

How the Spotify Streaming Model Affects the Modern American Musician

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Abstract

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Throughout the digital era, issues concerning the fair compensation of creators have plagued various industries from film and academia to music. With the advent of music subscription services in a nascent 21st century, musicians, songwriters and their teams have raised this issue to new prominence.

My thesis seeks to answer whether or not public policy needs to adjust in order to better compensate these musicians, and if this new model of consumption is truly treating them as unjustly as those in the industry like Taylor Swift suggest. By detailing prior recording industry models and analyzing American copyright law using utilitarianism and welfare economics, I argue that the streaming model is a continuation of prior industry practices and models, whereby money is largely siphoned off by groups and corporations, leaving creators with very little in comparison, but that the streaming model is good for musicians and consumers alike. Ultimately, the streaming model is a significant improvement upon the purchase model that dominated the industry in the 20th century.

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INTRODUCTION

Throughout the 2000s decade, the music recording industry lived and breathed by purchases of albums at concerts, in department stores, in coffee shops, and perhaps most critically, online. The industry was amid rapid digitization, but a new incarnation of it was just on the horizon.

On July 14th, 2011, the Swedish music streaming company Spotify launched in the United States, its arrival treated by industry protagonists like that of a horseman of the apocalypse. Record labels began pulling their catalogs from the service in fear of music streaming “cannibalizing” digital and physical sales, motivated by a plethora of songwriter testimonials and articles, perhaps most infamously one that circulated a \$167 payout to Lady Gaga for one million streams of her 2009 hit “Poker Face.”

Just a few months after Spotify’s American debut in 2012, I sat in a classroom during my freshman year of high school listening to music industry aficionado Scott Aiges warn of the new industry reality fast on approach, where consumers would no longer pay for single units of music, but instead pay recurring monthly subscriptions to services like Spotify, *or not even pay at all*. For the many aspiring musicians next to me at the New Orleans Center for Creative Arts, Aiges’ words implied that they would need to adapt to a world that was diverging from the one in which our idols grew up.

With Spotify burgeoning over the next few years, the debate over its royalty payments to musicians and songwriters reached a critical tipping point when in 2014, Taylor Swift pulled her entire music catalog off of Spotify. At the time, Swift was the most streamed artist on the platform. Justifying the move in *the Wall Street Journal*, Swift pinned the decision on her concern with the royalty rates that were being paid to her fellow musicians by the service. In her wake, Swift gave salience to a myriad of questions about the legitimacy of Spotify and music streaming at large, and whether or not musicians would be able to survive off of a business model that paid far less for a play of a song or album than a full purchase of it.

While Swift herself has since returned her music catalog to Spotify, the question persists: is music streaming a sustainable source of income for musicians who are more often than not struggling to make ends meet? Moreover, what can or should policymakers do to respond? My thesis seeks to not only provide the context for this debate but also begin to devise the answers. Chapter 1 details the history of Spotify and the streaming model as well as the digitization of the music industry. Chapter 2 lays out the philosophical justifications for copyright and intellectual property in the United States. Chapter 3 presents the copyright statutes for musical works as well as the music industry structures that have to work with them. Finally, Chapter 4 analyzes the effects of the streaming model in a cost-benefit framework using welfare economics as the lens of doing so. Because

this work ties in concepts and key terms from philosophy, intellectual property, and the music business, a glossary is available at the end of this paper for quick reference.

The research that I am doing is primarily for musicians and those within the recording industry, as they have raised concern about possible inequities and flaws within the Spotify streaming model for the better half of a decade. While they may be the prime audience for this piece, because I am using frameworks and theories from intellectual property and economics to evaluate these concerns, experts in those fields are also within the broader audience of this work. The goal of this thesis is to provide the context necessary for understanding the current debate surrounding streaming royalties and to establish that the recording industry is not in crisis as some have been led to believe.

I. The Spotify Streaming Model

This section seeks to provide the historical context for the rise in prevalence of the streaming model in the United States, from the physical album model in the 20th century, to digital downloads and music piracy that succeeded it in the 2000s and finally to Spotify's formation and dominance in the industry today. In establishing this chronology, I will be setting up an argument for how the streaming model is a continuation of prior industry practices whereby money from royalties is siphoned off from creators and redirected to associated businesses and organizations. That set up will be fully realized in Section III, which concerns industry structures and practices.

I will analyze Spotify in particular based on the following merits: while all other streaming services such as Apple Music and Tidal use variations of the same music-subscription model as Spotify, Spotify is viewed as the pioneer of it and is the streaming platform with the most paid subscribers.¹ While other music subscription services preceded Spotify like Rhapsody and Napster 2.0, Spotify experienced unmatched commercial success upon its arrival and irrevocably altered the American music industry in a way that these other, successive services did not. As the champion of the streaming model, it often garners the most scrutiny from academics and media sources,

¹ Spotify Shareholder Letter Q4 2018. (2019, February 6). 1-13.

making an analysis of it more feasible and appropriate than the other services previously mentioned.

In addition to the above, it should be noted that when referring to streaming services and models, I am referring to *on-demand* streaming services specifically. There are other types of music streaming that are not within the scope of this thesis. These types include streaming radio services like Pandora or iHeart radio, which prevent the listener from choosing which specific songs play but rather let the service determine what to play based on their preferences. This type of service is also referred to as a *non-interactive service*, as it negates a listener's ability to choose specific musical pieces to play. Spotify offers non-interactive radio stations as a part of its services, but it is the interactive streaming that it is most well known for, and that will be the focus of this thesis.

A. Introduction to Spotify

Spotify was founded in Sweden in 2006. The service officially launched in 2008 in a limited number of European countries before reaching the United States in 2011, after inking licensing agreements with the major worldwide record labels. These agreements provided Spotify with access to

label catalogs for negotiated royalty rates, and in exchange, the record labels obtained shares of the company itself.²

Like other streaming services today such as Tidal and Apple Music, Spotify offers two subscription tiers: free, and premium. On its free tier, subscribers have access to Spotify's catalog of music but are forced to listen to albums on "shuffle" when on mobile devices, and are additionally subjected to periodic 30-second advertisements. The premium subscription, by contrast, is approximately \$10 a month and allows users to save music for offline listening, provides access to higher quality streams, and removes the "shuffle" restriction and all advertisements.

Spotify has achieved significant success worldwide: at the end of 2018, Spotify reported that it had 96 million paid subscribers and 207 million total active users across 78 countries, generating nearly \$6 billion in revenue.³ Its users have access to a catalog of 40 million songs covering 2,000 distinct genres, compared to the iTunes store's catalog of 50 million songs.⁴

While the above covers Spotify from the user or consumer's perspective, it is the treatment of artists and copyright holders by this model that has generated the controversy that is the crux of this paper. Recording

² Wikhamn, Bjorn Remneland, and David Knights. "Associations for Disruptiveness – The Pirate Bay vs. Spotify." *Journal of Technology Management & Innovation* 11, no. 3 (2016): 40-49.

³ While the company has generated billions in revenue over the past several years, Q4 of 2018 was the first quarter ever in which the company was profitable. Spotify, *supra* note 1.

⁴ iTunes - Music. (n.d.). Accessed February 4, 2019.
<https://www.apple.com/lae/itunes/music/>

industry protagonists have widely criticized the streaming model from record labels and musicians alike as not sufficiently paying copyright holders. As Rolling Stone author Tim Ingram explained, the Spotify streaming model determines royalty payments as follows:

“Spotify, in accordance with other leading audio streaming services, currently pays money to music rights-holders via a simple ‘pro rata’ model. Essentially, this means that the firm pools all of the distributable riches it generates each month, [and] then divvies up this cash based on the popularity of individual tracks. So, if five Drake songs pull in two percent of all subscriber plays in December, Drake (and the other folks who own rights to those five tracks) will get two percent of Spotify’s user-paid money.”⁵

This “pro rata” model has two unique consequences: first, this model disproportionately concentrates the bulk of its royalty payments to the most streamed tracks and artists. Digital Media Finland found that the .4% most streamed tracks received nearly 9.9% of royalty payments, due in part to the second consequence, that users’ subscription payments do not go directly to the artists they stream, rather their payments are all pooled. Thus, if a user decides they will *only* stream music from Yo-Yo Ma, the distributable portion

⁵ Ingram, Tim. "Should Spotify Change the Way It Pays Artists?" Rolling Stone. December 07, 2018. Accessed February 25, 2019. <https://www.rollingstone.com/music/music-features/should-spotify-change-the-way-it-pays-artists-763986/>.

of their subscription — about \$6.99 — does not go directly to Ma but instead will go to other artists that the user did not stream.⁶

The rise in prevalence of Spotify and the streaming model has been widely cited as instigating the demise of the album purchase or record sale model that commanded the industry ever since the development of vinyl LPs in 1948. While the streaming model's ascent to dominance was so meteoric that it might appear abrupt, it is attributable to the two decades of digitization that preceded it.

B. The Album Purchase Model to Digital Piracy

For most of the 20th century, the recording industry lived on the sales of physical albums in the form of either 12" vinyl LPs or cassette tapes, otherwise known as "analog" formats.⁷ After the advent of the compact disc (CD) in 1982, a new format was then added to this record-purchasing model: the digital format. The premise of the recording industry's business model, however, remained the same as it had been for decades; consumers were buying individual, physical copies of music, distributed at brick and mortar

⁶ *Id.*

⁷ An analog format is one in which "information is stored or represented in the form of some continuously variable quantity: the shape of a record groove, voltage, the position of a magnetic particles on a tape, and so on" (Fisher, 14).

retailers, online webstores, concert venues, etc.⁸ By the late 80s, sales of analog records began to fall while sales of CDs began to rise.⁹ CDs began to overtake their analog counterparts mainly because digital recordings do not degrade over time, whereas analog recordings do.¹⁰ Burned copies of CDs are perfectly identical to their originals, and because CDs are a digital media, they can be compressed into files like the mp3 format and stored on other devices like a computer or flash drive as well.¹¹ All of these qualities led to CDs commercially overtaking its analog equivalents rather quickly — they surpassed sales of cassette tapes by 1991¹² — and sparked concern within the recording industry.

While analog formats of music were previously vulnerable to bootlegging, CDs made the practice far more viable. If one wanted to make a copy of an analog record like a 12” vinyl or cassette tape, they would have used a tape recorder, which creates a distorted copy with an audible “hiss,” i.e., a deteriorated copy. However, CDs, as a digital format, can produce perfect copies, which could be made or “burned” by any consumer with a

⁸ Cohn, D. Y., & Vaccaro, V. L. (2011). The Evolution of Business Models and Marketing Strategies in the Music Industry. *The International Journal on Media Management*, 6(1), 46-58. Retrieved February 26, 2019.

⁹ Fisher, William W. *Promises to Keep: Technology, Law and the Future of Entertainment*. Stanford, CA: Stanford Law and Politics, 2004, at p. 14.

¹⁰ While some audiophiles may argue that analog formats can provide better sound under the right conditions — with the right turntable and speakers, etc. — this is largely situational.

¹¹ Fisher, *supra* note 9 at p. 14-15.

¹² Perry, M. J. (2017, April 30). How CDs have been supplanted by music streaming | Opinion. Retrieved February 26, 2019, from <https://www.newsweek.com/how-cds-have-been-supplanted-music-streaming-588819>

computer, *and* the songs could be downloaded from the CD onto the computer and rapidly distributed over the Internet.¹³ With CDs, the monopoly that record labels had on high-quality reproductions of musical recordings was broken. While the record industry was aware that bootlegging was cutting into profit margins during the analog era – in 1984 the Recording Industry Association of America (RIAA) estimated that the industry lost \$1.5 billion to the practice – they chose not to crack down on it because of the limitations of analog copies, and because consumers were adamant about their right to make them.¹⁴ Digital recording copies, however, presented a new dilemma worthy of a response, and the RIAA began pursuing litigation against illicit mp3 distributors as often as possible.¹⁵ By the time the RIAA stepped in, 165 million songs were being illegally transferred every day.¹⁶

Around the time that the recording industry began to launch its assault on digital piracy, the CD's sharp rise in popularity was being followed by a short-lived reign of commercial dominance. By 2000, the American music saw unit sales of all physical albums, including CDs, decline by 3.7%, a trend that would continue largely uninterrupted to the present day, and one that has echoed across international recording industries as well.¹⁷ Left in the wake were increasing digital downloads for singles – single musical tracks –

¹³ Lam, Calvin K.M., and Bernard C.Y. Tan. "The Internet Is Changing the Music Industry." *Communications of the ACM* 44, no. 8 (August 2001): 62.

¹⁴ Fisher, *supra* note 9 at p. 84.

¹⁵ Lam, *supra* note 13.

¹⁶ In the US or WW? Vroom, G., & Boquet, I. (2014). Spotify: Face the Music. IESE Business School.

¹⁷ Fisher, *supra* note 9 at p. 32.

courtesy of distributors like mp3.com and later iTunes, but also the appearances of services like Napster, Limewire, and the Pirate Bay. These services allowed users to illegally download digital copies of music for free using peer-to-peer technology.¹⁸ These illegal downloads were viewed as a hemorrhaging of potential paid downloads from an industry that was losing revenue for the first time, and thus drew the ire of the RIAA. It is worth mentioning, however, that even legal download services like iTunes were seen as cutting into profit margins as well, as consumers were now opting to buy single tracks from albums that they enjoyed as opposed to the entire record.¹⁹

¹⁸ Peer to peer technology allows one user to download encrypted files from another user's computer.

¹⁹ Covert, A. (2013, April 25). A decade of iTunes singles killed the music industry. Retrieved February 14, 2019, from <https://money.cnn.com/2013/04/25/technology/itunes-music-decline/index.html>.

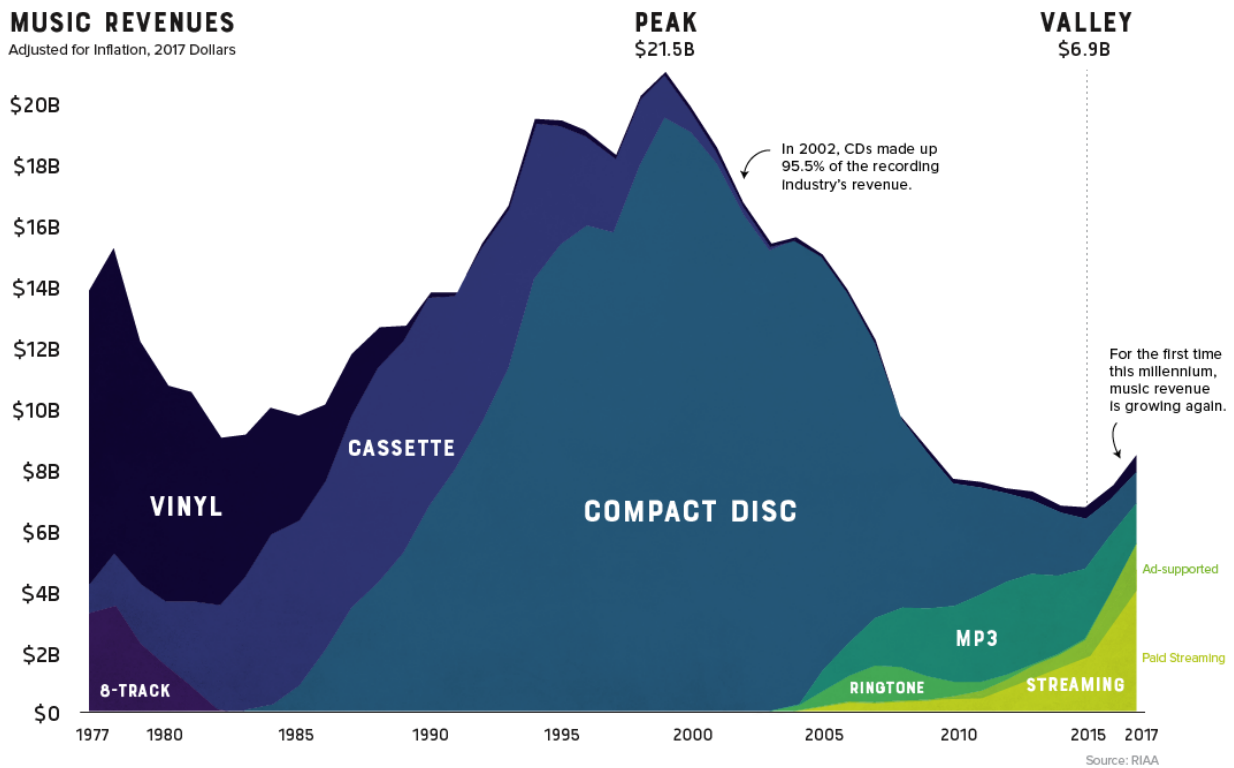


Figure 1: Record Industry revenues over time, with breakdowns based on format. Since 2015 as streaming revenues have begun to rise, industry revenues overall have also been pushed up for the first time in more than a decade. Source: Nick Routley, Visual Capitalist.

Spotify itself is the product of the Internet piracy that undercut the recording industry throughout the 2000s. For example, in its genesis, Spotify used pirated mp3 files instead of officially obtained versions.²⁰ Though music is now streamed directly from Spotify's servers since 2014, before this, songs

²⁰ Jones, Rhett, and Rhett Jones. "Early Spotify Was Built on Pirated MP3 Files, New Book Claims." Gizmodo. May 11, 2017. Accessed February 7, 2019. <https://gizmodo.com/early-spotify-was-built-on-pirated-mp3-files-new-book-1795109991>.

were streamed in a peer-to-peer fashion, similar to torrent technology.²¹ This history is compounded by the fact that Daniel Ek, Spotify's co-founder, was the CEO of µTorrent, a BitTorrent program. Given these ties to digital piracy, Spotify has argued that its merits should not be based on comparisons to digital downloading platforms like iTunes, but rather in comparison to digital piracy; i.e., Spotify contends that it has monetized a consumer behavior — piracy — that previously generated no revenue for the recording industry at all.²²

In the early 2010s, paid digital downloads consisted of as much as 50% of the music industry's entire (shrinking) revenue.²³ In the 16 years between 2000 and 2015, industry revenues declined in 15 of them.

As streaming began to grow exponentially in 2013 and 2014, digital downloads dropped, and with it, music industry revenues bottomed out at a third of 1999 levels, from \$20.9 billion (adjusted for inflation) to \$7 billion in 2013 and 2014.²⁴ Since then, however, industry revenues have been increasing year on year, a trend that did not exist in the digital download era.

Today, with streaming reaching new heights in terms of consumption year after year, music industry revenues have begun to increase as well. In its 2017 report, Nielsen Soundscan noted "Streaming continued its leadership

²¹ Wikhman, *supra* note 2 at p. 44.

²² This contention will be evaluated in a successive chapter, but it is worth mentioning here.

²³ Marshall, Lee. "'Let's Keep Music Special. F—Spotify': On-demand Streaming and the Controversy over Artist Royalties." *Creative Industries Journal* 8, no. 2 (2015): 177-89. doi:10.1080/17510694.2015.1096618.

²⁴ Fisher, *supra* note 9 at p. 75.

over downloads as the dominant music consumption platform of 2017, fueling the music industry's overall volume growth of 12.5% year over year. The increase was led by a 58.7% increase in On-Demand Audio streams compared to 2016.” During the same period, however, total album sales and digital download equivalents²⁵ declined by 19.2%.²⁶

C. Criticisms of Spotify and the Streaming Model

As Spotify and the streaming model it pioneered grew in prevalence in the recording industry, it attracted the criticism of musicians and industry protagonists alike. The first widely publicized criticism of Spotify emerged in 2009, just one year after its official launch when it was reported that after 1,000,000 streams of her single “Poker Face,” Lady Gaga received just \$167 from the service.²⁷ Though the figure was misleading,²⁸ the idea that Spotify did not compensate copyright owners fairly stuck, and by 2011, independent record labels had begun withdrawing their catalogs from the service. One of those labels was Projekt Records, and in a public statement, Projekt founder Sam Rosenthal wrote: “In the world I want to live in, I envision artists fairly

²⁵ 10 digital track downloads are considered by the RIAA, Nielsen Soundscan, and *Billboard* to be the equivalent of 1 album.

²⁶ *2017 Year End Music Report*. Report. Nielsen Music. 1-33.

²⁷ Marshall, *supra* note 23 at p. 5.

²⁸ *Id.*

The figure was misleading as it only reflected Gaga's publishing royalty (for a song on which she had additional co-writers) after deductions from her streams in Sweden.

compensated for their creations...Spotify is NOT a service that does this. Projekt will not be part of this unprincipled concept.”²⁹ Similarly, in announcing they were also withdrawing their catalog from on-demand streaming platforms, metal record label Century Media wrote: “This is about survival, nothing less and it is time that fans and consumers realize that for artists it is essential to sell music to keep their heads above water.”³⁰ Numerous other labels echoed these sentiments, including Prosthetic Records, Metal Blade, and Sumerian Records, whom all withdrew from Spotify by the end of 2011.³¹

The issue of compensation reached a zenith in salience in 2014, as Country and Pop superstar Taylor Swift announced that she would be withdrawing her entire personal catalog from the service.³² At that time, Swift was the most listened to artist on Spotify.³³ In a *Time Magazine* interview, Swift specified that the removal was not in response to the streaming model as a concept, rather that Spotify offered a free tier which doles out significantly lower royalties than its paid equivalent: “With Beats Music and Rhapsody you have to pay for a premium package in order to access my albums. And that places a perception of value on what I've created.

²⁹ Marshall, *supra* note 23 at p. 5.

³⁰ Marshall, *supra* note 23 at p. 5.

³¹ *Id.*

³² Her record label at the time, Nashville’s Big Machine Records, did not remove its catalog, rather this was a decision made by Swift herself.

³³ Rosenstein, Ariel. "How Did Taylor Swift Affect Spotify." SimilarWeb. April 25, 2016. Accessed February 26, 2019. <https://www.similarweb.com/blog/what-does-the-taylor-swift-v-spotify-fallout-mean-for-music>.

On Spotify, they don't have any settings or any kind of qualifications for who gets what music.”³⁴ In an op-ed for *The Wall Street Journal*, Swift underpinned this argument with another: that music and art should be paid for. Swift wrote,

“Music is art, and art is important and rare. Important, rare things are valuable. Valuable things should be paid for. It’s my opinion that music should not be free, and my prediction is that individual artists and their labels will someday decide what an album’s price point is. I hope they don’t underestimate themselves or undervalue their art.”³⁵

Numerous other musicians have echoed Swift’s argument that Spotify’s compensation model is disrespectful to artists as well: Icelandic singer Björk told *Fast Company* that she believes “This streaming thing just does not feel right. I don’t know why, but it just seems insane. ... To work on something for two or three years and then just, 'Oh, here it is for free.' It's not about the money; it’s about respect...”³⁶ Thomas Yorke of Radiohead fame infamously referred to Spotify as “the last desperate fart of a dying corpse,” in

³⁴ Engel, Pamela. "Taylor Swift Explains Why She Left Spotify." *Business Insider*. November 13, 2014. Accessed February 20, 2019. <https://www.businessinsider.com/taylor-swift-explains-why-she-left-spotify-2014-11>.

³⁵ Linshi, Jack. "Taylor Swift: Why Taylor Swift Pulled Her Music From Spotify." *Time*. November 03, 2014. Accessed February 21, 2019. <http://time.com/3554468/why-taylor-swift-spotify/>.

³⁶ Kreps, D. (2018, June 25). Bjork on Spotify: 'It Just Seems Insane'. Retrieved February 26, 2019, from <https://www.rollingstone.com/music/music-news/bjork-keeping-vulnicura-off-spotify-it-just-seems-insane-59159/>.

reference to the recording industry.³⁷ Speaking to Mexican media outlet

Sopitas, Yorke stated:

“I feel like as musicians we need to fight the Spotify thing. I feel that in some ways what’s happening in the mainstream is the last gasp of the old industry. Once that does finally die, which it will, something else will happen. But it’s all about how we change the way we listen to music, it’s all about what happens next in terms of technology, in terms of how people talk to each other about music, and a lot of it could be really fucking bad. I don’t subscribe to the whole thing that a lot of people do within the music industry that’s ‘well this is all we’ve got left. we’ll just have to do this.’ I just don’t agree.”³⁸

While in the end, Swift’s move, in particular, did not have a direct, attributable economic effect on Spotify; it further raised the profile of these anti-Spotify arguments from within and outside of the recording industry. Spotify competitor Apple Music even increased its royalty payments during its free trial periods specifically to appease Swift.³⁹ Furthermore, Swift, along with many of the labels mentioned above, have since returned their catalogs to the service.⁴⁰

³⁷ Renshaw, David. "Thom Yorke Labels Spotify 'The Last Desperate Fart of a Dying Corpse'." NME. October 04, 2013. Accessed March 31, 2019. <https://www.nme.com/news/music/radiohead-154-1246066>.

³⁸ *Id.*

³⁹ "Apple Music Changes Policy after Taylor Swift Stand." BBC News. June 22, 2015. Accessed February 21, 2019. <https://www.bbc.com/news/entertainment-arts-33220189>.

⁴⁰ Marshall, *supra* note 22 at p. 7.

Swift has, however, delayed releases of subsequent projects on Spotify, such as her sixth studio album *Reputation*, which appeared on Spotify a month after its release for physical and digital purchase.

II. Theoretical Foundations of American Copyright Law

Before introducing the specific statutes involved with music copyright and royalties in the United States, the philosophical foundations of American copyright law will be established so that the policy recommendations provided at the end of this paper are theoretically consistent with the current law, and are thus more viable. The objective in this section is to establish both the underlying theoretical and philosophical concepts needed to evaluate American copyright policy, and also to introduce the intellectual property concepts that illuminate and contextualize the current debate encompassing the merits of the streaming model.

Most, if not all creative or expressive works — which includes music — have the same two features: the first being that once they are distributed to one individual, it is difficult if not impossible to limit their dissemination to others, i.e., they are *nonexcludable*. The second feature is that the enjoyment of these goods by one individual does not directly affect their enjoyment by another, the quality known as being nonrival or *nonrivalrous*.⁴¹ Beyond these two features, expressive works are also significantly cheaper to reproduce than to produce originally, which means that in a world without copyright, simply copying a work is more financially advantageous than creating one, which may deter potential creators from creating at all.

⁴¹ Bracha, O., & Syed, T. (June 2014). Beyond the Incentive — Access Paradigm? Product Differentiation & Copyright Revisited. *Texas Law Review Association*, 92(7), page 1848.

The law seeks to remedy this dilemma by giving the creator of a work the ability to *exclude* others from copying their work, while also attempting to provide as much access as possible, given that these works are nonrivalrous by nature and copyright has to place some limits on access in order to incentivize creators.⁴² This push and pull known as the incentives-access paradigm is what frames economic debates around intellectual property,⁴³ with the controversy around Spotify being no exception.

A. Justification of Copyright

Though the founding fathers and numerous Presidents – among them Thomas Jefferson and Abraham Lincoln – subscribed to the Lockean view of intellectual property as a natural right,⁴⁴ the Copyright Clause in section Article I Section 8. Clause 8 of the constitution nevertheless provides a utilitarian rationale. The clause grants Congress the power “To promote the progress of science and useful arts, by securing for limited times to authors

⁴² When modifying copyright, lawmakers work to keep access in mind as these creative works would have no limits on access in a world without copyright, given that it is difficult to exclude their use and not useful to do so given that they are nonrivalous. Legislators strive to maximize access, as it is perhaps *the* ideal feature of creative works that they can be shared by all equally.

⁴³ Bracha, *supra* note 41 at p. 1848.

⁴⁴ Abraham Lincoln, Speech at Chicago, Illinois, in 2 Collected Works of Abraham Lincoln 493 (R.P. Basler et al. ed. 1953), “each individual is naturally entitled to do as he pleases with himself and the fruit of his labor.” Letter from Thomas Jefferson to Isaac McPherson (August 13th, 1813), in 13 The Writings of Thomas Jefferson 326, “That ideas should feely spread from one to another over the globe... seems to have been peculiarly benevolently designed by nature.”

and inventors the exclusive right to their respective writings and discoveries,”⁴⁵ propelling the notion that copyright’s purpose in the United States is to provide incentives to creators and maximize social good, in line with utilitarian reasoning.

As many scholars in the field of intellectual property and lawmakers have argued, the utilitarian approach is the most popular (and familiar) approach for justifying and understanding copyright law and intellectual property within the United States.⁴⁶ Utilitarianism “requires lawmakers to strike an optimal balance between, on one hand, the power of exclusive rights to stimulate the creation of inventions and works of art and, on the other, the partially offsetting tendency of such rights to curtail widespread public enjoyment of those works” in order to maximize social welfare or utility.⁴⁷

In order to provide a financial incentive for authors to create, utilitarian theory introduces the concept of copyright, which allows a creator to exclude others from reproducing their work, distributing copies of it, or from preparing a derivative work on it for a given period of time. These legal exclusions increase the opportunity for creators to recoup their investment by sanctioning those who seek to profit from their works without the copyright

⁴⁵ U.S. Const. art. I, § 8.

⁴⁶ Fisher, *supra* note 9 at p. 1; Harper & Row, Publishers v. Nation Enters., 471 U.S. 539, 558 (1985), Fromer, J. C. (December 2012). Expressive Incentives in Intellectual Property. *Virginia Law Review*, 98 (8), 1745-1824. Retrieved March 2, 2019.

⁴⁷ Fisher, *supra* note 9 at p. 1.

holder's consent.⁴⁸ While artistic works are nonexcludable and nonrivalrous by nature, copyright works to cancel out these qualities; while being able to exclude others from distributing a creative work is the primary purpose of copyright, it creates drag by making these works rivalrous.

As mentioned above, creative works are nonrivalrous by nature, which is not true of other forms of property. For example, one can share a digital music file with as many people as possible, and one person's enjoyment of that work is not affected by someone else's use or enjoyment of that same music file. This is different than from one, for example, sharing an apple with his or her friends: there is only so much enjoyment that each person can have of that apple before it is gone. By making creative works excludable, copyright places limits on who is able to enjoy a work, which works against their naturally nonrivalrous nature, perhaps the most desirable feature of creative works.

To illustrate how copyright does this, let us imagine a world in which there is no copyright, and that I have just recorded an album. I have put in thousands of dollars into the creative process — paying for time in a recording studio, and compensation for sound engineers, musicians, etc. — and after its completion, I release the album for a simple, one-time purchase on my website.⁴⁹ Within hours, download links begin to sprout across the Internet, all of which allow a user to download my album for free. Without

⁴⁸ *Supra* note 39.

⁴⁹ We're assuming that I am not using a distributor who would cut into my profit margins from my album.

copyright, I have no legal recourse to remove those download links, and I now stand little chance of recouping my financial investment into my album, as potential buyers of my work are instead downloading it for free. There is, therefore, no incentive for me to continue to create; after all, I spent thousands to create my work while others are downloading it for free and the costs to copy it thereafter are nominal.⁵⁰ From a financial perspective, why would *any* creator continue to pursue works of intellectual property when they could copy another's work for significantly less, or turn toward a more lucrative career?⁵¹ Copyright could remedy this predicament by allowing me to exclude others from copying and distributing my work for a limited duration, increasing my chances of recouping my investment, and therefore giving me the incentive to create.

In the scenario above, copyright provides incentive, but it also limits access. Let's say that my copyright now offers me sweeping protections, so much so that I am able to recoup not just the cost of my investment into the creation of my work, but maximize my possible profits from it. This broad copyright protection inherently limits the public's access to my work by giving me the power to price my works so that some people cannot or will not

⁵⁰ As illustrated by this example and the prior discussion on bootlegging analog copies of sound recordings, the digital era has significantly compounded the disparity between the costs of creating and the costs of copying.

⁵¹ Fisher, *supra* note 9.

A creator may continue to create if they do not mind losing their investment into the product, such as an amateur painter or someone who creates as a hobby out of passion, but the concern here is for those who wish to make a career out of creative expression.

pay the price that I have set. This group of people is now inhibited from the use of the works that I have created and thus causes limitations on access, given that one individual's enjoyment of a work does not affect any other's enjoyment of the same work. After all, from the perspective of static use, the limiting of public access is only a consequence of copyright. As creative works are nonrivalrous, limiting the public's ability to use these works only hinders one of the great, inherent features of those works.⁵² These short anecdotes are used to illustrate the fact that copyright cannot create a world in which access and incentives are both operating at 100%.⁵³

Copyright itself, however, builds its own paradox: by limiting public access, it also limits the creation of new creative works. Expressive works to greatly varying degrees rely on the creative works and ideas before it,⁵⁴ so by excluding some potential consumers who would not be detracting from other's enjoyment of the work,⁵⁵ copyright has also constricted future innovations

⁵² Bracha, Oren. "Give Us Back Our Tragedy: Nonrivalry in Intellectual Property Law and Policy." *Theoretical Inquiries in Law* 19, no. 2 (2018): 633-70 at p. 647.

⁵³ We can imagine other solutions to this predicament, however: the government could provide grants to provide incentives like they do with academic research, or subsidize the costs of my production. However, the possible effects of these solutions are outside the scope of this particular project, and are seen from the utilitarian perspective as using more social resources than they would otherwise save.

It is also worth noting that time limits on copyright – in addition to the scope of the copyright – serve to balance the relationship between access and incentive. Fisher, *supra* note 9, at p. 2.

⁵⁴ To illustrate this in an exaggerated manner, it would be very difficult for one to create a musical work if they had no access to the music of others whatsoever.

⁵⁵ Bracha, *supra* note 36, at p. 1850.

based on copyrighted creative works. For example, consider a nascent world with very strong copyright protections: successive copyright protections on top of this would chill the creation of new works. Copyright would never completely freeze creation, but you get more cost than benefit to creation at a certain margin where it would begin to slow. The paradox that emerges here is that copyright hinders the development of future expressive works when part of its purpose is to provide an incentive to create these works to begin with.

In short, the primary takeaway from the above normative perspective is that there are two particular inefficiencies of copyright as a solution to the incentive problem: 1) static deadweight loss, which is the limiting of public consumption that would not occur were copyright not to exist, and 2), dynamic deadweight loss, the limitation of access which creates a drag on future innovation. If we are to accept copyright as the proper solution to the incentives-access problem — which, for the purposes of this thesis, we are — then it suffices to say that there must be an optimal balance between these two forces, where drag is minimized, and incentives are maximized.⁵⁶

⁵⁶ Day, Brian R. "In Defense of Copyright: Creativity, Record Labels, and the Future of Music." *SSRN Electronic Journal*, 2011. doi:10.2139/ssrn.1609689. As determined in *Mazer v. Stein*, 347 U.S. 201, 219 (1954) and *Eldred v. Ashcroft*, 537 U.S. 186, 212 n.18 (2001), the Supreme Court has determined that intellectual property rights ensure the progress and development of not just the arts but the sciences as well in order to "enrich the public domain." A concern that may arise from this discussion is the delegating upon the government the power to incentivize certain behavior. From a libertarian perspective, if we do not want the government to censor or prohibit certain civic activities, why would we allow the government to incentivize them? Copyright, much like freedom of speech in the United States, is content neutral; all creative works are entitled to copyright protections much like any person's speech is

It is ultimately up to policymakers to find this marginally optimal balance, and unfortunately for them, the information required to find this harmony is impossible in practice. If lawmakers had infinite information, they could seek to provide enough IP rights to each individual creator so that he or she would have exactly enough incentive to continue creating and no more.⁵⁷ Instead, they have to issue one, universal standard of copyright based on their cost-benefit estimations that leaves some creators unable to cross the line of having enough incentive, and others well past it. The question, therefore, for lawmakers when making adjustments to intellectual property rights is whether or not providing more copyright protections would help enough creators cross the incentive line to outweigh its restrictions on public access. At some point, the copyright policy reaches the marginal tipping point where the balance between incentives and access is equal, and no further adjustments are necessary.

In an attempt to mediate the relationship between incentives and access as well as the paradox above, copyright laws are constrained in both

protected so long as it does not infringe upon another's rights. While there is a tension between freedom of speech and copyright as copyright does exclude some from accessing a work, both concepts were enshrined in the Constitution by the Framers at the same time. Copyright protections are ultimately used to generate more content, regardless of its content, in the same manner that freedom of speech rights are used to promote speech regardless of its content as well.

⁵⁷ In an economist's view, a creator would never reap all of the potential value of their copyrighted work, but copyright should aim to give them just enough incentive to create, which in a simplified world would be one in which they break even from their initial investment. The more accurate version in a world with unlimited information would be one where copyright ensures that one creates instead of going for alternatives like pursuing a career in stock brokering, for example, but of course, this is not feasible in practice.

duration and scope. The duration of copyrights in the United States varies depending on the circumstances of creation,⁵⁸ while the scope of copyright protection is constrained in order to facilitate the production of new works. For example, if someone wanted to record a parody version of my album, wide-ranging copyright protections may prevent him or her from doing so, while more narrow protections would allow this to take place.

B. Critiques of and Concerns With Utilitarianism

At this point, a few problems with the utilitarian approach should be made apparent, albeit without getting too bogged down in them. For example utilitarianism is a demanding theory when applied to ethics: for example, “if a doctor can save five people from death by killing one healthy person and using that person’s organs for life-saving transplants, then act utilitarianism implies that the doctor should kill the one person to save five.”⁵⁹ In this

⁵⁸ As the U.S. Patent and Trademark Office describes, “The duration of copyright protection depends on several factors. For works created by an individual, protection lasts for the life of the author, plus 70 years. For works created anonymously, pseudonymously, and for hire, protection lasts 95 years from the date of publication or 120 years from the date of creation, whichever is shorter.” The durations of copyright have also been subject to change over time. *Trademark, Patent, or Copyright?* U.S. Patent and Trademark Office, <http://www.uspto.gov/trademarks-getting-started/trademark-basics/trademark-patent-or-copyright>

⁵⁹ “Act utilitarianism” is the ethical application of utilitarianism whereby a person is only acting in a morally righteous way if and only if his or her actions produce the best possible results in a given scenario, i.e., the most good for the most number of people.

scenario, utilitarianism coerces its followers into killing another person for the sake of benefitting the majority, theoretically creating a society in which doctors are killing bystanders for the sake of harvesting their organs for those who need them.

Utilitarianism is additionally not concerned with the distribution of states of pleasure, but rather what the total sums of that distribution are. For example, if the consequence of a given action generates happiness for all members of a society except for one, then that one person's considerations are effectively rendered moot.⁶⁰ They would therefore be subject to the "tyranny of the majority."

The greatest flaw of utilitarianism for our purposes however, is that utilitarian theory poses here is that there is no method for determining which legal arrangement generates the *most societal good*, as measured in an ideal theoretical world by generating a sum for all individual states of pleasure or benefit in a group and measure that against a sum for all states of displeasure or detriment. But of course, in practice, this is more intractable, and issues arise from this definition. While it is clear that utilitarianism tries to balance the oscillation between incentives and access to maximize social welfare, the values that it assigns to each force is imprecise at best.

Utilitarianism thus requires a nebulous calculus to contrast the total net social welfare that different solutions offer to the incentives-access problem.

Nathanson, Stephen. "Act and Rule Utilitarianism." Internet Encyclopedia of Philosophy. Accessed March 31, 2019. <https://www.iep.utm.edu/util-a-r/#SH3b>.

⁶⁰ *Id.*

These weaknesses do present a problem for lawmakers trying to offer a solution to the incentives-access paradigm (and others), but for the purposes of this analysis, the utilitarian framework is useful and insightful in evaluating the costs and benefits of the streaming model. While this framework requires infinite information for policy making — which we will of course never be able to obtain — what it can be used for instead is deriving guidelines for public policy by making rough predictions on the effects of certain actions. Given that American copyright law sits upon a utilitarian foundation, justifying a public policy adjustment toward music streaming in utilitarian terms is consistent with this foundation. Not only this justification, but utilizing this approach will place my proposal within the American IP discourse at large, as utilitarianism is, as previously mentioned, the framework of choice by academics.

For this paper, I will be using the economic equivalent of utilitarianism known as welfare economics for evaluating the streaming model. Whereas utilitarianism is concerned with the maximization of states of pleasure or utility and minimizing harm or pain, welfare economics seeks “the economic state that will create the highest overall level of social satisfaction among its members” as measured by wealth or money.⁶¹ Utilitarianism does not have a way of measuring states of happiness against those of pain, which makes the framework difficult to apply in that manner.

⁶¹ Kenton, Will. "Welfare Economics." Investopedia. March 12, 2019. Accessed March 25, 2019. https://www.investopedia.com/terms/w/welfare_economics.asp.

By contrast, welfare economics measures these states or utility in money, which solves this particular issue.⁶² In performing a cost-benefit analysis of Spotify, I will, therefore, be using money as the means of calculating the impact on incentives vs. access. However, welfare economics inherently introduces another litany of issues, such as the exclusion of some groups from these calculations, which are further addressed in Section IV.

⁶² Because utility is abstract and impossible to measure, for my purposes we are defining money — one's willingness and ability to pay for something — as a measure of utility and the states of pleasure and displeasure. Within welfare economics, the market assigns negative and positive values to a given product or arrangement by using money.

III. Musical Copyright and Industry Structures

In order to proceed with this essay, it is crucial that the reader understand some of the fundamental pieces of both the legal frameworks that govern the music industry, as well as how the industry operates in practice in the United States. Many different tangents may arise in attempting to establish this overview; however, the only topics elaborated on here will concern the streaming model. Other valid and compelling discussions on, for example, music sampling, are outside the scope of this document and thus will not be covered in-depth.

A. Two Musical Copyrights

Every musical piece is entitled to two copyrights in the United States once it is fixed in a tangible medium:⁶³ copyright for the underlying composition of a song, and the second for a sound recording. The first copyright, for composition, is for the *songwriter or composer*. The melody, rhythms, and instrumental arrangements would all fall under this type of copyright, essentially encompassing a song as it would be recorded on sheet music. The second copyright, for a sound recording, is for the *recording artist*. Their performance of a song as recorded by microphones (and potentially

⁶³ A tangible medium is a physical manifestation of a musical work like a CD or hard drive with an MP3 file, or a set of instructions for its recreation in the absence of its creator, such as sheet music.

further mixed and mastered by producers) functions under a *separate* copyright than the songwriter's.

To illustrate this difference, let us consider the case of a cover recording. In 1970, the Jackson 5 released their hit single "I'll Be There" through Motown Records. The song was written by Berry Gordy et al., and performed by the Jackson 5. Therefore, Berry Gordy would (theoretically) own the copyright for the composition of the song, while the Jackson 5 and Motown Records would own the copyright for their specific recording of that composition. When Mariah Carey recorded and released the song in 1992 as a part of her *MTV Unplugged* set through Columbia Records, Berry Gordy et al. still owned the copyright for the composition of Carey's cover, while Carey and Columbia maintained the copyright of her recorded performance. The Jackson 5 were entitled to no legal rights to any part of Carey's recording, as they did not write the song, even though they indisputably popularized it. If one were to stream either the Jackson 5 or Mariah Carey's version of the song on Spotify, he or she would be streaming musical works in which both composition and recording copyrights are present⁶⁴.

It is important to note that the copyrights for a musical composition and an audio recording are not equal in scope; the copyright for a sound recording affords much narrower protections. If one were to go into a studio and record a cover of the Beatles' "Hey Jude" and attempted to mimic every

⁶⁴ 17 U.S.C. § 1101(a)(2) (1998).

growl, distortion and pitch fluctuation in Paul McCartney's vocal in the original recording as possible, it would not be an infringement of the audio recording copyright. An audio recording's copyright is only violated in the case that the *exact* fixed sounds in the recording are used without permission of the copyright holder. Simply emulating those sounds does not constitute an infringement. However, the copyright for a musical composition *is* infringed upon in the case that one tries to imitate it.

B. Copyright Protections

As seen above, each of these copyrights provides different and similar types of protections and rights. Every copyright in the United States affords the owner certain liberties, which will be covered here, using music industry cases as examples. In this section, the rights described are more theoretical than practical: exceptions to the rights described here will be discussed in the following section of this chapter.

First, copyrights provide the owner with the exclusive right to control the reproduction of their work. In the music industry, musical compositions are reproduced as phonorecords, which are defined as “material objects in which sounds ...are fixed ... and from which the sounds can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a

machine or device.”⁶⁵ Composers can, for example, decide who can sell their work in phonorecords as sheet music, and audio recording copyright holders may choose in which format their recordings are manifested. Phonorecords of a recording contain both an underlying composition and a specific recording of a song, and thus both copyright owners are entitled to protections and rights of it.⁶⁶

Copyright owners may additionally decide who distributes their work. This second right is separate from reproduction: for example, a manufacturing plant reproduces a work in a phonorecord such as a CD or LP, whereas a record label distributes these copies. The entity that reproduces a musical work is not always the one that distributes or sells it. The copyright owner may choose who has the right to distribute their works.

The third and final right necessary to know for our purposes⁶⁷ is the right to public performance. As a composer, one has the right to choose when and where someone may publicly perform his or her work. If one were to happen upon a street performer in Times Square covering their composition, they would have the right to stop that performance (or, by the same function, to let it continue). This public performance right extends not just to live

⁶⁵ *Id.* § 101 (“phonorecords”).

⁶⁶ Reese, R. Anthony. “Copyright and Internet Music Transmissions: Existing Law, Major Controversies, Possible Solutions.” *SSRN Electronic Journal*, 3rd ser., 55, no. 2 (January 1, 2001): 237-73, at p. 241, 242.

⁶⁷ There are two other distinct rights for copyright holders that exist but are not relevant for our discussion: the right to make a derivative work, and the right to display a work publicly. The former in the context of the music industry would concern the use of “sampling,” while the latter would apply to websites that display lyrics of a song.

performances, but “performances” of a sound recording as well, however, the public performance right in this case is very narrow. AM/FM radio transmissions, for example, are exempt from the public performance right; however, Congress determined that there is a public performance right for digital transmissions of a sound recording over satellite radio and Internet radio.

Of course, no one copyright owner can police every public avenue for public performances of their songs. Instead, they sign deals with Performance Rights Organizations (PROs), which, in the US, mainly consist of BMI, ASCAP, and SESAC, which will do this policing for the composers. More elaboration on the role of PROs will follow in later sections of this paper.

C. Compulsory Licenses

Of course, none of these rights is as unambiguous as presented here. Numerous exceptions and exemptions mediate these rights. While it is not necessary to elaborate on each of these for the scope of this project, there are a few which are important to understanding the context and debate surrounding music streaming in the United States.

The first is the idea of a “compulsory license,” in which an activity which would ordinarily infringe upon one’s copyrights is legally permissible if the actor pays a fee or royalty as determined by the federal government, and

abides by further rules and restrictions⁶⁸. In these cases, a copyright owner is forced to yield his or her work to the public and is not given the authority to charge his or her own fee or rate for this use.

A musical copyright owner is only compelled to issue a license in this manner if *all* of the following conditions are met:⁶⁹

1. The musical work is classified as “non-dramatic”⁷⁰
2. It has been previously recorded
3. This recording has been distributed publicly
4. The new recording does not change the character or melody of the song
5. The new recording is only used in phonorecords

The “previously recorded” clause affords a copyright owner the right of “first use.” The copyright owner is allowed to determine how they want to the public to first be exposed to their song. The third condition — public distribution — closes a loophole so that if an artist records a song and doesn’t choose to release it that the compulsory license is not triggered.⁷¹

⁶⁸ Fisher, *supra* note 9 at p. 41.

⁶⁹ Passman, Donald S. *All You Need to Know About the Music Business*. 9th ed. New York, NY: Viking, 2015, at p. 230.

⁷⁰ It is not clear what qualifies a song as “non-dramatic”, but is thought of as excluding compositions in dramatic performances such as operas or musicals.

⁷¹ Songwriters often circulate their works to various recording artists within the music industry. For example, Lady Gaga wrote the 2009 song “Telephone” and offered the track to Britney Spears, who then recorded it. After Spears decided not to release it, Lady Gaga publicly released her recording of the song instead. Spears’ initial recording did not open the floodgates for anyone else to record and release the song as he or she pleased because of this provision, though Gaga’s did.

The fourth provision allows one to rearrange a song to fit his or her “manner of interpretation,” but would prevent someone like “Weird Al” Yankovic from obtaining a compulsory license to take one’s musical piece and parody it.

The fifth condition is where the issue becomes more opaque than the previous: here, phonorecords only refers to audio recordings. This clause is the result of successful lobbying from music publishers for the 1976 Copyright Act. The consequence of it is that home video devices — most infamously a VCR and DVD player — do not count as phonorecords, so motion picture companies must negotiate with copyright owners for the usage of their musical works.⁷² Phonorecords do, however, apply to digital downloads known as DPDs (digital phonorecord delivery), such as those from iTunes.

If the above conditions are satisfied, one may file notices the copyright office and begin issuing payments for their usage. Under a compulsory license, the copyright holder is paid at the “Statutory rate,” which is set by the United States Copyright Board. At present, the mechanical royalty rate⁷³ — i.e., the rate for producing a copy of a song — is set at 9.1 cents or 1.75 cents per minute of the musical composition, whichever is greater. The statutory rate is re-certified by a panel of three judges every two years with

⁷² Passman, *supra* note 55.

⁷³ This may also be shorthand as “mechanicals.” The name derives from the practice of music publishing companies in the early 1900s using a piano-roll to reproduce a musical work.

the input of industry protagonists but has not increased from its current rate since January 1st, 2006.⁷⁴

The most notable case where a compulsory license is used is concerning the public performance right. Digital Radio stations in the United States – in compliance with the Federal Communications Commission (FCC) – have compulsory licenses; meaning that they can play (or “perform”) any publicly released sound recording whenever they please. This rule holds for satellite (XM) and Internet radio stations (ex. Pandora).⁷⁵

Otherwise, compulsory licenses are not used often. Record companies would prefer to track these licenses themselves than hand them off to bureaucrats. However, the mechanical royalty is pivotal in the industry because it is the maximum that anyone would be willing to pay for the use of the work.⁷⁶

The government’s sole justification and legal basis for the creation of the compulsory license was to prevent the formation of a monopoly.⁷⁷ In the United States, the compulsory license emerged in music as a result of the Supreme Court decision *White-Smith Music Publishing Company v. Apollo Company* (1908) and its subsequent undermining by the US Congress: while

⁷⁴ A timeline of the mechanical royalty rate can be found here: https://www.harryfox.com/license_music/what_mechanical_royalty_rates.html

⁷⁵ AM and FM radio transmissions do not implicate sound recording performance rights because there is no entitlement; compulsory licenses kick in with digital audio transmission where this *is* a limited entitlement.

⁷⁶ Passman, *supra* note 55 at p. 233.

⁷⁷ 7(d): “The danger of a monopoly in the situation existing in 1909 was apparently the sole reason for the compulsory license.”

the Supreme Court ruled that sheet music was not a copy of a composition (rather parts of a piano roll),⁷⁸ Congress superseded this decision by passing the Copyright Act of 1909, which recognized a right to create mechanical reproductions, and also created the compulsory mechanical license (and thus the mechanical royalty rate).

At the time, the piano roll firm the Aeolian Company dominated the industry and stood to gain enormously from this additional right. To mediate the concerns of smaller firms, Congress added the compulsory license. The consequences of the license, however, reached far beyond its intended effect. The fears of an Aeolian monopoly may have been unfounded, as numerous competitors to the Aeolian Company sprouted after the Copyright Act, which neutralized the initial rationale for the license. However, something else occurred: record labels became reliant on the license, and their influence has kept the compulsory license in effect ever since. The Copyright Act of 1976 and subsequent legislation eventually replaced this Act, but the compulsory license remains as a result.⁷⁹

Copyright owners⁸⁰ object to the compulsory license because it strips them of their agency to set their own rates and control the audio distribution of their works. They have a legal basis for revoking the license as well: as

⁷⁸ 209 U.S. 1 (1908).

⁷⁹ Merges, Robert P. "Errata: Contracting into Liability Rules: Intellectual Property Rights and Collective Rights Organizations." *California Law Review* 84, no. 2 (October 1996): 1293-393, at p. 1308-1310.

⁸⁰ As will be described in the next section of this chapter, copyright owners in this case mainly refers to composers and music publishing companies.

there is no longer a threat of monopoly in the music industry, the compulsory license is no longer justified. A 1961 Congressional report laid out the points arguing for the license's benevolence:

“(1) It provides the public with a variety of recordings of any particular musical work, which might not be true if the copyright owner could give an exclusive license to one record company.

(2) It enables smaller record companies to compete with the larger ones by offering other recordings of the same music.

3) It benefits authors and publishers by giving their works public exposure through several different recordings, thereby increasing their revenue from royalties.”

The report then, however, eviscerated this line of thinking, recommended that the compulsory license be eliminated. The report pointed out that the music industries of countries without compulsory licenses grew just as much as that of the United States, and that while exclusive licenses would reduce the frequency of multiple recordings of the same song, it would thereby pressure record companies to make more copies of *different* songs.

Revoking the mechanical license now would perhaps have an effect beyond forcing record labels to potentially pay rates beyond the mechanical rate: if every musical copyright owner had the right to negotiate their own

rates and fees, there would be an infinite web of negotiations between different parties at all times, and the industry may grind to a halt.⁸¹ This dilemma could, however, be remedied in the case that the statute was revoked by leaving its provisions in place long enough for the industry to adjust.⁸²

This aspect of copyright raises an important question: can the value of the public's access to an artist's work outweigh the benefit of giving an artist complete autonomy over their creation? If so, how should these competing interests be balanced in the eyes of the law? This dilemma has been present since the dawn of copyright law and is especially prevalent in the digital age where access to artistic material is widespread, and the cost of this access is nominal. Additionally, this question is consistently raised by artists in objection to the streaming model and will be evaluated in the final chapter of this paper.

D. Industry Structures

With the essential legal frameworks of the United States established, it is necessary to know the relevant actors — organizations, businesses, and institutions — that have established themselves within the music industry. This background will not be all-encompassing: as the issue at hand is

⁸¹ Fisher, *supra* note 9 at p. 42.

⁸² The 1961 Congressional report recommends a one-year transition period as being sufficient.

royalties from music streaming services, this section will lay out how money trades hands within the music industry under copyright law, and how a check from a company like Spotify would eventually reach a musical artist. Because of this, there will not be an in-depth discussion concerning, for example, synchronization licenses in movies and television.

To begin, we will start with a songwriter and one of their (likely many) copyrighted works. As mentioned briefly on page 6, a songwriter cannot realistically monitor every possible avenue for violations of their copyright, nor negotiate with every interested party like a record label or movie production company usage of their material. Instead, what is most common within the music industry is for a songwriter to assign or split their rights with a *music publishing company*. Each contract with a music publisher and an artist is, of course, different depending on numerous factors such as their relationships within the industry and their knowledge of it, but one's copyright is divisible,⁸³ and songwriters most often allocate more of these rights to a publisher than less of them. A standard deal would entail splitting royalties from the copyright 50/50.⁸⁴ In return, a publishing company can offer to promote the copyrighted work and possibly offer a monetary advance in exchange for the various rights described in the previous section. The publishing company will be able to reap royalties from the copyright, which

⁸³ Fisher, *supra* note 9 at p. 47.

⁸⁴ Passman, *supra* note 55 at p. 236.

encourages them to promote the work — and thus the songwriter — to generate more revenue from it.

Promotion for the music publisher would entail issuing reproduction licenses to sheet music printers, synchronization licenses for movies and television shows, as well as arranging the first commercial recording of the composition. Many artists in the music industry write and record their music, but still many rely on songwriters to compose great works for them. In the case that a composer or songwriter wishes to make the first commercial recording of their work, this would be referred to as a “controlled composition.” For this example, we will assume that the writer does not record the song to illustrate just how divided a musical royalty may be.

A music publisher and a recording company have to agree on the usage of a song, and in order to do so, they usually — but not necessarily — rely on an intermediary to act as a middleman. In the United States, this is often a task for the Harry Fox Agency, which is the largest such intermediary in the country. Theoretically, the music publisher could demand a rate that exceeds the statutory or mechanical royalty rate, as they are not compelled by a compulsory license to forfeit their work for any less. However, record labels will rarely offer to pay more than the statutory rate,⁸⁵ so they will likely pay around that price for access to the work.

⁸⁵ Both Fisher and Passman describe this fact, but the House Judiciary Committee provides a more thorough elaboration on how this effect came to be in their 1961 report:

Once a recording is made, that recording can be “publicly performed” over radio airwaves and on street corners by bussing musicians. As this is another right protected by copyright, a music publisher in this scenario would have the right to monitor these performances. However, they instead choose to use an aforementioned Performing Rights Organization (PRO) to do this monitoring on their behalf.⁸⁶ There are three major PROs in the United States: BMI, ASCAP and — the significantly smaller — SESAC. PROs issue blanket licenses to performance venues, restaurants, retail stores, and radio stations, which provide access to their entire catalog of works for a flat rate. PROs then use formulas and tracking methods to divide their total revenues after overhead charges amongst their members based on the relative popularity of their works.^{87,88}

The description laid out above was only for the compositional copyright. The copyright for an audio recording navigates a different route through the industry. This section will begin with a recording artist, and

“In practice the authors of musical works generally assign their recording and other rights to publishers, under an agreement for the division of royalties. But in most instances the record companies secure licenses from the publishers, thereby avoiding some of the mechanics of notice and accounting required by the statute for exercise of the compulsory license. But the statutory rate of 2 cents per record operates as a ceiling on the royalty rate paid, even as to the first recording.”

⁸⁶ PROs could, in theory, cut the publisher out of the equation. However, two of these PROs and the largest of them — ASCAP and BMI — are prevented from doing so by anti-trust laws.

⁸⁷ Passman, *supra* note 55 at p. 242.

This description is true of ASCAP and BMI; SESAC pays its signatories negotiated membership fees and retains the remainder as a profit.

⁸⁸ Fisher, *supra* note 9 at p. 51.

“their” song, and follow its copyright through the various exchanges it undergoes. For this section, when referring to the “song,” this will refer only to the recording of the song, not necessarily the underlying composition and the separate copyright that is parallel to it.

A recording artist, like a songwriter or composer, often relinquishes their copyright to another entity. In this case, it is often handed off to a record label. Record labels offer some benefits to a recording artist in exchange for this transaction; first, recording an album is an expensive enterprise. It often requires a recording studio (which often has to be rented), producing, mixing and mastering, back up musicians, and may, as described above, require obtaining the rights to have the first recording of a composition. A record company could not only provide the funds for this project, but can also connect a recording artist with a network of contacts to bring all of the necessary actors into the project, *and* find a distributor for the album. Just the cost of making an album “can easily cost” \$150,000,⁸⁹ which makes the prospect of having someone cover those fees upfront attractive to recording artists.

The recording artist will likely receive between 10 – 20% of the revenue generated by retail sales of their work as a part of their contract,⁹⁰ but their share will also be reduced by:

⁸⁹ Passman, *supra* note 55 at p. 99.

⁹⁰ Fisher, *supra* note 9 at p. 55.

- Charges for the packaging of the album in its various formats (CD, LP, cassette, etc.)
- Charges for “promotional copies” of the album which are sent to radio stations and other promoters for free
- Charges for copies of the album that are produced and distributed but not sold at retail
- A share of their revenue which will be split with the producer of the album

There are various other deductions as well, such as promotional fees, advance recoupments, legal fees, and so forth. Though the record label will front the costs of the recording process, an artist is responsible for bringing that money back to the label. After all of the deductions and expenses that cut into a recording artist’s 10 — 20% share of revenue, it is likely for an artist to owe the record label *more* than what they generated. There are a virtually infinite number of anecdotes of this occurrence from even those at the top of the music industry, such as Thirty Seconds to Mars selling 2 million albums or Lyle Lovett selling 4.6 million albums and seeing *zero* dollars in album sales from their label.⁹¹ In 2018, Citigroup published an extensive report that determined that from the \$43 billion generated by the music industry in

⁹¹ Masnick, Mike. "RIAA Accounting: Why Even Major Label Musicians Rarely Make Money From Album Sales." Techdirt. July 13, 2010. Accessed December 13, 2018. <https://www.techdirt.com/articles/20100712/23482610186.shtml>

2017, just 12% of that sum found its way to the musicians themselves as a result of the numerous intermediaries and middlemen within the industry.⁹²

In signing a recording contract, the artist is often considered a “work made for hire,”⁹³ meaning that while under their contract they will create copyrighted works, they will have no legal rights to the work. Legally, they are considered an employee working with the scope of their employment, and the owner of the copyright — i.e., the record label — is recognized as its original creator. This strips him or her of their right of termination, where thirty-five years after a transfer of copyright one can reclaim it. In this case, however, no legal transfer is recognized, and thus there is no right of termination applicable.⁹⁴

It is worth noting that as mentioned in the section on copyright, there is no public performance right for an audio recording in the United States. When a song is played on the radio, there are royalties generated under the compositional copyright, but not for the audio recording. This further handicaps potential revenue streams for a recording artist and increases the chance of one having an “unrecouped” balance for an album.

⁹² Bazinet, Jason B et al. *Putting the Band Back Together: Remastering the World of Music*. Report. Citigroup. 2018. 1-88.

⁹³ Passman, *supra* note 55 at p. 341.
To meet all of the legal requirements for being a work for hire, the work must be 1) commissioned at the request of someone else, 2) there must be a written agreement explaining that the work is for hire, and 3) is created for use in a series of subcategories. In the music industry, record labels consider musical recordings to fall under the “collective work” category as an album.

⁹⁴ Passman, *supra* note 55 at p. 344.

E. Review

There are two copyrights for a musical work in the United States: one for the composition, and another for an audio recording of that composition. These two copyrights are each governed by different yet overlapping entities in the music industry, based on the rights that each copyright affords and whether the creator is a composer or recording artist.

Because of the complexities of these two copyrights, there is a complicated web of actors, each cutting in on the revenue that is generated from the royalties of a copyrighted work for the services that they provide. Even when a work is widely commercially successful in the United States, it is not unusual for its creators to see very little of the profits from it. This fact is more relevant than ever, as advancing technologies have been able to radically change the music industry both the ways in which royalties are generated and the magnitude of them.

IV. A Cost-Benefit Analysis of the Spotify Streaming Model

With the context of the Spotify debate over artist royalties detailed from the recent history of Spotify and the music industry, as well as how copyright is underpinned and operates concerning musical recordings, we can now begin to analyze the benefits and detriments of the Spotify streaming model using a welfare economics approach.⁹⁵ The main concern for this section of the thesis is whether or not the streaming model causes more harm to society than is necessary or tolerable as measured by wealth maximization, and balancing the dichotomy between incentive and access.

With the streaming model, the question of fair compensation can be framed as a debate over fair *incentives* in a modern music industry where the bar for (legal) access to music has never been lower. Because streaming services offer a catalog of millions of songs to consumers for the same monthly price that they would have paid for a single album in the purchase model, access has inarguably been increased. The discourse at hand concerns whether or not this unprecedented access potentially creates too much drag on incentives.

Before proceeding with this cost-benefit analysis, the inherent flaws with wealth maximization should be made apparent. The first is that in a system where utility or social good is being measured by money that those

⁹⁵ Welfare economics concerns the maximization of societal wealth, not good or utility.

who are able to pay come out on top of those who are not able to do so, i.e., the wealthy come out on top of the destitute. Consider the case of a new drug that emerges on the market: for person x, the drug could save their life, while for person y, the drug would only create a short term, recreational high. The drug, however, is extraordinarily expensive, so much so that person x is merely unable to pay for it, whereas person y, who is a billionaire, has no issue paying upfront for the drug. Under wealth maximization, because person y is both able and willing to pay for the drug, he should receive it, even though person x may die without it. This example poses a moral dilemma for many people, including myself, but wealth maximization offers no course to rectify it.

The second issue that this framework poses is the issue of marginal benefits. Using the same two people from above, if I were to give \$100 to person x, it provides more benefit to them compared to giving \$100 to a billionaire like person y. Though they have both received an extra \$100, it represents less of percentage increase in a billionaire's bank account than to someone with say a few thousand dollars in theirs. Again, wealth maximization does not account for marginal benefits like this and would value each distribution the same.

I will not ignore the apparent problems from applying this framework, and will address concerns about distribution that arise by discussing them from outside of the framework. By arguing both from within this framework

and outside of it, I can address the concerns and analyses of not only economists but musicians as well. Despite the holes in welfare economics — which I will do my best to highlight and retort when applying this framework — I am choosing to use it because it is the most widely used approach within the field of economics, and makes the conclusions that I draw more directly comparable to the other voices within this debate.

It is worth directly addressing a point that was alluded to in previous sections: the recording industry has never been known for its just compensation of musicians and artists. There have always been artists that have profited well beyond the incentive that they would need to create, while there have always been far more that do not recoup the costs of those investments in time and money.⁹⁶ In this way, the debate chronicled throughout this thesis thus far fits squarely within previous criticisms of the industry. Unfortunately, some critics may be looking for solutions that will never be realized.

Before delving into the raw data comparing the royalty payments of these respective systems, it is also crucial to reiterate the incentives-access paradigm, which is a paramount subject in this debate. While the more pre-eminent issue for much of this thesis is the incentives received by artists in the form of royalties to encourage them to continue creating, the streaming model's vast augmentation of access that the public has to recorded music is

⁹⁶ This fact is true of most, if not *all*-creative industries; for example, consider actors, painters, and chefs, who may all put significant investments into their work and see little in return for it.

part of this picture as well. For about \$10 — roughly the cost required for purchasing the average album on iTunes — consumers have access to millions of songs and artists for a full month. This is inarguably of great utility to the general public, as they have access to astronomically more content for significantly less.

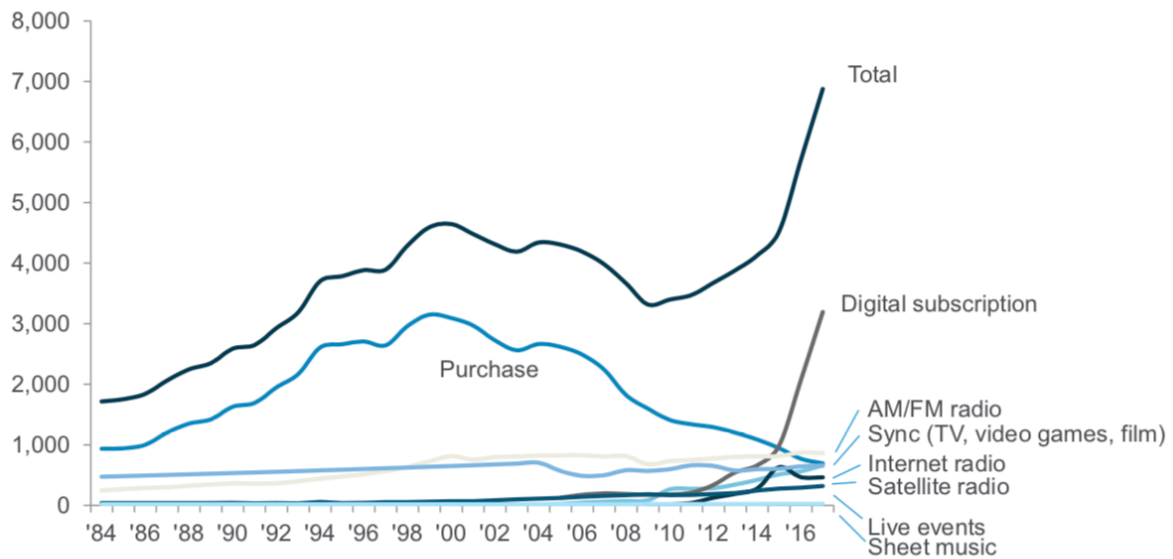
While the general public is undoubtedly the winner in this setup, the concern for this thesis focuses on incentives; can a system that provides a colossal amount of access strike the crucial balance with incentives that policymakers are concerned with? While many within the music industry as previously mentioned have lambasted Spotify for their perceived destabilizing of this balance, the startling answer is that Spotify has not only improved access but improved incentives as well.

A. Streaming Royalties vs. Purchase Royalties

Streaming services are now generating more royalties for rights holders — not just revenues for the industry — than the album purchase model ever did over the past three decades. These royalties have been inherited not just by sound recording copyright holders, but by composition copyright holders as well.⁹⁷

⁹⁷ Bazinet, *supra* note 89 at p. 25.

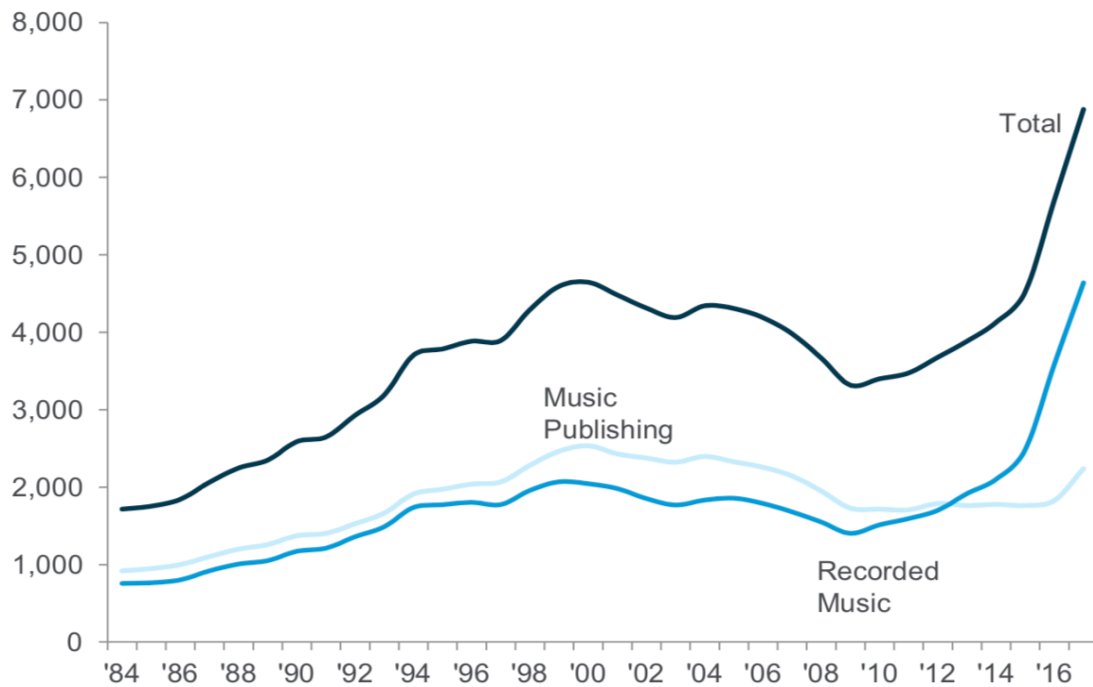
Figure 19. Total U.S. Music Royalties by Consumer Activity (\$ millions)



Source: Citi Research; HFA; ASCAP; BMI; Warner Music

Figure 2: Breakdown of music industry royalties generated by revenue source. Digital subscription services like Spotify and Apple Music generate a plurality of industry royalties as of 2017. Source: Putting the Band Back Together: Remastering The World of Music. Citigroup. Bazinet et al, page 24.

Figure 18. Total U.S. Music Royalties (\$ millions)



Source: Citi Research; HFA; ASCAP; BMI; Warner Music

Figure 3: Breakdown of music industry revenues by copyright.

Royalties generated by both the copyright for the recording and the copyright for the underlying composition are sharply increasing due to music subscription services like Spotify as seen from Figure 2. Source: Putting the Band Back Together: Remastering The World of Music. Citigroup. Bazinet et al, page 22.

A 2018 Citigroup report entitled “Putting the Band Back Together” pegged total recording industry royalty payments at \$7.3 billion in 2017, a record-breaking figure. Of that tally, streaming subscription services generated over \$3 billion, well above the royalties now generated from any

other source (i.e., radio, sheet music, synchronization licenses) and now higher than the annual royalties ever generated from purchasing music. Both recorded music copyright holders and music publishers are receiving increased royalty payments as a result, though the royalties for the recording copyright have significantly outpaced those for the composition's copyright.⁹⁸

The striking data that Citigroup presents should be trusted based on the following merits: Citigroup previously owned one of the “big four” record labels, EMI, in 2011, and counts Live Nation and Sirius XM amongst its investment clientele. The bank's connections to and knowledge of the industry are also bolstered by the fact that it cited figures directly from the major labels like Warner Music, as well as the major PROs BMI and ASCAP, and the Harry Fox Agency. These figures match the trends described by Nielsen Soundscan, regarded as “the Bible” by industry protagonists, which show recording industry revenues soaring in the streaming era.

What one can take from this data is that there is no crisis within the music industry. Revenues have begun to increase in the streaming era as evidenced in Section I, and Citigroup's data indicates that these revenues have benefitted copyright holders in the form of increased royalties. Though some may argue that royalty payments within the industry as still insufficient by some standard, they are beyond sufficient by 2000 standards when the industry's royalty payments previously plateaued.

⁹⁸ Citigroup reports that “The publishers suggest the compulsory license structure in the U.S. retards the economic value of Music Publishing,” which creates this disparity between recording and composition royalties.

When launching their criticisms at the streaming model's payment of artists, critics very often point to the album purchase model as being the exemplary and ideal state of the industry. These arguments in favor of the purchase model are often underpinned by another: that music should be purchased in order to place an inherent value upon it. Aforementioned critics like Taylor Swift, Björk, and other record labels, contend that Spotify's free subscription tier dampens the value of music and art at large.

There are a few points to consider in response to these arguments: first and foremost, even if Spotify users on the free subscription tier are not paying for access to the Spotify catalog with money, they are paying for it by listening to repeated advertisements. These advertisers are effectively paying for the free tier users to have access to Spotify's catalog. If the issue is truly that consumers themselves should have to pay for music, then it is difficult to determine what an appropriate payment threshold would be. If \$10 for an album is appropriate, what about \$5? Or \$1? Is the issue truly that consumers should merely pay *something* for an album, or are there more precise criteria that should be met?

As Swift herself wrote, "...my prediction is that individual artists and their labels will someday decide what an album's price point is. I hope they don't underestimate themselves or undervalue their art."⁹⁹ Swift does not offer a solution to this dilemma, though understandably so, as she is a

⁹⁹ Linshi, *supra* note 35.

musician and not an economist or policymaker. The fact remains, however, that Swift's argument doesn't make sense in this framework or seemingly in any other; it doesn't make sense to have people pay more for music *just because*, if incentives and access are both benefitting from this model.

The criticisms raised against Spotify emerged mainly in the early 2010s when subscription services were taking off but before they surpassed purchases in revenue. They are perhaps justified by the fact that the purchase model is the one that created the current recording industry setup to begin with, and any change to that model would precipitate a significant shift to an industry that has previously seen none, which would reasonably concern some. Now, however, these concerns appear to be outdated.

While, again, wealth maximization does not concern itself with the distribution of wealth, but rather the maximization of it, there is a potential criticism that is worth dismissing outright. A critique when evaluating this data is that some genres, artists, and songs may be accumulating more of these royalties in such a disproportionate manner that some groups may actually be seeing *fewer* royalties than before. After all, as mentioned in Section I, a 2018 study found that the top 0.4% streamed songs on Spotify generated 10% of the company's royalty payouts.¹⁰⁰ This is, however, a significant improvement from the purchase model in digital (iTunes) era, where Page and Bud found that the top 0.4% of songs consolidated 80% of

¹⁰⁰ Ingham, *supra* note 5.

revenues, and that “85% of albums online *never sold a single copy during the one year period of the study.*”¹⁰¹ In the streaming era, more artists are receiving some degree of revenue stream from their recordings, i.e., more artists are being incentivized to create than before.

The long-tail distribution of popularity that was so prolific in the purchase era has now been consolidated in the streaming era so that the additional wealth in the system is being shared amongst more artists and projects. As the question steering this thesis is whether or not the streaming model is sustainable for musicians, this data presents a picture that this model is, in fact, more sustainable for more musicians than the purchase model. In addition, with the long tail distribution being elongated as to capture more artists in it, the public now has more options to satisfy their preferences as well, another benefit of this system.

B. Streaming’s Impact on Touring

While it has been established that there is more money in circulation for copyright holders in the music industry thanks to music streaming, this new model has had a significant effect on the live music industry as well. Though consumers may be spending less money to listen to recorded music, they are not spending less money on music overall: the live music industry has grown significantly in the aftermath of the streaming model. This

¹⁰¹ As synthesized by Day, *supra* note 56 at p. 82.

relationship is not one just based on correlation, it is, in fact, a causal one: as consumers have the opportunity to listen to more music, streaming services fuel the discovery of new artists and thus fuel interest in live shows from those same artists.¹⁰²

Midia Research found that “the live music industry accounted for 33 percent of overall industry revenue in 2000, compared to 53 percent attributed to retail recorded music. By 2016 that number shifted dramatically [with] live music garnering 43 percent as opposed to recorded music's dwindling 38 percent.”¹⁰³ Musicians now see live performances constitute nearly 60% of their overall income; whereas live performances were previously seen as a means to an end in boosting record sales, and still are to a lesser extent, live music is now a vital source of income in its own right.¹⁰⁴ In the same Citigroup report discussed at length above, Citigroup concluded that artists saw 12% of total music industry revenues, which was actually an improvement from 2000 when artists saw just 7% of industry revenue. Citigroup attributed the “bulk of the increase” to “strength in the concert business.”¹⁰⁵

¹⁰² Sanchez, Daniel. "The Live Music Industry Will Be Worth \$31 Billion Worldwide by 2022." Digital Music News. October 26, 2018. Accessed March 10, 2019. <https://www.digitalmusicnews.com/2018/10/26/latest-live-music-revenue-31-billion-2022/>.

¹⁰³ "How Does Live Music Impact the Music Industry Financially?" U Miami Online. January 08, 2018. Accessed March 10, 2019. <https://frostonline.miami.edu/articles/live-music-financial-impact-on-music-industry.aspx>.

¹⁰⁴ *Id.*

¹⁰⁵ Bazinet, *supra* note 89 at p. 3.

Musicians themselves have begun to capitalize on this connection. In an editorial for Forbes, American Indie pop artist Vérité wrote that while her initial royalty payments from Spotify were nominal, she credits Spotify for constructing a dedicated fanbase for her that would attend her live shows:

“I was not considering streaming as a path toward revenue. I knew Spotify paid less than pennies per stream...Much to my surprise...Streaming began to be and remains, by far, my largest source of income, contrary to what is popularly said. Streaming revenue has allowed me to...move forward knowing I have a channel of distribution that has provided me with a wealth of consistent, engaged listeners I get to convert into real fans...Spotify won't build your career, nor is that its responsibility. It provides a platform for discovery. It will link your listeners to your merchandise and concerts, and it will provide back-end data for you to locate and analyze your followers.”¹⁰⁶

Spotify itself plays a role in funneling its subscribers to the live music industry. Artist pages allow tour dates to be integrated within its interface so that when a subscriber is on an artist's page, they will see the nearest concert date from that artist.¹⁰⁷ Spotify's portal for labels and artists — Spotify for Artists — allows these groups to dissect Spotify's data so that they can see fine-tuned streaming trends such as popular days of the week for artists and

¹⁰⁶ V. (2018, March 19). Spotify Isn't Killing The Music Industry; It's A Tool For Enterprising Indie Artists. Retrieved March 25, 2019, from <https://www.forbes.com/sites/bizblog/2018/03/19/spotify-isnt-killing-the-music-industry-its-a-tool-for-enterprising-indie-artists/#266b84e1476b>
Vérité is the stage name for musician Kelsey Regina Byrne. She has amassed over 200 million streams on Spotify as of April 2019.

¹⁰⁷ Artist webstores can also be integrated within Spotify's interface as well so that subscribers can be directly linked to an artist's merchandise.

their songs, but perhaps most importantly, *where* their music is generating the most interest. This aspect is an underrated and under-analyzed one of streaming services; their ability to synthesize and disseminate complex data when “Just a decade ago, bands had to rely on information gathered by costly professional radio campaigns to determine where to book shows,” that is now provided by streaming services for free.¹⁰⁸

Spotify’s connections to the live music industry run even more directly than this, as can be seen by their collaborations with the Goliath of the live music scene, Live Nation. In 2018, Spotify executive Troy Carter announced that through their Fans First program that they had generated \$40 million in ticket sales. The program is similar to the aforementioned Spotify For Artists portal in that it presents detailed listener information to artists and their teams, but it goes beyond this by being able “to target potential ticket-buyers via email with special offers—in this case, the option to buy pre-sale concert tickets before they’re available elsewhere.”¹⁰⁹ Since then, Live Nation has partnered with Spotify in creating tours for artists on popular Spotify playlists such as RapCaviar and Hot Country.¹¹⁰

¹⁰⁸ McGuire, Patrick, Dan Reifsnyder, Angela Mastrogiacomo, and Dre DiMura. "New Trends in Touring – Soundfly." Soundfly. July 05, 2018. Accessed March 25, 2019. <https://flypaper.soundfly.com/hustle/new-trends-in-touring/>.

¹⁰⁹ Titlow, J. P. (2017, June 30). Spotify's Plan To Win Over Anxious Artists—And Win The Streaming War. Retrieved March 25, 2019, from <https://www.fastcompany.com/3068915/spotify-artists-streaming-playlists-data>

¹¹⁰ Ingham, T. (2018, June 26). Spotify generated \$40m in ticket sales last year. Now, it's accelerating its presence in live music. Retrieved March 25, 2019, from <https://www.musicbusinessworldwide.com/spotify-generated-40m-in-ticket-sales-last-year-now-its-accelerating-its-presence-in-live-music/>

It is worth noting, however, that the growth of the touring industry in place of recording revenues has inevitably drawn some criticism. New York Times columnist Mike Errico argued in “Touring Can’t Save Musicians in the Age of Spotify” that as record labels feel the pinch of decreasing download and physical sales that the “360 deal” has become more prolific; a record deal by which the label is given profits from a musician’s live music and merchandising revenues, not just from their recorded music revenues. Record labels incur no “risk” in these deals and run the risk of running their artists into the ground physically under relentless touring schedules.¹¹¹ While this concern may have been valid at the time it was written in early 2016 when recorded music revenues were decreasing, they have now begun to *rise* primarily due to music streaming, so it would follow that a record label’s dependence on the 360 deal would thus decrease in response. Musicians have toured regardless of the state of the recording industry; drawing a causal relationship between 360 deals and increased potential for injuries appears to be misplaced or at the very least marginal at best.

Instead, the more valid criticism is that some artists do not want to tour or are physically unable to tour. Once musicians reach ages in their 80s

¹¹¹ “But labels do not take on the additional risks associated with their additional profits. Instead of protecting the health of their revenue-generating engine, they simply point to an artist’s independent-contractor status, which releases them from any liability they would be on the hook for if artists were labeled employees.”

Errico, Mike. "Touring Can't Save Musicians in the Age of Spotify." January 25, 2016. Accessed March 9, 2019.

<https://www.nytimes.com/2016/01/25/magazine/touring-cant-save-musicians-in-the-age-of-spotify.html>.

and 90s, it becomes unrealistic to expect them to endure rigorous touring regimens to support themselves financially, as it would be to expect *any* octogenarian to perform physical labor. While these concerns are, again, legitimate, I believe that the problem remedied by the fact that streaming revenues continue to be generated by artists who are touring and those who aren't, though the magnitude of those revenues may vary accordingly.

As for those who don't want to tour, a nomadic life on the road can precipitate life-endangering struggles on the road. Michael Angelakos of the American synthpop act Passion Pit told *Consequence of Sound* upon his brief stepping out from the music industry in 2017 that his battles with bipolar disorder, combined with "The risks associated with being a commercialized artist and embarking on a typical album release, like endless promotion and touring, have nearly killed me."¹¹² Despite this, Angelakos embarked upon a new tour in 2018 in order to cover the medical costs related to his mental health treatment.¹¹³

Ultimately, the welfare economics analysis deployed in this section would contend that because there is more wealth in the music industry both

¹¹² Geslani, Michelle. "Michael Angelakos Clarifies Future of Passion Pit: "Protecting Health Is the First Step in Maintaining a Culture's Artistic Output"." *Consequence of Sound*. July 25, 2017. Accessed March 31, 2019. <https://consequenceofsound.net/2017/07/michael-angelakos-clarifies-future-of-passion-pit-protecting-health-is-the-first-step-in-maintaining-a-cultures-artistic-output/>.

¹¹³ Schatz, Lake. "Passion Pit's Michael Angelakos Says He Needs to Tour to Cover Mental Health Medical Costs." *Consequence of Sound*. January 18, 2018. Accessed March 31, 2019. <https://consequenceofsound.net/2018/01/passion-pits-michael-angelakos-says-he-needs-to-tour-to-cover-mental-health-medical-costs/>.

live and recorded because of streaming than previously, that an arrangement more dependent on live music would be preferential to the prior one. Outside of this frame, it *is* important to note the case of Angelakos as to be considerate to the many musicians like him who struggle with mental illnesses. However, it is equally important to recognize that those who struggle with mental illness working in *any* profession may have to work in some capacity in order to pay the costs of their medical treatment in the United States. The music industry, in this way, is no exception to this predicament and ultimately, the issue lies outside of the industry itself.

While the growth of the live music industry as a result of the streaming model's explosion may alter the way that musicians structure their careers, it is not a requirement that they increase their touring regimens. Given that more royalties are being paid out for their songs and recordings, the expansion of the concert industry only provides an extra opportunity for them to receive more money than before. In short, the live music industry's growth has created an avenue for further increasing incentives for its performers with no collateral damage to recording incentives.

C. Reshaping the Music Industry

Spotify provides a unique opportunity for artists to distribute their music to their service without intermediary services. Historically, musicians would need to pay to both create and distribute physical manifestations of

their recordings, and even in the digital age would need to use a third party to have their music uploaded to outlets like iTunes for retail. However, Spotify's For Artist portal now allows musicians who own the copyright to their works to upload directly to the service.

As mentioned in chapter three, royalties and revenues for musicians are often siphoned off by the multiple bodies associated with disseminating and protecting their works, like record labels, publishers and PROs, and distributors. What Spotify is essentially offering to independent musicians is the ability to reduce distribution costs to \$0 and increase their capacity to recoup the investments into their music. It is worth mentioning that this option is only available to independent musicians who own their own copyright; recording artists signed to labels would not personally see the benefit of distribution costs being reduced in the same manner.

Just as Spotify is cutting distributors out of the picture, they may have their crosshairs on a much larger target: record labels. It has been widely speculated that Spotify may make its own foray into the recording industry by signing artists and generating their own content rather than relying solely on the catalogs of record labels.¹¹⁴ The groundwork for this vertical integration has already been laid: the New York Times reported in September of 2018 that Spotify "has quietly struck direct licensing deals with a small number of independent artists. The deals give those artists a way

¹¹⁴ Kopf, Dan. "Why Spotify Wants to Be like Netflix Now." Quartz. February 06, 2019. Accessed April 01, 2019. <https://qz.com/1543627/why-spotify-wants-to-be-like-netflix-now/>.

onto the streaming platform and a closer relationship to the company — an advantage when pitching music for its influential playlists — while bypassing the major labels altogether.”¹¹⁵

While record labels have been decisive in propelling the careers of virtually every industry juggernaut imaginable, the musicians working directly with Spotify have instant access to nearly 200 million global users, receive preference in playlisting opportunities,¹¹⁶ and preserve the copyright to their works. American Idol contestant Mia Coleman told Bloomberg with respect to her deal with Spotify that “It’s an all-around positive for me...I have complete control. I have more money. I choose how I get branded.”¹¹⁷

The scenario above has a striking equivalent within the film industry that can help to illuminate the issue. Netflix, much like Spotify, is the product of rapid digitization and offers recurring monthly subscriptions to its users who in turn have access to a catalog of TV shows, documentaries, and movies licensed to Netflix by various production companies. While early in its inception Netflix relied solely on previously created content for its services, it has since garnered significant attention for its original series and films

¹¹⁵ Sisario, Ben. "A New Spotify Initiative Makes the Big Record Labels Nervous." September 06, 2018. Accessed March 27, 2019. <https://www.nytimes.com/2018/09/06/business/media/spotify-music-industry-record-labels.html>.

¹¹⁶ Spotify’s playlists represent major promotional opportunities for musicians of all levels of notoriety.

¹¹⁷ Shaw, Lucas. "Spotify to Musicians: Let Us Be Your Label." Bloomberg.com. November 9, 2018. Accessed March 27, 2019. <https://www.bloomberg.com/news/articles/2018-11-09/spotify-to-musicians-let-us-be-your-label>.

beginning in 2012. With shows like *House of Cards* and *Orange is the New Black* and films like 2019's *Roma*, Netflix has received the highest accolades in the industry such as Golden Globes, Emmy Awards, and Academy Awards (Oscars).

Netflix's original content has not only legitimized the company as a production company, but it has also helped to reverse its financial fortunes after years of negative net revenues. By creating its own (successful) content, Netflix has saved significant money on negotiating licensing costs from other production companies over the long term. For a company like Spotify, which has only become profitable within the last year despite significant revenues and market penetration, Netflix's success in cutting out the middlemen will likely precede Spotify pursuing a similar course of action.

Back within the recording industry, it is a concern that record labels may be undercut by Spotify offering these exclusive distribution deals directly to artists, but there are a few worthwhile considerations: first and foremost, independent artists have always existed within the recording industry, and record labels have endured their presence thus far. In offering these distribution deals to musicians that come with advances,¹¹⁸ Spotify becomes the sole distributor for one's catalog, which may doubt alienate those who wish to have their music available on multiple platforms such as Apple

¹¹⁸ An advance is a payment made to an artist in advance of the release of their work, that then must be recouped by the artist before they begin seeing royalty payments directly deposited to them, as mentioned in chapter two.

Music, Amazon, Tidal, etc. Record labels, on the other hand, are significantly more likely to offer multiple retailers to its artists.

For those musicians who neither want to sign to a record label nor strike an exclusive deal with Spotify, they may use the Spotify For Artists portal and upload their copyrighted works directly to the service, and seek for other avenues of distribution on their own. While Spotify is providing mechanisms to accommodate independent musicians, record labels will buffet some of the risk associated with being independent for their signees, most notably the costs of recording an album. The choice for musicians concerning the distribution of their catalogs, therefore, concerns which balance of risk and exclusivity they wish to strike.

In this world, record labels would still be likely to endure as a central entity within the industry; record labels in the streaming era will continue to offer an array of services in a single deal that have a wide appeal to many artists, beyond just covering the initial cost of recording. Record labels connect artists with songwriters, producers, PR teams and managers, and offer access to their marketing and advertising departments as well. In 2018, the RIAA reported that the major labels — Universal, Warner and Sony — have begun to sign more artists than when the industry was in decline; when industry revenues hit a nadir in 2014, the majors signed 589 new artists. In 2017, with industry revenues rising once again thanks to streaming services,

they signed 658 new acts.¹¹⁹ While smaller record labels may struggle to adapt to a changing industry, larger ones will likely be able to weather any further storms that emerge as a result of the streaming model.

While independent musicians seeing more money in their bank accounts and record labels cutting down on distribution costs may seem to be an unusual arrangement where both groups win, a new consideration may emerge for those who work for distributors. Just as there are people who depend on creating music for their careers, there are also those who depend on distributing that music for *their* careers. In an industry where artists upload directly and for free to a distributor like Spotify, those who work for traditional distributors like CD and vinyl producers are then undercut. The quick response to this problem is that welfare economics would not make special consideration for their case. Because welfare economics only concerns the maximization of wealth and not the distribution of that wealth, these types of workers would not be accounted for in any meaningful manner.

I would argue that having more options available to creators is more valuable than having more traditional but more limited options. By giving musicians more opportunity to choose how they want to structure their careers and the distribution of their music, one would likely see musicians overall gain more autonomy over their creations and thus increase their satisfaction within the music industry. Given that most record labels and

¹¹⁹ Glazier, Mitch. "50 Million Reasons For Optimism." Medium. February 28, 2019. Accessed May 02, 2019. <https://medium.com/@RIAA/50-million-reasons-for-optimism-d70cff45c8ab>.

current industry structures would survive an industry arrangement with these extra options available, there appears to be no reason why these options should not be welcomed if they are of such benefit to musicians. With the new alternative career path that artists have by working directly with Spotify, there is a new approach to the industry that can better fit the needs and desires of more musicians. This would likely incentive more musicians to create, as they would have new recourse to navigate their careers on their own terms, at no foreseeable cost or change to the public's access.

D. Copyright Policy Adjustments

One of the recurring considerations of this thesis was that of the policymaker and public policy. It is the duty of lawmakers to make adjustments to policy whenever appropriate to best serve the needs of the public. In the era of music streaming, copyright law is working effectively to ensure that artists are incentivized and that the public has reasonable access to their works.

As discussed in Section I, copyright law was struggling in the digital era to police unauthorized reproductions of music via piracy. Though these reproductions were undoubtedly illegal, it was an arduous task for the government to track these illicit downloads and prevent them. What Spotify and other streaming services have seemingly managed to do is capture Internet users who previously pirated music and convinced them to subscribe

to their services as a matter of convenience. Pirating music often requires visiting numerous domains to obtain the desired file in the ideal format and quality at the risk of contracting a computer virus, whereas streaming services provide a simple interface and large quantities of high-quality music for relatively low prices. The argument purported by Spotify executives that they have monetized “existing consumer behavior” is seemingly valid now that consumers are individually paying less for access to music yet the recording industry is generating *more* revenue.

What this means for policymakers is that the industry has come up with its own solution to copyright law’s inadequate enforcement. The protections provided by copyright are enough to generate revenue for copyright holders, while music consumers have been convinced and even corralled by the industry to no longer engage in illicit behavior. As incentives and access have benefitted from the streaming model, how, then, should lawmakers respond? The answer is seemingly that they should not respond at all based on the criteria we’ve established. The music industry is not in an economic crisis relative to its peak in the 2000s. Policymakers should only tweak music copyright law if they believe that the current system has always been inefficient, which is well beyond the scope of this thesis.

Despite this, Congress and the Trump administration have already reacted to the dominance of the streaming model by passing the Orrin Hatch Music Modernization Act in late 2018. Though the act is a consolidation of

numerous bills and thus has a myriad of provisions that affect areas of the industry outside of streaming services, it does improve certain inefficiencies with these services that are otherwise not covered in this analysis. Streaming services have encountered difficulty with identifying copyright holders for recordings in the past, which has resulted in a class action lawsuit against Spotify totaling \$43.4 million;¹²⁰ now, a new governing agency will create databases and handle the identification of these copyright holders on their end.¹²¹

A difficulty in trying to adjust copyright policy in the streaming era is that its meteoric rise to industry prominence has meant that data and evaluations of the model lose insight rather quickly. For example, Richardson in 2014 suggested a reevaluation of compulsory licenses in music copyright law due to the fact that "...compulsory licensing sets a price floor for one party; in this case, it is the record labels. In the current framework, content owners can insist on receiving a minimum of the compulsory rate, and thus come to the table with significantly more bargaining power than

¹²⁰ When Spotify struggled to find the publishers for songs, it would set aside money to pay them once they were identified. This, while noble, was not compliant with the law.

Levine, Robert. "Spotify Settles Class Action Lawsuits Filed By David Lowery and Melissa Ferrick With \$43.4 Million Fund." *Billboard*. May 27, 2017. Accessed April 27, 2019. <https://www.billboard.com/articles/business/7809561/spotify-settles-class-action-lawsuits-filed-by-david-lowery-and-melissa>.

¹²¹ It is worth noting that these sort of technical errors with the programs behind streaming services are likely to persist in varying degrees. Singleton, Micah. "Congress May Actually Fix Music Royalties." *The Verge*. January 26, 2018. Accessed April 28, 2019. <https://www.theverge.com/2018/1/26/16931966/congress-music-modernization-act-licensing-royalties>.

distributors.”¹²² Richardson proposed that each license would be set “equal to each individual platform’s net revenue,” so that distributors would have “an obvious incentive to negotiate with content providers.”¹²³

The shortcoming with his solution is that it was based on the contemporary data, which reasonably suggested that Spotify would struggle to become profitable without creating its own content like Netflix. Because at the time, “streaming services continue to experience substantial losses, there is a need for a solution that brings both parties — content owners and content distributors — to the table” to negotiate.¹²⁴ However, Spotify, for the first time earlier this year, announced that it had become profitable without generating its own content to the same degree that Netflix has begun to do so, though as previously mentioned, Spotify has begun to experiment with doing so. This thus undermines a significant pillar of Richardson’s solution, which assumes that streaming services will be compelled to negotiate because they were struggling to become profitable. As the industry landscape continues to change rapidly in this new era, it becomes progressively more difficult to pin down potential policy adjustments that could be pursued and justified.

¹²² Richardson, James Harold. "The Spotify Paradox: How the Creation of a Compulsory License Scheme for Streaming On-Demand Music Services Can Save the Music Industry." *SSRN Electronic Journal*, 2014. doi:10.2139/ssrn.2557709.

¹²³ *Id.*

¹²⁴ *Id.*

Conclusion

The music industry has buffeted radical changes as a result of rapid digitization over the past several decades, from the rise of the CD, to the mp3, and now, music streaming services. During those shifts, industry revenues rose sharply and often dropped just as precipitously, threatening sources of income for musicians, and thus a pivotal piece of human culture as well. Each of these innovations has induced a myriad of complex problems that require swift adjustments not only from policymakers but from industry entities and protagonists as well.

The paramount, guiding question for this thesis was whether or not a recording industry so dependent on a model that requires individual users to pay less for access to music was sustainable for musicians and songwriters. Was a model that provided so much access for so little capable of providing enough incentives for musicians to continue to create? The startling answer here is that not only is access benefitting from this system, but incentives are as well. Music industry revenues and royalties are higher than they've ever been in the past forty plus years. The effects of the streaming model have reached outside of just the recording industry, but have helped to stimulate a surge in the live music industry as well.

The explanation for how revenues are increasing in an era when consumers are paying less per person for access to music than before is the capturing of Internet users who previously paid nothing for music at all. By

not only lowering the bar for access but also providing millions of high-quality copies of music in one safe, searchable system, people are thereby incentivized to subscribe to a legitimate music distributor than an illicit one.

While there was more focus on recording artists and their incentives for the purposes of this thesis, those who are not performers have also seemingly benefitted from the system as well. Royalties for the musical composition copyright have risen in the streaming era, and are tracking to surpass their peak levels from 2000. With the expansion of the live music industry, songwriters stand to gain from having their works performed more frequently to larger audiences.

With that being said, these benefits should not be conflated with absolute perfection. Though the streaming model may be superior to the purchase model in its incentivizing of musicians, this fact does not necessarily imply that the streaming model cannot still be improved.¹²⁵ Though Spotify is helping to close the schism between the over-incentivized and under-incentivized musicians by allowing consumers to listen to a greater number of musical projects, it is not the end of the conversation. Rather, it is a starting point for moving forward with this trajectory.

¹²⁵ The focus of this paper was largely on recording artists, and did not take into account the numerous other actors that help create a piece of music, from producers and instrumentalists, to A&R executives who are left out of this royalty system. There may indeed be necessary reforms to properly compensate these people as well, but they are unfortunately outside of the scope of this thesis.

Glossary

This Glossary is not intended to be all encompassing, but rather assist the reader as they navigate this work and the numerous terms that illuminate it.

Advance — money that is paid upfront to a recording artist that is owed back to the entity that provided it, most often a record label. The advance is recouped by royalties from a copyrighted work, and after the advance is fully recouped royalties begin going toward the artist.

Analog recording — a copy of sound recording that is manifested in a tangible manner so that when properly used, it recreates the sounds of a recording. Examples include vinyl LPs and cassette tapes. The quality of each successive copy degrades.

Compulsory license — A license that the owner of a copyright is forced or compelled to issue. In the United States, for example, radio stations have the right to compel songwriters to license their songs to them for radio play after meeting various criteria. For more, see:

Copyright — “the exclusive legal right, given to an originator or an assignee to print, publish, perform, film, or record literary, artistic, or musical material, and to authorize others to do the same.”¹²⁶

¹²⁶ *Merriam-Webster Dictionary*, s.v. “copyright,” accessed April 22, 2019, <https://www.merriam-webster.com/dictionary/copyright>

Digital download — the digital transfer of a file to a receiver that can decode and process it, such as a computer or mp3 player. Song purchases from iTunes, for example, result in digital downloads.

Dynamic production — producing a new expressive work, including by building on preexisting expressive works.

Incentive-access paradigm — the push and pull that strikes to achieve the optimal balance between providing incentives to creators to continue creating, but also to create a system that provides as much access to the public as possible.

Intellectual property — the set of legal rights in intangible resources (ex. artistic works) that treats them as property by giving the creator exclusive rights in their use. This should not be used as a synonym for creative works.

Mechanical royalty — royalties paid to a songwriter (or the owner of the copyright for the musical composition) when a copy of that work is produced.

Napster — A peer-to-peer file sharing website launched in 1999 that was sued by the RIAA in *A&M Records, Inc. vs. Napster Inc.* and found to be infringing upon the copyright of songs.

Nielsen Soundscan — An information and tracking organization that has tracked sales and airplay data in the United States since 1991, partnering with Billboard magazine.

Nonexcludability — The quality of expressive works or ideas that makes them difficult if not impossible to prevent them from being made widely available once they are first made public.

Non-interactive service — A music streaming service that *does not* allow users to choose individual tracks to play.

Nonrivalrous — The quality of expressive works or ideas that makes it so that one person's enjoyment of a piece of work does not effect another's similar enjoyment of the same work.

On-demand streaming service — A music streaming service that *does* allow users to choose individual tracks to play.

Piracy — The illicit downloading or copying of copyrighted materials without permission.

Publisher — the entity responsible for ensuring that songwriters receive compensation for the sale and/or reproduction of their work.

Performing Rights Organization (PRO) —

Record label — A company that signs contracts with musicians to help record, market, and promote their recordings. Often record labels maintain ownership of an artist's recordings, not the artist themselves.

Recording Industry Association of America (RIAA) — An organization representing record labels and distributors that conducts research as well as lobbying on their behalf. They are also the entity responsible for certifying albums and singles Gold, Platinum, Multi-Platinum, etc.

Static use — The use of existing expressive works in order to enjoy the value of it.

Statutory Rate — “the rate set forth by the Copyright Arbitration Royalty Panel for compulsory mechanical licenses. Assuming the work has been previously released to the public, this is the licensing fee the licensee can pay to sell a cover version of a song without having to obtain direct permission from the rightsholder. In the US, this rate is currently set at 9.1¢ per track or 1.75¢ for each minute of playing time, whichever is greater.”¹²⁷

Streaming — A method of digitally delivering a file to a user’s device so that the given file is never stored in its entirety at any one time. Streaming is utilized in music by services such as Spotify, Apple Music, Tidal, and Amazon Music, but also for film and TV by services such as Netflix and Hulu.

Utilitarianism — “The doctrine that an action is right insofar as it promotes happiness, and that the greatest happiness of the greatest number should be the guiding principle of conduct.”¹²⁸

Welfare economics — “The model of economics that seeks to evaluate the effects of economic policy on the well being of a given community.”¹²⁹

¹²⁷ *Songtrust*, s.v. “statutory mechanical rate,” accessed April 22, 2019, <https://www.songtrust.com/music-publishing-glossary/glossary-statutory-mechanical-royalty-rate>

¹²⁸ *Oxford Dictionaries*, s.v. “utilitarianism,” accessed April 22, 2019, <https://en.oxforddictionaries.com/definition/utilitarianism>

¹²⁹ *Britannica*, s.v. “welfare economics,” accessed April 22, 2019, <https://www.britannica.com/topic/welfare-economics>

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Biography

Hunter Gierhart was born in San Antonio, Texas in 1996. He grew up in the Austin area before moving to New Orleans, Louisiana where he attended the New Orleans Center for Creative Arts, studying classical and jazz trombone performance. He enrolled at the University of Texas at Austin (UT) in 2015 as a student in the Plan II Honors program and Government. During his time at UT, he studied at Queen Mary University of London, served as President of the live-music organization Euphoria ATX, a life and arts issue for the Daily Texan, and interned for Musx, as well as Mascot Label Group at their North American headquarters in New York City. After graduation, he plans to apply to law school to pursue a career in Entertainment law while working in the Austin area.