

COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON COURTS, INTELLECTUAL PROPERTY AND THE INTERNET

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before the

United States of America House of Representatives

House Judiciary Committee
Subcommittee on Courts, Intellectual Property and the Internet
2138 Rayburn House Office Building
Washington, D.C. 20515

Hearing on:
Music Licensing Under Title 17, Part Two
2141 Rayburn House Office Building
10:00 AM
June 25, 2014

Chairman Coble and Ranking Member Nadler, and members of the subcommittee, thank you for inviting me to testify today on behalf of the small and medium sized businesses that make up the American Association of Independent Music (“A2IM”).

My name is Darius Van Arman and I am an elected member of the A2IM board of directors. A2IM is a 501(c)(6) not-for-profit trade organization representing a broad coalition of over 330 independently owned U.S. music labels. We are primarily American-owned small and medium-sized enterprises (SMEs) who directly support the American creative community. We are not only investors in creative enterprise, but our members either directly facilitate the creative process or are recording artists and songwriters themselves. Our community is a diverse community. We release music in all genres, we are based in all parts of the United States—from Florida to Indiana to Hawaii—and we come in all shapes and sizes. Some of our members have dozens of employees in multiple locations, some are very small shops with just a handful of employees, and some are just artists themselves who self-release their own music.

Being independent doesn’t mean being small. Independent labels release commercially successful hit records by artists such as Taylor Swift, Adele, Paul McCartney, Mumford & Sons, the Lumineers and Vampire Weekend, to name a few. According to Billboard Magazine—using Nielsen SoundScan data for 2013 and computing on the basis of copyright control or ownership—the independent music label sector now comprises 34.6% of the U.S. recorded music sales market. Looking at just digital sales or streaming figures using the same methodology, the independent market share figure is significantly higher, closer to 40%. Independents also currently release over 90 percent of all music released by music labels in the United States. We are not on the margins of the music industry; we are, together with the artist creators who we support, at the very vibrant core of it.

In addition to testifying as an A2IM board member, I also come here today as an entrepreneur. I founded the record label Jagjaguwar in 1996 out of my bedroom in Charlottesville, Virginia. Since then, I have become a co-owner in the labels Dead Oceans, Secretly Canadian and Numero Group. These four labels are now known as Secretly Group, we are headquartered in the Midwest of the United States (primarily in Bloomington, Indiana), and, together with affiliated companies SC Distribution, Fort William Artist Management and Secretly Canadian Publishing, we currently employ seventy U.S. employees. For the most part, our companies fund, release and champion new music by new artists, but we also re-release older works, investing to richly re-contextualize them when we do and always with an eye on spotlighting artists who have been overlooked or underappreciated. Although our companies have not invested in the insider games prevalent within the U.S. commercial radio world, we’ve achieved multiple gold albums and singles on the strength of our repertoire. Our recording artists have also achieved some of the highest accolades within the industry. For example, in 2012, Jagjaguwar recording artist Bon Iver won two Grammy Awards (for Best New Artist and Best Alternative Album), and, in

2014, Secretly Canadian recording artist Tig Notaro was nominated for a Grammy Award for Best Comedy Album. We are for-profit companies, with an eye on the bottom line and with the intent to grow our businesses and create job growth without any reliance on government subsidies or handouts. At the same time, the primary purpose of all of our companies from day one has been to make a deep and lasting cultural contribution. We exist to profitably invest our time and resources in the creative enterprises of artists in order to accomplish this purpose.

It should also be mentioned, as it will come up later in my testimony, that I am a non-voting observer on the board of Merlin, which is an international rights agency used by independent music companies to collectively license their repertoire to digital services.

This is my testimony on the state of music licensing today in the United States, and it reflects my views, the views of AZIM and the perspective of the independent community.

COPYRIGHT AND THE MUSIC INDUSTRY

Copyright was established to stimulate the creation of new artistic and scientific expression. With this public interest in mind, the United States Congress passed copyright legislation providing creators with exclusive rights to their works for a set period of time. This, in effect, created markets for intellectual expression. It was Congress's intent that these markets sustain the efforts of creators and the institutions that directly support and finance them. Otherwise, the purpose of copyright would never come to fruition, either for lack of sufficiently motivated creators or for lack of sufficient investment in creative enterprises.

While these exclusive rights are essential to sustaining creators and those who invest in creative enterprises, if copyright laws inadvertently established effective markets that compensated creators either too poorly or too generously, then the dissemination of intellectual expression would suffer. Either it would not be worth the time for creators to create new works, or the cost of new works would be too great for the public to either have access to them or to afford them. Thus, Congress must be primarily concerned with achieving and maintaining the right balance when it contemplates changing copyright law and protection—the balance not only between the public interest and the interests of creators, but also the balance between the various constituents on the creator side. In the music industry context, the interests of the creator side that Congress must balance are those of the small and medium recording companies (i.e. “the independents”), the major recording companies, the recording artists, the songwriters, the producers, the publishers, the musical performers and the performance societies.

What does the music industry agree on? We agree that copyright is essential, and that without strong copyright our music industry would not be viable. We also agree that copyright protections have become too thin, and, as a result, too much of the compensation stemming from musical copyrights on both the sound recording side and the songwriting side is falling into the coffers of large technology companies and large broadcasters. When these large companies defend themselves against criticism that they are not adequately or fairly compensating rights holders for the musical expressions they are exploiting, they claim they are serving the public interest and that any increase in compensation to rights holders would dampen the public's access to content. At the same time, they fail to mention or gloss over the record profits they are enjoying on the backs of content rights holders. The reality is this: in sharp contrast to the fortunes of the technology companies and the broadcasters, the music industry revenues are now just a fraction of what they were 15 years ago. Since then, U.S. Track Equivalent Units per Nielsen SoundScan (which factors 10 single sales as equal to one album) have declined 45% from 755 million in 1999 to 415 million in 2013. According to RIAA statistics, there has been an even greater 52% dollar decline from \$14.6 billion to \$7 billion in overall recorded music revenues, a decline of 65% after factoring in the Consumer Price Index. This greater decline is the result of both lower music sale prices and new revenue streams, such as streaming, not making up the difference.

While much of this erosion in the value of copyright is due to the disruption caused by the digital revolution, digital transmission is an innovation that the independent sector embraces, as it has substantially improved our community's direct access to consumers, both commercially and promotionally. At the same time, it is the very ease now with which consumers can digitally access music that has caused the copyright balance to shift away from creator interests and towards public access and the so-called-intermediaries of access. In light of this, it is wholly appropriate for Congress to act now to reset the overall copyright balance. Or, at the very least, Congress should set policy to prevent any further erosion of copyright value.

MARKET CONCENTRATION

Within the music industry, one imbalance in particular is the primary threat to musical creative enterprise: market concentration. Twenty-five years ago, there were six major labels in the recorded music market in the United States. Today, just three companies exist—whose interests are represented by the Recording Industry Association of America, Inc. (“RIAA”)—comprising 65.4% of the recorded music sales market in the United States based on copyright ownership, the largest two of which are subsidiaries of foreign corporations. These three major recording companies control an even higher percentage of the total market share of U.S. music distribution, and each of their parent companies also have music publishing arms that, altogether, own or control composition copyrights that represent almost 50%

of publishing revenues in the United States. Even the RIAA, who represents just the three major recording companies, claims on its website and in its regulatory filings that the “RIAA is the trade organization that represents the music companies that create, manufacture and/or distribute approximately 85% of all legitimate recorded music produced and sold in the United States”.

What does this market concentration lead to? Well, using their market clout and misrepresenting their market share figures¹, the three major recording companies have become proficient at extracting a disproportionate share of copyright-related revenue from the marketplace. For example, it is a common practice for the largest of the three, Universal, to require new digital services—who cannot rely on compulsory statutory licenses—to provide advances or guarantees so large that there is no recourse left to the digital service other than to heavily discount what they can offer as compensation to independent rights holders. This is an unfair trade practice and deserves Congress’s and the Copyright Office’s special attention. But the underlying mechanics of this practice are even more problematic, causing a deeper inequity, which I will expand on below.

For example, consider the scenario where a digital service offers a streaming deal to a major recording company, where it proposes a royalty rate (which could be a certain amount that is paid per each stream of the major’s repertoire) as well as a guarantee on what income the major will receive over the first year of the deal regardless of how many streams actually occur. In the negotiation that ensues, the major could try to increase the royalty rate, the guarantee or both.

In this scenario, what would be the most advantageous negotiation strategy for the major? Well, if the major uses all of its bargaining power to maximize just the guarantee—with the intention that the guarantee is so high that it can’t possibly be recouped in the period of time allotted for it—then the unrecouped portion of the guarantee is a significant boon to the major. It is revenue that cannot be attributed to specific recordings or performances, and thus the major does not have to share it with its artists, the independent labels distributed by the major, or publishing interests, unless there are special contractual stipulations covering this kind of income (which is an accommodation that is attainable by only the largest and most established artists and labels). Also, a very similar dynamic to the one described above is the practice where majors receive equity stakes in digital services, presumably in exchange for providing such services more favorable terms for their copyrights. For example, all three major recording companies have received equity

¹ For example, the Billboard Magazine article on 2013 market share dated January 15, 2014 shows Universal Music with a 38.9% market share based upon distribution (which is in of itself an overstated percentage of distribution share as some labels Universal distributes do not use Universal for 100% of their distribution) but only a 28.5% market share based upon copyright ownership. Universal uses the higher market share figure to increase the guarantees and advances it gets in negotiations. A2IM believes that copyright ownership is the only appropriate market share definition.

stakes in the interactive streaming service Spotify. If Spotify has an IPO and these equity stakes are liquidated, how will the proceeds be shared?

This additional revenue that is earned from unrecouped advances, annual guarantees or equity stakes can be referred to as “breakage”. These breakage revenues are not just earned by the major recording companies, they are also earned by independent labels, which is one of the reasons why the independent sector is well aware of breakage and how much value it can potentially divert from both the independent community and the overall creative community. The international rights agency Merlin—of which many of A2IM’s members are also members—, not only maintains equity stakes in some of the digital services that it has concluded deals with, just like the majors, but it recently reported that it would be paying its members over a million USD from unrecouped guarantees from just two global streaming deals. In one deal, this breakage is over half of what was earned in royalties, and, in the second deal, the breakage is almost five times what was earned. It is worth considering what this latter case actually represents value-wise to get a full sense of how much breakage can distort compensation, i.e. when a label receives \$600 through this second streaming deal, it could theoretically keep \$500 (the unrecouped portion, i.e. the breakage portion) as its pure profit and only share with the artist a portion of \$100 (the recouped portion, i.e. earned from streams that occurred). This is a significant inequity.

While it is Merlin’s practice to apportion such breakage revenues it has received pro-rata to what was actually performed on each service, which encourages that such extra value is passed on to artist creators, the independent labels and distributors that Merlin represents are not obligated to share this breakage income in this way. Counterbalancing this to an extent, many leading independent labels have decided to sign on to the “Labels’ Fair Digital Deal Declaration” that the Worldwide Independent Network has authored (see Exhibit 1), volunteering² to equitably share such income with creators in the same manner they share royalties. But the voluntary measures will not be enough. What must be enacted in copyright law are provisions (some of which are recommended further below) that will protect against the inequities caused by breakage. Quite simply, playing breakage games is not the way the independents want to do business; it’s unfair and highly inefficient. Although we’ve gotten a small taste of how lucrative breakage can be, the vast majority of the value of the copyright marketplace being misallocated by this practice is done so at the hands of the major recording companies. It is also our preference for primarily non-interactive services that, whenever possible, the compensation is aggregated and allocated via a system of

² One of the major recording companies, Warner Music Group, currently has a more progressive stance than the other two majors with regards to breakage, volunteering to share unrecouped advances and guarantees (but not equity) as a matter of policy with artists and with the independent labels that it fully digitally distributes.

compulsory statutory rates set via a copyright court that ensures that all creators are paid fairly based on the actual consumption of music.

The intent of copyright is to create markets to stimulate new expressions, not to provide a handful of private interests the ability to make profits by using their market clout to siphon off an unfair share of the compensation that was intended to reward creators and the institutions that most directly support them. If the music industry is to be compared to an ecosystem like the ocean, it can't be a viable or vibrant one if a few really big fish are sucking up most or all of the oxygen that copyright is providing. Also, this music industry ecosystem would not be a fair and equitable one if the appropriate copyright balances between the constituents within the music industry were determined by just the big fish and outside the full purview of Congress and the Copyright Office. While we like the idea of a comprehensive enactment of omnibus music copyright legislation that the whole music industry supports, this bus must be driven by all members of the music creator community, not steered by just a few major private interests towards only their goals.

The current music licensing system is broken, and while Congress and the Copyright Office consider the full range of possible remedies, it should take great care not to replace our current system with one that is even more privately controlled, that leads to more market concentration and that further incentivizes breakage-like practices.

"FAIR MARKET VALUE" AND THE COMPULSORY STATUTORY LICENSE

Within the scope of recorded music sales, the fair market value of recorded music copyrights can be easily determined, whether these copyrights are embodied in the form of compact discs, vinyl records or permanent MP3 downloads. Fair market value in this context is simply a function of what the market will bear. A music label or a distributor sets a wholesale price for its recordings, using its best business judgment as to what price will maximize revenue. A physical or digital music retailer then marks up this wholesale price by whatever percentage it chooses (or the retailer could decide to rely on an agency model, where it always marks up a certain set percentage). It is then left to the market what revenue actually comes back to rights holders. If one label sets too high of a price for a recording, there is no negative impact on the sales revenue performance of a different recording from another label.

Now, however, a new music economy is emerging where recorded music sales in the form of compact discs and permanent MP3 downloads, as described above, have been dramatically diminished. Replacing recorded music sales are access models in the form of interactive digital services such as Spotify, Rdio, Beats and Rhapsody and semi-interactive custom radio services such as Pandora and iTunes Radio. Since 1999 per Soundscan, CD sales have fallen from over 750 million

units per year to 165 million units in 2013, while sales of digital downloads are now in steep decline, falling 5 percent in 2013 and dropping 13 percent in the first quarter of this year.³ Counterbalancing this, the number of Spotify paid subscribers has climbed to 10 million worldwide, and Pandora has grown 28 percent over the previous year.⁴

One can now very easily imagine where all this is heading. David Carr, music writer for the New York Times, may have stated it best when he wrote, “With scarcity now gone, songs are in the air, a mist we move through like so much department store perfume. We are no longer collecting music; it is collecting us on various platforms.”

So, in this new emerging paradigm, what is the most appropriate method of determining the fair market value of a music copyright?

The answer is obvious. When a digital service such as Pandora earns revenue by either charging a subscription fee or by selling advertising, it ends up with a fixed revenue pie from which it shares revenue with all rights holders. This revenue pie is the same value, regardless of which specific recordings on the service are played, whether Led Zeppelin is played 100 times or 100,000 times. So the most equitable way for a service like Pandora to divvy up its revenue with rights holders is to do so in direct proportion to the number of streams that actually occur for each rights holder. This is what Congress clearly intended when they enacted the Digital Performance Right in Sound Recordings Act in 1995 (the “DPRA”) and the Digital Millennium Copyright Act in 1998 (the “DMCA”). “A song by a pop artist such as Justin Bieber shouldn't be valued more than a blues song by an artist by the name of Koko Taylor,” A2IM president Rich Bengloff said just recently in an interview with NPR. “They should have the exact same value. Justin Bieber may get paid 10 times more because his music is listened to 10 times more, and that's fair.”⁵

In the new music economy, each music copyright should possess the same intrinsic value, where the revenue that each copyright earns for its rights holder should only be a function of how many times the copyright is performed by the public, not a more abstract notion controlled by gate keepers, the major publishers or the major recording companies. Music copyrights should be competing in the market place for “user attention” on a level playing field. Pedigree or the so-called imprimatur of a copyright being owned by a larger company doesn't increase a copyright's value. Only the actual performance of copyrights by users matters. Valuing music copyright in this way is not only fair and market-based, but there is

³ Cited from Jon Maples, <http://jonmaples.com/2014/05/08/the-magic-numbers-how-apple-beats-the-demise-of-music-downloads/>

⁴ Cited from David Carr's column “The Media Equation” in the New York Times, <http://www.nytimes.com/2014/06/09/business/media/free-music-at-least-while-it-lasts.html>

⁵ Rich Bengloff interviewed by NPR, <http://www.npr.org/2014/06/09/320324953/reach-for-the-sky-youtube-music-service-in-standoff>

no other methodology that comports more efficiently to the very intent of copyright law than this.

The level playing field for compensation as described above is a central aspect of the compulsory statutory licensing provisions established in sections 114 and 115 of the Copyright Act, and it is why the compulsory statutory license on both the recorded side and the publishing side is so important to the independent sector. But the compulsory statutory license also protects against the practice previously discussed of major recording companies abusing their market clout to get a disproportionate share of fixed revenues. Remember, with music sales through CDs or MP3s, if a price is raised on one recording, it has no deleterious effect on the income prospects of another recording. In contrast, in the new world of access model digital services where revenue to rights holders comes from fixed revenue pools, if a major recording company finds a way to make an extra dollar for its copyrights, it's one less dollar that the digital service can afford for everyone else's copyrights. The compulsory statutory license protects against this inequity by creating a value floor for all copyright owners and removing the incentive for digital services to trade guarantees and advances for lower royalty rates (which only lowers the value of music and artist compensation). The compulsory statutory license assures that all compensation stemming from the exploitation of copyrights is attributable to specific performances, such that compensation is shared fully with all rights holders including creators and songwriters.

Another really good rationale for maintaining or significantly expanding the scope of compulsory statutory licensing is the reduction of transactions costs for the entire industry that comes with it, which Bob Kohn, author of *Kohn On Music Licensing*, makes a strong argument for in his recent Library of Congress U.S. Copyright Office music licensing filing.⁶ This transaction cost savings is not lost on the technological sector in particular, which is one of the reasons why they are in favor of compulsory statutory licensing as well. In an interview with CNET at SXSW in 2013, Spotify founder Daniel Ek said, "That is one of our biggest limiters to growth, the restriction that you can't share any piece of content anywhere. You need collecting societies in every market and publishing deals in every market."⁷

STATUTORY REFORMS WE SUPPORT

Currently, on the recorded music side, the compulsory statutory license outlined in Section 114 is applicable only to services that are "non-interactive" and

⁶ As Bob Kohn stated in his recent Library of Congress U.S. Copyright Office music licensing filing, "But what justifies restricting the copyright owner's freedom of contract? It could only be that, by reducing transaction costs, the public will benefit from the availability of a greater variety of recordings (within legitimate limits that protect artistic integrity) of existing musical works—which is the ultimate purpose of incentivizing creators in the first place."

⁷ Spotify founder Daniel EK interviewed by CNET, <http://www.cnet.com/news/the-future-of-music-according-to-spotifys-daniel-ek/>

that comply with certain programming restrictions. It clearly applies to non-interactive internet radio simulcasts (such as streaming by radio stations KEXP or KCRW) and non-interactive transmissions from Sirius XM satellite radio, and it clearly does not apply to fully interactive services like Spotify and Rdio. But it is unclear whether it applies to services that are semi-interactive, such as iTunes Radio, which could potentially rely upon a compulsory statutory license but instead relies on a direct license (which by itself, does not make it a non-statutory service, as direct licenses for statutory services are permitted by our copyright law). There is no common agreement, including between the major recording companies, whether iTunes Radio is eligible for the Section 114 license.

With this in mind, AZIM supports the following ways of clarifying or expanding the scope of the compulsory statutory license:

- 1) Congress, when adapting copyright law, should more precisely delineate the distinctions between interactive, semi-interactive and non-interactive services, and it should also provide some ruling mechanism to determine the eligibility of services for the Section 114 license (or for the applicable mechanical rate according to the Section 115 license) when there is ambiguity regarding interactivity and functionality. Compulsory statutory licenses should be made available to semi-interactive services such as iTunes Radio.
- 2) Congress should prohibit the pervasive practice where some portion of compensation stemming from interactive licenses is not apportioned to performances of copyright. This would not only prevent an end run around the intent of copyright, it will also provide some compulsory-like protection against the ill effects of market concentration in the interactive streaming space.
- 3) The U.S. Copyright Office and the CRB must ensure that all services using sound recordings within their services be required to use an International Standard Recording Code (i.e. "ISRC" codes) and an International Standard Name Identifier (i.e. "ISNI" codes) to identify all recordings, and such services should also be required to incorporate these codes into the metadata of the recordings they use in order to achieve more accurate accounting and distribution of sound recording royalties. Additionally, all services relying on the statutory license should be required to report all musical performances that occur through their service to royalty collecting collectives such as SoundExchange, clearly delineating which performances are relying on the statutory license and which are relying on direct licenses instead, to better ensure fair and accurate accounting to all parties. A major concern for independent music labels is not just contractually getting their correct proportionate share of revenues based upon actual copyright ownership. A second challenge is ensuring that the accounting received is correct and that independents are actually getting

paid for all of their copyright repertoire. A group must be created to set standards and help create and maintain copyright ownership databases under the auspices of the U.S. Copyright Office, and not under the auspices or control of the RIAA or the major recording companies, to ensure high standards are maintained on a fair and equitable basis.⁸

4) A terrestrial radio performance right on the recording side must be established (see below), and Section 114 must be expanded to provide a compulsory statutory license for it. As SoundExchange commented in its recent filing with the Copyright Office, “Businesses using music for commercial advantage should pay for the privilege, and such payments are what makes possible the creation of new music. Accordingly, the lack of a terrestrial radio performance right is a glaring iniquity in U.S. law that should be addressed. Where rights exist, music licensing provides a framework for channeling payments to creators to enable more creativity.”

5) Pre-1972 sound recordings must be included within the Section 112 and 114 statutory licenses. It is unfair when services using pre-1972 recordings do so without compensating creators for those usages. Our heritage artists deserve equitable compensation for their significant cultural contributions.

THE TERRESTRIAL RIGHT

The U.S. is the only one of the 34 Organisation for Economic Co-operation Development Countries (“OECD”) that does not have a performance right for public broadcast radio performances. For the over-the-air traditional AM/FM broadcast radio dial, the independents have made significant inroads in airplay. But we still don’t have a performance right that would ensure that music creators get paid when their sound recordings are broadcast on over-the-air radio. This must change. AM/FM broadcasters make billions selling ads to folks who tune in for our music while our sound recording creators get nothing. That’s unfair. A2IM are members of the musicFIRST coalition, along with featured artists, backing musicians and vocalists, artist managers and others working toward making this legislation happen in the U.S.

In addition, this lack of a broadcast performance right impacts our international business, as our royalties overseas remain captive to the fact that, unlike other industrialized nations, we don’t compensate performers for terrestrial

⁸ A2IM will be filing with the U.S. Copyright Royalty Board (the “CRB”) in response to their request for comments on “Record Keeping For Use of Sound Recordings Under Statutory Licenses”, outlining in further detail some of the items discussed above, as strict detailed data reporting requirements are essential to ensure the proper copyright owners are compensated for their investment in the musical creation process.

airplay. So without this legal reciprocity right, our royalties are, in effect, not available to U.S. independent music labels and their artists. If we allow radio or internet services to force zero rates or below market rates on us, to subsidize their business models, we will have allowed the gift wrapping to take on much greater value than the treasure that is in the box, the music! Our artist's music that fuels AM/FM radio and every other platform that features music must be compensated.

A2IM's members also believe in parity for all members of the music community. The lack of a sound recording performance right is unfair to the digital transmission music services (both interactive and non-interactive) who already support sound recording owners with compensation. We believe that allowing terrestrial broadcast stations to continue to pay nothing may undermine the critical structures that are now emerging which may lead us towards a fair and equitable music industry. So we believe that some form of rate parity between terrestrial and digital broadcasters must be a goal of any music licensing revisions contemplated by the U.S. Congress, however we stress that this parity should not be established by discounting what is already being paid on the digital side, as we contemplate a music marketplace which will become increasingly more digital and less terrestrial over time.

MUSICAL WORKS

A2IM represents music labels who are the investors in the creation of sound recordings. That said we believe that over one-third of our music label members also have ownership interests in and are involved in the exploitation of musical works. As a result, a large number of A2IM members are involved in both the creation of and the use of written compositions.

The National Music Publishers Association ("NMPA") and the Performance Rights Organizations ("PRO's") ASCAP, BMI and SESAC have been advocating for an overhaul of the musical works licensing process, stating that the songwriters and publishers that they represent are not receiving fair compensation for their work. A2IM as an organization has the utmost respect for these creator colleagues and the individuals and companies they represent. That said we believe the current system of mechanical licensing under section 115 using compulsory statutory licensing rates is a fair system to use for compensating songwriters and publishers.

Music labels are the major investors in the music creation process. Music labels sign artists and incur at-risk capital to support artists with advances and funding of the recording of sound performances. Music labels then incur the costs to market and promote the artist's music and employ both internal staff, with high fixed costs, and pay external staff to cover the areas of publicity, advertising, marketing, radio and video promotion, etc. Most label's artist signings are not

ultimately profitable and overall music label profit margins in the aggregate are very low.

Contrast this with publishers. Many publishers sign songwriters and give advances only after either a songwriter is established or after a music label has agreed to sign the songwriter/ recording artist for recordings because they know at that point that the above music label investment process will commence. Publisher's investments in songwriters are modest to non-existent, except for established proven writers who have already achieved success, and their marketing budgets are low. As a result, the bottom line for Publishers is high. Based upon public releases for ASCAP and BMI, Publishers had revenues from music performances of almost \$1.9 billion for their most recently reported fiscal years. If you add an estimate for SESAC, which does not disclose revenues, we believe the number should exceed \$2 billion. Both ASCAP and BMI have disclosed overhead rates before distributions of under 14%, in the aggregate about 13%. The balance of 87% is distributed, which means that there are profits of over \$1.7 billion from PRO performance sources. The publishers then additionally have their revenue streams from sales, synchronization licensing and other sources.

The above data, we believe, confirms that the publishers make considerably more profits than the sound recording owners, and we believe the net profits earned by the creator community should be the criteria considered, not the gross amounts received which the NMPA erroneously keeps emphasizing. Let us assure you that there is no expense waste or high salary creep in our community. The Section 115 compulsory statutory mechanical licensing process, using CRB rates, is working for all parties. There is no need for a blanket licensing process for mechanical licenses for songs used in the sale of recorded music. Any elimination of statutory rates for these recurring standard usages will tip the profit scales further in favor of the publishers and market concentration. We also believe that the use of musical works for audio/visual synchronizations and other non-standard usages of written compositions for television, games, advertisements, toys, etc. should continue to be negotiated on a direct license basis.

THE DMCA SAFE HARBOR AND GOOGLE YOUTUBE

Google, currently the largest corporation in the world by market capitalization, is cognizant of the rising perception that the copyright imbalance has moved too far away from adequately compensating rights holders. So much so that the vice president of YouTube content at Google, Tom Pickett, recently told music industry attendees at the Midem conference in Cannes, France that Google YouTube "[has] paid out to the music industry over the last several years over a billion dollars."⁹ However, this sum is far less than what more music-oriented digital

⁹ Cited on Creative Intelligentsia's Content & Technology Report, February 7, 2014, <http://www.creativeintelligentsia.com/content-technology-policy-report-february-7-2014/>

services such as Spotify and Pandora are paying creators and labels, especially when taking into account that these other services are paying significantly more based on less streaming and to satisfy fewer consumers. It should be pointed out that the manner in which Google YouTube has decided to pay the music industry—often with large advances or guarantees to only the largest labels, where a significant portion of such advances are not attributable to specific performances or streams, i.e. the practice of breakage we discussed previously—means that the compensation offered for content does not flow efficiently to the creators. Also, Google YouTube currently relies on a safe harbor granted by the DMCA which allows for user-generated content (i.e., “UGC”) to be uploaded to the YouTube service without Google YouTube itself having copyright infringement liability (provided it reacts in a timely fashion to take down requests), a safe harbor provision that Google YouTube claims it needs for the YouTube service to remain viable.

Currently, a significant portion of the independent sector is involved in a public dispute with Google YouTube over its new subscription music service that it plans to unveil in the next few months. AZIM President Rich Bengloff said in a recent letter to the Federal Trade Commission (see Exhibit 2) about Google YouTube’s unfair trade practices connected to this launch, “Google has shown little willingness to play fair on issues such as tax responsibility, and it now shows a similar lack of regard for cultural diversity and creativity and marketplace access. We would argue that a dominant player such as YouTube forcing SMEs to accept lower rates than non-SMEs constitutes abuse of a dominant position, with regard to the digital music and video streaming market.”

Also, one account of this dispute claimed that YouTube will start blocking the videos of independent repertoire in some countries very soon. According to Associated Press sources, “YouTube will block the music videos so users of the test version won’t be confused about which content they can access for free and which features require payment. Allowing free streams of music by certain artists while not offering them on the paid service would erode the value of the paid plan.”¹⁰ This relates to the premium videos that labels and artists create. YouTube has announced their intention to continue to stream consumer’s UGC videos, so as to continue to supply Google with consumer traffic and the resulting advertising revenues. But related to the UGC videos of the independent music community, it seems that Google YouTube no longer plans to monetize those videos with advertisements or to make available to creators the YouTube content management system that enables efficient management of the availability of creator assets within the YouTube service. This will result in creators having to fall back into the costly whack-a-mole process of copyright protection, which we believe was not the intent when Congress enacted the DMCA legislation in 1998.

If the above is true and if takedowns occur in the United States, not only will

¹⁰ Cited by Associated Press, June 17, 2014, <http://abcnews.go.com/Technology/wireStory/youtube-launch-music-service-amid-indie-dispute-24183506>

consumer access to the rich musical heritage and diverse American musical culture that the independent music community brings to the world be jeopardized, but also the hypocrisy in Google YouTube's position on the DMCA safe harbor will come in sharp focus. How can Google YouTube argue that it needs the DMCA Safe Harbor to remain viable and to protect access to the public on the one hand while, on the other hand, it has found the resources and the wherewithal to take down music videos simply because these videos have the potential to create confusion or erode value to the detriment of its new commercial enterprise?

Perhaps the existing safe harbor that the DMCA has created for UGC has inadvertently given Google YouTube too great an advantage in the marketplace, an advantage that the largest corporation in the world doesn't need, and one that is contrary to the interests of copyright, especially when Google YouTube is now contemplating a new commercial product using the advantages of the DMCA safe harbor to compete against the more music-oriented digital services who don't have this safe harbor and who more adequately and more fairly compensate creators. Google YouTube must immediately cease waving the flag that "the public deserves access to all content" without also including the fine print caveat that reflects their true purpose: "unless it gets in the way of our commercial interests".

THE AMERICAN INDEPENDENT POSITION

In the music licensing discussion, the greatest concern of American independents is the ill effects of market concentration: big companies using their power and accumulated resources to take what is not fairly due to them. Not only has market concentration made artist creators and members of the independent sector commercially poorer, it is also to blame for our country's copyright system moving dangerously away from its early and principled moorings towards a newer mindset that benefits private interests and that disadvantages creators at large.

Lord Thomas Babington Macaulay, one of the forefathers of copyright law in the English-speaking world, said in the 1800's, "It is good that authors should be remunerated; and the least exceptionable way of remunerating them is by a monopoly. Yet monopoly is an evil. For the sake of the good we must submit to the evil but the evil ought not to last a day longer than is necessary for the purpose of securing the good." Contrast that with how Lucien Grange, current Chairman of Universal Music Group, talks about power (that he has accumulated because of copyright), in his February 16th 2013 Billboard Magazine Power interview: "Power is about who calls who and whose call you take. That's power. Power is a combination of the ability to write checks, the ability to make things happen, the ability to block things—political power, the ability to testify and the requirement to testify at a Senate hearing and have five commissioners against zero in favor of what you said. Power is the ability to buy and sell businesses. Power is the ability to stop new services. Power is the ability to create new services. That's power."

To a large extent, the market concentration issues we are facing (and the evolving mindsets such as Grange's above that are rewarded and promoted by such concentration) are a product of a basic systemic problem. The current copyright system provides incentives for the wrong behavior (such as maximizing breakage). Large publicly traded companies, whose only fealty is to making profits for its shareholders in the short-term, are acting rationally when they take advantage of whatever inefficiencies exist in the marketplace. The same can be said about independent companies or their digital agencies, such as Merlin, when they take advantage of the same systemic issues to protect their own interests. But the key question to the whole music industry is this: while we do what we all have to do to protect our own interests and maximize our own profits, do we have the conviction and the wherewithal to push for real reform to improve the whole copyright system, to make it more equitable and to reduce inefficiencies? The independent community's answer to this question is a resounding yes, and our sincere hope is that we can come to these reforms in partnership with the whole music industry, including the majors.

The financial sector had a very similar moment, recently, when the Investors Exchange ("IEX") was created in response to systemic issues with the high-frequency financial trading market. Some Wall Street traders were taking advantage of an issue that only a few really understood and had the resources to exploit: slightly uneven trading transmission delays, where those geographically closer to electronic market hubs had better information and better opportunities than others. Exploiting this issue generated huge profits, where every dollar of profit generated was one less dollar left for everyone else. This is very analogous to the systemic issues that the majors are taking advantage of with their innovations in digital music licensing. American non-fiction author Michael Lewis's book on high-frequency trading entitled "Flash Boys: A Wall Street Revolt" provides an inspiring outcome, where the major financial traders all moved to IEX to trade on a level playing field. This should give great hope to the whole music industry when it seeks to address systemic issues within music licensing markets.

IEX had made its point: That to function properly, a financial market didn't need to be rigged in someone's favor. It didn't need payment for order flow and co-location and all sorts of unfair advantages possessed by a small handful of traders. All it needed was for investors to take responsibility for understanding it, and then to seize its controls. "The backbone of the market," [IEX CEO and co-founder Brad] Katsuyama says, "is investors coming together to trade."¹¹

¹¹ As excerpted in the New York Times, "The Wolf Hunters of Wall Street, An Adaptation From 'Flash Boys: A Wall Street Revolt'" by Michael Lewis, <http://www.nytimes.com/2014/04/06/magazine/flash-boys-michael-lewis.html>

Because copyright is not a private property right, it would not be possible to make the same kind of adjustment to address systemic issues just within the music industry (like IEX achieved within the financial sector) without the help of Congress and the Copyright Office. But the whole music industry can work together to support the revisions to copyright laws and protections that Congress and the Copyright Office find necessary in its review. The independent sector trusts that Congress and the Copyright Office will find that the compulsory statutory license must be strengthened, not weakened, that breakage-like practices must not be incentivized, and that the independent sector must be provided more tools, such as antitrust relief, in order to more effectively use what power the independents already have to stave off big business market concentration. In the end, all the independent sector wants is a free market with a level playing field. We want to compete, to provide the economic growth and job creation that our American economy needs.

Congress and the Copyright Office must also consider carefully the practical implications of the music copyright reforms in the world market. Currently, the United States is being particularly hard hit and needs support as we're losing our place in the world music market economy. The overall world market has declined at a slower pace than the U.S. market per the International Federation of the Phonographic Industry ("IFPI", www.ifpi.org) wholesale statistics. In 2005 the U.S.'s share of the international music market was 34%. By 2010, the U.S. was down to 26% world market share. In addition to the overall drop in U.S. share of worldwide music sales, the IFPI has also confirmed that the percentage of U.S. repertoire sales within overseas markets is also declining. As America's manufacturing and service sectors continue to shift abroad, Intellectual Property is one of the few potential growth areas for our economy via exports and we, as music creators and small businessmen and investors in music creation from across the country, need our government's support for a cooperative effort to restore American global competitiveness in the music business.

The vast majority of small and medium enterprises that comprise the independent sector are American companies, employing American citizens in American offices, directly supporting American creators, and who pay their taxes almost entirely (and fully) within the United States. By contrast, the top two of the three major recording companies are owned by foreign subsidiaries, and the Recording Industry of America gets the majority of its funding from these foreign-owned companies. So almost every dollar that is earned by an independently owned copyright has a much greater positive impact on the U.S. economy than every dollar earned by a major label copyright. Congress and the Copyright Office should keep this primarily in mind when it contemplates copyright law revisions, as American copyright law should inure primarily to the benefit of American consumers, American creators and American enterprises.

Thank you for your time and for inviting me to testify at this important hearing.

EXHIBIT 1



“The big print giveth and the small print taketh away.”
- Tom Waits

LABELS’ FAIR DIGITAL DEALS DECLARATION

We make the following declaration in connection with the distribution of recordings in digital services.

We will:

1. Ensure that artists’ share of download and streaming revenues is clearly explained in recording agreements and royalty statements in reasonable summary form.
2. Account to artists a good-faith pro-rata share of any revenues and other compensation from digital services that stem from the monetization of recordings but are not attributed to specific recordings or performances.
3. Encourage better standards of information from digital services on the usage and monetisation of music.
4. Support artists who choose to oppose, including publicly, unauthorized uses of their music.
5. Support the collective position of the global independent record company sector as outlined in the Global Independent Manifesto below.

We wholly disapprove of certain practices which leave artists under-recompensed and under-informed in the digital marketplace and will work together with the artist community to counter these practices.

Signed on behalf of [Label]

[Print name]

[Date]

Global Independent Manifesto

The points below represent the collective position of the global independent record company sector, put forward by the sector's collective voice, WIN (Worldwide Independent Network: www.winformusic.org).

All points are equal in stature, and are not numbered according to any form of ranking or significance.

1. We, the independents, will work to grow the value of music and the music business. We deserve equal market access and parity of terms with Universal, Sony and Warner, and an independent copyright should be valued and remunerated at the same level as a major company copyright. We will work with the majors in areas where we have a common goal. We will work to ensure that all companies in our sector are best equipped to maximize the value of their rights.
2. We support creators' freedom to decide how their music may be used commercially, and we will encourage individual artists and labels to speak out directly against unauthorized uses of music as well as commercial uses of music that stifle that freedom. We support creators' right to earn a living from their work, which should be respected as a basic human right. We expect any use of music by commercial third party operators to be subject to fairly negotiated licensing terms, in a market where any use of music is an end in itself, not so-called promotion driving a subsequent sale.
3. We support independent music labels that treat their artists as partners and who work with them on reasonable commercial terms, noting that labels are investors who deserve a fair return alongside their artists.
4. We promote transparency in the digital music market; artists and companies are entitled to clarity on commercial terms.
5. We oppose further consolidation in the recorded music, publishing and radio sectors since this is bad for independent music companies, their artists and fans, as it reduces market access and consumer choice.
6. We support initiatives which confront market abuse, and which aim to adapt competition laws to promote independent market access and foster collective responses by independents to potentially anti-competitive conduct by large operators.
7. We recognize that all independent music businesses contribute to local culture, diversity, jobs and export opportunities, and multiply the economic success of related industries. We will ask governments to promote and support the independent music sector in securing access to finance and tax credits, and to local and international markets.
8. We hold that collecting society revenues must be allocated and distributed accurately and transparently. This includes distribution of unclaimed money that logically belongs to the independents. We will push for the independent sector to be formally represented in the governance of collecting societies, with trade associations being eligible for board seats.
9. We support the creation of a worldwide track-level sound recording rights database, subject to neutral governance and ownership, to ensure accurate distribution of rights revenues to their rightful owners.
10. The independents will, as always, actively encourage and support new commercial opportunities for music, and will continue to support and develop new, legitimate business structures and partnerships.

EXHIBIT 2



American Association
of Independent Music

Chairwoman Edith Ramirez
Director Bureau of Competition Deborah L. Feinstein
Federal Trade Commission
600 Pennsylvania Avenue, NW
Washington, DC 20580

June 4, 2014

Re: Google/YouTube Notice-Independent music labels and their artists' content to be blocked on the YouTube music website

Dear Chairwoman Ramirez and Director Feinstein,

I am writing as a follow-up to previous letters I have sent to the FTC regarding the investigation of the Universal Music acquisition of EMI's recorded music assets that concluded with the FTC's transaction approval approximately two years ago. My last letter dated September 6, 2013 is attached. **Today I am writing to draw your urgent attention to recent actions taken by YouTube with regard to music recordings from Independent music rights holders where, due to anti-trust restriction on the allowed behavior of A2IM and our members, we respectively request urgent government intervention.**

During the course of the FTC's review of the Universal transaction the American Association of Independent Music ("A2IM"), the not-for-profit 501(c)(6) organization representing the U.S. Independent music label community and of which I am the president, shared our thoughts and those of our members with Robert Tovsky of the FTC. During the lengthy process we expressed our concerns to Bob and made a public statement to the press (read statement [HERE](#)) expressing the Independent music community's concerns about the ramifications that acquisition would bring to consumers, emerging technology companies, and the Independent music label sector.

As we'd previously shared with the FTC prior to the EMI acquisition, UMGD had made a practice of using their existing market share as a means of figuratively holding hostage new and exciting music consumer platforms from launching unless said music consumer platforms were willing to give unreasonably favorable terms to UMGD. Since the acquisition, it is becoming evident that this near monopoly (or duopoly with Sony Music) is turning into a vicious cycle that gives further market clout to a single player, or two players, which in turn gives those players a gigantic advantage in exposing and monetizing their music at the expense of competition, thus leading to fewer music choices and fewer music access points, for consumers.

These trends underline our previously stated fear that UMG will abuse their market dominance by extracting unsustainable terms from digital services. We urged you to investigate UMGD's practices because, ultimately, we see a music landscape where the primary outlet for artists, music businesses, and consumers to create and enjoy music will be via one or two entities. We were confident time was not our ally; that things were certain to get worse as UMGD's advantages in access and financial terms provided greater advantage over any possible competitor which, in turn, will only allow them even greater clout.

Today I am writing to draw your urgent attention to recent action taken by YouTube with regard to music recordings from Independent music rights holders.

The Independent music sector is made up of small and medium size enterprises ("SME's") which the past two Presidential Administrations have seen as the growth engine of the U.S. economy via increased exports improving the U.S. balance of trade and creating commerce abroad and creating jobs at home. The U.S. Independent music sector employs 80% of the industry's workforce and accounts for well over 80% of all new commercial music releases. Independent record companies act as investors in creativity and culture, searching out individual talent and giving them the starting point to build a sustainable career in the creative industries. They perform a vital role both economically and culturally in meeting consumer needs and providing musical diversity. Every new genre and trend in music has been kick-started by the Independent sector.

Even though Independent labels are individually smaller entities than the three individual "so called" major record labels, based upon copyright ownership collectively the Independent music labels are the largest music label industry segment. According to Billboard Magazine, Independent labels altogether were 34.6% of the overall U.S. recorded music market in 2013.

You Tube is a dominant Internet source of music with approximately 80% of Internet users engaging with You Tube for video streaming. As you know, YouTube has been a wholly owned subsidiary of Google since 2006. YouTube is expected to launch a new audio music streaming service to compete with established services such as Pandora and Spotify, and is attempting to force contract terms upon the Independent sector which we understand from our members are significantly inferior to those offered to the international non-U.S. owned 'major' record companies (Sony, Warner and Universal).

Our members have been informed that if they do not sign up to these revised terms, YouTube has given notice to them that YouTube will remove/block our members' and their artists' musical repertoire from the entire YouTube service, not just the new audio music streaming service. As YouTube is one of the leading music outlets the effect on our members on the promotion and monetization of their artists will be severe as the premium videos our members create will be blocked and the User Generated Content videos created by consumers using our members artists' music will cease to be monetized via advertising. Our members will then be forced to engage in the "whack-a-mole" process of getting these non-monetized videos off of YouTube, so as not to detract attention from services that are paying our Independent members, as was not anticipated when Congress enacted the DMCA in 1998.

According to our members, the terms currently on offer to Independent companies from YouTube are non-negotiable and highly unfavorable, and in many cases, unworkable (for example insisting on global rights which the Independent may not be able to grant). They also undermine existing rates in the marketplace from music streaming partners such as Spotify, Rdio, Rhapsody and others but are reportedly planning to launch their service charging consumers a subscription fee similar to or at the same rate as what these competitor services charge. All of these competitor companies chose to pre-license Independent content at terms which are comparable to the majors, something which YouTube has never attempted to do.

If this threatening and intimidating behavior does not stop, the implications are very serious, not only for the music industry, but for all creative and rights based industries. We face the very real prospect of all internet based trade in creative output being controlled by three non-U.S. owned companies who seem intent on taking as much value for themselves, and passing as little value as possible back to those companies and artists creating the very content on which their businesses are built, and are dependent upon, to the detriment of our primarily U.S. owned and based Independent membership. There are parallels in the book retailing world: it is now a matter of public record that Amazon is punishing publishers who refuse to sign new terms which amount to a transfer of value, not a benefit to the consumer.

Google has shown little willingness to play fair on issues such as tax responsibility, and it now shows a similar lack of regard for cultural diversity and creativity and marketplace access. We would argue that a dominant player such as YouTube forcing SMEs to accept lower rates than non-SMEs constitutes abuse of a dominant position, with regard to the digital music and video streaming market.

We ask the U.S. Government to urgently intervene, in order that other creative sectors are not forced into expensive and wasteful litigation against dominant players such as Google. We call on the U.S. Government to provide injunctive relief to prevent YouTube from blocking these Independent companies from their music platforms while our members seek a commercial solution.

The significance of this issue is such that our European Independent music sector colleagues, through their Brussels based lobbying body IMPALA and worldwide Independent music label umbrella organization WIN, are also requesting that action be taken at the European Commission level on this matter as a matter of urgency. Our international colleagues across the rest of the world are also contacting their governments requesting action.

We would be very happy to provide you with further information on this matter. Sadly, all our fears about the effects of the Universal/EMI purchase are coming to pass. More scale has been created and the effects of the Universal and Sony duopoly leveraging that scale are visible everywhere. When rights owners license to fixed-pie digital services - those where there's an income pie to share, rather than a wholesale price - French owned Universal and Japanese owned Sony demand more than their copyright ownership market share, and those excesses end up coming out of the indies' share. Independents which are primarily U.S. owned music labels who traditionally have introduced new musical trends and who are the custodians of our U.S. music culture in genres such as Reggae, Jazz, Blues, Americana, etc., genres that have largely been abandoned by the three non-U.S. owned major labels. Our

Indie music community is often an early adopter of new consumer friendly digital services, as opposed to those larger creators who inhibit market innovation and often block marketplace entry. As Lucien Grange, Chairman of Universal Music Group, noted in his February 16th Billboard Magazine Power interview:

“Power is about who calls who and whose call you take. That’s power. Power is a combination of the ability to write checks, the ability to make things happen, the ability to block things—political power, the ability to testify and the requirement to testify at a Senate hearing and have five commissioners against zero in favor of what you said. Power is the ability to buy and sell businesses. Power is the ability to stop new services. Power is the ability to create new services. That’s power.”

Collective licensing has enormous benefits for the music market and consumers. It provides broadcasters and services with a one stop license for the world’s repertoire under compulsory statutory licenses with rate setting by the Copyright Royalty Board. Collective statutory licensing as set by Congress under the DSPA in 1995 and DMCA in 1998 which recognized that each song is created equal and each copyright holder should be compensated equally for each song, and that size of the creator of the song performance or the economic power of the investor in the sound recording should be irrelevant. The only differentiation in pay should be based upon consumer demand for the music, e.g. the number of streams each receives, not the ownership company. That’s the basis of the compulsory statutory license; each individual jazz song, blues song, pop song or classical song should all have the same basic single usage value. The non-interactive compulsory statutory licensing regime ensures equity and fairness for all copyright owners and allows greater music service marketplace access resulting in greater consumer choice

Unfortunately for non-statutory services requiring direct licenses under U.S. anti-trust laws, collective negotiation of interactive-on-demand licenses by Independent music labels is limited, which, instead of promoting competition, and thus allowing consumers greater choice and broader music service choices as barriers to music usage are lowered, reduces competitiveness of Independent labels and their artists. This lack of ability to collectively negotiate a group license also bars certain services from access to “so called” major label music should they decide not to license and to a wide swath of Independent music which they need to successfully launch in the market place due to more difficult licensing logistics. **We come to you today to request government intervention related to YouTube’s proposed blocking of our member’s content** since we are forbidden under anti-trust laws to negotiate collectively or collectively advocate a boycott of a service.

While the Universal/EMI merger has been completed the repercussions continue to be felt. We hope you’d agree that the importance of a robust and competitive music market place is still a worthwhile goal for the U.S. economy, consumers, and emerging technological services. I would most appreciate being able to have a conversation with someone from your offices regarding our concerns about both YouTube and the Universal/Sony duopoly. My thanks for your time and I look forward to hearing from you.

Sincerely,
/s/Richard Bengloff
Rich Bengloff
President, American Association of Independent Music ("A2IM")

C. C .Robert Tovsky
C.C. Janet Kim
FTC- Bureau of Competition

C.C. Monsura Sirajee
Office of Chairwoman Edith Ramirez
Federal Trade Commission
600 Pennsylvania Avenue, NW
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C.C. Assistant Attorney General William J. Baer