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U.S. House of Representatives Committee on the Judiciary
Subcommittee on Courts, Intellectual Property, and the Internet

Hearing on Music Licensing Under Title 17

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Chairman Goodlatte, Chairman Coble, Ranking Members Conyers and Nadler, and Members of the Subcommittee:

My name is David J. Frear. I am the Executive Vice President and Chief Financial Officer for Sirius XM Holdings Inc. ("Sirius XM"), a position I have held since 2002. On behalf of Sirius XM, I thank you for the opportunity to offer testimony to the Subcommittee.

Sirius XM, with an estimated 40 million listeners, is one of the largest radio providers in the United States. We employ over 2,100 people at our facilities in New York, Washington, DC, Florida, New Jersey, Texas and California. Since our inception, we have operated pursuant to licenses from ASCAP, BMI, and SESAC for the public performance of musical compositions, and we operate under the Section 112 and 114 statutory licenses with respect to the public performance of sound recordings. We have also fully litigated two rate-setting proceedings before the Copyright Royalty Board.

In 2013 alone, we paid approximately $325 million to record companies, publishers, song writers, and recording artists. We have paid well over $1 billion in sound recording performance royalties since we launched in late 2001.

This experience has provided us with great insight into the issues before the Subcommittee, including what works and what does not work within the music licensing market as currently structured. My testimony, builds on that experience – as well as similar comments Sirius XM recently submitted to the Copyright Office as part of its music licensing inquiry – and centers on four key points:

1. **<u>The Need for Platform Parity</u>**: There is no reason that satellite radio and Internet radio should pay sound recording performance royalties while terrestrial radio continues to enjoy an exemption from that obligation.

2. **<u>The Importance of the 801(b) Rate-Setting Standard</u>**: The 801(b) standard provides the Copyright Royalty Judges with both the ability to examine potentially relevant marketplace transactions and the flexibility to balance the interests of both the copyright owners and licensees. The 801(b) standard has proven far superior to the "willing buyer willing seller" standard championed by the rights-owner community. It should be maintained.

3. **The Continued Necessity of the Consent Decrees Governing ASCAP and BMI**: The antitrust consent decrees are not outdated "relics" that prevent competition or copyright owners achieving fair market value for their works, but a necessary antidote to the extreme concentration that persists in the market and would, absent the decrees, violate the antitrust laws. In short, they help *ensure* that rates are set fairly.

3. **The Significant Problems with the Proposed RESPECT Act for Pre-1972 Sound Recordings**: The proposed act would further exacerbate the irrational disparity between digital services and terrestrial radio (which would remain exempt from paying performance royalties for *any* recordings), create a new payment obligation on a narrow set of licensees, and bestow a one-sided windfall on owners of recordings created 70 or 80 years ago, without advancing in the least the foundational purpose of copyright law: providing an incentive for the creation of new recordings.

As may be evident, a common-theme pervades my comments. In statement after statement, copyright owners suggest that the current regulatory framework – including the statutory licenses, the 801(b) rate-setting standard and the antitrust consent decrees – artificially interferes with the normal working of a free and competitive market. The unmistakable tenor of the conversation is that copyright owners are being unfairly forced to subsidize licensees with below-market rates. But these sorts of comments conveniently overlook the reality on the ground in the music licensing marketplace.

On the publishing side, for example, we confront two collectives (ASCAP and BMI) that each control distinct repertories approaching 50% of the market, and a third (SESAC) that, while smaller, makes outrageous fee demands under threat of statutory infringement claims while refusing to identify the works it is licensing. On the record-label side, we see three major labels that likewise control distinct repertories ranging from 20% to nearly 40% of the market each – and over 85% collectively. These entities control separate catalogs of works that are not substitutes for one another. They do not compete with one another as that term is typically understood. A "free" market in licensing – if by that term one means giving copyright owners free rein to exploit the market power they enjoy by having amassed massive repertories of works – would be neither fair nor competitive, but be plagued by rates approaching monopoly levels.

By contrast, the regulatory framework that has developed over the years, rather than forestalling competition or preventing copyright owners from achieving fair market value, helps to achieve the opposite result: ensuring that rates paid by entities like Sirius XM are at least somewhat insulated from the incredible market concentration that would otherwise push them to monopoly levels.

My comments below provide additional detail on these points.

I. Platform Parity Is Vital

As the Subcommittee no doubt is aware, music services in the U.S. operate under a patchwork of statutes, rules, and regulations that distinguish audio entertainment services based upon the mechanism or medium of delivery. This framework is the product of historical compromises and trade-offs between interested parties that no longer make sense and, as many participants noted in the June 10th hearing before the Subcommittee, it is a framework that no one would readily choose again today.

The current framework exempts traditional "terrestrial" radio from the obligation to pay performance royalties to sound recording owners, while requiring other radio services that offer essentially the same service to make such payments. Further, drawing any distinction based on the claim that some services transmit digitally while others do not is nonsensical: terrestrial radio began broadcasting digital signals over a decade ago and has made use of digital copies of sound recordings to further their broadcasts for 30 years. It is antiquated, inequitable, and simply bad public policy to reward the biggest entities in the radio field with a competitive cost advantage while penalizing innovators whose services increase economic activity and create jobs.

To start, similar services – regardless of the mechanism or medium through which they are delivered – should be treated similarly. Copyright law does not distinguish between AM and FM radio based on technology, and should not distinguish between terrestrial and satellite radio, or terrestrial and Internet radio, either. The playing field – that is to say, the requirement that performance royalties be paid, and the standard under which royalty rates are set – should be leveled for all participants in the radio market. In short, "radio is radio," regardless of whether it is AM/FM radio, HD radio, satellite radio, cable radio or Internet radio. *See, e.g.*, *In re Petition of Pandora Media, Inc.*, No. 12 Civ. 8035 (DLC), at 14 (S.D.N.Y. Mar. 18, 2014) (Opinion & Order) (explaining that the "radio experience has remained constant through the years, regardless of whether radio programming is transmitted by broadcasting, through a cable, from a satellite, or over the internet").[1]

Continuing the distinctions between various forms of radio established in 17 U.S.C. § 114 – whereby AM/FM radio is exempted from any sound recording performance right obligation, while satellite, Internet, and other audio services (including simulcasts of those very same AM/FM broadcasts) are not – is bad and unjustified policy. Chiefly, it has the effect of subsidizing the largest entities in the industry – the $15 billion/year AM/FM radio station market – and is exactly the opposite of what the public would expect: accommodations to *new* entrants to encourage growth and entrepreneurship. Such a policy punishes digital pioneers with massive royalty obligations not borne by their established and entrenched competitor. For example, Sirius XM, despite enjoying a subscriber base of nearly 25 million, went 18 years until it achieved profitability in 2010 – and then only after running up cumulative net operating losses of $8 billion, merging the two predecessor companies, and narrowly surviving two brushes with bankruptcy. At the same time, it paid well over $1 billion in royalty payments to the recording industry, while AM/FM radio stations paid precisely *zero*.

[1] We do not mean to suggest by this that all services should pay the exact same fees, but rather that similar services should have their fees set pursuant to the same rate-setting standard and process. As we discuss below, the 801(b) rate-setting standard provides the Copyright Royalty Judges with the necessary and appropriate latitude to account for variations between particular services or service categories in the rate-setting process.

That sort of inequity hampers innovation and job creation. While Sirius XM survived, and while most AM/FM stations continue to offer some form of simulcast, one need only survey the graveyard of services that have tried and failed to establish viable standalone digital radio businesses (including major companies like Yahoo! and AOL) to see the depth of the problem. Winners and losers in the audio entertainment field should be selected by the market on the basis of innovation and the entertainment and other value they provide to consumers, not historical anomalies or cost-side inequities created by statute.

II. The Importance of the 801(b) Rate-Setting Standard

Copyright owners have stated that 17 U.S.C. § 801(b) provides an artificial subsidy to services and suggested that the "willing buyer-willing seller" (WBWS) standard be applied to all Section 114 licenses, or that the 801(b) standard be altered, for example by removing the "disruption" factor found at 801(b)(1)(D). They are wrong.

To start, it is important to highlight the continuing importance of the statutory licenses for national services using thousands (or tens of thousands) of sound recordings. Negotiating with each and every copyright owner would be extremely difficult and costly for at least two reasons. First, any service would need to be able to identify and then negotiate with the copyright owners of hundreds of thousands (or even millions) of songs. Second, the service would be forced to confront a record industry that has become incredibly concentrated, with three majors (and the smaller independent labels distributed by the majors) accounting for over 85% of the market. This concentration provides those record companies with tremendous negotiating leverage, as each major is a "must have" that many services cannot do without.

For similar reasons, the 801(b) standard should be retained as written. Copyright owners blithely characterize the 801(b) standard as devoid of marketplace considerations. But the 801(b) standard requires the Judges set rates that are "reasonable," and in prior proceedings the Judges have started their rate-setting analyses under that standard by first identifying a "zone of reasonableness" defined by *market* benchmarks, and only then using the 801(b) policy factors to identify a rate *within* the *marketplace* range.[2] Moreover, as the economists who have testified on behalf of the industry have argued repeatedly to the Judges, the 801(b) factors – such as the goals of ensuring a fair return and fair income for the parties, and recognizing their "relative contributions" – are those that parties to a *marketplace* transaction would themselves consider. The 801(b) standard thus allows the Judges to consider *marketplace* benchmarks and considerations as part of their determinations, but also provides the Judges with the latitude and flexibility to consider the enumerated policy factors (for example, in the *Satellite I* proceeding, the disruption that Sirius XM would suffer at the rates proposed by SoundExchange, as well as Sirius XM's need to spend hundreds of millions of dollars in satellite-related expenditures).

[2] That approach has been blessed by the D.C. Circuit. *See Recording Indus. Ass'n of America, Inc. v. Librarian of Cong.*, 608 F.3d 861, 865 (D.C. Cir. 2010). *See also* 17 U.S.C. § 114(f)(1)(B) (specifying that "the Copyright Royalty Judges may consider the rates and terms for comparable types of subscription digital audio transmission services and comparable circumstances under voluntary license agreements").

The WBWS standard, by comparison, has proven to be a failure. In the absence of marketplace benchmarks involving non-interactive services, the Judges have been forced to rely on agreements between record companies and completely different categories of music users (*e.g.*, interactive services) and adjust them for application to non-interactive services – an inexact science at best, and one that causes the Judges to apply all manner of imprecise "interactivity" and other adjustments. In the wake of the *Webcasting II* decision, Congress was compelled to enact two Webcaster Settlement Acts to allow the record industry and various services to negotiate "voluntary" agreements (the so-called "WSA" deals) at rates other than those set by the Judges, which would have bankrupted most services. By the time of the *Webcasting III* proceeding, some 95% of the market was operating under such agreements (*i.e.*, <u>not</u> operating under rates set according to the WBWS standard), and only one commercial service of any size participated in the proceeding. Meanwhile, the three largest providers (Yahoo!, AOL, and Microsoft) all exited the market.[3] In contrast, the decisions pursuant to the 801(b) standard have not resulted in the participants rushing to Congress for legislative relief.

Retention of the 801(b) standard is justified not only because it is fundamentally superior to the WBWS standard, but also as a matter of simple fairness. Congress implemented (and later retained) that standard in recognition that services subject to those standards founded their services at a time when there was no sound recording performance right at all. To change the standard now would fundamentally undercut the reliance interests of those services.

To those who would argue that anything other than a free-market standard amounts to a perversion of their property rights and an unfair subsidy from the recording industry to the digital services, it must be remembered that the statutory license was an integral part of the bargain reflected in the Digital Performance Right Act in 1995. Namely, sound recording record companies were provided with a digital audio transmission right against non-interactive services only on the condition that such services (who were being hit with a new royalty not borne by terrestrial radio) have access to a statutory license[4] -- and, in the case of satellite radio, the 801(b)(1) rate-setting standard. Sound recording owners present their right to public performance royalties as a given, and the statutory license as a burden on that right; but that position fails to recognize that the statutory license was the *price* for receiving the performance

[3] Similar problems plagued the satellite television market. After Congress shifted the Section 119 compulsory license to a "fair market value" standard in the Satellite Home Viewer Act of 1994, the rate increase implemented by the CARP was so drastic that Congress was compelled, in the Satellite Home Viewer Improvement Act of 1999, to slash rates by 45%. *See* Register of Copyrights, Satellite Home Viewer Extension and Reauthorization Act § 110 Report, at 8-11 (Feb. 2006).

[4] This is compared to the interactive services – the providers of the so-called "celestial jukebox" – which Congress feared would substitute for CD sales and which drove the legislation. Sound recording owners, who had never enjoyed a public performance right in the U.S., received a full digital performance right as against on-demand streamers, but not as against non-interactive services that were not viewed as creating the same threat of substitution. Several CARP and CRB proceedings have lent further support to this distinction, as the record industry has failed to present any credible evidence that non-interactive services substitute for record sales.

right in the first place. *See* H.R. Rep. 104-274, at 14 (describing need for "balance" among interests and resulting "limitations" on the performance right, including the statutory license).

III. The ASCAP and BMI Antitrust Consent Decrees

Sirius XM operates pursuant to blanket licenses from ASCAP, BMI, and SESAC covering the public performance of musical works. In our experience, the ASCAP and BMI consent decrees and the licensing process that they mandate work relatively well. As a result of the mandatory license requirement, Sirius XM is assured that it has license coverage for the full repertories without needing to contact and negotiate with every single songwriter and publisher featured on its service. Each side has the opportunity to pursue rate-court litigation if it feels the other side is being unreasonable. Despite that possibility (or likely because of it), Sirius XM has enjoyed relatively amicable negotiations with each of ASCAP and BMI over the past decade, and has not needed to litigate. The publishing community, for its part, has received hundreds of millions of dollars in royalty payments from Sirius XM.

The recent trends in this area, however, are disturbing. The first such trend is the publishers' increasingly strident suggestions, in the press and on Capitol Hill, that the consent decrees are a relic of the past that should simply be dispensed with. Changing times, however, do not change the facts. As noted in the introduction, ASCAP and BMI collectively represent close to 50% of the market each – and a *distinct* 50%. A music service like Sirius XM must take a license from each of those entities to operate effectively – they are not substitutes for one another. ASCAP and BMI do not compete against one another on price, as one would expect to find in a typical "competitive" market – *i.e.*, Sirius XM can't tell ASCAP that if it doesn't lower its price, we will purchase the rights we need from BMI instead. As is obvious, this gives each organization a tremendous amount of market power over licensees who need a license from each to operate a successful service.

As a result, what was true in the 1940s when the consent decrees were adopted, and reiterated throughout the decades, remains just as true now: the PROs' blanket licensing practices are "inherently anti-competitive," reflecting their exercise of "disproportionate power over the market for music rights." *United States v. Broad. Music, Inc. (In re Application of Music Choice),* 426 F.3d 91, 93, 96 (2d Cir. 2005); *see also United States v. ASCAP (In re Application of RealNetworks, Inc.*), 627 F.3d 64, 76 (2d Cir. 2010) (explaining that "ASCAP, as a monopolist, exercise[s] disproportionate power over the market for music rights") (alteration in original) (citation and internal quotation omitted).

While the efficiencies of the blanket licenses and one-stop shopping may justify the PROs' existence, the consent decrees are crucial to protecting against the inevitably non-competitive rate demands (and the ability to shut a service down that does not accede to those demands) that result when publishers are allowed to negotiate collectively. Put simply: a "free" market in this context – i.e., one where publishers are given free rein to negotiate collectively and wield their market power without constraint – would be neither "fair" nor competitive" as the copyright owners like to suggest. The consent decrees do not interfere with competition; they prevent activities that would otherwise constitute clear violations of the antitrust laws.

The existence of national music services playing tens of thousands of songs in reliance on blanket licenses makes the consent decrees all the *more* necessary. Given the practical impossibility of a service identifying and negotiating privately with every copyright owner featured in its programming – ASCAP alone purports to represent over 500,000 songwriters and publishers, while services such as Spotify (to give just one example) advertise libraries of millions of tracks – a music service could face dramatic exposure to infringement liability (and statutory damages) absent the compulsory licensing mechanism of the consent decrees.

Sirius XM's own experience with SESAC (which, unlike ASCAP and BMI, is not bound by a consent decree) drives home the importance of the consent decrees. In prior negotiations with Sirius XM, SESAC has demanded oversized fees that are totally unsupported by the information available regarding its catalogue, and always with the implicit threat of infringement liability. At the same time, it has refused to identify its catalogue of musical works, meaning that Sirius XM cannot (as it could with a single copyright holder) simply remove the tracks at issue from its service. This combination of concentrated ownership and either an unwillingness or inability to be transparent as to what works are actually in the repertory creates a completely untenable situation.[5]

Such anti-competitive concerns have been exacerbated by recent attempts by publishers to withdraw from ASCAP and BMI. As detailed by Judge Cote from the record of the ASCAP-Pandora litigation, publishers that control hundreds or thousands of smaller catalogues (and millions of songs) under one licensing umbrella – making them effectively private PROs five or ten times the size of SESAC – have (a) insisted on the ability to partially withdraw from ASCAP; (b) made exorbitant fee demands, under the threat of litigation, to force direct licenses on services who no longer have access to those publishers' works via the PROs; and (c) refused to provide catalog data that would allow the targeted service to diminish or stop performing the works of those publishers absent a more reasonable fee demand.

To the extent PRO withdrawals become a regular feature of the music licensing landscape, complete transparency with respect to copyright ownership – *i.e.*, what exactly is in the catalogues of each publisher – is an absolute must. Congress should insist on a comprehensive, up-to-date public database of musical work and sound recording ownership information that is available freely to all potential licensees. Second, licensees should enjoy a safe harbor from statutory infringement exposure for copyright owners in such situations who fail properly to identify their works and allow reasonable and sufficient time to remove them from the service's servers and playlists. It is a travesty that a company can assemble millions of copyrights under a single licensing umbrella, insist on an exorbitant fee, but then not tell the licensee which copyrights it is forcing the service to license or stop playing.

IV. Pre-72 Recordings

Sirius XM has been the target of a spate of recent lawsuits regarding its use of sound recordings fixed before February 5, 1972 ("Pre-72 Recordings"). Three suits involve a putative

[5] Judge Engelmayer recognized this exact problem in his recent summary judgment ruling in the television broadcasters' case against SESAC. *Meredith Corp., et al. v. SESAC, LLC*, No. 09 Civ. 9177 (PAE), 2014 WL 812795 (S.D.N.Y. Mar. 3, 2014).

class of record companies suing Sirius XM in California, Florida, and New York seeking damages and license fees under the law of those three states. A fourth suit involves the major record companies and ABKCO (coordinated by the Recording Industry Association of America) suing Sirius XM in California for damages and license fees pursuant to California law. Those same Plaintiffs have also sued Pandora in state court in New York.

Simultaneous with these state-law cases, SoundExchange – the entity that collects and distributes royalties for copyrighted (*i.e.*, "Post-72") recordings pursuant to the statutory licenses found at Sections 112 and 114 of the Copyright Act -- has sued Sirius XM in the District of Columbia for failure to pay for the same performances of Pre-72 Recordings under the *federal* statutory license. SoundExchange has also lobbied for introduction of the RESPECT Act, which would force statutory licensees like Sirius XM and Pandora to pay for performances of Pre-72 Recordings under the (federal) statutory license.

Respectfully, the RESPECT Act is riddled with problems.

First, and worst, by adding a new royalty obligation solely to digital services that currently pay for performances of Post-72 recordings under the federal statutory license, it only further exacerbates the above-described disparity between other audio services and terrestrial radio stations, which would continue to be exempted from performance royalties, not only for Post-72 recordings, but for Pre-72 Recordings as well.

Second, the bill as drafted does not actually grant federal copyright protection to Pre-72 Recordings: it simply forces statutory licensees paying for Post-72 recordings to pay royalties for Pre-72 Recordings as well, without creating any underlying entitlement to such payments.[6] The bill thus effectively exempts Pre-72 Recordings from the limits that typically apply to works covered by the Copyright Act: for example, the need to register works prior to litigation; a limited term of protection; the "Homestyle" exemption at Section 110 (which shelters small business establishments and religious facilities from public performance liability); and, significantly, the DMCA safe harbors at Section 512 (which protect Internet services from infringement liability if they respond promptly to takedown notices from copyright owners). These limitations are crucial to the purposes of the Copyright Act, which seeks to strike a balance between copyright owners and the interest of the public in gaining access to copyrighted works. Owners of Pre-72 Recording should not gain the benefits of copyright protection (royalty payments under Section 114) without being subject to these important limits.[7]

[6] To the extent the Act is predicated on a purported state-law performance right in sound recordings, no such right exists. After months of litigation in three different states, the record companies have failed to demonstrate that such a right exists in those states, much less in the 47 states in which no such litigation is taking place.

[7] The music industry has fought tooth and nail to deny the Section 512 safe harbor to services that offer Pre-72 Recordings – and succeeded – on the ground that a federal statute cannot shelter infringements of non-federally-copyrighted works. (See, for example, the *UMG Recordings v. Escape Media* case in New York). And the RIAA came out strongly *against* the federalization of Pre-72 Recordings in response to a recent Copyright Office inquiry on the subject, no doubt hoping to avoid the limitations in the Act. They cannot have it both ways.

More generally, the RESPECT Act does not serve the fundamental purpose of the Copyright Act: to serve the public interest by providing only the protection necessary to incentivize the creation of works in the first instance before allowing them pass into the public domain.[8] Demanding a new and retroactive royalty obligation for recordings created 45 or more years ago will not, and by definition cannot, serve that purpose. Clearly, the protections that existed prior to 1972, which did not include the prospect of performance-related income, were more than sufficient to prompt the creation of such recordings. And no doubt the same was true of the period between 1972 and 1995, where there continued to be no public performance right – and millions of sound recordings created nonetheless.[9] Absent any public performance right, recording artists continued to make recordings, expected that radio stations would play them, and in fact encouraged radio to do so because they knew it would help them sell even more records.

In short, demanding payment now for what radio has never, in 100 years, had to pay for will merely create a windfall that the artists did not expect when they created the works. Sirius XM, by contrast, will be confronted with tens of millions of dollars in a new, unforeseen, and significant payment obligation that was *not* part of the rights framework in place when it started its business – money that will no longer be available for improving our products and services, innovating, or hiring new employees.

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In conclusion, I would like to thank the members of the Subcommittee once again for the opportunity to submit this testimony. Sirius XM stands ready to provide any additional information or testimony that the Subcommittee would find helpful as it continues its consideration of these important issues. It is crucial that all participants in the music industry

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[8] The Court of Appeals for the Second Circuit reiterated these basic principles just this week: "As the Supreme Court has explained, the overriding purpose of copyright is to promote the Progress of Science and useful Arts. . . . In short, our law recognizes that copyright is not an inevitable, divine, or natural right that confers on authors the absolute ownership of the creations. It is designed rather to stimulate activity and progress in the arts for the intellectual enrichment of the public." *Authors Guild, Inc., et al. v. HathiTrust, et al.,* No. 12-4547-cv, at 10-11 (2d Cir. June 10, 2014) (internal quotations and citations removed).

[9] The Sound Recording Act of 1971 was passed by Congress specifically to remedy the specific problem of record piracy, which was forbidden by laws in certain state laws but not in others. Congress thus intentionally withheld a public performance right, which it recognized had never existed at the state level (clearly radio stations were not paying performance royalties, and never had). Notably, the 1971 Act also bestowed federal reproduction and distribution rights solely to those recordings created *after* enactment on February 15, 1972. The effect of this was that once the Act was passed, recordings created *even a few months earlier* were left completely unprotected as to public performance rights, and unprotected with respect to unauthorized reproduction and distribution in states that had no record piracy laws. In light of this long history, the current complaints that Sirius XM and Pandora are acting unfairly or even "shamefully" by not paying performance royalties for pre-72 recordings ring hollow.

ecosystem – digital services as well as content creators – have a seat at the table as reforms are considered and debated.