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Mechanical Licenses and The Willing Buyer/Willing Seller Standard: Establishing Royalty Rates in a Vacuum of Knowledge

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MECHANICAL LICENSES AND THE WILLING BUYER/WILLING SELLER STANDARD: ESTABLISHING ROYALTY RATES IN A VACUUM OF KNOWLEDGE♦

INTRODUCTION

The Music Modernization Act (MMA) was signed into law for the purpose of ushering music-related copyright law into the twenty-first century.[1] An important, but often overlooked, change was the revision of section 115 of the Copyright Act, which replaced the policy-oriented section 801(b)(1) rate-setting standard for mechanical royalties with the willing buyer/willing seller standard.[2] This seemingly minuscule adjustment will have an effect on music copyright owners, streaming services, individuals, and record labels that wish to record a cover song, and even the average music listener—as any increase in royalty rates will ultimately fall back on the consuming public.

This new standard has previously been used in other areas of law, most notably in determining the fair market value for certain public performance royalty rates for digital noninteractive services.[3] It has been praised for being a more equitable standard for the Copyright Royalty Board (CRB) to establish mechanical royalty rates moving forward.[4] However, a deeper analysis into the standard and how it has been applied in other contexts shows that establishing a fair market value for mechanical royalties will be far more complicated than it may initially appear. Due to the complexities of mechanical licenses, the absence of a traditional market due to statutory licenses, and the lack of a suitable alternative market for comparison, establishing these rates based on a willing buyer/willing seller standard will not be an easy task. As a result, there will be a likelihood of potentially inconsistent decisions with one side feeling as though they are getting the short end of the bargain, which

[1] Orrin G. Hatch-Bob Goodlatte Music Modernization Act, Pub. L. No. 115-264, 132 Stat. 3676 (2018).
[2] *Id.* § 102(a); 17 U.S.C. §§ 115, 801(b)(1) (2018).
[3] 17 U.S.C. § 114(f)(1)(B) (2020).
[4] *See* Peter DiCola & David Touve, *Licensing in the Shadow of Copyright*, 17 STAN. TECH. L. REV. 397, 415 (2014); *see also* Chris Marple, *The Times They Are A-Changin': How Music's Mechanical Licensing System May Have Finally Moved into the 21st Century*, 26 RICH. J.L. & TECH. 1, P34 (2020) (noting that the MMA received "praise from stakeholders in each corner of the music industry").

was precisely the issue that the revision to section 115 was intended to cure.[5]

This is not an argument against the new standard, as a comparison between the new standard and the original 801(b)(1) standard reveals that the willing buyer/willing seller standard is better suited for establishing a fair market price for mechanical licenses.[6] Rather, by looking into the CRB's application of the standard in its previous determinations for public performance royalty rates for noninteractive services' use of sound recordings, this Note will draw inferences on how this standard may be applied to mechanical royalties and the difficulties likely to arise given the current state of mechanical licenses. Based on the differences between the types of royalties, this Note will also raise concerns about why the new standard for mechanical royalties may lead to more contention in the short term and examine the major factors that will complicate its application.

This analysis leads to the conclusion that, while the market for public performance licenses for noninteractive services is the closest comparable market that uses the willing buyer/willing seller standard, it is too different to draw any substantial comparisons in applying the standard. Therefore, due to the lack of a comparable market and the absence of an open market free from influence by statutory rates under the previous 801(b)(1) standard,[7] mechanical royalty rates under the willing buyer/willing seller standard will be decided within a vacuum of knowledge. Based on the history of noninteractive public performance royalties when faced with a similar issue,[8] it may be concluded that when faced with a similar issue, mechanical royalty rates will be highly contested and potentially volatile for the foreseeable future. Additionally, due to the increased complexity of mechanical licenses compared to statutory public performance licenses, the CRB will likely find that it is faced with even more difficulty to determine mechanical royalty rates that represent a true willing buyer and willing seller.

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[5] Jacob Victor, *Reconceptualizing Compulsory Copyright Licenses*, 72 STAN. L. REV. 915, 922 (2020).

[6] BRIAN T. YEH, CONG. RESEARCH SERV., RL33631, COPYRIGHT LICENSING IN MUSIC DISTRIBUTION, REPRODUCTION, AND PUBLIC PERFORMANCE (2015) (discussing how public performance rates under the 801(b)(1) "resulted in significantly lower rates" compared to public performance rates under the willing buyer/willing seller standard); *see also* DiCola & Touve, *supra* note 4, at 415.

[7] 17 U.S.C. 801(b)(1).

[8] *See infra* Section III.A.

I. MUSIC LAW AND MECHANICAL LICENSES OVERVIEW

A. *Copyright Law for Music*

A song, as we commonly think of it, is comprised of two separate copyrightable parts: the musical work and the sound recording.[9] A musical work is the original composition of a song along with any accompanying lyrics.[10] The right over the musical work traditionally vests in the songwriter or composer.[11] However, as is often the case in publishing deals, the right over the musical work can instead be assigned to the publisher.[12]

"Sound Recordings" are defined as "works that result from the fixation of a series of musical, spoken, or other sounds."[13] Although, sound recordings may include non-musical recorded sounds but, for purposes of this Note, sound recordings are the embodiment of a recorded performance of the musical work in any medium.[14]

It should be noted that musical works and sound recordings are often owned by different people or entities.[15] The songwriter may also be the performing artist on a sound recording, however, often this is not the case.[16] In addition, similar to songwriters transferring ownership to publishers, recording artists often assign their rights in a sound recording to record labels.[17]

Copyright owners are granted certain exclusive rights over their works.[18] Through these exclusive rights, creators are able to benefit from

[9] *Musical Works, Sound Recordings & Copyright*, U.S. COPYRIGHT OFFICE, https://www.copyright.gov/music-modernization/sound-recordings-vs-musical-works.pdf [https://perma.cc/98AX-U3TK] (Feb. 2020).

[10] *See* 17 U.S.C. § 102(a)(2) (2020); U.S. COPYRIGHT OFFICE, COMPENDIUM OF US COPYRIGHT OFFICE PRACTICES § 802.1 (3d ed. 2017), https://www.copyright.gov/comp3/chap800/ch800-performing-arts.pdf [https://perma.cc/QA7N-QCWN].

[11] *Circular 56A: Copyright Registration of Musical Compositions and Sound Recording*, U.S. COPYRIGHT OFFICE (rev. ed. July 2020), https://www.copyright.gov/circs/circ56a.pdf.

[12] *See generally* Todd Brabec & Jeff Brabec, *Songwriter and Music Publisher Agreements: A Relationship Necessary for Success*, ASCAP, https://www.ascap.com/help/music-business-101/200809 [https://perma.cc/795J-QG58].

[13] 17 U.S.C. § 101 (2020).

[14] *Circular 56A: Copyright Registration of Musical Compositions and Sound Recording*, U.S. COPYRIGHT OFFICE (rev. ed. July 2020), https://www.copyright.gov/circs/circ56a.pdf.

[15] Mark R. Carter, *Applying the Fragmented Literal Similarity Test to Musical-Work and Sound-Recording Infringement: Correcting the Bridgeport Music, Inc. v. Dimension Films Legacy*, 14 MINN. J.L. SCI. & TECH. 669, 676.

[16] A classic example of this situation is a cover song recording. When an artist records a cover song, that artist or their record label would own the sound recording to that cover. The rights over the underlying musical work, however, remain with the songwriter.

[17] *See* Tuneen E. Chisolm, *Whose Song Is That? Searching For Equity and Inspiration For Music Vocalists Under the Copyright Act*, 19 Yale J.L. & Tech. 274, 278 (2017).

[18] Copyright owners have the exclusive rights to do and to authorize others to do the following: (1) reproduce the work; (2) create derivative works; (3) distribute copies of the work; (4) perform the work publicly; (5) display the work publicly; and (6) perform sound recordings publicly through digital audio transmission. *See* 17 U.S.C. § 106 (2020).

their work while excluding others from doing so.[19] These laws promote societal progression and incentivize creative advancements through the arts by providing economic protection for creators. However, in certain circumstances, there are exceptions and limitations to these exclusive rights. One limitation is when a right is subject to a statutory or compulsory license.[20] These types of licenses are required by statute to be granted to the licensee, if the licensee satisfies the necessary criteria for obtaining the statutory license and pays the statutory royalty fees.[21]

Generally, in order to use a copyright protected song, permission must be acquired.[22] This permission may be granted through various licenses depending on how the song will be used. The three main types of music licenses are: (1) public performance licenses, which are required when a song is used in public; (2) synchronization licenses, which are required whenever a musical work is being used in conjunction with a visual work, such as a movie or TV show;[23] and (3) mechanical licenses, which are required when a musical composition is being copied and distributed in an audio-only format.[24] Typically, to obtain music licenses, an individual or entity would make deals with music rights collectives or copyright holders directly.[25] For instance, when an independent film director wishes to use a song in her movie, she must negotiate a synchronization license with the publishers of the musical work and a Master Use License with the record company that owns the sound recording.[26] Acquiring these licenses is a relatively simple process involving negotiations between willing buyers and sellers of music.[27] Statutory licenses, however, complicate the matter.

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19 17 U.S.C. § 106.

20 CONG. RESEARCH SERV., RL33631, COPYRIGHT LICENSING IN MUSIC DISTRIBUTION, REPRODUCTION, AND PUBLIC PERFORMANCE 4 (2015).

21 *Id.*

22 *But see* 17 U.S.C. § 107 (there is an exception to this general rule if the use falls under the doctrine of fair use).

23 There are also Master Use Licenses, which are essentially synchronization licenses for the use of a sound recording rather than the use of the musical work. *See How To Acquire Music For Films*, ASCAP, https://www.ascap.com/help/career-development/How-To-Acquire-Music-For-Films [https://perma.cc/S79A-9N77].

24 *See* Rajan Desai, *Music Licensing, Performance Rights Societies, and Moral Rights for Music: A Need in the Current U.S. Music Licensing* Scheme, 10 U. BALT. INTELL. PROP. L.J. 1, 4–11 (2001).

25 DiCola & Touve, *supra* note 4, at 409. "Rights collectives represent some exclusive right (e.g., the performance right) or rights (e.g., the reproduction and distribution rights) on behalf of some aggregated set of copyright stakeholders related to one type of subject matter. This agglomeration of owners and rights can occur through willful membership, assignment, or Copyright Office designation." *Id.*

26 *A Check List for Using Music in Film or other Audio-Video Content*, ASCAP, https://www.ascap.com/help/career-development/a-checklist-for-using-music-in-film [https://perma.cc/X9SX-ZGSH].

27 *How to Acquire Music For Films*, ASCAP, https://www.ascap.com/help/career-development/How-To-Acquire-Music-For-Films.

Synchronization licenses and some public performance licenses are not subject to any statutory license requirements, meaning that if an agreement is not reached between the buyer (the person or entity wishing to use the music) and seller (the owner of the music), the license is simply not granted.[28] However, some copyright owners' rights to turn away potential buyers have been restricted through acts of Congress imposing statutory licenses, allowing qualifying parties to use a song without acquiring permission from rightsholders.[29] This means if someone wants to use a song in a way that qualifies as a use that would permit a statutory license, they may negotiate directly to obtain a license; however, if such negotiation is not possible, an agreement cannot be reached, or the party simply wishes to bypass negotiations altogether, then it may obtain a statutory license and pay a statutory royalty rate.[30] To understand these licenses and how statutory royalty rates are determined, it is imperative to acknowledge the history of such licenses. In the interest of clarity, this Note will first and foremost focus on the progression of mechanical licenses, as these licenses are the recipients of the rate-setting standard change made in the MMA's revision of section 115. A history of public performance licenses is covered in Section III of this Note in addressing how the standard has been used in the past.

B. *Mechanical Royalties and Compulsory Licenses*

1. Piano Rolls and the Creation of the Mechanical License

At the start of the twentieth century, self-playing pianos, known as player pianos, were rapidly gaining popularity as the new way to listen to music.[31] Piano rolls, made from perforated paper or cloth, allowed a player piano to mechanically reproduce a song without the need for a pianist.[32] In 1902, an estimated 1.5 million piano rolls were manufactured in the United States.[33] Prior to the passage of the Copyright Act of 1909, unauthorized mechanical reproduction of musical compositions did not violate copyright law and, therefore, manufacturers of piano rolls could create a piano roll for any song without compensating the composer or composers of the musical works.[34]

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[28] *See Resources and Learning: Licensing*, RECORDING INDUSTRY ASSOCIATION OF AMERICA, https://www.riaa.com/resources-learning/licensing [https://perma.cc/TG3J-3KFF].
[29] CONG. RESEARCH SERV., RL33631, COPYRIGHT LICENSING IN MUSIC DISTRIBUTION, REPRODUCTION, AND PUBLIC PERFORMANCE 4 (2015).
[30] *Id.*
[31] Jenna Hentoff, *Compulsory Licensing of Musical Works in the Digital Age: Why the Current Process is Ineffective & How Congress is Attempting to Fix it*, 8 J. HIGH TECH. L. 113, 130 (2008).
[32] Michael B. Landau, *MUSIC: "Publication," Musical Compositions, and the Copyright Act of 1909: Still Crazy After all these Years*, 2 Vand. J. Ent. L. & Prac. 29, 34 (2000).
[33] White Smith Music Publ'g Co. v. Apollo Co., 209 U.S. 1, 9 (1908).
[34] AMBER NICOLE SHAVERS, The Little Book of Music Law 24–27 (2013).

Composers and publishers criticized this lack of protection for mechanical reproductions of their music, arguing that they had protectable printing and public performance rights and that the reproductions of musical works in piano rolls should also qualify as protectable uses of their work.[35] Publishers began suing manufacturers of piano rolls hoping that courts would agree.[36]

Recognizing a potential shift in copyright law, the Aeolian Company, a major player piano and piano roll manufacturer, began negotiating deals with publishers to pay royalties for music used going forward if the Supreme Court determined that piano rolls constituted copies of a musical work.[37] As a part of its terms, Aeolian required music publishers to grant Aeolian the exclusive right to use the publishers' compositions for manufacturing piano rolls.[38] Currently having no deals for any compensation from piano rolls, many publishers agreed to these terms.[39]

The Copyright Act of 1909 extended the rights of musical works owners, in part, by granting rights to the mechanical reproductions of a composition.[40] However, with Aeolian's exclusive deals raising concerns of monopolization over piano rolls, Congress also created the compulsory "mechanical" license, allowing anyone to make a mechanical reproduction of a musical work without the knowledge or consent of the copyright owner, provided that the licensee meets the certain qualifications for the license and that the copyright owner is compensated through a statutorily established royalty rate.[41] Important conditions for a mechanical reproduction to be eligible for a compulsory license include: (1) the song is a non-dramatic musical work; (2) the song was previously recorded, (meaning that the "first use" of a musical work in a recording does not require a compulsory license, only subsequent reproductions); (3) the work has been publicly distributed in phonorecords;[42] and (4) the

35 *Id.* at 30.
36 The courts did not. *See* White Smith Music Publ'g Co. v. Apollo Co., 209 U.S. 1, 9 (1908); *see also* Zvi S. Rosen, *Common-Law Copyright*, 85 U.Cin. L. Rev. 1055, 1078–80 (2018).
37 SHAVERS, *supra* note 34, at 28–29.
38 16 Melville B. Nimmer & David Nimmer, *Nimmer on Copyright Copyright Law Revision: House Judiciary Subcommittee Hearings June 10, 1965 on H.R. 4347, H.R. 5680, H.R. 6831, H.R. 6835 (Serial No. 8, Part 2)* (rev. ed. 2020).
39 SHAVERS, *supra* note 34, at 29.
40 *The Register of Copyright Before the Subcommittee on Courts, The Internet and Intellectual Property of the House Committee on the Judiciary*, 108th Cong. (2004) (statement of Marybeth Peters).
41 SHAVERS, *supra* note 34, at 30; *see also The Register of Copyright Before the Subcommittee on Courts, the Internet, and Intellectual Property, Committee on the Judiciary*, 109th Cong. (2005) (statement of Marybeth Peters).
42 Originally, phonorecords were tangible objects in which a song is fixed in any manner "from which the sounds can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device." *See* 17 U.S.C. § 101 (2020). Today, the term phonorecord includes both physical and digital fixations of a musical work. This includes both "first use" recordings and subsequent recordings of a musical work.

new recording does not fundamentally change the musical work's character or melody.[43]

Today, while the threat of the Aeolian Company's unfair competition practices in contracting for exclusive mechanical reproduction rights is long gone, reproduction and distribution rights for musical works are still subject to compulsory mechanical licenses.[44] The dual purposes of this compulsory licensing scheme for mechanical reproductions are to avoid monopolization as well as provide for a legal and efficient framework for musical works to be licensed.[45] The structure of the compulsory license provides a much more streamlined approach for services to obtain the necessary licenses to use music than the alternative of direct deals.[46] There are, however, major disadvantages to this system as well.[47] As discussed in the following sections, the growth in technological innovations for the reproduction of musical works has led to the creation of cover songs and contemporary music consumption as we know it. However, the music industry's rapid technological evolution has created a multitude of complications in establishing compulsory mechanical royalty rates.

2. The Progression of Mechanical Licenses

Mechanical royalties are the monetary compensation owed to the copyright owner of a musical work whenever the work is accessed through a mechanical license.[48] The initial rates for mechanical licenses

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[43] DONALD S. PASSMAN, ALL YOU NEED TO KNOW ABOUT THE MUSIC BUSINESS 216–17 (10th ed. 2019).

[44] Aeolian's influence on the industry steadily declined with the advent of newer music consumption options and the company eventually declared bankruptcy in 1985. *History of the manufacturer Aeolian Company, The; New York*, RADIOMUSEUM, https://www.radiomuseum.org/dsp_hersteller_detail.cfm?company_id=16474 [https://perma.cc/UFB3-AWMH].

[45] Richard Stim, *Copyright and Compulsory Licenses*, NOLO, https://www.nolo.com/legal-encyclopedia/copyright-compulsory-license.html [https://perma.cc/56WH-9G3F]. This efficient framework for music licensing is crucial for musicians, the music industry, and the consuming public. Some consequences of an inefficient licensing system may include "stifled innovation, chastened economic growth, and reduced consumer welfare." DiCola & Touve, *supra* note 4, at 402–03.

[46] It has been hypothesized that this streamlined system has the potential to support the progression of innovation in the music industry by reducing the time services must spend in negotiations before getting to market. *See* DiCola & Touve, *supra* note 4, at 444–46. However, in that particular study, it was found that the rate-setting process for compulsory licenses may require a similar amount of time as direct licensing. *Id.* at 456.

[47] In 1961, the Register of Copyrights advocated for the termination of the compulsory license, but having grown accustomed to this framework, music publishers and composers opposed this position. *See The Register of Copyright before the Subcommittee on Courts, the Internet, and Intellectual Property, Committee on the Judiciary*, 109th Cong. (2005) (statement of Marybeth Peters). For an argument against compulsory licensing based on property concepts, *see* Robert P. Merges, *Contracting into Liability Rules: Intellectual Property Rights and Collective Rights Organizations*, 84 CALIF. L. REV. 1293, 1300 (1996).

[48] *See generally Compulsory License for Making and Distributing Phonorecords*, U.S. COPYRIGHT OFFICE (2019), https://www.copyright.gov/circs/circ73a.pdf [https://perma.cc/FT3Q-Z56T].

were two cents per song, which lasted until 1977.[49] Traditionally, as explained above, these reproductions were in the form of piano rolls.[50] Now, musical works copyright owners receive mechanical royalties from the reproduction of their compositions through CDs, vinyl, digital downloads, and interactive streaming.[51]

The contemporary mechanical license is best known as the license required when an individual or record company wishes to record a cover of a previously released song and distribute the recording in a physical or digital format.[52] The contemporary mechanical rights system recognizes that while the interests in protecting the rights of songwriters and providing a means of monetization when others use their work are as important now as they were at the time of piano rolls. However, there is also great merit in providing ample opportunity for artists to create cover songs of original compositions. The mechanical licensing scheme, and indeed copyright law in general, aims to strike a balance between protecting and compensating creators for their work while permitting legally protected use by third parties to promote societal progress and creativity.[53] The cover song is a classic example of another's use of a musical work that provides a new artistic expression through a preexisting work that can potentially generate immense cultural value. The evolution of creativity and the expansion of societal understanding aside, who doesn't love a good cover song? The compulsory mechanical license ensures that whoever wishes to participate in furthering artistic expression in this manner can do so.

Although the process of reproducing and distributing a song may no longer involve actual mechanical reproduction, the name "mechanical licenses" has stuck. Currently, mechanical rates for physical phonorecords and permanent downloads are 9.1 cents per song or 1.75 cents per minute of playing time, whichever is greater.[54] Apart from cover songs, mechanical licenses are also required for all songs on interactive streaming services.[55] Interactive streaming and limited downloads are

[49] *Mechanical License Royalty Rates*, U.S. COPYRIGHT OFFICE (Sept. 2018), https://copyright.gov/licensing/m200a.pdf [https://perma.cc/A5ZR-W5CN].
[50] *See* discussion *supra* Section I.B.1.
[51] Unlike interactive streaming, non-interactive streaming does not require a mechanical license; only a public performance license. *See* PASSMAN, *supra* note 43, at 233.
[52] Peter S. Menell, *Content: Symposium Notice and Notice Failure in Intellectual Property Law: Panel V: Economic Analysis of Copyright Notice: Tracing and Scope in the Digital Age*, 96 B.U.L. REV. 967, 1018 (2016) (discussing the compulsory mechanical license as a "cover" license).
[53] *See United States Copyright Office: A Brief Introduction and History*, U.S. COPYRIGHT OFFICE, https://www.copyright.gov/circs/circ1a.html [https://perma.cc/TV4W-7YZ4].
[54] *Mechanical License Royalty Rates*, *supra* note 44. However, these rates may be negotiable. *See* Mark A. Lemley, *Contracting Around Liability Rules*, 100 CALIF. L. REV. 463, 479 (2012).
[55] Jason Koransky, *Digital Dilemmas: The Music Industry Confronts Licensing for On-Demand Streaming Services*, LANDSLIDE (Jan./Feb. 2016), https://www.americanbar.org/groups/intellectual_property_law/publications/landslide/2015-16/january-february/digital-dilemmas-music-industry-confronts-licensing-on-demand-streaming-services/ [https://perma.cc/97V9-

determined through a formula consisting of different percentages based on the services.[56] Due to the changes in music consumption, i.e., an increase in the use of digital services,[57] the use of musical works in a manner that requires a mechanical license has increased.[58]

Over the years, there have been some changes to mechanical reproduction and distribution rights. However, despite the advancements in technology, the essential framework has remained the same. One notable change was the new conditions and clarifications contained in section 115 of the Copyright Act of 1976.[59] The most applicable addition to mechanical rights for this discussion was the creation of the Copyright Royalty Tribunal, the first independent rate-setting body for copyright royalties.[60] This was the predecessor of the current rate-setting body, the Copyright Royalty Board (CRB).[61] The CRB is a panel of three Copyright Royalty Judges, elected by the Librarian of Congress, whose duties include determining and adjusting the terms and rates of royalty payments that are subject to statutory or compulsory licenses.[62] As the entity that sets the rates for mechanical and statutory public performance licenses, the CRB will be further discussed in the subsequent sections of this Note.[63]

Following the Copyright Act of 1976, the music industry has survived technological advancements through a system of piecemeal legislation over the years.[64] As new technology is created and questions arise regarding whether licensing is necessary and, if so, what royalties should be paid out, Congress and the courts have reacted by expanding protections and imposing regulations.[65]

ND3K] [hereinafter *Digital Dilemmas*].

[56] *Mechanical License Royalty Rates*, *supra* note 44. For the formulas for determining rates for limited downloads and interactive streaming, *see* 37 C.F.R. §§ 385.10–385.17.

[57] *See Streaming Music Revenue in the United States From 1st Half 2015 to 1st Half 2020, By Source*, STATISTA (Sept. 2020), https://www.statista.com/statistics/492881/digital-music-revenue-in-the-us-by-source/ [https://perma.cc/H6WZ-7Z83] (showing the steady rise in streaming music revenue over the last several years).

[58] Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. 1918, 1921 (Copyright Royalty Bd. Feb. 5, 2019) (discussing how the "growing consumer demand for streaming" coincides with the increase of mechanical licenses).

[59] *The Register of Copyright before the Subcommittee on Courts, the Internet, and Intellectual Property, Committee on the Judiciary*, 109th Cong. (2005) (statement of Marybeth Peters) (listing the most notable changes set forth in section 115 under the Copyright Act of 1976).

[60] *Copyright Royalty Tribunal Notices and Proceedings Archive 1980 - 1993*, IP MALL (Dec. 22, 1993), https://www.ipmall.info/content/copyright-royalty-tribunal-notices-and-proceedings-archive-1980-1993 [https://perma.cc/JGD5-WXUY].

[61] The Copyright Royalty Tribunal was replaced by the Copyright Royalty Judges that make up the CRB in the Copyright Royalty and Distribution Reform Act of 2004. Copyright Royalty and Distribution Reform Act of 2004, Pub. L. No. 108-419, 118 Stat. 2341 (2004); *Copyright Act*, COPYRIGHT ROYALTY BOARD, https://www.crb.gov/laws/ [https://perma.cc/9P45-VZZT].

[62] 17 U.S.C. § 801 (2020).

[63] *See infra* Sections I.C.2 and II.

[64] *See generally Copyright Timeline: A History of Copyright in the United States*, ASSOCIATION OF RESEARCH LIBRARIES, https://www.arl.org/copyright-timeline/ [https://perma.cc/R69T-8UA6].

[65] *See* DiCola & Touve, *supra* note 4, at 404–05 (describing how amendments to copyright law

C. *State of Mechanical Royalties Before the Passage of the MMA*

With respect to granting mechanical licenses and collecting royalties, some publishers have direct deals with companies that reproduce and distribute music.[66] When this is not the case, publishers used third party organizations like the Harry Fox Agency (HFA) to issue licenses and handle royalty payments.[67] In terms of physical phonorecords, if a direct deal exists, record companies will pay mechanical royalties to the songwriter's publisher.[68] If a direct deal does not exist, the HFA would provide a mechanical license to the record company, which would then pay the statutory mechanical royalty rate to the HFA for distribution to the respective publishers.[69] Similar rules apply for digital services, but the different types of services and uses of the songs have further complicated the process.[70]

1. Complications Arising Out of Internet Developments

In terms of streaming, there are two primary categories in which a service may qualify: interactive and noninteractive.[71] Interactive services, such as Spotify, allow users to choose songs they want to hear on demand.[72] Conversely, noninteractive services, such as Pandora or SiriusXM Internet radio, do not provide users with on-demand control.[73] Noninteractive services may provide users with more personalization options than traditional terrestrial radio, but do not allow complete freedom of choice like interactive services.[74] Both sound recordings and musical works require a public performance license to be used on either type of digital service.[75] Mechanical licenses, on the other hand, only apply to musical works and are only required for interactive services.[76]

over the past few decades have "employed an approach based on narrow, detailed, and technology-specific provisions.").

66 Budi Voogt, *The Indie Guide to Music Copyright and Publishing*, HEROIC ACADEMY (Feb. 12, 2019), https://heroic.academy/indie-guide-music-copyright-publishing/ [https://perma.cc/TSU7-Y3KD].

67 DiCola & Touve, *supra* note 4, at 410.

68 PASSMAN, *supra* note 43, at 231.

69 *Id.*

70 As of January 1, 2021, a new non-profit organization called the Mechanical Licensing Collective (MLC), which was designated by the Copyright Office pursuant to the Music Modernization Act of 2018, began issuing and administering blanket mechanical licenses for digital services. *See About Us*, THE MLC, https://www.themlc.com/our-story [https://perma.cc/U958-7E87]; *see also Preparing for 2021*, THE MLC, https://themlc.com/preparing-2021 [https://perma.cc/87GN-AY6E].

71 Lital Helman, *Fair Trade Copyright*, 36 COLUM. J.L. & ARTS 157, 165–66 (2013) (discussing the different types of streaming services and corresponding licenses).

72 *Licensing 101*, SOUNDEXCHANGE, https://www.soundexchange.com/service-provider/licensing-101/ [https://perma.cc/Z8AN-D5UU] [hereinafter *Licensng 101*].

73 *Id.*

74 *Id.*

75 *Licensing 101*, *supra* note 72.

76 DiCola & Touve, *supra* note 4, at 416–17.

The history of the distinguishing between interactive and noninteractive services in terms of requiring a mechanical license is complex. In *UMG Recordings, Inc. et al. v. MP3.com, Inc.*, the District Court for the Southern District of New York held that a copy of a song on a server constitutes a reproduction that gives rise to the necessitates of a mechanical license.[77] for a service to provide a song for transmission to its users, it must have a copy of the song saved to its server.[78] This would suggest that musical works owners would be entitled to royalties under their reproduction rights from both interactive and noninteractive services. Past private negotiations between rightsholders and services, however, resulted in noninteractive services only having to pay for performance rights, while interactive services must pay for both performance and reproduction rights.[79]

2. Recent Disputes Regarding Mechanical Royalty Rates

The CRB's ruling in *Determination of Rates and Terms for Making and Distributing Phonorecords* (known as "*Phonorecords III*") created the largest increase to mechanical royalties in its history, with a tiered rate increase each year from 2018 to 2022.[80] This tiered rate is known as the all-in royalty rate, which is used to determine the mechanical royalty rates for interactive streaming.[81] The all-in rate for streaming services is the greater of its revenue and total content cost percentages.[82] Although both are important, the industry tends to focus on the percent of revenue rates.[83] The percent of revenue rate in 2018 was set at 11.4% and was

77 UMG Recordings et al. v. MP3.com, Inc., 92 F. Supp. 2d 349, 350–53 (2000).

78 *See id.* at 350; *see also Digital Dilemmas*, *supra* note 55.

79 Noninteractive streaming is treated much like traditional radio. Since a radio DJ does not make a copy of a record each time that it is played over the air, the radio station does not have to pay for a mechanical license. Interactive streaming, on the other hand, is treated differently as a result of a rule adopted by the CRB. For more on the history of this distinction, *see* DiCola & Touve, *supra* note 4, at 416.

80 Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. 1918, 1918 (Copyright Royalty Bd. Feb. 5, 2019), https://www.govinfo.gov/content/pkg/FR-2019-02-05/pdf/2019-00249.pdf [https://perma.cc/Z8AN-D5UU]; *see also* Blake Brittain, *Streaming Music Services Win Redo of Royalty Rate Rule (1)*, BLOOMBERG LAW (Aug. 12, 2020, 1:01 PM), https://news.bloomberglaw.com/ip-law/major-streaming-music-services-win-challenge-to-royalty-rates [https://perma.cc/N58K-4CY4]. Keep in mind that although this was a large increase from the previous determination, at this time, the CRB was still determining mechanical royalty rates under the 801(b)(1) standard.

81 Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. 1918, 1918 (Copyright Royalty Bd. Feb. 5, 2019), https://www.govinfo.gov/content/pkg/FR-2019-02-05/pdf/2019-00249.pdf [https://perma.cc/HK6M-H8K2].

82 *Id.*

83 *See e.g.*, Music Business Worldwide, *Major Victory for Songwriters as US Streaming Royalty Rates Rise 44%*, MUSIC BUSINESS WORLDWIDE (Jan. 27, 2018), https://www.musicbusinessworldwide.com/major-victory-songwriters-us-mechanical-rates-will-rise-44-2018/ [https://perma.cc/C8CF-CSK3]; *see also* Tim Ingham, *Songwriters Are Already Fighting For Better Pay. But in 2021, They Face an Even Bigger Battle*, ROLLING STONE (June 15, 2020), https://www.rollingstone.com/pro/features/songwriters-spotify-amazon-crb-royalties-war-1015116/

increased each year by almost one percent until it would reach 15.1% in 2022.[84]

In *Johnson v. Copyright Royalty Board*, streaming services successfully challenged the CRB's determination in *Phonorecords III*.[85] The D.C. Circuit in *Johnson* vacated and remanded *Phonorecords III*, finding the CRB failed to provide "adequate notice or to sufficiently explain" its decision in adopting the rate structure and percentages.[86] Given this ruling, the CRB must reassess its decision and provide an explanation for the royalty rate that it comes to, whether it confirms its original rates or changes them.[87] However, in the period between the time that *Phonorecords III* ruling and *Johnson* decision, Congress passed the Orrin G. Hatch-Bob Goodlatte Music Modernization Act (MMA), which changed the standard for CRB's mechanical royalty rates determination.[88]

3. The Previous § 801(b)(1) Standard for Mechanical Royalty Rates

Since its creation, the CRB has set royalty rates and terms for mechanical licenses every five years.[89] The policy-oriented § 801(b)(1) standard that was previously used for mechanical licenses, including in *Phonorecords III*, required the CRB to determine a royalty rate that would achieve the following objectives:

> A. To maximize the availability of creative works to the public.
>
> B. To afford the copyright owner a fair return for his or her creative work and the copyright user a fair income under existing economic conditions.
>
> C. To reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect

[https://perma.cc/F4QZ-TWSZ].

[84] *Id.* To put this into perspective, if a streaming service had a total reported revenue of $1 billion in 2018, the service would pay $114 million in royalties. If the service also reported a total revenue of $1 billion in 2022, the service would pay $151 million in royalties—an increase of $37 million without any increase of revenue. Of course, it can be expected that a healthy company sees a rise in total reported revenue within these five years. If so, its royalty payment would also be higher. Digital services' main question with this tiered rate is whether the yearly royalty rate increase may be offset by the yearly rise in revenue.

[85] Johnson v. Copyright Royalty Bd., 969 F.3d 363 (D.C. Cir. 2020); *see also* Brittain, *supra* note 80.

[86] *Johnson*, 969 F.3d at 367, 376.

[87] *Id.* at 383; Samantha Handler, *Copyright Panel Rethinking Royalties Streamers Pay*, BLOOMBERG LAW (Aug. 11, 2021), https://news.bloomberglaw.com/ip-law/copyright-panel-rethinking-song-royalties-streamers-pay [https://perma.cc/M5BD-PBFD].

[88] Orrin G. Hatch-Bob Goodlatte Music Modernization Act, Pub. L. No. 115-264, § 102(a), 132 Stat. 3676 (2018).

[89] *See* Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. 1918, 1919 (Copyright Royalty Bd. Feb. 5, 2019); *see also* CONG. RESEARCH SERV., RL33631, COPYRIGHT LICENSING IN MUSIC DISTRIBUTION, REPRODUCTION, AND PUBLIC PERFORMANCE 4 (2015).

> 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.
>
> D. To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices.[90]

This standard has long been criticized by copyright owners and music rights organizations as a subpar standard for determining mechanical royalty rates.[91] Advocators for music rights have argued that the standard as applied by the CRB consistently resulted in rates substantially lower than they would be under a willing buyer/willing seller standard.[92] They have contended that the policy objectives of 801(b)(1) to provide compensation for facilitating access of music to the public yielded exceedingly large discounts to streaming services.[93] The most criticized objective is the fourth factor, which has been known to play "a key role in leading to lower rates" due to its broad potential for shifting rates for the sake of minimizing industry disruption.[94]

D. *Adoption of the Willing Buyer/Willing Seller Standard to Mechanical Licenses Through the Music Modernization Act*

In 2018, the Music Modernization Act (MMA) was signed into law.[95] This omnibus legislation, aimed at ushering the music industry into the twenty-first century, is comprised of three key titles: Title I—Musical Works Modernization; Title II—Classics Protection and Access; and Title III—Allocation for Music Producers.[96] The MMA is championed by a wide array of stakeholders in the music industry.[97] A pivotal, yet

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90 17 U.S.C. § 801(b)(1) (2016). The 801(b)(1) standard has commonly been referred to as a policy-oriented standard because its four factors were designed to serve the policy objective of rewarding the parties compensation for their "relative roles" in providing the public with access to music. Jacob Victor, *Reconceptualizing Compulsory Copyright Licenses*, 72 STAN. L. REV. 915, 920–21 (2020).

91 *Copyright and the Music Marketplace*, U.S. COPYRIGHT OFFICE, 82–83 (Feb. 2015), https://fas.org/sgp/crs/misc/R43984.pdf.

92 *Id. See also* CONG. RESEARCH SERV., RL33631, COPYRIGHT LICENSING IN MUSIC DISTRIBUTION, REPRODUCTION, AND PUBLIC PERFORMANCE (2015) (discussing how public performance rates under the 801(b)(1) "resulted in significantly lower rates" compared to public performance rates under the willing buyer/willing seller standard).

93 Victor, *supra* note 90, at 984 n.371. However, under the willing buyer/willing seller standard, the facilitation of public access to music is still a permissible consideration as relevant market data for the CRB's decision. *Id.* at 927 (discussing the importance of "efficient allocation" of a copyrighted work as an essential part of its market).

94 John Villasenor, *Digital Music Broadcast Royalties: The Case for a Level Playing Field*, ISSUES IN TECHNOLOGY INNOVATION 8 (Aug. 2012), https://www.brookings.edu/wp-content/uploads/2016/06/CTI_19_Villasenor.pdf [https://perma.cc/LYD8-2U2B].

95 *The Creation of the Music Modernization Act*, U.S. COPYRIGHT OFFICE, https://www.copyright.gov/music-modernization/creation.html?loclr=eamma [https://perma.cc/8X64-MFSW].

96 Orrin G. Hatch-Bob Goodlatte Music Modernization Act, Pub. L. No. 115-264, § 1, 132 Stat. 3676 (2018).

97 *See* Marple, *supra* note 4, at P34 (noting that the MMA received "praise from stakeholders in

often overlooked, component of the MMA is its change to the standard used in the CRB's determination of mechanical royalty rates. As of October 11, 2018, the MMA replaced the previous policy-oriented 801(b)(1) rate-setting standard, adopting a willing buyer/willing seller standard for mechanical royalty determinations.[98] This new standard eliminates the fourth consideration of the 801(b)(1) analysis and allows the CRB to consider all relevant market data to determine a fair rate between a hypothetical willing buyer and willing seller.[99] Rather than the "limited-evidence process" of 801(b)(1), which confines permissible evidence to its four factors, the parties may now bring additional relevant evidence to demonstrate the state of the overall market.[100]

The switch to the willing buyer/willing seller standard is expected to result in the CRB establishing significantly higher rates than it did under the old standard.[101] However, questions still remain such as how much these rates will increase and if the analysis employed by the CRB to establish the rates will be accepted as an equitable method of determining fair market value that would have been reached by a willing buyer and a willing seller.

II. MECHANICAL ROYALTY RATES: STARTING ANEW

With this change in rate-setting standard, the CRB is forced to start anew with its mechanical royalty rate determinations.[102] Before looking into the CRB's implementation of this new standard, it is critical to first understand the obstacles and limitations the CRB faces in making its next *Phonorecords* determination. First, the CRB cannot rely on past determinations based on the 801(b)(1) standard.[103] Second, the compulsory license structure stifles open market negotiations between the parties, limiting the number of agreements between actual willing buyers and willing sellers for the CRB to base its decisions.[104] Lastly, even the few direct deals that have been made are a product of the statutory licensing scheme and standard that were in place.[105] Such deals, muddied by old, rejected standards, must be carefully scrutinized. [106]

each corner of the music industry").
98 Orrin G. Hatch-Bob Goodlatte Music Modernization Act § 102(a); 17 U.S.C. § 115 (2018).
99 PASSMAN, *supra* note 43, at 234.
100 *Id.*; *see also* 17 U.S.C. § 801(b)(1) (2016).
101 This projection is based off of the difference in performance royalty rates for satellite and digital cable radio versus Internet radio broadcasters, which are determined under the § 801(b)(1) standard and willing buyer/willing seller standard, respectively. YEH, *supra* note 6, at 27.
102 *See* discussion *infra* Part II.
103 *Id.*
104 *Id.*
105 *Id.*
106 *Id.*

While it is expected that the rates will generally be higher than they were under the 801(b)(1) standard, the CRB cannot use those rates as a benchmark to build off of. The CRB has found that generally "[t]here is no *a priori* reason to conclude that the rates set in [an] earlier proceeding failed to reflect or approximate market forces," and therefore, earlier determinations may be used as a factor in establishing new rates.[107] However, it was agreed that proceedings for compulsory licenses are to be established de novo.[108] This should especially be the case given the change in standard. While in some circumstances, relying on past decisions could be beneficial, it would be counterintuitive to rely on rates set by a standard that was replaced for being an inequitable method of establishing rates.

The CRB is also extremely limited when assessing the new standard based on voluntary negotiations. Statutory licensing schemes have been known for having the effect of stifling voluntary agreements.[109] Having the rates of the CRB or its predecessors to fall back on, services and publishers do not have an extensive history of open market agreements between true willing buyers and willing sellers. Statutory licensing schemes tend to have this effect because the compulsory license is easier to obtain in the sense that the parties do not need to engage in negotiations.[110] As a result, rather than engaging in negotiations, stakeholders may instead spend time and resources on preparing their arguments for more favorable royalty rates during CRB proceedings. Additionally, from a business perspective, services generally do not want to pay more than the minimum statutory rate, so negotiations are less advantageous from a monetary standpoint unless the parties have a prior relationship.[111] These factors lead to low levels of direct negotiations between the parties, giving the CRB little to refer to in order to establish what a willing buyer and a willing seller in the mechanical licensing market would consider to be a fair value.

Further, what few voluntary agreements that have been made were created under a "shadow" of the statutory licensing scheme that was in place at the time of the agreements.[112] As a result of the connection

[107] Determination of Royalty Rates and Terms for Ephemeral Recording and Webcasting Digital Performance of Sound Recordings (Web IV), 81 Fed. Reg. 26,316, 26,382 (Copyright Royalty Bd. May 2, 2016).
[108] Effect of Rates, 37 C.F.R. 385.17 (2009), https://www.govinfo.gov/content/pkg/CFR-2012-title37-vol1/pdf/CFR-2012-title37-vol1-sec385-17.pdf [https://perma.cc/R2BU-Z44A].
[109] U.S. COPYRIGHT OFFICE, COPYRIGHT AND THE MUSIC MARKETPLACE: A REPORT OF THE REGISTER OF COPYRIGHTS 111 (2015) (addressing parties' objections to the statutory licensing structure and claims that "[t]he free market is stifled under Section 115 licensing requirements […]").
[110] YEH, *supra* note 6.
[111] Lemley, *supra* note 54, at 479.
[112] *See* DiCola & Touve, *supra* note 4.

between voluntary and statutory rates, mechanical licenses' minimal history of voluntary agreements is tainted by the previous 801(b)(1) standard. Given that these voluntary agreements do not represent a true willing buyer and willing seller transaction, mechanical royalty rates based on the new willing buyer/willing seller standard will be assessed within a vacuum of knowledge.

Despite the statutory license stifling open agreements, it is not unheard of for music copyright owners and music users to come to partial settlements prior to the CRB's determinations.[113] In this case, the CRB would review the voluntary agreements among the parties as a factor in establishing and adjusting rates and terms.[114] Scholars have argued that rate-setting entities should give great deference to voluntary agreements, as rights owners are in a better position to evaluate and determine a fair price for their work than the courts.[115] However, past negotiations and compromises for direct agreements weighed heavily on the standard used by the CRB to establish the statutory royalty rate. When there is a statutory licensing scheme on which to rely, voluntary agreements are made while considering this alternative and parties only reach settlements they believe will be more beneficial to them than if the rates were in the hands of the CRB.[116]

As Mark A. Lemley, William H. Neukom Professor of Law at Stanford Law School and Director of the Stanford Program in Law, Science and Technology, explains, when compulsory licenses are in place, "[w]hile bargaining will still occur, the baseline may still affect the outcome."[117] In terms of *Phonorecords* determinations, this means that while some voluntary negotiations may take place, they may not accurately represent the agreements of true willing buyers and sellers because their decisions were predicated upon the statutory rate set under the 801(b)(1) standard.[118] Since negotiating parties are likely to "take the nominal legal default as a normative entitlement and be reluctant to disturb it," any negotiations that do occur in a market under a compulsory licensing scheme hinge on the determinations, and therefore the applicable rate-setting standard, of the CRB.[119] Settlements are, in effect, a product of the standard in place.

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113 *See* Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. 1918, 1919–20 (Copyright Royalty Bd. Feb. 5, 2019) (laying out a brief history of prior CRB proceedings and settlements among the parties).
114 17 U.S.C. § 115(d)(7)(B)(i)(II).
115 *See* Merges, *supra* note 42, at 1300; Lemley, *supra* note 54, at 470.
116 *See* DiCola & Touve, *supra* note 4, at 456–57 (concluding that voluntary direct licensing is affected by statutory schemes because of the tension between public and private markets).
117 Lemley, *supra* note 54, at 485.
118 *Id.*
119 *Id.*

Additionally, the CRB decides when to initiate the voluntary negotiation period between the parties.[120] Once the voluntary negotiation period is initiated, the parties have three months to negotiate an agreement before the CRB moves forward with its proceeding.[121] The fact that the CRB controls when negotiations are to occur between the parties further points towards the constraint on voluntary agreements by the licensing system.

With the switch to the willing buyer/willing seller standard, mechanical licenses are, in a sense, starting anew. Once a history has been established through CRB hearings and determinations, appeals, and party settlements, the willing buyer/willing seller standard is expected to result in a less contentious rate-setting procedure and, in theory, a fair market value for music. Until then, however, disputes over mechanical royalties will likely rise rather than fall. With the change in standard, it may well be that settlements between music owners and digital services are unlikely to occur due to the unknowns in how the new standard will affect the CRB's determination.

At the time of this writing, the CRB has not yet used the willing buyer/willing seller standard to determine mechanical royalty rates.[122] After the CRB reassesses its determination of the rates for the term of 2018–2022, as required by the ruling in *Johnson v. Copyright Royalty Board*,[123] it may be that the parties will feel confident enough in their understanding of the CRB's application of the willing buyer/willing seller standard to attempt a partial settlement for the following *Phonorecords* rate period. However, given the circumstances between the standard shift during the term, the court ruling against the CRB's initial determination, and the complexities of mechanical licenses, it is quite possible that consistent application of the willing buyer/willing seller standard will not be settled until after further *Phonorecords* determinations. In an attempt to understand what the future holds for *Phonorecords* determinations, it is helpful to understand the history of the willing buyer/willing seller standard as applied in other contexts and whether there is a comparable market that may be used to gain some footing with how this standard will play out for mechanical royalties.

II. APPLICATION OF THE WILLING BUYER/WILLING SELLER STANDARD IN

120 17 U.S.C. § 803(b)(3)(A).
121 17 U.S.C. § 803(b)(3)(B).
122 *See* Samantha Handler, *Copyright Panel Rethinking Song Royalties Streamers Pay*, BLOOMBERG LAW (Aug. 11, 2021, 5:02 AM), https://news.bloomberglaw.com/ip-law/copyright-panel-rethinking-song-royalties-streamers-pay [https://perma.cc/M5BD-PBFD].
123 Johnson v. Copyright Royalty Bd., 969 F.3d 363, 383 (D.C. Cir. 2020).

OTHER AREAS OF LAW

Prior to the standard being adopted to establish music royalty rates, the willing buyer/willing seller standard has long been a method of evaluating the fair market value for property. In applying this standard for the valuation of property, judges must review all relevant market facts to determine what a hypothetical willing buyer and willing seller would find to be a fair exchange while acting "objectively based upon their knowledge of the relevant facts."[124] In this hypothetical situation, a fair market is "made up of informed buyers and an informed seller, all dealing at arm's length."[125] The value of the property in this hypothetical fair market should be "the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts."[126]

In finding this fair market price, courts often depend on open market negotiations. In terms of federal estate tax purposes under the standard, the value of stock is the "mean between the highest and lowest quoted selling prices on a given day."[127] Without these real, direct deals between actual willing buyers and willing sellers, determining a price in a hypothetical exchange would be extremely difficult. In that situation, a court would have to rely only on any applicable prior court-established rates and any other evidence brought by the parties. These basic principles of the willing buyer/willing seller standard as used for federal estate tax purposes apply in the context of music royalties.

A. *Use of the Willing Buyer/Willing Seller Standard for Sound Recordings' Public Performance Rights for Digital Noninteractive Services*

The MMA adopted an identical application of the willing buyer/willing seller standard for mechanical licenses as was previously used for noninteractive public performance licenses for webcasters.[128] Being the only music royalty market subject to statutory royalty rates under the willing buyer/willing seller standard, noninteractive public performance royalty rate proceedings ("*Web* proceedings") are the closest comparable application of the standard for the purposes of analyzing how the standard will affect mechanical royalty rates. Before discussing the

124 Hicks v. United States, 335 F. Supp. 474, 479 (D. Colo. 1971).
125 *Id.* at 481.
126 26 C.F.R. § 20.2031-1(b) (2022).
127 United States v. Cartwright, 411 U.S. 546, 551 (1973).
128 *Compare* Orrin G. Hatch–Bob Goodlatte Music Modernization Act, Pub. L. No. 115-264, § 102(a)(3), 132 Stat. 3676 (2018), *with* 17 U.S.C. § 114(f) (2016).

application of the standard for public performance royalties, this subsection addresses the relevant history of this license.

Upon the advent of digital distribution services, it became clear that, in many respects, these were desirable services that would reduce consumers' use of the traditional physical formats for music consumption.[129] In response to growing digital music consumption, Congress enacted the Digital Performance Right in Sound Recordings Act of 1995 (DPRA).[130] Prior to the passage of the DPRA, only musical works owners were granted performance rights, while sound recording owners were not.[131] Addressing the inequality in public performance rights between musical works and sound recording owners, the DPRA grants sound recording owners the limited right over the public performance of their sound recordings on digital audio transmissions.[132] This limited right is often referred to as the digital performance right and the digital audio transmissions of phonorecords are called "digital phonorecord deliveries" (DPDs).[133]

Sound recording owners' performance rights over DPDs, when used by certain nonexempt, noninteractive subscription services and preexisting satellite radio services, are subject to a statutory license.[134] Similar to the mechanical license, this statutory license means that noninteractive digital services can either negotiate directly with copyright owners (in this case sound recording copyright owners) to determine a voluntary royalty rate or, if an agreement is not made among the parties, they are subject to the statutory rate.[135] At the time of the DPRA's enactment, rates were determined by the CRB's predecessor, the Copyright Arbitration Royalty Panel (CARP) under the objectives set out in section 801(b)(1) of the Copyright Act.[136]

The DPRA also updated section 115 by including DPDs as a qualifying reproduction of a musical work for purposes of obtaining a

129 *Summary of Statement of Marybeth Peters Before the S. Comm. on the Judiciary Subcomm. on Intell. Prop.*, 109th Cong. 4 (2005) (statement of Marybeth Peters, Register of Copyrights), https://www.judiciary.senate.gov/imo/media/doc/peters_testimony_07_12_05.pdf [https://perma.cc/H3UH-KKG2].

130 Digital Performance Right in Sound Recordings Act of 1995, Pub. L. No. 104–39, 109 Stat. 336 (1995).

131 Digital Performance Right in Sound Recordings and Ephemeral Recordings, 72 Fed. Reg. 24084, 24086 (May 1, 2007) (to be codified at 37 C.F.R. pt. 380).

132 17 U.S.C. § 106(6).

133 *Chapter 8: The Digital Performance Right in Sound Recordings Act of 1995*, ARNOLD & PORTER, https://www.arnoldporter.com/en/perspectives/publications/1997/01/chapter-8-the-digital-performance-right-in-sound__ [https://perma.cc/U8LK-HXYH].

134 17 U.S.C. § 114(d)(2).

135 Digital Performance Right in Sound Recordings and Ephemeral Recordings, 72 Fed. Reg. at 24086.

136 *Id.*; *Summary of Statement of Marybeth Peters Before the S. Comm. on the Judiciary, Subcomm. on Intell. Prop.*, *supra* note 129. A notable difference between CARP and the CRB is that the CRB sets rates every five years while the CARP only set rates on an ad hoc basis. *See* 17 U.S.C. § 801.

mechanical license.[137] Each individual delivery of a musical work through a digital transmission, regardless of if the transmission is also a public performance, requires a mechanical license.[138]

The Digital Millennium Copyright Act (DMCA) expanded the digital performance right created in the DPRA by extending the right to webcasters, i.e., digital services that distribute an audio or video file through Internet streaming.[139] Noninteractive services may obtain statutory digital performance licenses that are administered through SoundExchange on behalf of sound recording owners.[140] SoundExchange will collect and distribute royalties from the licenses to the respective copyright owners.[141]

For interactive services, there are no statutory public performance licenses.[142] However, for noninteractive webcasters, the DMCA created a public performance statutory license, the royalties for which would be determined by the rates and terms that represent those that "would have been negotiated in the marketplace between a willing buyer and a willing seller."[143] This marks the first time that music royalty rates were to be determined under the willing buyer/willing seller standard.

However, up until the passage of the MMA, the statutory royalty rate procedure for noninteractive services was subject to separate standards depended on which subcategory of noninteractive services each service fell.[144] For preexisting noninteractive services, such as satellite radio services and other noninteractive subscription services that were in

137 17 U.S.C. § 115(a)(1)(a).

138 17 U.S.C. § 115(d); Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. 1918, 1919 (Copyright Royalty Bd. Feb. 5, 2019) (to be codified at 37 C.F.R. pt. 385).

139 Cydney A. Tune & Christopher R. Lockard, *Navigating the Tangled Web of Webcasting Royalties*, 27 ENT. & SPORTS L. 3 (2009), https://www.pillsburylaw.com/images/content/2/8/v2/2844/NavigatingtheTangledWebofWebcastingRoyaltiesBylinedArticleCydney.pdf [https://perma.cc/5XCT-7HSQ].

140 17 U.S.C. §§ 112, 114; *see also* Koransky, *supra* note 55.

141 *General FAQs*, SOUNDEXCHANGE, https://www.soundexchange.com/about/general-faqs/ [https://perma.cc/92SK-BZM4]. While there are multiple Performing Rights Organizations (PROs) that may provide public performance licenses, SoundExchange is the only organization currently authorized by Congress to administer the statutory licenses for noninteractive services under sections 112 and 114 of the Copyright Act. *Licensing 101*, *supra* note 72.

142 17 U.S.C. § 114(j)(7) (defining the term interactive service).

143 17 U.S.C. § 144(f)(2)(B). For a brief legislative history of this distinction, *see* Arista Records, LLC v. Launch Media, Inc., 578 F.3d 148, 153–57 (2009). The DMCA also created a statutory license for "ephemeral" copies of a sound recording for situations when a webcaster under the section 114 license makes a temporary copy in order to transmit the recording through the webcaster's service. 17 U.S.C. § 112. The rates for this ephemeral license are decided through the willing buyer/willing seller standard within the *Web* proceedings. 17 U.S.C. § 122(e)(4).

144 17 U.S.C. § 114(f). Section 103 of the MMA erased the discrepancy between rate-setting standards for the different types of noninteractive services by amending section 114(f) to make the willing buyer/willing seller standard the "uniform rate standard" for all noninteractive services. Orrin G. Hatch–Bob Goodlatte Music Modernization Act, Pub. L. No. 115-264, § 103, 132 Stat. 3676 (2018). However, the MMA extended the statutory licensing rate for preexisting services through the end of 2027. This means that the CRB will not have to render a new royalty determination for these services until 2028. *Id.*; 17 U.S.C. § 804(b)(3)(B).

existence prior to the passage of the DMCA in 1998, the statutory licensing rate has been determined by the CRB through the same multi-factor balancing test standard set out in 801(b)(1) that applied to mechanical royalties.[145] Conversely, royalties paid out by webcasters and any new digital services created after the passage of the DCMA have been determined under the willing buyer/willing seller standard.[146]

Under the 801(b)(1) standard, the most recent royalty rate for preexisting subscription services was set at 7.5% of the service's gross revenues.[147] Under the willing buyer/willing seller standard, the most recent rate for all other noninteractive commercial subscription services was set at $0.0026 per performance in 2021, which is adjusted annually according to the Consumer Price Index.[148] The different ways in which the royalties are calculated make comparing the two standards as they apply to noninteractive services rather vague. However, what can ultimately be drawn from these vastly different rates is the underlying priority of the standards. For the 801(b)(1) standard, gross revenue is the baseline measurement because of the standard's linchpin factor for minimizing "any disruptive impact" on these services.[149] A rate that is based on gross revenue hinges on the success of the service that is paying the royalty rate, rather than revolving around whether the payout is considered a fair market value to the copyright owner. Services under the willing buyer/willing seller standard, on the other hand, are subject to "per performance" rates in order to reflect a static rate that is more representative of a hypothetical willing buyer and seller agreement.[150]

While the comparison of royalty rates between preexisting and post-1998 noninteractive services illustrates how the different goals underlying each standard can affect royalty rates, an even more enlightening comparison exists between mechanical licenses and public performance licenses—which will be addressed in the following sections.

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145 YEH, *supra* note 5, at 27. The purpose for these differing standards for public performance royalties from noninteractive services was "to prevent disruption of the existing operations by such services." *Id.* These services are analyzed together in the CRB's *Determination of Rates and Terms for Satellite Radio and "Preexisting" Subscription Services (SDARS)* proceedings. *See* Determination of Rates and Terms for Satellite Radio and "Preexisting" Subscription Services (SDARS III), 83 Fed. Reg. 65210 (Dec. 19, 2018).

146 17 U.S.C. § 114 (f)(2)(B). The rates for these services are analyzed together in the CRB's *Determination of Royalty Rates and Terms for Ephemeral Record and Digital Performance of Sound Recordings* ("Web determinations"). *See* Determination of Royalty Rates and Terms for Ephemeral Recording and Webcasting Digital Performance of Sound Recordings (Web IV), 81 Fed. Reg. 26316 (Copyright Royalty Bd. May 2, 2016) (to be codified at 37 C.F.R. pt. 380).

147 Determination of Rates and Terms for Satellite Radio and "Preexisting" Subscription Services (SDARS III), 83 Fed. Reg. at 65210.

148 *Copyright Royalty Judges Announce Determination on Rates in Web V Proceeding*, U.S. COPYRIGHT ROYALTY BD. (June 11, 2021), https://www.crb.gov/announcements/ [https://perma.cc/EPZ9-KGDK].

149 17 U.S.C. § 801(b)(1).

150 *See* Determination of Royalty Rates and Terms for Ephemeral Recording and Webcasting Digital Performance of Sound Recordings (Web IV), 81 Fed. Reg. at 26405 n. 237.

The application of the willing buyer/willing seller standard for noninteractive digital services in the CRB's web determinations provides the closest comparable market for analyzing the standard in terms of mechanical royalties.

B. *The Willing Buyer/Willing Seller Standard*

The willing buyer/willing seller standard that has been applied to noninteractive public performance royalties, and now applies to mechanical royalties, requires the CRB to "establish rates and terms that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller."[151] The Copyright Royalty Judges are to make their determinations under this standard based on "economic, competitive, and programming information presented by the parties," including the likelihood of substitution or promotion of sales, or any interference or enhancement of the copyright owners' revenue streams, as well as the roles of the stakeholders "with respect to the relative creative contribution, technological contribution, capital investment, cost, and risk."[152]

IV. THE FUTURE OF MECHANICAL ROYALTIES UNDER THE WILLING BUYER/WILLING SELLER STANDARD

This Section illustrates why this standard may be more difficult for the CRB to adequately apply to mechanical royalties compared to public performance royalties. At the very least, the first determinations using the standard for mechanical royalties are likely to be highly contested. After already establishing that mechanical royalty rates will be starting anew in Section II of this Note, this Section argues that the closest comparable determinations using the standard cannot provide an adequate comparison for the CRB because of the substantial differences between royalties making the comparisons that can be drawn from those markets too abstract. Subsection B then looks to web determinations' contentious history for a clue on how the standard operated for noninteractive public performance royalties when these determinations had no other market from which to draw. Now that mechanical royalties are in a similar position as noninteractive public performance royalties were when the willing buyer/willing seller standard was first adopted for web determinations, this history may provide insight in order to predict what is in store for *Phonorecords* determinations. Next, Subsection C briefly

[151] Orrin G. Hatch–Bob Goodlatte Music Modernization Act, Pub. L. No. 115–264, § 102(a)(3), 132 Stat. 3676 (2018); 17 U.S.C. § 114(f)(1)(B).
[152] 17 U.S.C. § 114(f)(1)(B)(i) (2016); Orrin G. Hatch–Bob Goodlatte Music Modernization Act § 102(a)(3).

outlines a few important differences that make mechanical licenses more complicated than noninteractive public performance licenses, which may lead to increased uncertainty and disagreement. Finally, Subsection D wraps up the findings of this Note and explores a potential lesson from this analysis.

A. *Comparisons Between the Standard as Applied to Public Performance Royalties and How It May Be Applied to Mechanical Royalties Are Limited*

While the language of the standard is interchangeable for web determinations and phonorecord determinations,[153] public performance licenses and mechanical licenses are far too dissimilar to extract and substitute the rates. As required under the standard, royalty rates must be established through hearings and analysis of "economic, competitive, and programming information presented by the parties."[154] While the standard may be the same, the differences in not only the rates, but also the parties involved and the uses of the songs demand extensive evaluation of the intricacies of each royalty stream in order to establish a rate representing a hypothetical willing buyer and willing seller negotiation.

To begin with the differences in rates, as previously mentioned, mechanical rates for physical phonorecords and permanent downloads are the greater of 9.1 cents per song or 1.75 cents per minute of playing time.[155] Interactive streaming and limited downloads are determined through a formula consisting of an all-in rate based on the individual services, rather than a flat rate.[156] The percent of revenue rate in 2018 was set at 11.4% and was determined to be increased each year until it would reach 15.1% in 2022.[157] While these rates are subject to change after the outcome in *Johnson v. Copyright Royalty Board*, they present a basic idea of the price points of mechanical licenses.[158]

The rates for public performance licenses on the other hand are much lower.[159] *Web V*, the most recent web determination, established

153 *Compare* 17 U.S.C. § 115(c)(3)(F), *with* 17 U.S.C. § 114(f)(1)(B).
154 Orrin G. Hatch–Bob Goodlatte Music Modernization Act § 102(c)(1)(F); 17 U.S.C. § 114(f)(2)(B).
155 *Mechanical License Royalty Rates*, *supra* note 44.
156 *Id.* For the formulas for determining rates for limited downloads and interactive streaming, *see* 37 C.F.R. §§ 385.10–385.17 (2014).
157 Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. 1918, 1918 (Copyright Royalty Bd. Feb. 5, 2019) (to be codified at 37 C.F.R. pt. 385).
158 Johnson v. Copyright Royalty Bd., 969 F.3d 363 (D.C. Cir. 2020).
159 *Copyright Royalty Judges Announce Determination on Rates in Web V Proceeding*, *supra* note 148. To clarify, the rates are lower for the public performance licenses than for mechanical licenses due to the value and other market conditions for each type of license. Given the trend of the 801(b)(1) standard creating lower rates than the willing buyer/willing seller standard, it may be

the per-play rate for commercial subscription noninteractive streaming services and commercial non-subscription, noninteractive streaming services as $0.0026 and $0.0021, respectively, for 2021, with an annual adjustment reflecting changes in the Consumer Price Index through the end of 2025.[160]

Taking a step back from these figures, simply consider the "willing buyers" and "willing sellers" for these two categories of music licenses. The sellers for statutory public performance licenses are sound recording owners (i.e., recording artists and record labels), who are represented by SoundExchange as a unified voice advocating for the best price for these copyright owners.[161] Since the statutory license only covers noninteractive digital services, the two main types of buyers are Internet radio services, such as SiriusXM, and noninteractive streaming services, such as Pandora.[162]

Due to the variety of uses that demand a mechanical license, *Phonorecord* proceedings involve a wider range of buyers and sellers. The primary group of sellers are the musical works' owners (i.e., songwriters and publishers). However, for purposes of CRB proceedings, the interests of these copyright owners are advocated by a variety of major music publishers, collective rights organizations, and trade associations.[163]

There is a heightened complexity to the types of buyers involved for mechanical royalties as well. For public performance royalties, the CRB's primary objective is to establish a rate based on the willing buyer/willing seller standard for noninteractive services.[164] While noninteractive services may differ in terms of platform layout and options for customization, the ultimate use of music through these services is the same—that is, a mode of digital music consumption in which the user cannot choose the songs on-demand but, rather, mimics traditional radio.[165] Mechanical royalties, on the other hand, come from a variety of sources which the CRB has categorized into three subparts for the purpose of determining royalty rates.[166] Subpart A includes reproductions

inferred that statutory public performance license royalties would be even lower if they were determined under the 801(b)(1) standard.

160 *Id.*

161 Pet. to Participate at 1, CRB Webcasting IV, 14-CRB-0001-WR (2016–2020), https://www.crb.gov/proceedings/14-CRB-0001/SX.pdf [https://perma.cc/M6KN-7PK8].

162 17 U.S.C. § 114; *Licensing 101*, *supra* note 72.

163 *See* Notice of Amended Participant List and Order for Further Proceedings, 16-CRB-0003-PR (U.S. Copyright Royalty Judges 2016), https://www.crb.gov/rate/16-CRB-0003-PR/orders/6-15-16-order-for-further-further-proceedings-mv2.0.pdf [https://perma.cc/8CAM-595D].

164 *See generally* Determination of Royalty Rates and Terms for Ephemeral Recording and Webcasting Digital Performance of Sound Recordings (Web IV), 81 Fed. Reg. at 26316 (Copyright Royalty Bd. May 2, 2016) (to be codified at 37 C.F.R. pt. 380).

165 *See Licensing 101*, *supra* note 72.

166 Determination of Royalty Rates and Terms for Making and Distributing Phonorecords

of musical works in physical form, digital form for permanent digital downloads, and musical works purchased for use as a ringtone.[167] Subpart B includes interactive streaming and limited downloads.[168] Subpart C "relates to limited offerings, mixed bundles, music bundles, paid locker services, and purchased content locker services."[169]

For traditional cover song use, any qualifying individuals or record companies under section 115 wishing to record and distribute a song would be buyers of a mechanical license for physical phonorecords and digital downloads under Subpart A.[170] Buyers under Subparts B and C include all companies that are or own interactive streaming services such as Amazon, Apple, Google, and Spotify.[171] The broader range of uses that require a mechanical license, and higher numbers of buyers that engage in those uses, complicate the rate-setting process. While the different uses are assigned separate rates to reflect the market for the type of use, they nevertheless raise additional intricacies in phonorecord proceedings and potential for subsequent disputes to phonorecord determinations.

Since CRB proceedings are extremely involved and rely heavily on the arguments and evidence posed by the parties, the CRB is highly restricted in its ability to transfer one application of the standard to factor in for determinations of another. Due to the weight of the individualized party hearings and any relevant voluntary settlements, one could not speculate on what the royalty rate will ultimately be under the willing buyer/willing seller standard. As discussed in section IV.B, a conclusion that can be made, however, is that given web determinations' history in using the standard, mechanical royalty rates under the standard will be highly contested for years to come.

B. *The Contentious History of the CRB's Webcaster Determinations*

There has been a long history of adversarial decisions for public performance royalties under the willing buyer/willing seller standard. In the first web proceeding (*Web I*), the CARP was faced with establishing a rate under the willing buyer/willing seller standard without prior determinations to refer to or good faith, voluntary agreements absent of influence from the statutory licensing scheme.[172] Music rights owners and webcasters both focused their efforts in establishing favorable rates

(Phonorecords III), 84 Fed. Reg. 1918, 1919 (Copyright Royalty Bd. Feb. 5, 2019) (to be codified at 37 C.F.R. pt. 385).

167 *Id.*

168 *Id.*

169 *Id.*

170 17 U.S.C. § 115(a)(1).

171 Notice of Amended Participant List and Order for Further Proceedings, *supra* note 163, at Exhibit A.

172 Peter DiCola & Matthew Sag, *An Information-Gathering Approach to Copyright Policy*, 34 CARDOZO L. REV. 173, 226 (2012).

through the arbitration proceedings rather than concern themselves with negotiations, leaving "the CARP with the unenviable task of ascertaining what a willing webcaster and a willing record label would consider to be a fair deal for Internet radio royalties in the face of an almost total absence of real world evidence."[173] This clearly presents difficulties for the CARP, but this reliance on and belief in a statutory rate being decided in one's favor ultimately leads to dashed hopes and expectations on at least one, but often both of the sides subject to the determined rates.

In *Beethoven.com LLC v. Librarian of Congress*, copyright owners sued over the determination of *Web I*, alleging that the CARP's rates were determined arbitrarily.[174] The D.C. Circuit Court did find, however, under an "extremely deferential review," that despite the lack of consideration to a few past agreements on record, there were plausible explanations for the rates and upheld the CARP's decision.[175]

While the copyright owners' claims did not prevail in court,[176] small webcasters succeeded on the claim that the CARP's single-rate decision for all webcasters was unfair, leading to the enactment of the Small Webcaster Settlement Act of 2002 (the "SWSA").[177] The SWSA provided small and noncommercial webcasters with an opportunity to negotiate for reduced fees.[178] Then, due to concerns with the CARP's operation, the Copyright Royalty and Distribution Reform Act of 2004 was enacted.[179] The Act abolished the CARP, replacing it with the CRB, in an attempt to restructure the clearly problematic rate-setting process.[180]

If the ultimate goal was to substantially minimize the necessity of the courts and Congress to step in after a royalty rate has been established, the creation of the CRB missed its mark. In making its determination in *Web II*, the CRB relied primarily on the CARP's decision in *Web I*, setting another single rate for commercial webcasters, regardless of their size.[181] These rates were found to be too high for small webcasting companies, again requiring intervention by Congress.[182] The Webcaster Settlement Act of 2008, which was essentially an expansion of the SWSA, was

173 *Id.*
174 Beethoven.com LLC v. Librarian of Cong., 394 F.3d 939, 942 (D.C. Cir. 2005).
175 *Id.* at 953.
176 *Id.* at 954.
177 *See* Bruce G. Joseph, Karyn K. Ablin & Matthew J. Astle, *Congress Passes Webcaster Settlement Act of 2008*, LEXOLOGY (Oct. 6, 2008), https://www.lexology.com/library/detail.aspx?g=47d4650a-c2ca-4671-954a-aad9b1908dc2 [https://perma.cc/2EM5-ZQRL].
178 *Id.*
179 DiCola & Sag, *supra* note 172, at 231–32.
180 *Id.* at 232.
181 Paul Musser, *The Internet Radio Equality Act: A Needed Substantive Cure for Webcasting Royalty Standards and Congressional Bargaining Chip*, 8 LOY. L. & TECH. ANN. 1, 23 (2008) (discussing the issue that small webcasters faced in trying to be recognized separately from large webcasters for the CRB's rate-setting process).
182 Joseph, Ablin & Astle, *supra* note 177.

passed in order to encourage private negotiation between webcasters and SoundExchange, rather than having to rely on the rates set by the CRB in *Web II*.[183]

Over the years, various suits were also brought regarding the rates that should be applied to particular services and challenges against the CRB's constitutionality.[184] In *Intercollegiate Broad System v. Copyright Royalty Board*, finding that the CRB's structure was unconstitutional under the Appointments Clause of the Constitution at the time it issued the determination for *Web II*, the Court of Appeals for the D.C. Circuit vacated and remanded the CRB's determination.[185] This decision was predicated on the finding that the CRB had "vast discretion over the determination of rates and terms, and apply ratemaking formulas that are hugely open ended" without proper procedures in place for removing these judges from such a position.[186]

Following this case, the CRB could not use its previous decisions as a benchmark and had to start anew in determining public performance royalty rates under the willing buyer/willing seller standard. The best information at its disposal were a few deals between SoundExchange, SiriusXM and the National Association of Broadcasters.[187] However, these deals heavily relied on the CRB's rate determination in *Web II*.[188] This means that while the CRB could use these direct public performance licensing deals, the underlying basis for these agreed upon rates relied on past statutory rates set by the CRB and were not in fact a product of a true willing buyer and a willing seller absent of influence by a statutory licensing scheme. In addition, the CRB found webcasters to differ enough from satellite and terrestrial radio as to make a comparison between those rates and *Web* rates impermissible.[189] While this was likely the right call, it further limited the scope of agreements that the CRB could consider in making its decision.

Despite the lessons that may have been learned from the previous three web determinations, the CRB's next web decision, *Web IV*, was yet again subject to contentious litigation. In *SoundExchange, Inc., v. Copyright Royalty Board*, SoundExchange claimed that the "proceedings

183 *Id.*
184 *See generally* Arista Records, LLC. V. Launch Media, Inc., 578 F.3d 148 (2d Cir. 2009); Live365, Inc. v. Copyright Royalty Bd., 698 F. Supp. 2d 25 (D.D.C. 2010).
185 Intercollegiate Broad Sys., Inc. v. Copyright Royalty Bd., 684 F.3d 1332, 1342 (D.C. Cir. 2012); s*ee also* DiCola & Sag, *supra* note 148, at 238.
186 *IP/Entertainment Case Law Updates: Intercollegiate Broadcasting Sys., Inc. v. Copyright Royalty Board, Library of Congress*, LOEB & LOEB LLP (July 6, 2012), https://www.loeb.com/en/insights/publications/2012/07/intercollegiate-broadcasting-sys-inc-v-copyright__ [https://perma.cc/8QK3-FT9M%5d].
187 DiCola & Sag, *supra* note 172, at 239.
188 *Id.*
189 *Id.*

d[id] not reflect a fair market price for music and w[ould] erode the value of music in our economy."[190] SoundExchange challenged the market evidence that the CRB chose to rely on and its decision in setting different rates for different types of services as arbitrary and capricious.[191] SoundExchange argued that the Board's selection of benchmark agreements used to determine the per-performance rate was "flawed" and that the Board "arbitrarily ignored how the statutory license generally prevents parties from negotiating rates above the statutory royalty."[192] The court ultimately rejected these claims and upheld the decision of the CRB.[193]

Regardless of the success of these claims, when viewing this history it becomes evident how highly contestable the determinations remain despite years of having the standard in place. Whether the rate-setting board has voluntary agreements or refers to a previous determination, the pattern of appeals indicates the failure of each decision in achieving a rate upon which buyers and sellers can agree.

Based on the history of difficulties in applying the standard for noninteractive public performance royalties, it can be inferred that phonorecord determinations will face similar difficulties. Web determinations were in a similar situation that phonorecord determinations are in now—i.e., the CRB was faced with determining rates de novo due to the inability to refer to previous determinations or depend on a pattern of voluntary agreements. What the history of web determinations and subsequent motions and appeals against those decisions has revealed is that mechanical royalty rates' problems are not going to be solved overnight with the switch to the willing buyer/willing seller standard. In theory, as the application of the willing buyer/willing seller standard is intended to produce a more accurate fair market value for mechanical licenses than the 801(b)(1) standard,[194] over time the determinations should inch closer to a less frequently contested rate structure.[195] The results of this theory, however, have not yet come to fruition for web determinations, despite nearly two decades of the willing buyer/willing seller standard being in place for noninteractive public performance royalties.

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190 *SoundExchange Statement on Web IV Appeal*, SOUNDEXCHANGE (May 31, 2016), https://www.soundexchange.com/news/soundexchange-statement-on-web-iv-appeal/ [https://perma.cc/V97F-VRT7].

191 SoundExchange, Inc., v. Copyright Royalty Bd., 904 F.3d 41, 49–50, 57–59 (D.C. Cir. 2018).

192 *Id.* at 50–51.

193 *Id.* at 62.

194 17 U.S.C. 801(b)(1).

195 *See* DiCola & Touve, *supra* note 4, at 415 (stating that the 801(b)(1) standard consistently results in lower rates that may not represent an agreement that would be made by willing market participants).

There appears to be no evidence of any reason why mechanical royalties will not confront similar difficulties. Parties to *Phonorecord* proceedings are in an almost identical situation as the parties to *Web I*. The introduction of the willing buyer/willing seller standard generates considerable uncertainty and unpredictability, allowing both sides to independently conjure up their own conclusions of what a willing buyer and willing seller agreement should look like without actually attempting to have such negotiations with the other side. As a result, any determination of rates will fail to live up to the optimistic desires of the parties, and the cycle of appeals will follow.

C. *Increased Difficulty in Standard Application to Mechanical Royalties*

Building upon the likelihood of mechanical royalties being subject to a highly contentious period where the CRB's decisions are made in a vacuum of knowledge and the parties are continuously fighting over the outcome, there are some additional factors to mechanical licenses that make establishing royalty rates perhaps even harder than rates for noninteractive public performance licenses.

An unsurprising factor, which has been touched on previously in this Note, is the wide range of different uses of a musical work that triggers the requirement of obtaining a mechanical license—i.e., cover songs on physical and digital formats, ringtones, interactive streaming, permanent and limited downloads, and music bundles.[196] These differing revenue streams, each with distinguishable uses for the musical work, must all be taken into account. This added complexity provides an increase in potential points of dispute compared to the relatively similar noninteractive uses by webcasters for statutory public performance licenses. Since mechanical licenses are required whenever a song is copied and distributed, plus the fact that new and old methods of music consumption may coexist within the same market, the CRB has a broad scope of services to consider in making its determination for mechanical royalties.[197] These different avenues for music consumption, subsisting of drastically different offerings and technologies, add layers to the application of the standard—far more than those of public performance's different noninteractive services.

For streaming services specifically, a broader range of opportunities for users to interact with the service and customize their profiles may also complicate the rate-setting process. While noninteractive services still

196 *See* Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. 1918, 1919 (Copyright Royalty Bd. Feb. 5, 2019) (to be codified at 37 C.F.R. pt. 385).

197 DiCola & Touve, *supra* note 4, at 422–23 (explaining how, in the music industry, competing "new and old technologies come to coexist").

compete in expanding user personalization on their platforms,[198] ultimately the nature of interactive streaming allows services to provide a wider range of offerings for user interaction and account customization. These substantial differences in offerings sets interactive streaming services farther apart from their direct competitors than noninteractive services. The wider the range of offerings provided by services, the harder it may become for the CRB to set uniform percentages for calculating the royalty rates. While this is not a new issue presented by interactive streaming services, since the CRB is now in the position of having to set the next rate de novo, this existing complication suggests an additional hurdle for the next *Phonorecords* determination.

In a similar vein, the ever-changing nature of interactive streaming technologies have the potential to render royalty decisions outdated far faster than noninteractive services. The five-year rate period set by the CRB is seemingly short, but with the rate of innovation in streaming technologies, five years is a considerable amount of time.[199] Copyright legislation has attempted to strike a balance by providing broad rights to include future innovations as well as specific legislation for existing technologies.[200] However, while Congress may attempt to encompass some future technologies, the CRB is much less likely to entertain hypotheticals about the future without tangible evidence presented by the parties.[201] The result is that the CRB will largely establish rates based on the current offerings of the services. By the time of the next proceeding, interactive streaming technology would likely have advanced substantially within those five years, requiring a bigger change between the new and previous rate than for noninteractive services that do not change offerings as drastically. These more dramatic increases carry the escalated potential of appeals to the determinations.

D. *Findings and Lesson Learned*

There is little argument against the notion that the willing buyer/willing seller standard is an improvement upon the original 801(b)(1) standard for music creators.[202] Nevertheless, this change should

198 *See Recommendations and Personalization on Pandora*, PANDORA HELP, https://help.pandora.com/s/article/000001078?language=en_US [https://perma.cc/GW4M-LFET]; *see also Your Weekly Mixtape—A New Personalized Playlist Every Week Just for You*, IHEARTRADIO BLOG (July 30, 2018), https://blog.iheart.com/post/your-weekly-mixtape-new-personalized-playlist-every-week-just-you [https://perma.cc/339Q-45QC].

199 *See* Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. at 1919 (explaining that section 115 royalties are determined every fifth year).

200 DiCola & Touve, *supra* note 4, at 405.

201 *See* Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III), 84 Fed. Reg. at 1966, 1991–92.

202 17 U.S.C. 801(b)(1).

not be viewed as the end-all solution for compulsory mechanical licenses' royalty issues. Since the statutory public performance license for sound recordings on noninteractive services was created, determinations under the willing buyer/willing seller standard have continuously resulted in dispute and contention.[203] If the history of web determinations shows anything, it shows that the transition to the willing buyer/willing seller standard will not be a simple one. Based on nearly two decades of disputed web determinations under the willing buyer/willing seller standard, even when the standard is no longer new as applied to mechanical royalties, it is highly improbable that determining these rates will no longer be a quarrelsome endeavor. The ultimate outcome of these findings is clear: until an application of the standard is more settled, presumably through more than one determination of mechanical royalty rates and any subsequent appeals to these decisions, mechanical royalties under the willing buyer/willing seller standard will be determined in a vacuum of knowledge and will likely be subject to a highly contentious period in which there will be a back and forth between the CRB, the interested parties, and the courts.

If there is any lesson to be learned from this less-than-optimistic prediction it is this: while the CRB may be in a vacuum of knowledge, the parties do not have to be. If the buyers and sellers of mechanical licenses treat this situation as a blank slate opportunity to negotiate as true willing market participants, these freely negotiated deals can be used as a base for the CRB's next determination. The primary issue with statutory rates is that the parties rely too heavily on the established rate, stifling the negotiation process that is so vital for real exchanges between willing buyers and sellers. Both the buyers and the sellers should take this opportunity to negotiate the best deal for themselves before the standard is more stable and it becomes harder to go against the established rate. It would be reckless for either side to assume that the CRB will be persuaded by a party's independent vision of a hypothetical willing buyer and willing seller agreement. It was precisely this type of thinking that created the ongoing struggle seen in the history of the web determinations. While engaging in these negotiations will not solve every issue, avoiding this previous mindset and making bona fide attempts to reach voluntary agreements as early on as possible presents the best path for the future of mechanical licenses.

V. CONCLUSION

Due to the lack of voluntary agreements without the influence of a statutory licensing scheme and the absence of an actual comparable

[203] DiCola & Sag, *supra* note 172, at 224–36.

market through public performance licenses, the first determinations of mechanical royalty rates under the willing buyer/willing seller standard will take place in a vacuum of knowledge. While it is expected that the change in standard will result in higher royalty rates for mechanical licenses, the magnitude of the shift remains unclear.

While the switch to the willing buyer/willing seller standard in the MMA was a result of music industry stakeholders coming together to improve music law and diminish disputes, the parties undoubtedly will have differing views of what a fair market value looks like.[204] It would behoove music industry stakeholders, however, if such disagreements were brought in the form of bona fide negotiations rather than in subsequent appeals to future phonorecord determinations. By viewing this change in standard as a clean slate opportunity for negotiations, the buyers and sellers of mechanical rights would have enormous power to shape future statutory royalty rates under the willing buyer/willing seller standard. The fewer voluntary agreements for the CRB to consider, the harder it will be to establish a fair market value and the less likely it will be that phonorecord determinations will receive broad acceptance by the parties.

It should be expected that even with evidence of new voluntary agreements for the CRB to consider, the willing buyer/willing seller standard will still experience some growing pains in its first applications to mechanical licenses. However, only time will tell whether phonorecord determinations under the willing buyer/willing seller standard will eventually be accepted by stakeholders as the fair market value for mechanical licenses or, instead, the contentious history of noninteractive public performance licenses will be replicated.

Natalie Linn[*]

[204] Octavious A. Buiey, Jr., *Copyright's Facelift: An Analysis of the New Look of Copyright Following the Music Modernization Act and the United States-Mexico-Canada Agreement*, 51 U. MIAMI INTER- AM. L. REV. 217, 236–37 (2019) (noting the Copyright Office's statement about the MMA's expected benefit for a wide range of stakeholders in the music industry).

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