> SoundExchange is a nonprofit collective rights organization established by Congress as the sole entity responsible for the administration, collection, and dispersal of sound recording royalties to artists who register. For a more detailed discussion of SoundExchange's history and responsibilities, see Masur, *supra* note 8, at 48.

<sup>168</sup> See generally Small Webcaster Settlement Act of 2002, Pub. L. No. 107-321, 116 Stat. 2780 (codified as amended throughout the Copyright Act).

<sup>169</sup> See Notification of Agreement Under the Small Webcaster Settlement Act of 2002, 67 Fed. Reg. 78,510, 78,511 (Dec. 24, 2002) (maintaining a flat annual fee for noncommercial webcasters while establishing a royalty rate for commercial webcasters between eight and twelve percent of revenue from 1998 to 2004).

<sup>170</sup> See Kellen Myers, Note, *The RIAA, the DMCA, and the Forgotten Few Webcasters: A Call for Change in Digital Copyright Royalties*, 61 FED. COMM. L.J. 431, 448 (2009) (detailing the specific percentages of revenue and flat fees to be paid under the agreement).

<sup>171</sup> See Duvall, *supra* note 11, at 277 (explaining that there were many benefits provided by the Small Webcasters Settlement Act of 2002 as compared to the CARP royalty rates). *But see* Hardman, *supra* note 10, at 296 (explaining that record labels prefer direct negotiations because the current statutory license scheme demands that up to fifty percent of royalties be given to performing artists).

from webcasters by SoundExchange.<sup>172</sup> After collecting payments from webcasters, SoundExchange would distribute fifty percent of the royalties to the sound recording copyright holder, forty-five percent of the royalties to the recording artist performing the digital sound recordings, and the remaining five percent of the royalties to the collective agencies for nonfeatured musicians and vocalists.<sup>173</sup> Though the specific terms of this compromise were not precedential, Congress effectively delegated negotiating power to SoundExchange to set an industry-wide rate for all copyright holders and recording artists. This ensured that royalties were collected as efficiently as possible.<sup>174</sup>

### B. *The CRB Proceedings*

As was the case with the CRT proceedings, however, CARP proceedings were criticized as too lengthy and expensive.<sup>175</sup> Not only were decisions unpredictable and inconsistent, but also they had been found to occasionally threaten the survival of participants on one side of the dispute.<sup>176</sup> In fact, many Internet radio stations ended their streams after learning how burdensome and expensive it would be to pay sound recording royalties in addition to the compulsory licensing rate required for songwriters and composers.<sup>177</sup> Therefore, in 2004, Congress enacted the Copyright Royalty and Distribution Reform Act, which permitted the Librarian of Congress to appoint three full-time Copyright Royalty Judges (CRJs) to the newly formed CRB.<sup>178</sup>

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<sup>172</sup> See 17 U.S.C. § 114(g)(2) (2006) (vesting the organization with such responsibilities); see also *About*, SOUND EXCHANGE, <http://www.soundexchange.com/about> (last visited May 6, 2013) (providing background information on the collective agency).

<sup>173</sup> See 17 U.S.C. § 114(g)(2)(A)-(D) (establishing the specific formula for royalty payments).

<sup>174</sup> See *The Numbers*, SOUND EXCHANGE, <http://soundexchange.com/about/the-numbers> (last visited May 6, 2013) (stating that the organization has distributed over \$1 billion in royalties); see also Mary LaFrance, *From Whether to How: The Challenge of Implementing a Full Public Performance Right in Sound Recordings*, 2 HARV. J. SPORTS & ENT. L. 221, 225 (2011) (revealing that SoundExchange has also entered into reciprocal agreements with collective rights organizations in the United Kingdom, the Netherlands, Brazil, Spain, and Mexico to collect royalties owed to U.S. copyright owners); Myers & Howard, *supra* note 35, at 240 (explaining that royalty payments to the record industry are continuing to rise, even as music sales continue to decline). *But see* Day, *supra* note 48, at 198 (estimating that over \$600 million in royalties have gone uncollected because of international reciprocity requirements).

<sup>175</sup> See H.R. REP. NO. 108-408, at 18 (2004) (explaining that CARP arbitrators were unable to render acceptable decisions due to a lack of expertise).

<sup>176</sup> See *id.* (criticizing the rate determinations because they “frequently reflect either a ‘content’ or ‘user’ bias”).

<sup>177</sup> See Myers, *supra* note 170, at 449 (explaining that WebRock.net, CyberRadio2000, and Clear Channel all stopped broadcasts of their stations following the agreement).

<sup>178</sup> Copyright Royalty and Distribution Reform Act of 2004, Pub. L. No. 108-419, 118 Stat. 2341, 2341 (codified as amended throughout the Copyright Act).

Importantly, one of the main objectives of the CRB was to “maximize the availability of creative works to the public.”<sup>179</sup>

The initial intention of the new proceedings was to set a royalty rate for sound recordings through voluntary negotiation.<sup>180</sup> Webcasters and record labels, however, were yet again unable to agree upon an acceptable rate. Therefore, on May 1, 2007, the CRB established the royalty rate for the 2006–2010 licensing period by once again utilizing the “willing buyer and seller” model.<sup>181</sup> Employing the calculation procedures commonly used in voluntary transactions between interactive webcasters and record labels, the CRB chose to require noninteractive webcasters to pay on a per-performance basis at an escalating rate ranging from eight-hundredths of a cent in 2006 to nineteen-hundredths of a cent in 2010.<sup>182</sup>

Despite the newly formed CRB’s methodology, almost every digital sound recording broadcaster voiced fierce opposition.<sup>183</sup> Both large and small webcasters alike predicted that the CRB rates would result in the demise of Internet radio and force almost every webcaster out of business.<sup>184</sup>

<sup>179</sup> See *id.*; 17 U.S.C. § 801(a)-(b) (2004). Other stated objectives included balancing the interests of the copyright owner and user and minimizing disruptions of current industry practices and business models. See generally 17 U.S.C. § 802.

<sup>180</sup> See Day, *supra* note 48, at 189-90 (discussing in detail the progression of the first CRB rate-setting procedures).

<sup>181</sup> See Digital Performance Right in Sound Recordings and Ephemeral Recordings, Final Rule and Order, 72 Fed. Reg. 24,084 (May 1, 2007) (codified at 37 C.F.R. pt. 380) (upheld on appeal in *Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd.*, 571 F.3d 69 (D.C. Cir. 2009)); see also Cassandra C. Anderson, Note, “*We Can Work It Out: A Chance to Level the Playing Field for Radio Broadcasters*,” 11 N.C. J.L. & TECH. 72, 79 (2010) (“CRB judges look only at the perceived economic value of the sound recording when making their decision. . . . [T]hey are not concerned with balancing the competing considerations of charging a fair rate against providing goods to the public.” (footnote omitted) (internal quotation marks omitted)).

<sup>182</sup> See Digital Performance Right in Sound Recordings and Ephemeral Recordings, 72 Fed. Reg. at 24,084.

<sup>183</sup> See Day, *supra* note 48, at 190 (describing the hostile reaction as “immediate and dramatic”).

<sup>184</sup> See Duvall, *supra* note 11, at 280-81 (“Smaller webcasters, like Bill Goldsmith from Radio Paradise, were facing bills of up to 125 percent of their yearly income . . . .”); Stephenson, *supra* note 16, at 403 (“The mood of webcasters was summed up by [the CEO] of Pandora . . . in his statement that he was ‘not aware of any Internet radio service that believes they can sustain a business at the rates set by [the CRB’s] decision.’” (citing Louis Hau, *Will Web Radio Get Turned Off?*, FORBES, Mar. 7, 2007, [http://www.forbes.com/2007/03/06/radio-internet-ruling-tech-cx\\_lh\\_0307radio.html](http://www.forbes.com/2007/03/06/radio-internet-ruling-tech-cx_lh_0307radio.html))); Tim Westergren, *RIAA’s New Royalty Rates Will Kill Online Radio!!*, PANDORA (Mar. 6, 2007, 12:49 AM), <http://blog.pandora.com/pandora/archives/2007/03/riaas-new-royal.html> (“The RIAA has effectively convinced [the CRB] to establish rates that make online radio a nonviable business.”). Some larger webcasters estimated that under the 2006–2010 compulsory licensing rates, they would be required to pay between 50% and 70% of annual revenues in sound recording performance royalties alone. See *Performance Rights Act: Hearing on H.R. 4789 Before the Subcomm. on Courts, the Internet, and Intellectual Prop. of the H. Comm. on the Judiciary*, 110th Cong.

Thus, it seemed evident that the CRB once again disfavored the interests of webcasters in the arbitration proceedings,<sup>185</sup> which would threaten the survival of Internet radio and, in the process, a valuable form of revenue for the recording industry.<sup>186</sup>

In light of this opposition, Congress swiftly enacted the Webcaster Settlement Act of 2008, permitting further negotiations between the Digital Media Association (DiMA), which represented webcasters,<sup>187</sup> and SoundExchange.<sup>188</sup> After negotiations reached a stalemate, SoundExchange finally entered into an agreement with three individual webcasters, which established acceptable royalty rates through 2015.<sup>189</sup> Other noninteractive commercial webcasters were permitted to opt in to the terms of the agreement should they choose to do so.<sup>190</sup> For the most part, webcasters who opted in to the agreement paid the standard rate of twenty-five percent of annual revenue in royalties.<sup>191</sup>

The July 2009 agreement serves as the most recent example of the preference for a percentage of revenue scheme, rather than a per-performance fee, to ensure that webcasters are not forced to pay royalties in excess of

160 (2008) (statement of Pandora representatives); Duvall, *supra* note 11, at 281 (explaining that “larger webcasters like Pandora . . . could have a royalty bill of \$2 billion just for one year”); *see also* Myers, *supra* note 170, at 451 (explaining that the CRB royalty rate would make webcasters pay between 50 and 1000 % of their total annual revenue).

<sup>185</sup> *See* Stephenson, *supra* note 16, at 407 (“As a unified voice for copyright owners, SoundExchange is able to present a more forceful message of its needs and requirements before the Copyright Royalty Board. Copyright users, however, have divergent interests that dilute their message before the Board.”).

<sup>186</sup> *See* Myers, *supra* note 170, at 444 (providing an example where fractional differences in the royalty rate can equate to millions of dollars in extra costs or revenues per year); Stephenson, *supra* note 16, at 399 (“The large volume of musical performances used by webcasters results in a situation where fractions of a cent per performance may make the difference between the viability of a commercial webcaster or its demise.” (footnote omitted)); *see also* Day, *supra* note 14, at 75-76 (explaining that record labels and their investments provide a “ripple effect” across the economy by purchasing services from others involved in the music industry and buying advertising space from a variety of media companies). *But see* Duvall, *supra* note 11, at 279 (setting forth reasons why the CRB chose a per-performance rate rather than a revenue-based rate).

<sup>187</sup> *See* Stephenson, *supra* note 16, at 398 (explaining that DiMA is an organization focused upon promoting and ensuring “business model innovation for commercial webcasters”).

<sup>188</sup> *See generally* The Webcaster Settlement Act of 2008, Pub. L. No. 110-435, 122 Stat. 4974 (codified as amended throughout the Copyright Act).

<sup>189</sup> *See* Dan Wilson, *Internet Radio Agreement Reached Between SoundExchange and Webcasters*, BEST SYNDICATION (July 7, 2009), [http://www.bestsyndication.com/?q=20090707\\_soundexchange\\_music\\_rights\\_pandora.htm](http://www.bestsyndication.com/?q=20090707_soundexchange_music_rights_pandora.htm) (explaining that the agreement permitted payment of a discounted CRB-based per-song rate or twenty-five percent of annual revenue).

<sup>190</sup> *See* Hoffman, *supra* note 122, at 1527 (clarifying that essentially all webcasters, by opting in, could pay “the greater of twenty-five percent of gross revenues or a per-play rate that is heavily discounted from the default CRB per-play rate”).

<sup>191</sup> *See id.* (explaining that there was a clear preference for the revenue-based option).



yearly revenue.<sup>192</sup> After all, if webcasters are unable to provide their services to consumers due to escalating costs that outpace revenue, the statutorily established compulsory license provides sound recording copyright owners with less revenue than they would receive with these services in business.<sup>193</sup>

However, on January 5, 2011, the CRB once again convened and issued the current compulsory licensing rate for eligible and qualifying noninteractive webcasters,<sup>194</sup> which once again opted for a purely per-performance compulsory fee when setting the 2011 to 2015 royalty rates.<sup>195</sup> As commentators have noted, “[s]ince both the CRB’s rates and the negotiated agreements terminate in 2015, the high statutory license rates and the CRB’s questionable track record still loom as significant concerns for the future of webcasting.”<sup>196</sup>

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<sup>192</sup> See *id.* at 1522 (explaining that this movement occurred because “the existing rate structure has been thought to already be prohibitively expensive” (footnote omitted)).

<sup>193</sup> This statement assumes that these noninteractive services do not significantly displace album sales, and thus there would not be an increase in consumer album or song purchases once these webcasters went out of business.

<sup>194</sup> See generally Digital Performance Right in Sound Recordings and Ephemeral Recordings, 76 Fed. Reg. 13,026 (Mar. 9, 2011) (codified at 37 C.F.R. pt. 380).

<sup>195</sup> *Id.* With the July 2009 agreement in place, which extends through 2015, the CRB simply preferred to address the per-performance rate option included in the agreement, rather than take the initiative to statutorily provide for a revenue-based option that would apply to all webcasters. The CRB based the current per-performance rates on those already in effect for 2010, adjusting the figures upward by using the same escalation formula used for the 2006 to 2010 period. A gradual escalation was provided for each subsequent year, with 2015 requiring royalty payments from commercial noninteractive webcasters of \$0.0025 per performance. See Kevin Goldberg, *The Webcasters’ Next Five-Year Plan*, COMMLAWBLOG (Dec. 19, 2010, 9:16 PM), <http://www.commlawblog.com/2010/12/articles/intellectual-property/the-webcasters-next-fiveyear-plan/> (providing a per-performance rate chart for the 2011 to 2015 period).

<sup>196</sup> Pals, *supra* note 84, at 688-89 (footnotes omitted). In response to these concerns, Pandora, Clear Channel, and other companies closely tied to music webcasting have founded the Internet Radio Fairness Coalition, “a collection of companies, trade associations and advocacy groups . . . that are throwing their weight behind bills that aim to lower the rates webcasters pay for the performance of sounds recordings.” Glenn Peoples, *Pandora, Clear Channel, Others Form Advocacy Group for Lower Web Radio Payments; MusicFirst Pushes Back*, BILLBOARD (Oct. 25, 2012) <http://www.billboard.com/biz/articles/news/1083273/pandora-clear-channel-others-form-advocacy-group-for-lower-web-radio>. The group introduced the Internet Radio Fairness Act of 2012, legislation that was aimed at lowering webcaster royalties by replacing the CRB’s “willing buyer and willing seller” standard with the guidelines used by satellite radio and cable broadcasters. Under these new guidelines, the royalty rate would be set after taking “into account the public interest, the return earned by copyright owners, the minimization of risk in the industry, and the interplay between creative contribution and capital investment.” *Id.*; see also Internet Radio Fairness Act of 2012, H.R. 6480, 112th Cong. (2013). The bill, however, failed to gain the necessary support to be enacted and has thus been referred back to committee. See Peoples, *supra* (noting that “artists, music creators and other people wrote over 11,000 letters to Congress opposing the Internet Radio Fairness Act” in a single weekend).

In light of the tumultuous history of the § 114 compulsory license rate, it is imperative for Congress to recognize the superiority of a revenue-based system when establishing the proposed compulsory license rate for interactive webcasting.<sup>197</sup> The establishment of a higher compulsory licensing rate for interactive webcasters as compared to noninteractive webcasters can appease the concerns of both copyright owners and webcasters while simultaneously providing consumers with a greater supply and diversity of music tailored to more personalized interests. Most importantly, over time, a statutorily set compulsory license rate for interactive webcasters will incentivize record labels to embrace the digital distribution of music, allow sound recording copyright owners to capitalize on new streams of revenue, and drastically decrease music piracy in the digital age.

#### V. ESTABLISHING COMPULSORY ROYALTIES FOR INTERACTIVE WEBCASTERS

The history of the public performance right in sound recordings shows that Congress has continued to tailor legislation and rate determinations to the overwhelming influence and power of the record labels. By adopting a more holistic view of the music industry and taking into account the interests of copyright holders, webcasters, and consumers as a whole, Congress can help overcome the resistance to change that the recording industry has displayed in recent years.<sup>198</sup>

##### A. *The Need for Revenue-Based Compulsory License Rates for All Webcasters*

The first step in the process is to recognize that the per-performance standard for the compulsory licensing rate established under 17 U.S.C. § 114 for noninteractive services should be abandoned. Once Congress recognizes that market forces have settled on a royalty figure in the range of twenty-five percent of annual revenue for noninteractive services, not only will

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<sup>197</sup> See Duvall, *supra* note 11, at 291 (2008) (“The revenue-based model presumes that most services will survive; the current per performance rates do not.”).

<sup>198</sup> See Pals, *supra* note 84, at 690 (stating that “[t]here are times when the music industry seems so nervous about the new challenges that digital technology poses that it forgets to take into account the positive influences new technology may have on the music industry”); Perritt, *supra* note 7, at 80 (explaining that “[record labels’] business processes and fixed costs were designed to succeed in the environment of the last quarter of the twentieth century, but have not been adjusted to fit current technology” (footnote omitted)).

noninteractive services be ensured a promising future,<sup>199</sup> but also a higher statutory rate for interactive services can easily be established as well.<sup>200</sup>

Under per-performance rates, more popular stations and webcasting services could face licensing fees that are “either an exorbitant percentage of or are greater than gross revenues.”<sup>201</sup> As a result, Internet broadcasters may be forced to charge high monthly subscription fees to cover their operating costs. By doing so, these services risk losing their primary audience to illegal services that are capable of providing similar music selections and comparable online music services to consumers for free: “Some industry experts warn that if regulated webcasters are driven off the web, listeners are likely to turn to illegal services, which pay no royalties, or those who operate from overseas.”<sup>202</sup>

A revenue-based model will ensure that licensing fees do not exceed gross revenues.<sup>203</sup> Webcasting services will no longer have to waste valuable resources in the courts litigating the definition of interactivity, as the implementation of a revenue-based compulsory license rate for both noninteractive and interactive webcasters will eliminate the high costs and burdens that this issue has imposed upon all parties in recent years. Instead of having the courts determine whether a service is interactive or noninteractive, the establishment of a royalty rate for interactive webcasters could shift the determination responsibility to the CRB.<sup>204</sup> This specialized panel,

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<sup>199</sup> See Duvall, *supra* note 11, at 268 (“[I]f royalty rates are set too high for all but the largest webcasters to stay in business, the variety of music available will be severely restricted[,] . . . [and it would] destroy one of the last readily accessible sources of alternative, nonmainstream music.” (footnote omitted)); Hardman, *supra* note 10, at 312-13 (explaining that the lack of a collective rights organization for sound recordings leads interactive webcasters to negotiate with record labels that own a greater number of copyrights and more mainstream music because transaction costs are lower with such owners).

<sup>200</sup> See Mike King, *How Does Spotify Pay Artists? Interview with Spotify's D.A. Wallach*, BERKLEEMUSIC (Sept. 4, 2012), <http://mikeking.berkleemusicblogs.com/2012/09/04/how-does-spotify-pay-artists-interview-with-spotify%E2%80%99s-d-a-wallach> (explaining that Spotify, an interactive webcaster that has thousands of contracts with artists and record labels, distributes 70 % of its annual revenues to copyright owners).

<sup>201</sup> Hoffman, *supra* note 122, at 1525. For a thorough discussion of the perverse incentives per-performance royalty rates create, see Duvall, *supra* note 11, at 268-70. Duvall provides detailed calculations based upon moderate estimates of interactive webcasting use by consumers to display how royalty fees can actually exceed the revenue webcasters can garner from advertising.

<sup>202</sup> Duvall, *supra* note 11, at 280 (citing Eliot Van Buskirk, *Royalty Hike Panics Webcasters*, WIRED (Mar. 6, 2007), <http://www.wired.com/entertainment/music/news/2007/03/72879>).

<sup>203</sup> See, e.g., Small Webcaster Settlement Act of 2002, Pub. L. No. 107-321, 116 Stat. 2780, 2782 (2002) (specifying that “[a]ny such agreement for small commercial webcasters shall include provisions for payment of royalties on the basis of a percentage of revenue or expenses, or both”).

<sup>204</sup> See Hardman, *supra* note 10, at 313-14 (discussing the advantages of establishing an interactive webcaster royalty rate).

which has already analyzed in depth the conflicting concerns and interests of participants in the webcasting industry, would be able to resolve important disputes on a more specialized level and with less cost to the parties involved.<sup>205</sup> In the process, the chilling effect that webcasters have recently experienced would be drastically reduced as the CRB determinations would not create the high-stakes litigation that currently occurs under § 114. Under the new structure, the CRB “would not need to decide whether a license should issue—only at what price.”<sup>206</sup>

With webcasting costs lowered, Internet broadcasters will have the ability to be more creative and aggressive in the formats and functions of their services, providing consumers with a greater variety of music and a greater degree of control over their musical experiences. This should generally drive more consumers to use webcasting, averting them from obtaining pirated music through illegal downloads and P2P networks. As more and more consumers utilize these webcasting services, advertising revenues will increase. Ultimately, this will lead to greater revenues for record labels, so long as the compulsory license rates are structured in such a way as to provide webcasters with the ability to pay copyright owners a pre-determined percentage of their annual revenues.

#### B. *Proposed Compulsory License Rate for Interactive Webcasters*

To establish a revenue-based compulsory license for interactive webcasters, Congress needs only slightly to amend the tripartite system established under 17 U.S.C § 114. Terrestrial radio broadcasters should remain exempt from compensating sound recording copyright owners for broadcasting their works. Additionally, noninteractive webcasters should continue to pay a compulsory license rate to SoundExchange, but only as a percentage of revenue. Finally, Congress should establish a revenue-based compulsory rate for interactive webcasters.

Under this proposed structure, interactive webcasters will be permitted to use sound recordings without the copyright owner’s express consent. In recognition of the risk that interactive services might displace physical and digital music sales and diminish copyright owners’ abilities to control the distribution and performance of their works, the compulsory license rate for interactive services must be a higher percentage of revenue than the

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<sup>205</sup> See Stephenson, *supra* note 16, at 395 (“Delegation is most commonly used where the industry sector to be regulated is highly technical or where their regulation requires a course of continuous decision.”); see also Hardman, *supra* note 10, at 313 (“Shifting the burden in this way from courts to the [CRB] might be a more efficient allocation of governmental resources.”).

<sup>206</sup> Hardman, *supra* note 10, at 313.

compulsory license rate for noninteractive webcasters.<sup>207</sup> The revenue-based scheme need not be the sole option for webcasting royalty rate payments, but webcasters should never be required to pay fees in excess of the statutorily set percentage of revenue. While some smaller webcasting services may therefore continue to privately bargain with copyright owners around the established royalty rate, or opt for a per-performance compensation rate, a default rule based upon percentages of revenue will incentivize interactive streaming services to reach their growth potential.

It should be a much less challenging process for the CRB to extrapolate an acceptable revenue-based rate for interactive webcasters because of the numerous license rate negotiations between noninteractive webcasters and copyright owners that have taken place in the past. In fact, the CRB per-performance royalty rates for noninteractive webcasters have always been primarily based upon extrapolations from the voluntary agreements entered into by interactive webcasters and record companies.<sup>208</sup> Thus, much of the direct comparison work between interactive and noninteractive webcasters and the effects different services will likely have on album sales has already been completed during the CARP and CRB noninteractive rate proceedings.<sup>209</sup> The key data needed to set a higher interactive compulsory license rate has already been collected, including the average retail price interactive services charge consumers, the average royalty charged by record companies from these interactive webcasters, the license fee to retail price ratio of these services, and the effect of interactivity on demand.<sup>210</sup> Taking all of these factors into account, noninteractive services that are identical to interactive services in all other respects should charge between fifty-three and sixty-three percent of the retail price of the average interactive service.<sup>211</sup>

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<sup>207</sup> See, e.g., Andrews, *supra* note 132 (“Spotify pays back nearly 70% of all the money [it] get[s] in to rightsholders.” (internal quotation marks omitted)). Further, to ensure as best as possible that interactive webcasting does not lead to increased piracy, the new compulsory license for interactive services should be subject to the statutory requirement that webcasters take certain anticopying protective measures in order to be eligible for the congressionally established compulsory license. See 17 U.S.C. § 114(d)(2)(C)(v) (2006) (requiring transmitting entities to cooperate in order to prevent various types of piracy).

<sup>208</sup> See Hoffman, *supra* note 122, at 1536-40 (discussing Dr. Pelcovits’s approach for extrapolating noninteractive rates and the CRB’s adoption of his methodology).

<sup>209</sup> See *id.* at 1536-37 (discussing how the value of interactivity has already been isolated and adjustments have been made for noninteractive webcasting royalty rates).

<sup>210</sup> See *id.* (outlining the highly empirical analysis the CRB uses to set the noninteractive royalty rates).

<sup>211</sup> See Testimony of Michael Pelcovits at 39, *In re* Digital Performance Right in Sound Recordings and Ephemeral Recordings, Docket No. 2005-1 CRB DTRA (Oct. 31, 2005) (Testimony of Michael Pelcovits), available at [www.loc.gov/crb/proceedings/2005-5/soundex-pelcovits-written.pdf](http://www.loc.gov/crb/proceedings/2005-5/soundex-pelcovits-written.pdf) (noting that “interactivity raises the price of an online music service by 60% above the

The CRB should begin by utilizing the 25 % of revenue figure that was agreed upon in July 2009 for noninteractive services. It can then extrapolate from this figure using the same methodology accepted and utilized by the CRB previously. After the two staggered revenue-based compulsory license rates are established, SoundExchange can best collect the fees that interactive webcasters would pay under § 114. SoundExchange would be better able to monitor and collect royalties from webcasting services and end users, and then distribute the proper percentage of the total royalty payments to performing artists and record labels based upon airplay. This will ensure that the most popular artists, or holders of the most valuable copyrights, will be compensated the most for their creation of such beneficial works.<sup>212</sup> Yet, the same incentives will be given to all artists and record labels, encouraging them to strive for widespread success and popularity since copyright owners and recording artists will only be compensated through SoundExchange if their music is played on these services.<sup>213</sup>

In order to benefit from the efficiencies of SoundExchange, performing artists and record labels should be required to register with the organization. SoundExchange would maintain a database to identify producers, performers, and copyright owners and their contact information to ensure the proper distribution of royalties. Technologies already exist that allow digital files to be embedded with identifying and contact information for rights holders.<sup>214</sup> Thus, each song's total airplay, or number of performances, would be relatively easy for music services to track and report to SoundExchange.

It is imperative, however, that this database and embedded identifying information be made available not only to SoundExchange, but also to record labels and performing artists. This would ensure that royalties are fully collected and distributed to the proper parties.<sup>215</sup> Royalties that are

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level of a noninteractive service that is identical in every other respect"); *see also* Hoffman, *supra* note 122, at 1544 (arguing that statutory rates should be adjusted based on the customizability of the digital broadcast service); Myers & Howard, *supra* note 35, at 240 (explaining that the history of the sound recording public performance right has already established a framework for determining reasonable royalty rates by the CRB and SoundExchange and for collecting, monitoring, and dispersing these fees effectively and easily).

<sup>212</sup> *See* King, *supra* note 200 ("On an individual artist level, we're paying out royalties of \$200-300 thousand dollars a month for some of the biggest acts."); *see also id.* ("If we can get to the scale of Netflix—which has 20 million subscribers—we estimate we'd be paying out to artists what iTunes is paying out on a year to year basis.").

<sup>213</sup> *See* Andrews, *supra* note 132 (explaining that Spotify has "paid out more than \$500 million [in royalties to rights holders] and it's more than doubled in the last nine months").

<sup>214</sup> *See* LaFrance, *supra* note 174, at 259 ("Tracking usage of specific recordings is relatively easy because the necessary information is encoded in the digital recordings.").

<sup>215</sup> *See id.* at 256 (suggesting that SoundExchange follow a similar structure to ensure proper collection and dispersal of sound recording royalties).

incapable of being distributed to copyright owners or performing artists—possibly because registration has not been completed or ownership of the relevant copyright has been transferred without updating the database information—would be held and made available to be claimed for a certain sufficient period of time (i.e., five years). Any unclaimed funds, in addition to a small percentage of total royalties collected, would then be used by SoundExchange to cover the costs of administering the system as well as monitoring, collecting, and dispersing royalties.<sup>216</sup> This distribution scheme would thus capitalize on the lower costs and greater enforceability that collective rights organizations can provide to copyright owners.

The details of such a plan will undoubtedly be the subject of fierce and lengthy bargaining between sound recording copyright owners and desired users. However, Congress and the recording industry should begin to recognize the power and importance of streaming technology in today's world. The first step in that process is for Congress to amend the Copyright Act to create a compulsory license for interactive webcasters. By eliminating the need for interactive webcasters to directly negotiate with sound recording copyright owners, the high transaction costs that stunt the growth of the interactive webcasting industry will be curtailed. Valuable resources will no longer have to be expended in order to obtain the rights to publicly perform sound recordings, and the search process will be streamlined as SoundExchange will collectively govern the rights of all sound recording copyright owners in the digital world. While it may take many years to establish an interactive webcasting royalty rate that properly compensates copyright owners while still allowing Internet services and webcasting companies to expand or develop highly profitable business plans, the experience the music industry has gained from the establishment of the noninteractive webcasting royalty rate should expedite the process.

### *C. The Benefits of Amending § 114 as Compared to Other Proposals*

Over the last fifteen years, scholars and commentators have suggested both traditional and novel solutions to combat diminishing record label revenues and the music piracy epidemic. Some of these suggested solutions have been and continue to be pursued through the courts and Congress, while others have been overwhelmingly resisted or rejected. This Comment does not argue that establishing a compulsory license rate for interactive webcasters will be the sole solution to all of the music industry's problems.

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<sup>216</sup> See *id.* at 256-59 (discussing ways that relevant copyright owners can be encouraged to register with SoundExchange and properly protect their rights).

In order to ensure the health and profitability of the industry in the future, many changes and sacrifices must be made by all market participants involved. Instead, this Comment proposes that the entire music industry needs to be incentivized to follow a different and modernized path in order to ensure long-term success and growth. Before discussing in greater detail the breadth of benefits that would accrue to copyright owners, webcasters, and consumers from this Comment's proposed statutory changes, I highlight a few of the more recent and promising proposals in order to shed light on the superior value and benefits compulsory licensing can provide.

Recently, it has been suggested that the music industry embrace a Hulu-like model<sup>217</sup> in an attempt to combat diminishing profits.<sup>218</sup> By focusing upon partnerships with online intermediaries that can offer free streaming and downloading services to consumers, these online distribution services would gain the majority of their profits through advertising.<sup>219</sup> An escalating revenue stream based upon increasing levels of consumer use would thus result.<sup>220</sup> Meanwhile, by embracing a new distribution system that is more in line with consumer preferences, record labels and other copyright owners would increase their annual profits.<sup>221</sup>

While this solution properly recognizes the need for the music industry to embrace streaming technology and promising new delivery methods, the history of the DPRSRA suggests that voluntary negotiations between record labels and online providers would take decades to complete. In order to overcome the high transaction costs that might hinder such negotiations and to ensure the health and growth of the music industry, Congress should take the initiative to amend the Copyright Act. A more comprehensive statutory licensing scheme will adequately address the complexity of Internet radio broadcasters and ensure that value can be derived from all of the services offered to consumers in today's online music industry.<sup>222</sup>

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<sup>217</sup> Established as a joint venture between NBCUniversal, Fox Entertainment Group, and Disney-ABC Television Group, Hulu is a website that offers ad supported-on demand streaming video of television shows, motion pictures, and webisodes. Users can enjoy the Hulu media content for free, or through a monthly subscription option that provides them with more content. See HULU, [www.hulu.com](http://www.hulu.com) (last visited May 6, 2013).

<sup>218</sup> See Masur, *supra* note 8, at 56 (explaining that new media services like Hulu and Netflix have experienced extensive growth and success in the market for high quality digital content).

<sup>219</sup> For a more detailed discussion of this proposal, see Jessica Wang, *A Brave New Step: Why the Music Industry Should Follow the Hulu Model*, 51 IDEA 511, 531-49 (2011).

<sup>220</sup> *Id.* at 546-47 (describing potential revenue streams from the "Hulu Model").

<sup>221</sup> See Duvall, *supra* note 11, at 294 ("Pandora gives listeners access to over 39,000 performers; terrestrial radio plays fewer than three hundred different artists." (footnote omitted)).

<sup>222</sup> Compare Hoffman, *supra* note 122, at 1517 ("[T]he rate scheme should contain a finer gradation of rates . . . . To only recognize the two extremes—fully interactive on one end and completely noninteractive on the other—is to ignore the range of the value that exists in



Alternatively, some scholars have suggested amending the Copyright Act to essentially legalize unauthorized downloading and streaming of music through the establishment of a federal digital music tax.<sup>223</sup> The goal of this tax would be to ensure adequate compensation for sound recording copyright owners in the face of widespread music piracy. The tax revenue would be allocated to copyright owners based upon the frequency of use of their works as compared to other sound recordings.<sup>224</sup> Proponents argue that such a system would ensure that owners of sound recordings, and specifically record labels, are adequately compensated, while providing consumers with legal, free music.<sup>225</sup>

However, the major shortcoming of such a widespread government tax system is the heavy cross-subsidization that would result. Since not all taxpayers use or download sound recordings to the same extent, high-volume music listeners would be subsidized by low-volume or no-volume music listeners.<sup>226</sup> Some individuals today choose never to pay for music online, preferring the radio or their already assembled collections of CDs and digital albums. Consequently, a tax imposed upon these individuals in order to compensate record labels and other copyright owners while allowing copyright infringers to escape liability seems to be an unjust allocation of financial burdens.<sup>227</sup> While it would be wise to adopt a system that distributes fees to copyright owners based upon the frequency of consumer use, individuals should not be forced to pay for services and copyrighted works for which they have no use or desire to engage.

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between.”), *with* Wang, *supra* note 219, at 531-36 (arguing that the Hulu Model is the best solution for the music industry).

<sup>223</sup> See WILLIAM W. FISHER III, PROMISES TO KEEP: TECHNOLOGY, LAW, AND THE FUTURE OF ENTERTAINMENT 199-258 (2004) (arguing for a tax-based compensation system); *see also* Welsh, *supra* note 9, at 1497 (suggesting “an absolute privilege against copyright liability for noncommercial reproduction and distribution of sound recordings by individuals”).

<sup>224</sup> See FISHER, *supra* note 223, at 223-34 (discussing ways to allocate possible tax revenues to copyright owners).

<sup>225</sup> *Id.* at 224 (suggesting that the best system would be to allocate revenue based upon the frequency with which sound recordings are downloaded).

<sup>226</sup> See Masur, *supra* note 8, at 54 (stating that many opponents of the tax solution have pointed to the inequity in allocating costs to all users equally despite differences in levels of media consumption).

<sup>227</sup> *But see id.* at 45 (explaining a proposed solution that would “create a right to collect reasonable fees from all Internet users at their point of access”).

## VI. BENEFITS OF COMPULSORY LICENSING FOR INTERACTIVE WEBCASTING

It will not be easy to garner the necessary political and economic support to implement this Comment's proposed changes. The recording industry will most likely vehemently resist the establishment of a royalty rate for interactive webcasters.<sup>228</sup> Record labels and copyright owners will argue that they will experience drastic decreases in record and song sales from the imposition of such a compulsory license rate because of the greater ease of piracy and severe cannibalization associated with these services. However, by establishing a significantly higher compulsory license rate than is currently in place for noninteractive webcasters, copyright owners can be adequately compensated for the risks they are incurring and the potential shift in consumer consumption decisions. In the short-term, record label profits are likely to continue diminishing or remain relatively stagnant. But as a greater variety of webcasting services form and interactive webcasting is permitted to flourish under a revenue-based model that ensures the survival and growth of new music delivery technologies, consumers, webcasters, and copyright owners will all benefit.<sup>229</sup>

While the predictability of interactive webcasting worries the recording industry because of the greater possibility and ease of illegal copying and reproduction, streaming technology and interactive webcasting provide several advantages over permanent download formats in today's digital world. Though songs can still be copied and dispersed when streamed to a user's computer, there is a greater opportunity cost for the initial infringer to copy streaming audio.<sup>230</sup>

With regard to digital file downloads, an individual who wants to illegally copy and disperse a file to the public can do so in a matter of seconds. This

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<sup>228</sup> See Robert Andrews, *Interview: Spotify Exec on Royalties and Keeping Labels Happy*, PAIDCONTENT (Dec. 10, 2012), <http://paidcontent.org/2012/12/10/interview-spotify-exec-on-royalties-and-keeping-labels-happy> (noting that "major artists like Adele, Coldplay, deadmau5[,] Taylor Swift[,] and Rihanna have, over the last year, withheld their latest albums from streaming services, hoping for a downloads pay-day before a streaming long tail"). See also Ben Sisario, *AC/DC Joins iTunes, as Spotify Emerges as Music's New Disrupter*, N.Y. TIMES (Nov. 19, 2012, 5:14 PM), <http://mediadecoder.blogs.nytimes.com/2012/11/19/acdc-joins-itunes-as-spotify-emerges-as-musics-new-disrupter> ("The Apple iTunes store . . . won over a last holdout—AC/DC—on Monday. But the band's decision to join iTunes has also revealed that the industry has found a new digital frenemy: Spotify, where AC/DC's music is still nowhere to be found.").

<sup>229</sup> See King, *supra* note 200 (suggesting that, as websites such as Spotify grow, "the pool of revenue will increase, and the royalty rate will increase for rights holders").

<sup>230</sup> See generally DAVID AUSTERBERRY, *THE TECHNOLOGY OF VIDEO AND AUDIO STREAMING* 133-40 (2d ed. 2005) (providing a detailed discussion of the technology behind and uses of streaming media in the digital world).

is because the file is permanently downloadable to the user's computer desktop and a plethora of software is available to copy digital files in the same high quality format. Similarly, with physical albums, many forms of "ripping" software have been developed that allow an infringer to make permanent digital copies of an entire CD and automatically divide the copy into individual song files in a matter of seconds.<sup>231</sup> But with a streaming audio recording, the music pirate must allow the entire song to play in real-time in order to create a copy of the work. Additionally, a new file must be created since no permanent file is placed on the user's computer when streaming a song. Therefore, the costs associated with pirating music are increased because in order to pirate music files, consumers must invest in high quality sound recording software, programs, or systems, stream the entire song to copy it fully, and then divide up the streaming music copies into individual files for dispersal to the public.<sup>232</sup> As a result, many user-influenced services do "not pose an unusually grave threat to copyright holders" when useful business models, technology, and anti-copying protections are in place because "copying from a stream is so inefficient for pirating specific songs that very few users would consider trying it."<sup>233</sup>

With the recent rise in popularity of services like Hulu and Netflix,<sup>234</sup> it seems that society has embraced streaming-based services and technologies. This trend is likely to continue as Internet and wireless speeds increase, mobile devices become more sophisticated, and 4G networks provide greater connectivity to programs, websites, and services throughout the world. Companies are increasingly relying upon mobile applications and streaming technologies to satisfy consumer preferences and needs.<sup>235</sup> Yet the recording industry has for the most part resisted such new technologies, fighting vigorously to maintain an outdated business model dependent on physical album sales. But if copyright owners of sound recordings can recognize the advantages of webcasting, accept statutory changes that are

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<sup>231</sup> While the music industry made it harder to copy CDs and DVDs in the mid-2000s with the use of anti-circumvention technology, this practice has been largely abandoned due to consumer frustration and backlash.

<sup>232</sup> See AUSTERBERRY, *supra* note 230, at 137-38 (discussing the many benefits and valuable uses of streaming technology).

<sup>233</sup> Pals, *supra* note 84, at 691 (footnote omitted).

<sup>234</sup> See generally NETFLIX, [www.netflix.com](http://www.netflix.com) (last visited May 6, 2013). Netflix originally began as a successful provider of flat-rate DVD-by-mail services. In recent years, however, the company has steadily shifted toward an on-demand Internet-streaming media platform.

<sup>235</sup> See, e.g., *Mobile Apps: NFL Sunday Ticket*, DIRECTV, [http://www.directv.com/DTVAPP/content/technology/mobile\\_apps/nfl\\_sunday\\_ticket](http://www.directv.com/DTVAPP/content/technology/mobile_apps/nfl_sunday_ticket) (last visited May 6, 2013) (announcing that with the NFL Sunday Ticket app, consumers can now watch every Sunday NFL football game on their smartphone or tablet).

more directed toward long-term growth rather than short-term profit, and shift the focus of the entire music industry from permanent file formats and physical ownership of music to streaming services, all music industry market participants can achieve greater benefits and profits.

#### A. *Short-Term Benefits*

It is important to recognize that record labels and copyright owners will most likely suffer short-term losses due to the proposed changes and consequent rapid shift in the market. However, as companies begin to profitably offer more customizable and personalized services to the public, and consumers begin to utilize free interactive webcasting or subscription-based services, less piracy should occur. In the long-run, while the use of interactive services may largely displace traditional record sales, the savings associated with significantly reducing the illegal downloading, copying, and distribution of sound recordings can more than offset these losses.<sup>236</sup>

By establishing a revenue-based royalty rate that incentivizes interactive webcasters to capture as much of the market as possible, consumers will find it easier to obtain the music and personalized services that they overwhelmingly desire. Consumers who enjoy discovering new music and being randomly exposed to new artists and unique genres can continue to engage with noninteractive services governed by a lower compulsory license rate. However, individuals who prefer to exercise control over their music will be permitted to do so in more affordable and convenient ways than ever before.<sup>237</sup> Interactive webcasters will be able to offer consumers millions of songs through vast and relatively comprehensive music catalogues, providing users with any sound recording they could possibly desire.<sup>238</sup>

Further, a revenue-based model would permit webcasters to focus on creating value and achieving sustained growth because SoundExchange would perform the distribution of royalties to each copyright owner. These webcasters would no longer have to waste resources determining which

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<sup>236</sup> See Duvall, *supra* note 11, at 295 (concluding that having a wide variety of music available will ultimately benefit both society and the music industry, which can “tak[e] advantage of the unique aspects of webcasting to promote their products”).

<sup>237</sup> See King, *supra* note 200 (explaining, through an interview with Spotify’s “Artist in Residence,” that a yearly subscription to the service costs \$120 in the United States, £120 in the United Kingdom, and €120 in the European Union).

<sup>238</sup> Robert Andrews, *Spotify Solves Discovery by Discovering Music Ain’t So Social After All*, PAIDCONTENT (Dec. 6, 2012, 5:37 PM), <http://paidcontent.org/2012/12/06/spotify-solves-discovery-by-discovering-music-aint-so-social-after-all> (“Spotify is a great way to listen to 18 million tracks. Now it has plugged its biggest hole—discovering them.”); see also Andrews, *supra*, note 132 (detailing how Spotify is “[a]dding 10,000 to 20,000 new songs every single day”).

songs attract the most users or what sound recordings are profitable based upon a certain level of use. Webcasters could instead focus on increasing the general demand for music, which would raise their annual revenues and result in greater compensation to copyright owners as a whole. In essence, this Comment's proposed changes would ensure that interactive webcasters and record labels work as partners in a unified effort to increase the supply and demand of legal sound recordings, rather than bicker over the division of diminishing profit margins in the face of music piracy.

### B. *Long-Term Benefits*

As the music industry, the Internet, and streaming technologies continue to evolve, a new statutory scheme for webcasting can produce significant benefits. Consumers, webcasters, and record labels will hopefully be able to realize great gains as the music industry pie once again begins to grow with compulsory license rates in place for all webcasters.

Consumers will benefit from the establishment of an interactive compulsory license rate for a variety of reasons. Due to lower operating costs, webcasters should be able to more effectively compete with the overwhelming availability of free pirated music. This is because webcasters will have the flexibility to structure their businesses to operate primarily on advertising revenue, which would allow consumers the option of streaming music for free. However, even if interactive webcasters chose to charge a low monthly subscription fee, for example in the range ten to fifteen dollars per month, the advantages associated with gaining access to such an organized and vast selection of music will undoubtedly be attractive to consumers. Subscribers will be offered a variety of genres, artists, and songs, all in furtherance of providing consumers with any song they could ever possibly desire.<sup>239</sup> By establishing a compulsory license rate for interactive webcasters through a congressional amendment, an even greater repertoire of music can be compiled, since webcasters will only be required to pay a lump percentage of revenue to SoundExchange. Without having to engage in private negotiations or the tracking and dispersal of royalty fees to individual copyright owners, webcasters will be able to offer consumers any copyrighted musical performance they want. These lower costs will also likely lower the monthly fees charged by webcasters.

Unlike illegal file sharing websites and pirated music services, interactive webcasters can effectively eliminate the risk of consumers being sued for

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<sup>239</sup> See Johnson, *supra* note 69 (providing a quick look at Rhapsody's structure and the reasons for its success).

copyright infringement. Furthermore, since webcasting does not leave a permanent file on a user's system, the harms that can result from downloading corrupted files will be eliminated. Technology has reached a point where many consumers might prefer to use streaming musical services rather than to own physical or digital copies of sound recordings. Due to the increasing speeds and availability of wireless Internet services, the creation of 4G networks, and the advancement of mobile devices, consumers no longer feel uncomfortable "renting" music.<sup>240</sup> Interactive webcasting allows consumers to instantly own tens of millions of songs, so long as they are capable of connecting to the Internet.

Services will be able to offer consumers access to vast libraries of music through a variety of devices: computers, cell phones, portable music players (such as iPods), and televisions, to name a few.<sup>241</sup> It is nearly impossible to predict what new technologies or devices will be developed that will offer consumers even greater connectivity. But it is safe to say that interactive webcasting services have the potential to offer music listeners something unique and highly valuable—an unlimited capacity to store sound recordings and the ability to access and listen to almost any song at any time.

Comparably, interactive webcasting services will experience drastic growth and will attract more lucrative opportunities under a new statutory scheme. They will benefit from the greater flexibility that a compulsory license rate can provide. As the consumer base of successful interactive webcasting services grows,<sup>242</sup> web-based advertising will be in greater demand and will prove more profitable. Companies will be willing to pay higher rates for access to a greater number and wider array of potential customers. This will lead to greater revenues for webcasting services, permitting such companies to offer more creative and revolutionary services to consumers. More importantly, with a revenue-based royalty rate structure in place, webcasters will not be in danger of going bankrupt because of disproportionate royalty fees that could exceed their total annual revenue.

Subscription fees should become more acceptable to consumers as webcasters offer greater personalization and allow consumers to amass a

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<sup>240</sup> See Steve O'Hear, *Music Industry: Five Alternative Business Models*, LAST100 (Oct. 11, 2007), <http://www.last100.com/2007/10/11/music-industry-five-alternative-business-models> (citing legendary music producer Rick Rubin and predicting that "[w]hen all of our music can 'live in the clouds,'[sic] accessible at any time, owning it outright may no longer be that important").

<sup>241</sup> See Andrews, *supra* note 132 (noting that just after one year, Spotify had more than twenty million active users who created more than one billion playlists, and over one million songs were streamed in just the first week after the company launched its mobile application).

<sup>242</sup> See King, *supra* note 200 (predicting that "subscription based interactive streaming model[s] will likely continue to play a growing part in the future of music consumption").

seemingly limitless library of sound recordings. As a result, the most successful and efficient webcasters will be able to profitably charge a low monthly fee that will bolster total revenue.<sup>243</sup> As interactive webcasting evolves and is able to offer consumers benefits that P2P networks and pirated music cannot provide—such as more efficient searching, assurances of the highest quality music, and security from copyright infringement claims—more and more consumers should flock to legal music delivery services.

Most importantly, the interests of webcasters and sound recording copyright owners will be aligned under the new statutory scheme. The more users that webcasting services obtain, the more subscription fees and advertising revenue they receive. Consequently, record labels will receive higher payments through established compulsory royalties. The mutual desire of webcasters and record labels to increase legal music consumption and market share will induce record companies to promote successful webcasting services, in addition to physical and digital album purchases. With the vast resources of the major record companies behind interactive webcasters, costs can be further lowered and services will become more efficient. All in all, more consumers will be driven into the interactive webcasting market, raising annual revenues and profits for the entire streaming music industry.

By creating a system that can effectively curb and diminish music piracy throughout the world, the entire music industry can achieve consistent growth for the first time in many years. As the webcasting industry advances and consumers benefit from the convenience and availability of millions of songs at the touch of a button, streaming music delivery will lead to a greater number of consumers turning to these legal means of music consumption: the risks and inconveniences associated with individually searching for and using pirated music will no longer be worth it.

Record labels will also have lower costs once they no longer have to incur litigation expenses by trying to enforce their copyrights. As evidenced by the recording industry's numerous past and current attempts to combat music piracy, the money spent on enforcing sound recording copyrights, whether against large P2P services or individual infringers, is rarely recouped through favorable decisions or orders.<sup>244</sup> Further, less infringement should

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<sup>243</sup> See Andrews, *supra* note 132 (reporting that Spotify acquired over one million paid subscribers within three months and now has over five million paying customers worldwide).

<sup>244</sup> Even if found liable by the courts, individual defendants in illegal downloading suits are often judgment-proof and unable to pay. See David Kravets, *File Sharing Lawsuits at a Crossroads, After 5 Years of RIAA Litigation*, WIRE (Sept. 4, 2008), <http://www.wired.com/threatlevel/2008/09/proving-file-sh> (quoting Casey Lentz, a former student sued by the RIAA, who explains

occur generally as legal forms of music delivery and webcasting begin to satisfy the needs and desires of consumers better than illegal downloading or streaming services.

Though sound recording copyright owners will no longer have the right to exclude interactive webcasters from using their works, they should be adequately compensated by the overall growth of the music industry and the guaranteed royalty payments that will be enforced and distributed by SoundExchange. No longer will record labels have to individually negotiate with potential users and police the world for copyright infringement. Instead, they can benefit from the efficiency and decreased costs of collective action and put their valuable resources to better use.

Finally, since the mid-1990s, the public perception of the recording industry has been severely marred. By embracing new technologies and shifting consumer preferences, record labels can hopefully mend their damaged reputations. By offering consumers personalized services and access to a greater variety of music, record labels will benefit from the positive public relations effects that will result. While it is likely that record labels will continue to be criticized for the sometimes one-sided contracts and arrangements they enter into with recording artists,<sup>245</sup> the media will no longer be dominated by negative stories concerning powerful record labels suing less fortunate end users. Record labels will no longer have to pursue legislation that media companies, website operators, and the public view as "censorship."<sup>246</sup> The improved reputation of and diminished hostility toward the recording industry will hopefully result in even less illegal downloading and streaming by users. By incentivizing consumers to engage in legal music consumption, the new statutory rate scheme will benefit record labels the most.

While the establishment of a compulsory license may not prove to be the answer to all of the music industry's problems, amending the Copyright Act would be a significant step in the right direction. Under this new structure, music piracy would be more effectively curtailed, and pirates would no longer be able to as easily siphon off profits that rightfully belong

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that the major record labels "want[ed] \$7,500 for 10 [illegally downloaded] songs," but she "only had \$500 in [her] bank account").

<sup>245</sup> See Mike Masnick, *Record Labels Screwing Over Musicians Is Nothing New; The Buddy Holly Edition*, TECHDIRT (Feb. 3, 2010), <http://www.techdirt.com/articles/20100201/0234157986.shtml> (discussing how record labels have a history of failing to protect musicians' interests and suggesting that digital technology may provide performing artists with more bargaining power).

<sup>246</sup> See Melissa Knowles, *Popular Websites to Go Dark Over SOPA Controversy*, YAHOO! NEWS (Jan. 17, 2012), <http://news.yahoo.com/blogs/trending-now/popular-websites-dark-over-sopa-controversy-174211626.html> (discussing the recent boycott that website operators initiated in response to two proposed congressional bills).



to the recording industry. As music piracy decreases, annual revenues for record labels will inevitably increase. As a result, the recording industry may very well be able to exceed the \$14.6 billion annual revenue plateau reached in the late 1990s.<sup>247</sup> By embracing a novel solution that harnesses innovative and promising technologies and capitalizes on consumer preferences, annual revenues may reach a level that no one would have thought possible in recent years.

#### CONCLUSION

Under a new, more affordable statutory framework, the benefits and decreased costs associated with using legal interactive webcasting services can finally exceed the advantages many people find in illegal file sharing. More consumers will begin paying for legal access to music due to the decreased transaction costs, superior services, safety from corrupted files, and extinguished threat of expensive litigation provided by interactive webcasters.<sup>248</sup> The decrease in CD sales and corresponding rapid increase in digital music file purchases demonstrate that consumers “prefer more convenient formats, that they resist having the songs they want being tied to songs they do not want, and that they want the prices they are charged to reflect the much lower costs of production and distribution which new technologies make possible.”<sup>249</sup>

There is strong evidence that consumers are still willing to purchase music.<sup>250</sup> Despite the meteoric rise of music piracy in the Internet era, consumers have shown a willingness to purchase songs through iTunes or join subscription-based interactive webcasters such as Rhapsody and Spotify.<sup>251</sup> Simply stated, if “services have proven themselves, it is plausible

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<sup>247</sup> For example, as vocalist and songwriter D.A. Wallach explained, Spotify is “trying to create . . . a system in which you earn royalties forever for good music.” King, *supra* note 200. He further clarified that, “[i]f you took the effective per play rate that I’ve paid for every time I’ve listened to my *Dark Side of The Moon* CD, it would be trivial compared to what I’d have generated if I’d done all that listening on Spotify.” *Id.*

<sup>248</sup> See Perritt, *supra* note 7, at 208-09 (arguing that record labels can effectively compete with the presence of free music in the marketplace by offering consumers advantages that pirated music cannot provide).

<sup>249</sup> *Id.* at 90.

<sup>250</sup> See LAWRENCE LESSIG, *FREE CULTURE: HOW BIG MEDIA USES TECHNOLOGY AND THE LAW TO LOCK DOWN CULTURE AND CONTROL CREATIVITY* 297-98 (2004) (predicting that growth in wireless Internet technology will result in people being more willing to pay to stream content from service providers than to purchase and own permanent copies of copyrighted works).

<sup>251</sup> See Andrews, *supra* note 132 (revealing that as of the end of 2012, even though Spotify has only operated in the United States for a little over a year, the service has quickly gained over one

that consumers will be willing to pay something, especially on a subscription basis, for the service, even though they theoretically could spend 200 days per year finding the music themselves.”<sup>252</sup>

It is true that record labels will no longer be able to refuse access to copyrighted works or deny the use of sound recordings that they own. Sound recording copyright owners thus have a legitimate short-term fear that profits will suffer as the royalty rates established by the CRB may lead to a significant displacement of album sales.<sup>253</sup> But, in addition to incentivizing consumers to engage in legal music consumption, “[b]y removing the transaction cost problem associated with individual license negotiations, [compulsory] licensing would make it easier for webcasters that provide interactive services to comply with the law.”<sup>254</sup>

As a result, music piracy will decrease, litigation costs will decline, and though royalty fees, when broken down on a per-stream basis, may be less than what record labels desire, overall royalty revenue received from webcasters will inevitably increase.<sup>255</sup> If the mission of major record labels is to increase their annual revenues and combat music piracy affordably, then amending the Copyright Act to establish a compulsory license for interactive webcasters seems to be one of the most effective ways to accomplish that goal.

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million monthly subscribers and now has over twenty million active users utilizing either the free ad-supported or the subscription options worldwide).

<sup>252</sup> Perritt, *supra* note 7, at 209; *see also* Rajiv K. Sinha & Naomi Mandel, *Preventing Digital Music Piracy: The Carrot or the Stick?*, 72 J. MARKETING 1, 1 (2008) (“[T]he success of iTunes and other legal file-sharing Web sites seems to indicate that . . . a portion of music consumers are willing to pay a positive amount to download music legally.” (citation omitted)).

<sup>253</sup> *But see* Hardman, *supra* note 10, at 314 (explaining how short-term consequences will likely be offset by long-term gains in terms of total revenue).

<sup>254</sup> *Id.*; *see also* Stephenson, *supra* note 16, at 409-10 (“The organized nature of copyright owners versus the disparate interests of copyright users ensures the continued need for a statutory system to deliver the policy goals of broad access to the copyrighted materials and fair return for the copyright owners.”).

<sup>255</sup> *See* Henslee, *supra* note 151, at 747 (“[C]opyright legislation must ensure the necessary balance between giving authors necessary monetary incentive without limiting access to an author’s works.” (footnote omitted)); Hardman, *supra* note 10, at 317 (“Removing the interactivity distinction entirely and replacing it with a blanket compulsory licensing scheme stands out among other solutions as the one that best negotiates the balance between . . . protecting record sales and encouraging the continued creation of music, and . . . the Constitutional mandate of promoting progress by encouraging the development of new technologies and new media.”); *see also* Myers & Howard, *supra* note 35, at 239 (stating that “public performance royalties would clearly bolster overall revenues in the music business”).