

# Music Rights Regime Needs Updating, Should Embrace New Technologies

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This policy post surveys a number of music-related issues that have been the subject in recent years of legislative proposals or policy debates. It is intended to provide background on the issues; highlight key areas where current law is under strain and may warrant reform; and offer some principles to guide current or future reform efforts.

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## **(1) Music Rights Regime Needs Updating, Should Embrace New Technologies**

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Digital technologies and the Internet have deeply affected many industries, but few more so than the music industry. Much attention has focused on the challenges posed by widespread illegal copying of music from peer-to-peer networks. But within the realm of the legitimate industry as well, the way people obtain and enjoy music is changing in fundamental ways. There are entirely new distribution channels that barely existed just a few years ago, from online music stores to digital radio to webcasting and podcasting. There are entirely new business models, many still experimental. And there are new capabilities for consumers, from improved portability to more sophisticated digital recording and custom playlist functions.

Rapid changes and innovation in the distribution and use of music have raised a number of policy issues separate from the question of how to combat large-scale infringement.

- Statutory provisions governing music licensing, specifically sections 114 and 115 of the Copyright Act, appear outdated or ill-suited in some respects to the emerging digital music environment.
- A number of parties dispute the fairness of existing license fees. For example, webcasters have been fighting against a recent substantial rate hike, and terrestrial broadcasters (i.e., traditional, over-the-air radio stations) remain exempt from performance fees that webcasters, satellite radio broadcasters, and cablecasters must pay.
- The recording industry advocates using licensing conditions or legal rules concerning technology functionality to restrict the uncontrolled deployment of digital recording technology that can facilitate high quality, convenient private recordings to "cherry pick" songs from sources like satellite radio, terrestrial digital radio and webcasts.

The music-licensing regime is complex, and making changes will undoubtedly require overcoming substantial political hurdles. But a well-functioning system is important - not just to ensure fair compensation for all parties involved in individual music transactions, but also to enable an innovative music marketplace with proliferating legal choices for consumers. As CDT observed in a [2005 paper offering a framework for approaching digital copyright issues](#) [1], any failure of the legal marketplace to provide content in attractive and convenient forms will fuel demand for and popularity of illegal sources.

Section 2 below provides an overview of shortcomings that have prompted efforts to reform the current licensing regime. Section 3 reviews the arguments over whether action is needed to limit certain types of automatic copying capability unless authorized by copyright holders. Section 4 concludes with CDT's suggested principles for reform. CDT's view is that the goal of reform should be to provide fair compensation to rights holders, without playing favorites as between business models or technologies and with reasonable clarity for all parties. Efforts to mandate or restrict specific technological capabilities should be avoided; instead, the law should seek to address the impact of new technologies through appropriate licensing and compensation arrangements. For example, the changing music landscape warrants reconsideration of terrestrial radio's exemption from section 114 royalties.

## **(2) Shortcomings of Existing Music Licensing Law**

Recorded music is subject to two separate copyrights. First, there is the copyright for the musical composition, typically held by the music publisher or composer/songwriter. Second, there is the copyright for the sound recording, typically held by the record company or the performer. Thus, anyone seeking copyright clearance for an activity involving a musical recording needs to consider both sets of rights. And in each case, the licensing treatment depends on the type of activity. In particular, public performances (for example, playing a song on the radio or in a public place) are subject to different licensing arrangements than reproduction and distribution (for example, selling copies of the song via CD or download). A [brief chart summarizing the resulting licensing categories](#) [2] can be found at the CDT web site.

For two of these categories, Congress has imposed specific licensing arrangements by statute. Section 114 of the Copyright Act creates a statutory license under which parties such as webcasters and satellite radio companies providing radio-like (i.e., not interactive or on-demand) services pay a government-set rate to the owners of the sound recording copyrights for publicly performing those recordings. Section 115 creates a compulsory license effectively setting the standard rate that a party making and distributing a recording of a song would pay to compensate the owner of the underlying musical composition.

Sections 114 and 115 are both very complex, and their application to new music offerings is often unclear. For one thing, categorizing new services neatly as either "performances" or "distributions" is not as easy as it was when virtually all music was either sold on physical media (like records or CDs) or programmed by someone other than the listener (like a radio DJ or program director). For example, streaming services may provide users with ongoing access to music of their choice, while certain downloads could be set to expire after just a few plays (or even one). Moreover, as a technical matter, streaming and downloading each require both some transmission and some copying of data. There has in fact been litigation over whether transmitting music in connection with a download involves a performance as well as a distribution. And buffer, server, and cache copies remain a disputed and important issue. Online services inevitably involve the creation of multiple short-term copies as a technical by-product of streaming or downloading, raising questions about whether and when such transitory copies require separate licenses.

It can also be unclear when new features or capabilities can affect licensing eligibility or trigger new obligations. For example, "interactive services" are excluded from the section 114 license, but the term's definition is open to interpretation and there is no mechanism short of an actual lawsuit for resolving whether a particular service qualifies. This leaves service providers uncertain about what particular features they can add without becoming "interactive" and jeopardizing their eligibility for

the statutory license. Likewise, the maker of a CD containing a single album copied into two different formats to ensure compatibility with different playback systems would face uncertainty about whether two separate licensing fees may be required under section 115.

Congress addressed certain digital music distribution issues in the 1990s, extending the section 115 compulsory license to "digital phonorecord deliveries" - essentially, digital downloads. But the statutory framework for this license still remains burdensome and fails to provide clarity, to the extent that the Register of Copyrights has referred to section 115 as "dysfunctional." Legislation was proposed last year in the House to turn section 115 into a more streamlined "blanket" license. (Under a blanket license, licensees acquire the rights to a full range of music by paying a single fee to a central collecting society. In contrast, the existing compulsory license requires licensees to track down the appropriate rights holders on a song-by-song basis.) At present, however, the legislation appears to be stalled.

Specific complaints about section 114, meanwhile, have tended to center on who pays royalties and how much. Lack of parity is of particular concern. The section requires payment from satellite radio, webcasters, and cablecasters, but exempts terrestrial broadcasters entirely. The recording industry and some performers recently began to advocate aggressively for a repeal of this exemption. Legislation to repeal the exemption is expected to be introduced soon.

Section 114 also departs from parity by establishing separate standards to guide rate-setting proceedings for satellite radio and cable on the one hand and webcasting on the other. Webcasters are subject to a standard that focuses on what "a willing buyer and a willing seller" of the performance right would negotiate in the marketplace. The standard for satellite and cable looks at multiple factors, including a fair rate of return for the copyright holder and fair income to the copyright user, maximizing the availability of creative works to the public, and minimizing disruption in the industry.

A Copyright Royalty Board decision earlier this year applying the "willing buyer, willing seller" standard resulted in significant rate hikes for webcasters, which webcasters have been fighting in a highly public battle. Record companies argue that the new webcasting rates are the product of an extensive and fair process in which all relevant issues were fully considered. Webcasters complain they cannot afford the rate hikes, and some critics maintain that the [rate benchmarks used in the proceeding may fail to reflect the range of pricing arrangements](#) [3] that record companies and smaller, non-interactive webcasters might agree to in a competitive marketplace. Webcasters and SoundExchange, the organization that collects and distributes the royalties in question, continue to negotiate in an effort to resolve the controversy, and agreements have been reached on certain issues.

### **(3) Controversy over Private Copying**

There is also an ongoing debate about advanced personal copying capabilities that would allow consumers automatically to record music from lawfully acquired streams - digital radio, satellite radio, or webcasts, for example - and to select or sort those recordings by artist, song, or album. (The focus here is on recording for personal use, not redistribution over the Internet.)

On one hand, personal copying from radio broadcasts is by now well accepted. The 1984 Supreme Court decision regarding Sony's video recorders found consumer "time shifting" of over-the-air broadcasts to be "fair use" in the television context, and the 1992 Audio Home Recording Act made clear that consumers may engage in non-commercial copying using dedicated music recording devices. (Computers, however, are outside the scope of the statute.) Such copying does not require permission from the rights holders of the content that is copied.

On the other hand, section 114 bars licensees from engaging in certain specified activities that would tend to facilitate selective copying, such as providing a detailed program guide in advance or playing a large block of music from a single artist. For webcasters, section 114 expressly bars assisting or inducing recording by recipients.

Record companies argue that advanced copying capabilities can effectively turn streaming services, licensed as "public performances," into the equivalent of downloading services. In this view, if a consumer can program a device automatically to scan the airwaves and make high quality recordings of whatever individual songs the consumer wants, the result is essentially the same as ordering specific downloads from a distribution service like iTunes. Rights holders therefore say they should be entitled to license and negotiate compensation for the devices or services that enable such recordings, just as they do for services that enable consumers to purchase downloads.

Of course, the extent to which recording capability can substitute for music purchases is likely a question of degree. Home taping likely displaced some purchases too, but quality and convenience were limiting factors. Digital recording capabilities will be better, but may still not offer the full choice and flexibility of purchasing songs for download. For example, consumers looking for a specific song may have to wait until it is played; may find that the broadcast version does not give them the song in its entirety or includes DJ chatter; and may in some cases have less ability than with purchased music to transfer the song to different devices. In terms of end user functionality, copying capabilities generally will precisely mirror neither pure performance nor pure distribution services, but rather will fall somewhere on a spectrum in between. How close specific copying devices or services are to either end of that spectrum, and if or when they should trigger licensing obligations as opposed to being treated like traditional home recording, will be key issues of dispute.

Those concerned about advanced personal copying capabilities not authorized by rights holders have sought protection on several fronts.

In the satellite radio context, record companies have sued XM Satellite Radio for selling portable receivers with significant copying capabilities, charging that selling such devices violates XM's license under section 114. (XM counters that its recording device is in full compliance with the scheme set out in the Audio Home Recording Act, which includes paying levies on each device to compensate copyright owners.) The initial court ruling went against XM, but the case is ongoing. No such lawsuit was filed against Sirius Satellite Radio, because it negotiated deals for record company permission before releasing receivers with copying capabilities.

Measures to limit copying have also been included in licensing reform legislation. A bill introduced by Senator Feinstein would amend section 114 to require section 114 licensees - webcasters as well as satellite radio - to use "reasonably available technology" to prevent copying capabilities that can target individual songs or artists. A proposed section 115 reform bill in the House contained provisions designed to prevent streaming services from doing anything to encourage copying.

In addition, for terrestrial radio, record companies have advocated instituting an "audio flag" regime. This would involve either a legislative or regulatory mandate that devices with digital radio receivers include some kind of copy restricting functionality. Specific technologies to achieve the required functionality might be developed through cross-industry discussions or by private parties. Some proposals have envisioned a significant role for the Federal Communications Commission (FCC) as well, in developing rules and perhaps approving technologies.

## **(4) Key Principles for Reform Efforts**

Reforming music licensing laws is a complicated undertaking, with multiple stakeholders whose interests often diverge. Any reform effort would raise numerous details. But from the perspective of promoting sound technology and digital copyright policy, CDT suggests several key principles.

*Clarity and Simplification:* Clarity and ease-of-use in the licensing regime is important for building legal music delivery services and hence minimizing the appeal of illegal music sources. As the Internet facilitates more diverse participation in legal music delivery, more parties - including small webcasters and pioneering start-ups - need to be able to navigate the legal regime. In particular, service providers of all kinds need the ability to determine with reasonable certainty when they need a performance license versus a distribution license.

In addition, changing section 115 to a blanket license could provide a streamlined way for digital

distribution services to license a comprehensive catalog of music. Peer-to-peer networks offering illegal downloads tend to have highly comprehensive selection, so legal services are at a distinct disadvantage if they cannot do likewise - and nobody in the legal music ecosystem benefits when music fans go to illicit sources instead of licensed ones.

*No Extra Burdens for Online Delivery:* The system should not handicap online delivery by forcing online providers to deal with more layers of copyright clearance than their offline counterparts. A provider engaged in a single type of online music delivery should be subject to licensing for a public performance or a distribution, but not both. Having licensed the activity appropriately, no further license should be required for the making of ephemeral buffer, cache, or server copies that are merely by-products of the licensed activity and have no separate use or value. And there is no good reason why rate-setting proceedings under section 114 should be governed by one standard in the case of webcasting and an entirely different standard in the case of satellite radio or cablecasting.

*No Technology Mandates:* Neither licensing law nor statutory or regulatory requirements should be used to restrain or dictate the design of technology. Digital technology inevitably leads to creative new features and capabilities for the delivery and enjoyment of music, some of which can pose challenges to existing business models. But the law should aim to accommodate new technologies within an overall system of fair compensation for rights holders, not to hold back technological progress or make it contingent on rights holders' permission and control.

Mandating the inclusion of anti-copying or similar technologies in consumer devices, as through implementation of an "audio flag" regime, can impose significant costs and serve as a serious drag on innovation. It effectively gives a government body significant authority to determine what new technologies will be allowed to enter the marketplace. (CDT did a [case study of the specific innovation impact of the FCC's short-lived broadcast flag regime](#) [4]) Imposing technology mandates as a precondition for obtaining statutory licenses may have similar effects, because operating without the benefit of those licenses - and hence taking on the burden of negotiating licenses individually in the marketplace - will often be impractical, particularly for smaller companies.

*Fair Compensation:* While the licensing regime should not serve to hold back new technology, changes in the technological landscape may well call for reexamination of some elements of the existing licensing structure. In particular, changing consumer capabilities and consumption patterns appear to be undermining the rationale for the total exemption of terrestrial radio from paying for its use of sound recordings. The traditional policy rationale was that radio play promotes record sales - and the under-the-table practice of "payola," in which radio stations were paid to play particular music instead of vice versa, suggests that radio's promotional role was indeed highly valued.

As technology opens up new channels for exposing people to music, however, radio's promotional role no longer seems unique. Webcasting and satellite radio play, for example, can provide significant exposure too.

In addition, if the rollout of terrestrial digital radio is accompanied by devices with advanced personal copying capabilities, radio's promotional value may decline. More consumers may come to view time-shifting via radio recordings as a substitute for music purchases. Thus, deployment of advanced copying features may argue strongly for compensating sound recording copyright holders for terrestrial digital radio transmissions - in other words, ending radio's exemption from the section 114 license. CDT believes that dealing with the new technology by providing a new stream of licensing fees to copyright holders is a better policy response than trying to drive the recording features of new digital devices to mimic the limitations of audio cassette decks, as some legislation has seemed to propose.

At present, a number of bills on music licensing questions have received some attention at the congressional committee level, but none has achieved consensus. Thus, imminent major reform is unlikely, and music licensing issues are likely to remain open for some time to come.

[S. 256](#) [5] (Feinstein bill on 114 and copying capability)

[H.R. 6052](#) [6] (2006 House bill to reform section 115)

[S. 1353](#) [7], [H.R. 2060](#) [8] (webcasting bills):

[H.R. 5252](#) [9] (2006 communications bill containing "audio flag" proposal)

[H.R. 4861](#) [10] (2006 audio flag House bill)

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