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IP Value Commentator

Maximizing the financial return from Intellectual Property April 2003

The Webcast Royalty Debacle: Lessons for Copyright Owners

by Barry Werbin

Something went terribly wrong.

It shouldn't have taken three-and-a-half years and an act of Congress to set compulsory royalty rates for a new and rapidly-evolving industry.

Alas, that's precisely what happened when the government tried to set royalty rates for webcasters (i.e., providers of streaming music via the Internet).

Everyone concerned in this royalty-setting process has been being hurt by the delay and confusion. During these several years, approximately 1500 U.S. webcasters were driven off the Net altogether—30 percent of the country's total webcasters, according to George Bundy, CEO of San Francisco-based BRS Media. At the same time, the number of foreign webcasters (who were unaffected by any U.S.-imposed royalty rates) continued to grow, said Bundy.

As a result, consumers' choices for streaming music were significantly limited. This in turn hurt CD sales for music companies' lesser known artists, since the public is less likely to hear (and so want to buy) music from these artists, who desperately need some exposure.

The worst part, however, is that the forces which created this mess are not unique to webcasting. Copyright owners, fueled by sometimes exaggerated fears of new technologies and a desire to extract the greatest short-term royalties, are waging a highly publicized series of legal wars involving MP3 distribution, encryption controls, digital recording and streaming media.

There is a better way, however, if copyright owners are willing to learn from the webcast royalty fiasco.

Section 114 of the Copyright Act authorizes webcasters to stream copyrighted music over the Net, provided they pay a statutory license fee to the music's copyright owners. But problems began when the Recording Industry of America (RIAA), as the copyright owners' agent, sought to set rates applicable to all webcasters, including small and non-commercial operators.

The Digital Media Association (which represented many webcasters) failed to reach terms on compulsory rates with the RIAA. As a result, the rate-setting process shifted in July 2000 to an Internet radio copyright arbitration royalty panel (CARP) appointed by the Copyright Office.

This left an entire fledgling industry in dangerous limbo, not knowing whether the ultimate rates would be based on a percentage of a webcaster's revenues or assessed on a per-song basis. Moreover, regardless of the rate structure outcome, the final rates would be retroactive to 1998. Paying this huge retroactive bill could be devastating to many small webcasters, who faced the prospect of having to shut down rather than pay.

THE CARP GOES BAD

Many of the webcasters' worst fears seemed to be realized in February 2002. The CARP recommended a royalty of 0.14 cents per performance for Internet-only retransmissions and 0.07 cents for retransmissions of AM/FM radio broadcasts, regardless of the webcaster's income. But while a webcaster might reach tens of thousands of listeners, its income might be de minimus after expenses, forcing it to either stop webcasting, or pay compulsory rates that would insure its bankruptcy. Not coincidentally, many such webcasters were effectively precluded from the CARP process; they lacked the necessary time and money to be involved in the complex procedures.

Webcasters complained vociferously about the CARP ruling, and on July 8, 2002, the Librarian of Congress (LOC) reduced the flat rate per song for Internet-only retransmissions to 0.07 cents. Yet, the Librarian rejected the request of small and non-commercial webcasters to base that royalty on a percent of revenues rather than per performance.

Many Internet broadcasters were highly critical of the LOC decision, arguing that even a 0.07 cent per performance/per listener rate would strangle many broadcasters in an economy that still was struggling to get back on its feet and where advertising revenues were down significantly.

REPEATING PAST MISTAKES

Congress then stepped in to quell a potential political storm. It passed, and the President signed, The Small Webcaster Settlement Act of 2002. The Act permits the RIAA to negotiate special, lower rates directly with small commercial and all non-commercial webcasters. These rates are to be based

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on a percentage of revenues or expenses, or both, plus a minimum fee.

The Act reflects the type of compromise that should have been reached through the CARP process. Had the RIAA's initial stance been tempered to support a more structured royalty system based on actual market share or revenue per webcaster, a more realistic market-driven structure would have emerged that would have satisfied both the goals of fairly compensating copyright owners and maximizing public exposure to copyrighted works through new technology.

This is not the first time that institutional copyright owners have come down too hard on new technology affecting their products. When VCR sales took off in the early 1980's, for instance, the major broadcast networks and film studios waged a futile battle to stop consumers from using these devices. However, the TV and movie industries' fears of lost advertising revenues and sales never came to fruition; rather, video sales and rentals skyrocketed and spawned a new profitable market for the very same industries that sought to kill the new media outlet in its cradle.

Copyright owners are still repeating the mistakes of the past. They are now engaged in efforts to stifle a wide variety of new technologies, from file-sharing to DVD burning.

Rather than fighting to kill off these nascent technological markets that offer services craved by the public, a better strategy would be to seek cooperation, coexistence and common ground that would both protect valuable copyrights through fair but reasonable royalties, while giving these new technologies breathing room to grow and thereby give the pubic what it wants.

The public demand for new media technologies will not subside, especially as improved broadband access becomes cheaper and widespread. For every Napster that's killed off, a dozen more file sharing services pop up. Copyrights are of course to be protected, but wiping out entire markets without offering the public any reasonable alternative is a disservice that is detrimental to copyright owners' profits—and to the goal of our copyright law to promote the public's access to new works in music, art and science. **IPV**

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For a more complete discussion of the legal and regulatory processes for setting webcast royalties, see the expanded version of this article at www.ipnewsletters.com.