

provided that the services pay a reasonable royalty fee and comply with the terms of the statutory license. Among the categories of services that may use the section 114 license are preexisting subscription services¹ of which there are only three: Digital Cable Radio Associates, now known as Music Choice; DMX Music, Inc. ("DMX"); and Muzak, L.P. ("Muzak").

Rates and terms for this license are established in one of two ways. Interested parties may either negotiate rates and terms which, if approved through a notice and public comment proceeding, become the final rules for the relevant license period. Alternatively, if industry representatives cannot reach a voluntary settlement, the Librarian of Congress convenes a three-person Copyright Arbitration Royalty Panel ("CARP") for the purpose of determining the applicable rates and terms.

In 1995, the Librarian of Congress initiated the first rate adjustment proceeding for the purpose of setting rates and terms of payment for use of sound recordings by the preexisting services pursuant to the section 114 license. The three preexisting subscription services and the Recording Industry Association of America ("RIAA") participated in this proceeding which concluded with the issuance of a final rule and order by the Librarian of Congress. *See* 63 FR 25394 (May 8, 1998).

In that proceeding, the parties proposed, and the CARP adopted, a term which gave the RIAA the responsibility for collecting and distributing the royalty fees to all copyright owners. *Id.* at 25397. The Librarian adopted this term, then crafted additional regulations that afforded copyright owners a means to verify the accuracy of the royalty payments made by the RIAA collective,² established the value of each performance, specified the nature of the costs that RIAA may deduct from the royalty fees prior to distribution, and set forth a procedure for handling royalty fees in the case

where the collective is unable to identify or locate a copyright owner who is entitled to receive royalties collected under the statutory license.

RIAA appealed both the rate set by the Librarian and the additional conditions imposed on the RIAA collective in its capacity as the collection agent for copyright owners. *See, Recording Industry Ass'n v. Librarian of Congress*, 176 F.3d 528 (D.C. Cir. 1999). The United States Court of Appeals for the District of Columbia Circuit upheld the rate set by the Librarian and found that the Librarian has the authority to impose terms on copyright owners or their agents. However, it remanded for further consideration certain terms imposed on RIAA under 37 CFR 260.2(d), 260.3(d), 260.6(b), and 260.7, because the CARP had not considered these issues, leaving the record devoid of any evidence upon which to fashion any terms concerning the collection and distribution of the royalty fees. *Id.* at 536.

On February 13, 2001, the Copyright Office initiated a new proceeding to consider the terms remanded by the court with the issuance of a scheduling order, directing the parties to this proceeding to file their direct cases with the Office on April 17, 2001. *See, Order in Docket No. 96-5 CARP DSTR* (February 13, 2001). However, instead of filing a direct case on April 17, RIAA filed a petition to establish terms governing the RIAA collective and to suspend the scheduled proceeding. No party to the original proceeding objected to the proposed terms. In fact, Music Choice had already informed the Office by letter dated February 26, 2001, of its intent not to participate further in this proceeding and that it did not object to the terms to be proposed by RIAA.

Subsequently, RIAA revised these terms to remove a reference to the section 112 statutory license for the making of ephemeral copies and to make clear that membership in the collective is open only to those copyright owners whose works are subject to statutory licensing and thus generate the funds to be distributed by the collective. RIAA also asked the Copyright Office to publish the revised terms pursuant to § 251.63(b). This provision allows the Librarian of Congress to adopt proposed terms that are the result of settlement negotiations, provided that no person with a substantial interest and an intent to participate in a CARP proceeding files an objection. This procedure to adopt negotiated rates and terms in the case where an agreement has been reached has been specifically endorsed by Congress.

If an agreement as to rates and terms is reached and there is no controversy as to these matters, it would make no sense to subject the interested parties to the needless expense of an arbitration proceeding conducted under (section 114(f)(2) (1995)). Thus, it is the Committee's intention that in such a case, as under the Copyright Office's current regulations concerning rate adjustment proceedings, the Librarian of Congress should notify the public of the proposed agreement in a notice-and-comment proceeding and, if no opposing comment is received from a party with a substantial interest and an intent to participate in an arbitration proceeding, the Librarian of Congress should adopt the rates embodied in the agreement without convening an arbitration panel.

S. Rep. No. 104-128, at 29 (1995)(citations omitted).

Accordingly, the Copyright Office published the proposed terms in the **Federal Register** and requested public comment. 66 FR 38226 (July 23, 2001). In response to this notice, the American Federation of Musicians ("AFM") and the American Federation of Television and Radio Artists ("AFTRA") filed a Notice of Intent to Participate and objections to certain of the proposed terms. Shortly thereafter, RIAA began discussions with AFTRA and AFM, regarding their objections, and the matter has been held in abeyance.

Since that time, a significant event has occurred that bears directly on the resolution of this proceeding. In December of 2002, Congress passed the Small Webcaster Settlement Act of 2002 ("SWSA"), Public Law 107-321, 116 Stat. 2780. Among other things, the SWSA amended 17 U.S.C. 114(g) in two important ways which address specific issues which are the subject of this proceeding. First, the SWSA provides for direct payment to featured recording artists and to the administrators of the escrow accounts provided for in 17 U.S.C. 114(g)(2)(B)&(C). Second, the act allows a designated agent, prior to the distribution of the royalty receipts, to deduct reasonable costs incurred by that agent in the administration of those receipts, including, but not limited to, costs associated with the collection and distribution of the royalty fees and the costs incurred in the participation of negotiations or arbitration proceedings under sections 112 and 114.

Because of these changes in the law, RIAA has again revised its proposed amendments to 37 CFR 260 to conform the terms in dispute to the new law and, in doing so, it has addressed the concerns of AFM and AFTRA. Consequently, AFM and AFTRA have withdrawn their objections to the proposed terms and their Notice of Intent to Participate in a CARP

¹ A "preexisting subscription service" is defined as: A service that performs sound recordings by means of noninteractive audio-only subscription digital audio transmissions, which was in existence and was making such transmissions to the public for a fee on or before July 31, 1998, and may include a number of limited number of sample channels representative of the subscription service that are made available on a nonsubscription basis in order to promote the subscription service. 17 U.S.C. 114(j)(11).

² In November 2000, RIAA formed "SoundExchange," an unincorporated division of RIAA, to administer statutory licenses, including its responsibilities under the Librarian's May 8 Order. *See, Revised RIAA Petition to Establish Terms Governing SoundExchange* at 1 n.1.