

# HEINONLINE

Citation: 80 B.U. L. Rev. 2000

Content downloaded/printed from  
HeinOnline (<http://heinonline.org>)  
Tue Aug 18 14:01:32 2009

- Your use of this HeinOnline PDF indicates your acceptance of HeinOnline's Terms and Conditions of the license agreement available at <http://heinonline.org/HOL/License>
- The search text of this PDF is generated from uncorrected OCR text.
- To obtain permission to use this article beyond the scope of your HeinOnline license, please use:

[https://www.copyright.com/ccc/basicSearch.do?  
&operation=go&searchType=0  
&lastSearch=simple&all=on&titleOrStdNo=0006-8047](https://www.copyright.com/ccc/basicSearch.do?&operation=go&searchType=0&lastSearch=simple&all=on&titleOrStdNo=0006-8047)

---

**WORLD MUSIC ON A U.S. STAGE: A BERNE/TRIPS AND  
ECONOMIC ANALYSIS OF THE FAIRNESS IN MUSIC  
LICENSING ACT**

**LAURENCE R. HELFER\***

INTRODUCTION .....	95
I. EXPLAINING THE FIMLA: AN ECONOMIC EFFICIENCY AND DISTRIBUTIONAL ANALYSIS.....	105
A. <i>The Economic Efficiency Approach</i> .....	106
1. Copyright's Property Rules, Transaction Costs and Market Failures.....	106
2. Public Performance Rights, PROs and Government Regulation .....	110
3. "Through to the Viewer" Licenses and Secondary Uses of Broadcast Music.....	111
4. The Effects of Enforcement Costs and User Resistance on PRO Licensing Practices .....	113
B. <i>The Distributional and Fairness Approach</i> .....	115
1. "Double Dipping" for Licensing Fees .....	116
2. Abuses of Monopoly Power.....	117
3. Overly Aggressive Licensing and Enforcement Tactics .....	118
II. IDENTIFYING RENT SEEKING AND MARKET FAILURES: LEGAL REGULATION OF SECONDARY USES OF BROADCAST MUSIC IN THE UNITED STATES.....	119
A. <i>Copyright Rent Seeking in Congress and the Courts</i> .....	120
B. <i>Tracing the History of Music Licensing for Commercial        Establishments</i> .....	122
1. 1920s to 1931: The Initial Battle Over a Licensing Market .....	122
2. 1931 to 1975: Market Failure Emerges .....	124
3. 1975 to 1977: The Multiple Performance Doctrine Briefly Repudiated .....	127

---

\* Associate Professor of Law, Loyola Law School, Los Angeles. Thanks to Nancy Neiman Auerbach, David Boyd, Jay Dougherty, Paul Geller, Rick Hasen and Lydia Loren for talking with me about some of the ideas in this article and for thoughtful comments on earlier drafts. Thanks also to Jason Cole for careful research assistance and to Jennifer Ostertag-Tevjovits for French translations. Work on this article was supported by a summer research grant from Loyola Law School.

4.	1978 to Early 1990s: Litigating the Homestyle Exemption .....	130
5.	Early 1990s to 1998: Users' Judicial and Legislative Resistance Increases .....	131
	a. <i>Judicial Expansion of the Homestyle Exemption</i> .....	131
	b. <i>Legislative Expansion of the Homestyle Exemption</i> .....	132
	1) Early Licensing Reform Bills.....	132
	2) The Fairness in Music Licensing Act of 1997.....	134
	3) The NLBA Agreement.....	135
	4) The Fairness in Music Licensing Act of 1998.....	137
	6. Implementing the FIMLA: Continued User Resistance? .....	138
	C. <i>Summarizing the Historical Evidence</i> .....	139
III.	ANALYZING THE FIMLA AND HOMESTYLE EXEMPTIONS UNDER THE BERNE AND TRIPS TREATIES .....	141
	A. <i>Framing the FIMLA Dispute: A Methodological Note</i> .....	141
	B. <i>The Violation of Berne/TRIPS' Exclusive Rights</i> .....	142
	C. <i>Exceptions and Limitations Defenses: Choosing the Correct Legal Standard</i> .....	147
	D. <i>Article 11bis(2)—Imposing Conditions on the Broadcast Right</i> ....	151
	E. <i>Implied Exceptions to Broadcast and Performance Rights</i> .....	152
	F. <i>Reintroducing the Three-Step Test Through the Back Door</i> .....	155
	1. Step One—The “Special Cases” Requirement.....	157
	a. <i>Arguments for the United States</i> .....	157
	b. <i>Arguments for the European Community</i> .....	159
	c. <i>Evaluating Commercial Establishments' Distributional and Fairness Arguments</i> .....	160
	1) Double Dipping .....	161
	2) Abuse of Monopoly Power & Aggressive Licensing and Enforcement Tactics .....	165
	2. Step Two—The “Normal Exploitation” Requirement .....	167
	a. <i>Arguments for the European Community</i> .....	167
	b. <i>Arguments for the United States</i> .....	168
	c. <i>Normal Exploitation Defined by Market Failure</i> .....	169
	d. <i>Normal Exploitation Measured by Other Copyright Statutes</i> .....	171
	3. Step Three—The “Unreasonable Prejudice” Requirement .....	181
	G. <i>Summarizing the Treaty Arguments and Their Significance for Future WTO Litigation</i> .....	182
IV.	SOLUTIONS TO THE FIMLA DISPUTE: ENCOURAGING PRIVATE AGREEMENT WHILE COMPLYING WITH THE BERNE AND TRIPS TREATIES .....	185
	A. <i>Repeal the FIMLA and Homestyle Exemptions for Foreign Music Only</i> .....	185
	B. <i>Mandate Broadcasters to Pay for Secondary Uses of Broadcast Music</i> .....	187
	C. <i>Encourage Private Agreements Through a Property Rule or a Liability Rule</i> .....	191

1. Assessing the Advantages of Private Agreements over Statutory Exemptions for Secondary Uses of Broadcast Music .....	191
2. The Treaty Compatibility of Private Agreements .....	195
3. Choosing Between a Property Rule and a Liability Rule .....	196
a. <i>A Modified Property Rule</i> .....	196
b. <i>An Ex Post Liability Rule</i> .....	197
c. <i>The Juke Box Compulsory License and Private Agreement</i> .....	199
d. <i>Qualifying the Juke Box Agreement as a Precedent</i> .....	202
CONCLUSION .....	204

### INTRODUCTION

Nineteen ninety-eight was a banner year for copyright legislation in the United States. After much partisan debate and interest group wrangling, Congress passed a slew of new copyright statutes. Most notably, it extended copyright law into cyberspace, and it lengthened the basic term of copyright protection by twenty years.<sup>1</sup> Little noticed amid all the sound and fury was a more modest enactment—the Fairness in Music Licensing Act of 1998 (“FIMLA”).<sup>2</sup> The heart of the statute is an amendment to section 110(5) of the Copyright Act, a provision of the law that, since 1978, has authorized restaurants, bars and retail stores using “homestyle” audio and video equipment to play broadcast music without paying license fees.<sup>3</sup>

In its original form, this homestyle exemption did not create a broad exception to music copyright owners’ exclusive right to perform their works

<sup>1</sup> See Digital Millennium Copyright Act, Pub. L. No. 105-304, §§ 1-505, 112 Stat. 2860, 2877-86 (1998) (extending copyright protection and liability for copyright infringement to the Internet); Sony Bono Copyright Term Extension Act, Pub. L. 105-298, § 102, 112 Stat. 2827, 2827 (1998) (providing for a basic term of copyright protection equal to 70 years following the author’s death).

<sup>2</sup> See Fairness in Music Licensing Act, Pub. L. 105-298, § 202, 112 Stat. 2830-31 (1998), (codified in principal part at 17 U.S.C. § 110(5)(B) and at §§ 101, 504, 513 (1999)) [hereinafter “FIMLA”].

<sup>3</sup> Prior to its revision in 1998, section 110(5) provided:

Notwithstanding the provisions of section 106, the following are not infringements of copyright: . . .

(5)(A) communication of a transmission embodying a performance or display of a work by the public reception of the transmission on a single receiving apparatus of a kind commonly used in private homes, unless -

(i) a direct charge is made to see or hear the transmission; or

(ii) the transmission thus received is further transmitted to the public.

17 U.S.C. § 110(5) (1994). Although the homestyle exemption has been widely used by commercial establishments, Congress also intended it “to exempt from copyright liability anyone who merely turns on, in a public place, an ordinary radio or television receiving apparatus of a kind commonly sold to members of the public for private use.” H.R. REP. NO. 94-1476, at 86 (1976). See also *infra* Part II.B.4.

publicly. Nevertheless, the statute was a thorn in the side of performing rights organizations (“PROs”) such as the American Society of Composers, Authors and Publishers (“ASCAP”), Broadcast Music, Inc. (“BMI”) and the Society of European State Authors and Composers (“SESAC, Inc.”) who issue licenses on behalf of both domestic and foreign songwriters, composers and music publishers.<sup>4</sup> According to the PROs, commercial establishments entertained their customers with broadcast music and thus derived significant financial benefit for which their members were entitled to seek compensation. The PROs sought to limit the exemption to small businesses and brought infringement suits against non-exempt establishments who refused to purchase licenses.

Businesses were also dissatisfied with the homestyle exemption, but for very different reasons. They argued that the PROs were seeking to “double dip” for royalties by charging for performances that had already been licensed to be broadcast by radio, television and cable stations. Led by restaurant, bar and small business associations, these groups lobbied Congress to exempt all “secondary uses of broadcast music.”<sup>5</sup> The PROs stridently opposed any relaxation of the exemption and succeeded in blocking any change in the law for several years.<sup>6</sup>

The FIMLA represents the compromise Congress brokered between these two groups. The new law does not repeal the “homestyle” exemption. Rather, it adds a new and additional exemption for performances of nondramatic musical works that is based not on the use of “homestyle” receiving equipment but rather on the size of the establishment and the number of speakers or television sets used to transmit the music.<sup>7</sup> The FIMLA grants a blanket

---

<sup>4</sup> See AL KOHN & BOB KOHN, KOHN ON MUSIC LICENSING 863-84 (2d ed. 1996) (discussing the history and licensing activities of PROs).

<sup>5</sup> I use the phrases “secondary uses of broadcast music” or “in-store performances” to refer to the act of a business using receiving equipment to tune into a radio, television or cable program transmitted to the public so as to make that program heard within the confines of its establishment. I realize, however, that some cable programs received in this manner may not actually be broadcast. For the importance of this distinction, see *infra* notes 210 and 467.

<sup>6</sup> See *infra* Part II.B.5.b (discussing legislative history of FIMLA).

<sup>7</sup> When Congress enacted the FIMLA, it retained the text of the homestyle exemption in its entirety. It also split the preexisting section 110(5) into two subsections—section 110(5)(A) for the homestyle exemption and section 110(5)(B) for the FIMLA itself. See Lydia Pallas Loren, *Paying the Piper*, 3 J. SMALL & EMERGING BUS. L. (forthcoming) (draft on file with author) (providing a detailed analysis of the FIMLA and a comparison with the homestyle exemption).

The relationship between the two subsections is somewhat ambiguous, however. Section 110(5)(A)’s homestyle exemption is preceded by the words “Except as otherwise provided in paragraph (B). . .” 17 U.S.C. § 110(5)(A) (1999). A logical interpretation of this phrase would be that the statutory text which follows contains a licensing exemption that is separate and additional to the new FIMLA exemption codified in section 110(5)(B).

licensing exemption to retail establishments that are smaller than 2000 square feet and to food service or drinking establishments that are smaller than 3750 square feet.<sup>8</sup> Larger businesses are also exempt, provided that they use fewer

---

According to this view, a commercial establishment that failed to meet the detailed standards of section 110(5)(B) would still be exempt from the payment of license fees if it satisfied the requirements of section 110(5)(A). See Loren, *supra*, at 8, 11 (suggesting this interpretation).

Alternatively, because section 110(5)(B) applies only to defined “establishments,” the “except as otherwise provided” clause might be interpreted to preclude such establishments (but not other copyright users) from relying on the homestyle exemption in the event that the establishment fails to qualify for the FIMLA exemption.

In defending the statutes before the World Trade Organization, however, the United States has adopted an entirely different and far more controversial construction of the “except as otherwise provided” clause. Seizing on the fact that the FIMLA applies solely to nondramatic musical works, the United States has argued that the homestyle exemption now applies only to copyrighted works *other than* nondramatic musical works. See *First Submission of the United States of America*, United States – Section 110(5) of the U.S. Copyright Act, WTO Doc. WT/DS 160, at 5 (Oct. 26, 1999) [hereinafter *First U.S. Submission*] (copy on file with author) (“the 1998 Amendment [to section 110(5)] dramatically limited the homestyle exemption . . . . Section 110(5)(A) no longer covers nondramatic musical works at all.”).

Although WTO jurists are more likely to find such a narrow construction of the homestyle exemption compatible with the United States’ international copyright treaty obligations, the construction requires an exceptionally strained reading of the statutory text. Had Congress intended to exclude nondramatic musical works from the homestyle exemption, it could have easily done so by amending section 110(5)(A) to exempt a “communication of a transmission embodying a performance or display of a work, *other than a nondramatic musical work*, by the public reception of the transmission on a single receiving apparatus of a kind commonly used in private homes . . . .” As it stands, Congress did not expressly limit the type of works to which the homestyle exemption applies.

More fundamentally, the interpretation advocated by the United States would radically alter the careful balance struck by the Copyright Act between copyright owners and copyright users. Indeed, if the homestyle exemption no longer applies to non-dramatic musical works, then it turns a principal justification for enacting the homestyle exemption on its head. For example, under the approach the United States advocates, any member of the public who plays music by “merely turn[ing] on, in a public place, an ordinary radio or television receiving apparatus of a kind commonly sold to members of the public for private use,” H.R. REP. NO. 94-1733, at 75 (1976), is now a copyright infringer. If Congress had intended such a radical (and nonsensical) revision of United States copyright laws, presumably it would have made its intent clear. However, nothing in the FIMLA’s legislative history suggests that Congress intended to narrow the homestyle exemption at all, let alone adopt such a fundamental change to United States copyright policy. See *infra* Part II.B (analyzing legislative history of section 110(5)). For these reasons, I will assume in the remainder of this Article that the homestyle exemption continues to encompass nondramatic musical works.

<sup>8</sup> The FIMLA defines an “establishment” as “a store, shop, or similar place of business that is open to the general public for the primary purpose of selling goods or services.” 17

than a specified number of speakers or television sets.<sup>9</sup> Taken together, these new rules will make it significantly easier for business establishments to avoid paying license fees to performing rights societies for playing radio and TV broadcasts of copyrighted music to entertain their customers and employees.<sup>10</sup>

Given its narrow, albeit detailed, focus, the FIMLA seems at first glance to

---

U.S.C. § 101 (1999) (defining establishment). It defines a “food service or drinking establishment” as “a restaurant, inn, bar, tavern, or any other similar place of business in which the public or patrons assemble for the primary purpose of being served food or drink.” 17 U.S.C. § 101 (1999) (defining food service or drinking establishment).

<sup>9</sup> The FIMLA’s equipment requirements are exceptionally detailed. They provide that stores greater than 2000 square feet and bars and restaurants greater than 3750 square feet are exempt from paying license fees if, in the case of *audio performances only*, “the performance is communicated by means of a total or not more than 6 loudspeakers, of which not more than 4 loudspeakers are located in any 1 room of adjoining outdoor space.” 17 U.S.C. §§ 110(5)(B)(i)(I), (5)(B)(ii)(I) (1999). In the case of *audiovisual performances*, businesses are exempt if:

any visual portion of the performance or display is communicated by means of a total of not more than 4 audiovisual devices, of which not more than 1 audiovisual device is located in any 1 room, and no such audiovisual device has a diagonal screen size greater than 55 inches, and any audio portion of the performance or display is communicated by means of a total of not more than 6 loudspeakers, of which not more than 4 loudspeakers are located in any 1 room or adjoining outdoor space.

*Id.* §§ 110(5)(B)(i)(II), (5)(B)(ii)(II) (1999).

<sup>10</sup> See Jon M. Garon, *Media & Monopoly in the Information Age: Slowing the Convergence at the Marketplace of Ideas*, 17 CARDOZO ARTS. & ENT. L.J. 491, 525 (1999) (“The Fairness in Music Licensing Act changed the legal balance between the performing rights societies and the restaurant owners in favor of the restaurateurs and publicans.”); Jane C. Ginsburg, *Copyright Legislation for the “Digital Millennium”*, 23 COLUM.-VLA J. L. & ARTS. 137, 178 (1999) (“Given the terms of new § 110(5)(B), it is no longer possible to rationalize the provision as exempting ‘incidental uses’ of music; now music may be very much in the foreground of the business establishment’s operations, yet remain uncompensated.”).

The FIMLA did more than just broaden the homestyle exemption. It also created a new process for businesses to challenge the royalty rates charged by PROs. Previously, businesses seeking to challenge the reasonableness of ASCAP or BMI’s licensing rates were required to litigate the issue before the federal district court in New York charged with overseeing the antitrust content decrees governing the PROs’ activities. See *infra* Part I.A.2. Under the new rules, individual proprietors who own or operate fewer than seven non-publicly traded establishments may initiate a challenge by bringing suit before the federal district court in the seat of the federal circuit court where the business establishment is located. All challenges must be adjudicated within six months after they are filed. See 17 U.S.C. § 513 (1999).

As a concession to music copyright owners, the statute also provides that if a business asserts section 110(5) as a defense to an infringement action without having reasonable grounds for believing that its exemption are applicable, the plaintiff is entitled to recover twice the amount of the licensing fee the business should have paid for up three years, in addition to another other applicable damages. See 17 U.S.C. § 504(d) (1999).

be among the least notable copyright developments of 1998. However, the statute is noteworthy for two reasons. First, because it is at odds with a long-standing trend in United States law toward expanding the rights of copyright owners and narrowing the free use exemptions applicable to users of copyrighted works,<sup>11</sup> and second, because it breaches the United States' international copyright treaty obligations.<sup>12</sup>

Within days of the law's entry into force in January 1999, the fifteen-member European Community ("EC") challenged both the FIMLA and the homestyle exemption under the dispute settlement procedures of the World Trade Organization ("WTO"). The EC is acting on a complaint by the Irish Music Rights Organization that the FIMLA is causing its members to lose \$1.36 million annually in licensing royalties.<sup>13</sup> Canada, Australia and Switzerland soon joined the EC in seeking formal consultations with the United States, alleging that their songwriters and music publishers will also be denied foregone performance royalties.<sup>14</sup> At issue in the talks was whether the FIMLA violates the Berne Convention for the Protection of Literary and Artistic Works ("Berne"),<sup>15</sup> as incorporated into the Agreement on the Trade-Related Aspects of Intellectual Property Rights ("TRIPs Agreement"),<sup>16</sup> by authorizing secondary uses of broadcast music without the payment of license fees.

When the parties were unable to resolve their differences, on May 26, 1999, the EC requested the WTO to convene a dispute settlement panel to decide its complaint.<sup>17</sup> Under the rapid timetable for WTO dispute settlement, a three-

---

<sup>11</sup> See *infra* Part II.

<sup>12</sup> See *infra* Part III.

<sup>13</sup> See Daniel Pruzin, *EU Seeks WTO Talks on 1998 Changes to United States Music-Licensing Copyright Rules*, 16 INT'L TRADE REP. (BNA) 224, 224 (Feb. 10, 1999); Daniel Pruzin, *Three Countries Join EU-United States Talks on Rules Violations Under Copyright Act*, 16 INT'L TRADE REP. (BNA) 321, 321 (Feb. 24, 1999).

<sup>14</sup> Australia, for example, alleged that the United States is "a major source of performance royalties for its copyright holders, whose losses from the Fairness in Music Licensing Act are estimated at over \$1 million per year." Pruzin, *Three Countries Join*, *supra* note 13, at 321.

<sup>15</sup> Berne Convention for the Protection of Literary and Artistic Works, Sept. 9, 1886, 828 U.N.T.S. 221 (last revised at Paris, July 24, 1971) [hereinafter Berne Convention]. The United States ratified the Berne Convention on March 1, 1989. As of July 1999, 140 nations were parties to the Berne Convention. See *Contracting Parties Of Treaties Administered By World Intellectual Property Organization, Berne Convention* (visited Nov. 1, 1999) <<http://www.wipo.org/eng/ratific/e-berne.htm>> [hereinafter *Contracting Parties*] (listing parties to Berne Convention).

<sup>16</sup> See Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1C, LEGAL INSTRUMENTS—RESULTS OF THE URUGUAY ROUND vol. 31; 33 I.L.M. 1197, 1201 (1994) [hereinafter TRIPs].

<sup>17</sup> Australia, Japan and Switzerland reserved their third-party rights to participate in the

member panel of international trade and copyright experts will review the complaint and issue a decision in the Spring of 2000. The losing party may then appeal the panel's decision to the WTO's Appellate Body, whose decisions cannot be overturned except by a consensus vote of all 134 WTO member States.<sup>18</sup> For reasons explained in greater detail below, a ruling in favor of the EC seems likely. Thus, in the first year of the new millennium, Congress may be faced with an unprecedented choice: modify the Copyright Act to satisfy the demands of international trade jurists or face retaliatory trade sanctions.

Although the dispute over the FILMA is rather modest in monetary terms,<sup>19</sup> there are three reasons why the case has an importance far broader than might first seem apparent. First, the dispute comes at a time when the United States has adopted an aggressive international trade enforcement policy. The United States has been the most frequent and successful litigant before the WTO,<sup>20</sup>

---

proceedings. See *Overview of the State-of-Play of WTO Disputes* (last modified Aug. 6, 1999) <<http://www.wto.org/wto/dispute/bulletin.htm>> [hereinafter *State of Play*].

<sup>18</sup> As of November 23, 1999, there were 135 members of the WTO and TRIPs Agreements. See <<http://www.wto.org/wto/about/organsn6.htm>> (listing WTO members).

<sup>19</sup> The EC claims that music copyright owners in its fifteen member nations will lose \$30.3 million annual under the United States law. See Pruzin, *Three Countries Join*, *supra* note 13, at 321. By contrast, losses to the United States and Canada from the EC's ban on hormone-treated beef and its banana import system each total more than \$200 million dollars. See Daniel Pruzin, *United States Blocks EU Request for Banana Panel While Hormone Beef Issue Simmers at WTO*, 16 INT'L TRADE REP. (BNA) 945, 945 (June 2, 1999).

Nor are the royalties particularly large from the perspective of commercial establishments. In 1997, ASCAP, one of three United States PROs, estimated that the average restaurant paid a license fee of \$1.58 per day for the right to play broadcast music from ASCAP's repertory. See *Music Licensing in Restaurants and Retail and Other Establishments, Hearings Before the Subcomm. on Courts and Intellectual Property of the House Comm. on the Judiciary*, 105th Cong. 74 (1997) (statement of Wayland Holyfield, on behalf of ASCAP) [hereinafter *1997 Hearings*] (arguing that allowing establishments to play music without a license deprives songwriters of their property and adding that \$1.58 "is less than the cost of a tall cola where I come from").

In 1996, ASCAP's blanket license for retail establishments to perform broadcast music was \$153 per year for a store using three speakers, with \$31.50 for each additional speaker. BMI's blanket license ranged from \$60 per year for retail stores up to 1500 square feet to \$480 per year for stores of over 5000 square feet. Rates for restaurants and bars are based on different factors, including maximum room occupancy and entertainment expenses. See E. Scott Johnson, *Storecasting and the Copyright Law - Understanding the § 110(5) Exemption for Small Commercial Establishments* at S-10 in NATIONAL ASSOCIATION OF BROADCASTERS, LEGAL GUIDE TO BROADCAST LAW AND REGULATION (5th ed. 1996).

<sup>20</sup> Gary G. Yerkey, *United States Using WTO Dispute Resolution System Far More Aggressively Than Other Countries*, 16 INT'L TRADE REP. (BNA) 540, 540 (Mar. 31, 1999) (quoting a United States Trade Representative's statement that "the United States success rate in the WTO so far has been 'very strong.'"); see also Chad Bowman, *United States To*

using the dispute settlement system and the threat of trade sanctions to pressure other treaty parties to modify their national laws.<sup>21</sup>

The United States has been equally assertive in seeking to protect the intellectual property rights of American businesses, authors and inventors. In the first case decided under the TRIPs Agreement, the United States successfully sued India for failing to protect pharmaceutical and agricultural patents.<sup>22</sup> Its efforts in the area of copyright law have proved equally fruitful. In the last three years, the United States reached favorable settlements in complaints against Ireland, Japan and Sweden, all of which agreed to augment their national copyright statutes to provide increased levels of copyright protection and enforcement that the United States claimed was compelled by the Berne and TRIPs treaties.<sup>23</sup> In addition to these actions, complaints against Greece (for unauthorized broadcasts of American movies and television programs) and Denmark (for inadequate *ex parte* enforcement measures in civil infringement cases) remain on hold pending consultations between the parties.<sup>24</sup>

This strong enforcement stance makes the FIMLA dispute—the first challenge to American intellectual property laws to come before the WTO—particularly embarrassing for the United States. Indeed, the Register of Copyrights, the former Commissioner of Patents and Trademarks, and the Secretary of Commerce all stressed to Congress that a broad licensing exemption was suspect under the Berne and TRIPs treaties and warned that the

---

*Use WTO Dispute Settlement Process To Press For TRIPs Compliance, Official Says*, 15 INT'L TRADE REP. (BNA) 1959, 1959 (Nov. 25, 1998) (characterizing the United States experience with dispute settlement under TRIPs as "satisfactory").

<sup>21</sup> For example, when the United States perceived that the EC's import restrictions on bananas and hormone-treated beef violated WTO agreements, it filed and won two hard-fought cases. When EC nations refused to alter their trade laws to comply with those rulings, the United States swiftly imposed punitive trade sanctions on a variety of European goods. See Pruzin, *supra* note 19, at 945 (summarizing disputes).

<sup>22</sup> See *India - Patent Protection for Pharmaceutical and Agricultural Chemical Products*, Status Report by India, (Apr. 16, 1999) available in 1999 WL 231665.

<sup>23</sup> See Gary G. Yerkey, *United States, Sweden Settle Dispute Over Intellectual Property Protection*, 15 INT'L TRADE REP. (BNA) 2065, 2065 (Dec. 9, 1998) (noting that the Swedish Parliament adopted new legislation to enhance provisional remedies available to copyright owners in civil cases); *US Withdraws Request for WTO Panel on Ireland IP After Understanding Reached*, 15 INT'L TRADE REP. (BNA) 269, 270 (Feb. 18, 1998) (reporting that the United States and Ireland concluded an "understanding" in which Ireland committed to enact copyright legislation relating to translations of official works, architectural works, anonymous and pseudonymous works, ownership of rights in films, and exceptions to exclusive rights); *Record Firms See More Gold in Oldies in Wake of US-Japan Copyright Pact*, J. COMMERCE, Jan. 28, 1997, at 3A (reporting settlement of dispute between United States and Japan over the latter's failure to protect sound recordings published in the United States prior to 1971).

<sup>24</sup> For a compendium of all disputes filed with the WTO's Dispute Settlement Body and copies of reports by the WTO panels and Appellate Body, see *State of Play*, *supra* note 17.

EC would challenge such an exemption were it enacted.<sup>25</sup> Yet Congress chose to disregard their warnings in its rush to split the difference between business interests who wanted a total exemption for secondary uses of broadcast music and PROs and copyright owners who opposed any relaxation of the homestyle exemption.<sup>26</sup> Given the years of negotiation required to reach this compromise, it is uncertain whether Congress will change its stance if WTO jurists agree with the EC that section 110(5) is incompatible with the treaties.<sup>27</sup> If it does not, the United States will find it increasingly difficult to continue pursuing an aggressive international trade and intellectual property enforcement policy against other treaty parties.

Congress' willful refusal to follow international copyright law illustrates the second way in which the FIMLA dispute is important. Since ratifying the

---

<sup>25</sup> See Mar. 20, 1998 Letter from William M. Daley, Secretary of Commerce to Newt Gingrich, Speaker of the House of Representatives, *reprinted in* 56 PAT., TRADEMARK & COPYRIGHT J. (BNA), No. 1396, 740-41 (Oct. 15, 1998) ("we know that our trading partners will claim that [an earlier version of the FIMLA] is an overly broad exception that violates our obligations under . . . the Berne Convention . . . and TRIPs . . ."); see also Jan. 16, 1998 Letter from Bruce A. Lehmann, Assistant Secretary of Commerce and Commissioner of Patents and Trademarks to Hon. Howard Coble, Chairman, House Subcommittee on Courts and Intellectual Property, *reprinted in*, 56 PAT., TRADEMARK & COPYRIGHT J. (BNA), No. 1396, 740-41 (Oct. 15, 1998) ("We are seriously concerned, as you are, that, if enacted, Section 110(5) of H.R. 789 could be challenged by our trading partners, who could argue that it is an overly broad exception that would violate our obligations under the Berne Convention . . ."); Sept. 28, 1994 Letter of Marybeth Peters, Register of Copyrights to William J. Hughes, Chairman, House Subcommittee on Intellectual Property and Judicial Administration, *reprinted in* 56 PAT., TRADEMARK & COPYRIGHT J. (BNA), No. 1396, 741 (Oct. 15, 1998) ("My concern is that the proposed amendment to section 110(5) would do further violence to our Berne obligations."). For a more detailed discussion of these arguments and the FIMLA's legislative history, see *infra* Part II.B.5.b.

<sup>26</sup> In this respect, Congress confounded copyright experts, who predicted that the Berne Convention would act "as a brake on legislative creativity" and prevent legislators from "cut[ting] the baby in half" when faced with a dispute between copyright owners and the users of creative works. See Ralph Oman, *The Impact of the Berne Convention on United States Copyright*, 455 PLI/PAT 233, 248 (1996).

<sup>27</sup> The United States has so far complied with the few WTO decisions it has lost, although whether its modifications of United States law in the Shrimp-Turtle case are sufficient is a matter of debate among WTO member states. See *Asians Contest U.S. Shrimp/Turtle Rule, Call for Complete Lifting of Import Ban*, 16 INT'L TRADE REP. (BNA) 1250 (July 28, 1999); William R. Sprance, *The World Trade Organization and United States' Sovereignty: The Political and Procedural Realities of the System*, 13 AM. U. INT'L L. REV. 1225, at 1226-27, 1246 (1998) (discussing the conflict between United States membership in the WTO and concerns over United States sovereignty). In addition, bills are currently pending in Congress to create a WTO Dispute Settlement Review Commission empowered to examine rulings adverse to the United States to determine, *inter alia*, if they are arbitrary or capricious. Such findings could eventually force a vote on United States withdrawal from the WTO. See Trade Policy Reform Act, H.R. 2612, 106th Cong. §§ 4103-04 (1999).

Berne Convention in 1989 and the TRIPs Agreement in 1994, Congress has generally conformed its domestic laws to the requirements of international copyright treaties by steadily increasing legal protections for authors and copyright owners.<sup>28</sup> In those few areas where United States copyright law was arguably not compatible with the treaties, the United States sought to shield itself from international scrutiny.<sup>29</sup> The FIMLA—a plainly treaty-incompatible statute open to challenge by United States' trading partners before the WTO—is an exception to both of these trends.

A third reason for observers to be concerned about the FIMLA dispute concerns WTO jurists' interpretation of copyright treaty exceptions and limitations clauses. For more than a century since the founding of the Berne Union in 1886, these clauses have granted national governments discretion to balance the rights of copyright owners against other important societal goals, including the proliferation of knowledge and artistic expression, the promotion of freedom of expression and the development of culture.<sup>30</sup> Article 13 of the TRIPs Agreement broke new ground by adopting a three-step test to judge the legality of all exceptions and limitations on copyright owners' exclusive rights.<sup>31</sup> The precise meaning of article 13, and its relationship to the exceptions and limitations set out in the Berne Convention, are among the most ambiguous and contested issues in international copyright law.<sup>32</sup> Were WTO jurists to construe the three-step test narrowly, they might preclude member states from tailoring their copyright laws to achieve these vital objectives. For the United States in particular, a narrow construction of the three-step test would call into question the validity of many aspects of the fair use doctrine.

To avoid the dangers that an adverse WTO ruling poses, the United States

---

<sup>28</sup> The United States has enacted numerous revisions to the Copyright Act over the last decade to comply with its treaty obligations, including the two statutes that accompanied the FIMLA. See CRAIG JOYCE ET AL, *COPYRIGHT LAW* 34-44 (4th ed. 1998) (reviewing legislation); Ralph Oman, *US Enacts New Law on Internet Copyright*, IP Worldwide, Jan.-Feb. 1999, available in LEXIS, CURNWS File (reviewing the Digital Millennium Copyright Act).

<sup>29</sup> See Laurence R. Helfer, *Adjudicating Copyright Claims Under the TRIPs Agreement: The Case for a European Human Rights Analogy*, 39 HARV. INT'L L.J. 357, 379 & n.92 (1998) (noting that moral rights are excluded from TRIPs because of United States concerns over treaty-compatibility of its domestic laws); J.H. Reichman, *Universal Minimum Standards of Intellectual Property Protection under the TRIPs Component of the WTO Agreement*, 29 INT'L LAW 345, 366-67 (1995) (noting that the exception provided for rental rights for cinematographic works protects United States movie rental business).

<sup>30</sup> See Helfer, *supra* note 29, at 370-71 & nn.47-50 (citing authorities).

<sup>31</sup> See TRIPs, *supra* note 16, art. 13.

<sup>32</sup> See Neil W. Netanel, *The Next Round: The Impact of the WIPO Copyright Treaty on TRIPs Dispute Settlement*, 37 VA. J. INT'L L. 441, 459-60 & n.72 (1997) [hereinafter Netanel, *The Next Round*] (discussing relationship among the Berne Convention, TRIPs and the WIPO Copyright Treaty regarding article 13). For a more detailed discussion, see *infra* Part III.C.

should seek an amicable resolution with the EC before the WTO's Appellate Body issues a final ruling.<sup>33</sup> As this Article explains in greater detail below, although the United States can raise several plausible arguments in defense of the homestyle exemption and the FIMLA, it is highly probable that WTO dispute settlement jurists will rule in favor of the EC. Thus, whether the United State chooses to settle the dispute or litigates it to an unsuccessful conclusion, Congress will soon need to address whether it can comply with the WTO ruling while preserving the hard-fought and carefully-negotiated compromise that the FIMLA's detailed rules embody.

In this Article I seek to explain why Congress deliberately chose to ignore the United States' international trade and intellectual property policies when it enacted the FIMLA. Drawing on insights from law and economics, and from a study of the history of laws and licensing practices governing in-store performances, I demonstrate that Congress and the courts have enacted and then expanded an increasingly broad free use exemption for businesses who play radio and television music. The exemption stems from a desire to correct market failures created by the high transaction costs of licensing secondary uses of broadcast music. Rather than correcting these market failures, however, the successive revisions of the copyright law have had the opposite effect, diverting resources of PROs and collective associations of copyright users away from negotiating private licensing arrangements and toward seeking a further widening of the exemption in Congress and the courts. At the conclusion of the Article, I use insights from economics and history to develop a legislative reform proposal that is compatible with the United States' treaty obligations and creates incentives for music copyright owners and business users to reach an efficient private licensing agreement to resolve the FIMLA dispute.

Part I begins by identifying two distinct analytical approaches to analyzing copyright in general and secondary uses of broadcast music in particular: an economic efficiency approach and a distributional and fairness approach. Each of these approaches prescribes different roles for government intervention in the private licensing market for copyrighted works, and each has played a role in shaping the complex web of laws currently regulating the practices of the three PROs in the United States. These two analytical approaches also help to explain the widespread culture of resistance that has emerged among United States copyright users to paying for public performance rights, particularly for secondary uses of broadcast music.

Part II analyzes the history of legal regulation of secondary uses of

---

<sup>33</sup> It is unlikely, however, that the parties will settle their dispute. That the United States chose to temporarily block the WTO from forming a dispute settlement panel to review the FIMLA, together with its recent filing of fresh WTO challenges to EC trade and intellectual property laws, suggests that that a compromise without a formal ruling by WTO jurists is unlikely. See *U.S. Blocks EU Attempt to Establish WTO Panel on Copyright Act Provision*, 16 INT'L TRADE REP. (BNA) 776, 776 (May 5, 1999).

broadcast music in the United States since the advent of radio broadcasting in the 1920s. It describes the relationship between rent seeking by PROs in Congress and the courts and market failures for licensing secondary uses of broadcast music. Part II concludes that Congress' attempts to modify the Copyright Act to correct these market failures has had the paradoxical effect of increasing both rent seeking and user resistance to PRO licensing efforts, resulting in an increasingly broad exemption benefiting business establishments.

Part III identifies and critiques the international treaty arguments that the EC has leveled against the FIMLA and "homestyle exemptions" under the Berne Convention and the TRIPs Agreement, and the United States' response to those arguments. It explores in detail the difficult interpretive issues that WTO jurists are likely to encounter in analyzing the treaties' exceptions and limitations clauses, particularly each part of the controversial three-step test in article 9(2) of the Berne Convention and article 13 of the TRIPs Agreement. Part III, after explaining why the WTO panel and Appellate Body are likely to rule in favor of the EC, highlights the dangers to all treaty parties associated with a narrow interpretation of the treaties' exceptions and limitations clauses.

Finally, Part IV draws upon the economic and distributional arguments identified in Part I, the historical analysis developed in Part II, and the international treaty obligations discussed in Part III, to develop legislative reform options for Congress that are compatible with the United States' treaty obligations and that will encourage copyright owners and copyright users to reach an efficient private licensing agreement for secondary uses of broadcast music. In particular, Part IV rejects, on efficiency and political pragmatism grounds, proposals to repeal the FIMLA for foreign copyrighted music only and to require broadcasters to pay for in-store performances. Then, after assessing the advantages of private agreements over legislative solutions to the market failure problem, Part IV explores the differing incentives for private bargaining created if Congress restores a modified property rule entitlement to music copyright owners, or, in the alternative, enacts a liability rule compulsory license system and encourages the parties to bargain in its shadow.

#### I. EXPLAINING THE FIMLA: AN ECONOMIC EFFICIENCY AND DISTRIBUTIONAL ANALYSIS

To understand why Congress would endorse a statute that so clearly deviates from recent United States international trade and copyright policies requires stepping back to explore two distinct analytical approaches to secondary uses of broadcast music. Each of these approaches helps to explain the evolution and structure of the licensing market for these secondary uses, and each has played a prominent part in the opposing arguments copyright owners and users have raised to shape the legal rules regulating that market.

The first analytical approach adopts economic efficiency as its goal. It advocates granting broad exclusive rights to music copyright owners as the most effective way of creating a licensing system that transfers performance

rights to their most productive uses. Under this efficiency rubric, the principal concern is to facilitate private exchanges. Government intervention is limited to correcting market failures that result from high transaction costs and regulating excessive monopoly power that arises when copyright owners license their musical works collectively through PROs.

The second analytical approach focuses on distributional concerns. It questions the fairness of granting music copyright owners the unfettered right to demand royalties for secondary uses of broadcast music, particularly given the fees they have already collected from radio, television and cable stations for the same performances. This distributional approach envisions government intervention in the licensing market as an antidote to the monopoly pricing power of PROs and as a means to achieve an equitable allocation of entitlements between copyright owners and copyright users.

#### A. *The Economic Efficiency Approach*

##### 1. Copyright's Property Rules, Transaction Costs and Market Failures

The exclusive rights that national copyright laws confer upon the authors of creative works and their assignees are "quintessential property rule entitlements."<sup>34</sup> That is, anyone seeking to exploit one of those exclusive rights must obtain the prior permission of the copyright owner, which normally involves payment of a license fee.<sup>35</sup> In the absence of such prior permission, the copyright owner may seek an injunction to prevent unauthorized acts from occurring as well as damages necessary to deter future infringements.<sup>36</sup>

According to neoclassical copyright theorists,<sup>37</sup> granting copyright owners the exclusive right to control the exploitation of their creative works not only provides the incentives necessary to generate creative works in the first instance, it is also allocatively efficient. Once a copyrighted work is created, its owner's profit-maximizing incentives will encourage the transfer of the right to exploit that work to users who value it most highly, with value determined by the market's pricing system. The role of government in this conception of copyright is to establish a statutory regime that grants creators strong initial entitlements to control their works, and then to step back and allow the formation of licensing markets that facilitate the transfer of rights to their highest and best uses.<sup>38</sup>

Problems arise, however, where the presence of transaction costs impede the

---

<sup>34</sup> See Robert P. Merges, *Contracting into Liability Rules: Intellectual Property Rights and Collective Rights Organizations*, 84 CAL. L. REV. 1293, 1302 (1996) [hereinafter Merges, *Contracting into Liability Rules*].

<sup>35</sup> See *id.*

<sup>36</sup> See *id.*

<sup>37</sup> See Neil W. Netanel, *Copyright and a Democratic Civil Society*, 106 YALE L.J. 283, 308 (1996) [hereinafter Netanel, *Democratic Civil Society*].

<sup>38</sup> See *id.* at 310.

formation of efficient licensing markets. In fact, bargaining for the exchange of intellectual property rights is rarely cost free. Copyright owners must search for and negotiate with potential licensees, and once a deal is struck, they must monitor the licensees' conduct and punish any violations of that deal.<sup>39</sup> So long as the aggregate of these costs do not exceed the value users place on exploiting a copyrighted work, both parties have an incentive to negotiate for a license.<sup>40</sup> But when transaction costs reach a sufficient magnitude, they will eventually exceed that value, creating a "market failure" for copyright licensing.<sup>41</sup> In such situations, potential licensees must either refrain from using the work or use it illegally without the copyright owner's permission.<sup>42</sup>

Three regulatory responses to the phenomenon of market failure are possible. First, the government may convert the property rule entitlement to a "liability rule." Second, it may permit the free use of the work. And third, it may eschew any regulatory intervention and allow copyright owners to structure private solutions to the market failure problem. I briefly outline each of these responses and their drawbacks below.

Liability rules function on the principle of "take now, pay later." They permit users to exploit the copyrighted work without the prior permission of its owner provided that they compensate the owner for that use after the fact. In the copyright context, liability rules take the form of statutory or judicial compulsory licenses. These are government-set royalty rates the payment of which entitles any licensee to use the work.<sup>43</sup> By eliminating the need to locate licensees, bargain over price and transfer assets from one party to the other, compulsory licenses reduce transaction costs and thus facilitate many transfers that would otherwise not occur.<sup>44</sup> However, they also create inefficiencies, as copyright owners and users expend scarce resources lobbying the legislature over how to structure and revise the compulsory license system.<sup>45</sup>

The free use approach is premised on a different solution to the market failure problem. Rather than establishing a fixed fee for all users, the government might simply eliminate the copyright owners' legal entitlement over certain modes of exploiting their works, particularly modes that are

---

<sup>39</sup> See ROBERT COOTER & THOMAS ULEN, *LAW AND ECONOMICS* 84 (2d ed. 1997) (identifying these transaction costs).

<sup>40</sup> See *id.* at 82.

<sup>41</sup> See *id.* (recognizing that parties will not bargain if transaction costs exceed the productive gain of the bargain).

<sup>42</sup> See Jay M. Fujitani, Comment, *Controlling the Market Power of Performing Rights Societies: An Administrative Substitute for Antitrust Regulation*, 72 CAL. L. REV. 103, 107 (1984) (identifying these as two potential options for licensees where transaction costs are high).

<sup>43</sup> See Merges, *Contracting into Liability Rules*, *supra* note 34, at 1302.

<sup>44</sup> Government bodies administering a compulsory license also often serve record keeping and collection functions. See *id.* at 1295.

<sup>45</sup> See *id.* at 1299 (summarizing arguments against compulsory licenses).

considered socially valuable.<sup>46</sup> The uncompensated use of copyrighted works sanctioned by the fair use doctrine is often justified on precisely these grounds, with the scope of the doctrine tailored to the degree of market failure.<sup>47</sup> Legally sanctioned free uses of this sort eliminate transaction costs because no exchange need take place for the copyrighted work to be put to a productive use.<sup>48</sup> However, the free use approach is not without its dangers. Commentators have argued that free use should be enacted only if doing so would not substantially diminish authors' initial incentives to create.<sup>49</sup>

The final approach to market failure is to refrain from any regulation of the market. When faced with high transaction costs, copyright owners will naturally find creative ways to reduce them. Specifically, they will overcome collective action problems and conjoin their property rights to be administered by private collective rights organizations that engage in group-based licensing and enforcement of copyrighted works.<sup>50</sup> By offering a more or less uniform menu of licensing options to individual licensees, by pooling enforcement efforts and by fixing a predetermined formula for royalty distributions, these organizations significantly reduce, but do not eliminate, transaction costs without the initial intervention of the government.<sup>51</sup> However, these organizations also enjoy substantial market power to extract monopoly rents from licensees. They thus create their own market distortions that have long

---

<sup>46</sup> See Robert P. Merges, *The End of Friction? Property Rights and Contract in the "Newtonian" World of On-Line Commerce*, 12 BERKELEY TECH. L.J. 115, 130 (1997) ("Market failure occurs when the transaction costs of a voluntary transfer are so high that a consensual transfer is unlikely to take place spontaneously. In such a case, the law provides users of copyrighted works with the statutory defense of fair use.")

<sup>47</sup> See *id.*; see also Wendy Gordon, *Fair Use as Market Failure: A Structural and Economic Analysis of the Betamax Case and its Predecessors*, 82 COLUM. L. REV. 1600, 1614-15 (1982) (describing a three part test for determining when fair use should be awarded to a defendant in a copyright infringement action).

<sup>48</sup> See Robert P. Merges, *Of Property Rules, Coase, and Intellectual Property*, 94 COLUM. L. REV. 2655, 2657 (1994) (applying this principle to patent law). Free use can also be conceived of as the government's creation of a compulsory license system with a royalty rate of zero. See *id.*

<sup>49</sup> See Gordon, *supra* note 47, at 1614 (listing the impact on authors' incentives to create as an important consideration in an optimal fair use system).

<sup>50</sup> See 2 PAUL GOLDSTEIN, COPYRIGHT § 10.1.1, at 10:7 & n.19 (2d ed. Supp. 1999); see also Merges, *Contracting into Liability Rules*, *supra* note 34, at 1328-58 (discussing performing rights organizations and patent pools).

<sup>51</sup> For an explanation of why residual transaction costs will remain even after collective rights organizations have formed, see *infra* Part I.A.4. For a discussion of why bargaining between collective rights organizations and centralized associations of copyright users can reduce these residual transaction costs, see *infra* text accompanying notes 181-88 (discussing the NLBA agreement); see also *infra* Part IV.C.1 (discussing the advantages of private licensing agreements over statutory solutions).

attracted the attention of antitrust regulators.<sup>52</sup>

Each of these three solutions to the market failure problem may be further modified by private agreement. In the case of free uses, the parties may see advantages in trading exploitation rights recognized by statute or judicial decision for other sorts of access to copyrighted works.<sup>53</sup> In the case of liability rules, copyright owners and users may bargain around a government-created compulsory license to reach alternative licensing arrangements.<sup>54</sup> Finally, collective rights organizations, once formed, often negotiate industry-wide licensing agreements with centralized trade associations of copyright users, who have solved their own collective action problems and formed private organizations to bargain over royalties on a group basis.<sup>55</sup> In each instance, private agreements may result in a use of resources that is more efficient than regulated solutions to the market failure problem (in the case of compulsory licenses and free use exemptions), or than the initial licensing options offered by collective rights organizations to individual, unorganized copyright users.<sup>56</sup> This efficiency claim is, however, controversial in the case of users who bargain away their free use rights.<sup>57</sup>

---

<sup>52</sup> See generally STANLEY M. BESEN & SHEILA NATARAJ KIRBY, *COMPENSATING CREATORS OF INTELLECTUAL PROPERTY: COLLECTIVES THAT COLLECT* (1989) (providing an in-depth economic analysis of PROs and their licensing practices).

<sup>53</sup> See, e.g., Tom W. Bell, *Fair Use vs. Fared Use: The Impact of Automated Rights Management Information on Copyright's Fair Use Doctrine*, 76 N.C. L. REV. 557, 590-91 (1998).

<sup>54</sup> See Ian Ayres & Eric Talley, *Solomonic Bargaining: Dividing a Legal Entitlement to Facilitate Coasean Trade*, 104 YALE L.J. 1027, 1037-38 (1995).

<sup>55</sup> See, e.g., KOHN & KOHN, *supra* note 4, at 879-81 (providing examples of complex licensing agreements between PROs and industry-wide trade associations of copyright users); Stanley M. Besen et al., *An Economic Analysis of Copyright Collectives*, 78 VA. L. REV. 383, 398-99 & n.59 (1992) (citing negotiated agreements between PROs and the All Industry Music Licensing Committee that set license fees for radio and television stations and networks); Michael J. Freegard, *Collective Administration: The Relationship Between Authors' Organizations and Users of Works*, in 1985 COPYRIGHT 443, 445-51 (identifying numerous group agreements with user associations); see also BESEN & KIRBY, *supra* note 52, at 20 (stating that "negotiated agreements with associations representing user industries" are often "tailored to the industry being licensed").

<sup>56</sup> See Ayres & Talley, *supra* note 54, at 1036-39 (compulsory license agreements); Bell, *supra* note 53, at 599-600 (free use agreements); Freegard, *supra* note 55, at 448 (agreements between PROs and associations of copyright users).

<sup>57</sup> See Julie E. Cohen, *WIPO Copyright Treaty Implementation in the United States: Will Fair Use Survive?* 21 EUR. INTELL. PROP. REV. 236, 239-40 (1999) (critiquing commentators who view copyright law as "merely establish[ing] a set of default rules, which may be varied by contract"); see also *infra* Part IV.C.1.

## 2. Public Performance Rights, PROs and Government Regulation

For copyright owners seeking to license the public performance of copyrighted music, the market failure problem is especially acute because the transaction costs standing in the way of bargained-for exchanges are exceptionally high. These costs include identifying numerous potential licensees in disparate locations, negotiating with them over payment terms, monitoring compliance with each licensing agreement and taking legal action to prevent infringements.<sup>58</sup> A music copyright owner's public performance right would be worth little if she were required to undertake each of these activities on her own.

PROs formed in the United States in the first half of this century as a direct response to the prohibitive costs of individual licensing.<sup>59</sup> PROs reduce transaction costs in several significant ways. They provide a clearinghouse for users seeking licenses, they collect and distribute revenues to the songwriters, composers and publishers who are their members, they monitor the activities of licensees and they take enforcement action where necessary to vindicate their members' rights.<sup>60</sup> The largest cost savings are achieved through "blanket licenses" that authorize licensees to perform all of the songs within the PRO's repertory for a fixed fee. Blanket licensing serves the interests of both parties to the licensing transaction because "[m]ost users want unplanned, rapid, and indemnified access to any and all of the repertory of compositions, and the owners want a reliable method of collecting for the use of their copyrights."<sup>61</sup>

Blanket licenses are not without their critics, however. As a recent Congressional research report stated, "[t]he price of the blanket license and its unlimited nature have been controversial almost from ASCAP's first days of operation, especially among small business users who perform relatively small amounts of music."<sup>62</sup> From an antitrust perspective, blanket licenses eliminate competition among music copyright owners over the price of their works by

---

<sup>58</sup> See, e.g., BESEN & KIRBY, *supra* note 52, at 2-10 (explaining the economies of scale benefits inherent in PROs); Fujitani, *supra* note 42, at 107 (labeling the costs of individual transactions as "staggering").

<sup>59</sup> ASCAP was founded in 1914 by a group of composers, lyricists and music publishers. BMI was established in 1939 by radio broadcasters to create an alternative music licensing mechanisms that counteracted ASCAP's market power. Together, these two PROs control virtually all music licensing in the United States, although a third and much smaller organization, SESAC, Inc. licenses a small repertory specializing in country and gospel music. See KOHN & KOHN, *supra* note 4, at 863-67, 871-72.

<sup>60</sup> See BESEN & KIRBY, *supra* note 52, at 2-10; Merges, *Contracting into Liability Rules*, *supra* note 34, at 1329-30.

<sup>61</sup> *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1, 20 (1979).

<sup>62</sup> *Music Licensing Copyright Proposals: An Overview of H.R. 789 and S.28*, Congressional Research Service, at 4 (Aug. 18, 1998) [hereinafter *Music Licensing Copyright Proposals*].

linking the licensing of one work to the licensing of the entire repertory.<sup>63</sup> For this reason, ASCAP and BMI, the two largest PROs in the United States, have been subject to numerous antitrust challenges and currently operate under consent decrees designed to limit their market power.<sup>64</sup>

### 3. “Through to the Viewer” Licenses and Secondary Uses of Broadcast Music

Although the consent decrees validate the use of blanket licensing, they also require the PROs to offer alternatives.<sup>65</sup> In the case of radio, television and wired music networks, for example, the consent decrees require the PROs to offer a single license, known as a “through to the viewer” license, to the entire network and forbid them from demanding separate performance licenses from each of the network’s affiliated stations.<sup>66</sup> In this way, the PROs are forced to bargain with the more powerful networks rather than the weaker affiliates, with the costs of the license spread among the network’s members through contractual arrangements.<sup>67</sup>

---

<sup>63</sup> See BESEN & KIRBY, *supra* note 52, at 7-9; Besen, *supra* note 55, at 391-94 (commenting on the virtual monopoly over copyright use held by PROs).

<sup>64</sup> See *Music Licensing Copyright Proposals*, *supra* note 62, at 6. In brief, the consent decrees permit PROs to acquire only non-exclusive performance rights from their members, thereby allowing users to negotiate a license directly with the copyright owner. The PROs must also offer a blanket license to anyone who requests it and must charge equivalent rates to similarly situated users. Licensees may challenge these rates before a federal district court in the Southern District of New York known as the “Rate Court,” at which proceeding the PROs have the burden to prove that the rates are reasonable. *See id.*

<sup>65</sup> For example, PROs must offer radio and television broadcasters “per program” licenses which reflect the more limited use of music for particular programs. Under a per program license, broadcasters may perform any musical work in the PRO’s repertory in exchange for either a flat fee for each program in which music is performed or a percentage of the advertising revenues received for that program. This compensation scheme excludes revenues from programs that do not contain music within the repertory. *See Fujitani, supra* note 42, at 114 n.51. *See also KOHN & KOHN, supra* note 4, at 880-81 (characterizing per program licenses as a “modified blanket license”).

<sup>66</sup> *See United States v. Broadcast Music, Inc.*, 1966 Trade Cas. (CCH) ¶ 71,941 at 83,326 (S.D.N.Y. 1966); *United States v. ASCAP*, 1950-51 Trade Cas. (CCH) ¶ 62,595 at 65,752 (S.D.N.Y. 1950). These licenses are sometimes also referred to as “source licenses” since public performance rights “are cleared at the ‘source’ or initiating point in a performance chain.” *Music Licensing Copyright Proposals*, *supra* note 62, at 5 n.19. However, the term source license is also used to describe any licenses obtained directly from copyright owners rather than from PROs. *See KOHN & KOHN, supra* note 4, at 878-79.

<sup>67</sup> As the “Rate Court” explained in a recent decision applying the “through to the viewer” license to cable television operators, in the absence of such a restriction the PROs could use their market power:

to extract non-competitive fees by the simple expedient of demanding not only a license from the network—which conceivably has some bargaining power by virtue of its ability to control the choice of music to be included in its network programming—

The “through to the viewer” license is something of a misnomer, however, since it does not authorize the transmission of music to all viewers or listeners.<sup>68</sup> To the contrary, the PROs’ licensing agreements with radio and television broadcasters seek to prohibit anyone who receives the broadcast from performing it in public locations for direct or indirect financial gain.<sup>69</sup> Relying on this licensing reservation and on the Copyright Act’s “multiple performance doctrine,”<sup>70</sup> PROs have long demanded separate blanket licenses from businesses who play broadcast music, just as they have from businesses who use live or recorded music.<sup>71</sup>

---

but also a separate license from each of the affiliated stations, which lack this leverage since they do not control what music is included in the network programming that they air.

United States v. ASCAP (In re Turner Broadcasting Sys. Inc.), 782 F. Supp. 778, 790 (S.D.N.Y. 1991), *aff’d* 956 F.2d 21 (2d Cir. 1992).

<sup>68</sup> See *Music Licensing Copyright Proposals*, *supra* note 62, at 5 n.19. In addition, the “through to the viewer” licenses are not applicable to all broadcast music. For music used in non-network programming, individual radio and television stations must obtain their own performance licenses either from the PROs or from the copyright owners. See *id.* Such licenses would also be required to broadcast the music contained in locally produced or syndicated radio or television programs. See *id.*

<sup>69</sup> See *Music Licensing Practices of Performing Rights Societies: Hearings Before the Subcomm. on Intellectual Property and Judicial Administration of the House Comm. On the Judiciary*, 103d Cong. 275 (1994) [hereinafter *1994 Hearings*] (rebuttal statement of ASCAP) (“ASCAP’s licenses for broadcasters are limited to the performance by the broadcasters. Excluded from the scope of those licenses are performances which take place through the reception of programs by users who entertain their patrons with those receptions.”). An early version of the relevant language in the broadcaster licenses reads:

Nothing herein contained shall be construed as authorizing licensee to grant to others any right to reproduce or perform publicly for profit by any means, method or process whatsoever, any of the musical compositions licensed hereunder or as authorizing any receiver of any such broadcast rendition to public perform or reproduce the same for profit, by any means, method or process whatsoever.

STANLEY ROTHENBERG, COPYRIGHT AND PUBLIC PERFORMANCE OF MUSIC 24-25 (1954).

<sup>70</sup> According to the “multiple performance doctrine,” each retransmission of a performance is an act of exploitation over which the copyright owner may exercise control. See, e.g., H.R. REP. NO. 94-1476, at 63 (1975) (“[A] singer is performing when he or she sings a song; a broadcasting network is performing when it transmits his or her performance . . . ; a local broadcaster is performing when it transmits the network broadcast; a cable television system is performing when it retransmits the broadcast to its subscribers. . . .”); see also MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT § 8.18[A] at 8-193 to 8-194 (1999).

<sup>71</sup> See *Broadcast Music, Inc. v. Moor-Law, Inc.*, 527 F. Supp. 758, 763-64 (D. Del. 1981) (explaining application of blanket licenses to nightclubs and bars and rejecting antitrust challenge to same), *aff’d*, 691 F.2d 490 (3d Cir. 1982). Courts have recognized that the rationale for blanket licensing is particularly compelling in the case of diffuse copyright users who often have little control over selecting the particular musical works performed on their premises. See *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1, 20 (1979); *Moor-Law*,

The net effect of this licensing system permits PROs to collect two sets of royalties: one set from the radio and television stations who broadcast copyrighted music to the public and a second set from commercial establishments for the in-store performance of those same broadcasts. From an economic perspective, this dual licensing system functions as “a risk-sharing mechanism” that enhances the public distribution of copyrighted works. “By providing authors with rights at multiple stages . . . the Copyright Act enables authors to share the risks by lowering the price of the initial sale license (hence encouraging uptake), and then earning income later.”<sup>72</sup> Stated more concretely, collecting two sets of royalties theoretically allows PROs to charge broadcasters lower license fees to transmit music to listeners and viewers located in homes, cars and offices than the fees they would be forced to charge if broadcasters, rather than commercial establishments, were required to pay for in-store performances as well.<sup>73</sup> At the margins, these increased fees, if they cannot be fully passed on to advertisers, would cause the stations to broadcast less copyrighted music to the public.

#### 4. The Effects of Enforcement Costs and User Resistance on PRO Licensing Practices

As explained above, music copyright owners successfully reduced the instances of market failure by creating PROs to license their works to users. Government intervention occurred only much later to limit the monopoly power that results from blanket licensing. But even without government regulation, PROs would face significant market constraints on the prices they charge to commercial establishments. These constraints have two related sources: first, the enforcement costs associated with policing unauthorized performances, and second, the resistance by music copyright users to paying license fees.

The relatively high cost of enforcement stems from the public goods character of copyrighted music and the nature of the mass marketplace. Musical works are non-rivalrous, meaning that multiple users can consume them at no additional marginal cost.<sup>74</sup> They are also widely dispersed in society through broadcasts and the sale of records. For these two reasons, many free riders will escape detection even where copyright owners band

---

*Inc.*, 527 F. Supp. at 763-64.

<sup>72</sup> Jeremy Thorpe, *Collective Licensing of Copyright: Options For Competitive Reform*, 5 AGENDA 213, 214-15 (1998). Compare *infra* Part I.B.1 (discussing allegations by commercial establishments that dual licensing permits “double dipping” for fees).

<sup>73</sup> See 1994 Hearings, *supra* note 69, at 275 (rebuttal statement of ASCAP). For an evaluation of how this argument operates in practice, see *infra* Part III.F.1.c.1).

<sup>74</sup> See *Moor-Law, Inc.*, 527 F. Supp. at 763 (noting that “unlike private goods (e.g. apples), one can use a public good without leaving any less for others to consume. Once a musical composition is created, the marginal cost of additional consumption is zero”).

together in organizations that devote significant resources to enforcement.<sup>75</sup> The enforcement gap is particularly wide for commercial establishments, which are far more numerous than broadcast stations or theaters and whose use of copyrighted music is often a subsidiary aspect of their business operations.

When perfect policing of music performances is impossible, an economically rational response is to minimize enforcement costs by reducing the number of infringers and increasing the number of licensees. The PROs adopted a carrot and stick strategy to achieve this objective. First, they used aggressive, high profile litigation to signal that infringers would be treated severely if caught performing copyrighted music.<sup>76</sup> Second, they sought to make licensing a more attractive option by lowering their blanket license rates. The net result was lower blanket license fees but a higher percentage of licensed businesses. As the court in *Broadcast Music, Inc. v. Moor-Law, Inc.* explained:

While normal competitive forces do not operate in this market, it is not true that BMI's price for its [license to bars and nightclubs] is unconstrained. . . . [T]he free rider problem does provide a significant constraint on the price BMI charges. *The higher the price it charges, the greater the resistance of [business] users is likely to be, and, conversely, the lower the price, the lower the resistance will be.* Since the free rider problem tends to make BMI's enforcement costs high and can, indeed, cause increased costs to more than consume increased revenue from a higher price, BMI considers this problem when setting a price.<sup>77</sup>

The resistance by copyright users described by the court in *Moor-Law* affects the market for performance licenses in two distinct ways. First, resistance inhibits the PROs' power to charge monopoly license fees. In fact, if the enforcement costs generated by user resistance are high enough, license fees will be reduced to the same rate as they would be under competitive conditions.<sup>78</sup> For this reason, resistance by users actually helps to counteract the market distortions blanket licensing engenders, even in the absence of government regulation. Licensing rates approaching the competitive market price are particularly likely to result when centralized associations of copyright users collectively negotiate license rates with PROs.<sup>79</sup>

---

<sup>75</sup> *See id.*

<sup>76</sup> The early history of ASCAP, for example, involved enforcement efforts so aggressive that one commentator has characterized the organization as "little more than a cost-spreading club for copyright litigation." Merges, *Contracting into Liability Rules*, *supra* note 34, at 1330.

<sup>77</sup> *Moor-Law, Inc.*, 527 F. Supp. at 764 (emphasis added).

<sup>78</sup> *See* Lionel S. Sobel, *The Music Business and the Sherman Act: An Analysis of the "Economic Realities" of Blanket Licensing*, 3 LOYOLA L.A. ENT. L.J. 1, 38 (1983).

<sup>79</sup> *See 1994 Hearings*, *supra* note 69, at 89 (statement of Marvin Berenson, Vice President and General Counsel, BMI) ("In an effort to reduce the cost of licensing . . . BMI will negotiate master license agreements with an association of small business which use

Second, resistance by users can create resource inefficiencies. Prior to the time when a deal is struck, resistance causes both parties to the putative licensing transaction to divert time and money away from productive activities.<sup>80</sup> Copyright owners, for example, invest resources in education campaigns to persuade copyright users about the benefits of complying with the law and in enforcement actions against users who fail to comply.<sup>81</sup> Copyright users, by contrast, expend resources to devise additional ways of evading detection or making enforcement more difficult.<sup>82</sup> Ultimately, these indirect costs generated by user resistance may encourage the parties to reach a mutually acceptable licensing agreement. Until such an agreement is reached, however, resistance both dissipates resources and acts as an additional transaction cost that impedes private bargaining and magnifies the failure in the licensing market.

### B. *The Distributional and Fairness Approach*

Whether copyright owners and users ultimately perceive the transaction cost-reducing benefits of licensing agreements cannot, however, be determined solely from a cost-benefit perspective. Economists have long been aware that non-monetary factors may cause the parties to miscalculate the advantages of reaching an agreement. Such miscalculations are particularly likely to occur “when the parties are committed to conflicting moral positions about fairness” or where they harbor “hostility” toward one another.<sup>83</sup>

Precisely such conflicting moral positions and hostility have pervaded the

---

music. Such an agreement is administered by the association for the benefit of its members and will usually provide a reduced rate.”); *see also* Besen, *supra* note 55, at 398-99 (when licensees negotiate with PROs in groups, the PRO “may be forced to set fees, even all-or-none fees, that leave a portion of the surplus to licensees”).

<sup>80</sup> Cf. Richard L. Hasen & Richard H. McAdams, *The Surprisingly Complex Case Against Theft*, 17 INT’L REV. L. & ECON. 367, 371 (1998) (arguing that theft is inefficient because of its “indirect costs,” including (a) investments thieves make in theft and (b) defensive measures taken by owners). Because copyright law grants to songwriters and publishers the right to control public performances of music and subjects infringers to civil and criminal penalties, unauthorized performances can be seen as a form of theft.

<sup>81</sup> See John M. Kernochan, *Music Performing Rights Organizations in the United States of America: Special Characteristics; Restraints; and Public Attitudes*, in 21 COPYRIGHT 389, 393 (1985) (advocating massive educational efforts to change user resistance to paying for performance licenses).

<sup>82</sup> The resistance strategies adopted by music copyright users, which overlap with rent seeking activities, include: (1) pooling funds to fight PROs in litigation, (2) lobbying for legislation to exempt particular users or uses or to create favorable compulsory licenses (3) lobbying for laws to curb particular enforcement activities by the PROs, (4) contesting coverage and payment of licenses both in and out of court and asserting meritless defenses and (5) challenging the PROs’ structure and licensing arrangements using antitrust laws. *See id.* at 393-94. For a further discussion of rent seeking, *see infra* Part II.A.

<sup>83</sup> COOTER & ULEN, *supra* note 39, at 85, 86.

music licensing market, with users' resistance to paying fees rooted not merely in economic self-interest but also "in incredulity, lack of comprehension, [and] a want of sympathy for the [public performance] right."<sup>84</sup> In the case of secondary uses of broadcast music, resistance has coalesced around three clusters of arguments focused on distributional and fairness concerns. Because these three arguments are likely to surface during the WTO dispute settlement proceedings and their aftermath as justifications for the United States' music licensing legislation, each of them merits discussion.

### 1. "Double Dipping" for Licensing Fees

The most strident objection voiced by commercial establishments is that copyright owners are "double dipping" for license fees. Double dipping occurs, the establishments allege, because copyright owners collect a second set of royalties for performances of music for which they have already received license fees from broadcasters.<sup>85</sup> This practice is unfair both because it targets one class of recipients to pay for broadcast music that any member of the public can hear free of charge and because it provides excessive compensation to copyright owners.<sup>86</sup> Businesses using broadcasts as background music rather than to attract or influence the behavior of customers perceive double dipping to be particularly inequitable. They assert that background music confers only a de minimis financial benefit and thus should not require a license.<sup>87</sup>

---

<sup>84</sup> Kernochan, *supra* note 81, at 393. See, e.g., 1997 Hearings, *supra* note 19, at 221 (statement of Pete Madland, President, Tavern League of Wisconsin) ("Being forced to pay anywhere between \$300—\$1,000.00 a year to simply turn on a TV or radio is wrong.").

<sup>85</sup> According to Stephen Barba, President of the Balsams Grand Resort Hotel:

ASCAP and BMI can hit up a hotel or restaurant for licensing fees on background music that comes over television and radios. That is patently unfair because the rights to use that music have already been paid for, usually many times over, by television and radio stations.

I want to give you an example to be sure you understand what I mean by unfair "double dipping." Think about when you see Michigan State's marching band play a song at halftime of a nationally televised football game. Now guess how many times ASCAP and BMI collect fees when that song is played over the air. Once? Twice? Three times? No, they collect fees five times from five different sources—once each from the stadium, the national TV network, the local TV station, the local cable system, and—finally—from the bar that is showing the game.

*Music Licensing and Small Business, Hearing Before the House Committee on Small Business*, 104th Cong. 67 (1996) [hereinafter 1996 Hearings].

<sup>86</sup> See Julie B. Raines, *The Fairness in Musical Licensing Act: The Tavern Bill Casts a Shadow*, 20 HASTINGS COMM. & ENT. L.J. 169, 189-90 (1997) (businesses "believe they are being singled out to pay licensing fees for the rebroadcast of radio and television signals when the rest of the world can tune in for free").

<sup>87</sup> See 1994 Hearings, *supra* note 69, at 137 (statement of Guy Gregg, Nat'l Restaurant Ass'n) ("The presence of background music in a restaurant or tavern . . . is genuinely incidental, not in any way used to attract customers."); *id.* at 117 (statement of Joe Johnson,

PROs and music copyright owners respond that they are justified in seeking such fees because businesses derive a financial benefit from performing broadcast music that is distinct from the benefit accruing to radio, television and cable stations, namely the use of music to entertain customers or increase the productivity of employees.<sup>88</sup> Although that financial benefit may be indirect for background music, it nevertheless contributes to the businesses' overall profitability.<sup>89</sup> In addition, PROs contend that the royalty fees paid by broadcasters and cable companies are priced to exclude the separate performances by commercial establishments.<sup>90</sup>

## 2. Abuses of Monopoly Power

A second argument businesses invoke to contest the payment of license fees focuses on the PROs' abuse of their monopoly pricing power. This argument is based not on any economic theory, but rather on the claim that PROs are overreaching in various ways in the manner in which they license secondary uses of broadcast music.

First, businesses claim that the "all or nothing" nature of blanket licensing forces them to purchase rights to more copyrighted music than they are ever likely to consume.<sup>91</sup> In particular, because the content of the broadcasts is beyond their control, businesses must purchase licenses from all three PROs to avoid claims of infringement—a fact in tension with the underlying rationale for blanket licensing.<sup>92</sup> Second, commercial establishments assert that PROs provide them with insufficient information about how blanket license fees are calculated or the identity of the songs in their repertoires.<sup>93</sup> This information deficit prevents users from ascertaining whether the PROs are charging equivalent rates to similarly situated users and from making an informed choice between broadcast music and other alternatives.<sup>94</sup> Finally, businesses

---

Nat'l Licensed Beverage Ass'n) ("There is little economic advantage to us in having pleasant radio or other background music in a restaurant or in having a television on the bar for our customers.").

<sup>88</sup> See *id.* at 275 (rebuttal statement of ASCAP).

<sup>89</sup> *Music Listening Copyright Proposals*, *supra* note 62, at 23 (noting that "parsley, which is incidental to food service, is paid for—similarly, incidental music, which is performed because it attracts patrons, should be paid for").

<sup>90</sup> See *1994 Hearings*, *supra* note 69, at 275 (rebuttal statement of ASCAP). See *infra* Part III.C.3.a.3 (evaluating this claim).

<sup>91</sup> See *Raines*, *supra* note 86, at 192 (business owners "argue that they use only a fraction of the thousands of song titles which they are currently licensed to use").

<sup>92</sup> See *Broadcast Music, Inc. v. Moor-Law, Inc.*, 527 F. Supp. 758, 766 (D. Del. 1981), *aff'd*, 691 F.2d 490 (3d Cir. 1982) ("When the only option the seller offers is all-or-nothing, the buyer presumably wants to deal with as few sellers as possible.").

<sup>93</sup> See *1996 Hearings*, *supra* note 85, at 191 (submission of Music Licensing Coalition) (asserting that licensees "get no product information, no comparison shopping opportunities, and no way to choose an alternative product . . .").

<sup>94</sup> See *e.g.*, *1996 Hearings*, *supra* note 85, at 3 (statement of Rep. Meyers). Alternatives

claim that they have no practical way to dispute unfair or excessive license fees.<sup>95</sup> Although the antitrust consent decrees permit licensees to challenge royalty fees before a Rate Court, that court is located in New York, and litigation before it is prohibitively expensive in comparison to the amount of license fees at stake.<sup>96</sup>

The PROs defend the blanket licensing as the only practical way for many businesses to purchase access to their repertoires.<sup>97</sup> They also stress the importance of blanket license royalties to their members' livelihoods and creative efforts.<sup>98</sup> With respect to information about their repertoires and licensing practices, the PROs assert that such information is already widely available, and that it would be impractical to provide the additional data commercial establishments seek without incurring significant costs or disclosing private or commercially sensitive information.<sup>99</sup> Finally, PROs claim that the strictures of the consent decree are sufficient to control any alleged abuses of monopoly power, and that the Rate Court's expertise in setting reasonable license rates is preferable to a system of local arbitration that would result in different fees for identical uses.<sup>100</sup>

### 3. Overly Aggressive Licensing and Enforcement Tactics

A third argument invoked by businesses concerns the strong-arm approach that PROs use to compel the purchase of blanket licenses. ASCAP and BMI have been accused of using harassing tactics to compel the purchase of blanket licenses by monitoring commercial establishments and threatening litigation.<sup>101</sup>

---

to broadcast music include recorded music or the services of a background music service such as Muzak. If businesses could conclusively ascertain the songs in each PRO's repertoire, they could purchase a license to perform recorded music from a single PRO or, in theory, negotiate a license directly with the music copyright owners.

<sup>95</sup> See, e.g., *1994 Hearings*, *supra* note 69, at 120-21 (statement of Michael Leonard on behalf of Nat'l Licensed Beverage Ass'n); *id.* at 127 (statement of John Deion, on behalf of Nat'l Restaurant Ass'n).

<sup>96</sup> See, e.g., *1997 Hearings*, *supra* note 19, at 4-5 (statement of Rep. Coble); *id.* at 229 (statement of Peter Kilgore, General Counsel, Nat'l Restaurant Ass'n) (arguing that "for a business in California or in Florida or Indiana, or virtually any other place, to resolve this issue by going to the rate court in New York is cost-prohibitive").

<sup>97</sup> See *Moor-Law, Inc.*, 527 F. Supp. at 763, 767-72 (noting advantages of blanket licensing and rejecting night club owner's alternative licensing proposals based on use); see also *1994 Hearings*, *supra* note 69, at 22 (statement of Morton Gould, President Emeritus, ASCAP) (asserting that blanket licenses are "tailored for the industry being licensed").

<sup>98</sup> See *1997 Hearings*, *supra* note 19, at 131 (statement of Mac Davis, on Behalf of BMI).

<sup>99</sup> See e.g., *1997 Hearings*, *supra* note 19, at 122 (statement of Patrick Collins, Senior Vice President for Licensing, SESAC, Inc.); *1994 Hearings*, *supra* note 69, at 336-37 (BMI response to Guy Gregg); *Music Listening Copyright Proposals*, *supra* note 62, at 24.

<sup>100</sup> See *Music Listening Copyright Proposals*, *supra* note 62, at 24.

<sup>101</sup> As one commentator described ASCAP's approach earlier this century: "An ASCAP

Other alleged acts of harassment and overreaching include burdensome and repetitive requests to prove music usage, confusing billing practices, solicitations containing misrepresentations and undercover surveillance tactics.<sup>102</sup>

Each of the PROs disputes this characterization of their activities and offers alternative narratives that emphasize the repeated and unjustified efforts by users to avoid payment of license fees.<sup>103</sup> They also stress their attempts to seek “cooperation and partnership in the licensing process” by negotiating with industry-wide business associations.<sup>104</sup>

## II. IDENTIFYING RENT SEEKING AND MARKET FAILURES: LEGAL REGULATION OF SECONDARY USES OF BROADCAST MUSIC IN THE UNITED STATES

Given the competing distributional and fairness arguments invoked by copyright owners and users, it might be expected that these groups would turn to Congress and the courts seeking favorable regulation of secondary uses of broadcast music. In fact, the history of music licensing in the United States reveals that both copyright owners and users have actively engaged in just such rent seeking. Although legislative and judicial battles over the contours of United States copyright law are hardly unique to in-store performances of music, what distinguishes this narrow slice of the public performance right from other copyright battles is the comparative success that copyright users have enjoyed in convincing Congress and the courts to adopt their position. Whereas other areas of United States copyright law reflects an expansion of copyright owners’ statutory rights,<sup>105</sup> the legal regulation of secondary uses of

---

representative would first offer to sell a blanket license. When the business refused to purchase one, ASCAP’s representatives would monitor the business, document its performance of ASCAP songs, and then sue for infringement. Many businesses chose to purchase licenses to settle the litigation.” Jessica D. Litman, *Copyright Legislation and Technological Change*, 68 OR. L. REV. 275, 291 n.83 (1989) [hereinafter Litman, *Copyright Legislation*].

<sup>102</sup> See, e.g., *1994 Hearings, supra* note 69, at 123-24 (statement of Michael Leonard, Nat’l Licensed Beverage Ass’n); *id.* at 137 (statement of Guy Gregg, Nat’l Restaurant Ass’n); see also *id.* at 199 (statement of Jerald Jacobs, American Society of Ass’n of Executives) (complaining of unfounded accusations of copyright infringement, litigation threats, and demands for on-the-spot signing of licenses).

<sup>103</sup> See, e.g., *1994 Hearings, supra* note 69, at 22-23 (statement of Morton Gould, ASCAP) (“We carefully train and instruct our field representatives in ASCAP’s operation in the law and in the proper and courteous way to approach [users] . . . . ASCAP is always happy to talk with users.”); *id.* at 332-38 (BMI response to Guy Gregg); *1997 Hearings, supra* note 19, at 110 (statement of Patrick Collins, SESAC, Inc.) (“The licensing organizations did not wish to be viewed as litigious and . . . filed lawsuits only as a last resort.”).

<sup>104</sup> *1997 Hearings, supra* note 19, at 111 (statement of Patrick Collins, SESAC, Inc.).

<sup>105</sup> See, e.g., Cohen, *supra* note 57, at 238 (“[T]he history of United States copyright law

broadcast music reveals something different: the slow but steady growth of a free use exemption benefiting commercial establishments.

This Part first briefly explains why copyright owners and users engage in rent seeking and the economic inefficiencies that rent-seeking creates, as compared to private bargaining. It then traces the history of the exemption for secondary uses of broadcast music, illustrating how rent seeking and market failures have affected the formation and scope of that exemption since the advent of radio broadcasting in the early 1920s.

#### A. *Copyright Rent Seeking in Congress and the Courts*

Public choice theorists teach that individuals and interest groups will devote significant resources to lobbying legislatures and litigating for legal change in courts<sup>106</sup> if doing so allows them to acquire a transfer of wealth through government regulation that is unavailable in the private marketplace.<sup>107</sup> Although the purpose of such “rent seeking”<sup>108</sup> is to increase private gain at the expense of other members of society, rent seeking is not objectionable from an efficiency perspective for this reason. Rather, it is generally perceived as inefficient because it “consumes resources without adding to the net social product.”<sup>109</sup> Resources “which could have been invested elsewhere in new

---

suggests that its operation will be shaped largely by special-interest lobbying. For most of the last century, that lobbying has been done almost exclusively by the copyright industries, and the resulting copyright legislation reflects this imbalance.”); Stewart E. Sterk, *Rhetoric and Reality in Copyright Law*, 94 MICH. L. REV. 1197, 1197 (1996) (noting arguments used to justify “two centuries of copyright expansion”).

<sup>106</sup> Although most of the public choice literature focuses on legislative lobbying, courts are frequently “the target of the same interest-group rent-seeking that plagues legislatures,” particularly by “interest groups who are unable to prevail in the political process.” A.C. Pritchard & Todd J. Zywicki, *Finding The Constitution: An Economic Analysis of Tradition’s Role in Constitutional Interpretation*, 77 N.C. L. REV. 409, 494 (1999).

<sup>107</sup> See Gordon Tullock, *The Welfare Costs of Tariffs, Monopolies and Theft*, 5 W. ECON. J. 224, 230 (1967).

<sup>108</sup> The “rents” referred to in rent seeking are the private benefits created through government regulation “that were unavailable other than through politics, or were more cheaply available through politics.” FRED S. MCCHESENEY, MONEY FOR NOTHING: POLITICIANS, RENT EXTRACTION, AND POLITICAL EXTORTION 10 (1997). See also Lanier Saperstein, *Copyrights, Criminal Sanctions and Economic Rents: Applying the Rent Seeking Model to the Criminal Law Formulation Process*, 87 J. CRIM. L. & CRIMINOLOGY 1470, 1483 (1997) (defining “rents” as “that part of the payment to an owner of a resource over and above that which the resource could command in its next highest use”).

<sup>109</sup> Fred S. McChesney, *Boxed In: Economists and Benefits from Crime*, 13 INT’L REV. L. & ECON. 225, 229 (1993) [hereinafter McChesney, *Boxed In*]. In theory, rent seeking can be efficient where it is used to block the enactment of an inefficient law or to achieve the enactment of an efficient one. However, efficient rent seeking exists only in the very limited situation where: (a) the law transfers ownership of noncash goods from one party to another, (b) the recipients value the good more than those from whom the good is taken, and (c) “the indirect costs of the rent seeking are lower than the transaction costs of the [good’s]

forms of production or innovation [are] instead spent lobbying government officials,” producing a substantial dead-weight loss.<sup>110</sup> The greater the advantages accruing from rent seeking as compared to other activities, the greater the resources that will be devoted to it.<sup>111</sup>

Because copyright’s governmentally-conferred exclusive rights offer substantial economic benefits to the owners of protected works, copyright law naturally generates rent seeking behavior both by those favoring and those opposed to copyright protection. Professor Jessica Litman’s detailed historical studies of the 1909 Act and 1976 Act revisions demonstrate the paramount role that interest group advocacy played in shaping United States copyright statutes.<sup>112</sup> During these interest group battles, copyright owners lobbied for expansive definitions of their exclusive rights while copyright users sought specially tailored free use exemptions or compulsory licenses that benefited their respective industries.<sup>113</sup>

A Congressional grant of certain statutory entitlements to copyright owners does not, however, guarantee that copyright users will bargain with owners for the right to use those entitlements. To the contrary, wealth dissipating rent seeking by copyright users and other interests groups is likely to continue.<sup>114</sup> The degree to which copyright users engage in such rent seeking will depend in part on the benefits that flow from rent seeking as compared to bargaining with copyright owners. Because “some sets of actors in the IPR [Intellectual Property Rights] field, as elsewhere, possess . . . a degree of influence in the legislative arena that is disproportionate to their economic leverage in purely private transactions,” these actors can sometimes obtain legislation that contains “a better deal than they could negotiate directly” with copyright owners.<sup>115</sup> For this reason, copyright users’ perceptions about the

---

sales.” Hasen & McAdams, *supra* note 80, at 370 n.8. It is unlikely that all of these conditions hold in the context of rent seeking over the Copyright Act.

<sup>110</sup> Saperstein, *supra* note 108, at 1491.

<sup>111</sup> *See id.* at 1489 (arguing resources will be invested in rent seeking “until rates of return are similar to other investments”).

<sup>112</sup> *See* Jessica Litman, *The Exclusive Right to Read*, 13 CARDOZO ARTS & ENT. L. J. 29 (1994) [hereinafter Litman, *Exclusive Right*]; Jessica Litman, *Copyright and Information Policy*, 55 L. & CONTEMP. PROBS., Spring 1992 at 185 (1992) [hereinafter Litman, *Copyright and Information Policy*]; Litman, *Copyright Legislation*, *supra* note 101; Jessica Litman, *Copyright, Compromise, and Legislative History*, 72 CORNELL L. REV. 857 (1987) [hereinafter Litman, *Compromise*].

<sup>113</sup> *See* Litman, *Copyright Legislation*, *supra* note 101, at 321 (demonstrating that during 1976 Act revisions, interest groups reached a consensus which “jelled around a strategy of granting broad rights in an expansive field of copyrightable works and subjecting the rights to specific, narrowly tailored exceptions”).

<sup>114</sup> *See* Saperstein, *supra* note 108, at 1492 (“Once the monopoly is granted, other interests do not sit passively by. Rather, they continue their rent seeking efforts.”).

<sup>115</sup> Merges, *Contracting into Liability Rules*, *supra* note 34, at 1313 (discussing examples of compulsory licenses and legislative efforts to limit ASCAP’s powers).

receptiveness of legislatures and the courts to reshaping copyright law in their favor can influence their resistance to copyright owners' licensing efforts and, in turn, affect the scope of market failures.<sup>116</sup> Although user resistance to PROs is not in itself a form of rent seeking, it interacts dynamically with rent seeking to distort market transactions.

#### B. *Tracing the History of Music Licensing for Commercial Establishments*

The history of legal and licensing battles over the secondary uses of broadcast music is long and tortuous.<sup>117</sup> What commentators have not explored, however, is the relationship between the legal rules in force during different periods of time and the development of a licensing market for in-store performances during those periods. The sections that follow trace that relationship and then summarize it in chart form. For each time period, the discussion identifies the licensing and enforcement efforts by PROs, the resistance by copyright users that those efforts engendered and the market failures that resulted. It then documents how Congress and the courts responded to those failures and ultimately created an increasingly broad licensing exemption that set the stage for the EC's complaint to the WTO.

##### 1. 1920s to 1931: The Initial Battle Over a Licensing Market

Congress first granted copyright owners the right to control public performances of their music in 1897. But it was the medium of radio broadcasting, which first entered into widespread use in the 1920s, that significantly enhanced the economic value of the public performance right.<sup>118</sup> At the same time, radio broadcasting made it essential for music copyright owners to adopt collective licensing and enforcement practices to control this new technology. In 1914, a group of composers and music publishers formed ASCAP to combat the culture of free music use that had developed among many commercial copyright users in the United States.<sup>119</sup> A decade later, ASCAP expanded its activities to include the fledgling radio industry. After a

---

<sup>116</sup> See Ralph Oman, *Source Licensing: The Latest Skirmish in an Old Battle*, 11 COLUM.-VLA J.L. & ARTS 251, 273 n.111 (1987) (former Register of Copyrights analyzing dispute between PROs and television broadcasters over licensing structure and noting that "[o]f course, it would have made no sense to negotiate while [broadcasters] had the chance to prevail in the courts or in Congress").

<sup>117</sup> For doctrinal analyses, see GOLDSTEIN, *supra* note 50, § 5.8.1, at 5:150 to 5:156; NIMMER & NIMMER, *supra* note 70, § 8.18[C], at 8-208 to 8-220; Burt A. Lazar, *Mere Reception in Public Under the Copyright Act of 1976: Exempt or Extinct*, 1 ALB. L.J. SCI. & TECH. 97, 113-19 (1991); David M. Lilenfeld, Note, *Why Congress Should Eliminate the Multiple Performance Doctrine*, 58 OHIO ST. L. J. 695, 716-25 (1997).

<sup>118</sup> See *Jerome H. Remik & Co. v. American Auto. Accessories Co.*, 5 F.2d 411, 412 (6th Cir. 1925).

<sup>119</sup> See Ruth Charles, *ASCAP—A Half Century of Progress*, 11 BULL. COPYRIGHT SOC'Y USA. 133 (1964).

brief period of permitting free use, ASCAP vigorously enforced the rights of its members, quickly winning a series of court cases against radio stations who refused to pay for the right to broadcast music over the airwaves.<sup>120</sup>

ASCAP then turned its attention to the secondary users of broadcast music—the hotels, stores and restaurants that used the new technology to attract and entertain their customers. As a result of an earlier judicial victory by ASCAP, these businesses could not use live music for this purpose without purchasing a performance license.<sup>121</sup> Naturally, they turned to broadcast music as a substitute.<sup>122</sup> ASCAP challenged this practice, actively seeking to license this new and potentially lucrative market. Where its licensing efforts were unsuccessful, ASCAP used the judicial process to enjoin infringers and compel them to negotiate for the right to perform broadcast music in their establishments. Copyright users stridently resisted both of these efforts, refusing to submit voluntarily to ASCAP's licensing demands, defending charges of infringement in court and introducing bills to abolish ASCAP and narrow the public performance right.<sup>123</sup>

As a result of these heated disputes, the market for secondary use licenses from the early 1920s to 1931 was unstable and still in a formative stage. Although both copyright owners and users might have achieved significant cost savings by negotiating industry-wide agreements over licensing rates, both found greater advantage in using their resources in other ways. For the newly created ASCAP, resources expended on compliance and enforcement made long-term economic sense because these efforts enhanced the organization's reputation, encouraged new members to join, and weaned businesses from a culture of free use. From the business users' perspective, resisting ASCAP and its licensing practices was equally sensible because it held out the prospect that the courts or Congress might sanction some free use of broadcast music.

---

<sup>120</sup> See Merges, *Contracting into Liability Rules*, *supra* note 34, at 1333 (outlining ASCAP's enforcement strategy against radio broadcasters).

<sup>121</sup> In an early and influential decision under the Copyright Act of 1909, ASCAP convinced the Supreme Court to interpret the "for profit" limitation on the public performance right to include performances that provided only an indirect financial benefit to users. See *Herbert v. Shanley*, 242 U.S. 591 (1917). After this ruling, businesses were required to purchase a license even if they did not charge their patrons a separate fee for hearing the music.

<sup>122</sup> See Kernochan, *supra* note 81, at 393.

<sup>123</sup> See, e.g., Litman, *Copyright Legislation*, *supra* note 101, at 291 & n.83 (noting users refusal to purchase a blanket performance license until after litigation commenced by ASCAP); Merges, *Contracting into Liability Rules*, *supra* note 34, at 1333 (ASCAP commenced a "series of lawsuits" against "early commercial users of radio – mostly retail stores and hotels – and helped ASCAP establish the right for compensation to *all* music played over the radio").

## 2. 1931 to 1975: Market Failure Emerges

In these early legal battles, it was ASCAP who ultimately prevailed. In 1931, the organization convinced a unanimous Supreme Court in *Buck v. Jewell-La Salle Realty Co.*<sup>124</sup> that a hotel using a radio receiver and loudspeakers to transmit an unlicensed radio broadcast to its public and guest rooms was performing the music contained in the broadcast.<sup>125</sup> The decision endorsed a “multiple performance” approach to the Copyright Act, granting copyright owners the right to control and collect royalties not only for an initial broadcast by a radio station, but also for any retransmissions of that broadcast by the commercial establishments receiving it.<sup>126</sup>

By clarifying the legal landscape in favor of music copyright owners, *Jewell-La Salle* confirmed the PROs’ right to control secondary uses of broadcast music. The decision became the basis for a widespread licensing practice under which ASCAP (and later BMI and SESAC, Inc.) collected royalties from commercial establishments that used loudspeakers to receive radio and television broadcasts.<sup>127</sup>

The PROs’ licensing efforts did not go unchallenged, at least initially. Copyright users seized upon two statements made by the Court in *Jewell-La Salle*, both of which suggested that an exemption for secondary uses of broadcast music might be justified under different facts. First, the Court limited its holding to situations where the radio station had not received a license to broadcast ASCAP members’ music to the public. Had such a license been obtained, the Court suggested, it might well have encompassed secondary uses by persons tuning into the broadcast.<sup>128</sup> Second, the Court implied that Congress could exempt secondary uses altogether once copyright owners gained adequate control over licensing radio broadcasts.<sup>129</sup>

---

<sup>124</sup> 283 U.S. 191 (1931)

<sup>125</sup> *See id.* at 197-98.

<sup>126</sup> *Id.* at 198 (“[N]othing in the [Copyright] Act circumscribes the meaning to be attributed to the term ‘performance,’ or prevents a single rendition of a copyrighted selection from resulting in more than one public performance for profit.”).

<sup>127</sup> *See* ROTHENBERG, *supra* note 69, at 24; Bernard Korman, *Performance Rights in Music Under Sections 110 and 118 of the 1976 Copyright Act*, 22 N.Y. L. SCH. L. REV. 521, 528 n.32 (1977); *see also infra* notes 135-37 and accompanying text (discussing PRO licensing practices during the 1960s and 1970s).

<sup>128</sup> *Jewell-La Salle*, 283 U.S. at 199 n.5 (“If the copyrighted composition had been broadcast by [the radio station] with plaintiffs’ consent, a license for its commercial reception and distribution by the hotel company might possibly have been implied.”).

<sup>129</sup> The Court stated:

It may be that proper control over broadcasting programs would automatically secure to the copyright owner sufficient protection from unauthorized public performances by use of a radio receiving set, and that this might justify legislation denying relief against those who in using the receiving set innocently invade the copyright, but the existing

Each of these statements became the fulcrum for disputes between copyright owners and users over secondary uses of broadcast music during the 1930s and early 1940s. The PROs responded to the Court's suggestions by continuing to collect royalties from commercial establishments tuning in to broadcasts and by redrafting their license agreements with radio (and later television) stations to preclude the possibility of an implied license flowing from the stations to the establishments.<sup>130</sup> Copyright users did not resist these licensing efforts in the courts.<sup>131</sup> Instead, they adopted a legislative strategy, introducing a flurry of bills in the years immediately following *Jewell-La Salle* to eliminate the multiple performance doctrine or to privilege the secondary use of broadcast music in some manner.<sup>132</sup> Between 1931 and 1937, thirteen different bills were introduced which would have reversed the holding in *Jewell-La Salle*. None of these bills was enacted, however.<sup>133</sup> Moreover, when in 1961 a Copyright Office study proposed applying a "through to the viewer" license to business users receiving radio and television broadcasts, the PROs criticized this proposal, and the Copyright Office abandoned it.<sup>134</sup>

---

statute makes no such exception.

*Id.* at 199 (footnotes omitted).

<sup>130</sup> ROTHENBERG, *supra* note 69, at 24-25 (reproducing licenses).

<sup>131</sup> Between 1931 and 1975, there are only two published cases dealing with secondary uses of broadcast music. *See* Society of European Stage Authors & Composers, Inc. v. New York Hotel Statler Co., 19 F. Supp. 1 (S.D.N.Y. 1937) (finding that hotel used master receiving set to broadcast song and relay it to speakers in private rooms; court rejected hotel's attempt to distinguish *Jewell-LaSalle* on ground that original radio broadcast was licensed); Twentieth Century Music Corp. v. Aiken, 422 U.S. 151 (1975) (rejecting multiple performance doctrine and narrowing *Jewell-LaSalle* solely to unlicensed broadcasts); *see also* Leo Feist, Inc., v. Lew Tendler Tavern, Inc., 117 U.S.P.Q. 272 (E.D. Pa. 1958) (applying *Jewell-LaSalle* to enjoin defendant who used unlicensed background music service to entertain customers). These cases do not, of course, reveal whether PROs took judicial enforcement actions which settled or did not result in the publication of an opinion.

<sup>132</sup> In addition, "the Copyright Office received numerous complaints from small businessmen who were being contacted by representatives" of PROs seeking to license their secondary use of broadcast music. Lazar, *supra* note 117, at 106-07.

<sup>133</sup> Korman, *supra* note 127, at 531 & n.50 (citing bills introduced in Congress after *Jewell-la Salle* and before 1957). In 1932, for example, six bills were introduced, each of which would have exempted the reception of any copyrighted work "by the use of receiving, reproducing, or distributing apparatus" in the absence of an admission charge. *See, e.g.*, H.R. 10364, 72d Cong. § 12 (1932). For a detailed discussion of the bills introduced to overturn *Jewell-La Salle*, and unsuccessful bills introduced in 1940, 1941 and 1957 to circumscribe the case in other ways, *see* Brief for Petitioners at 30-32, Twentieth Century Music Corp. v. Aiken, 422 U.S. 151 (1975) (No. 74-452).

<sup>134</sup> Compare STAFF OF HOUSE COMM. ON THE JUDICIARY, 87TH CONG., COPYRIGHT LAW REVISION, REPORT OF THE REGISTER OF COPYRIGHTS ON THE GEN. REVISION OF THE U.S. COPYRIGHT LAW at 30-31 (Comm. Print 1961) [hereinafter 1961 REGISTER REPORT] (arguing that any revised copyright statute "should exempt the mere reception of broadcasts from the public performance right, except where the receiver makes a charge to the public

Although copyright users' legislative reform efforts were not successful, their resistance appears to have affected their relationships with PROs outside of the legislative and judicial arenas. Between 1931 to 1975, PROs voluntarily refrained from enforcing the multiple performance doctrine to its full extent, declining to seek licenses from smaller businesses playing broadcast music. The scope of this licensing forbearance is uncertain, however. According to the PROs, this voluntary exemption covered only small commercial businesses using a radio receiver with a single built-in speaker.<sup>135</sup> Other sources, however, suggest that some larger commercial businesses using more than one speaker were also exempt.<sup>136</sup>

Whatever the exemption's precise scope, its existence is a clear manifestation of a market failure for licensing secondary uses of broadcast music. As ASCAP's General Counsel explained the organization's licensing practices during these years:

---

for such reception") with STAFF OF HOUSE COMM. ON THE JUDICIARY, 88TH CONG., COPYRIGHT LAW REVISION, PT. 2, DISCUSSION AND COMMENTS ON REPORT OF THE REGISTER OF COPYRIGHTS ON THE GEN. REVISION OF UNITED STATES COPYRIGHT LAW 283 (Comm. Print 1963) [hereinafter PART 2 DISCUSSION AND COMMENTS] (criticizing Register's proposal as "wholly unwarranted" because it would "appropriate the creations of authorship for the benefit of a special class of commercial users"). By 1964, the Copyright Office had retreated from its initial position and advocated instead an exemption only where a broadcast was retransmitted to a hotels private, not its public, rooms. See STAFF OF HOUSE COMM. ON THE JUDICIARY, 88TH CONG., COPYRIGHT LAW REVISION, PT. 3, DISCUSSION AND COMMENTS ON REPORT OF THE REGISTER OF COPYRIGHTS ON THE GEN. REVISION OF UNITED STATES COPYRIGHT LAW 238-41 (Comm. Print 1964) (statement of Barbara Ringer).

<sup>135</sup> See PART 2 DISCUSSION AND COMMENTS, *supra* note 134 at 290; *id.* at 283.

<sup>136</sup> See 1961 REGISTER REPORT, *supra* note 134, at 30-31 (stating Registers' understanding that PROs "have generally followed the policy of confining their demands for license fees to those establishments, such as the hotel in the *Jewell-La Salle* case, that retransmit broadcasts to their various rooms. Other similar organizations, however, may not have the same policy. And there have been complaints from some small establishments that they were asked to obtain performing licenses for the mere operation of receiving sets."). See also *Fortnightly Corp. v. United Artists Television, Inc.*, 392 U.S. 390, 405 n.3 (1968) (Fortas, J., dissenting) ("Nimmer, a leading authority in the copyright field, states that although 'the two major performing right societies, ASCAP and BMI, do not choose to enforce the *Jewell-La Salle* doctrine to its logical extreme in that they do not demand performing licenses from commercial establishments such as bars and restaurants which operate radio or television sets for the amusement of their customers, . . . such demands are made of hotels which operate in the manner of the LaSalle Hotel.' NIMMER, COPYRIGHT § 107.41, n.204 (1968)."). Professor Nimmer later conceded that this footnote was "misleading." See Brief for Petitioners, *supra* note 133, at 8; see also *Twentieth Century Music Corp. v. Aiken*, 356 F. Supp. 271, 274 n.4 (W.D. Pa. 1973) ("Herman Finkelstein, a witness for ASCAP, disputes the comment in Nimmer . . . that licenses have not been required from commercial establishments such as bars and restaurants which operate radio sets for the amusement of the customers . . . . We credit the testimony of Mr. Finkelstein that Nimmer is incorrect and that ASCAP has in fact been requiring licenses in many of these situations.").

As a matter of business policy, ASCAP did not attempt to license establishments which used only a home-type receiver with no further loudspeaker installation. In these instances, very small establishments of the “Mom and Pop” variety were treated as *de minimis* users. Indeed, ASCAP’s experience with small establishments which had one or two loudspeakers has been that many would refrain from using any music rather than pay even the minimum license fee of \$60 per year which ASCAP asked for such uses.<sup>137</sup>

This statement reflects the common sense proposition that where the financial benefits accruing to small businesses that perform broadcast music are minimal, licensing those businesses is not cost effective for PROs. Even if some of these businesses were willing to pay a nominal license fee, the transaction costs required to collect it would outweigh such a fee.

Faced with this market failure for in-store performance licenses, Congress intervened. The Register of Copyrights, troubled by the prospect of leaving “the free use of receiving sets . . . to the grace or forbearance of the performing rights organizations,”<sup>138</sup> drafted a proposal in 1965 to codify the PROs’ voluntary licensing practices.<sup>139</sup> The Register urged that the Copyright Act should exempt businesses who transmitted broadcasts using “ordinary” radio sets like those sold for “private [home] use” from paying license fees.<sup>140</sup> This proposal, with only slightly modified language, was included in several copyright revision bills that received widespread Congressional support.<sup>141</sup> Before these bills could be enacted, however, the Supreme Court altered the legal landscape.

### 3. 1975 to 1977: The Multiple Performance Doctrine Briefly Repudiated

Two years before a long overdue overhaul of the Copyright Act could be completed, the Supreme Court effectively repudiated the multiple performance

---

<sup>137</sup> Korman, *supra* note 127, at 528 n.32 (citing Brief for Petitioners, *supra* note 133, at 8, 9); accord GOLDSTEIN, *supra* note 50, § 5.8.1, at 5:155 (“There will be many uses for which even the costs of negotiating a blanket license will prove to be disabling.”).

<sup>138</sup> 1961 REGISTER REPORT, *supra* note 134, at 31.

<sup>139</sup> See Korman, *supra* note 127, at 531 (stating that this exemption “would have codified the holding of *Jewell-La Salle* and ASCAP’s post-*Jewell-La Salle* licensing practice”).

<sup>140</sup> See HOUSE COMM. ON THE JUDICIARY, 89TH CONG., COPYRIGHT LAW REVISION PT. 6: SUPPLEMENTARY REPORT OF THE REGISTER OF COPYRIGHTS ON THE GENERAL REVISION OF THE U.S. COPYRIGHT LAW: 1965 REVISION BILL XIX, 44 (Comm. Print 1965).

<sup>141</sup> See Brief for Petitioners, *supra* note 133, at 31-32 (discussing the legislative history of copyright revision bills). The exemption contained in the bills privileged the “communication embodying a performance or display of a work by the public reception of the transmission on a single receiving apparatus of a kind commonly used in private homes,” unless a direct charge was “made to see or hear the transmission; or the transmission [is] further transmitted to the public.” *Id.* at 32 (quoting S. 1361, 93d Cong.(1974)). This was later adopted as the so-called “homestyle exemption” in section 110(5) of the Copyright Act of 1976.

doctrine. *Twentieth Century Music Corp. v. Aiken*<sup>142</sup> concerned a small fast food franchise operator who installed four speakers in the ceiling of his business to play radio broadcasts for his employees and customers. Aiken had refused to purchase a license from ASCAP, which then brought an infringement action against him seeking to enjoin his unauthorized performances.<sup>143</sup> Although the Court acknowledged that ASCAP had, in reliance on *Jewell-La Salle*, issued more than 5100 licenses to commercial establishments across the United States to play broadcast and recorded music,<sup>144</sup> it nevertheless concluded that Aiken had not “performed” the musical works when he turned on the radio receiver in his establishment.<sup>145</sup>

The Court’s decision was animated by a desire to grant copyright owners limited monopoly powers over their creative works in order to serve copyright’s overarching purpose of “promoting broad public availability of literature, music, and the other arts.”<sup>146</sup> Licensing secondary uses of broadcast music did not serve this broad policy objective, since it authorized copyright owners to exact “multiple tribute” from both radio stations and commercial establishments that “would go far beyond what is required for the economic protection of copyright owners, and would be wholly at odds with the balanced congressional purpose” underlying the public performance right.<sup>147</sup> The Court buttressed its conclusion by asserting that a contrary decision would be both inequitable and unenforceable as a practical matter.<sup>148</sup>

The Court’s decision in *Aiken*, if implemented, would have prohibited PROs from collecting license fees for *any* secondary uses of broadcast music—a result far more sweeping than the narrow homestyle exemption that Congress was then considering.<sup>149</sup> PROs did not allow *Aiken* to survive for long, however.

---

<sup>142</sup> 422 U.S. 151 (1975).

<sup>143</sup> Aiken’s refusal to purchase a license provides an apt example of resistance by copyright users. His decision was based not on financial considerations, but rather on a fairness objection to paying for the use of broadcast music. See Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit in *Twentieth Century Music Corp. v. Aiken* at 61A (trial testimony of George Aiken) (“I could easily well pay the license but I think there comes a time in a business you have to say well is it really a law or isn’t it.”).

<sup>144</sup> *Aiken*, 422 U.S. at 162 n.12.

<sup>145</sup> See *id.* at 155.

<sup>146</sup> *Id.* at 156.

<sup>147</sup> *Id.* at 163 (footnote omitted).

<sup>148</sup> The inequity argument was premised on the belief that businesses would have “no sure way of [protecting themselves] against copyright infringement” from music copyright owners whose compositions were not controlled by ASCAP except by turning the radio off. NIMMER & NIMMER, *supra* note 70, § 8.18[A], at 8-204 to 8-205. The unenforceability argument was premised on the Court’s belief that any “evenhanded effort [by] copyright owners to license even a substantial percentage” of the many commercial establishments playing radio and television broadcasts would be futile. *Aiken*, 422 U.S. at 162.

<sup>149</sup> It is unclear whether PROs refrained from enforcing their licenses with commercial

They had already secured language in copyright revision bills to codify the multiple performance doctrine.<sup>150</sup> PROs now moved to repudiate the *Aiken* decision entirely by clarifying that secondary uses of broadcast music were licensable public performances unless they fell within the homestyle exemption's narrow confines.<sup>151</sup>

In effect, the PROs sought to restore the status quo found in all of the copyright reform bills introduced between 1966 and 1975. Examining only the statute's text, they appear to have succeeded; the exemption codified in section 110(5) of the 1976 Copyright Act is identical to the versions the PROs had agreed to prior to *Aiken*. The legislative history, however, belies this victory by adding significant ambiguities concerning the exemption's scope. Whereas the PROs appear to have intended the words "single receiving apparatus of a kind commonly used in private homes" to encompass a receiver with only a single built-in speaker,<sup>152</sup> Congress intended this phrase to be construed more broadly. According to the House Report, "the outer limit of the exemption" would be "the particular fact situation in the *Aiken* case," that is, "a small commercial establishment and the use of a home receiver with four ordinary loudspeakers grouped within a relatively narrow circumference from the set."<sup>153</sup> This language vitiated the Court's reasoning in *Aiken*, while affirming its judgment for the restaurant owner based on the case's specific facts.

---

establishments in the two years between the 1975 *Aiken* decision and the entry into force of the Copyright Act of 1976 on January 1, 1978. See Korman, *supra* note 127, at 531-32 (discussing PROs' response to *Aiken* without mentioning whether PROs altered their licensing practices during this period). A search of the case law does not disclose any decision in which the PROs took enforcement action against commercial establishments during this period.

<sup>150</sup> See Korman, *supra* note 127, at 531.

<sup>151</sup> As the House Report on the Copyright Act of 1976 explains:

The majority of the Supreme Court in the *Aiken* case based its decision on a narrow construction of the word "perform" in the 1909 statute. This basis for the decision is completely overturned by the present bill and its broad definition of "perform" in section 101. The Committee has adopted the language of section 110(5), with an amendment expressly denying the exemption in situations where "the performance or display is further transmitted beyond the place where the receiving apparatus is located"; in doing so, it accepts the traditional, pre-*Aiken*, interpretation of the *Jewell-LaSalle* decision, under which public communication by means other than a home receiving set or further transmission of a broadcast to the public, is considered an infringing act.

H.R. REP. NO. 94-1476, at 87 (1975).

<sup>152</sup> See Korman, *supra* note 127, at 528 n.32, 531.

<sup>153</sup> H.R. REP. NO. 94-1476, at 87 (1975); see also H.R. CONF. REP. NO. 94-1733, at 75 (1976) ("It is the intent of the conferees that a small commercial establishment of the type involved in [*Aiken*], which merely augmented a home-type receiver and which was not of sufficient size to justify, as a practical matter, a subscription to a commercial background music service, would be exempt. However, where the public communication was by means of something other than a home-type receiving apparatus, or where the establishment actually makes a further transmission to the public, the exemption would not apply.").

#### 4. 1978 to Early 1990s: Litigating the Homestyle Exemption

With the codification of a slightly broader version of the PROs' license forbearance practices, it seemed that Congress had remedied the market failure that prevailed prior to 1978 by expressly sanctioning the PROs' right to demand royalties for in-store performances, while permitting the free use of broadcast music for those small business users that would not have purchased licenses because of transaction costs. In fact, however, Congress' transformation of a decision by private parties to forebear the collection of royalties into a statutory free use mandate had precisely the opposite effect; it led copyright users to engage in fresh acts of resistance and to seek an expansion of the homestyle exemption to an ever wider array of businesses.

Between 1978 and the early 1990s, section 110(5) became "the most litigated exemption of the Copyright Act,"<sup>154</sup> as PROs brought numerous infringement claims against businesses that failed to purchase licenses for their secondary use of broadcast music. Significantly, nearly all of the cases litigated during this period involved businesses whose sophisticated sound systems clearly disentitled them to the exemption.<sup>155</sup> Why, then, did these businesses litigate? Professor Jessica Litman suggests one reason why compliance with the law was "grudging at best," even though "licenses are sold relatively cheaply."

People perceive the law to be grossly unfair, partly because enforcement is incomplete and uneven; there's no guarantee that the business down the street is licensed, and who wants to be a chump? Then there are all of the exceptions in section 110, which don't make any sense. How come a bar with one 27" television doesn't need a license, while another bar with two 13" televisions does? Copyright lawyers might understand that the reason for this is that the words in section 110(5) say "[single] receiving apparatus of a kind commonly used in private homes," but there is nothing intuitively appealing about the distinction. Some prospective licensees fail to buy licenses because they believe the law could not possibly have been intended to apply to their situation; others find its complex provisions arbitrary and incomprehensible, and, therefore, unfair. *And, every single year, despite the fact that the liability of unlicensed commercial establishments is well settled, people choose to litigate rather than pay up. And, of course, they lose.*<sup>156</sup>

Litman's colorful statement suggests that resistance by commercial

---

<sup>154</sup> 140 CONG. REC. E1700-03 (daily ed. Aug. 10, 1994) (statement of Rep. Jack Reed).

<sup>155</sup> See Brief for Appellee at 49, *Edison Bros. Stores, Inc. v. BMI*, 954 F.2d 1419 (8th Cir. 1992) (providing a chart with a comparison of Edison Bros.' relatively simple equipment with the equipment in stores which were denied a section 110(5) exemption); *1994 Hearings, supra* note 69, at 33, 42-47 (statement of Morton Gould, ASCAP) (providing synopsis's of cases in which the outer-limit of the exemption was surpassed).

<sup>156</sup> Litman, *Exclusive Right, supra* note 112, at 49-50 (footnotes omitted) (emphasis added).

establishments to PROs' licensing practices increased rather than diminished after Congress codified the PROs' voluntary exemption.<sup>157</sup> With this renewed existence came a widening of the market failure for secondary uses of broadcast music. According to the EC, it was during this period of intensive litigation that PROs in the United States began to face "strong resistance when attempting to license small to medium size[d] premises which do not benefit from the exemption."<sup>158</sup> This resistance raised transaction costs, causing PROs to "refrain[] from licensing such business[es]."<sup>159</sup>

#### 5. Early 1990s to 1998: Users' Judicial and Legislative Resistance Increases

During the early 1990s, users' efforts to resist paying performance license fees expanded in two ways. First, large commercial establishments successfully advocated a broad construction of the homestyle exemption based on the text of the statute rather than its legislative history. Second, business associations lobbied Congress to privilege all or nearly all secondary uses of broadcast music. The result of these expanded resistance efforts, according to the EC, was that PROs in the United States "abandoned the field, and [did] not even try to license small and medium size[d] businesses" that did not qualify for the homestyle exemption.<sup>160</sup>

##### a. *Judicial Expansion of the Homestyle Exemption*

The homestyle exemption generated a large volume of litigation not only because of user resistance, but also because of the dissonance between the text of the exemption and its legislative history. The text focuses solely on three factors—the nature of the receiving equipment, the further transmission of the broadcast to the public and the collection of a direct charge to see or hear the broadcast.<sup>161</sup> The legislative history, however, urged courts to focus on two additional factors: a comparison of the size of the commercial establishment with that in *Aiken* and the establishment's ability to afford a background commercial music service.<sup>162</sup> During the exemption's first decade, nearly all courts relied on both the statute and its legislative history to determine whether

---

<sup>157</sup> See *supra* note 131 (only two published cases involving infringing secondary uses of broadcast music were decided between 1931 and 1975).

<sup>158</sup> European Commission, *Examination Procedure Regarding the Licensing of Music Works in the United States of America*, LE.3/JVE D(98), Feb.23,1998 at 30 [hereinafter *Examination Procedure*].

<sup>159</sup> *Id.*

<sup>160</sup> *Id.* at 31.

<sup>161</sup> 17 U.S.C. § 110(5) (1994).

<sup>162</sup> See, e.g., *NIMMER & NIMMER*, *supra* note 70, § 8.18[C][2] at 8-214 to 8-217. See also *Edison Bros. Stores, Inc., v. BMI*, 954 F.3d 1419, 1422 (8th Cir. 1991) (noting that the restaurant in *Aiken* contained a total of 1055 square feet, with 620 square feet for public use, but refusing to consider size of establishment as a factor in analyzing homestyle exemption).

a business was required to purchase a license. However, beginning with a pair of appellate court decisions rendered in the early 1990s, several courts shifted ground to focus almost exclusively on the statute's text.<sup>163</sup>

These decisions markedly expanded the homestyle exemption. Whereas under prior rulings commercial establishments larger than the restaurant in *Aiken* were unlikely to be found exempt, under the strict statutory construction approach even large and highly profitable chain stores could avoid the PROs' licensing demands by using a receiver and four or fewer speakers.<sup>164</sup> This configuration of equipment enables customers and employees to hear music in businesses up to four times the size of the *Aiken* restaurant.<sup>165</sup>

#### b. *Legislative Expansion of the Homestyle Exemption*

The dissonance between the statutory and legislative history approaches to the homestyle exemption created ambiguities that encouraged businesses to litigate rather than acquiesce in paying blanket licensing fees. But even after obtaining a favorable construction of section 110(5) from several courts, businesses continued to resist PROs' licensing efforts, turning from the judiciary to Congress to seek even broader relief.<sup>166</sup>

##### 1) Early Licensing Reform Bills

Beginning in the fall of 1993 and continuing into 1995, a broad cross section of business associations, including restaurants, bars and retail stores, gave their support to bills introduced in the 103d and 104th Congresses to repeal section 110(5).<sup>167</sup> These bills, the Public Accommodations Exception Act of 1993 and

---

<sup>163</sup> See, e.g., *Edison Bros. Stores, Inc.*, 954 F.2d at 1425; *BMI v. Claire's Boutiques, Inc.*, 949 F.2d 1482, 1493 (7th Cir. 1991) ("[T]he job of this Court is to apply the laws passed by Congress, and not to enforce a generalized and vague notion of intent. In any event, Congress' intent to limit the exemption to financially small organizations is far from clear.").

<sup>164</sup> See *NIMMER & NIMMER*, *supra* note 70, § 8.18[C][2] at 8-218 (noting that construction of exemption that focuses exclusively on statutory factors causes music copyright owners to lose cases "that, under the legislative history method, they would have won."). Even the placement of speakers in the ceiling would not vitiate the exemption. See *Claire's Boutiques, Inc.*, 949 F.2d at 1493 (holding that other factors, besides only placement of speakers, can lead to a store qualifying for the homestyle exemption).

<sup>165</sup> See John Wilk, Note, *Seeing the Words and Hearing the Music: Contradictions in the Construction of 17 U.S.C. Section 110(5)*, 45 RUTGERS L. REV. 783, 805 & n.110 (1993) (citing studies demonstrating that businesses as large as 4000 square feet "can provide adequate background music using ordinary home equipment").

<sup>166</sup> Litigation over the homestyle exemption became increasingly less active starting in the mid 1990s. LEXIS and WESTLAW searches reveal no published or unpublished cases interpreting or applying section 110(5) after May 1996. This is consistent with the EC's claim that PROs "abandoned the field" in licensing many non-exempt businesses during this period. See *Examination Procedure*, *supra* note 158, at 31.

<sup>167</sup> Supporters of the bills referred to themselves as the Music Licensing Fairness

the Fairness in Music Licensing Acts of 1994 and 1995,<sup>168</sup> sought to privilege “incidental” performances of licensed broadcast music regardless of the size of the establishment or the type of equipment used.<sup>169</sup> Proponents of these bills raised the arguments identified above in opposing the right of PROs to collect licenses for in-store performances, including double dipping, abuse of monopoly power and overly aggressive licensing and enforcement practices. The PROs challenged these arguments and defended their right to collect royalties for in-store performances.<sup>170</sup>

---

Coalition. *See 1997 Hearings, supra* note 19, at 303.

<sup>168</sup> The proposed Public Accommodations Exception Act, H.R. 3288, 103d Cong. § 2 (1993) would have added a new subsection to section 110 to exempt the:

communication of a transmission, by radio or television, embodying a performance or display of a work by the public reception of the transmission on a receiving or recording apparatus in a restaurant, tavern, or other commercial establishment serving food or drink, the performance of which is incidental to the main purpose of the restaurant, tavern, or other commercial establishment, unless a direct charge is made to see or hear the transmission.

The proposed Fairness in Music Licensing Act of 1995 would have amended section 110(5) to exempt the

communication by electronic device of a transmission embodying a performance or display of a work by the reception of a broadcast, cable, satellite, or other transmission, unless—

(A) an admission fee is charged specifically to see or hear the transmission, or

(B) the transmission is not properly licensed,

except that this paragraph shall apply in the case of a performance or display in a commercial establishment only if the performance or display is incidental to the main purpose of the establishment.

H.R. 789, 104th Cong. § 2; *see also* Fairness in Music Licensing Act of 1994, S. 2515, 103d Cong. § 2 (containing a nearly identical exemption); H.R. 4936, 103d Cong. § 2 (1994) (containing similar exemption “unless a direct or indirect charge is made to see or hear the transmission”).

<sup>169</sup> Except for excluding from the exemption’s purview businesses that collected a charge or admission fee to see or hear the performance, the bills did not define the term “incidental.” However, witness testimony at hearings held before the House Judiciary Committee’s Subcommittee on Intellectual Property and Judicial Administration in February 1994 and the House Committee on Small Business in May 1996 suggested that the exemption would apply to all performances of “background” music not directly used to attract customers. *See, e.g., 1994 Hearings, supra* note 69, at 137 (statement of Guy Gregg, Nat’l Restaurant Ass’n) (conceding that proposed exemption would not be applicable to a business that advertised its performance of music); *1996 Hearings, supra* note 85, at 35 (statement of Marvin Berenson, General Counsel for BMI) (contesting claim that background music provides only an incidental business benefit).

<sup>170</sup> *See supra* Part I.B; *see also* Raines, *supra* note 86, at 187-97 (summarizing the arguments of the bills’ proponents and opponents).

## 2) The Fairness in Music Licensing Act of 1997

When these bills died in committee, similar legislative proposals were reintroduced in the House and Senate at the beginning of the 105th Congress. Titled the Fairness in Music Licensing Act of 1997, these bills were broader than their earlier incarnations in that they eliminated the requirement that businesses derive only an incidental benefit from the music.<sup>171</sup> They proposed to amend the Copyright Act to exempt any communication “of a nondramatic musical work by the reception of a broadcast, cable, satellite, or other transmission.”<sup>172</sup> Only if the individual or business charged an admission fee “specifically to see or hear the transmission,” or if the transmission “was not properly licensed” could royalties be collected.<sup>173</sup>

Hearings on the House version of the bills were held before the House Judiciary’s Subcommittee on Courts and Intellectual Property in July 1997.<sup>174</sup> In addition to reiterating arguments previously raised by both sides supporting and opposing earlier exemption bills, the Subcommittee received testimony from government officials who warned of the dangers that the exemption posed for the United States’ treaty obligations and international trade relations.<sup>175</sup>

The testimony of Marybeth Peters, the Register of Copyrights, was particularly illuminating.<sup>176</sup> The Register stated that the homestyle exemption represented a “careful balancing of interests between rights-holders and users” which was “narrowly drawn to ensure that [it does not] substitute for a meaningful commercial exploitation.”<sup>177</sup> The proposed exemption, by contrast, would permit “businesses of any size, including large, national chains, [to] use copyrighted music for free in order to entertain their customers

---

<sup>171</sup> H.R. 789, 105th Cong. § 2 (1997); S. 28 105th Cong. § 2 (1997). In addition, two somewhat more moderate exemption proposals were introduced in the Senate by Senators Hatch and Brown in 1996. *See* S. 1619, 104th Cong. (1996); S. 1628, 104th Cong. (1996). It does not appear, however, that hearings were ever held on either of these of these bills.

<sup>172</sup> *See* H.R. 789 and S. 28.

<sup>173</sup> *Id.*

<sup>174</sup> *See 1997 Hearings, supra* note 19, at 1.

<sup>175</sup> *See id.* at 16, 19 (statement of Marybeth Peters, Register of Copyrights, Copyright Office of the United States) (“The breadth of the proposed amendment to Section 110(5) goes much further than any exemption that has been considered as a small exemption or minor reservation permitted by the Berne Convention.”). Bruce Lehman, Assistant Commissioner of Patents and Trademarks, also testified against the bill because of these treaty concerns. *See id.* at 44 (“Our trading partners are likely to allege that several of the changes to the copyright law proposed in section two of the proposed bill may be inconsistent with our obligations under the Berne Convention and [TRIPs].”). For a detailed treaty analysis of both the homestyle exemption and the FIMLA as ultimately enacted, see *infra* Part III.

<sup>176</sup> *1997 Hearings, supra* note 19, at 16.

<sup>177</sup> *Id.*

and thereby stimulate sales of their own goods or services.”<sup>178</sup> Given this breadth, the Register predicted the exemption “would lead to claims by other countries that the United States was in violation of its obligations” under the Berne Convention and the TRIPs Agreement and create a “difficult case” for the United States at the WTO.<sup>179</sup> She argued, however, that the existing homestyle exemption was consistent with the treaties and, in addition, that the Copyright Office could help the Committee draft a narrower exemption that would survive a WTO challenge.<sup>180</sup>

### 3) The NLBA Agreement

Although the Register did not describe this narrower exemption, she may have been referring to a private agreement previously reached between the PROs and the National Licensed Beverage Association (“NLBA”). This agreement was negotiated after members of the House subcommittee urged the parties to structure their own licensing arrangement rather than to force Congress to amend the Copyright Act.<sup>181</sup> With the fate of the music licensing bills still uncertain in 1995, the two sides reached a solution that differed significantly from the exemptions proposed in the bills and created numerous benefits for both music copyright owners and for the taverns, restaurants and retail stores who comprise NLBA’s membership.

Several facets of the NLBA agreement are noteworthy. First, the agreement

---

<sup>178</sup> *Id.* at 17, 18; *see also id.* (claiming that expanded exemption could supplant market for background music services).

<sup>179</sup> *Id.* at 32 (“An exception this broad appears to be outside the scope of the permissible ‘small exceptions’ to the Berne rights of public performance and communication. Allowing virtually every business to play music to its customers through loudspeakers or audiovisual devices would invite a difficult case against the United States for violating our TRIPs obligations.”). The Register’s prediction of a future WTO dispute was not speculative. In April 1997, the Irish Music Rights Organization (“IMRO”) filed a complaint with the European Commission asking it to investigate the trade distortions created by the homestyle exemption. *See Examination Procedure, supra* note 158, at 1 (describing complaint of IMRO). By June of 1997, a month before the hearings, the Commission had found “sufficient evidence of the existence of obstacles to trade and adverse trade effects resulting therefrom for the purpose of initiating an examination procedure.” *Id.*

<sup>180</sup> *See id.* at 19 (“a reasonable exemption which is narrow in scope and which complies with the standards of Berne and TRIPs could be drafted”); *see also id.* at 46 (“I clearly believe that existing section 110(5) does not violate the obligations that we have under the Berne Convention.”).

<sup>181</sup> *See 1994 Hearings, supra* note 69, at 110-11 (statement of Rep. Carlos J. Moorhead) (“I think there is a very, very great need to get together and try to work this out without having a legislative solution imposed on you . . . . It is always much better to work something out than it is to have Congress impose something.”); *see also id.* at 109 (statement of Fred Koenigsberg, counsel for ASCAP) (“If we could sit down and work things out with the trade associations which represent the bulk of users here . . . there would be no need for Congress to address the issue.”).

used a combination of square footage and equipment requirements to determine the exempt status of a commercial establishment.<sup>182</sup> These criteria improved upon the homestyle exemption by eliminating the ambiguous statutory and legislative history factors courts had used to interpret it and supplanting them with a set of clear, detailed rules.<sup>183</sup>

Second, the NLBA agreement contained numerous efficiencies not found in the proposed exemption bills. These efficiencies were possible because all three PROs and an industry-wide trade association of copyright users negotiated the agreement.<sup>184</sup> The global nature of the negotiations thus allowed the parties to resolve not only the broadcast music licensing dispute, but an array of related issues as well.

For example, the agreement permitted businesses who did not qualify for the exemption to pay a single, reduced annual fee for the privilege of performing broadcast, recorded and live music controlled by all three PROs, rather than the three separate and higher fees they had paid in the past.<sup>185</sup> In addition, enforcement and monitoring costs were reduced by having NLBA members deal only with the NLBA: businesses purchasing a license paid fees directly to the NLBA (which then distributed them to the PROs), while other businesses submitted proof of their eligibility for the exemption to the NLBA.<sup>186</sup> Under

---

<sup>182</sup> See *1997 Hearings*, *supra* note 19, at 99-100.

<sup>183</sup> The exemption criteria contained in the NLBA Agreement were as follows: *For eating and drinking establishments*: (1) All businesses 3500 square feet of gross leasable space or larger are totally exempt provided that they use no more than: (a) six external radio and/or TV speakers with no more than 4 in any one room, and (b) three televisions with screen sizes of 55 or smaller with no more than two televisions in any one room. (2) All businesses smaller than 3500 square feet are totally exempt from any music licensing fees for radio and TV use. *For retail establishments*: (1) All businesses with 1500 square feet of gross leasable space or larger are totally exempt provided that they use no more than: (a) four external radio or TV speakers, and (b) two televisions with screen sizes of 55 inches or smaller. (2) All places smaller than 1500 square feet are totally exempt from any music licensing fees for radio and TV use. See *1997 Hearings*, *supra* note 19, at 99-100 (statement of Debra Leach, Executive Director of NLBA). The exemption did not apply if a business charged customers a fee or if the transmission was further transmitted beyond the establishment. See Johnson, *supra* note 19, at S-11. NLBA members qualifying for the exemption were required to pay a \$30 administrative fee for the NLBA. See *1997 Hearings*, *supra* note 19, at 332 (statement of Debra Leach, NLBA).

<sup>184</sup> See *1997 Hearings*, *supra* note 19, at 101. For additional details on the NLBA Agreement, see *NLBA and Performing Rights Organizations Finalize Licensing Plan*, (visited Dec. 4, 1999) <<http://nlba.org/nlba/music.html>> [hereinafter *Licensing Plan*].

<sup>185</sup> See *Licensing Plan*, *supra* note 184, at 3; *1997 Hearings*, *supra* note 19, at 101 (statement of Debra Leach, Executive Director of NLBA) (describing “discounted fees” for businesses who chose to adopt the agreement).

<sup>186</sup> See *1997 Hearings*, *supra* note 19, at 183 (supplementary letter from ASCAP) (NLBA agreement “includes an important provision in which they are responsible for collecting fees from their members”); see also *The NLBA Performance License Application*, (visited Nov. 30, 1999) <<http://nlba.org/nlba/musicapp.html>> (requiring members to submit

this arrangement, compliance with the agreement would be supervised by an organization of copyright users rather than by the PROs, whose heavy-handed enforcement measures were cited as a principal reason for music licensing reform. The PROs also agreed to share information with NLBA members on ways to use music to enhance their business, and the NLBA agreed to educate its membership about their obligation to comply with the copyright law.<sup>187</sup> Finally, the parties negotiated a three-year initial period for the agreement, allowing them to modify its terms in light of experience or changed market conditions.<sup>188</sup>

#### 4) The Fairness in Music Licensing Act of 1998

Had other associations of copyright users negotiated licensing arrangements similar to the NLBA agreement, Congress might have avoided altering the homestyle exemption altogether. Not all associations were willing to conclude such agreements, however. The National Restaurant Association (“NRA”) was particularly resistant to efforts by PROs to negotiate a private agreement.<sup>189</sup> It continued to demand that Congress incorporate a revised exemption into the Copyright Act,<sup>190</sup> notwithstanding statements by several legislators that a private solution to the licensing dispute would be preferable.<sup>191</sup>

Faced with the NRA’s intransigence, Congress attempted to broker a compromise. As with the homestyle exemption before it, Congress turned to private licensing practices as a template for its legislation.<sup>192</sup> Thus, the Fairness in Music Licensing Act of 1998, passed by the House in March 1998, adopted square footage and equipment requirements modeled on those used in the NLBA agreement to determine the exempt status of a commercial

---

official documents demonstrating gross square footage of establishment)

<sup>187</sup> See *Licensing Plan*, *supra* note 184, at 2.

<sup>188</sup> See *1997 Hearings*, *supra* note 19, at 161 (statement of Fred Koenigsberg, counsel for ASCAP). The NLBA hoped to negotiate lower license fees if most of its members signed up for the initial agreement. See *Licensing Plan*, *supra* note 184, at 5.

<sup>189</sup> The NRA’s stated reasons for opposing a private agreement included a desire to eliminate the homestyle exemption’s uncertainties and a concern that the agreement would not be permanent. In addition, the NRA strongly favored legislation to compel the PROs to identify their entire repertoires and to require local arbitration of rate disputes rather than the prohibitively expensive litigation before the New York rate court. See *1997 Hearings*, *supra* note 19, at 230, 242 (statement of Peter Kilgore, General Counsel of NRA).

<sup>190</sup> See *id.* at 245.

<sup>191</sup> See *1996 Hearings*, *supra* note 85, at 18 (statement of Marvin Berenson, General Counsel for BMI) (stating that offers “to increase the size of commercial establishment[s] qualified for exemption from licensing requirements, increase the size and types of equipment and other offers, were unacceptable to the NRA”); see also *id.* at 31-32 (statements of Reps. Kelly and Bono) (questioning whether agreement between PROs and Nat’l Restaurant Ass’n was possible).

<sup>192</sup> See H.R. 2589, 105th Cong. § 202 (1997).

establishment.<sup>193</sup> The Congressional Research Service reported that adopting these requirements would exempt 65.2% of all eating establishments and 71.8% of all drinking establishments from any licensing obligations.<sup>194</sup>

Negotiations over the scope of the exemptions continued during the next several months, with supporters pressing for the FIMLA to be included in the copyright term extension bills then pending before Congress.<sup>195</sup> The final version of the FIMLA that emerged from these negotiations and passed both houses of Congress on October 7, 1998 resembled the NLBA agreement even more closely. It adopted the agreement's distinction between eating and drinking establishments and retail businesses, as well as slightly enlarged versions of its square footage and equipment criteria.<sup>196</sup>

#### 6. Implementing the FIMLA: Continued User Resistance?

With the adoption of the FIMLA, Congress repeated the pattern it followed twenty years earlier, codifying licensing arrangements that private parties had voluntarily adopted or negotiated.<sup>197</sup> Although it is too soon to determine whether the statute, as the homestyle exemption before it, will encourage non-exempt commercial establishments to resist paying license fees, early indications suggest that the PROs are concerned that the compliance gap may widen. In the months after the FIMLA's effective date in January 1999, BMI and ASCAP adopted new marketing campaigns to educate non-exempt businesses about the advantages of obtaining a license.<sup>198</sup> Both organizations

---

<sup>193</sup> See *id.* H.R. 2589 was broader than the NLBA agreement, since it exempted *all* types of commercial establishments whose premises contained less than 3500 square feet of publicly accessible space. Larger establishments were exempt if they used less than a specified number of audio speakers or televisions. See *id.* § 202(a). These equipment requirements were identical to those found in the NLBA agreement, except that they would have permitted businesses to use only two television sets rather than three. See *id.*

<sup>194</sup> See 1997 *Hearings*, *supra* note 19, at 81 (statement of Wayland Holyfield on behalf of ASCAP) (reviewing findings of Congressional Research Service).

<sup>195</sup> See, e.g., Charles Schumer, *Exemption Weakens Ideas-Fueled Economy*, BILLBOARD, Apr. 10, 1999, available in LEXIS, News Library, BILLBOARD file (noting that FIMLA was added as an amendment to bills extending the term of copyright protection).

<sup>196</sup> The FIMLA increased the NLBA's square footage limits from 3500 square feet to 3750 square feet for bars and restaurants, and from 1500 square feet to 2000 square feet for other establishments. It also slightly increased the number of loudspeakers and televisions each type of business could employ. Compare 17 U.S.C. § 110(5)(B) (1999) (defining square footage and equipment requirements under FIMLA), with 1997 *Hearings*, *supra* note 19, at 99-100 (statement of Debra Leach, Executive Director of NLBA) (describing exemptions based on square footage for retail and eating establishments under the NLBA agreement).

<sup>197</sup> See *supra* Part II.B.2-3.

<sup>198</sup> See Irv Lichtman, *BMI Bows Customer-Outreach Plan*, BILLBOARD, Mar. 6, 1999, available in 1999 WL 10038128 (describing BMI's efforts to educate restaurants and bars on using music to improve revenues and "provid[ing] information about general music

also revised their fee structures to make licensing more attractive and affordable.<sup>199</sup> One objective of these campaigns is to generate royalties from non-exempt businesses to offset royalty losses caused by the FIMLA.<sup>200</sup> But an equally important aim is to curb resistance from those businesses to paying any license fees for performances of music.<sup>201</sup>

### C. *Summarizing the Historical Evidence*

As discussed in this section and summarized in the chart below, the legal regulation of secondary uses of broadcast music in the United States has evolved significantly since the Copyright Act first recognized the right of music copyright owners to control the public performances of their works. In particular, Congress and the courts have recognized and slowly expanded an exemption that permits commercial establishments, under specified conditions, to transmit broadcast music without purchasing a license. The exemption seeks, at least in part, to correct market failures created by the high transaction costs associated with licensing businesses, including the costs of user resistance to paying license fees.

Although attempts to correct these market failures would seem justified under the economic efficiency approach discussed in Part I, this Part has shown that revising the copyright law has had the effect of diverting the resources of copyright users away from reaching private licensing arrangements with PROs and toward more intensive acts of resistance and rent seeking in Congress and the courts. In short, legislative and judicial intervention, rather than correcting failures in the licensing market, actually exacerbated those failures by encouraging users to contest PROs' licensing efforts and to devote resources toward seeking a further widening of the exemption.

Whether this trend will be repeated under the FIMLA's new exemption rules cannot, however, be predicted by analyzing United States copyright law alone. Congress and the courts no longer have an entirely free hand to revise or interpret the Copyright Act when doing so clashes with the United States' treaty obligations. The crucial question, then, for both legislators and for copyright owners and users, is whether the WTO dispute settlement bodies will find that the licensing exemptions violate these treaties. It is to that issue that I now turn.

---

licensing").

<sup>199</sup> *Id.*

<sup>200</sup> *See id.* (ASCAP anticipates seven percent decline in revenues as a result of FIMLA).

<sup>201</sup> *See* Carrington Nelson, *No Longer the Same Old Song: Performance Rights Groups BMI, ASCAP Launch Campaigns to Soften Images*, *THE TENNESSEAN*, Apr. 9, 1999 at 1E, available in 1999 WL 5764187 (noting continued "resentment" from businesses over paying license fees).

### HISTORY: LEGAL REGULATION OF SECONDARY USES OF BROADCAST MUSIC IN THE UNITED STATES

Time Period	Law Applicable to Public Performances of Music	Licensing & Enforcement Efforts by PROs	Response by Copyright Users	Evidence of Market Failure
1920s-1931	Right to control public performances for profit recognized, but unclear whether right extends to secondary uses of broadcast music.	(1) Active efforts to license commercial establishments. (2) Litigation against infringers.	(1) Refusal to pay license fees voluntarily. (2) Litigation and bills challenging public performance right.	Licensing market still in formative stages.
1931-1975	(1) <i>Buck v. Jewell-La Salle Realty Co.</i> , 283 US 191 (1931) recognizes multiple performance doctrine. Requires hotel transmitting unlicensed radio broadcast to guest and public rooms to purchase a license. (2) Doctrine may not apply if broadcasters licensed by PROs. (3) Court suggests Congress may create exemption if all broadcasters licensed.	(1) Active efforts to license commercial establishments. (2) Modification of broadcaster contracts to prevent implied license from broadcasters to commercial establishments.	(1) Support for bills introduced in 1930s and early 1940s to overturn multiple performance doctrine or exempt secondary uses of broadcast music. (2) Limited litigation challenging PROs' licensing practices (only two reported decisions between 1931 and 1975)	(1) PROs voluntarily abstain from collecting license fees from "mom and pop" businesses using a radio receiver with a single speaker. (2) Scope of voluntary abstention unclear. May apply to businesses using radio receivers or TV sets with multiple speakers.
1975-1977	<i>Twentieth Century Music Corp. v. Aiken</i> , 422 US 151 (1975) rejects multiple performance doctrine. Exempts fast food restaurant using receiver and four speakers mounted in ceiling to perform radio broadcast for employees and customers.	(1) Licensing precluded by Supreme Court decision. (2) Legislative efforts to restore multiple performance doctrine.	Support for bills to exempt secondary use of broadcast music by commercial establishments.	Not applicable because licensing prohibited.
1978-early 1990s	(1) Multiple performance doctrine restored by statute. (2) Homestyle exemption adopted in 17 U.S.C. § 110(5). No performance license fee payable by commercial establishments that meet requirements of homestyle exemption.	(1) Efforts to license commercial establishments not falling within exemption. (2) Intensive litigation against non-exempt commercial establishments who fail to purchase licenses.	Litigation relying on exemption to justify refusal to pay license fees, even where exemption clearly not applicable.	Uncertain. European Community claims that licensing businesses at margins of homestyle exemption
Early 1990s-Jan. 1999	Strict statutory construction approach to homestyle exemption. Exemption applied to retail chain stores.	(1) Uncertain efforts to license commercial establishments not falling within exemption. (2) Decrease in litigation (no reported decisions after May 1986).	(1) Bills introduced to exempt most secondary uses of broadcast music. (2) NLBA negotiates private agreement with PROs; NRA does not.	European Community claims that US PROs "abandoned the field" for licensing small and medium sized businesses, including those which perform recorded music.
Jan. 1999 to present	Fairness in Music Licensing Act exempts commercial establishments meeting detailed square footage and equipment requirements.	PROs seek to license non-exempt commercial establishments and to improve relations with copyright users.	Uncertain. PROs marketing campaign suggests concern over continued resistance to licensing by non-exempt users.	Unknown.

### III. ANALYZING THE FIMLA AND HOMESTYLE EXEMPTIONS UNDER THE BERNE AND TRIPS TREATIES

In the complaint pending before the WTO dispute settlement panel, the EC has alleged that both the FIMLA and the “homestyle” exemption violate the TRIPs Agreement and the Berne Convention. This Part analyzes the EC’s allegations in favor of finding a violation of the treaties and the arguments the United States has raised and can raise in response. It highlights the ways in which the FIMLA dispute differs from past TRIPs cases and identifies those legal issues that will be the most difficult and controversial for WTO jurists to resolve. The Part concludes with a prediction that both the panel and the Appellate Body will accept the EC’s claim that both statutes violate Berne and TRIPs and will recommend that the United States revise the Copyright Act to bring it into compliance with the treaties.

#### A. Framing the FIMLA Dispute: A Methodological Note

The FIMLA dispute raises two discrete questions for WTO jurists: first, whether the FIMLA and the homestyle exemption violate the exclusive “minimum rights” guaranteed under Berne and TRIPs; and second, if such a violation exists, whether it can be justified under the exceptions or limitations clauses of the two treaties. The first question is quite straightforward, whereas the second is far more complex and will be the most difficult to resolve.

To answer each of these questions, WTO jurists will apply the rules of treaty interpretation set out in the Vienna Convention on the Law of Treaties.<sup>202</sup> The Vienna Convention’s rules give primacy to a treaty’s text, which must be interpreted in its “context” and in light of the treaty’s “object and purpose.”<sup>203</sup> Subsequently concluded treaties and “subsequent practice” by the parties to the treaty that establish the text’s meaning may also be considered.<sup>204</sup> However, unlike the interpretive methodologies applied by United States courts, the Vienna Convention restricts use of extra-textual means to interpret treaties, including reliance on a treaty’s *travaux préparatoires* or drafting history.<sup>205</sup>

---

<sup>202</sup> See Vienna Convention on the Law of Treaties, *opened for signature* May 23, 1969, 1155 U.N.T.S. 331, 341 [hereinafter Vienna Convention]. In its first decision, United States — Standard for Reformulated and Conventional Gasoline, 35 I.L.M. 603 (May 20, 1996), the WTO Appellate Body held that all WTO treaties would be interpreted according to the rules found in the Vienna Convention.

<sup>203</sup> Vienna Convention, *supra* note 202, art. 31(1). The “context” of a treaty includes, *inter alia*, the text of the entire agreement, including its preamble and annexes. See *id.* art. 31(2).

<sup>204</sup> See *id.* art. 31(3). “Subsequent practice” is often found in the manner in which State parties to a treaty incorporate its provisions into their national laws. For a discussion of how WTO jurists should use national legislation to aid in interpreting the TRIPs Agreement, see Helfer, *supra* note 29, at 426-31.

<sup>205</sup> See RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 325 cmt. g (1987) (noting that United States courts are “more willing than those of other

Jurists may consult these sources only “to confirm the meaning” resulting from a textual, contextual and purposive analysis, or to “determine the meaning” when such analysis leaves the treaty’s meaning “ambiguous or obscure” or leads to a result that is “manifestly absurd or unreasonable.”<sup>206</sup>

As explained below, the Vienna Convention’s interpretive rules will play a significant role in shaping the resolution of the FIMLA dispute. In particular, they may provide a means for WTO jurists to rule on the EC’s complaint without considering the policy-oriented economic and distributional arguments identified in Part II that the United States may raise in defense of the music licensing exemptions.

### B. *The Violation of Berne/TRIPs’ Exclusive Rights*

The first issue that WTO jurists must address is whether the FIMLA and homestyle exemptions violate the exclusive rights guaranteed to musical works of foreign origin under international copyright law.<sup>207</sup> The EC has not alleged that any exclusive rights guaranteed by TRIPs *itself* have been violated; rather it has invoked article 9(1) of TRIPs which incorporates the Berne Convention by reference.<sup>208</sup> Thus, to determine whether the United States has violated TRIPs, WTO jurists will need to analyze the text of Berne—the first time WTO dispute settlement bodies will have interpreted this foundational copyright treaty.<sup>209</sup>

---

states to look outside the [treaty] to determine its meaning”).

<sup>206</sup> Vienna Convention, *supra* note 202, art. 32. See IAN SINCLAIR, THE VIENNA CONVENTION ON THE LAW OF TREATIES 141 (2d ed. 1984) (explaining primacy of textual and contextual analysis and secondary role accorded to drafting history in Vienna Convention’s hierarchy of interpretive rules).

<sup>207</sup> The Berne and TRIPs treaties impose obligations on their signatories only with respect to copyrighted works whose country of origin is another Berne or TRIPs member State. The treaties do not require that signatories grant protection to works of domestic origin. Copyrighted works entitled to protection under this standard include: (1) works *first published* in another member State; (2) works first published simultaneously in the United States and another member State that gives a shorter term of copyright protection; and (3) works first published in a non-member State whose author is a national of a member State other than the United States. See *Final Report of the Ad Hoc Working Group on U.S. Adherence to the Berne Convention*, 10 COLUM.-VLA J.L. & ARTS 513, 529 (1986) [hereinafter *Final Report*].

<sup>208</sup> See *First Submission of the European Communities and their Member States to the Panel*, United States – Section 110(5) of the U.S. Copyright Act, WTO Doc. WT/DS 160 at ¶ 71 (Oct. 5, 1999) [hereinafter *First EC Submission*] (copy on file with the author) (citing TRIPs, *supra* note 16, article 9(1), which “stipulates the principle that WTO Members have to comply with the substantive provisions of the Berne Convention”).

<sup>209</sup> See Allen N. Dixon, *TRIPs Case Law Developments in the WTO: A Review and Analysis*, FORDHAM UNIV. SCH. OF LAW, 7TH ANNUAL CONF. ON INT’L INTELL. PRP. L. & POL. 1, 12 (Apr. 8-9, 1999) (unpublished conference paper on file with author) (reviewing past TRIPs cases).

The Berne Convention's provisions concerning broadcast music are clear and unequivocal. Since the 1948 Brussels revision, the Convention has granted to copyright owners both the right to control the broadcast of their works by radio and television, and the separate and distinct right to control secondary uses of those same broadcasts. Specifically, Berne article 11bis(1)(iii) provides that

[a]uthors of literary and artistic works shall enjoy the exclusive right of authorizing:

(i) the broadcasting of their works or the communication thereof to the public by any other means of wireless diffusion of signs, sounds or images; . . .

(iii) *the public communication by loudspeaker or any other analogous instrument transmitting, by signs, sounds or images, the broadcast of the work.*<sup>210</sup>

Under United States copyright law, restaurants, bars and commercial establishments are indisputably "public" places.<sup>211</sup> When these businesses use stereo systems and televisions to play the copyrighted music contained in radio and television broadcasts to customers or employees located on their premises, they are "communicat[ing]" or "transmitting" a "broadcast" of the music "by loudspeaker or any other analogous instrument." For this reason, both the FIMLA and the homestyle exemption authorize U.S. businesses to engage in precisely the activity that Berne consigns to the copyright owners' exclusive control.

Given the clarity of this textual and contextual analysis, WTO jurists need not even consult Berne's drafting history to find that the United States has

---

<sup>210</sup> Berne Convention, *supra* note 15, art. 11bis(1)(i), (iii) (emphasis added).

The EC has also alleged that the United States' licensing laws violate article 11(ii) of the Berne Convention to the extent that they permit businesses to use wired cable transmissions in their establishments. See *First EC Submission*, *supra* note 208, at ¶¶ 90-92. Article 11(ii) grants copyright owners the exclusive right to control cable transmissions of musical works to the public when the entire transmission is by wire. See World Intellectual Property Organization [hereinafter WIPO], GUIDE TO THE BERNE CONVENTION FOR THE PROTECTION OF LITERARY AND ARTISTIC WORKS 65 (1978) [hereinafter 1978 WIPO GUIDE].

<sup>211</sup> See 17 U.S.C. § 101 (1999) (defining public performances to include any performances "at a place open to the public or at any place where a substantial number of persons outside of a normal circle of family and its social acquaintances is gathered"). Under the Berne Convention, "[t]he law of the country of protection determines when the communication is public." WILHELM NORDEMANN ET AL, INTERNATIONAL COPYRIGHT AND NEIGHBORING RIGHTS LAW: COMMENTARY WITH SPECIAL EMPHASIS ON THE EUROPEAN COMMUNITY 127 (1990). By contrast, the treaty does not grant copyright owners the right to control "private" communications, broadcasts or performances of their works, which are generally limited to works received in the company of family members and friends. See SAM RICKETSON, THE BERNE CONVENTION FOR THE PROTECTION OF LITERARY AND ARTISTIC WORKS: 1886-1986, 432-33 (1986).

violated article 11*bis*(1)(iii). However, in the event that the jurists refer the preparatory work to “confirm” the meaning of the text,<sup>212</sup> they will find ample additional evidence to support this conclusion.

The drafting history of article 11*bis*(1)(iii) indicates that Berne member States were concerned about the significant increase in the size of the listening audience that could result when broadcasts of copyrighted works were transmitted over loudspeakers located in public places. Prior to 1948, member States’ laws were in disharmony over whether such secondary transmissions were subject to the copyright owner’s control, prompting a move to revise the treaty.<sup>213</sup>

According to the drafting history of the 1948 Brussels conference, there was “no significant opposition” by member States to adding an express right for copyright owners to control the retransmission of broadcasts in public places.<sup>214</sup> Although the drafters did not seek to draw a definitive boundary between public and private broadcasts (the latter of which are beyond the copyright owner’s control), they did provide examples of locations that they considered to be public.<sup>215</sup> These included “above all, places where people meet: in the cinema, in restaurants, in tea rooms, railway carriages,” as well as “places where people worked and conduct their business, such as factories, shops, and offices.”<sup>216</sup>

Further guidance on the scope of article 11*bis*(1)(iii) is found in the World Intellectual Property Organization’s 1978 official guide to the Berne Convention.<sup>217</sup> Emphasizing the distinction between copyright owners’ right to authorize radio and televisions broadcasts and the separate right to authorize secondary uses of those broadcasts, the guide states:

In places where people gather (cafes, restaurants, tea-rooms, hotels, large shops, trains, aircraft, etc.) the practice is growing of providing broadcast program[s]. . . . The question is whether the license given by the author to the broadcasting station covers, in addition, all the use made of the

---

<sup>212</sup> See Vienna Convention, *supra* note 202, art. 32.

<sup>213</sup> See RICKETSON, *supra* note 211, at 452; see also I STEPHEN P. LADAS, THE INTERNATIONAL PROTECTION OF LITERARY AND ARTISTIC PROPERTY 48-81 (1938) (noting divergence in national court case law as to copyright owners’ control over secondary uses of broadcast music).

<sup>214</sup> Report by the Sub-Committee on Broadcasting and Mechanical Instruments, June 13, 1948, reprinted and translated in WIPO, THE BERNE CONVENTION FOR THE PROTECTION OF LITERARY AND ARTISTIC WORKS FROM 1886 TO 1986, 185 (1986).

<sup>215</sup> See RICKETSON, *supra* note 211, at 453 (providing examples of public locations).

<sup>216</sup> *Id.* (quoting Comments in program for the Brussels Conference to the Berne, *Documents de la Conference reunie a Bruxelles du 5 au 26 Juin 1948* at 266) [hereinafter Brussels Conference Comments]. Accord NORDEMANN ET AL, *supra* note 211, at 127 (citing similar public places); STEPHEN M. STEWART, INTERNATIONAL COPYRIGHT AND NEIGHBORING RIGHTS 125 (2d ed. 1989) (same).

<sup>217</sup> See 1978 WIPO GUIDE, *supra* note 210, at 68-69.

broadcast, which may or may not be for commercial ends.

The Convention's answer is 'no.' Just as, in the case of a relay of broadcast by wire, an additional audience is created . . . so, in this case too, the work is made perceptible to listeners (and perhaps viewers) other than those contemplated by the author when his permission was given. Although, by definition, the number of people receiving a broadcast cannot be ascertained with any certainty, the author thinks of his license to broadcast as covering only the direct audience receiving the signal within the family circle. Once this reception is done in order to entertain a wider circle, often for profit, an additional section of the public is able to enjoy the work and it ceases to be merely a matter of broadcasting. The author is given control over the new public performance of his work.<sup>218</sup>

Given Berne's text and its drafting history, the United States cannot defend the FIMLA's broad secondary use licensing exemption as compatible with article 11*bis*(1)(iii). To the contrary, prior to the United States' ratification of the Berne Convention in 1989, the Ad Hoc Working Group on the United States Adherence to the Berne Convention acknowledged that "the principal concern of [Berne's] drafters" in enacting article 11*bis*(1)(iii) was the "use of a loudspeaker in a public place to communicate the contents of a broadcast work," an act which "constituted a new use of a broadcast to reach a new public."<sup>219</sup>

Although the FIMLA is unmistakably incompatible with article 11*bis*(1)(iii), the legality of the homestyle exemption is marginally more uncertain. In its 1986 report, the Ad Hoc Working Group concluded that the homestyle exemption was permissible under the treaty. It relied on a distinction in Berne's drafting history between "lower-amplification home receivers" (the use of which did not require authorization from copyright owners) and "loudspeakers" (which involved a "qualitatively different" technology and thus required such authorization).<sup>220</sup>

There is some support for this distinction in the drafting history.<sup>221</sup>

---

<sup>218</sup> *Id.*

<sup>219</sup> See *Final Report*, *supra* note 207, at 529.

<sup>220</sup> *Id.*

<sup>221</sup> At the Brussels conference, the drafters of Article 11*bis* stressed the copyright owner's right to control performances of music in public places and noted the difference between "receivers" and "loudspeakers." However, the drafters also questioned whether the type of receiver used should make a difference in deciding whether an additional license was required:

Why make a legal difference depending on whether the amplifier is weak and solely intended for private usage, or sufficiently strong to work for the satisfaction of a more or less large public? The sounds made by the receiver (even if they are amplified by a loud speaker) constitute only the continuation and the achievement of the program; consequently the authorization to broadcast [given by the copyright owner] includes

Nevertheless, WTO jurists should invoke the primacy given to textual and purposive analysis in the Vienna Convention and should eschew reliance on this distinction as a basis for upholding the homestyle exemption.

First, article 11*bis*(1)(iii) expressly refers to “communication by loudspeaker or any other analogous instrument . . . .”<sup>222</sup> This language precludes any distinction based on the type of equipment used to transmit broadcast music where the technology used is sufficiently powerful to reach a significant number of listeners or viewers located in commercial establishments. This is so even if individuals who receive the broadcasts in their private homes use the same technology.<sup>223</sup> Moreover, the EC can point to at least one judicial interpretation of the homestyle exemption to demonstrate that United States courts have sanctioned some augmentation of standard home receiving equipment as technology available to private consumers has become more sophisticated over the years.<sup>224</sup>

Second, the purpose underlying article 11*bis*(1)(iii) is to grant to copyright owners a distinct right to control secondary uses of broadcast music in a variety of public venues, including in particular bars, restaurants and commercial establishments.<sup>225</sup> As PROs in the United States have long argued, secondary uses of broadcast music in these locations are not encompassed within the license given to radio and television stations to transmit music to individuals receiving the broadcast in private.<sup>226</sup> Thus, even the use of homestyle receiving equipment by businesses allows broadcast music to reach

---

also the authorization to communicate the program to all listeners which the receiving set can reach.

*Brussels Conference Comments*, *supra* note 216, at 266 (English translation on file with author). *But see* LADAS, *supra* note 213, at 480 (characterizing this argument as “specious”).

<sup>222</sup> Berne Convention, *supra* note 15, art. 11*bis*(1)(iii).

<sup>223</sup> Recall that contemporary “homestyle” receiving equipment is sufficiently powerful to enable businesses to transmit background music in stores as large as 4000 square feet. *See* Wilk, *supra* note 165, at 805 & n.110.

<sup>224</sup> *See* Broadcast Music, Inc. v. Claire’s Boutiques, Inc., 949 F.2d 1482, 1493 (7th Cir. 1991) (analyzing factors including “number of speakers used, manner in which the speakers are installed, use of concealed wiring, distance of speakers from the receiver, and integration of the stereo system with other technologies” and holding that “hiding of the speakers in a dropped ceiling and the concealment of the speaker wires” did not vitiate exemption); *see also Examination Procedure*, *supra* note 158 at 5 (“Technology is under constant evolution and the household radio technology of the 70s has been superseded several times, increasing the scope of the homestyle exemption.”); Johnson, *supra* note 19, at S-6 (noting that consumers are used more sophisticated electronic equipment today compared to date when statute was enacted).

<sup>225</sup> *See* 1978 WIPO GUIDE, *supra* note 210; LADAS, *supra* note 213, at 480-81 (“The diffusion by loud speaker is a new and distinct communication to the public, jurisdictionally independent of the original broadcasting.”).

<sup>226</sup> *See* 1994 Hearings, *supra* note 69, at 275; *see also* ROTHENBERG, *supra* note 69, at 24-25.

an additional public audience and thus requires the copyright owners' prior authorization.

For these reasons, WTO dispute settlement jurists should conclude that both the FIMLA and the homestyle exemption are *prima facie* violations of the minimum standards of copyright protection guaranteed by the Berne and TRIPs treaties.

C. *Exceptions and Limitations Defenses: Choosing the Correct Legal Standard*

The exclusive rights guaranteed to authors and copyright owners are not unlimited. To the contrary, members of the Berne Union have long enjoyed significant discretion to curb those rights by adopting exceptions and limitations in the form of free use exemptions or compulsory licenses. These copyright-limiting tools allow member states to balance the rights of copyright owners against the interests of the public at large and to achieve other important social objectives. The heart of the FIMLA dispute, therefore turns on whether the United States can invoke any of the "exceptions and limitations" clauses contained in either the Berne Convention or the TRIPs Agreement to justify its music licensing laws.

A preliminary issue of vital significance for resolving the FIMLA dispute is the relationship between the exceptions and limitations found in Berne and those set forth in TRIPs. Unlike Berne, which attaches different exceptions and limitations to each exclusive right enjoyed by copyright owners,<sup>227</sup> TRIPs article 13 contains a single standard for measuring all such restrictions. According to this standard, each treaty party must "confine limitations or exceptions to exclusive rights to certain *special cases* which do not conflict with a *normal exploitation of the work* and do not *unreasonably prejudice the legitimate interests* of the right holder."<sup>228</sup>

The proper construction of article 13's "three-step" test<sup>229</sup> is among the most uncertain and contested issues in international copyright law. The test was transplanted from a provision of the Berne Convention permitting member States to impose free use limitations on copyright owners' reproduction right.<sup>230</sup> Although member States unanimously adopted the three-step test in

---

<sup>227</sup> See Paul Edward Geller, *International Copyright: An Introduction* § 5[5][b][ii] at INT-202 [hereinafter Geller, *International Copyright*] in 1 INTERNATIONAL COPYRIGHT LAW AND PRACTICE (Paul Edward Geller & Melville B. Nimmer eds. 1998) [hereinafter INT'L COPYRIGHT LAW]; see also Helfer, *supra* note 29, at 370-71 & n.52 (identifying Berne exceptions and limitations).

<sup>228</sup> TRIPs, *supra* note 16, art. 13 (emphasis added).

<sup>229</sup> See Thomas Heide, *The Berne Three-Step Test and the Proposed Copyright Directive*, 21 EUR. INTELL. PRP. REV. 105, 105 (1999).

<sup>230</sup> Berne Convention, *supra* note 15, art. 9(2) ("It shall be a matter for legislation in the countries of the Union to permit the reproduction of [literary and artistic] works in certain *special cases*, provided that such reproduction does not conflict with a *normal exploitation*

the diplomatic conference preceding the most recent revision of Berne, they could not agree on how each of the three steps in the test should be interpreted or applied.<sup>231</sup> As a result of this lack of consensus, Berne's signatories have enjoyed broad discretion to decide which cases are "special," what exploitation is "normal" and whether "unreasonable prejudice" results from a particular free use.<sup>232</sup> With that discretion, a wide divergence of approaches among domestic legal systems has evolved.<sup>233</sup>

Whether member States' broad discretion continues under the TRIPS Agreement is uncertain, however. In particular, it is unclear whether article 13's three-step test contains a stricter standard for measuring the treaty-compatibility of national law exceptions and limitations than the multifarious standards found in Berne.<sup>234</sup> Commentators have argued, however, that such a strict construction of article 13 would be unwise as a matter of copyright policy and should be avoided by WTO jurists.<sup>235</sup>

---

of the work and does not *unreasonably prejudice* the legitimate interests of the author.") (emphasis added).

<sup>231</sup> See Heide, *supra* note 229, at 105 ("[T]here is still considerable dispute as to [the three-part test's] scope, with notes to the Conference [at which the test was drafted] offering no guidance as to the meaning of the various conditions constituting the test."); Helfer, *supra* note 29, at 372 ("[T]here is little common ground to interpret these 'vague' and 'elusive' phrases" of the three-part test, and noting that "the treaty's preparatory work sheds little light on their meaning") (footnotes and citations omitted).

<sup>232</sup> See NORDEMANN ET AL, *supra* note 211, at 17 (stating that it is "predominantly the case" that Berne leaves "to domestic law to enact general limitations or limitations covering certain cases or the details of execution"); RICKETSON, *supra* note 211, at 483 (finding that normal exploitation "will be a matter for national legislation, and ultimately national tribunals, to determine"); *id.* at 484 (showing that the unreasonable prejudice standard is "ultimately determined by each national law"); *id.* at 487 (finding that article 9(2) "leaves a considerable area of discretion to national legislation"); STEWART, *supra* note 216, at 80 ("[E]ach member country has to decide what the legitimate interests of the author are, whether the prejudice of these interests . . . is reasonable or unreasonable, and what amounts to a normal exploitation of the work which must be safeguarded.").

<sup>233</sup> See Thomas Dreier, *The Cable and Satellite Analogy in THE FUTURE OF COPYRIGHT IN A DIGITAL ENVIRONMENT* 57, 63 (P. Bernt Hugenholtz, ed. 1995) (describing national law implementation of article 9(2) as in "total disharmony").

<sup>234</sup> See Netanel, *The Next Round*, *supra* note 32, at 459 ("TRIPs article 13 arguably circumscribes more narrowly than Berne the limitations and exceptions to copyright owner rights that member states may allow.").

<sup>235</sup> See Helfer, *supra* note 29, at 432-39 (arguing that WTO jurists should grant significant deference to national legislatures when reviewing exceptions and limitations in domestic copyright statutes). See also Rochelle Cooper Dreyfuss & Andreas Lowenfeld, *Two Achievements of the Uruguay Round: Putting TRIPs and Dispute Settlement Together*, 37 VA. J. INT'L L. 275, 297 (1997) (advancing similar arguments for construing the TRIPs-compatibility of exceptions and limitations found in all intellectual property laws); Netanel, *The Next Round*, *supra* note 32, at 449, 487-89 (advancing similar arguments based on adoption of WIPO Copyright Treaty and international free speech principles).

Although the question whether TRIPS *constrains* member states' discretion to adopt exceptions and limitations is open to debate, the converse question of whether TRIPS article 13 *expands* that discretion is not subject to dispute. By virtue of TRIPS article 2(2), member States decided that nothing in TRIPS could be interpreted as authorizing national governments to "derogate from existing obligations" created by the Berne Convention.<sup>236</sup> Stated more concretely, article 2(2) makes plain that no member state may invoke the TRIPS Agreement to justify *more expansive* exceptions and limitations than those already found in Berne. In effect, even with the adoption of a seemingly unitary standard in TRIPS article 13, any narrower exceptions and limitations

---

<sup>236</sup> TRIPS, *supra* note 16, art. 2(2) ("Nothing in Parts I to IV of this Agreement shall derogate from existing obligations that Members may have to each other under" *inter alia*, "the Berne Convention . . ."). A similar prohibition is found in Berne itself. *See* Berne Convention, *supra* note 15, art. 20 (reserving member states' "right to enter into special agreements among themselves, in so far as such agreements grant to authors *more extensive rights* than those granted by the [Berne] Convention, or contain other provisions not contrary to this Convention") (emphasis added).

Further support for this interpretation is found in the recently-adopted WIPO Copyright Treaty, Dec. 20, 1996, CRNR/DC/94 (1996), *reprinted in* 36 I.L.M. 65 (1997) ("WCT"), an international agreement adopted by the members of the Berne Convention in principal part to extend copyright protection to the Internet. Article 10 of the WCT adopts a three-step limitations and exceptions test identical to that found in TRIPS article 13, and it applies that test to both the new exclusive rights recognized in the WCT and to the exclusive rights already protected by the Berne Convention. *See, e.g.*, WCT, *supra* art. 10(2) ("Contracting Parties shall, when applying the Berne Convention, confine any limitations of or exceptions to rights provided for therein to certain special cases that do not conflict with a normal exploitation of the work and do not unreasonably prejudice the legitimate interests of the author."). Although this language provides little guidance on whether the three-step test authorizes exceptions and limitations broader than those found in the Berne Convention, an Agreed Statement adopted together with the WTC does provide an informative gloss on how the three-step test should be interpreted:

It is understood that the provisions of Article 10 permit Contracting Parties to carry forward and appropriately extend into the digital environment limitations and exceptions in their national laws *which have been considered acceptable under the Berne Convention*. Similarly, these provisions should be understood to permit Contracting Parties to devise *new exceptions and limitations* that are appropriate in the *digital network environment*.

It is also understood that Article 10(2) *neither reduces nor extends the scope of applicability of the limitations and exceptions permitted by the Berne Convention*.

Agreed Statements Concerning the WIPO Copyright Treaty, WIPO Doc. CRNR/DC/96 (Dec. 20, 1996) (emphasis added). Although not entirely free from ambiguity, the Agreed Statement strongly suggests that States may apply more generous exceptions and limitations to exclusive rights "in the digital network environment," but must adhere to existing Berne standards in non-digital media. Moreover, the Agreed Statement's gloss on the three-step test in the WTC is also persuasive authority for interpreting the identical test in the TRIPS Agreement. *See* Netanel, *The Next Round*, *supra* note 32, at 488 (arguing that WTO jurists should look to Agreed Statement when deciding copyright disputes under TRIPS article 13).

clauses contained in the Berne Convention will continue to serve as a floor below which national exceptions and limitations laws may not fall.<sup>237</sup>

The insight that the Berne Convention constrains member States' power to restrict copyright owners' exclusive rights provides a means for WTO jurists to simplify the FIMLA dispute and to avoid deciding the case on the basis of the contested three-step test.<sup>238</sup> Specifically, the jurists can use this insight to limit the arguments that the United States can raise in defense of its music licensing laws. The United States can argue that its laws are compatible with any of the exceptions and limitations found in the Berne Convention itself. The United States may not, however, defend the statutes as TRIPs-compatible based on an autonomous construction of article 13's three-step test, if that construction would result in upholding an exemption that is more expansive than the exemptions permitted under the exceptions and limitations recognized by Berne.<sup>239</sup>

---

<sup>237</sup> As Paul Geller has written, the three-step test contained in article 13 is "potentially misleading" because it "purports to set out general parameters for all limitations and exceptions to copyright," and therefore suggests that TRIPs member states' national laws may contain exceptions and limitations broader than those permitted under the Berne Convention. Geller, *International Copyright*, *supra* note 227, § 5[5][b][ii] at INT-202. Such a construction of Article 13 is erroneous, he argues:

Berne rights are respectively subject to specific limitations and exceptions, and countries would impermissibly derogate from these rights if they respected only broader limitations or exceptions. Article 2(2) of the TRIPs Agreement categorically precludes anything in the operative copyright provisions from derogating from "existing obligations" under, *inter alia*, the Berne or Rome Conventions. A TRIPs panel should therefore read Article 13 of the TRIPs Agreement as further restricted by such narrower limitations or exceptions as the Berne Convention specifically sets out to its minimum rights.

*Id.* at INT-202 to INT-203. *Accord* DANIEL GERVAIS, *THE TRIPs AGREEMENT: A DRAFTING HISTORY AND ANALYSIS* 45-46, 89-90 (1998) (construing TRIPs article 2(2) together with article 13 to conclude that Berne imposes a constraint on permissible exceptions and limitations); J.A.L. STERLING, *WORLD COPYRIGHT LAW* 550 (1999) (rejecting argument that "Article 13 of TRIPs carries the implication that, as regards rights guaranteed under the Berne Convention, limitations and exceptions additional to those permitted under the Berne Convention may be introduced, provided the 'three step' test is applied"). For an early articulation of this construction of the two treaties, see Mihaly Ficsor, *International Norm-setting in the Field of Copyright and Neighboring Rights: A Growing Number of Unsettled Problems* at 66-67 (paper delivered at International Conference on Intellectual and Industrial Property held by EC Commission, Athens, Apr. 11-13, 1994) (on file with author).

<sup>238</sup> See *infra* Part III.F (explaining why WTO jurists should frame their decision so as to avoid applying the three-step test to judge the treaty-compatibility of the United States' music licensing laws).

<sup>239</sup> The United States' initial brief to the WTO fails to grasp this crucial point. Without citing to or distinguishing TRIPs article 2(2) or Berne article 20, the United States argues that "[t]he relevant issue in this case is not whether Berne rights are implicated, but whether the provisions at issue are permissible exceptions under the standard of TRIPs Article 13."

In the sections that follow, I identify two distinct Berne-based exceptions and limitations arguments that the United States can raise in support of the FIMLA and the homestyle exemptions. Neither of these arguments, however, is likely to convince WTO jurists to uphold the exemptions. I then turn to a third argument, one that may lead to a “back door” reintroduction of the three-step test and to the economic and distributional arguments that the test enables the United States to raise.

D. *Article 11bis(2)–Imposing Conditions on the Broadcast Right*

One argument in defense of United States music licensing laws is found in the first sentence of Article 11*bis*(2), which gives Berne signatories the authority to enact “legislation . . . to determine the conditions under which the rights mentioned [the first paragraph of in Article 11*bis*] shall be exercised.”<sup>240</sup> At first glance, this provision appears to give the United States wide latitude to limit copyright owners’ control over secondary use of broadcast music. However, the word “conditions” is a term of art in Berne that authorizes member States to enact compulsory licenses but not free use exemptions.<sup>241</sup> This is confirmed by the second sentence of article 11*bis*(2), which emphasizes that any conditions a member state imposes “shall not in any circumstances be prejudicial to . . . [the author’s] right to obtain *equitable remuneration* which, in the absence of agreement, shall be fixed by competent authority.”<sup>242</sup>

The reasons for allowing member States to impose conditions on the broadcast right (including the right to control secondary uses of broadcast music) can be traced back to fears about the monopoly powers of national collective rights organizations “which controlled the performing rights in most musical works, and which might be tempted to abuse these rights in relation to the new medium of broadcasting.”<sup>243</sup> However, States were divided over exactly how to limit copyright owners’ control over broadcast works. Some governments favored exempting particular uses of broadcast works altogether,

---

*First U.S. Submission, supra* note 7, at 11.

<sup>240</sup> Berne Convention, *supra* note 15, art. 11*bis*(2).

<sup>241</sup> As Ricketson explains, “[t]he reference to ‘conditions’ in article 11*bis*(2) is usually taken to refer to the imposition of compulsory licenses, but the form of these licenses if left to national legislation to determine.” However, “the power to impose conditions on the exercise of rights does not carry with it the power to deny those rights.” RICKETSON, *supra* note 211, at 525.

<sup>242</sup> Berne Convention, *supra* note 15, art. 11*bis*(2) (emphasis added); *see also* NORDEMANN ET AL, *supra* note 211, at 128 (“If it had been the intention of the Berne Convention to follow the domestic concepts of what is considered equitable in each and every country of the Union . . . , then it could have spared itself the trouble of referring to an equitable remuneration; for after all some countries consider a minimal or even no remuneration at all, to be ‘equitable.’ The purpose of par. 2, however, is precisely to *limit* the authority of the countries of the Union in this area, and it therefore proceeds from a concept of what would be equitable all over the countries of the Union.”).

<sup>243</sup> RICKETSON, *supra* note 211, at 522; *see also* LADAS, *supra* note 213, at 405.

whereas others opposed any form of restriction on copyright owners' licensing powers. A compromise was ultimately reached under which national governments could impose a system of compulsory licenses on all types of broadcasts, but could not impose free use exemptions that deny copyright owners the right to receive payment for the use of their works.<sup>244</sup>

Under article 11*bis*(2), therefore, national governments enjoy wide discretion to determine the form of compulsory licenses for secondary uses of broadcast works, including the structure of the governmental bodies that administer those licenses.<sup>245</sup> But they do not have the authority to remove an entire category of uses from the copyright owner's control without providing some form of compensation. Both the FIMLA and the homestyle exemptions achieve precisely that result.<sup>246</sup> For this reason, WTO jurists should have little trouble rejecting the music licensing laws as justified under article 11*bis*(2).

#### E. *Implied Exceptions to Broadcast and Performance Rights*

A more plausible argument for the United States to assert is that Berne Convention signatories enjoy, outside of Article 11*bis*, the authority to restrict copyright owners' public performance and broadcast rights even if no compensation is paid. Nothing in the text of the treaty authorizes such restrictions. But the Convention's preparatory work does recognize "a number of exceptions that are to be implied and which, according to the wishes of successive conferences of revision, will not be in conflict with the Convention if they are embodied in national legislation of member countries."<sup>247</sup> The question for WTO jurists to resolve is whether these implied exceptions are broad enough to encompass the United States' music licensing laws.

As an initial matter, it might be argued that the absence of any textual support for such copyright restrictions precludes WTO jurists from even considering an implied exceptions argument by the United States. Had State parties to the TRIPs Agreement wanted to validate these unwritten exceptions, they could easily have done so by including a clause to that effect in the treaty. This is particularly true given that TRIPs expressly clarifies other copyright

---

<sup>244</sup> RICKETSON, *supra* note 211, at 523. In addition, article 11*bis*(2) expressly states that governments may impose compulsory licenses only in "the absence of agreement" between copyright owners and users. For an argument on how the United States might structure a compulsory license system to encourage such an agreement, see *infra* Part IV.C.3.

<sup>245</sup> For a discussion of how the United States should capitalize on this discretion in fashioning a solution to the FIMLA dispute, see *infra* Part IV.C.

<sup>246</sup> See STEWART, *supra* note 216, at 125 ("[A]rticle 11*bis*(2) leaves the national legislation a very wide discretion in the treatment of the broadcasting right including the application of a compulsory licence system;" however, national laws cannot eviscerate the "right to equitable remuneration . . ."); see also *Examination Procedure*, *supra* note 158, at 13 (stating that the homestyle exemption violates Article 11*bis*(2) because it "not only abolishes the rightholders' right to authorise the use of their music, it also deprives them of all remuneration in respect of the use of their works").

<sup>247</sup> RICKETSON, *supra* note 211, at 532.

obligations that were ambiguous under Berne.<sup>248</sup> Nevertheless, the fact that TRIPs incorporates the Berne Convention by reference rather than merely reproducing its text *within TRIPs itself* strongly suggests that TRIPs' drafters did not intend to divorce Berne's bare text from the historical and interpretive context in which it was created and interpreted by courts and commentators.<sup>249</sup> In addition, the EC concedes that implied exceptions are part of the Convention's "spirit,"<sup>250</sup> and argues instead that the FIMLA and homestyle exemptions are beyond the permissible scope of these exceptions. For these theoretical and practical reasons, WTO jurists are likely to evaluate the implied exceptions argument on its merits.

The power of Berne member States to impose implied restrictions on the exclusive broadcast and public performance rights arose from the step-by-step historical evolution of the Convention's protected rights. Prior to the 1948 Brussels revision, the Berne Convention recognized only limited public performance and radio broadcast rights. As a result, the domestic copyright laws of most member States permitted certain unauthorized public performances and broadcasts of copyrighted works.<sup>251</sup> With the addition of more comprehensive broadcast and performance rights into Berne in 1948, the question arose whether these laws were compatible with the treaty.<sup>252</sup>

Member States discussed this issue extensively during the 1948 Brussels revision of the Convention. As an initial matter, the government representatives do not appear to have understood these implied exceptions as formal treaty "reservations."<sup>253</sup> Such a designation would have restricted the exceptions' application to national laws already in force on the date that a State

---

<sup>248</sup> See, e.g., TRIPs, *supra* note 16, art. 10 (clarifying that "computer programs . . . shall be protected as literary works under the Berne Convention").

<sup>249</sup> See Frederick M. Abbott, *WTO Dispute Settlement and the Agreement on Trade-Related Aspects of Intellectual Property Rights*, in *INTERNATIONAL TRADE LAW AND THE GATT/WTO DISPUTE SETTLEMENT SYSTEM* 421, 421 (1997); see also Netanel, *The Next Round*, *supra* note 32, at 452 ("It is doubtful that the TRIPs drafters intended to incorporate the Berne provisions in their strict textual form without any connection to the Berne Convention's pre-existing interpretive framework.").

<sup>250</sup> *Examination Procedure*, *supra* note 158, at 13; see also *First EC Submission*, *supra* note 208, at ¶¶ 93-96 (noting the existence of implied exceptions but arguing that they do not excuse United States licensing laws).

<sup>251</sup> See LADAS, *supra* note 213, at 401-02 (identifying national laws permitting public performances without payment to copyright owners prior to 1948 Brussels revision of Berne Convention).

<sup>252</sup> RICKETSON, *supra* note 211, at 437-38, 533.

<sup>253</sup> See *id.* at 533 (noting that government delegates rejected an amendment to the Berne Convention authorizing member States "to retain limitations *presently existing* in their national laws") (emphasis added); see also Ficsor, *supra* note 237, at 66-67 (noting that these unwritten limitations on copyright owner's exclusive rights are "more precisely characterized" as "minor exceptions" rather than "minor reservations").

became a member of the Berne Union<sup>254</sup> and thus would have precluded the United States, which ratified Berne in 1989, from defending the 1998 FIMLA (but not the 1976 homestyle exemption) as an implied exception under the treaty.

The drafters did, however, reject a proposal to incorporate an express limitations clause into the treaty on two grounds. First, it was “impossible to list all the exceptions exhaustively in the Convention as they were too varied.” Second, a more general reference to exceptions “presently existing in . . . national laws” would encourage States to incorporate new exceptions into their national laws before joining Berne. Yet the drafters also agreed that these domestic laws did not violate the treaty.<sup>255</sup>

Although the implications of these discussions are far from clear, substantial evidence suggests that the drafters intended to permit national laws under an “implied exceptions” theory only if they derogated insignificantly from copyright owners’ exclusive rights. In particular, the preparatory work (1) characterized these exceptions as “minor reservations” that should be interpreted restrictively, (2) stated that the exceptions could not be justified merely if they were made “without the aim of profit” and (3) referred to examples of acceptable exemptions as including public performances during religious ceremonies, holidays, military parades and charitable functions as well as performances furthering the needs of child and adult education.<sup>256</sup>

According to a leading commentator on the Convention, this drafting history compels the conclusion that

[implied] exceptions to the rights granted . . . *must be concerned with uses of minimal, or no, significance to the author.* . . . The fact that [the drafters] rejected the option of inserting in the Convention a provision expressly reserving the right of national legislation to make such minor exceptions also confirms these exceptions are acceptable only when they are of a *de minimis* kind. If an express provision had been inserted, this would make it far easier for member nations to assert that the Convention recognised their right to make such exceptions and that they were therefore free to go beyond those of a purely *de minimis* kind, for example, because of a particular public interest that might justify the abridgement of the authors’ rights in these circumstances.<sup>257</sup>

---

<sup>254</sup> See RICKETSON, *supra* note 211, at 764-79 (discussing reservations which “grandfathered” a national law exceptions in force at the time a State ratified the Berne Convention and the extent to which such reservations were authorized under different revisions of the Convention).

<sup>255</sup> See *id.* at 534.

<sup>256</sup> See *id.* at 533-34.

<sup>257</sup> *Id.* at 536 (emphasis added). It is clear from Ricketson’s comments that the implied exceptions do not require payment be made to copyright owners for unauthorized uses of their works. *But see* NORDEMANN ET AL, *supra* note 211, at 126 (noting a dispute on this point but arguing that remuneration must be paid when member states rely on implied

This history and commentary impose a heavy burden on the United States to justify either the FIMLA or the homestyle exemption as a permissible implied exception to music copyright owners' exclusive broadcast and performance rights. Both laws sanction the free commercial exploitation of copyrighted music by a large segment of United States businesses, businesses that PROs in the United States had once actively sought to license.<sup>258</sup> Furthermore, both the EC and the United States sources have estimated that PROs will lose significant licensing revenues as a result of the exemption's expansion in 1998.<sup>259</sup> Thus, if WTO jurists rely solely on Berne's preparatory work to analyze these implied exceptions, they will have ample authority to find both laws in violation of article 11*bis*(1)(iii) of the Berne Convention and thus in violation of article 9(1) of the TRIPs Agreement.

#### F. *Reintroducing the Three-Step Test Through the Back Door*

At this juncture, the WTO jurists hearing the FIMLA dispute should conclude their legal analysis and issue a decision in favor of the EC. Although the United States is defending the FIMLA and homestyle exemptions under an autonomous construction of TRIPs article 13, that defense is foreclosed by of the TRIPs article 2(2) which precludes member States from adopting copyright exceptions and limitations broader than those permitted under the Berne Convention.<sup>260</sup> In addition, this simple resolution of the FIMLA dispute would avoid entangling WTO jurists in the complex and unresolved issues surrounding the proper interpretation of the three-step test and would allow

---

limitations).

<sup>258</sup> See NIMMER & NIMMER, *supra* note 70, § 8.18[C][2] at 8-217 n.94.3 (noting that BMI lost \$40,000 per year from application of homestyle exemption in *Claire's Boutique* case to retail chain stores); *Examination Procedure*, *supra* note 158, at 31 (stating that BMI estimated a loss of \$50,000 in licensing revenue from application of homestyle exemption in *Edison Brothers* case to 1500 chain stores); Commission Decision of December 11, 1998 under the provisions of Council Regulation (EC) No. 3286/94 concerning section 110(5) of the Copyright Act of the United States of America, 1998 O.J. (L 346) 60, 61 ("The [homestyle] exemption is widely applied on a commercial basis [throughout] the United States and the economic losses incurred by Community right-holders are important, ranging between 13 percent to 24 percent of the United States performing rights organizations' annual distributions to Community collecting societies representing composers and arrangers of music, lyricists and publishers."). See also Loren, *supra* note 7, at 26-30 (discussing PROs attempts to downplay homestyle exemption in their licensing literature).

<sup>259</sup> See Pruzin, *Three Countries Join*, *supra* note 13, at 321 (noting that the Irish Music Rights Organization estimated \$30.3 million annual losses as a result of the United States licensing laws); *1997 Hearings*, *supra* note 19, at 81 (statement of Wayland Holyfield on behalf of ASCAP) (reviewing findings of Congressional Research Service that FIMLA would exempt 65.2 percent of all eating establishments and 71.8 percent of all drinking establishments from any licensing obligations).

<sup>260</sup> See *First U.S. Submission*, *supra* note 7, at 11; see also *supra* Part III.C.

them to defer those issues to future dispute settlement proceedings.<sup>261</sup>

Unfortunately, one argument advanced by the EC may impede this neat conclusion to the case. In its February 1998 legal analysis of the music licensing laws, The EC asserted that the three-step test in TRIPs article 13 is inapplicable to the FIMLA dispute.<sup>262</sup> Yet in a somewhat perplexing move, it adopted the same three-step test to judge the United States' implied exceptions argument under the Berne Convention. More specifically, the EC asserted that because the Berne Convention's drafting history does not provide a clear standard to determine which national laws are permissible under an implied exceptions theory, WTO jurists should import the standard found in article 9(2) of the Berne Convention.<sup>263</sup> As noted above, article 9(2) contains a three-step test that is almost identical to that found in TRIPs article 13.<sup>264</sup>

This reintroduction of the three-step test is significant. At each step of the test, the United States has a window to present the economic and distributional

---

<sup>261</sup> In theory, the WTO jurists could apply TRIPs article 13 as a means of *narrowing* the implied exceptions previously considered permissible under the Berne Convention. See GERVAIS, *supra* note 237, at 90 ("When these [implied Berne] exceptions are invoked, they may from now on be submitted to the general test of Article 13, which should be interpreted on the basis of Article 9(2) of the Berne Convention."). As I explain in Part III.F, however, such a narrowing construction of article 13 is both unwise and unnecessary to resolve the FIMLA dispute.

<sup>262</sup> The EC argued that:

Article 13 of TRIPs cannot apply to the homestyle exemption because the homestyle exemption denies equitable remuneration to the rightholder. Such a denial of equitable remuneration is not a limitation or exception to an exclusive right; once conditions have been placed on the exercise of the right so that *only* a right to remuneration exists, that is no longer an exclusive right and there can be no further limitations.

*Examination Procedure*, *supra* note 158, at 19. The EC appears to reason that no treaty party may invoke Article 13 to justify a restriction on a Berne Convention right which is subject to compulsory licensing, because anyone may infringe such a right subject to the payment of compensation. Thus, the right is exclusive in name only. This claim is a more specific version of the point that TRIPs member States may not invoke article 13 to broaden the exceptions and limitations found in the Berne Convention. See *supra* Part III.B.

<sup>263</sup> See *Examination Procedure*, *supra* note 158, at 13 ("The problem is how to define the criteria to which an exemption should respond to be regarded as minor. In this regard, the criteria laid down in Article 9(2) of the Berne Convention may well provide an appropriate yardstick."). In its initial submission to the WTO panel, the EC did not raise this argument in detail, reserving its right to comment on all exceptions and limitations defenses after the United States filed its initial submission to the panel. See *First EC Submission*, *supra* note 208, at ¶ 96.

<sup>264</sup> Recall that the three-step test requires treaty parties to confine limitations or exceptions (1) to "certain special cases," (2) which do "not conflict with a normal exploitation of the work," and (3) "do not unreasonably prejudice the legitimate interests" of the author or right holder. Berne Convention, *supra* note 15, art. 9(2); TRIPs, *supra* note 16, art. 13. However, the Berne Convention's drafting history offers no apparent support for using Article 9(2)'s three-step test as the standard for measuring implied exceptions. See *supra* Part III.E.

arguments discussed in Part II. Given the lack of agreement among the treaty parties over the three-step test's meaning, WTO jurists will be unable to interpret and apply the test solely by applying the traditional methods of treaty analysis set forth in the Vienna Convention or by consulting commentators' writings.<sup>265</sup> They will also need to address broader policy-based issues, including: (1) the importance of balancing copyright protection against the public interest and other social objectives, (2) the need to grant national legislators, administrators and judges discretion to strike that balance, (3) the extent to which other Berne and TRIPs member States have enacted statutes similar to the FIMLA and the homestyle exemption and (4) whether international copyright law endorses a "market failure" approach to exceptions and limitations.

If the WTO jurists choose to apply the three-part test to United States copyright laws,<sup>266</sup> they will provide crucial guidance to interpret a standard by which to judge the treaty compatibility of exceptions and limitations laws in all 135 TRIPs member States.<sup>267</sup> The construction of the three-part test will be, therefore, one of the most important and contested issue in the dispute between the United States and the EC. It thus requires extended analysis.

### 1. Step One—The "Special Cases" Requirement

As a threshold matter, member States can justify a limitation on copyright owners' exclusive rights only in "certain special cases." According to Ricketson, this first step of the test implies two distinct requirements. "First, the use in question must be for quite a specific purpose: a broad kind of exemption would not be justified. Secondly [*sic*], there must be something 'special' about this purpose, 'special' here meaning that it is justified by some clear reason of public policy or some other exceptional circumstance."<sup>268</sup>

#### a. *Arguments for the United States*

What arguments support the United States music licensing exemptions as a special case?<sup>269</sup> For the FIMLA, the United States can argue that its provisions

---

<sup>265</sup> See *supra* Parts III.(A), (C).

<sup>266</sup> For a discussion of whether the jurists will apply the three-step test, see *supra* Part III.F.

<sup>267</sup> See Dixon, *supra* note 209, at 14 ("[A]ny WTO interpretation of the Berne three-step test in [the FIMLA] case with respect to a United States copyright exception could well have repercussions in future cases that the United States may want to bring to challenge other countries' exceptions.").

<sup>268</sup> RICKETSON, *supra* note 211, at 482.

<sup>269</sup> In its initial brief to the WTO, the United States adopts a narrow interpretation the "special cases" requirement. It argues that the phrase requires only "that exceptions should be clearly delineated rather than vague and open ended." *First U.S. Submission*, *supra* note 7, at 13 (quotations omitted). Under this standard, even very broad exceptions to exclusive rights would meet the special cases requirement simply by virtue of their clarity.

are limited in a number of distinct ways. First, the statute applies exclusively to nondramatic musical works; it does not exempt dramatic musical works (e.g. operas and Broadway musicals), news programs, talk shows or readings of literary works.<sup>270</sup> Second, the statute imposes equipment restrictions on larger restaurants, bars and stores.<sup>271</sup> Third, the statute only exempts music received from broadcast and cable transmissions; performances of live music or mechanical recordings such as CDs or phonorecords require a license.<sup>272</sup> Fourth, the exemption is vitiated if businesses collect a “direct charge . . . to see or hear” the broadcast.<sup>273</sup> Fifth, the transmission may not be “further transmitted beyond the establishment where it is received.”<sup>274</sup> Finally, the broadcast or transmission from the radio, television or cable station must be “licensed by the copyright owner of the work so publicly performed or displayed.”<sup>275</sup>

The arguments in support of the homestyle exemption as a special case overlap in part with those supporting the FIMLA.<sup>276</sup> The homestyle exemption applies more broadly to performances or displays of all copyrighted works and does not require that the initial broadcast be licensed by the copyright owners.<sup>277</sup> The broadcasting and “direct charge” limitations, however, apply in the same way as they do in the FIMLA. The homestyle exemption’s “further transmitted” restriction is somewhat broader, applying not to transmissions beyond “the establishment,” but to any “further retransmission” [of the

---

<sup>270</sup> 17 U.S.C. § 110(5)(B) (1999) (noting that exemption applies to “communications by an establishment of a transmission or retransmission embodying a performance or display of a *nondramatic musical work*”) (emphasis added).

<sup>271</sup> See 17 U.S.C. §§ 110(5)(B)(i)(I); 5(B)(ii)(I); (5)(B)(i)(II); (5)(B)(ii)(II) (1999).

<sup>272</sup> Consequently, commercial establishments that want to exercise significant control over the content of the music they play for their customers or employees or that want to eliminate commercial advertisements from the performances must either (a) subscribe to a background music service such as Muzak (whose fees already include a performance license) or (b) purchase a license to perform recorded music directly from one or more PRO. For a study concluding that a business’s control over the type of music played significantly affects customer behavior, see Ronald E. Milliman, *Using Background Music to Affect the Behavior of Supermarket Shoppers*, 46 J. MARKETING 86, 90-91 (1982).

<sup>273</sup> 17 U.S.C. § 110(5)(B)(iii) (1999) (conditioning exemption on “no direct charge . . . to see or hear the transmission or retransmission”).

<sup>274</sup> 17 U.S.C. § 110(5)(B)(iv) (1999).

<sup>275</sup> 17 U.S.C. § 110(5)(B)(v) (1999).

<sup>276</sup> The discussion that follows presumes that the FIMLA did not repeal the homestyle exemption’s application to non-dramatic musical works. For a discussion of this point, see *supra* note 7.

<sup>277</sup> This initial licensing requirement has little practical significance given that nearly all radio, television and cable stations are licensed by PROs to broadcast or transmit the musical works contained in their programming. *Cf.* *Buck v. Jewell-LaSalle Realty Co.*, 283 U.S. 191, 199 n.5 (1931) (finding copyright violation based on hotel’s secondary use of unlicensed radio broadcast).

copyrighted work] to the public.”<sup>278</sup> Finally, and most importantly, the performance or display must be made “on a single receiving apparatus of the type commonly used in private homes.”<sup>279</sup> Commercial sound systems or even augmented systems not widely available to consumers are not exempt.

Taken together, the limitations of the homestyle exemption and the FIMLA suggest that both laws have a narrow focus. In addition, the drafting history of article 9(2) of the Berne Convention supports the United States’ position that the two statutes’ limitations on copyright owners’ exclusive rights constitute “special cases.” Although the treaty does not contain an illustrative list of exceptions and limitations, the drafters’ debates reflect the wide variety of permissible exemptions found in national copyright laws. Permissible exemptions include judicial and administrative copying, private copying, copying for research and scientific purposes, industrial and commercial copying and copying for teaching purposes.<sup>280</sup> If these illustrative uses presumptively qualify as “special cases,” and if the drafters deliberately refused to codify this list to maintain the treaty’s flexibility,<sup>281</sup> then the United States may plausibly argue that exempting copyright owners’ control over some (but clearly not all) secondary uses of broadcast music is similarly special.

b. *Arguments for the European Community*

In response to these arguments, the EC can assert several powerful challenges to both statutes. In fact, a slight shift in perspective reveals how easily the laws can be characterized as broad invasions of foreign copyright owners’ exclusive rights. Recall that the Berne Convention requires member States to recognize secondary uses of broadcast music as a distinct treaty-protected right. Both the FIMLA and the statutory construction approach to

---

<sup>278</sup> 17 U.S.C. § 110(5)(A) (1999). Several cases have refused to apply the exemption because the placement of speakers in a different room from the receiver constituted such a further transmission. *See Broadcast Music, Inc. v. Claire’s Boutiques, Inc.*, 949 F.2d 1482, 1495 n.14 (7th Cir. 1991).

<sup>279</sup> 17 U.S.C. § 110(5)(A) (1999). In addition, courts applying a legislative history approach impose additional limitations on the homestyle exemption based on the size of the establishment and the ability to afford a subscription to a background music service. Two recent appellate court decisions, however, focus exclusively on the statutory equipment requirement. *See supra* Part II.B.5.a.

<sup>280</sup> *See RICKETSON, supra* note 211, at 485-87 (discussing the origin and probable scope of each of these exemptions in national laws).

<sup>281</sup> *See id.* at 480, 485 (discussing treaty drafters’ refusal to catalogue permissible exceptions and limitations to reproduction right existing in member states’ national laws); Heide, *supra* note 229, at 105 (explaining that article 9(2) was “intended to be flexible enough to allow member countries to keep their array of exceptions and limitations already existing at the time [the article was adopted], as well as to provide a sufficient margin of freedom to craft inevitable exceptions in order to address important social or cultural needs”).

the homestyle exemption sanction an invasion of this right by commercial establishments that had for many years paid royalties to transmit broadcast music to their customers and employees.<sup>282</sup>

Given the breadth of the FIMLA and the homestyle exemption, the EC rejects treatment of these laws as special cases. It characterizes the exemptions as “the result of pressure by special interest groups” and states that “there is . . . clearly no reason of public interest justifying [their] existence.”<sup>283</sup> The EC also stresses the fact that the laws exempt a commercial use of copyrighted works by for-profit businesses. This sharply distinguishes them from most exceptions and limitations found in the national copyright laws of Berne and TRIPs signatories, including the United States.<sup>284</sup>

c. *Evaluating Commercial Establishments’ Distributional and Fairness Arguments*

The foregoing discussion demonstrates that treaty text, drafting history and commentary provide plausible arguments in support of either party’s position. Therefore, WTO jurists should supplement their analysis of the United States statutes by evaluating the three distributional and fairness arguments that commercial establishments have raised in domestic fora to oppose PROs’ licensing efforts.

---

<sup>282</sup> See *Examination Procedure*, *supra* note 158, at 29 (discussing percentages of exempt businesses and licensing losses projected under United States laws).

<sup>283</sup> *Id.* at 15 (emphasis omitted) (“[W]hen one looks at the exceptions contained in Section 110, it appears clear that . . . most are the result of pressure by special interest groups such as farmers, retailers or war veterans.”). Respected United States copyright commentators have characterized the exemptions in similar terms. See Ralph S. Brown, *Eligibility for Copyright Protection: A Search for Principled Standards*, 70 MINN. L. REV. 579, 593-94 (1985) (characterizing homestyle exemption as an unprincipled “pork-barrel exemption” created “simply because the beneficiaries had a lot of votes, were respectable, and did not want to pay ASCAP”); Litman, *Copyright Legislation*, *supra* note 101, at 354 (characterizing exemptions in section 110 as a “widen-the-loophole bills”). By contrast, the Supreme Court in *Aiken* provided the most principled defense for the exemption, reasoning that a contrary rule would permit copyright owners to exact “multiple tribute” extending “far beyond what is required for the economic protection of copyright owners,” and “would be wholly at odds with the balanced Congressional purpose behind” the public performance right. *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 163 (1975).

<sup>284</sup> For a discussion of many of those exceptions and limitations, see Center for International Legal Studies, *Copyright Infringement* (Dennis Campbell ed. 1997) (summarizing copyright laws of several industrialized and developing nations); *International Intellectual Property Law: Global Jurisdictions* (Dennis Campbell & Susan Cotter eds. 1996).

### 1) Double Dipping

Commercial establishments principally object to granting copyright owners control over secondary uses of broadcast music because such control authorizes the collection of performance royalties from both radio, television and cable stations and from the business that receive those stations' transmissions.<sup>285</sup> Although the double dipping argument seems persuasive in its raw form,<sup>286</sup> evaluating it under the Berne and TRIPs treaties requires disassembling the argument into its different strands and considering empirical evidence of PROs' licensing practices.

In its broadest form, the double dipping argument conflicts with a bedrock premise of the Berne and TRIPs treaties: that copyright owners possess distinct exclusive rights and may demand separate remuneration for exploitation of each of them.<sup>287</sup> Taken to its logical extreme, a double dipping rationale would, for example, prohibit a copyright owner from licensing a restaurant to play the songs on a compact disc because the owner had already collected royalties from the sale of that disc to the restaurant's proprietor.<sup>288</sup> Such a restriction would also undermine copyright law's goal of promoting distribution of music to the public.<sup>289</sup>

The double dipping argument fares little better when framed more narrowly as a challenge to the multiple performance doctrine or the distinction between public and private performances of copyrighted works. Article 11*bis*(1)(iii) of the Berne Convention clearly endorses a copyright owner's right to extract licensing fees for multiple performances of the same broadcast or transmission, just as it constrains member States from equating the playing of music bars, restaurants and stores with performances that take place in private.<sup>290</sup>

---

<sup>285</sup> See *supra* Part I.B.1 (discussing "double dipping" for licensing fees).

<sup>286</sup> See DENNIS M. MAGNUSSON & VICTOR NABHAN, EXEMPTIONS UNDER THE CANADIAN COPYRIGHT ACT 120 (1982) (concluding that the argument that "the copyright owner has already received compensation [for secondary] use of his work in the fees paid by the broadcaster for the right to broadcast the work . . . has considerable logical force" where broadcast revenues and copyright licensing fees "vary with the size of the estimated audience").

<sup>287</sup> See Berne Convention, *supra* note 15, arts. 8-14*ter* (listing exclusive minimum rights guaranteed by the treaty); TRIPs, *supra* note 16, arts. 10, 11, 12 (same).

<sup>288</sup> Some advocates of music licensing reform in the United States understood the double dipping argument in these broad terms. See 1994 Hearings, *supra* note 69, at 147 (testimony of Guy Gregg, National Restaurant Association).

<sup>289</sup> See Thorpe, *supra* note 72, at 214-15 (arguing that "double dipping" promotes the dissemination of works by enabling copyright owners to "lower[] the price of the initial sale" or distribution and spreading cost among multiple users).

<sup>290</sup> See Berne Convention, *supra* note 15, art. 11*bis*(1)(iii). This is not to suggest that Berne member States do not enjoy significant discretion to define the boundary between

A more subtle version of the double dipping argument, however, does have some empirical and logical support. United States PROs charge radio stations blanket and per-program license fees that are based on a percentage of the station's adjusted gross receipts. Those receipts are generated principally from advertising revenues.<sup>291</sup> Those revenues, in turn, are based on the total size of the audience,<sup>292</sup> including listeners and viewers who hear or see a broadcast or transmission in public places. Thus, copyright owners do receive remuneration *from broadcasters* that is attributable to the performance of broadcast music by bars, restaurants and other businesses.<sup>293</sup> To the extent that they also collect royalties *from commercial establishments* for those same broadcasts, copyright owners are compensated twice for the same performance.

This version of the double dipping argument accepts the appropriateness of collecting royalties for multiple performances of the same broadcast or transmission, but objects to exacting more than one set of royalties for the *same* performance—that is, the secondary uses of broadcast music by commercial establishments.<sup>294</sup> The argument is often buttressed by the empirically uncertain claim that exempting secondary uses of broadcast music will increase radio, television or cable listening or viewing, thereby increasing

---

public and private performances, for example, by adopting a rule that treats as a private (and therefore non-licensable) performance the secondary use of broadcast music undertaken by business establishments solely for the enjoyment of a small number of employees. *See infra* Part III.B.3.c (discussing such proposals under Australian and Canadian copyright law). However, the drafting history of article 11*bis*(1)(iii) precludes member states from stretching the public-private boundary to include what have historically been viewed as public spaces. *See supra* Part III.B.

<sup>291</sup> *See* KOHN & KOHN, *supra* note 4, at 878, 937-46 (reproducing sample radio station licenses).

<sup>292</sup> *See* MAGNUSSON & NABHAN, *supra* note 286, at 120 (noting that in commercial broadcasting, revenues received by broadcasters vary with the size of the audience, and fees paid to copyright owners vary with the size of broadcasters' revenues).

<sup>293</sup> *See, e.g.*, *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 163 n.14 (1975) (“[C]opyright holders can and do receive royalties in proportion to advertising revenues of licensed broadcasters, and a broadcaster’s advertising revenues reflect the total number of its listeners, *including those who listen to the broadcasts in public business establishments.*”) (emphasis added); Lilenfeld, *supra* note 117, at 710 n.70, 727 (“[T]he amount of the [license] fee advertisers pay broadcasters is based on the expected number of total listeners or viewers of the broadcast, including those listeners and viewers in public establishments”). *See also infra* note 296 (discussing Arbitron and Nielsen audience survey methods).

<sup>294</sup> As noted above, license agreements between PROs and broadcasters purport to grant broadcasters the right to transmit their broadcasts only to non-public locations such as homes, cars and offices. *See supra* note 69. This does not, however, weaken the challenge posed by this narrower version of the double dipping argument. Although PROs have formally excluded certain rights from the broadcasters' license, music copyright owners nonetheless receive broadcaster-paid royalties that are calculated to include performances occurring in public locations.

the size of the audience and, consequently, broadcaster revenues and copyright owners' royalties.<sup>295</sup>

Yet even this more moderate double dipping argument is potentially insufficient to treat the FIMLA and homestyle exemptions as "special cases" under the Berne Convention. First, the methods used by survey firms to measure the size of radio, television and cable audiences are likely to undercount significantly the number of viewers and listeners exposed to broadcast music in commercial establishments.<sup>296</sup> Second, even if these firms

---

<sup>295</sup> See Lilienfeld, *supra* note 117, at 727 (arguing that "copyright owners would benefit financially from freeing business proprietors to play radios and televisions" without licensing fees). In the absence of empirical studies, it is impossible to determine the net effect on PRO royalties caused by exempting secondary uses of broadcast music. Such an exemption may, for example, encourage businesses that now do not play music in their establishments to install or turn on radio receivers and television sets, thereby increasing the size of the broadcast audience and broadcaster license fees. However, the broadcast audience may also increase because commercial establishments give up paying license fees for recorded music or background music services and shift to broadcast music as a free substitute. PROs in the United States have raised the latter argument to deter Congress from adopting a broad exemption for in-store performances of broadcast music. See PART 2 DISCUSSION AND COMMENTS, *supra* note 134, at 283-84; see also NIMMER & NIMMER, *supra* note 70, § 8.18[C][2] at 8-215 to 8-216 (discussing how homestyle exemption's legislative history was structured to deprive Muzak of an argument that a "reduction of Muzak fees is warranted because it must contend with a competitive free use of background music by commercial establishments using radio sets"). Broadcast music is not, however, a perfect substitute for recorded music or Muzak because it results in a loss of control over content that may be essential to the benefits background music confers on commercial establishments. See Milliman, *supra* note 272, at 90-91 (presenting the conclusions of a study revealing that controlling content of background music crucial to influencing behavior of supermarket shoppers).

<sup>296</sup> Arbitron, a private organization that monitors consumer radio listening habits in the United States, randomly selects listeners to participate in surveys of their listening habits. These surveys ask participants to record all the radio programs they hear, with "listening" defined as "any time you hear a radio – whether you choose the station or not." Arbitron Ratings, *Your Radio Ratings Diary* (1997). The survey forms expressly request listeners to indicate "all the radio you hear," including at home, in a car, at work or in any "other place." *Id.* at 1. The forms do not, however, ask listeners to specify the location of that "other place."

Nielsen Media Research measures television viewing habits in the United States to provide broadcasters, programmers and commercial advertisers with estimates of audience size and composition. Nielsen randomly selects sample households and measures their viewing habits using diaries and a "People Meter" that is placed on each television set in the sample household. See Nielsen Media Research, *Who We Are and What We Do*, (visited December 4, 1999) <<http://www.nielsenmedia.com>>. Nielsen does not, however, include information on television viewing that occurs in out-of-home locations in its ratings analysis to broadcasters or advertisers. Telephone interview with Vincent Nasso, Nielsen Media Research Communications Department (Sept. 30, 1999). It may, however, survey this out-of-home viewing data as part of its "total television measurement [report] to the industry."

were able to measure audience size accurately, the royalties attributable to secondary uses of broadcast music would still constitute an extremely small percentage of total broadcaster royalties.<sup>297</sup> Third, because royalties paid by non-commercial broadcasters are not tied to advertiser revenue and audience size, those license fees may not fully account for listening and viewing in business establishments.<sup>298</sup> Finally, the text and legislative history of the homestyle exemption and the FIMLA suggest that Congress did not consider royalties from broadcasters as an adequate substitute for royalties from commercial establishments.<sup>299</sup> To the contrary, both statutes permit PROs to

---

Press Release, *More Than 25 Million Adults Watch Television in Out-of-Home Locations Each Week*, May 14, 1998 (discussing the results of a study commissioned by ABC and ESPN showing significant out-of-home viewing of football telecasts). Thus, advertising revenues received by television broadcasters will not always reflect the audience of viewers in commercial establishments.

<sup>297</sup> In the case of radio broadcasts, for example, the limited data available suggest that significantly less than five percent of a station's total royalty payments to PROs result from secondary uses of music by commercial establishments. See Arbitron, *Radio Today: How America Listens to Radio* at 11 (1998 ed.) (concluding that between 1.2 percent and 4.9 percent of radio listening occurs in locations other than home, car or work). In the case of television broadcasts, a 1998 commissioned survey suggested that 10 percent of out-of-home viewing occurs in restaurants and bars, and 14 percent occurs in other places, including waiting rooms and hospitals. See Press Release, *supra* note 296, at 2.

<sup>298</sup> See MAGNUSSON & NABHAN, *supra* note 286, at 121; see also Joanne Court, *The Notional Bargain Approach to the Determination of Equitable Remuneration for Compulsory Licenses*, 11 SYDNEY L. REV. 348, 364-66 (1987) (asserting that, in Australia, performance licenses are issued to public television broadcasters based upon the broadcasters' operational expenditures).

<sup>299</sup> In 1961, the Register of Copyrights proposed to exempt the reception of broadcasts from the public performance right except where an admission fee was charged on the theory that "[t]he performing license obtained by the broadcaster should suffice, with no further license required of those who merely receive the broadcast." 1961 Register Report, *supra* note 134, at 31. The Register quickly abandoned this proposal in the face of criticism from PROs and substituted the homestyle exemption in its place. See *supra* Part II.B.2. Before the exemption could be enacted, however, the Supreme Court decided *Twentieth Century Music Corp. v. Aiken*, holding that PROs had "not demonstrated that they cannot receive from a broadcaster adequate royalties based upon the total size of the broadcaster's audience." 422 U.S. 151, 163 n.14 (1975). Congress' decision to overrule *Aiken*, endorse the multiple performance doctrine, and adopt only a narrow exemption for businesses using "homestyle" receivers, strongly suggests that it did *not* consider royalties from broadcasters to provide adequate compensation to copyright owners for secondary uses of broadcast music.

The FIMLA's legislative history contains discussions of broader versions of the double dipping rationale, see *supra* Part I.B.1, but does not contain any discussion of whether the narrower duplicative royalties from broadcasters discussed above would adequately compensate copyright owners for secondary performances. Congress evidenced its intent to permit duplicative recover in at least some situations, however, in the provision authorizing PROs to collect fees from all businesses who receive a "direct charge . . . to see or hear the

collect license fees from at least some businesses, suggesting that Congress believed that copyright owners deserved additional royalties.<sup>300</sup>

This analysis of double dipping does not foreclose the United States from creating a licensing system in which PROs collect royalties for secondary uses of broadcast music directly from radio, television and cable stations. As explained below, both Canada and Australia have considered adopting such a system. Both countries' proposals, however, would have expressly authorized copyright owners to collect a separate fee for secondary uses of broadcast music, in addition to the royalties already received from broadcasters themselves.<sup>301</sup> Neither the FIMLA nor the homestyle exemption contemplates such a licensing arrangement and the FIMLA may in fact preclude it.<sup>302</sup> In the absence of a designated revenue stream for in-store performances, WTO jurists will likely conclude that the limited duplicative royalties copyright owners currently receive do not justify characterizing the United States' music licensing legislation as a special case.

## 2) Abuse of Monopoly Power & Aggressive Licensing and Enforcement Tactics

Business establishments have raised two additional arguments in support of the current licensing exemption. First, they have argued that PROs in the United States have abused their monopoly power in various ways; second, they have contended that United States PROs have used inappropriate methods to force businesses to purchase licenses on unfair terms. The United States might use these allegations to argue that its music licensing laws satisfy the special case requirement in two ways. First, unlike the exploitation of many copyrighted works, the public performance right for music is licensed through collective organizations that require extensive regulation to prevent abuses of their monopoly pricing powers. Second, the repeated allegations of harassment leveled by business establishments against PROs are sufficiently severe to justify the differential treatment of PROs, including a licensing exemption for in-store performances.

The validity of these arguments under the Berne and TRIPs treaties is uncertain. On one hand, both the text and drafting history of the Berne

---

transmission or retransmission." 17 U.S.C. § 110(5)(B)(iii) (1999).

<sup>300</sup> See Philip Nichols, *Trade Without Values*, 90 *Nw. L. Rev.* 658, 714-18 (1996) (arguing that WTO jurists may properly examine legislative motives when reviewing domestic legislation).

<sup>301</sup> See *infra* Part III.F.2.d.

<sup>302</sup> The FIMLA provides that its exemptions "shall not be taken into account in any administrative, judicial, or other governmental proceeding to set or adjust the royalties payable to copyright owners for the public performance or display of their works." 17 U.S.C. § 110 (1999). This provision appears to prohibit PROs from petitioning the Rate Court to increase royalties from broadcasters to offset the loss of licensing revenues previously collected from commercial establishments.

Convention reflect member States' concern about collective rights organizations abusing their monopoly position, particularly with regard to the performance and broadcast rights. Thus, in debates over the proper interpretation of Berne Convention article 17,<sup>303</sup> a consensus position emerged that "controls over collecting societies or other abuses of authors' rights did not come into conflict with the provisions of the Convention," and that member States could "take all necessary measures to restrict possible abuses of monopoly."<sup>304</sup> Although governments adopted differing views on how far such controls could extend while remaining compatible with the treaty,<sup>305</sup> most agreed that any controls must genuinely target abusive monopolistic practices, "and not simply [be a] pretext for abridging rights which states are obliged to protect under the Convention."<sup>306</sup>

Thus, in order to determine whether the United States legislation is compatible with these principles, WTO jurists must distinguish between permissible and excessive monopoly regulation. The drafting history supports the United States' power to impose significant constraints on PRO licensing activities through methods such as the antitrust consent decree and oversight of the Rate Court.<sup>307</sup> It is equally clear that the United States and its political subdivisions are entitled to restrict the manner in which PROs interact with copyright users over license fees and enforcement practices.<sup>308</sup> Yet even if the

---

<sup>303</sup> Article 17 provides: "The provisions of this Convention cannot in any way affect the right of the Government of each country of the Union to permit, to control, or to prohibit, by legislation or regulation, the circulation, presentation, or exhibition of any work or production in regard to which the competent authority may find it necessary to exercise that right." Berne Convention, *supra* note 15, art. 17.

<sup>304</sup> RICKETSON, *supra* note 211, at 546, 548 (quoting Berne Convention's drafting history). See also STEWART, *supra* note 216, at 139 ("[T]here is also nothing [in Berne] to prevent countries from enacting measures designed to control monopolies and restrictive practices as a matter of public policy.").

<sup>305</sup> In particular, it is unclear whether governments are authorized to impose compulsory licenses in response to monopoly abuses where the Berne Convention does not already authorize them. Compare RICKETSON, *supra* note 211, at 548 (suggesting authorization), with 1978 WIPO Guide, *supra* note 210, ¶ 17.3 (denying authorization).

<sup>306</sup> RICKETSON, *supra* note 211, at 548. See also NORDEMANN ET AL, *supra* note 211, at 160-61 (arguing that the authority conferred on member States by article 17 to prevent monopoly abuses does not permit countries to expropriate authors' minimum rights in whole or in part).

<sup>307</sup> See STEWART, *supra* note 216, at 139 ("[T]here is nothing to prevent countries from enacting measures designed to control monopolies and restrictive practices as a matter of public policy. The establishment of copyright tribunals to adjudicate in cases of disputes between collecting societies formed by copyright owners which are virtual monopolies and users of copyright, also come under this heading.").

<sup>308</sup> See Noel L. Hillman, *Intractable Consent: A Legislative Solution to the Problem of the Aging Consent Decrees in United States v. ASCAP and United States v. BMI*, 8 FORDHAM I.P., MEDIA & ENT. L.J. 733, 758-60 (1998) (discussing enacted and proposed state laws regulating activities of PROs in relation to commercial establishments). FIMLA

allegations by commercial establishments that PROs have abused their monopoly powers are valid, the United States will have difficulty arguing that this abuse justifies an exemption of an entire category of public performances and transmissions rather than mere conduct regulation or price controls. Although the Berne and TRIPs treaties do not impose a least restrictive means test on member States, they do prevent States from eviscerating the treaties' minimum rights under the guise of monopoly regulation.<sup>309</sup>

## 2. Step Two—The “Normal Exploitation” Requirement

Even if WTO jurists conclude that the FIMLA and the homestyle exemption are special cases, they cannot rule in favor of the United States unless they conclude that the statutes do not “conflict with a normal exploitation of the work.”<sup>310</sup> Here, too, Berne's text and drafting history provide limited guidance and State practice suggests that the issue is largely “a matter for national legislation, and ultimately national tribunals, to determine.”<sup>311</sup>

### a. Arguments for the European Community

According to the EC, the United States licensing laws directly conflict with the normal exploitation of copyrighted music owned by its songwriters and publishers. The EC reasons that because the Berne Convention expressly grants to copyright owners a distinct right to control the secondary use of broadcast music, by definition “such right is regarded by all Members of the Union of Berne [including the United States] as being part of the normal exploitation of a copyright work.”<sup>312</sup> It then argues that “any kind of *commercial exploitation* of a musical work . . . should always be considered as part of ‘the normal exploitation of a work’ in the sense that commercial exploitation of a work should always entitle the rightholder to remuneration.”<sup>313</sup>

---

appears to approve of these laws; it provides that “nothing in this title shall be construed to relieve any performing rights society of any obligation under any State or local statute, ordinance or law . . . governing its operation . . .” 17 U.S.C. § 101 note (1999).

<sup>309</sup> TRIPs itself supports a similar conclusion, although it too is not free of ambiguity. Articles 8(2) and 40(2) authorize member states to adopt “appropriate measures” to prevent abuses of intellectual property rights. TRIPs, *supra* note 16, arts. 8(2), 40(2). However, they also specify that these restrictions must be “consistent” with the provisions of the treaty. *See id.*; *see also* Reichman, *supra* note 29, at 379-80 (emphasizing the lack of consensus over how these provisions should be applied).

<sup>310</sup> Berne Convention, *supra* note 15, art. 9(2); TRIPs, *supra* note 16, art. 13.

<sup>311</sup> RICKETSON, *supra* note 211, at 483.

<sup>312</sup> *Examination Procedure*, *supra* note 158, at 17.

<sup>313</sup> *Id.*

b. *Arguments for the United States*

These claims by the EC are remarkably broad. They suggest that copyright owners are entitled to enjoy virtually unfettered control over all commercial uses of their works. If adopted in full by the WTO dispute settlement bodies, the EC position would significantly alter the discretion member States have long enjoyed to decide whether an exception or limitation to an exclusive right is necessary to achieve a proper balance of interests between copyright owners and users.<sup>314</sup>

In addition, the drafting history of article 9(2) strongly suggests that the Berne Convention does not require such an expansive interpretation of the "normal exploitation" requirement. Although, as noted above, the drafters could not agree on how the requirement would be applied in all cases, they did agree on conduct that was beyond its outer margin: making a "very large number of copies for a particular purpose," or making "a rather large number of copies for use in industrial undertakings," where no equitable remuneration is paid.<sup>315</sup> Finding an appropriate analogy in the performance and broadcast setting for this undisputed violation of the reproduction right is not a simple task. It is not immediately obvious, however, that either the FIMLA or the homestyle exemption exceeds this outer boundary. If it does not, more than a century of state practice and commentary dictate that the United States be afforded some deference to fashion its copyright laws as it sees fit.<sup>316</sup>

Consequently, as with the special cases requirement, WTO jurists must consider additional arguments to analyze the "normal exploitation" requirement persuasively. The EC has suggested two such arguments. Both are more narrowly tailored than the EC's principal argument and thus provide more persuasive challenges to the United States laws.

---

<sup>314</sup> In its initial WTO brief, the United States stresses the importance of this discretion. See *First U.S. Submission*, *supra* note 7, at 13 ("WTO Members have flexibility to determine for themselves whether a particular case represents an appropriate basis for an exception to exclusive rights.").

<sup>315</sup> See RICKETSON, *supra* note 211, at 483-84. See also Ruth L. Gana, *Prospects For Developing Countries Under The TRIPs Agreement*, 29 VAND. J. TRANSNAT'L L. 735, 760 (1996) ("Historical notes on the interpretation of Article 9(2) . . . suggest that conflict with 'normal exploitation' refers to such things as massive amounts of photocopying, particularly where it is done for industrial or economic gain."); Paul Edward Geller, *Legal Transplants in International Copyright: Some Problems of Method*, 13 UCLA PAC. BASIN L.J. 199, 215 (1994) (remarking that the meaning of cumulative tests in article 9(2) "remains unclear, except that together they would preclude large-scale copying without compensation").

<sup>316</sup> See RICKETSON, *supra* note 211, at 487 ("The decision of the [drafters] to delete any list of permissible purposes leaves a considerable area of discretion to national legislation. While this means that there will be divergences between national laws on these matters, it has the considerable advantage that each country is able to take into account its own particular needs."); Heide, *supra* note 229, at 105 (stating that article 9(2) "did not present Berne Union states with a solution and left it to each country to resolve the matter as it wished subject to the guideline language of that Article").

c. *Normal Exploitation Defined by Market Failure*

WTO jurists may attempt to decide which exploitations of copyrighted works are “normal” by analyzing PROs’ voluntary licensing practices.<sup>317</sup> Even where copyright statutes create broad exclusive rights, copyright owners may choose not to exercise those rights to their fullest extent because the transaction costs associated with licensing exceed the revenues generated by the licenses.<sup>318</sup> This situation will prevent users from purchasing a license, thereby precluding productive uses of copyrighted works. Faced with such failures in the licensing market, the economic efficiency approach discussed in Part I provides a compelling justification for national legislatures to create free use exemptions for copyright users.<sup>319</sup>

The history of secondary uses of broadcast music in the United States reveals that transaction costs have shaped the licensing practices of PROs, causing them to refrain voluntarily from licensing certain secondary uses of broadcast music even where those uses provide a financial benefit to commercial establishments. That history also demonstrates, however, that users not included in this voluntary practice have resisted paying licensing fees, both in interactions with PROs and in rent seeking before Congress and

---

<sup>317</sup> The United States’ WTO brief advocates this approach. *First U.S. Submission, supra* note 7, at 14 (“To determine what constitutes normal exploitation, the Panel must look at all the ways in which an author might reasonably be expected to exploit his work in the normal course of events.”) (quotations omitted).

<sup>318</sup> See *supra* Part I.A (discussing transactions costs as causes of market failures). Compare RICKETSON, *supra* note 211, at 483 (advocating an interpretation of normal exploitation which suggests a market failure approach), with Paul Edward Geller, *Reprography and Other Processes of Mass Use*, 38 J. COPYRIGHT SOC’Y U.S.A. 21, 23-31 (1990) [hereinafter Geller, *Reprography*] (arguing that mass uses of copyrighted works outside of functioning markets must be considered in determining normal exploitation).

<sup>319</sup> See *First U.S. Submission, supra* note 7, at 14 (“To determine what constitutes normal exploitation, the Panel must look at ‘all the ways in which an author might reasonably be expected to exploit his work in the normal course of events.’”) (quoting RICKETSON, *supra* note 211, at 483).

This is not to suggest that a market failure approach is the only or even the preferred method of analyzing whether national copyright law exemptions are compatible with Berne and TRIPs. To the contrary, statutory provisions that place “limits on the scope of copyright protection play a valuable role in promoting the progress of knowledge and the creative arts” distinct from their use in correcting market failures. See Cohen, *supra* note 57, at 239; see also Helfer, *supra* note 29, at 432-33 (explaining important social values many national law exceptions and limitations serve). It is difficult, however, for the United States to argue that the music licensing exemption promotes these objectives. Most commercial establishments who use broadcast music do so to enhance the ambience of their businesses, promote sales or increase the productivity of their employee. They do not use music to advance public discourse, or disseminate culture or ideas to the public, still less to create new copyrighted works of value to society. See *supra* note 283 (characterizing exemptions as a product of interest group politics). Thus, any such instrumental arguments the United States asserts to defend the laws are unlikely to persuade WTO jurists.

the courts. This resistance has increased the transactions costs of music licensing and, in part, explains congressional decisions in 1976 and 1998 to codify broader exemptions than the PROs' voluntary licensing forbearances dictated. For both the homestyle exemption and the FIMLA, therefore, Congress' action overcorrected the market failure, cut off a stream of royalties that PROs had been collecting (or at least actively seeking to collect) immediately prior to the statutes' adoptions, and encouraged users to engage in fresh acts of resistance to PRO licensing efforts.

The EC emphasizes many of these points. It acknowledges that market failures may justify free use exemptions to the public performance and broadcast rights, but it also identifies in-store performances that PROs had licensed prior to the statutes' enactments, including retail chain stores and private agreements with user industry associations such as the NLBA.<sup>320</sup> The EC further asserts that the exemptions have increased user resistance, thereby diminishing PRO incentives to seek licenses even from businesses outside the exemptions' scope.<sup>321</sup>

In response, the United States argues that PROs have no reasonable expectation of collecting license fees for in-store performances encompassed within the homestyle exemption and the FIMLA.<sup>322</sup> It asserts that the homestyle exemption "codif[ie]d licensing practices already in effect by the right holders and their licensing organizations," whereas the FIMLA merely enacted an exemption scheme that PROs had already accepted as part of the NLBA agreement.<sup>323</sup> The United States concludes that although the FIMLA may be marginally broader than the homestyle exemption and the NLBA agreement combined, "this minor limitation on some secondary uses of broadcasts to the public simply does not rise to the level of a conflict with normal exploitation."<sup>324</sup>

The flaw in the United States' argument is twofold. First, the United States mischaracterizes the scope of the homestyle exemption and the NLBA agreement. For example, the NLBA agreement is only available to its members; businesses that do not sell alcohol on their premises are ineligible to join.<sup>325</sup> Second, the United States' attempt to rely on a market failure theory is

---

<sup>320</sup> See *Examination Procedure*, *supra* note 158, at 15-16.

<sup>321</sup> See *id.* at 30 ("United States collecting societies encounter strong resistance when attempting to license small to medium size premises which do not benefit from the exemption, and particularly those which only marginally fail to meet the applicability criteria of Section 110(5).").

<sup>322</sup> See *First U.S. Submission*, *supra* note 7, at 15.

<sup>323</sup> *Id.* at 15, 16.

<sup>324</sup> *Id.* at 16.

<sup>325</sup> See *National Licensing Beverage Association*, (visited Dec. 4, 1999) <<http://nlba.org>> (NLBA represents over 16,000 bar, tavern, restaurant and package store owners); *First U.S. Submission*, *supra* note 7, at 7 n.17 (conceding in introductory section of brief that "an establishment must sell alcohol on its premises" to be an NLBA member).

unpersuasive. Although the economic efficiency approach to copyright regulation justifies creating free use exemptions to correct market failures, that justification is markedly weakened where user resistance and rent seeking are among the transaction costs creating those failures. In the United States, resistance and rent seeking have caused the legislature to exempt uses that were previously part of copyright owners' licensing market, thereby diminishing their royalties.<sup>326</sup> For this reason, WTO jurists are likely to rule in favor of the EC if they adopt a market failure approach to the "normal exploitation" step of the three-step test.

d. *Normal Exploitation Measured by Other Copyright Statutes*

A second method of determining whether the United States laws infringe a normal exploitation of copyrighted music is to compare the FIMLA and the homestyle exemption to the laws of other State parties to the Berne and TRIPs treaties. Accepted principles of treaty construction authorize using a comparative law approach focusing on the "State practice" of the signatories to supplement textual, purposive and other interpretive methodologies.<sup>327</sup> A comparative law analysis of national copyright statutes also enables WTO jurists to provide a specific contextual framework against which to measure United States laws, thereby providing further support for their rulings.<sup>328</sup>

*The European Community.* The EC recognizes the importance of comparative analysis. It asserts that none of its fifteen member states have

---

Relying on the NLBA agreement is also flawed because it was negotiated in the shadow of the Fairness in Music Licensing Act of 1997, a bill that contained a blanket exemption for secondary uses of broadcast music clearly incompatible with Berne and TRIPs. *See supra* Part II.B.5.b.1). For a discussion of the treaty-compatibility of private licensing agreements, *see infra* Part IV.C.2.

<sup>326</sup> The diminution of royalties will increase to the extent that commercial establishments substitute free broadcast music for licensed background music services or the performance of recorded music. *Compare 1997 Hearings, supra* note 19, at 18 (testimony of Marybeth Peters, Register of Copyrights, expressing this concern), *with supra* note 295 (contending that the extent of substitution, if any, is difficult to predict).

<sup>327</sup> *See* Vienna Convention, *supra* note 202, arts. 31, 32; IAN SINCLAIR, *THE VIENNA CONVENTION ON THE LAW OF TREATIES* 137-38 (2d ed. 1984).

<sup>328</sup> The national copyright laws of Berne member States and the judicial decisions interpreting them which preceded the entry into force of the TRIPs Agreement serve as an important interpretive guideposts for WTO jurists in interpreting TRIPs. *See* Frederick M. Abbott, *WTO Dispute Settlement and the Agreement on Trade-Related Aspects of Intellectual Property Rights*, in *INTERNATIONAL TRADE LAW AND THE GATT/WTO DISPUTE SETTLEMENT SYSTEM* 415, 421 (1997); Netanel, *The Next Round, supra* note 32, at 447. Legislative changes and judicial decisions by TRIPs member States that post-date the Agreement's entry into force are a form of State practice long recognized as an aid to treaty interpretation. *See* Helfer, *supra* note 29, at 426-31 (collecting authorities on treaty interpretation and explaining in detail ways in which WTO dispute settlement jurists can use national laws to assist in interpretation of the TRIPs Agreement).

enacted exemptions similar to those found in the United States, nor have they exercised their discretion under the Berne Convention to create a compulsory licensing system for the secondary use of broadcast music.<sup>329</sup> The EC also claims that the copyright laws of Australia, Canada, New Zealand and Brazil do not contain provisions similar to the homestyle exemption.<sup>330</sup> In fact, the legal situation is more complex.

*Australia.* By far the most revealing national copyright system against which to compare the United States statutes is found in Australia. In June 1998, the Australian Federal Parliament published a detailed study and recommendations devoted to the question of whether small business should be required to pay copyright royalties for playing music in their establishments.<sup>331</sup> The study was initiated at the urging of the Attorney General of Australia in July 1997 after the Australian Performing Rights Association ("APRA") stepped up efforts to collect royalties from small businesses. The Australian Copyright Act of 1968 grants copyright owners the exclusive right to perform their musical works publicly,<sup>332</sup> but it was not until the mid-1990s that APRA began a national compliance campaign that actively sought to license secondary uses of broadcast music.<sup>333</sup> Small business owners stridently objected to these licensing efforts, and asked the government to examine whether the APRA was authorized to collect such fees.<sup>334</sup>

---

<sup>329</sup> See *Examination Procedure*, *supra* note 158, at 17, n.31. See also Lionel Bently, *United Kingdom*, in *INT'L COPYRIGHT LAW*, *supra* note 227; Alberto Berovitz & German Berovitz, *Spain*, in *INT'L COPYRIGHT LAW*, *supra* note 227; Adolf Dietz, *Germany*, in *INT'L COPYRIGHT LAW*, *supra* note 227; Mario Fabiani, *Italy*, in *INT'L COPYRIGHT LAW*, *supra* note 227; Herman Cohen Jehoram, *The Netherlands*, in *INT'L COPYRIGHT LAW*, *supra* note 227; Gunnar Karnell, *Sweden*, in *INT'L COPYRIGHT LAW*, *supra* note 227; Georges Koumantos, *Greece*, in *INT'L COPYRIGHT LAW*, *supra* note 227; André Lucas & Robert Plaisant, *France*, in *INT'L COPYRIGHT LAW*, *supra* note 227; Alain Strowel & Jan Corbet, *Belgium*, in *INT'L COPYRIGHT LAW*, *supra* note 227.

<sup>330</sup> See *Examination Procedure*, *supra* note 158, at 17-18, n.32

<sup>331</sup> See House of Representatives Standing Committee on Legal & Const. Affairs, *Don't Stop the Music! A report of the inquiry into copyright, music and small business* (June 1, 1998) <<http://www.aph.gov.au/house/committee/LACA/Inquiryincopy.htm>> [hereinafter *Don't Stop the Music*].

<sup>332</sup> See *id.* at 13-15. (discussing Copyright Act framework). The Australian Copyright Act does not define which performances are public. However, judicial decisions have established a very broad definition of 'public.' See *id.* at 16 ("[T]he case law has established that if music is played in the presence of more than one person other than in private or domestic circumstances, it is likely that it will constitute a public performance.").

<sup>333</sup> The campaign involved a shift in APRA's licensing practices from personal meetings with individual business owners to a national "telemarketing campaign." Under the old enforcement regime, transaction costs precluded APRA from seeking licenses from small businesses. See *id.* at 30 ("Pursuing multiple businesses was costly and time consuming and the license fees for background music were not high.").

<sup>334</sup> See *id.* at 32 (describing reaction to enhanced compliance efforts as "one of confusion, disbelief and outrage").

The study examined a number of salient issues relating to the dispute between music copyright owners and small businesses. These included the fee structure of the licenses collected, the distinctions between broadcast and recorded music, the purposes for which small businesses use music, and the legal, economic and distributional arguments in favor of creating some form of exemption for small businesses. The study also analyzed the compatibility of a range of licensing exemptions with Australia's obligations under the Berne Convention and TRIPs.<sup>335</sup>

As an initial matter, the report noted a significant distinction between performances designed to provide an "ambience or mood" for customers and those intended for employees. As to the first type of performance, many business representatives who testified before the Parliamentary Committee accepted that licensing fees were reasonable given the "commercial nature for which the music is being used in these sort of situations."<sup>336</sup> They objected only to requiring a license fee when music was used to entertain employees and indirectly raise their productivity.<sup>337</sup>

Other business owners, however, asserted that they should not be required to pay any license fees for playing music in their establishments.<sup>338</sup> The Parliamentary Committee categorically rejected their argument, reasoning that a "blanket exemption for small businesses would mean that those businesses using music in a manifestly commercial manner would be exempt from paying license fees."<sup>339</sup> "It is highly likely that Australia would be in breach of its obligations under TRIPs and the Berne Convention if the Copyright Act was amended to prove an exemption for small business. Such an exemption would not fall within any of the exceptions contemplated by the treaties."<sup>340</sup>

The Committee considered in some detail the possibility of exempting businesses from paying license fees for broadcast music and instead shifting liability for those fees to radio and television broadcasters. The report made clear that this licensing system would require broadcasters to pay royalties "in

---

<sup>335</sup> See *id.* at 43-94.

<sup>336</sup> *Id.* at 49.

<sup>337</sup> See *id.* at 49-50 (giving examples of worker productivity and use of music).

<sup>338</sup> See *id.* at 66-68. (comparing United States, Canadian and Japanese rules). In part, this argument was premised on the claim that copyright owners seeking to license in-store performances of broadcast music were "double dipping" for license fees. The Committee noted both sides of this argument but did not evaluate its merits. See *id.* at 59-60.

<sup>339</sup> *Id.* at 61.

<sup>340</sup> *Id.* at 60. In support of this conclusion, the report cited the testimony of two law professors, Warwick Rothnie and James Lahore, who argued that "blanket exemptions covering a broad sector of the economy would probably be too broad to satisfy the 'special cases' requirement" of Berne article 9(2) and TRIPs article 13. The report also noted, without analysis, their views that any such exemption "in a commercial context" would conflict with the remaining two steps of the three-step test. See *id.* at 23. It is uncertain, however, whether these statements refer to a blanket exemption covering the performance of both broadcast and recorded music, or whether they are directed at broadcast music alone.

addition” to those currently collected by the APRA.<sup>341</sup> Both business and copyright owners endorsed such a proposal as having practical advantages over the collection of separate royalties from business owners.<sup>342</sup> Not surprisingly, the broadcasting industry strongly opposed this proposal.<sup>343</sup>

Although the Committee found the broadcaster licensing proposal superficially appealing, it ultimately rejected it on the ground that “there are significant legal, practical and philosophical barriers to its implementation that would be difficult to overcome.”<sup>344</sup> In particular, the Committee reasoned that “if anyone is to be paying license fees for public performance[s], it should be the person who is causing the public performance rather than a third party.”<sup>345</sup> The Committee concluded that the proposal would violate neither Berne nor TRIPs,<sup>346</sup> provided that music copyright owners received an additional royalty from broadcasters.<sup>347</sup>

---

<sup>341</sup> The APRA estimated that it collected approximately two million Australian dollars annually from the playing of radios and televisions, with the royalties divided equally among each media. *See id.* at 71-72. It also estimated that adding one million dollars to the fees currently paid by broadcasters would increase their licensing rates by seven to eight percent. *See id.*

<sup>342</sup> *See id.* at 71. Although the report does not discuss these advantages, they clearly include significant transaction cost savings for copyright owners. The proposed licensing system would no longer require APRA to engage in the time-consuming and expensive process of collecting royalties from the thousands of individual businesses throughout Australia.

<sup>343</sup> Commercial stations objected that they would not necessarily be able to pass on the royalties to their advertisers given the competitive market for advertising; community and public broadcasters argued that they would not be able to absorb the costs without additional government or public funding. Both groups argued that it would be “impossible to establish a fair method of setting an amount for collection and then dividing this amount amongst different broadcasters.” *Id.* at 77. Finally, they asserted that it would be unfair to expect either broadcasters or advertisers to pay for a commercial benefit received by small businesses who performed broadcast music for their customers or employees. *See id.* at 76-78.

<sup>344</sup> *Id.* at 93. The most significant legal barrier addressed was the likelihood that the proposed licensing system would create an unconstitutional tax on broadcasters. *See id.* at 80-83.

<sup>345</sup> *Id.* at 93.

<sup>346</sup> Canadian copyright law contains a broadcaster licensing system similar to that proposed by the ARPA. However, Canadian PROs do not currently receive license fees for the performances of music by commercial establishments. *See infra* text accompanying notes 363-65. The Committee’s report suggested that the Canadian law violates TRIPs. *See Don’t Stop the Music, supra* note 331, at 83.

<sup>347</sup> The Committee cited the views of professors Rothnie and Lahore, who argued that Article 11*bis* of the Berne Convention requires only that copyright owners be paid equitable remuneration for the secondary use of broadcast music; “[i]t does not stipulate that the person making the payment must be the person responsible for bringing about the public performance.” *Id.* at 83. However, the professors cautioned that a treaty breach was likely

The report considered two other proposals, one of which it adopted. The first proposal involved modifying the Copyright Act to define “public performance” in a way that excluded certain performances on business premises from music copyright owners’ licensing powers. The Committee rejected this proposal on the ground that the Berne Convention did not provide sufficient discretion for Australia to introduce such a “restrictive definition of public performance.”<sup>348</sup> The Committee also feared that the EC would challenge such a definition before the WTO.<sup>349</sup>

In its third and final proposal, the Committee urged the APRA to voluntarily issue complimentary licenses to small businesses whose employees play broadcast music. Although the Committee acknowledged that these businesses might gain some indirect financial benefit from this exemption, it considered that benefit too remote when weighed against the “compelling practical and philosophical arguments in favour of relaxing the licensing requirements.”<sup>350</sup> After consultation with the Committee, the APRA agreed to issue such complimentary licenses provided that: (1) the performance occurred by radio or television set; (2) the business employed fewer than twenty people and (3) the music was not intended to be heard by customers of the business or by the general public.<sup>351</sup> The third requirement is satisfied only if “neither the radio or television set nor any speakers are located in an area that is accessible to customers or the general public and any performance inadvertently heard by customers or the general public is manifestly unintentional.”<sup>352</sup>

The Committee hailed this solution as a compromise that alleviated the concerns of many small businesses while complying with Australia’s international obligations.<sup>353</sup> It also asserted that music copyright owners’ interests were protected, inasmuch as the APRA had already voluntarily refrained from seeking royalties from many small businesses using music in this way.<sup>354</sup> Finally, the Committee stated that it would monitor this

---

if Parliament created an exemption for small businesses without ensuring that copyright owners collected additional license fees from broadcasters. *See id.* The Attorney-General concurred in this view, stating that “there would need to be appropriate mechanisms in place to ensure that copyright owners were in fact equitably remunerated by broadcasters for the public performance of their works.” *Id.* at 84.

<sup>348</sup> *Id.* at 85.

<sup>349</sup> The report noted the EC’s reference to the legal situation in Australia as “the most important matter for concern, since there is a serious risk that this country may introduce legislation inspired by section 110(5) of the United States Copyright Act.” *See id.* at 88 (citing *Examination Procedure*, *supra* note 158, at 33).

<sup>350</sup> *Id.* at 68.

<sup>351</sup> *See id.* at 91.

<sup>352</sup> *Id.* Several examples contained in the report make clear that the complimentary license would be granted even if a radio or television set was located “behind the counter” where it could incidentally be heard by customers. *See id.* at 91-93.

<sup>353</sup> *See id.* at 10.

<sup>354</sup> *See id.* at 53, 68-69.

complementary licensing system and reserve the right to introduce a legislative solution if the policy did not succeed.<sup>355</sup>

Developments in Australia are highly favorable to the EC's complaint against the United States. Facing a situation remarkably similar to that which existed in the United States during the same time period, the Australian government compromised the competing interests of the businesses and music copyright industries by urging the adoption of a voluntary licensing system far narrower than either the FIMLA or the homestyle exemption. It also asserted that a broader exemption would violate international copyright norms.

*Canada.* The situation in Canada is somewhat more favorable to the United States. In 1938, the Canadian Parliament exempted businesses from paying royalties for broadcast and recorded music in response to a public perception that PROs were abusing their licensing powers.<sup>356</sup> At that time, courts in several Berne member States, including those in Europe, did not consider the reception of a radio broadcast as a public performance.<sup>357</sup> However, at least one Canadian court had concluded that such a reception was a public performance,<sup>358</sup> which motivated the Parliament explicitly to exempt such performances in the following language:

In respect of public performances by means of any radio receiving set or gramophone<sup>359</sup> in any place other than a theatre that is ordinarily and regularly used for entertainments to which an admission charge is made, no royalties shall be collectable from the owner or user of the radio receiving set, but the Copyright Appeal Board shall, in so far as possible, provide for the collection in advance from radio broadcasting stations or gramophone manufacturers, as the case may be, of fees, charges and royalties appropriate to the conditions produced by the provisions of this subsection and shall fix the amount of the same; in doing so the Board shall take into account all expenses of collection and other outlays, if any,

---

<sup>355</sup> See *id.* at 94. In commentary on the report, the Attorney General characterized the report as "a win-win outcome" for small businesses and music copyright owners. See Attorney General News Release, *Report on Playing Music in Small Businesses* (visited June 1, 1998) <[http://law.gov.au/aghome/agnews/1998newsag/424\\_98.htm](http://law.gov.au/aghome/agnews/1998newsag/424_98.htm)>.

<sup>356</sup> See MAGNUSSON & NABHAN, *supra* note 286, at 123 & 133 n.42 (noting that Canada adopted the exemption because of "a widespread public perception of unfairness and unreasonableness"); see also *Don't Stop the Music*, *supra* note 331, at 72 (noting this rationale when analyzing Canadian Copyright Act as possible precedent for revisions to Australian copyright law).

<sup>357</sup> See MAGNUSSON & NABHAN, *supra* note 286, at 132 n.33, 136 n.63

<sup>358</sup> See *Canadian Performing Rights Society v. Ford Hotel*, [1935] 2 D.L.R. 391, 396-97 (holding that the defendant had infringed the plaintiff's copyright by allowing songs to be performed without the plaintiff's consent).

<sup>359</sup> In 1993, the Parliament eliminated the exemption's application to performances by gramophone to comply with Canada's obligations under the North American Free Trade Agreement. See *An Act to Implement the North American Free Trade Agreement*, R.S.C., ch. 44, §73 (1993) (Can.).

saved or savable by, for or on behalf of the owner of the copyright or performing right concerned or his agents, in consequence this subsection.<sup>360</sup>

Several features of this law are noteworthy. First, the exemption applies to businesses using broadcast music for expressly commercial purposes, including business who collect a direct charge from customers to hear the broadcast. Second, judicial decisions have construed the statute to apply even to “fairly elaborate installations of . . . radio receiving equipment involving multiple speakers.”<sup>361</sup> Third, these judicial decisions have also characterized the exemption as “absolute, unqualified and unconditional” in making the public performances it embraces lawful and non-infringing.<sup>362</sup>

The last requirement is particularly significant given the way in which Canada has implemented the exemption. After the statute was adopted in 1938, the Canadian Copyright Board attempted to implement the new law by setting a tariff for broadcasters that took into account secondary uses of broadcast music. The Board had considerable difficulty in fixing an appropriate fee, however, in part because of a lack of information concerning the number of exempted radio receiving sets used by businesses across Canada.<sup>363</sup> Between 1939 and 1941, the Board authorized the Canadian Performing Rights Society to collect \$1000 per year from broadcasters, but for reasons that commentators have not been able to ascertain, the Society abandoned collection of that fee shortly thereafter.<sup>364</sup> No royalties have been paid to music copyright owners under this section of the statute since 1957 at the latest.<sup>365</sup>

In the years since the exemption was first enacted, several government and expert reports have analyzed this statute. In a 1957 study, a government commission recommended that the exemption be retained, arguing that it protected performances of radio broadcasts that “are essentially private” even if members of the public incidentally hear them.<sup>366</sup> Subsequent reports were

---

<sup>360</sup> See Canadian Copyright Act, § 50(7) (emphasis added), reprinted in A.A. Keyes & C. Brunet, *Copyright in Canada: Proposals for a Revision of the Law* 157 (1977). In 1985, section 50(7) was renumbered as section 69(2). See R.S.C., ch. C-42, § 69(2) (1985) (Can.); R.S.C., c. 10 (1985) (4th Supp.) (Can.).

<sup>361</sup> MAGNUSON & NABHAN, *supra* note 286, at 117-18 & n.9. The exemption does not, however, apply to “wired music systems” such as Muzak. See *id.* at 118.

<sup>362</sup> See, e.g., *Vigneux v. Canadian Performing Rights Society*, [1945] 2 D.L.R. 1, 10 (P.C.) (holding that no fee should be collected from owners of radios).

<sup>363</sup> See *Don't Stop the Music*, *supra* note 331, at 75 (quoting 1939 decision by Canadian Copyright Board).

<sup>364</sup> See *id.*

<sup>365</sup> See *id.* at 74 (stating this result based on inquiry to Canadian Copyright Board); see also Keyes & Brunet, *supra* note 360, at 160.

<sup>366</sup> *Royal Commission on Patents, Copyrights, Trademarks, and Industrial Design, Report on Copyright* 29 (1957).

far more critical, however. For example, a 1977 study, after stating that the law deprived copyright owners of any remuneration for in-store performances and was inconsistent with the Berne Convention's principles, recommended that the exemption be limited to business with three or fewer employees.<sup>367</sup>

A 1982 study provided the most detailed critique of the statute. The study found that the "double dipping" argument would have "considerable logical force" if evidence showed that license fees collected from broadcasters accurately correlated to the size of the listening audience. The study noted, however, that audience measurement services may not accurately account for the audiences tuned to in-store performances, that in-store audiences "may not be regarded as very valuable to advertisers" and that the performance royalties collected from non-commercial broadcasting may not be calculated based on audience size.<sup>368</sup>

Without resolving these empirical questions, the study noted a distributional objection to the double dipping argument. Even assuming that the royalties paid by radio broadcasters accurately reflect the size of the listening audience, the burden of those royalties do not fall on those who exploit them. For this reason, a "fairer system" would permit representatives of music copyright owners to receive royalties from broadcasters only for "private and domestic use" and collect a second set of royalties from commercial establishments.<sup>369</sup>

With respect to market failures, the study reasoned that although the cost of collecting license fees for in-store performances was high, PROs would seek such fees even from small businesses whenever they could obtain any net increase in revenue above those costs. However, the study questioned whether it was "in the public interest that scarce resources be squandered in the collection of these fees" and that some exemption might therefore be justified "to prevent [such] waste from occurring."<sup>370</sup>

Based on these considerations, the 1982 report encouraged the Canadian Parliament to adopt a statute similar to the United States homestyle exemption. The proposed law would apply only if the performances were "directed primarily at the proprietors, operators and employees" of the establishment using home-type audio or video receivers and were not further transmitted to the public.<sup>371</sup> Nor would the law exempt performances used directly or indirectly to enhance the profitability of a business.<sup>372</sup> However, the proposal

---

<sup>367</sup> See Keyes & Brunet, *supra* note 360, at 161 (suggesting that Canada is in violation of the treaty). In 1998, the Australian House of Representatives Standing Committee also suggested this conclusion. See *Don't Stop the Music*, *supra* note 331, at 75-76 ("With no royalties currently being paid for the public performance of music played on the radio, there is an issue as to whether Canada is fulfilling its obligations under TRIPs.").

<sup>368</sup> MAGNUSSON & NABHAN, *supra* note 286, at 120-21.

<sup>369</sup> *Id.* at 121.

<sup>370</sup> *Id.* at 122.

<sup>371</sup> *Id.* at 128.

<sup>372</sup> See *id.* (explaining that the exemption would be vitiated if the business charged a fee

did not limit the type of copyrighted works eligible for the exemption and, unlike the United States homestyle exemption, it applied to in-store performances of audio and video tapes.<sup>373</sup> According to the authors, this narrower exemption would not violate Canada's obligations under the Berne Convention.<sup>374</sup>

The final attempt to repeal section 69(2) occurred in 1993 and was defeated in a legislative committee.<sup>375</sup> As a result, Canadian copyright law currently contains an exemption for broadcast music far broader than that created by either the FIMLA or the homestyle exemption. As the foregoing discussion reveals, however, not only is the exemption not operating as originally intended, but studies have encouraged its restriction or elimination, and some commentators have characterized the statute as being in violation of both the Berne Convention and TRIPs.<sup>376</sup>

*Japan.* Japan maintains its own version of the homestyle exemption.<sup>377</sup> Article 38(3) of the Copyright Act of 1970 provides that:

It shall be permissible to communicate publicly, by means of a receiving apparatus, a work already broadcast or diffused by wire, for non-profit-making purposes and without charging any fees to audience or spectators. The same shall apply to such public communication made by means of a receiving apparatus of a kind commonly used in private homes.<sup>378</sup>

---

for or advertised the performance to the public).

<sup>373</sup> See *id.* at 124-25.

<sup>374</sup> See *id.* at 126-27. However, the authors addressed the compatibility issue under the 1928 Rome version of the Berne Convention. As noted above, the distinct right to communicate a work to the public by loudspeaker set forth in article 11*bis*(1)(iii) was not adopted by Berne member states until the Brussels revision of the Convention in 1948. See *supra* Part III.B. Canada did not become a party to this more recent version of the treaty until 1994. See David Vaver, *Canada* §1[2], in 1 INT'L COPYRIGHT LAW, *supra* note 227, at CAN-11. Thus, Canada enjoyed far greater leeway to adopt exemptions for the secondary use of broadcast music. See *id.*

<sup>375</sup> See Section 6, Bill C-88, An Act to Amend the Copyright Act, Third Sess. 34th Parl., 40-42 Eliz. II (1993). In addition, a 1984 government study outlined a variety of options for modifying the exemption, but did not recommend one of these for adoption by Parliament. See Judy Erola & Francis Fox, *From Gutenberg to Telidon, A White Paper on Copyright* 47-48 (1984).

<sup>376</sup> See MAGNUSSON & NABHAN, *supra* note 286, at 126-27; *Don't Stop the Music*, *supra* note 331, at 83-84.

<sup>377</sup> Japan has been a Berne member since 1899. However, it did not ratify the 1948 Brussels Act or the 1971 Paris Act of the Convention until after the enactment of its 1970 copyright law. Japan has also been a WTO and TRIPs member since 1995. See Teruo Doi, *Japan* §§ 1[1] & 1[2], in INT'L COPYRIGHT LAW, *supra* note 227, at JAP-5-8.

<sup>378</sup> MINPO, article 38(3), Law No. 48 (Japan) (as amended May 6, 1970) *translation available at* (visited Dec. 4, 1999) <[http://www.cric.or.jp/cric\\_e/ecolj/cl.html](http://www.cric.or.jp/cric_e/ecolj/cl.html)> (defining "fees" as including "any kind of charge to be imposed on the offering and the making available of a work to the public").

The second sentence of article 38(3) does not make clear whether it exempts all public communications by homestyle receivers or only those communications which are not carried out for profit. Furthermore, there are apparently no judicial decisions interpreting the statute's scope.<sup>379</sup> However, other provisions of the Copyright Act, including a provision exempting certain public performances of *recorded music* from a copyright owner's control, suggest by analogy that at least some secondary uses of broadcast music carried out for profit are exempted by section 38(3).<sup>380</sup> Further, in a statement relevant to the "normal exploitation" issue, one article recently noted efforts by Japanese courts to counteract "the still widespread attitude in Japan that copyright infringements by public performances of music are an elegant and negligible offence, if at all."<sup>381</sup>

*Other nations.* Research for this Article has not disclosed any other exemptions in the national copyright laws of other signatories to the Berne and TRIPs treaties. To the contrary, several national laws or judicial decisions expressly grant to copyright owners the right to control secondary uses of broadcast music.<sup>382</sup>

---

<sup>379</sup> See Doi, *supra* note 377, § 8[2][-b][v], at JAP-58. Reports from Australia and the United States conclude that Japan maintains a homestyle exemption closely analogous to that found in the United States. See *Don't Stop the Music*, *supra* note 331, at 67 (noting that Japan's exemption is broader than Australia's); Final Report, *supra* note 207, at 529.

<sup>380</sup> A supplementary provision of Japanese copyright law exempts "the public performance of musical works by the use of sound recordings made lawfully, other than those given by public transmission, and those given by enterprises which use such recordings for the purpose of profit-making and which are defined by Cabinet Order." Transitory Provisions, Article 14 (1969) (emphasis added), *translation available at* (visited Dec. 4, 1999) <[http://www.cric.or.jp/cric\\_e/ecolj/clsp.html](http://www.cric.or.jp/cric_e/ecolj/clsp.html)>. According to the Cabinet Order referred to in Article 14, the following establishments are *not* exempt from paying performance license fees for recorded music: "(i) coffee shops and restaurants which publicize by any means that they offer music to customers, or which are provided with special equipments for offering music to customers; (ii) cabarets, nightclubs, dance halls and other similar establishments with dance floors for customers; (iii) enterprises giving public entertainments accompanied with music, such as theatrical performances, variety shows and stage dances." Cabinet Order No. 335 (December 10, 1970), *translation available at* (visited Dec. 4, 1999) <[http://www.cric.or.jp/cric\\_e/ecolj/clold.html#clold+1\\_3](http://www.cric.or.jp/cric_e/ecolj/clold.html#clold+1_3)>. The net effect of these interlocking provisions is that "ordinary public establishments, such as hotels, coffee shops, and pinball parlors, may freely provide recorded background music if they fall outside these general and specific categories." Doi, *supra* note 377, § 8[2][a][iv], at JAP-57. Article 38(3)'s application to broadcast music in stores appears at least as broad.

<sup>381</sup> *Decisions: Copyright and Design Law: Japan: "Karaoke Snak Bar II,"* 30 IIC 467, 469 (1999) [hereinafter "Karaoke Snak Bar"].

<sup>382</sup> See, e.g., Dietz, *supra* note 329, at GER-108 (citing the German constitutional guarantee of property and the corresponding mandate of compensation for the author in situations involving "the continuous performance of music" in public places); Lucas & Plaisant, *supra* note 329, at FRA-123-24 (requiring payment to the author for performance of copyrighted works in all instances except performances within the family circle); see also

*Summary and Evaluation.* The overwhelming majority of the 135 TRIPs member States and 140 Berne signatories do not exempt the secondary use of broadcast music from copyright owners' licensing powers. Two States do maintain somewhat narrower exemptions, while a third, Canada, contains a much broader exemption than that found in the United States Copyright Act. This "head count" of national laws reveals that the United States is in an extremely isolated position compared to its international copyright colleagues and WTO trading partners.<sup>383</sup>

### 3. Step Three—The "Unreasonable Prejudice" Requirement

The final step in the three-step test requires proof that the United States' licensing legislation does not "unreasonably prejudice the legitimate interests of the author." The drafters of Article 9(2) clearly envisioned this step as an additional requirement upon which national laws might be found incompatible with the Berne Convention even if the laws survived examination under the first two steps. The drafters also believed that because *any* exercise of the copyright owner's exclusive rights would prejudice her interests to some degree, only unreasonable prejudice would be proscribed.<sup>384</sup> However, other than noting that the use of compulsory licenses would mitigate prejudice, the drafters could not reach agreement on the meaning of "unreasonable prejudice."<sup>385</sup> As a result, commentators have provided only cursory guidance to its application, characterizing this phrase as imposing a "flexible standard of

---

Copyright Act, 1994 (N.Z.) § 32(3), available at (visited Dec. 4, 1999) <[http://www.knowledge-basket.co.nz/gpprint/acts/maps/acts\\_c.html](http://www.knowledge-basket.co.nz/gpprint/acts/maps/acts_c.html)> (New Zealand copyright act noting that copyrighted work can be infringed "by the performance, playing, or showing of the work in public by means of apparatus for receiving visual images or sounds conveyed by electronic or other means"); Zambia Copyright and Performance Rights Act, 1994, § 17(2)(c) & (d), available at (visited Dec. 4, 1999) <<http://lii.zamnet.zm:8000/acts/1994/copyrt94.htm>> (granting music copyright owners control over "broadcasting or inclusion in a cable program service" or "communication to the public by any other means").

<sup>383</sup> A head count of national copyright laws is only one factor to consider in analyzing normal exploitation, however. WTO jurists should exercise caution in the early years of the dispute settlement system when asked to impose a position sanctions by the laws of a majority of member States against a State that has "not joined in an otherwise broad-based trend" interpreting the Berne and TRIPs treaties. See Helfer, *supra* note 29, at 428. However, statutes such as the FIMLA and the homestyle exemption which are "far outside of the global mainstream—as demonstrated by a comparative law analysis," bear a particular heavy burden of justification. *Id.* at 437.

<sup>384</sup> See RICKETSON, *supra* note 211, at 483-84.

<sup>385</sup> See 1978 WIPO Guide, *supra* note 210, at 56 ("In cases where there would be serious loss of profit for the copyright owner, the law should provide him with some compensation."); see also NORDEMANN ET AL, *supra* note 211, at 109 ("[T]he interests of the author always . . . have been unreasonably invaded when he can demonstrate a reasonable interest that this type of exploitation should remain reserved for him or that it should be permitted only upon payment of a suitable royalty.").

reasonableness” that is “to be ultimately determined by national law.”<sup>386</sup>

The EC asserts that the copyright owner’s “legitimate interests” refers to the royalties he or she may expect in return for using the work. It invites WTO jurists to apply “a rule of reason standard” that requires a ruling in its favor because the royalty losses created by the exemptions are more than “a negligible and insignificant fraction of [copyright owners’] income in respect of the public communication of their works in the United States.”<sup>387</sup> To support this argument, the EC uses an “extrapolation model” which projects that the homestyle exemption creates a loss to European copyright owners of between \$3.8 and \$6.9 million per year.<sup>388</sup>

The United States has responded by challenging the EC’s statistics as “failing to account for the majority of relevant factors that determine whether a right holder would be economically prejudiced” by the exemptions.<sup>389</sup> In particular, the United States argues that the EC has improperly overestimated the number of commercial establishments from which PROs collected royalties prior to the passage of the FIMLA. As a result, the United States concludes that “the EC has not presented a *prima facie* case that any prejudice suffered by EC right holders is unreasonable . . . .”<sup>390</sup> Given the uncertain meaning of this last step of the three-step test, it is difficult to predict how WTO jurists will respond to the parties’ arguments.

#### G. *Summarizing the Treaty Arguments and Their Significance for Future WTO Litigation*

The United States must overcome numerous hurdles to prove that its music licensing laws are compatible with the Berne and TRIPs treaties. The text of the treaties, their objectives, the practice of other signatory nations and, in some instances, the drafting history and writings of commentators all strongly suggest that the United States cannot overcome these hurdles. A ruling against the United States thus appears to be imminent.

---

<sup>386</sup> RICKETSON, *supra* note 211, at 484. *See also* STEWART, *supra* note 216, at 80 (“[E]ach member country has to decide what the legitimate interests of the author are [and] whether the prejudice of these interests, which is inevitable, is reasonable or unreasonable.”).

<sup>387</sup> *Examination Procedure*, *supra* note 158, at 18.

<sup>388</sup> *See id.* at 29-30. This figure is equal to between 13 percent and 24 percent of the remittances received from United States PROs. *See id.* To calculate this royalty loss, the EC’s extrapolation model first estimates the number of businesses exempted by United States law. It then calculates the lost royalties by applying a hypothetical license fee equal to the average fee PROs now charge such businesses for performing recorded music. Finally, the model estimates the EC’s share of those lost royalties based on the United States PROs’ annual royalty distributions to PROs within the EC. *See id.* at 24-30. Since the passage of the FIMLA, the EC has recalculated the total royalty losses to be \$30.3 million per year. *See supra* note 19.

<sup>389</sup> *First U.S. Submission*, *supra* note 7, at 18.

<sup>390</sup> *Id.* at 19.

Although the United States is likely to lose the FIMLA dispute, it is uncertain whether the WTO panel and Appellate Body will analyze United States laws under the three-step test. Precisely because the test is ambiguous and its proper interpretation contested, WTO jurists should decide the case on the narrowest possible grounds and decline to evaluate the United States laws under that standard.<sup>391</sup> Such a narrow resolution of the FIMLA dispute would provide only weak predictive value for future WTO litigation over copyright limitations and exceptions. It would also defer resolution of the most controversial and unsettled questions of treaty interpretation identified above, allowing member States additional time to harmonize their national laws in light of recently adopted international treaty standards.<sup>392</sup>

It is equally plausible, however, that WTO jurists will reach the three-step test, either because the parties have raised it<sup>393</sup> or because the jurists wish to

---

<sup>391</sup> For an argument that nascent dispute settlement bodies should resolve cases on narrow grounds and develop their jurisprudence incrementally to earn the trust of States parties, see Laurence R. Helfer & Anne-Marie Slaughter, *Toward a Theory of Effective Supranational Adjudication*, 107 YALE L.J. 273, 367 (1997); see also Helfer, *supra* note 29, at 438 (encouraging WTO jurists to “[proceed] cautiously and incrementally” when interpreting copyright exceptions and limitations clauses).

<sup>392</sup> TRIPs was adopted in 1994 and entered into force for industrialized nations on January 1, 1996. For nations with developing and transitional economies, however, most of TRIPs’ substantive provisions do not become binding until 2000 or 2006. See TRIPs, *supra* note 16, arts. 65(1) & 66; Helfer, *supra* note 29, at 377 (outlining implementation timetable for TRIPs signatories). Deferring a ruling on controversial questions of treaty interpretation will also allow additional time to clarify the relationship between TRIPs and the WIPO Copyright Treaty. Commentators have argued that the latter treaty restores much of the discretion that national decisionmakers arguably lost in the TRIPs Agreement through the adoption of the three-step test in TRIPs article 13. See *supra* Part III.C. Commentators have also noted, however, that the relationship between the two treaties will remain murky until the WIPO Copyright Treaty enters into force. See, e.g., Netanel, *The Next Round*, *supra* note 32, at 467-75.

<sup>393</sup> A conflicting record is emerging regarding whether WTO dispute settlement bodies are resolving disputes on narrow grounds that allow member States the discretion to balance free trade against other social objectives, including labor rights, environmental protection, national culture and a balanced regime of intellectual property protection. Several recent cases suggest that WTO jurists are giving free trade norms undue primacy over these equally crucial societal interests and are reaching to decide legal questions in favor of member nations complaining of treaty violations. See, e.g., Chi Carmody, *When “Cultural Identity Was Not At Issue”: Thinking About Canada—Certain Measures Concerning Periodicals*, 30 LAW & POL’Y INT’L BUS. 231, 239 (1999) (predicting that “future panels will view the Uruguay Round results strictly through an economic prism, meaning that there is apparently little room to evaluate the cultural content of goods and services or the distinct cultural purposes motivating certain laws”) (footnote omitted); Steve Charnovitz, *The World Trade Organization, Meat Hormones, and Food Safety*, 14 Int’l Trade Rep. (BNA) 1781, 1785 (Oct. 15, 1997) (criticizing a panel decision as “bludgeon[ing]” the losing party and reaching to decide issues at the contested intersection between trade and health law unnecessary to resolve the dispute).

provide guidance for States to interpret the test in future dispute settlement proceedings.<sup>394</sup> If the jurists choose this route, they will create a new jurisprudential gloss against which to judge whether the myriad exceptions and limitations in national copyright laws are permissible under the treaty. Given the cumulative strictures of the three-step test, that gloss is unlikely to favor countries seeking to preserve balanced intellectual property regimes tailored to suit local needs and conditions.<sup>395</sup> The approach is particularly unlikely to favor the United States, whose open-textured fair use doctrine is suspect under the three-step test and ripe for WTO challenge.<sup>396</sup>

---

Other decisions, by contrast, reflect a more circumspect approach and appear to grasp the virtues of deciding disputes on the narrowest or least controversial grounds to minimize the politically charged nature of the controversy and to encourage defending states to implement it. Compare J.H. Reichman, *Securing Compliance with the TRIPs Agreement After U.S. v. India*, 1 J. INT'L ECON. L.J. 585, 594-95, 596 (1998) (arguing that the WTO Appellate Body's first TRIPs decision endorsed a "cautious, strict constructionist approach" that "reinforce[s] the residual power of states to forge their own intellectual property laws and policies") with Geller, *International Copyright*, *supra* note 227, § 5[5][b][ii] at INT-201 ("strict construction" of first TRIPs decision may not apply to incorporated Berne articles). See also Charnovitz, *supra*, at 1785 ("When a panel finds a health or environmental measure in violation of WTO rules, the panel should decide the case on the narrowest possible ground. A panel should seek to nudge the violator into compliance.").

<sup>394</sup> See Serge Frechette, *Performance of the System III: Appellate Body*, 32 INT'L LAW. 747, 748 (1998) ("In some cases, the [WTO] Appellate Body has provided clear and concise explanations for its conclusions; in others, it has not."); Daniel Pruzin, *WTO Decision On EU Beef Imports To Have Impact Beyond Hormones*, 15 Int'l Trade Rep. (BNA) 142 (Jan. 28, 1998) (stating that member States attach particular importance to recent WTO rulings when predicting outcomes of other disputes relating to the same treaty).

<sup>395</sup> For commentators advocating such balanced regimes, see, e.g., Dreyfuss & Lowenfeld, *supra* note 235, at 300-07 (highlighting different ways that States might deal with copyright issues and urging deference to local solutions); Helfer, *supra* note 29, at 414 ("Some deference to national decisionmakers will thus be essential if TRIPs jurists are to avoid unduly straining the dispute settlement system's authority and legitimacy."); Neil W. Netanel, *Asserting Copyright's Democratic Principles in the Global Arena*, 51 VAND. L. REV. 217, 222 (1998) ("Copyrights' constitutive value for democratic development depends heavily on local circumstances."); J.H. Reichman, *From Free Riders to Fair Followers: Global Competition Under the TRIPs Agreement*, 29 N.Y.U. J. INT'L & POL. 11 (1997) (urging a pro-competitive strategy for implementing the TRIPs agreement whereby nations, especially developing ones, would be granted significant latitudes to account for local conditions).

<sup>396</sup> See Dreyfuss & Lowenfeld, *supra* note 235, at 306 (questioning the compatibility of the United States fair use doctrine with seemingly narrower TRIPs exceptions); Paul Edward Geller, *Can the GATT Incorporate Berne Whole?*, 12 EUR. INTELL. PROP. REV. 423, 425 (1990) (noting likelihood that United States fair use doctrine will be found to be in violation of TRIPs). See also Tyler G. Newby, Note, *What's Fair Here is Not Fair Everywhere: Does the American Fair Use Doctrine Violate International Copyright Law*, 51 STAN. L. REV. 1633, 1648 (1999) (expressing concern over whether the United States fair use doctrine is compatible with article 13's three-part test).

For these reasons, the United States would be prudent to settle the FIMLA dispute before WTO jurists issue a definitive ruling. If it does not, the EC may seek to impose sanctions against the United States, possibly by withholding remittances to United States PROs in an amount equal to the royalty losses to foreign copyright owners generated by the treaty-incompatible licensing laws.<sup>397</sup> Thus, whether the United States settles the dispute or instead chooses to litigate the case to a final ruling by the Appellate Body, Congress will soon need to consider revising the Copyright Act to bring the statute into compliance with United States treaty obligations.

#### IV. SOLUTIONS TO THE FIMLA DISPUTE: ENCOURAGING PRIVATE AGREEMENT WHILE COMPLYING WITH THE BERNE AND TRIPS TREATIES

If WTO jurists rule in favor of the EC, the United States will face the politically sensitive task of deciding whether and how to revise its copyright laws to conform to the Berne Convention and the TRIPs Agreement. This Part begins by dismissing on political and pragmatic grounds two alternative solutions to the FIMLA dispute—abolishing the licensing exemption solely for music of foreign origin and requiring broadcasters to pay for in-store performances. It then draws upon and extends the economic efficiency arguments developed in Part I, together with the historical precedents discussed in Part II and the international law arguments developed in Part III, to identify and defend a legislative reform option that is both compatible with United States' treaty obligations and that encourages copyright owners and copyright users to reach an efficient private agreement to resolve the dispute over licensing secondary uses of broadcast music.

##### A. *Repeal the FIMLA and Homestyle Exemptions for Foreign Music Only*

The United States could comply with an adverse WTO ruling by repealing the FIMLA and homestyle exemptions, but only for copyrighted music whose country of origin is other Berne or TRIPs member States. Because neither treaty compels governments to provide copyright protection to the works of its own nationals, the United States could adopt a dual copyright system, retaining the FIMLA for all copyrighted music whose country of origin is the United States, while repealing the statute for all musical works that originate from other Berne or TRIPs signatories.<sup>398</sup>

Although this foreign-domestic distinction is unassailable from the

---

<sup>397</sup> For a discussion of the Berne-compatibility of retaliatory measures relating to a TRIPs copyright dispute, see Geller, *International Copyright*, *supra* note 227, § 5[5][b][ii] at INT-203.

<sup>398</sup> See, e.g., NORDEMANN ET AL, *supra* note 211, at 21; STERLING, *supra* note 237, at 460. As noted above, the Berne Convention contains complex rules for determining the works to which it applies. There is no dispute, however, that for the United States the Convention would not apply to works first published in the United States. See *Final Report*, *supra* note 207, at 5.

perspective of the United States' treaty obligations, it is highly dubious as a political and practical matter. First, the Copyright Act's exclusive rights and exemptions provisions have treated foreign and domestic copyrighted works identically since the United States first became a Berne signatory.<sup>399</sup> Other State parties have followed the same approach.<sup>400</sup>

The reason for this de facto equal treatment is obvious: it is "politically difficult to grant rights to foreigners but not to nationals."<sup>401</sup> If United States PROs and American songwriters, lyricists and music publishers failed, when opposing the FIMLA, to muster sufficient political support to protect their interests over those of restaurants, bars and small businesses, they are unlikely to do so solely for foreign (and non-voting) music copyright owners.<sup>402</sup> This is so even though, under this proposal, foreign PROs will likely remit more money to United States copyright owners for secondary uses of broadcast music in foreign countries than United States PROs will remit to foreign owners whose works are played in bars, restaurants and retail stores in this country.<sup>403</sup>

Numerous practical problems would also plague a foreign-domestic exemption distinction. First, businesses tuning in to radio, television and cable broadcasts or transmissions cannot readily distinguish between foreign and domestic music nor can they exercise perfect control over the content of the music transmitted in their establishments.<sup>404</sup> A statute that exempted only

---

<sup>399</sup> See 17 U.S.C. §§ 106 (1994 & Supp. 1995), 106A (1994), 107 (1994), 110 (1994 & Supp. 1999); see also Scott M. Martin, *The Berne Convention and the U.S. Compulsory License For Jukeboxes: Why the Song Could Not Remain the Same*, 37 J. COPYRIGHT SOC'Y U.S.A. 262, 299-300 (1990) (noting that Berne implementing legislation "does not include a two-tiered structure" for juke box performance rights). Only a few provisions of United States law apply more favorable rules to foreign works. See, e.g., 17 U.S.C. § 104A (1994 & Supp. 1998) (restored works of foreign origin); § 411 (1994 & Supp. 1998) (registration).

<sup>400</sup> See, e.g., RICKETSON, *supra* note 211, at 206 ("[E]ach Union country will usually . . . grant identical protection both to its own authors and to Union authors."); David Vaver, *The National Treatment Requirements of the Berne and Universal Copyright Conventions*, 17 IIC 577, 586 (1986) (explaining that although Berne minimum standards only apply to foreigners, in practice states grant the same rights to nationals).

<sup>401</sup> Geller, *International Copyright*, *supra* note 227, § 2[3][b] at INT-39. See also NORDEMANN ET AL, *supra* note 211, at 72 ("[N]o country has any rational interest in placing foreigners in a better position than its own citizens.").

<sup>402</sup> Indeed, those politicians favoring a repeal of the FIMLA stress the harm that it causes to American composers, lyricists, and music publishers. See Schumer, *supra* note 195; E. Scott Johnson, *Law Gives Copyrights New Life*, Nat'l L.J., Feb. 8, 1999, at C12.

<sup>403</sup> Cf. 1997 Hearings, *supra* note 19, at 68 (letter of Robert L. Stoll, U.S. Patent and Trademark Office) (noting that United States music copyright owners received a net surplus of \$300 million in royalty remittances in 1996 from foreign PROs attributable to all types of performances of works).

<sup>404</sup> Cf. U.S. Copyright Office, *Implementing Legislation to Permit U.S. Adherence to the Berne Convention: A Draft Discussion Bill & Commentary*, 10 Colum.-VLA J. L. & the Arts 621, 631 (1986) ("[T]here must be a unitary system with respect to juke box rights,

domestic music would thus require PROs to devise a method to measure when businesses with highly diverse music needs perform non-exempt foreign music as opposed to free domestic music.<sup>405</sup> Such a measurement system—which is likely to be inaccurate, unpopular with users and subject to abuse by licensees—would increase significantly the transaction costs of licensing and enforcement. In addition, PROs are likely to face pressure from businesses that do perform foreign music to adopt a “mini-blanket license” for all foreign works in their repertoires or a royalty scheme based on the actual use of foreign works. Both of these systems would be far more cumbersome and expensive to administer than the traditional blanket license.<sup>406</sup>

#### B. *Mandate Broadcasters to Pay for Secondary Uses of Broadcast Music*

A second way for Congress to satisfy the United States’ treaty obligations is by requiring radio, television and cable stations to pay for the secondary uses of broadcast music by commercial establishments. Under this system, PROs would charge broadcasters a license fee in addition to the fee they currently

---

since it would be unduly burdensome to all concerned if a juke box proprietor could avail himself of a compulsory license for works of U.S. origin but had to negotiate a license for foreign works.”).

<sup>405</sup> For purposes of distributing royalties to their members, PROs use statistical sampling and surveys to determine which selections from their repertoires have been performed by radio, television, and cable stations and with what frequency. See KOHN & KOHN, *supra* note 4, at 883. No effort is made to sample secondary uses of broadcast music, however, on the “assumption that the music being performed over the radio and television is roughly the same as the music being performed in cafes, hotels, sports arenas, and restaurants, and nightclubs.” *Id.* That assumption would no longer hold under a system in which commercial establishments have an incentive to perform music that does not require a license. Thus, PROs would need to establish a separate system to monitor secondary uses of broadcast music. See *Broadcast Music, Inc. v. Moor-Law, Inc.*, 527 F. Supp. 758, 769-770 n.16 (D. Del. 1981) (dismissing proposal to create a performance license fee tailored to a nightclub’s use of only specific styles of music because proposal would require establishing a system to monitor use and nightclub would have an incentive to manipulate the system to reduce license fees), *aff’d*, 691 F.2d 490 (3d Cir. 1982).

<sup>406</sup> The early and influential court decision in the *Moor-Law, Inc.* case rejected a proposal for a use-based system or a “mini” blanket license for businesses seeking to perform only certain styles of music on precisely this ground. See *id.* at 768 (explaining that such licenses would “necessarily cost more to administer than the full repertory license” because they “involve categorization costs, additional policing costs, and the costs of resolving, and of attempting to avoid, disputes over the scope of the license”). A dual system might also harm foreign copyright owners in another way. Because commercial establishments under a dual system would have an interest in playing only domestic music and because broadcasters are aware that their advertising revenues are enhanced by the size of the listening audience, some radio stations might specialize in broadcasting only domestic music and encouraging businesses to “tune in for free.” Were such a system to become widespread, the royalties paid to foreign music copyright owners for in-store performances would diminish sharply.

collect to compensate copyright owners for performances of broadcast music by bars, restaurants and retail stores. This additional fee would satisfy the Berne and TRIPs requirement that copyright owners receive, at a minimum, "equitable remuneration" for secondary uses of broadcast music.<sup>407</sup> Having collected royalties from broadcasters, PROs would then be barred from collecting any additional royalties from commercial establishments for the secondary performances.

At first blush, this "broadcaster pays" proposal appears to create significant efficiency gains. In particular, it removes the significant transaction costs associated with negotiating, monitoring and enforcing license agreements for thousands of dispersed (and often resistant) commercial establishments and shifts those costs to more concentrated cable and broadcast networks and stations. Because these entities already negotiate with PROs for performance licenses on an industry-wide basis<sup>408</sup> and because their high-profile use of music constrains them from free riding without being noticed by PROs, consolidating licensing at the broadcaster-cable level at first appears more cost-efficient than a system compelling PROs to devote resources to licensing myriad secondary users of broadcast music.<sup>409</sup> Indeed, this proposal would effectively eliminate the market failure problem for end-user licensees since there would be no more market to license.<sup>410</sup>

Upon closer scrutiny, however, the transaction costs savings of a "broadcaster pays" proposal are far from clear. Although such a system would preclude PROs from licensing secondary uses of *broadcast* music from commercial establishments, it would not bar them from licensing businesses that perform *recorded or live* music. Thus, for businesses with omnivorous music needs, transaction cost savings would be negligible or nonexistent. More importantly, the freedom from PRO supervision created by a "broadcaster pays" proposal gives commercial establishments a strong

---

<sup>407</sup> Berne Convention, *supra* note 15, art. 11*bis*(2). As noted above, the treaties do not specify *from whom* equitable remuneration must be paid.

<sup>408</sup> See, e.g., Besen et al., *supra* note 55, at 399 & n.59 (providing example of PRO and industry-wide radio, television station and network licensing fee agreements).

<sup>409</sup> See *Don't Stop the Music*, *supra* note 331, at 71 (suggesting this conclusion); MAGNUSSON & NABHAN, *supra* note 286, at 122 (noting inefficiencies of charging licensing fees to broadcast receivers). In addition, to the extent that this proposal requires PROs to negotiate with copyright users possessing greater bargaining power, it may reduce the PROs monopoly pricing power. See *United States v. ASCAP (In re Turner Broadcasting, Inc.)* 782 F. Supp. 778, 790 (S.D.N.Y. 1991) *aff'd* 136 F.2d 21 (2nd Cir. 1992) (adopting this rationale as a justification for requiring PROs to negotiate with cable and broadcast networks rather than with each affiliated station).

<sup>410</sup> For example, the proposal would allow PROs to collect from broadcasters licensing fees that reflect *all* secondary uses of broadcast music, including uses by small businesses with homestyle equipment whose use of music was never licensed because of high transaction costs. See Korman, *supra* note 127, at 528 n.32.

incentive to switch secretly, from broadcast music to recorded music,<sup>411</sup> a performance medium that allows them to exert greater control over customer and employee behavior.<sup>412</sup> The risk of such infringing activity and the associated diminution in licensing royalties would deter PROs from cutting back on their monitoring and enforcement of commercial establishments, thereby significantly reducing the transaction costs savings of any “broadcaster pays” system.

Even assuming that a “broadcaster pays” solution to the FIMLA dispute is efficient, its distributional consequences may preclude Congress from adopting it. The proposal has the unusual characteristic of requiring entities *other* than the commercial establishments that receive financial benefits from the performance of music to pay for its exploitation. Determining which parties ultimately pay for in-store performances will depend on hard to quantify empirical data concerning the competitiveness of the broadcast industry and the substitution incentives for stores who now pay to perform recorded music or purchase background music services.<sup>413</sup>

For example, if the market for advertising is highly competitive, broadcasters will be unable to pass along to advertisers the additional license fees and will be forced to pay the royalties themselves.<sup>414</sup> This is likely to generate significant rent seeking by broadcasters in an effort to prevent Congress from adopting the proposal. However, even if advertisers are compelled to take on a share of the new royalties (a prospect that will depend in part on whether more businesses tune in to “free” broadcast music and

---

<sup>411</sup> See *Examination Procedure*, *supra* note 158, at 31 n.37 (arguing that the homestyle audio technology allows commercial establishments to shirk their licensing obligations by switching from exempt broadcast music to licensable recorded music, thereby reducing PRO royalties).

<sup>412</sup> See Milliman, *supra* note 272, at 90-91.

<sup>413</sup> See Wilk, *supra* note 165, at 839 (noting absence of empirical studies of alternative licensing models for secondary uses of broadcast music and arguing that because costs and benefits “are indirect, fleeting, and often indistinguishable from other costs, it is unlikely that comprehensive studies of the subject will be definitive”). Cf. Lewis Kurlantzick & Jacqueline E. Pennino, *The Audio Home Recording Act of 1992 and the Formation of Copyright Policy*, 45 J. COPYRIGHT SOC’Y U.S.A. 497, 508-15 (1998) (identifying numerous and conflicting variables associated with quantifying the economic impact of home recording and the effect of imposing a levy on the sale of recording equipment and blank tapes). See also *supra* note 295 and accompanying text (identifying variables affecting whether increase in size of broadcast audience will occur if secondary uses of broadcast music are exempted from PRO licensing powers).

<sup>414</sup> In a perfectly competitive market, radio, television or cable operators will be unable to absorb these fees and may thus go out of business or broadcast less copyrighted music to the public. If this occurs, one of the core objectives of the Copyright Act—maximizing the distribution of works to the public—would be undermined. See *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 156 (1975) (balancing creators’ rights against greater goal of “promoting broad public availability of literature, music, and the other arts”).

thereby increase the number of listeners and viewers hearing their commercials), producers of the advertised goods and services, or the consumers who purchase them, will ultimately bear the financial burden of increased broadcaster royalties.<sup>415</sup>

These same distributional inequities prompted the Australian Parliamentary Committee to recommend against adopting a “broadcaster pays” proposal and motivated Canadian copyright commentators to urge the abolition of Canada’s moribund “broadcaster pays” system.<sup>416</sup> Thus, even if a “broadcaster pays” system creates some efficiency gains, they are unlikely to overcome the political opposition created by the distributional effects of such a system, making the political feasibility of the proposal dubious at best.<sup>417</sup>

---

<sup>415</sup> See MAGNUSSON & NABHAN, *supra* note 286, at 121 (noting that “indirectly at least” the burden will fall “on the purchasers of goods and services from the advertisers who pay the broadcaster to advertise”). Note that these consumers may not be the same ones who pay marginally more to eat, drink or shop in establishments that play broadcast music. The extent to which the royalties will be paid by consumers, rather than producers, will depend on the shape of the relevant demand and supply curves for the goods and services in question. See PAUL A. SAMUELSON & WILLIAM D. NORDHAUS, *ECONOMICS* 60-66 (16th ed. 1996).

<sup>416</sup> See *Don’t Stop the Music*, *supra* note 331, at xxi, 78-79 (listing reasons why the Australian committee opposed a “broadcaster pays” system); MAGNUSSON & NABHAN, *supra* note 286, at 122-26 (listing inefficiencies of current Canadian system and recommending modifications).

<sup>417</sup> The Audio Home Recording Act of 1992, 17 U.S.C. §§ 1001-1010 (1994) (hereinafter AHRA) imposes a two percent levy on the sale of digital recording equipment and a three percent levy on the sale of blank audio tapes to offset the economic losses allegedly created by private home taping. See § 1004(a)(1) (1994); § 1004(b). As two commentators argued in a recent article criticizing Congress’ decision to adopt this royalty scheme, the AHRA creates significant distributional inequities and “violates the common precept that those who obtain a product or service ought to be the ones who pay for it.” Kurlantzick & Pennino, *supra* note 413, at 523. In particular, the statute forces recording equipment and blank tape purchasers who do not record copyrighted music to subsidize the activities of consumers who make such recordings. See *id.* at 522 (indicating that the “levy burdens all those who purchase blank audio tape an audio recording equipment irrespective of [their] actual use”).

Although Congress adopted the AHRA notwithstanding its distributional consequences, there are several reasons to believe that the distributional consequences of a “broadcaster pays” resolution to the FIMLA dispute will encounter far more significant political roadblocks. First, political opposition to the AHRA levy system diminished only after recording equipment manufacturers agreed to support the legislation. See *id.* at 500-01. They did so in part to settle a lawsuit brought by music copyright owners claiming that the sale of the recording equipment and tapes made manufacturers liable for home taping as contributory infringers. See *id.* at 500 n.9, 501. With manufacturer opposition to the levy eliminated, those most affected by the AHRA’s distributional effects—consumers who purchased recording equipment but did not engage in home taping—were largely unrepresented before Congress. See *id.* at 531-34 (noting discrepancy in lobbying power and presence between the industry desiring the legislation and the “diffuse, unorganized interests” of consumers). In the case of a “broadcaster pays” system for licensing in-store

C. *Encourage Private Agreements Through a Property Rule or a Liability Rule*

Although both politics and pragmatism make the foregoing proposals implausible solutions to the FIMLA dispute, Congress could act upon a third alternative—revising the Copyright Act to provide incentives for PROs and industry representatives of commercial establishments to negotiate private licensing agreements for secondary uses of broadcast music. This section first assesses the advantages of private agreements over legislatively-mandated compulsory licenses and free use exemptions. It then addresses whether these private agreements are compatible with the United States' treaty obligations. Finally, the section concludes by outlining two treaty-compatible legislative reforms for Congress that will encourage PROs and associations of commercial establishments to negotiate such private licensing deals.

1. *Assessing the Advantages of Private Agreements over Statutory Exemptions for Secondary Uses of Broadcast Music*

Intellectual property commentators have recently devoted considerable attention to the questions of how to encourage copyright owners and users to bargain around the baseline entitlements conferred by domestic copyright laws and of whether those baseline entitlements are superior or inferior to such

---

performances, by contrast, broadcasters are likely to voice significant opposition to the proposal. See *Don't Stop the Music*, *supra* note 331, at 78 (noting that broadcasters opposed a similar proposal in Australia). PROs may also oppose the proposal, particularly if they believe that the aggregate royalties received from broadcasters, commercial establishments and background music services under the new system will be lower than the aggregate royalties currently collected from these sources.

Second, under the AHRA levy scheme, manufacturers' support for the legislation was likely influenced by their ability to distribute, albeit imperfectly, the cost of the levy to consumers engaging in home taping. See Timothy J. Brennan, *An Economic Look at Taxing Home Audio Taping*, 32 J. BROAD. & ELEC. MEDIA 89, 101 (1988). This is unlikely to occur for the royalties collected by broadcasters for in-store performances, since there is no way for broadcasters to control who tunes into their programming or whether music is performed by commercial establishments. See *Don't Stop the Music*, *supra* note 331, at 78 (noting that broadcasters "have no control over or knowledge of the location and use of televisions or radios" by businesses). (In the limited case of in-store performances of music on cable television programs, however, the contractual relationship between cable operators and their subscribers could be revised to allow for such redistribution.) Thus, the financial burden of the proposal is likely to fall on a concentrated group of entities with a strong incentive to oppose it.

Third, although levies on the sale of recording equipment and blank tapes have been adopted by several industrialized countries who are Berne and TRIPs members, see Kurlantzick & Pennino, *supra* note 413, at 497, no signatory state has adopted a functioning "broadcaster pays" system for licensing secondary uses of broadcast music. See *supra* Part III.F.2.d. Thus, the treaty compatibility of such a system is untested.

private agreements.<sup>418</sup>

One of these commentators, Professor Robert Merges, authored a study of collective rights organizations (“CROs”) in which he argued that an intellectual property policy that encourages private agreements is superior to Congressional tinkering with the copyright law. The core insights of Merges’ article, when applied to secondary uses of broadcast music, illustrate the efficiency gains that result from resolving the FIMLA dispute through a legislative solution that encourages private agreements between centralized groups of copyright owners and users. However, as discussed in Part IV.C.3.b. below, Merges’ preference for property rules over liability rules may not in fact represent the optimal choice for encouraging private bargaining between PROs and centralized associations of businesses making secondary use of broadcast music.

Professor Merges’ principal claim is that Congress can best encourage private bargaining by enacting strong property rules for intellectual property owners and by refraining from enacting liability rules in the form of compulsory licenses. Although Congress may find itself tempted to enact compulsory licenses either as a result of rent seeking by copyright users or because of a need to correct market failures caused by high transaction costs, it should resist the temptation. He argues that any compulsory license Congress creates will eliminate copyright owners’ incentives to form CROs that can help to overcome the market failure problem on their own.

Merges asserts that the private licensing arrangements created by CROs are superior to compulsory licenses in several respects. First, CROs reduce the “political economy problems” that plague compulsory licenses, including an initial round of rent seeking by copyright owners and users over the structure of the licensing system and subsequent rent seeking to modify, repeal or retain it in the face of changed market conditions.<sup>419</sup> Second, CROs promote efficient consensual transfers more effectively than compulsory licenses.<sup>420</sup> They have greater flexibility, can rely on experts in the industry and can negotiate directly with associations of copyright users to create royalty rate structures that are “much more in tune with their needs than a congressional scheme of one-size-fits-all transactions.”<sup>421</sup> Thus, Merges concludes that “when private contracts or institutions are a viable alternative, bargaining

---

<sup>418</sup> See, e.g., Bell, *supra* note 53; Julie E. Cohen, *Lochner in Cyberspace: The New Economic Orthodoxy of ‘Right Management,’* 97 MICH. L. REV. 301 (1998); Merges, *Contracting into Liability Rules,* *supra* note 34; Netanel, *Democratic Civil Society,* *supra* note 37. For an insightful treatment of the TRIPs Agreement as a “set of default rules to be bargained around” by private parties and governmental actors, see J.H. Reichman & David Lange, *Bargaining Around the TRIPs Agreement: The Case for Ongoing Public-Private Initiatives to Facilitate World Intellectual Property Transactions,* 9 DUKE J. COMP. & INT’L L. 11, 16, 49-65 (1998).

<sup>419</sup> See Merges, *Contracting into Liability Rules,* *supra* note 34, at 1295.

<sup>420</sup> See *id.* at 1299.

<sup>421</sup> *Id.*

should be channeled out of the legislative arena” and into the private arena.<sup>422</sup>

An extension of Professor Merges’ insights both explains the history of United States laws governing secondary uses of broadcast music and points the way to treaty-compatible solutions to the FIMLA dispute that are also wealth maximizing. First, and most basically, Merges’ claims about the choice between private and legislative remedies to situations of market failure are not restricted to market conditions prevailing prior to the formation of CROs. Even after such organizations have eliminated many of the transaction costs associated with transferring intellectual property rights to their most productive uses, residual market failures will remain.<sup>423</sup> Thus, Congress must decide whether to adopt a legislative remedy for these residual market failures or, alternatively, to allow industry-wide associations of copyright users to negotiate group license fees with PROs that include previously unlicensed performances of music.

Second, Merges’ concerns about the dangers of compulsory licenses apply with at least equal force to free use exemptions. As with compulsory licenses, Congress’ decision to remedy a transaction-cost-induced market failure with a free use exemption generates incentives for rent seeking, both at the time Congress first creates the exemption and later as the parties battle over legislation to retain or modify it. Because free use exemptions are more beneficial to users and more financially harmful to copyright owners than compulsory licenses, they are also likely to incite even more intensive lobbying than rent seeking over compulsory licenses.<sup>424</sup> Furthermore, where copyright users enjoy significant political influence, as is true for the well-organized business interests supporting the FIMLA, they may even overcome the presumption favoring the legislative status quo and convince Congress to expand the exemption.<sup>425</sup>

Third, Merges’ analysis of how CROs overcome the search, negotiation, and enforcement costs that stand in the way of productive exchanges can be extended to transaction costs that take the form of resistance by copyright users to paying license fees. Indeed, Merges’ recounting of ASCAP’s early history

---

<sup>422</sup> *Id.* at 1314-15.

<sup>423</sup> See *supra* Part I.A.4 (discussing market failures created by enforcement and resistance costs); see also Korman, *supra* note 127, at 528 n.32 (describing how small businesses chose to turn off their radios rather than pay the least expensive license PROs could cost-effectively offer).

<sup>424</sup> See Cohen, *supra* note 57, at 238 (discussing protracted negotiations in Digital Millennium Copyright Act over exceptions to exclusive rights); Litman, *Copyright, Compromise, and Legislative History*, *supra* note 112, at 883 (noting that the 1976 Act’s “fair use provision resulted from elaborate, protracted, down-to-the-wire negotiations conducted under congressional sponsorship”).

<sup>425</sup> See Merges, *Contracting into Liability Rules*, *supra* note 34, at 1312. This political clout is most likely to exist for “pork barrel” exemptions benefiting defined interest groups than for more “principled” exemptions such as those favoring educational users or the fair use doctrine. See Brown, *supra* note 283, at 593-94.

illustrates how collective action by copyright owners, without any legislative intervention, reduced resistance through aggressive use of litigation and education efforts to reshape user preferences.<sup>426</sup>

Finally, Merges' prescription to legislators to avoid rushing to intervene in the private marketplace for intellectual property rights in order to encourage the formation of CROs is equally applicable to the issue of whether the government should permit copyright users to solve their own collective action problems by forming centralized or industry-wide associations to negotiate private agreements with PROs over licensing issues. As the example of the NLBA agreement demonstrates, these private agreements have significant advantages over adopting a legislative exemption solution to licensing dispute. They allow the parties to negotiate a package deal that encompasses a variety of issues of concern to both copyright owners and users. These agreements also markedly reduce transaction costs, including the cost of user resistance, by enlisting user associations themselves in education, monitoring and enforcement efforts. With reduced transaction costs, PROs can lower their license fees with no adverse effects on music copyright owners.<sup>427</sup> Finally, private agreements channel the resources of the disputing parties away from rent seeking and toward more productive activities.

For all of these reasons, private agreements provide the best opportunity to eliminate the market failure problem for secondary uses of broadcast music without encouraging the culture of user resistance that followed previous Congressional efforts to modify the Copyright Act. This is not to suggest, however, that a property rule rather than a liability rule is a superior device by which to encourage the parties to negotiate such an agreement. Nor does it imply that private agreements are superior solutions in *other* areas of copyright law, such as fair use, where the statutory entitlement baseline serves vital social objectives and where users are disaggregated and may be unable to bargain with copyright owners effectively.<sup>428</sup>

---

<sup>426</sup> See Merges, *Contracting into Liability Rules*, *supra* note 34, at 1330-33. The period from 1931 to 1975, after ASCAP's victory in *Jewell-LaSalle* solidified its right to collect royalties for secondary uses of broadcast music, provides further evidence of this concept. See *supra* Part II.B.2. After an initial flurry of rent seeking in the 1930s and early 1940s to overturn the decision legislatively or to narrow it judicially, copyright users appear to have largely acquiesced in PROs' licensing efforts—at least until Congress codified ASCAP's licensing practices in 1976. See *id.*

<sup>427</sup> The NLBA agreement contained reduced license fees unavailable to commercial establishments under the FIMLA. See *supra* Part II.B.5.b.3).

<sup>428</sup> Private agreements may in fact be inferior substitutes for legislative exemptions such as the fair use doctrine, which play an essential role in promoting the progress of knowledge and culture. As Professors Julie Cohen and Neil Netanel have observed, if society values limits on copyright protection because those limits serve important expressive, democracy-enhancing or other non-market objectives that are likely to be distorted by private transactions, then it would be desirable for Congress to limit the ability of parties to bargain for a different set of entitlements. See Cohen, *supra* note 418, at 335-44, 382-90; Cohen,

## 2. The Treaty Compatibility of Private Agreements

Can the United States legislatively encourage copyright owners and users to reach a private agreement consistently with its Berne and TRIPs obligations? Commentators analyzing the settlement of domestic law disputes have long observed that private parties bargaining over legal rights and obligations are strongly influenced by the legal framework that serves as a backdrop for their negotiations. Because private parties always “bargain in the shadow of the law,” this underlying legal framework shapes and sets parameters on the scope of their agreement.<sup>429</sup>

These insights are equally applicable to private agreements negotiated in the shadow of international treaty obligations and their domestic laws analogues. Consider the NBLA agreement and voluntary exemptions adopted in Australia as contrasting examples. The NLBA agreement was reached shortly after legislators sympathetic to business interests introduced bills to expand the homestyle exemption to all commercial establishments making incidental uses of music.<sup>430</sup> The fear that Congress might enact these bills and vitiate copyright owners’ control over secondary uses of broadcast music both enhanced PROs’ incentives to reach an agreement with the NLBA and shaped the content of that agreement.<sup>431</sup> By contrast, the decision of the Australian Performing Rights Association to adopt a much narrower voluntary exemption was influenced by the limited scope of the licensing reform proposals then pending before the Australian Parliament.<sup>432</sup>

The lessons of these examples for the United States in seeking to encourage the parties to reach a private agreement are clear. In the wake of an adverse WTO ruling, it would be risky for Congress to encourage the parties to bargain in the shadow of domestic laws that are incompatible with the Berne and TRIPs treaties because any agreement that resulted from such negotiations would also be suspect and subject to a WTO challenge.<sup>433</sup> Rather, the United

---

*supra* note 57, at 239-40; Netanel, *Democratic Civil Society*, *supra* note 37, at 341-64.

In the case of secondary uses of broadcast music, however, private bargaining between relatively well-matched copyright owner and user groups is likely to result in an exemption that is *broader* than any found in the Copyright Act. See *1997 Hearings*, *supra* note 19, at 61 (statement of Marybeth Peters). Moreover, bargaining in this area concerns an exploitation of copyrighted works that is hardly essential to the copyright’s knowledge or democracy-enhancing functions. See Brown, *supra* note 283, at 593-94.

<sup>429</sup> See Robert H. Mnookin & Lewis Kornhauser, *Bargaining in the Shadow of the Law: The Case of Divorce*, 88 YALE L.J. 950, 968-69 (1979) (arguing that in divorce proceedings the parties’ bargaining is a direct result of the “shadow of the law” under which they bargain).

<sup>430</sup> See *Examination Procedure*, *supra* note 158, at 21 (characterizing NLBA agreement as a “compromise” that sought to avoid expanding the homestyle exemption). See also *supra* Part II.B.5.b.3).

<sup>431</sup> See *id.*

<sup>432</sup> See *supra* Part III.F.2.d (discussing background of Australian exemption).

<sup>433</sup> See Martin, *supra* note 399, at 312-13, 326 (arguing that the private agreement

States should first bring the Copyright Act into compliance with the treaties, but should do so in a manner that preserves the parties' incentives to reach a private bargain.

### 3. Choosing Between a Property Rule and a Liability Rule

In seeking to make the Copyright Act treaty-compatible, Congress is not entirely constrained in its legislative options. To the contrary, both the Berne and TRIPs treaties grant Congress discretion in choosing among different alternatives. In particular, because Berne article 11*bis*(2) authorizes member States to create compulsory licenses for secondary uses of broadcast music, Congress may choose between a property rule and a liability rule in seeking to encourage private agreements between centralized associations of copyright users and PROs. The choice that Congress makes between these two approaches will significantly affect both the likelihood that the parties will negotiate a private agreement and the terms of that agreement.

#### a. *A Modified Property Rule*

Under a modified property rule regime, Congress would repeal the FIMLA and homestyle exemptions and restore to music copyright owners the right to control secondary uses of broadcast music, subject to the constraints of the antitrust consent decree.<sup>434</sup> Under this rule, all commercial establishments seeking to perform broadcast music would be required to purchase a license from PROs or from individual copyright owners and would otherwise risk an infringement action.

Although a modified property rule would unquestionably satisfy the United States' obligations under Berne and TRIPs, its effect on the licensing market is less certain. Much will depend on the strength and character of user resistance once copyright owners reacquire their statutory rights to demand royalties for in-store performances. If resistance is intense because commercial

---

between PROs and juke box owners was tainted because it was negotiated in the shadow of a Berne-incompatible compulsory license). For this reason, it is inaccurate to suggest that because an agreement reached between copyright owners and users is private it shields the United States from dispute settlement proceedings by the EC or other WTO member States. See *1997 Hearings*, *supra* note 19, at 62 (statement of Marybeth Peters) (responding affirmatively to the question of whether "because the NLBA agreement [was] a private agreement, a complaint against the United States would not stand"); see also *First U.S. Submission*, *supra* note 7, at 8, 16, 19-20 (relying heavily on fact that private NLBA agreement closely mirrors FIMLA as a means of refuting EC's argument that FIMLA violates the TRIPs Agreement).

<sup>434</sup> I characterize this property rule as "modified" because, as a result of the consent decrees, neither ASCAP nor BMI can withhold licenses from users who request one. See *supra* note 64. As Merges notes, however, the consent decrees merely formalized the practice that PROs had already adopted of voluntarily transforming their property rule entitlements into contractual liability rules. See Merges, *Contracting into Liability Rules*, *supra* note 34, at 1296-97, 1340.

establishments have had a taste of free use,<sup>435</sup> PROs may find that the costs of monitoring and enforcing licensing agreements are exceptionally high. Nor would a modified property rule regime entirely eliminate rent seeking. Even if the strictures of the United States' treaty obligations make legislative lobbying an unprofitable activity,<sup>436</sup> copyright users could still contest the amount of their license fees, either before the Rate Court in New York or by using the local challenge procedures created by the FIMLA.<sup>437</sup> Although businesses have made limited use of the Rate Court because of the high cost of litigating minor licensing disputes far from home, they may be far more active in challenging royalties under the new, more user-friendly challenge rules.<sup>438</sup>

Faced with these high transaction and resistance costs, the three PROs in the United States may seek to negotiate broad-based agreements with associations of copyright users to trade reduced license fees and exemptions for certain businesses in exchange for assistance from the associations in monitoring and enforcing the payment of fees by their members. Even if such agreements mirror the equipment and square footage requirements of the FIMLA exactly, they would still be compatible with the United States treaty obligations because they were negotiated in the shadow of a treaty-compatible statutory baseline. Of course, the parties are not certain to reach such agreements. If they do not, both parties would continue to waste significant resources seeking new ways to evade detection or catch infringers, thereby exacerbating market failures and preventing broadcast music from being put to a productive use.<sup>439</sup>

#### b. *An Ex Post Liability Rule*

Congress need not, however, incur the risks that a modified property rule engenders. Instead, it should devise a compulsory license regime that provides strong incentives for the parties to bargain in its shadow.

In his study of CROs, Professor Merges argues that only property rules create the proper incentives for private bargaining. Other commentators contend, however, that liability rules can provide at least as effective inducements for efficient consensual transfers between copyright owners and

---

<sup>435</sup> Cf. 2 WILLIAM F. PATRY, *COPYRIGHT LAW AND PRACTICE* 972 n.428 (1994) (noting widespread non-compliance with copyright law after abolition of free use exemption for juke box performances).

<sup>436</sup> See Donald J. Kochan, "*Public Use*" and *The Independent Judiciary: Condemnation in an Interest-Group Perspective*, 3 *TEX. REV. L. & POL.* 49, 92 (1998) ("When the likelihood of success . . . is too low, the economically rational special interest will find rent-seeking too expensive.").

<sup>437</sup> See 17 U.S.C. § 513 (1999).

<sup>438</sup> Given the discretion Berne and TRIPs confer on member states to regulate PROs' monopoly powers, see *supra* Part III.F.1.c.2), Congress would not have to remove these new royalty challenge procedures to comply with any WTO ruling.

<sup>439</sup> See *supra* Part I.A.4 (identifying harmful consequences of user resistance).

users.<sup>440</sup> Professors Ayres and Talley have demonstrated that “when two parties have private information about how much they value an entitlement,” endowing each party with a partial claim to the entitlement (the result achieved by a compulsory license) “can reduce the incentive to behave strategically during bargaining, thereby enhancing economic efficiency.”<sup>441</sup> For intellectual property rights, the authors use this model to demonstrate how a compulsory license can remove deadlocks in negotiations between two patent holders.<sup>442</sup>

Professor Neil Netanel has shown that Ayres’s and Talley’s claims are also applicable in the copyright context where multiple licensees are involved.<sup>443</sup> Netanel makes a distinction between compulsory license fees set in advance and those determined *ex post*. When the license fee is fixed in advance at an amount that most prospective licensees would be willing to pay, a “multiple taker” problem may arise.<sup>444</sup> Because the price of the license is likely to attract the interest of many potential licensees or “takers,” the copyright owner “will be unable to buy out unwanted uses and may have to accept less than the prescribed fee for prospective uses that she does not want to transpire.”<sup>445</sup> As a result, the bargaining price is skewed downward below what would otherwise have been the efficient market price.

By contrast, an efficient private agreement is far more likely to result when

---

<sup>440</sup> See Ayres & Talley, *supra* note 54, at 1032 (arguing in favor of a liability rule rather than a property rule because the liability rule “possess(es) an information-forcing” quality which facilitates “more efficient trade”); Netanel, *Democratic Civil Society*, *supra* note 37, at 334-35 (arguing in favor of liability rules to promote bargaining around compulsory licenses).

<sup>441</sup> Ayres & Talley, *supra* note 54, at 1029-30.

<sup>442</sup> See *id.* at 1093-94 (using example of a patent dispute case to show that a liability rule would minimize costs by facilitating the exchange of information, while a property right rule leads to deadlocks in negotiations). Professor Merges asserts that this conclusion is limited to a two-party context. Merges, *Contracting into Liability Rules*, *supra* note 34, at 1304-05 (stating that Ayres’ and Talley’s model is inapplicable when more than two parties are negotiating).

<sup>443</sup> See Netanel, *Democratic Civil Society*, *supra* note 37, at 334-35 & n.248 (addressing Merges’ claim that Ayres’ and Talley’s model would only apply to situations with two parties involved, and demonstrating that this “multiple taker” problem is solved by setting the compulsory license fees *ex post*).

<sup>444</sup> See *id.*

<sup>445</sup> *Id.* at 334 n.248. The core conceptual point here is that bargaining is a two way street—either party may pay the other for the right not to exercise its portion of the divided entitlement. See Ayres & Talley, *supra* note 54, at 1030-31. Thus, copyright owners who value entitlements highly may pay copyright users not to infringe. However, where there are many potential users, a fixed compulsory license fee encourages spurious claims of infringement to extort a payment from the copyright owner. The result is that the copyright owner is forced to accept royalties lower than the predetermined statutory rate. For a detailed discussion, see Merges, *Contracting into Liability Rules*, *supra* note 34, at 1305-06, 1310 & n.39 (using the example of a copyright holder’s futile attempt to pay off every firm that claimed an interest in making a cover version of a copyrighted song).

a compulsory license “takes the form of an ex post determination of the required license fee, whether on an individualized basis . . . or an industry-wide basis, as where government rate setting tribunals are authorized to prescribe across-the-board compulsory license fees after copyright holder and user groups cannot agree among themselves.”<sup>446</sup> With ex post licenses, uncertainties regarding the subsequently-determined fee amount and the specter of high adjudication costs “would discourage frivolous claimants and encourage efficient bargaining.”<sup>447</sup> Netanel concludes that “the most fruitful” compulsory license regimes “require industry-wide bargaining under the threat of administrative determination of binding ‘reasonable’ license fees if no voluntary agreement is reached.”<sup>448</sup>

c. *The Juke Box Compulsory License and Private Agreement*

The case for using compulsory licenses as incentives for efficient private exchanges is supported by more than economic theory. There is an apposite historical precedent that Congress could follow in establishing a compulsory license for secondary uses of broadcast music—the copyright law revisions relating to performances of music in juke boxes.

The Copyright Act of 1909 afforded the operators of juke boxes a free use exemption to perform copyrighted music publicly. Although music copyright owners initially supported the exemption, believing that juke box performances would promote the sale of sheet music, they later came to abhor its privileging of a multi-million dollar industry of music users. During the extensive negotiations leading up to the Copyright Act of 1976, PROs and juke box operators argued furiously over whether to repeal the exemption.<sup>449</sup> The two sides ultimately agreed to replace the exemption with a compulsory license that prescribed a predetermined annual royalty fee for each registered juke box. Congress enacted this compulsory license and authorized the newly created Copyright Royalty Tribunal to adjust the royalty rates in advance every year.<sup>450</sup>

However, this fixed compulsory license scheme did not work well. Juke box operators, accustomed to years of free music use, actively resisted by not

---

<sup>446</sup> Netanel, *Democratic Civil Society*, *supra* note 37, at 334-35 n.248.

<sup>447</sup> *Id.* Paul Geller’s analysis of how copyright owners and users bargained around the compulsory license rate fixed by the Australian Copyright Tribunal for educational use copying provides further support for this conclusion. See Geller, *Reprography*, *supra* note 318, at 34 & n.50 (1990).

<sup>448</sup> See Netanel, *Democratic Civil Society*, *supra* note 37, at 335 n.248 (citing 17 U.S.C. §§ 114(f) (1994 & Supp. 1998), 116, 118, 119(c)(2)-(3), as examples in the Copyright Act where this “basic model of providing for voluntary negotiations” has been adopted).

<sup>449</sup> See Litman, *Copyright Legislation*, *supra* note 101, at 306 n.172 (describing the dispute over the juke box exemption as a “pitched war” between juke box operators and copyright owners).

<sup>450</sup> See PATRY, *supra* note 435, at 977-82. In its 1980 rate adjustment proceeding, for example, the Royalty Tribunal established stepped increases each year from 1982 to 1989. See *id.* at 982.

registering their machines and not paying the license fees.<sup>451</sup> The PROs brought numerous infringement actions against them, but could not succeed in increasing the number of registered juke boxes.<sup>452</sup> In an effort to address these compliance problems, the three PROs and the Amusement and Music Operators Association (“AMOA”), the trade association representing juke box operators, sought to bargain around the compulsory license. Under the terms of a 1985 agreement, the PROs agreed to provide substantial royalty rebates to juke box operators, and in return the AMOA agreed to adopt programs to encourage its members to comply with the law.<sup>453</sup> The PROs agreed to pay the rebates, however, only if a certain number of juke boxes were registered by particular dates, targets that were never reached.<sup>454</sup> Thus, just as the economic theory predicted, a liability rule with a pre-set royalty resulted in increased infringements and inefficient bargaining below the compulsory license rate.

Congress soon realized that the statutory compulsory license was flawed in another way. With respect to works of foreign origin, the statute denied copyright owners the exclusive right to authorize public performances of music on juke boxes.<sup>455</sup> This conflicted directly with the public performance right of Article 11 of the Berne Convention, which, unlike the broadcast and retransmission rights in Article 11*bis*, does not allow for compulsory licenses.<sup>456</sup> Therefore, the juke box provisions of the Copyright Act stood as major obstacles to the United States ratification of the treaty and entry into the international copyright system.<sup>457</sup>

After extensive negotiations with copyright owners and users, Congress adopted a provision of the Berne Convention Implementation Act of 1988<sup>458</sup> to

---

<sup>451</sup> See *id.* at 982 (characterizing juke box compulsory license as “one of the greatest failures of the 1976 Act, entirely due to the deliberate lawlessness by the majority of jukebox operators”).

<sup>452</sup> See *id.* at 982-83 (discussing the steady decline of registered juke box operators up to 1989, despite the enforcement efforts of copyright owners which included over 1000 suits brought against noncomplying juke box operators).

<sup>453</sup> See *id.* at 983 n.492 (providing details of the 1985 agreement).

<sup>454</sup> See *id.* (noting that although the agreement provided for substantial rebates to be paid if 110,000 machines were licensed by 1987 and 115,000 by 1988, the number never reached 100,000). For a more detailed discussion of the 1985 agreement, see Martin, *supra* note 399, at 280-82. The agreement also prohibited the parties from seeking to modify the compulsory license, a provision added to prevent rent seeking by juke box operators that had occurred prior to the agreement’s adoption. See *id.* at 282.

<sup>455</sup> See *Final Report*, *supra* note 207, at 533 (concluding that with respect to work of foreign origin, the compulsory juke box license was incompatible with the public performance right secured by the Berne Convention).

<sup>456</sup> See *id.* at 534 (“Unlike the other provisions of the Convention, the public performance right in Article 11(1) does not expressly sanction compulsory licensing.”) (footnote omitted).

<sup>457</sup> See *id.* at 534-40.

<sup>458</sup> See 17 U.S.C. § 116A (1989) (current version at 17 U.S.C. § 116 (1994)) (outlining

encourage the parties to negotiate a private, treaty-compatible licensing agreement. First, the Act empowered the Copyright Royalty Tribunal to schedule negotiations between the parties. Second, it authorized copyright owners and juke box operators to designate common agents to conduct these negotiations, thereby encouraging group bargaining.<sup>459</sup> Third, it granted an antitrust exemption which permitted all three PROs to negotiate a common agreement with the AMOA.<sup>460</sup> Finally, and most importantly, Congress retained the compulsory license as a fallback position in the event the parties could not reach agreement.<sup>461</sup> Congress did, however, modify the fallback compulsory license in a significant way: it eliminated the system of *ex ante*, fixed royalty fees and replaced it with an *ex post* system of royalty valuations to be set by the Copyright Royalty Tribunal under a new and uncertain formula.<sup>462</sup> According to the economic theory discussed above, this modified compulsory license was precisely the sort of liability rule likely to produce an efficient private agreement.

Faced with these multiple incentives to bargain in the shadow of an *ex post* liability rule, the parties quickly reached a ten-year agreement over juke box licensing, precluding the fallback compulsory license from ever coming into force.<sup>463</sup> Unlike the 1985 compact, the 1990 agreement provided for a different and significantly higher royalty rate structure than the pre-Berne compulsory license.<sup>464</sup> The agreement has also proved remarkably stable over

---

procedures for negotiating licenses). This section was amended in 1993 by substituting an arbitration process for the compulsory license proceeding as the fallback remedy if the parties could not reach a negotiated agreement. *See* § 116.

<sup>459</sup> *See* § 116(b)(1).

<sup>460</sup> *See* NIMMER & NIMMER, *supra* note 70, § 8.17[C][1] at 8-192.63 n.85 (discussing how the parties negotiating under this subsection “enjoy an implicit antitrust exemption”).

<sup>461</sup> For a detailed discussion of each of these provisions, see *id.* § 8.17 at 8-192.51 to 8-192.65 (discussing the Juke box licensing dilemma and the recent changes in § 116A and 116); PATRY, *supra* note 435, at 983-87 (detailing the mechanics of the statute, in particular, the relationship between negotiated license agreements and the fallback position of compulsory licensing).

<sup>462</sup> *See* 17 U.S.C. § 801(b) (1989) (amended in 1993) (authorizing Royalty Tribunal to set fallback compulsory license rate taking into account rates previously determined by the Tribunal to provide a fair return to the copyright owner and rates contained in any license negotiated by the parties); Martin, *supra* note 399, at 311 (characterizing this as a “market rate standard” and stressing the differences from pre-Berne compulsory licenses).

<sup>463</sup> *See* Martin, *supra* note 399, at 315-16 (discussing the factors that influenced the negotiations for a licensing agreement, and emphasizing that the incentive produced by the *ex post* liability rule was essential to the parties coming to terms).

<sup>464</sup> Whereas the pre-Berne compulsory license fee provided for a royalty of \$63 per juke box per year for 1987, 1988 and 1989, the negotiated agreement set fees for 1990 at \$275 per year for the first juke box, \$55 per year for the second through tenth juke box and \$48 per year for each additional juke box, with subsequent rate adjustments linked to the consumer price index. *See* PATRY, *supra* note 435, at 982, 986. These rates are available to all juke box operators, not only to AMOA members. *See* Martin, *supra* note 399, at 327.

time. So stable, in fact, that in 1993 Congress repealed the fallback compulsory license altogether and replaced it with a system of ad hoc arbitration over royalty rates should the agreement ever unravel.<sup>465</sup> At present, however, the agreement is still in operation and is being automatically renewed each year.<sup>466</sup>

d. *Qualifying the Juke Box Agreement as a Precedent*

The statutory incentives adopted in 1988 to encourage a private licensing agreement between the three PROs and the AMOA provide a particularly apt analogy for Congress to consider if it chooses to modify the Copyright Act to comply with an adverse WTO ruling. Indeed, because article 11*bis*(2) of the Berne Convention expressly authorizes the United States to impose compulsory licenses for secondary uses of broadcast music, the use of a compulsory license to encourage private bargaining will not be tainted in the manner that the juke box agreement arguably was, even if the agreement it engenders mirrors the FIMLA exemption.<sup>467</sup>

A compulsory license is not the only way for Congress to assist the parties to reach a private agreement, however. When combined with other incentives such as forced negotiations through group agents or antitrust exemptions, a modified property rule can also encourage PROs and associations of commercial businesses to bargain. Thus, in choosing between a modified property and a liability rule, Congress will need to consider not only economic

---

Operators pay the fees to the Jukebox License Office, a consortium formed by the PROs to license the operators, collect the fees and encourage compliance with the agreement. *See id.* at 319 (providing a detailed description of how the 1990 agreement works).

<sup>465</sup> *See* Copyright Royalty Tribunal Reform Act, H.R. REP. 103-286, 103d Cong., 1st Sess. 14 (1993) (“The [negotiated] agreement has provisions for automatic renewal and the Committee expects that the parties will continue the agreement in 1999, and perhaps for another ten years.”); *see also* 17 U.S.C. § 801(b) (1994) (providing arbitration as fallback provision, in contrast to the prior law which employed a compulsory license as the fallback provision if the parties did not reach a negotiated agreement).

<sup>466</sup> Telephone interview with Mike Vaughan, Jukebox License Office, in Memphis, Tenn. (Aug. 20, 1999). Nevertheless, the number of licensed juke boxes has continued to decline during the 1990s, driven principally by factors unrelated to user resistance, including attrition of vinyl “45” juke boxes, regional declines in the bar and restaurant business, changing patterns of music use by commercial establishments, and sale of juke boxes for private use. *See* letter from Mike Vaughan, Jukebox License Office (Aug. 26, 1999) (on file with author).

<sup>467</sup> *See supra* Part III.D. This is not, however, the case with respect to one narrow segment of the FIMLA—secondary uses of non-broadcast cable transmissions. Under the Berne Convention, such uses are governed by Article 11 rather than Article 11*bis*, which member States may not subject to a compulsory license. *See* RICKETSON, *supra* note 211, at 432, 451 (distinguishing between broadcast and non-broadcast cable transmissions and noting that non-broadcast cable transmissions may not be subject to a compulsory license). Thus, to ensure the Berne compatibility of any private agreement, Congress would need to adopt a property rule for such cable transmissions.

efficiency, but distributional concerns as well.<sup>468</sup>

For example, if Congress adopts a modified property rule, it will give the PROs the power to set royalty rates unilaterally, placing the onus on copyright users to challenge before the Rate Court or the local arbitration panels the fees set by ASCAP and BMI as “unreasonable.”<sup>469</sup> If, by contrast, Congress adopts a fallback compulsory license with ex post royalty rates to be set by copyright arbitration royalty panels, it will give greater negotiating power to copyright users. This is particularly true if it instructs the panels to consider policy considerations other than those focused on market rates.<sup>470</sup>

In the wake of an adverse WTO ruling, there is thus likely to be a further round of rent seeking before Congress—a round similar to the lobbying by PROs and juke box operators that occurred in the years leading up to the United States ratification of the Berne Convention.<sup>471</sup> This rent seeking is

---

<sup>468</sup> See *supra* Part I.B (identifying distributional arguments raised by businesses supporting exemption for secondary uses of broadcast music).

<sup>469</sup> See *United States v. ASCAP*, 1950-51 Trade Cas. (CCH) ¶ 62,595 at ¶ IX(A) (S.D.N.Y. Mar. 14, 1950) (allowing licensees to apply to the Rate Court for the determination of a “reasonable” license fee if parties cannot agree on such a fee); *United States v. Broadcast Music, Inc.*, Civil No. 64-CV-3787, 1994 WL 901652, at \*1 (S.D.N.Y. Nov. 18, 1994) (modifying the original 1966 consent decree to provide procedures for copyright users to contest the reasonableness of fees set by BMI in accordance with the decree). Because it is not governed by the consent decree, SESAC Inc.’s license fees are not subject to review by the Rate Court.

<sup>470</sup> See *Martin*, *supra* note 399, at 311 (describing “market rate standard” initially adopted for the fallback juke box compulsory license). See also 17 U.S.C. § 114(f)(2)(B) (1994 & Supp. 1998) (Librarian of Congress to set compulsory license rates “that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller” for certain transmissions of digital audio music).

Under the current arbitration system, by contrast, arbitration panels must consider four statutory objectives in setting or adjusting juke box royalty rates: (1) maximizing the availability of creative works to the public; (2) affording the copyright owner a fair return for his or her creative work and the copyright user a fair income under existing economic conditions; (3) confirming the relative roles of the copyright owner and the copyright user in making the product available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk and contribution to the opening of new markets for creative expression and media for their communication; and (4) minimizing any disruptive impact on the structure and practices of the industries involved. See 17 U.S.C. § 801(b)(1) (1994). These factors do not require “market rates” for compulsory licenses. See *Recording Industry Ass’n of Am. v. Librarian of Congress*, 176 F.3d 528, 532-33 (D.C. Cir. 1999) (rejecting the plaintiff’s claim that § 801(b)(1) requires the use of a “market rate” and instead holding that the statute requires “reasonable rates” determined with reference to the four statutory criteria).

<sup>471</sup> See *PATRY*, *supra* note 435, at 983-84 (noting that because of the obvious conflict between § 116 and the Berne Convention, there were “extensive hearings over four years [concerning] a political and legal solution for repealing [the juke box compulsory license]”).

likely to address both the distributional and efficiency consequences of choosing between a modified property rule and a liability rule, and, if the latter approach is adopted, the structure of the fallback compulsory license. If, however, Congress can adopt a statutory baseline that contains adequate incentives for private bargaining, the juke box precedent suggests that the parties' energies will be channeled out of the legislative arena and toward reaching a more efficient private agreement.

#### CONCLUSION

In enacting the Fairness in Music Licensing Act of 1998, Congress deliberately chose to ignore the United States' international trade and intellectual property policies and to enact a treaty-incompatible statute that the European Community was virtually certain to challenge before the World Trade Organization. Congress' decision to expose United States copyright laws to the scrutiny of WTO jurists can only be understood by analyzing the complex web of licensing practices and legal regulations governing secondary uses of broadcast music that evolved in the United States over the last seventy-five years.

The tension between licensing and enforcement efforts by music copyright owners acting through performing rights organizations, and resistance to those licensing and enforcement efforts by copyright users created failures in the licensing market. Partially to remedy those market failures and partially in response to rent seeking by both parties, Congress in 1976 and again in 1998 adopted free use exemptions benefiting commercial establishments that perform broadcast music on their premises. The effect of those revisions to the Copyright Act did not, however, remedy the market failures. Rather, it led commercial establishments to devote increasing resources to resistance and rent seeking.

This Article has identified the economic and distributional arguments that underlie this complex history of domestic copyright laws and licensing practices. It has shown how these arguments are likely to affect WTO jurists' analysis of the EC's complaint against the United States, including an examination of the ambiguous and contested three-step test found in the exceptions and limitations clauses of the Berne Convention and the TRIPs Agreement. Finally, the Article has drawn on economic principles and historical precedent to outline treaty-compatible options for Congress to resolve the FIMLA dispute. These options will not only permit the United States to continue its efforts to protect the intellectual property rights of United States authors, inventors and businesses in other nations, but will also encourage the parties to channel their resources away from rent seeking and toward more efficient private licensing agreements.