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### Transcript—Legal and Business Issue in the Digital Distribution of Music: Licensing of Music and Records for Digital Use

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**TRANSCRIPT**  
**LEGAL AND BUSINESS ISSUES IN THE DIGITAL**  
**DISTRIBUTION OF MUSIC:**  
**LICENSING OF MUSIC AND RECORDS FOR**  
**DIGITAL USE**

*Ron Gertz, Moderator*<sup>\*</sup>  
*Robert H. Kohn, Panelist*<sup>\*\*</sup>  
*Steve Marks, Panelist*<sup>\*\*\*</sup>  
*Jeremy Silver, Panelist*<sup>\*\*\*\*</sup>  
*Ron Sobel, Panelist*<sup>\*\*\*\*\*</sup>  
*Charles Stanford, Panelist*<sup>\*\*\*\*\*</sup>

**JAY DOUGHERTY:** Now that we've laid the basic groundwork in terms of technology, and Lon [Sobel] has given us the legal overview, it's time for our panel on licensing issues. This panel will be moderated by Ron Gertz, and I'll let Ron introduce the other participants, but since Ron won't want to introduce himself, I'll do it. I've known Ron for about 20 years since we used to share pastrami sandwiches on Third Avenue in New York. But Ron has been in the center of the storm of music licensing for a long time. His company, initially, was the Copyright Clearing House, which was very much involved in synchronization licensing of music for films and television programs. He moved into dealing with one of the niches that Lon referred to indirectly in his talk, the licensing of music for television, making it more viable to go through per program and source licensing of music for television. He's been very involved in that with his company, Music Reports, Inc., and he's constantly involved in new efforts which I'll let him talk to you about to the extent he can on the music

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\*\*\*\*\* Mr. Stanford was an attorney for ABC Broadcasting at the time of this panel.

licensing side. He's also a very knowledgeable copyright attorney. Ron . . . it's all yours.

**RON GERTZ:** Thanks, Jay. The people on this panel are trying to create some business certainty in the midst of the discussions you heard previously. Business certainty is a hard thing to create. Lon was correct when he said that people will talk, and at least on the user end they are beginning to organize in order to talk. But, when talking about music rights, the talk begins in an environment that is already contentious and has been contentious for over 80 years. At the beginning of the process, the licensing models being examined borrow heavily from the licensing of music performing rights for songs (i.e., blanket licenses as a percentage of revenue). A number of parties are involved in these negotiations, aside from the individual transactions that may occur between owners and users. There are performing rights societies who represent songwriters and composers in the licensing of performance rights. There are reproduction rights organizations like the Harry Fox Agency that license rights on behalf of music publishers for mechanical distribution and reproduction. There are record companies licensing digital performance rights and reproduction rights. There is the Recording Industry Association of America ("RIAA"). It's alphabet soup, by the way. The RIAA is also creating a collective on behalf of record labels to collect license fees pursuant to the statutory licenses in the tradition of ASCAP and BMI or perhaps in the HFA model. Hopefully we'll find a little more about that as we go on.

There are a number of issues that in an industry-wide negotiation have to be dealt with and worked through in order to create licensing models that fit the kinds of uses that creative people want to make of music. All of those organizations are trying to negotiate license fees and stake out a claim to their own turf . . . that's *just* the U.S. We have to deal with the fact that Internet distribution is ultimately international, and when you add the other organizations that do similar things in other territories, the licensing models get very, very difficult. It's very easy to say let's look at the "ASCAP model" or the collective licensing model and work out blanket license rates to cover all of this stuff, and then go off and do our own business. Sometimes that model works; sometimes it doesn't, especially when the form of license doesn't necessarily track how music is used. We also operate in an environment with intense government regulation. ASCAP and BMI operate pursuant to structured government consent decrees that control their operations in a number of areas with the reasonableness of their licensing rates subject to judicial review. We have royalty arbitration proceedings, to set rates for certain narrow statutory licenses. In foreign territories there are government bodies, copyright

tribunals, copyright boards, that set tariffs for many of these things. In this period of uncertainty parties are taking conflicting positions as was mentioned this morning. The task will be to learn how to price products in an environment where nobody has really yet found a sustainable business model. This makes the process even more difficult, as management at certain organizations may not want to try new things for fear of getting fired. Sometimes it's better to let courts and governments decide things rather than make what may be perceived by your constituency as a bad deal. So, licensing models, unfortunately, are going to develop slowly and may very well be subject to a great deal of litigation. I can only cite as an example the television and radio industry's negotiations with the performing rights societies. It's quite possible this year, as those organizations' business models change, that we may see a rate court for local television, radio, cable and background music services for ASCAP and BMI all at the same time.

The goal of this panel is to define some of the common terms that you need to know about and present the relevant issues and let the parties present some of their thinking about the kinds of deals they do. On an overall basis, however, there's a problem administering multiple rights for multiple channels. By that I mean licensing performance rights through certain organizations and mechanical rights through others. Because of the tendency of those rights to merge in the digital space there seems to be an administrative conflict now among ASCAP, BMI and the Fox Agency. As was explained earlier, and distinctions between certain kinds of rights, performance and mechanical, ultimately become almost meaningless. The user is likely to say "I don't care what you call it, how much do I have to pay?" So the different clearance channels end up potentially hindering the kinds of negotiations that we seek at marketplace levels. There is a tendency for owners to seek blanket licenses, i.e., licenses that give blanket protection against copyright infringement. The societies really like those kinds of licenses because they're usually tied to the revenue of the user, but revenue-based licenses have always been a problem for users because the revenue that they're generating may not have much to do with the music that's used. That is one of the issues that has come up in television, where local stations have realized that the bulk of their revenue comes from news programs which don't make very heavy use of copyrighted music.

The societies operate pursuant to government induced consent decrees, and I want to spend a few minutes talking about the consent decrees because it frames many of the issues that we have to discuss. The societies are government-regulated monopolies, and the purpose of these consent decrees is to decrease the dependence on blanket licensing—the

one-size-fits-all license—and create incentives for the development of marketplace transactions for music performing rights. The consent decree created a mechanism for reasonable pricing by establishing a rate court. If a user or the society can't reach a negotiated agreement on fees the issue is referred to a rate court to determine reasonable blanket, per program and per piece license fees. In those kinds of proceedings, the societies have the burden of proving that the rates that they seek are reasonable. The ASCAP consent decree requires ASCAP to offer a blanket license—basically, a license for the entire catalog, which they like to price at a percentage of revenue—and they have to offer a per program license. Under a per program license, the user pays ASCAP only if a program has ASCAP music in it, meaning it doesn't pay ASCAP for a program that doesn't have ASCAP music in it. Over the years broadcasters and others have asked ASCAP and BMI for other types of licenses, and the societies have said, no, the consent decree requires us only to grant these two kinds of licenses. So one of the issues for interpretation in the future is are those two types of licenses the only ones the societies are required to offer, or must they offer any kind of reasonable license that makes sense? It's interesting to note that in the BMI consent decree, there's a provision for non-broadcasters to be able to pay on a per piece basis, even though BMI is not willing to grant that kind of license yet. So it will be interesting to see how the licensing requirements of the consent decrees are interpreted by the courts. When you as a user can pay on a per-piece basis, you begin to ask certain questions. Well, if my blanket license fee is X dollars, and I can negotiate a deal with copyright owners representing 20% of the music I use, can I get a 20% credit against blanket license fees for the deals I've negotiated directly with the copyright proprietors? This is a big issue, and the users are saying, well, if I can do a direct deal, I should be able to decrease my payments to ASCAP. Some copyright proprietors are saying, "Hey, you know what, given the way money gets distributed these days, maybe I'm better off if I make a direct deal and maybe I can get more money and maybe I can get it faster." Or, the user may say, "Why should I pay for works on a blanket license basis when some of the works I broadcast are in the public domain?" Or more importantly, a copyright owner may ask "Maybe I don't want a society getting in the way of a promotional performance that is helping to sell my CD" So, very shortly we will be going through this rate court process which may help create marketplace licensing mechanisms that better reflect the way people are going to be doing business over the Internet. I'm not going to talk about the ASCAP license, I'm going to let Ron Sobel talk about that. We will talk about mechanical licensing with Bob Kohn whose company, Emusic, has just

recently made a deal with the Harry Fox Agency for digital phonorecord deliveries. And we'll talk about the licensing of sound recordings. We will likely have conflicting opinions as we discuss the upcoming CARP proceedings. I'd like to start with Jeremy Silver of EMI.

**JEREMY SILVER:** Thank you. Hi, everyone. I'm not a lawyer, I think is the first thing I should say (applause). Just to give you a bit of background about me, just as a sort of typical case-in-point, I guess, I run the New Media Operation for the EMI Recorded Music Group in North America. That includes Capitol Records and Virgin Records. It also includes Priority Records and Capitol Nashville, Blue Note, Angel and various other labels that we have. As you can tell from my accent, I originally come from London. Bizarrely for someone working in this sort of technical field, my background is English literature. I received my Ph.D. in 1985. I found my way into the music business through sound archives and gradually worked my way through a variety of different incarnations into new media. So my background is very much a kind of label background. The growth of activity on the Internet is probably the single most compelling topic which is facing any major record company today, no question about it. I think that our ambition, as is that of any other ambitious company, is to become a digital record company within the next five years. Otherwise, we're not going to be here. In trying to do that and trying to set out what that means and what kind of strategies we need to adopt, one is faced with an extraordinary task because the impact, not just of the Internet, but also of digital technology, which is such a close part of it, impacts on every aspect of our business. From the moment that you place a recording artist in front of a microphone right through to the moment of making some music available to the consumer in some shape or form.

Almost every process that we currently do in analog or in paper form could be digitized. And so, in many respects, when people look at what record companies are doing and perhaps see record companies as reacting relatively slowly to the opportunities of the Web, most of the reason for that is because of this enormous task, most which really is back end stuff rather than deal-making and commercial operations. It's an enormous back office task to digitize assets, to create structures which address a different kind of market. You know, if we could all move from a conventional world producing physical product and jump instantly to a digital world in which everything was available digitally and we didn't have to worry about physical product, many of the issues and many of the problems that we're facing today wouldn't actually be problems for us. We could establish a relatively clean framework. It's precisely because of the fact that we're

dealing with all of these legacies and that we're dealing with a business which is going to continue in the conventional traditional way, as well as spawning new businesses, the shape of which we're only beginning to find out, that the issues are so much more complex.

EMI across the world currently runs something like 45 different websites. These are sites which are marketing and promotional-based sites in their origins. We've been selling physical CD's online here in the U.S. for a little while now, and mostly the sorts of selling deals are through third parties. It's basically an affiliate label kind of arrangement with a website, whether Amazon or CDNow. And clearly in the process of that kind of operation, we're beginning to feel our way, we're beginning to establish some consumer databases, we're beginning to see what some of the issues are. And alongside of that, what we're also seeing is an enormous opportunity for promotion. I think these have been referred to in some of the conversations you already had this morning. And a lot of the tensions that the record companies are facing right now is between what is potentially an enormous promotional opportunity of making other sites able to use our material, to be able to license material or make it available under promotional terms to third party sites to bring exposure and promotional opportunities to new artists, on the one hand, and on the other hand, a sense that the distinction between what is promotional and what is the product for sale, is becoming less and less clear. There is very little distinction, except we talk about 30 second clips. Well, 30 seconds is an arbitrary amount of time. If that starts to extend as a period of time, at what point does the promotional opportunity actually become the physical product itself? On most of our sites you can download 30 second clips. Big deal. The issue is not whether or not 30 seconds is going to damage our business; the issue is what kind of precedent are we setting in doing that and enabling the consumer to have that opportunity and what sort of expectations do we raise. So, this is the kind of environment that I'm sure is very familiar, but from the record company perspective, it's an interesting one to try and tread that line between promotion and commercial opportunity.

What's the different between a digital radio station that is digitally distributing its radio programming and digital distribution of music? There's very little real difference other than the terms under which that music is received and delivered, what sort of protection it may or may not have and perhaps some programming issues that you might want to put in there, as well. But there's some very interesting opportunities in that, but they're also foreseen as being some very interesting threats there for us. So this is always the negotiation that we're encountering. We're tried out lots and lots of different things. Our policy at EMI has been really let's have

some fun in this stuff for the last few years. We're getting a bit more serious about it now, but the breadth of opportunity and the scope of things that you can do has for us been an opportunity to learn about all of those things. That's what it's really meant, and we've spent a lot of time engaging in quite fun but relatively small scale initiatives, so for example, I think we were the first company a couple of years ago, with Liquid Audio, to allow a digitally downloaded single with the Duran Duran single that we downloaded from the Capitol Records site. This was a tremendous thing to do. It wasn't that we thought this was going to be the future here and now and we were putting a peg in the sand and saying from here on out this is going to be the shape of our business. Actually, it was none of that at all. It was, if we do this, what are the issues that confront us? Well, one of the issues that confronted us straight away was the retail community was up in arms and gave us a hell of a time. So, we learned a lot from those kinds of experiments.

Hopefully, we don't do things that are so traumatic to our business that those consequences are too terrible. I have to say, my role very often in these things is to act as the policeman within the company, which is something I never thought I'd have to do, but because we are on the receiving end of so many requests, so many suggestions, so many incredible creative ideas involving technology, involving our music, involving our artists, and we like to try as many of them out as we can. So we've worked very closely with companies like Liquid Audio, with A2B Music, who are experimenting in the digital download field. And we do that with a great sense of excitement, and a great sense of interest in terms of what the commercial possibilities really are there, and so far, you know, no one has arrived at a model that really necessarily is the final solution or the ultimate commercial model that really works, but the ways of working and the kinds of relationships that we're establishing, I think, are important for the future. One of the things, for example, that we've done recently with A2B Music on a number of occasions very successfully is to provide a digital download, but to do it in such a way that it actually encourages the consumer to go into retail. So that as the natural consequence from having the disaster with Liquid Audio where we said what are you doing, you're cutting us out of the whole food chain here, so the next day it was, well, actually, we still want to learn about digital distribution but we don't want to alienate our retail partners, so let's find a way of playing in that space that also allows us to drive traffic into brick and mortar stores and sell some records.

But we've also made some other initiatives as well. Recently, we signed a deal with Broadcast.com to stream a number of dedicated channels



from pages that they said which are our pages. So we're offering streaming video, we're offering a certain number of album tracks, we're offering some listening parties which give people an opportunity to preview albums before they come out, and that is beginning to be a very interesting area for us, and again, it's an area which changes the way in which we do business because it begins to allow us to move into being a media company and not just providing media assets for conventional media businesses to sell and to sell advertising around, but for us to actually control ourselves. Now how that affects the business and how we're able to evolve our business in that kind of context is a very interesting dilemma for us.

The tradition of business thinking over the late '80s and the early '90s was, you know, outsource everything that you're not an expert in. Strip your business down to core competencies and leverage your brand. Those are the mantras of that period. And what is very obvious in the new media world and the world of the Internet is that actually those mantras don't necessarily make sense anymore, but actually the ways in which you can evolve your business and migrate your business online become much more to do with what content you may be able to control, what your consumer base may be, how you can leverage a consumer market. An interesting issue for record companies on the issue of branding, of course, is that record companies for the most part don't really have brands that are meaningful to the consumer. It's the band that is the brand, and therein lie some interesting conundrums for us.

So, we have, I think, a fantastic digital future. We're facing some enormous challenges at the moment. I think that we will move to digital distribution probably much more quickly than many people a couple of years ago thought that we would, and I think that, the Mpeg3 phenomenon has probably, from our point of view, not been this horror story of piracy that we wish to obliterate from the face of the Earth. We don't want to have piracy and we're looking very, very hard to find ways of reducing it, but what it really has shown for us is there is a consumer appetite, and that's the real message that's come out of this situation. So we don't feel that Mpeg3 signals the end of the record business. We feel that actually what it's done is to seed the market and has provided us with the evidence that probably we would never have been able to go out to research ourselves to show that consumers actually want this. So how we make it work and what kinds of controls and what kinds of disciplines we place around digital distribution are topics of intense discussion and debate right now, as I'm sure you're aware, but we feel very excited and very positive about the future.

**RON GERTZ:** Thanks, Jeremy, I was actually glad to hear you talk about the economics of the business. It's a funny thing . . . technology changes; economics don't. And in that line, I want to suggest to everybody a book, not *Kohn on Music Licensing*, I'll get to that in a second, a book entitled *Information Rules*, written by a couple of economists . . . you know those types. I think Carl Shapiro is one of the fellows. It's an excellent book.

**STEVEN MARKS:** Hal Verian is the other.

**RON GERTZ:** Okay. Thank you. It's an excellent book about the economics of the online industry, and you should all read it if you want to some insight as to how business deals are going to evolve. Not for any particular reason other than the fact that he's next in line, is Steve Marks. Now, it's a funny thing about the contentious negotiations we get into. In those kinds of negotiations you can't help but hate certain people. And some people, you know, you maybe hate their positions . . .

**STEVEN MARKS:** That's a hell of an introduction, Ron. (laughter)

**RON GERTZ:** Yes. I'm not finished yet. Sometimes you hate their positions and you like the person. I think I like Steve, and Steve is a guy who seems to be taking the lead from the RIAA perspective in dealing with people who need to license sound recording performing rights, so I'm going to hanging on every word that Steve says and decide what I like and what I don't like. And I still will probably buy him lunch afterward.

**STEVEN MARKS:** I've already got my ticket. (laughter) I'm not sure exactly where to start after Lon's very good analysis and the issues that he raised as well as the provocative questions, I think, that were raised by many of you. While this was going on, I was trying to figure out what was more pathetic—the fact that this all seems so crystal-clear to me, or the fact that very esteemed academicians like Lon can't figure out certain of the provisions, so I don't know what that says about my life, but . . .

**RON GERTZ:** But you wrote the act.

**STEVEN MARKS:** Well, that's why it's so clear, I guess, but . . . I'd like to just take a step back and, undoubtedly, we can get into some of the legal issues, but I think from our perspective, this is really about working together with Internet businesses, as opposed to extracting huge royalties or shutting sites down. You know, there was a lot of laughter when I tried to make this distinction between the Cease and Desist letter and the letter that I sent out, but the reason I made the distinction was because we have never attempted to shut down a webcasting site. Years went by where we felt that as a technical legal matter our rights were being infringed by people who were webcasting. But our reaction was not to run out and sue them or 'cease and desist' them, but to attempt to engage them

in business discussions to figure out arrangements that made the most sense from perspective of record companies and artists receiving the value for the music that they create, as well as the exigencies and how these businesses are run.

You know, it's always amazed me that people take the position, and some webcasters did this, but not all webcasters did this, that they could build entire businesses without paying for the very content that was essentially their entire business. Ron mentioned the fact that a lot of them are struggling with revenues, but that doesn't seem to be hurting them in the [stock] markets, and you've got a lot of companies with market caps. I think, Charles was just talking about how Yahoo is four times Disney, or something. I mean, it's crazy. So, I think that what we did last year really wasn't RIAA running to Congress to get something put into the Digital Millennium Copyright Act at the last minute. In fact, we reacted to a group of webcasters that were formed under an organization called the Digital Media Association, ("DiMA"), which represented a few webcasters, including some of the largest ones. They had been lobbying for certain exemptions that we felt were undercutting our rights, and we ended up in a very productive negotiation whereby they were able to have access to the music that they needed on a day-to-day basis without having to, for instance, negotiate separate licenses going label to label, company to company, and Jeremy [Silver] can tell you that that's a benefit for us, as well, because having every single one of those companies at your door trying to negotiate licenses is something that a lot of record companies don't have the resources for. So they gain this access, and we all gained a mechanism by which we could hopefully negotiate licenses that make sense for the Internet space that they're in.

One of the keys for us, I think, was creating a statutory license, and we viewed this as giving up exclusive rights that we otherwise had, and that's why it was important to have a lot of the conditions put into the statutory license that Lon alluded to at the beginning, which are somewhat numerous, I will admit, but were all very important to us in terms of diminishing the threat that existed from certain types of webcasting. You know, the most obvious example is, you have digitally available an artist-only channel. Why would anybody go out and buy an album if they could dial up anytime and get CD-quality music from that artist. These are very real business issues for us, and therefore, we wanted some safeguards in the law.

Now, there may be certain situations, like Jeremy was just talking about, where Capitol does a deal with Broadcast.com where they control . . . they meaning Capitol does . . . the ability to "push" certain artists that

they want to promote. That's great. That's the marketplace at work where a sound recording copyright owner is making a business decision about how to use their music, but it's very different to allow users of music to make the decisions when they don't own the content and aren't involved in the business of selling that content.

I think there are a number of legal issues that were touched on in the last round. The one that comes to mind was this whole debate about, is a download a stream, is a stream a download? And from our perspective, and this is the way we kind of view this entire space, we have rights, both the streaming rights and the download rights. We don't have separate organizations like Harry Fox and ASCAP, but we like to view those types of situations from a commercial perspective, you know, what is the commercial value of the use, and not based on some way that the things deliver. One example that I always like to use is the five listen example. Somebody, a company sells five listens to a consumer to listen to a song five times. They can deliver that in one download, and then there's individual listens that expire on the end-user's computer. They can send it in five separate downloads, or they can stream it five times without any downloads. From our perspective, the commercial value may be the same, assuming that the listener, for instance, is able to pick when they want to listen to it. And trying to parse up, well, if it's five downloads, then we should have it be this much, and it's one download, then it's a whole different set of revenues or something like that. I think these are the issues that, hopefully, will be fleshed out in the future, if not legally or legislatively, commercially. But you can come up with any number of very good "law school-type" situations that are problematic right now as we're starting out, but hopefully, will be solved commercially, so . . . I'm going to turn it over, and if you've got specific questions, we can get into those.

**RON GERTZ:** I have a quick question. In the recent Copyright Royalty Arbitration Panel ("CARP") proceeding for the rate for digital subscription services, the rate was set at 5% of gross revenue which the Copyright Office kicked up to 6.5%. The RIAA originally went in with a demand of, I think, 41.5% of gross revenue?

**STEVEN MARKS:** That was our case.

**RON GERTZ:** Where did you *really* expect it to end up?

**STEVEN MARKS:** Let me explain. I did not come up with this number, but I had to litigate the case after the number was developed, and that number will haunt me, I think, for a very long time because every time we talk licenses, immediately the response is, well, what about 41.5? You guys just can't be dealt with. (laughter) Let me just explain what the rationale was behind that. The services that were at issue in that case were

three cable and satellite audio services. We undertook an analysis of what similar services on cable and satellite systems, i.e., those services that don't produce any of their own content but buy content or use the content of others and program it. What they pay as a percentage of revenue for the content that they then program. And this made sense, we thought, because these were services being delivered on cable and audio, and we're therefore competing with the other services, other types of channels in those media. That analysis came out at 41.5%. I kind of wish the number had come out lower, frankly, because it would have made for an easier case, but that was the analysis that was undertaken. It was looking at what similarly situated competitors were paying to be able to have space on those cable and satellite systems, and that's what the number was. There wasn't a whole lot of argument about whether that number was right. I mean, there was some argument about obviously about whether that theory was correct or not. And I think, frankly, we were prejudiced by the fact that the number was so high. I think that the theory would have been more acceptable in the proceeding if the number were at 15 or 20% of something like that. But that proceeding dealt only with those three services, and the opinion is written very carefully so *that rate applies only* to those three services under their particular financial situations at the time, and indeed, are under different criteria in terms of what criteria are to be used in setting a rate, for instance, for webcasters because the law has since changed. So, that's the six and a half percent.

**RON GERTZ:** Thanks, Steve. If there's one more comment to make about this whole process in the changes in the DMCA, I think, even though users just may not like the fact that the exemption for non-subscription services was eliminated, I think all of us respect and have our hats off to the RIAA for producing the result that it produced, and I'll leave it at that. You did an excellent job of getting your way there.

**STEVEN MARKS:** Of course, we don't think there was any exemption eliminated, but that's another matter.

**RON GERTZ:** Call it a change or modification, or clarification. Next is Ron Sobel. Now, on the scale of people I like or dislike . . . I actually. . . (laughter)

**STEVEN MARKS:** Are you going to offer him more than just lunch, Ron? (laughing)

**RON GERTZ:** Yeah, I did, I already did. I like Ron Sobel and I can prove it. A number of years ago, he was dating my doctor's daughter, and so I went in for a checkup and the doctor said, "You're in the music business. Do you know this guy named Ron Sobel? He's trying to date my

daughter.” And I said, yeah, he’s a nice guy. So you’ll have to tell me later what happened. (laughter)

**STEVE MARKS:** I bet you didn’t have that in your notes. (laughter)

**JEREMY SILVER:** The father probably told her to never see him again. (laughter)

**RON GERTZ:** Probably. (laughter) Ron is with ASCAP and has been with ASCAP for a long time and is one of the people that I like to talk to about what’s going on at ASCAP and ASCAP’s views and positions. So lay it on us.

**RON SOBEL:** Good afternoon. In the interest of fair disclosure, I am a *recovering* attorney. (laughter) I am clean and retired for thirteen years now so . . . Also, one other comment, I head the ASCAP/LA office and it’s a creative office, and my real job is to sign and work and develop writers and composers. I became involved with the Net in the last three or four years, and I’m on ASCAP’s New Media Council, and I’m fairly up to speed on the creative side of the Internet, so I’ll be able to take this discussion only so far, and certainly don’t want to tackle with Ron Gertz on some of the more technical legal issues or licensing issues, but I think I can get us at least to the 50 yard line on this. Initially, ASCAP has two challenges on the Net—two distinct mechanisms on how to approach copyrighted music and public performance on the net. The first challenge, obviously, is that ASCAP has to find the sites and identify the users of music so that we can issue and negotiate a license with those users. The second distinct challenge we have is to then find the musical works that are on the Net and identify those works that get transmitted.

Let me give you a brief headline on the current state of the ASCAP license on the Net, and I suspect I can speak generically for the other performance rights organizations. I think BMI is fairly closely aligned in their license approach, and I can’t speak as accurately for SESAC. The current ASCAP license is based on our experience in licensing music users for more than 85 years. After licensing live music clubs and radio, we underestimated the audience that cable television could deliver. We just didn’t think ten, twelve, thirteen years ago, that a wire to the house was ever going to be equal to what the three broadcast networks were doing in terms of delivering music to large numbers of listeners. So taking that experience to the Internet community, we’ve really tried to stay as close as we can to the tech community, as close as we can to the music providers, to understand what’s going on with the technology, what’s going on with the culture. Out of that effort has come a flexible approach, an affordable approach, in which ASCAP has three different kinds of licenses that we can offer to web site operators. One is based on website revenues, another is

based on annual operating expenditures, and the third license, for the small guys, is a flat \$250 license that covers a blanket use of all their music, and they don't have to provide expenses or revenues. That's it in a nutshell. We have really tried to make these licenses affordable and flexible. If you want more information, there is a reprint in the conference book of the three ASCAP licenses, and I encourage you to go to ASCAP.com if you want to take a look for your clients and see what we do. The materials also reprinted Frequently Asked Questions from our website, and that's a really good resource to start on the Net for public performance rights licensing.

When we move beyond the licensee and then go into identifying the work itself, we have, in that regard, two distinct challenges. First, we have to locate, monitor, and survey the music sites. Secondly, we have to identify the musical works being transmitted. Let me give you the headlines on the key aspects of both of those. In terms of performance monitoring, we utilize web analysis tools, and in this regard, ASCAP made partnerships with technology people. We've made a partnership with what initially was called Online Monitoring Service, OMS. They are now known as Cyveillance, and we created a software technology that can find and license and monitor music on the Internet. The software, called EZ Eagle, is a music bot—a powerful, aggressive web crawler that can identify sound files. Let me give you the key components of what the EZ Eagle can do for performance monitoring. First of all, it can locate Internet sites which use commonly available audio and video file formats. It's a bot that can make a distinction between a text file and an audio file, as it crawls and searches the web. The other interesting component of the bot is that, not only can it find embedded audio files, it can prioritize and distinguish the amount of audio files contained on a site. So if it comes across something that in its history is relatively small, as opposed to a website that has an enormous amount of audio files, it will go to the larger site first. Automatically, the bot, once it finds a website that has audio files, will send an electronic e-mail, a tap on the shoulder, gently congratulating the site for their use of music. . . (audience laughter) and *politely* informs them of the provisions of the copyright law and their obligation to obtain a license. Once again, the EZ Eagle identifies the site, sends them an e-mail, and starts a dialogue or a conversation to encourage a license.

Another thing that the EZ Eagle can do is track compliance with a license requirement the second fascinating aspect of the EZ Eagle is its ability to read and decode watermarks, referred to as performance identification. Again we have made partnerships with the tech community, and we've made two new deals, relatively new, within the last six or eight months. The first company we partnered with was Solana Technology

Development. Their audio watermark is called Electronic DNA. We recently announced a second partnership with Aris Technologies. Aris' watermark is called Music Code, and at this point we've taken two non-exclusive agreements with these two companies for them to design the watermark. Aris and Solana have now merged into a new company called Verance Technology. Let me give you the headlines of the key components of what has to happen in performance identification.

First of all, we want it to be an open standard. Secondly, we're trying to provide a secure envelope for delivering an ISWC, and International Standard Work Code. And the heartbeat of the watermark is this ISWC, this work code, which, for ease of conversation, is much like a license plate number. It's a license plate that refers back to a bank of information: songwriter, publisher, recording company, splits, performing artist, release date. We've issued approximately 500,000 ISWC's at this point. The international community seems to be coming together, at least on this notion of ISWC. The embedding technology is going to be a competitively driven, a market-driven result. We can't tell our members which watermarking technology to use. That's a decision that's really going to have to play out in the creative community. And then finally, the watermark has to provide an effective mechanism for ASCAP to ultimately monitor and identify the works being transmitted on the Net. In radio we have a sample survey. In television, certainly in the large stations and the networks and most of the large cables, we have minute-by-minute census surveys so we can identify music. The Net presents an incredibly larger challenge. Prior to EZ Eagle, we couldn't have identified who the transmitters, the broadcasters were; but with the technology we'll be able to identify and get a better handle on it.

That's the headline in an environment that's really complex. Our mission is clear. We like the vision of streamed media on the Net, so in that regard we feel comfortable, and our partners are comfortable with what we're doing. The international community has gotten behind what ASCAP's lead has been, and so from a streaming standpoint, we think we're on a good path.

**RON GERTZ:** Thanks, Ron. A couple of other things for people to understand about the consent decrees. There's a provision in the consent decrees that says, any user who wants a license, simply, but it's not really that simple, has to send a letter to ASCAP and BMI saying, "I want a license," and the user is licensed and can't be sued for copyright infringement. The rate is then subject to negotiation or a rate court determination. So, if you want to go out and start streaming music, you can get a license. Just send a letter. Of course, coming from my perspective,



the societies are trying to make it easy for people to get blanket licenses tied to revenue, in order to get enough of those licenses in place so that when a rate court proceeding does happen, the societies can say, "well, the license must be reasonable - look at all the people who took the licenses." Also, another little bit of subtext is the ISWC and information. Information is very important. Users want to know how much music they're using in order to figure out how to value the licenses. So, we hope that in this new media world, that use information will be shared by the societies with the users. Jay?

**JAY DOUGHERTY:** You mentioned the international side of things. What's ASCAP's position with regard to streaming? If you have a streaming originating from a website in the U.S., but the streaming is available in France, do you need a license from ASCAP and from the French performing rights society, or one or the other? Is there any international agreement in place yet to deal with that conflict of law problem?

**RON SOBEL:** Yes, I'd like my BMI counterpart to answer that question. (laughter) Someone on the panel might know but it's my understanding that we license the site by where it's domiciled, so my impression is, you know, we just hope that all sites just don't start moving way offshore just to avoid what would be a stringent U.S. copyright law enforcement protection, but. . .

**STEVEN MARKS:** Yeah, the answer is that there is a right implicated in both places. I mean, if you stream . . . if somebody in the U.K. goes up to a site and requests a stream from a site in the U.S. and that U.S. site makes a transmission to that person in the U.K., there's a right here as well as there. What we are trying to do is to enter into arrangements with our counterparts in the foreign countries so that we can basically offer a license to a site in the U.S. and say, this license also covers all of your transmissions into these countries, and that way . . . and then we [the RIAA] take on the obligation of dealing with how to distribute the money and who should get it and everything else. But it would make it easier for everyone involved. . . for us, the other collecting societies, the websites, etc., so it's a complicated issue and we're exploring ways to facilitate that licensing.

**JEREMY SILVER:** It's worth adding, as well, that in Europe there is a history of performance rights that applies to record companies as well as to the publishing, so there actually is more infrastructure that exists there and more of a history than there is here [in the United States], so that doesn't get over the complexities, but it actually gives a bit more facility at least to address them.

**STEVEN MARKS:** Yeah, what Jeremy's alluding to is that most other countries, for instance, in Europe, when radio plays a song, the producers get paid as well. The record companies and the artists get paid as well. It's only in the U.S., essentially, that there's been this exemption which is essentially an historical anomaly that's been perpetuated by a very effective broadcast lobby in our perspective, so. . . In other countries it's a different thing.

**RON SOBEL:** Just one other thing. The ASCAP experience is that we're growing at about three times a year at this point in revenues. We initially started licensing in 1997. We started distributing in 1998, and we're obviously continuing, but from what was a really meager startup of licensing revenues on the Net, less than \$100,000 in 1997, we're projecting that in this year in 1999, our license fees from the Net could approach \$1 million. Not a lot of money, but a tripling for each of the last three years. If you carry that out, and as our projections show us that we see network television remaining vibrant, radio remaining *very* vibrant, we see the Net, as we say, the pie just gets bigger.

**RON GERTZ:** Thanks, Ron. It's one footnote and some subtext for Jay's question. There are performing societies in territories all over the world. They all look at this revenue stream and say, where are we going to be? And the concept of licensing at, in the territory of the server, favors U.S. societies because this is where most of the servers are. And although I'm not going to take a position on whether that's good or bad, some of the foreign societies are saying, wait a minute, we may be in financial trouble unless we can figure out some way to take some piece of that revenue. Maybe instead of licensing at the site of the server, licensing ought to take place at the site of the content provider. I don't know how any of that will play out, but it'll be interesting to see how it develops. Our next speaker to Charlie Stanford. Charlie has a title so lofty we won't even mention it, but in terms of duties, I've been dealing with Charlie for many years. Charlie was the legal and business affairs guy with the ABC television network, ABC news and now, as a result of the acquisition by Disney, is head of legal and business affairs for, among other things, all the new media issues for the Disney and ABC websites. Now, also. . . Charlie is a client of my company, and during the course of the negotiations. . .

**STEVEN MARKS:** You should have said that first, Ron. (laughter)

**RON GERTZ:** During the course of the negotiations of the various services we provide to Charlie's companies, we were dealing with new sensitive issues, that we just didn't put in the contracts. Charlie would often say to me, if you ever do that, I'll cut your legs off. So on a scale of likeability, one to ten, Charlie's a hundred. I love the guy, I love him.

**CHARLIE STANFORD:** The introductions just keep getting better and better. First, a disclaimer. I'm glad to see that Ron's as confused about my title as I am. My primary work for ABC is cable and new media. ABC is, probably, you all know, is owned by Disney. Disney has its own Internet online group. We also have associations or own a piece of Infoseek and Starwave and God knows what else, all of whom have a lot of people that work in this area, so most of my activities are just for ABC, and ABC is, unlike a lot of the companies that are represented here today, I think ABC is a mainline . . . has been perceived as a mainline entertainment company. We've been around for a long time, and particularly when we were owned by CAP Cities, it was very difficult to convince the then management that the Internet and some of the new media were worth getting involved in because they were mainline broadcasters, and they perceived their core business as being broadcasting, so it was very difficult to get them to even let us experiment in the Internet, but notwithstanding that, about five years ago ABC did put up a couple of sites around ABC News and ABC.com, which was basically a promotional vehicle for the network. Now, when we were taken over by Disney, Disney sort of accelerated the process at ABC as well as having its own initiatives going on the Internet, and like it or not, ABC at this point has been dragged kicking and screaming into the digital environment, both the Internet and other digital media. We have committed to the FCC and to the country that we will have X number of digital radio and digital television stations up within the next year or so. The growth of that initiative has slowed considerably because we can't find transmitter sites in places like New York, but for us the digital environment is not just the Internet, it's digital over-the-air television, it's digital transmission over cable and a variety of other things.

At this point, we have probably . . . we, between, I guess, Disney, ABC and Infoseek, have 30 or 40, maybe even 50 websites up, and for the most part, we do use a fair amount of music on these websites, and the music use varies from, I guess, no music use all the way up to the radio station sites which are basically streaming retransmissions of our radio stations, which are extremely music intensive. Somewhere in between we have sites that will push music in the background of our sites. We have sites like Wall of Sound, which are focused on artists and albums and put up music in the context of reviewing artists. Some of the music is music that we own. Some of the music is music that we think we have a fair use position on, and under the fair use exception of the copyright law, doesn't need to be licensed. But the point is that we have any number of business models in our websites. We're experimenting with a lot of things, not

making money on most of them, or any of them probably, but the models are changing every day, and so in that environment it's very difficult for us to address some of these licensing issues in music as well as the licensing issues for all the other production elements that are used in the sites. So far because there's been so much uncertainty in the music licensing area, as lawyers we've sort of discouraged use of music on the sites as much as we can, and there's been enormous creative pressure from the people that are building the sites to let them experiment with music, but so far we've told them that the questions about what licenses are needed that have been mentioned here, whether we just need . . . I mean, and most of our sites are basically streaming sites. We're not, I don't think in any of our business models are in the download business yet, although the Disney record operations may get into that business at some point, but we're basically streaming, but even in the streaming environment, as other people have said here, it's sometimes unclear whether you just need a performance license or you need a performance and maybe another kind of license to cover distribution and to cover duplication, to cover even derivative works, and so, that confusion has been sort of a damper on a lot of our music use. Even in the performance environment, there's a fair amount of uncertainty about just what licenses apply in what scenario, what performance licenses? What performance license models apply?

On the ASCAP and BMI side, we have had conversations going on with ASCAP and BMI for the last couple of years. We have been trying to convince them to license us as a group rather than on a site-by-site basis, and ASCAP's been very responsive to that request, but we've always . . . in the broadcast environment, as Ron said, we've always had a real bias against revenue-based licenses because we think they're the wrong way to buy any production element, especially music. All the other production elements that we buy, we buy on a program by program basis whether it's talent, actors, writers, directors . . . whether it's underlying literary material, whether it's film clips . . . We buy those all on a program-by-program basis based on their value in the program, how much we're using, their value in the marketplace. Music is really the only thing over the years that we've bought on a bulk basis, at least performing rights, because most of our licenses, as Ron said, on the station side, on the network side are either flat rate licenses or percentage of revenue licenses that really don't have. . . or the amounts really don't have any relationship to the amount of music we're using or the importance of music to us, and in fact, in broadcasting, at least in television broadcasting, the importance of music has diminished a bit in the past few years cause we're going more toward reality-based programming and news programming, but those licenses

really don't take into account the real value music to us or the value of the music in the marketplace, so we've always had a bias against them, and when we saw the ASCAP and BMI licenses for the Internet, we had the same reaction because at the end of the day, they're basically revenue-based licenses.

And that may work well for some sites that are music-intensive, but it doesn't work quite as well for sites where the music use is incidental. Paying the same amount based on a percentage of revenues for a site that is music intensive to one that uses maybe one or two pieces of music in the course of a year or a week just doesn't make any sense. So we hope, especially with some of the technologies that Ron was mentioning, that ASCAP and BMI will be more receptive to licenses that more directly reflect music use. Licenses that maybe impose a fee based on the number of music streams that you're putting out, the amount of people that are accessing those streams, how long the streams are on . . . The technology is there now to measure all that stuff, and maybe coupled with some of this other technology, there's a way to construct licenses that reflect the actual use of music and the value of music a little more closely.

On the recording side, we, like everybody else, jumped fully into the loophole that we thought we had under the 1995 act to at least put our minds at ease that we didn't need to worry about the recording licenses because most of our sites, all our sites really, were non-subscription, non-interactive, but thanks to Steve's ingenuity and the RIAA, that loophole has been pretty firmly closed, so now we have to worry about the performance license for the recordings, as well. And that's been a real problem for us, and I guess the major problem is really our radio station sites. Like a lot of the other radio station owners, and I think we're up to about 35 or 40 or 50 stations now, which these days is not a lot compared with Chancellor and Clear Channel and some of the other owners, but we have a lot of our stations, music-formatted stations, that are now streaming on the Internet, and they're not really making any money at it. It's at this point I think they're up there more for their promotional value and the ego value, their ego-gratification of the stations. But still, they want to be up there, and we have a real problem trying to figure out just what we need to do about our stations. You know, if a guy like Lon Sobel can be confused about the digital performance rights law and whether stations are subject to the right or not subject to the right, at least it gives me some comfort because I haven't been able to figure it out.

But the problem we have is, if they're within the right, we have a choice between either negotiating with record companies on a case-by-case basis to try to clear the rights to each master that we play in the station or

qualifying for the compulsory license, but the problem is that most of our stations can't possibly qualify for the compulsory license. We quite often announce the songs before they're played; we quite often play a lot of songs by the same artist in the two-hour period . . . all things that you really can't do if you want to qualify for the license, and it's really difficult to tell a station manager that they've got to change their behavior, they've got to change the way their jocks introduce music in the air environment just to satisfy some requirements for a network compulsory license for retransmission. So, it's been a real conundrum for us, and we're talking to Steve and others about trying to somehow within the context of the CARP proceeding, clarify that, but all of this puts kind of a damper on people like us who want to use music on the Internet but can't really do it. But just like everything else in our business, these issues play out over time and eventually get resolved. We hope that we can find some creative solutions to it. As I said, I think both on the composition side, ASCAP/BMI side, and the RIAA master recording side, the technology exists to construct licenses that make use of the capabilities, the music-tracking capabilities that exist so that we can get away from some of the more traditional models that have been, we think, wildly inefficient and wildly inapplicable to a lot of our music-use models.

**RON GERTZ:** Thanks, Charlie. Another bit of subtext. Charlie mentioned that he is trying to discourage music use by some of his entities. One of my other clients, who owns 200 radio stations, has taken a different view. They have prohibited their stations from streaming on the Internet.

Our next speaker is Bob Kohn, and just to save Bob from being accused of shameless self-promotion, I will tell you that Bob and his father, Al Kohn, have written a wonderful book called *Kohn on Music Licensing*, and this shameless. . .

**BOB KOHN:** Is it shameless to do this?

**RON GERTZ:** No, it is not. . . although I must disclose that one of the reasons I said it is because I was given an acknowledgement in one of their first pages. . . . I was really glad to see the success of the book because the first guy that I ever negotiated a license with while I was in law school was Bob's father, Al. So on a scale of likeability, I like Bob, but I love his dad.

**BOB KOHN:** So do I. There's a lot I could talk about, but we will talk about the business models of how this digital download business is going to work. Our company is Goodnoise with a website Goodnoise.com. We'll soon be changing our name to Emusic.com, and that's going to be both the corporate name as well as the website. We're a public company. We sell MP3 files for 99 cents a track and 8.99 an album. August Grant's

discussion this morning could have been a page out of our business plan a year and a half ago with perhaps one exception, and that is, I'm not as optimistic on the application of encryption to protect music over the Internet, and we can discuss that in more detail if there are questions, or in the panel I'm going to be sitting on this afternoon. So, we do sell it for 99 cents a track, 8.99 an album. It's 99 cents because we're competing with zero, which is the piracy problem. We also want to make it an impulse buy, and I do agree with what was said this morning that we think it's going to perhaps double the size of the record industry as a result of the impulse buying and the ease of the use and the convenience that digital downloads give to the consumer. And we are going to make it easier to buy and to steal. We believe it is a convenience issue, and there are some real technological problems with trying to protect music on the Internet.

Now, what kind of licenses do we need in order to do digital downloads? And before . . . we all know, as Lon discussed this morning, you have two copyrights in each download. You have the copyright in the sound recording, you have the copyright in the underlying song. So let's begin with the underlying song. Well, first, clearly, under the 1995 act, Section 115, the compulsory license was modified to include digital phonorecord deliveries. In other words, a company like ours can compel music publishers to provide us with a license for the use of the underlying song for the statutory rate. We do pay the full statutory rate. It is our company policy to never ask a music publisher for a rate or anything less than the statutory rate. We have a license with the Harry Fox Agency that will greatly facilitate our obtaining of these licenses. We will pay the full statutory rate, and in several months, we'll begin to pay on a monthly basis rather than a quarterly basis. The Harry Fox license allows us to download the song or the recording to anywhere around the world, and if the publisher still requests, we will either pay at the statutory rate in the U.S. or the rate in which the customer is located, the country in which the customer is located. So that problem seems to be pretty well solved on the mechanical side. There [are] some questions as to whether the old mechanical licenses that the records labels that we work with have can be used, or whether we need to do it. If a label of ours that we work with has a license and they want to pay a lower rate, that's okay, we're happy to pay the difference. There's enough margin to go around. So at the end of the day, the publishers will always receive the statutory rate from us.

The other side of this, a discussion that we had this morning on performances . . . we do have an ASCAP license, we'll soon have a BMI license and a SESAC license for our website. We do a lot of streaming, real audio streaming of 30-second clips of the sound recordings that we

have to offer on the website, and it's quite clear that we need such a license. There are some companies out there who are taking some very interesting positions that I don't quite understand. For example, CD Now and Amazon and others who do streaming of music do not have licenses from ASCAP and BMI, which is quite shocking, cause it's pretty clear that they need one. Some of them are taking the position that they have a vendor establishment, in other words, like a record store exemption. Tower Records, for example, does not have to pay ASCAP and BMI because there's specific exemption under the law—I think it's 110. If you read it carefully, it doesn't apply to the Internet. The other problem with that is that what happens if you are streaming to someone located overseas, there is no such exemption for record stores in most countries around the world. So at the end of the day, I think, sites who do streaming on their websites of music need to have a license from the performance rights societies, and we think that ASCAP/BMI . . . and we will between talking to SESAC. We've already begun discussions and I've seen their license . . . are quite reasonable. We don't think we have any problem with paying a point and a half of our percentage to each of them—it's not quite that—of our revenues, our advertising revenues, for the use of the music. There is just no question about it that these songwriters and the publishers are entitled to it and there's certainly enough margin to go around when you don't have a cost-of-goods, returns, or inventory to deal with. Now, on the controversial question as to whether the performance license is required for a digital phonorecord delivery, that is still an open issue. It's quite an interesting issue. I don't think it's going to be resolved for some time. The performance rights societies are taking a position that it is a transmission, and since it's a transmission, it must be a performance, and if it's a performance, regardless of whether it's also a digital phonorecord delivery, you must get a performance license.

The problem with that argument, and I'll argue both sides of it, but the problem with that argument is Section 115, that is the compulsory license statute. It says, and it defines digital phonorecord delivery. I'll read the end first and then the beginning. It says, regardless of whether the digital transmission is also a performance of any non-dramatical musical work embodied therein, a digital phonorecord delivery is each individual delivery of a phonorecord which results in a specifically identifiable reproduction. In other words, regardless of whether it's also a performance, if it does these things . . . in other words it ends up in a copy on the end-user's hard disk, it's a digital phonorecord delivery. And if it's a digital phonorecord delivery, the statute says you only have to pay 7.1 cents, or the current statutory rate. So regardless of whether it's a



performance and whether they win that argument or not, it appears that you only require and you only have to pay the 7.1 cent or statutory rate.

Now, someone brought up earlier . . . I think it was Steven, actually, that there's a possibility that there are two different rates. There are incidental . . . a rate for incidental digital phonorecord delivery and a full digital phonorecord delivery, and they might argue for a higher digital phonorecord or statutory rate for digital phonorecord deliveries—a higher rate than for CDs. So that may come down the pike, and that's okay. We believe that most deliveries of music on the Internet at the end of the day are going to be digital phonorecord deliveries, and that just requires an understanding of how the client/server model works on the Internet. Right now you take a look at your browser and you browse the Internet, you'll notice all the pictures and all the things in the text files, etc., that get downloaded to your browser get cached onto your hard disk, and most of your browsers allow you to eliminate those files after 30 days. It's much more efficient to send you the bits and then let you consume the bits on your own time. In other words, there's no relationship between the amount of time it takes to deliver the bits to you and the amount of time it takes you to consume the bits. It's much more efficient for a server to send them all to you at once, and then go on to the next customer. So the question's going to be is how long are you going to keep it on your disk? There's a lot of data here, and there are a lot of issues on data storage, but at the end of the day, that's going to be the issue. So how it all works out between Harry Fox and the performance rights societies, we don't know. But, at the end of the day, you must pay for each digital download.

Now, finally, sound recordings. We just raised \$31 million. We're a public company. We're allocating half of that money—\$15 million—to pay advances for rights to do digital phonorecord deliveries from independent record companies. We're also offering equity in our company for artists with brand names and labels who have good catalogs. So if there are any attorneys out there who represent labels or artists, do not provide your digital phonorecord deliveries to anyone without sending me an e-mail. (audience laughter) It's [Bob@emusic.com]. And I'm serious about that. We have licensed the Ryko Catalog, which we started with Frank Zappa, Christine Hearst, and Morphine. We have several other independent labels that we've signed that we haven't announced quite yet because they're not on the website—we like to announce the same day of having it all on our website. We probably have about 150,000 tracks licenses at this point for just about every genre. So you'll be able to go to Emusic.com and you'll be able to get Ella Fitzgerald and Frank Sinatra. It may not be Capitol Records' Frank Sinatra. It may not be Capitol Records

or EMI or Sony and some of those, but we have the rights to that. We have the rights to many of the . . . They Might Be Giants is on our website, and certain other labels, certain other artists who have been dropping from record labels right now who are looking for deals or considering splitting off their digital rights to a company like ours and then providing the physical rights to some of the independents, and we're happy to work with them to provide the artist with deals with the independents.

As a matter of fact, in one instance, we've offered to pay advances to the independent record labels so that they can get the physical rights to the recording so that we could get the digital download rights. We're not in the business of providing physical distribution of CDs. We want to partner with record labels.

We are not a record company. We do not develop acts, we don't know how to promote acts, we're not in the business of making hits. We believe that on the Internet, with every garage band in the world being able to put their own music on their own website, so much noise is going to be created it's going to be very difficult to get above the noise level, and the one thing that's not scalable like computers it's good A&R and good promotion. We think independent record labels are going to become more important in the future, not less important. These are the people who are generally focused on a particular genre. They're generally focused on a particular region. They match the groups with producers, they finance their records, they help them with songwriter talent and they support regional touring. All of the good A&R has been coming out of the independent record labels over the past several years. So we want to partner with these companies and help them grow their businesses and be their source for distribution and marketing over the Internet, and the labels who have been signing up with us in the early stages, can actually get a significant kicker, I suppose, by having an interest in our company. So, that's that. Now, I do want to say before closing because we are running out of time. We can talk more about that this afternoon, that I agree, Steve Marks did a great job last summer for the RIAA. He certainly earned his salary and helped Hillary Rosen in what he was able to accomplish there.

**STEVEN MARKS:** I wish I had taped these comments.

**BOB KOHN:** They are on tape so you can . . . Now, there was one question that was raised this morning as part of Lon's discussion I want to raise now, and that is, whether a radio station who takes its analog broadcasts over the air and then puts them over the Internet and feeds over the Internet, whether that requires this compulsory license or any license from the record companies. And I want to make a correction that in the article that's in the materials that I wrote back in September, which you'll

find on. . . . I don't where these pages are numbered . . . but it's called a Primer on the Law of Webcasting and Digital Music Delivery. I provide some of the history there of how this October act came into existence, through some remarkable coincidences in timing issues with regard to the Digital Millenium Copyright Act and what had happened with respect to DiMA and the RIAA and some things that I was writing on the Internet. I do certainly believe that prior to the amendment to the Digital Act that anyone doing non-interactive, non-subscription transmission did not need a license from the record companies. I think that they may have blown the negotiations back in 1995 by focusing on subscription transmissions when the business model of the Internet turned out to be non-subscription or advertising-based websites. But they did manage to correct that, I think, and did a good job for the record companies they represent. But the question is whether a radio station can take their analog transmissions and then broadcast them digitally over the Internet. I think Steve Marks did an incredible job because I was wrong in my article. I think that exemption went away and he actually pointed out to me where it went away and that it's in the definition of an eligible transmission, if I'm not mistaken. So, let me repeat that we pay advances for digital download rights to sound recording, and I'll take any questions with the panel. Thanks.

**RON GERTZ:** Thanks, Bob. Jay Dougherty, several weeks ago, while we were in Palm Springs for a seminar, and we're sitting on the veranda and Jay said to me, "You know, I was thinking, Ron, I wonder what would happen if so-and-so and so-and-so . . ." So I'm going to let him ask the question.

**JAY DOUGHERTY:** Well, this question is addressed to the record folks on the panel, and that is, the digital performance right applies to sound recordings protected under the Copyright Act, which now covers all foreign sound recordings, and domestic recordings made after February of 1972. What's the situation regard to pre-1972 domestic sound recordings, which of course includes a whole lot of great stuff? Is there a digital performance right? Is it covered by any of these licenses at all?

**STEVEN MARKS:** Well, I mean, I think what . . .

**JEREMY SILVER:** I'll let him speak for us on this one.

**STEVEN MARKS:** I think what you said is, you know, there is obviously a date limitation, but most of those recordings have been digitally mastered or re-mastered since that time, so in practice, I think lots of recordings that you would think of that, you know, may not fit within that time period actually do because the recordings have been redone.

**JAY DOUGHERTY:** Sufficiently changed to become a new derivative work recording post '72?

**STEVEN MARKS:** I think so.

**RON SOBEL:** You kind of said that quietly, Steve. (laughter)

**STEVEN MARKS:** Yes. Yes.

**JAY DOUGHERTY:** Specifically going from mono to stereo doesn't constitute a derivative work, or does it?

**STEVEN MARKS:** I honestly don't have an answer to that. I don't know.

**RON SOBEL:** Yes.

**AUDIENCE MEMBER:** How, for Jeremy and Steve and Ron . . . how do you see promotional music videos with the accompanying audio falling into agreements?

**STEVEN MARKS:** Videos are audio-visual works.

**AUDIENCE MEMBER:** A streaming video, with accompanying audio.

**STEVEN MARKS:** Yeah, it would be an audio-visual work, and therefore, falls outside the compulsory licenses, for instance, that we've talked about, because that only deals with sound recordings. But licenses still need to be obtained, for instance, to sync sound recordings into audio-visual works. That remains unchanged by any of the new laws.

**JEREMY SILVER:** We don't license very much of what we do to anybody. If you go to Streamland or Tunes, you know, the Rolling Stone network or any of those places, you'll see a few videos from some of our companies but not many. And we're holding onto that for the moment, but we won't. I mean, we really see licenses and we will get into conversations. We already have those conversations with people, as well, on a direct, label-by-label basis.

**RON SOBEL:** And if I could just clarify, to follow-up and to clarify, there was an earlier question on a 30-second rule or a four-bar rule. From ASCAP's perspective, at this point, we're really clear that a 30-second clip is just as licensable as a full song. We don't make any distinction at all.

**BOB KOHN:** On that issue, that's absolutely correct. There is nothing in the law that provides anyone with a 30-second exemption, and clearly, even a 30-second stream of a clip off a website will require a license from the underlying music publishers. What Harry Fox has done, from what we understand on a very informal basis, they've broadcast at least to the Internet community that if you have a license from the owner of the sound recording, you can put up a 30 second sample, and they will not consider that an interactive transmittal, or they will not consider that a digital phonorecord delivery requiring a payment of a statutory rate. So, you do need to have for streaming a performance right, and if you have a

license from the owner of the record or if you own the record, then you can do a 30-second sample. Now, that's not anything that's written anywhere . . .

**STEVEN MARKS:** Yeah, it is actually. It's in the regulations for the mechanical. . . It's part of the regulations for the physical rates for mechanical fees.

**BOB KOHN:** All right, that's news to me. Next supplement.

**JAY DOUGHERTY:** There's a 30-second license from a record company in our materials too. The Warner Brothers form for 30-second promotional use of a record is one of the last documents in this handout material. We'll talk about it a little bit in the panel.

**RON GERTZ:** Lon?

**LON SOBEL (in Audience):** I was going to follow up with a more specific version of the question about video streaming and the extent to which it requires a license from the record company. It's still a situation in which a producer of motion pictures or video, for that matter, does properly acquire, not only a sync license from the music publisher, but also a master use license from the record company. But the terms of the license say nothing at all about . . . that is to say, with the record company. So there's nothing at all about what the movie or video producer is going to do with the video or movie, and one of the things a movie or video producer then does with it is to Internet stream clips or even eventually the whole thing, but given today's technology, video streams clips. Isn't it the case that . . . all the way ASCAP, BMI and SESAC license would be necessary because that would constitute a performance. No license would be necessary for, from the record company because that's now the streaming of an audio-visual work, and it doesn't have to be licensed at all.

**STEVEN MARKS:** Yeah, well, I think it's a contractual matter. I mean, the answer is that it's a contractual issue depending on that original contract. I mean . . .

**JEREMY SILVER:** We wouldn't issue a license that was that unspecific anyway. You said the producer would require a license, but, you know, the license would be quite specific about what applications and what the use . . .

**BOB KOHN:** It might say exhibition or broadcast.

**JEREMY SILVER:** No, it would be very clear today.

**RON SOBEL:** Lon, the ones we've seen are pretty specific. I mean, I think. . . Ron told me that some even exclude the Internet. . . some of the sync licenses we get exclude the Internet completely.

**STEVEN MARKS:** Lon, I think the point you're making, though, is the distinction between an audio-visual work and a sound recording and that the performance right specifically is with regard to, you know, sound recording, so it goes back to the contract about whether, you know, that syncing covered those types of uses that were performances on the Internet.

**LON SOBEL (*in Audience*):** And that's why a well-represented record company that didn't want to hear its recordings show up on the Internet without additional fees would draft a master use license with a producer that made it plain the producer wasn't entitled to stream video clips without a further negotiation.

**STEVEN MARKS:** Right.

**AUDIENCE MEMBER:** Is there any form for EMI?

**JEREMY SILVER:** Been there, done that.

**RON GERTZ:** By the way, there's another issue here. We've been talking about performing rights, but there's a whole issue of the ephemeral recording rights as well. Section 112A. There's a question about how far that goes. How far somebody can go to make a recording for purposes of facilitating broadcast. 112A basically says that a user can make one recording, subject to certain limitations. There's also a statutory license now in 112—I think it's 112e—that allows certain users, those who qualify for a statutory performance license, to make multiple copies on servers to facilitate transmissions. But all of that stuff is still up in the air and we're still trying to figure out how that applies. Maybe one more question. Sure.

**AUDIENCE MEMBER:** Bob Kohn, what you're selling is Mp3 files, correct?

**BOB KOHN:** That's correct.

**AUDIENCE MEMBER:** How do you keep folks from duplicating them once they're out there?

**BOB KOHN:** There's . . . even if it doesn't matter what format it's in, there's no way to stop them technologically from making copies. There's nothing SDMI can do, there's nothing Liquid Audio, A2B or anything anyone else can do to stop people from making copies. It's much too easy to circumvent.

**RON GERTZ:** We just price recording . . .

**STEVEN MARKS:** I don't think we'd agree with that, but . . .

**JAY DOUGHERTY:** We're going to have a panel later today on that topic.

**STEVEN MARKS:** Yeah, I mean, that's a whole other issue. I think there's really two issues. I mean, one is whether something's hack-proof, and one is whether it's, you know, hack-proof enough that honest people

are kept honest, that you make it difficult enough that only people, you know, college kids with tons of time and tons of . . .

**BOB KOHN:** It's going to be very difficult if you have an MP3 file next to an encrypted file with . . . based on a private key which can be lost at the same price, to convince a consumer to buy something that's the more inconvenient version versus the version that's an MP3.

**STEVEN MARKS:** Well, that's why you develop alternative markets and migrate people to new markets by, you know, offering additional value, etc., and by continuing to enforce against . . . I mean, if it takes somebody hours to get to an MP3 site and every time they go up they're dead links or they can't get the song, that's not the kind of consumer experience that's going to lead somebody to try and avoid, you know, buying a song legitimately.

**BOB KOHN:** It'll be a longer conversation in the afternoon, but the bottom line is that you gotta recognize that what the Internet has done has shift the power to the consumer, and you've to find business models that embrace that rather than using old world models to try to go against the grain. The software industry experienced this back in the 1980s, and they gave up on it. Anything that causes a user inconvenience. . . I mean, the Internet is all about convenience, and they'll be enough people who pay for the music rather than steal it to make a very, very good business. . .

**STEVEN MARKS:** Well, I think . . .

**JEREMY SILVER:** It's not just Microsoft going out of business as a result of that, Bob. (laughter)

**BOB KOHN:** Well, Microsoft . . . for every dollar that Microsoft gets in revenues, they lose a dollar to piracy. That's \$40 billion. That's the entire size. . . that's the size of the entire record industry. And they don't seem to be worrying too much about. . .

**JEREMY SILVER:** I don't know how you can possibly you calculate that.

**BOB KOHN:** Well, we'll talk about it later on. There's a lot more detail.

**RON GERTZ:** Just to put a final gloss on this, again, I recommend the book to you *Information Rules*. One of the first things that they said in that book was that copyright owners need to look at their terms and conditions of their contracts to maximize the value of the works being distributed, not to maximize protection because maximizing value is the only way to make money; maximizing protection is a *loser*. Time for lunch. Let's go. Thank you, everybody.