(OMB) under Executive Order 12866 (Regulatory Planning and Review).

Executive Order 12988

The Department of the Interior has conducted the reviews required by section 3 of Executive Order 12988 (Civil Justice Reform) and has determined that, to the extent allowed by law, this rule meets the applicable standards of subsections (a) and (b) of that section. However, these standards are not applicable to the actual language of State regulatory programs and program amendments since each such program is drafted and promulgated by a specific State, not by OSM. Under sections 503 and 505 of SMCRA (30 U.S.C. 1253 and 1255) and 30 CFR 730.11, 732.15, and 732.17(h)(10), decisions on proposed State regulatory programs and program amendments submitted by the States must be based solely on a determination of whether the submittal is consistent with SMCRA and its implementing Federal regulations and whether the other requirements of 30 CFR Parts 730, 731, and 732 have been met.

National Environmental Policy Act

No environmental impact statement is required for this rule since section 702(d) of SMCRA (30 U.S.C. 1292(d)) provides that agency decisions on proposed State regulatory program provisions do not constitute major Federal actions within the meaning of section 102(2)(C) of the National Environmental Policy Act (42 U.S.C. 4332(2)(C)).

Paperwork Reduction Act

This rule does not contain information collection requirements that require approval by OMB under the Paperwork Reduction Act (44 U.S.C. 3507 *et seq.*).

Regulatory Flexibility Act

The Department of the Interior has determined that this rule will not have a significant economic impact on a substantial number of small entities under the Regulatory Flexibility Act (5 U.S.C 601 *et seq.*). The State submittal which is the subject of this rule is based upon corresponding Federal regulations for which an economic analysis was prepared and certification made that such regulations would not have a significant economic effect upon a substantial number of small entities. Accordingly, this rule will ensure that existing requirements previously promulgated by OSM will be implemented by the State. In making the determination as to whether this rule would have a significant economic impact, the Department relied upon the data and assumptions for the corresponding Federal regulations.

Unfunded Mandates

OSM has determined and certifies pursuant to the Unfunded Mandates Reform Act (2 U.S.C. 1502 *et seq.*) that this rule will not impose a cost of $100 million or more in any given year on local, state, or tribal governments or private entities.

List of Subjects in 30 CFR Part 918

Intergovernmental relations, Surface mining, Underground mining.

Dated: April 28, 1997.

Brent Wahlquist,

Regional Director, Mid-Continent Regional Coordinating Center.

For the reasons set out in the preamble, 30 CFR Part 918 is amended as set forth below:

PART 918—LOUISIANA

1. The authority citation for Part 918 continues to read as follows:

Authority: 30 U.S.C. 1201 *et seq.*

2. Section 918.15 is amended in the table by adding a new entry in chronological order by "Date of final publication" to read as follows:

§ 918.15 Approval of Louisiana regulatory program amendments.

* * * * *

Original amendment submission date	Date of final publication	Citation/description
* *	* *	* * * *
October 24, 1997	May 8, 1998	Sections 105.; 2537.A.11.; 2725.A., A.2., A.3., A.3.a., C.1., F; 2907.C.5.; 3705.A.2., A.2a., A.2.b.; 3711.A., B.1. through B.6.; 3717.A., A.2., A.3.; 4501.A.3., A.4.; 5333.A.1. through A.13.; 5411.A.; 5413.A.; 5503.A.2.; 5507.A.4.; 6507.A.2.; 6913 .B.; 6915.B.1.; 6917.A.; 7105.C.

[FR Doc. 98-12249 Filed 5-7-98; 8:45 am]

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LIBRARY OF CONGRESS

Copyright Office

37 CFR Part 260

[Docket No. 96-5 CARP DSTRA]

Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings

AGENCY: Copyright Office, Library of Congress.

ACTION: Final rule and order.

SUMMARY: The Librarian of Congress, upon recommendation of the Register of Copyrights, is announcing the determination of the reasonable rates and terms for the compulsory license permitting certain digital performances of sound recordings.

EFFECTIVE DATE: May 8, 1998.

ADDRESS(ES): The full text of the public version of the Copyright Arbitration Royalty Panel's report to the Librarian of Congress is available for inspection and copying during normal working hours in the Office of the General Counsel, James Madison Building, Room LM-403, First and Independence Avenue, SE., Washington, DC, 20540.

FOR FURTHER INFORMATION CONTACT: David O. Carson, General Counsel, or Tanya Sandros, Attorney Advisor, Copyright Arbitration Royalty Panel (CARP), PO Box 70977, Southwest Station, Washington, D.C. 20024. Telephone (202) 707-8380. Telefax: (202) 707-8366.

SUPPLEMENTARY INFORMATION:

I. Background

The Digital Performance Right in Sound Recordings Act of 1995 (DPRSRA), Public Law 104-39, 109 Stat. 336, amended section 106 of the Copyright Act, title 17 of the United States Code, to give sound recording copyright owners an exclusive right, subject to certain limitations, to perform publicly sound recordings by digital audio transmissions. 17 U.S.C. 114. The bill affords certain digital transmission services a compulsory license to perform digital sound recordings publicly. The purpose of the bill is ''to provide copyright holders of sound recordings with the ability to control the distribution of their product by digital transmissions, without hampering the arrival of new technologies, and without imposing new and unreasonable burdens on radio and television broadcasters.'' S. Rep. No. 104–128, at 15 (1995).

All non-exempt digital subscription transmission services are eligible for the statutory license, provided that they are non-interactive and comply with the terms of the license. The statute requires that the service not violate the ''sound recording performance complement,''[1] not publish in advance a schedule of the programming to be performed, not cause any receiving device to switch from one program channel to another, include in each transmission certain identifying information encoded in each sound recording, pay the royalty fees and comply with the associated terms, and comply with any recordkeeping requirements promulgated by the Copyright Office.[2] 17 U.S.C. 114(d)(2)(A)–(E) and 114(f)(2)–(5).

The reasonable terms and rates of the section 114 statutory license are determined by voluntary negotiations among the parties and, where necessary, compulsory arbitration conducted under chapter 8 of the Copyright Act, title 17. 17 U.S.C. 114(f).

II. The CARP Proceeding To Set Reasonable Rates and Terms

On December 1, 1995, the Librarian of Congress (Librarian) initiated the statutorily mandated six month negotiation period within 30 days of the enactment of the DPRSRA, pursuant to section 114(f)(1) of the Copyright Act, with the publication of a notice initiating the voluntary negotiation process for determining reasonable terms and rates of royalty payments. *See* 60 FR 61655 (December 1, 1995). In the notice, the Library instructed those parties with a significant interest in the establishment of the reasonable terms and rates for the section 114 license to file a petition with the Copyright Office no later than August 1, 1996, in the event that the interested parties were unable to negotiate an agreement. *Id.*

Accordingly, the Recording Industry Association of America (RIAA) filed a petition with the Copyright Office in which it asked the Office to initiate an arbitration proceeding pursuant to chapter 8 of the Copyright Act. After making a determination that the petitioner RIAA had a significant interest in the proposed CARP proceeding, the Librarian published a notice setting the schedule for the 45-day precontroversy discovery period and announcing the date for the initiation of the 180-day arbitration period. 61 FR 40464 (August 2, 1996). The exchange of documents during the precontroversy discovery period did not proceed smoothly, requiring the Office to reschedule portions of the discovery period and vacate the scheduled date for the initiation of the CARP. *See* Order in Docket No. 96–5 CARP DSTRA (September 18, 1996); Order in Docket No. 96–5 CARP DSTRA (November 27, 1996). The Librarian announced the initiation of the 180-day arbitration period following the conclusion of the discovery period and the resolution of all pending motions. 62 FR 29742 (June 2, 1997).

The Parties

There are four parties to this proceeding: three digital audio subscription services (the Services) and the Recording Industry Association of America (RIAA).

1. The Recording Industry Association of America, Inc. (RIAA)—RIAA represents a collective, consisting of more than 275 record labels, established for the express purpose of administering the rights of these sound recording copyright owners. RIAA represents the interests of its members who are the copyright owners of more than 90% of all legitimate sound recordings sold in the United States. Record companies own the copyrights in the sound recordings.

2. Digital Cable Radio Associates (DCR)—A digital audio service established in the United States in 1987 by the Jerrold Communications Division of General Instrument Corporation. Current partners include Warner Music, Sony Corporation, EMI, Time Warner Cable, Continental Cablevision, Comcast Cable, Cox Cable, and Adelphia Cable.

3. Digital Music Express, Inc. (DMX)—A digital music subscription service established in 1986 as International Cablecasting Technologies, Inc. In 1997, DMX merged into TCI Music, Inc., a publicly traded company with approximately 80% of its shares held by TCI, Inc.

4. Muzak, L.P.—With roots dating back to 1922, Muzak is America's oldest background music provider for businesses. In the 1920s and 1930s, Muzak was part of the consumer music market until driven out of that market by the growing popularity of radio. Muzak remained out of the market until March, 1996, when it began providing 27 channels of digital music under the name DiSHCD, as part of Echostar's satellite-based DiSH Network.

The Position of the Parties at the Commencement of the Proceeding

RIAA, representing the interests of the sound recording copyright owners, requested a royalty rate set at 41.5% of a Service's gross revenues resulting from U.S. residential subscribers, or in some circumstances, a flat rate minimum fee. Report of the Copyright Arbitration Royalty Panel (Report) ¶ 33. RIAA also agreed to be named the single entity to collect, administer, and distribute the royalty fees. Report ¶ 184. RIAA proposed additional terms concerning the timing of payments, statements of accounts, retention of records, and audits. Report ¶ 33.

The three digital audio subscription services requested a royalty rate ranging from a low of 0.5% to a high of 2.0% of gross revenues resulting from U.S. residential subscribers, and unanimously opposed a flat rate minimum fee. Report ¶¶ 34–36, 172. The Services proposed that a single private entity or a government agency be named for purposes of administering the royalty fees, but proposed submitting payments on a quarterly basis rather than a monthly basis. Report ¶¶ 184–185. In addition, the Services proposed terms concerning recordkeeping and audits, confidentiality of business records, and payment terms for distributing license fees among featured artists and nonfeatured musicians and vocalists.

[1] (7) The ''sound recording performance complement'' is the transmission during any 3-hour period, on a particular channel used by a transmitting entity, of no more than—

(A) 3 different selections of sound recordings from any one phonorecord lawfully distributed for public performance or sale in the United States, if no more than 2 such selections are transmitted consecutively; or

(B) 4 different selections of sound recordings—

(i) By the same featured recording artist; or

(ii) From any set or compilation of phonorecords lawfully distributed together as a unit for public performance or sale in the United States, if no more than three such selections are transmitted consecutively: *Provided,* That the transmission of selections in excess of the numerical limits provided for in clauses (A) and (B) from multiple phonorecords shall nonetheless qualify as a sound recording performance complement if the programming of the multiple phonorecords was not willfully intended to avoid the numerical limitations prescribed in such clauses.

17 U.S.C. 114(j)(7).

[2] See Notice of Proposed Rulemaking, 61 FR 22004 (May 13, 1996); Notice of Proposed Rulemaking, 62 FR 34035 (June 24, 1997).

The Panel's Determination of a Reasonable Rate

The Panel evaluated the four statutory objectives,[3] and their component parts, in light of the evidence and determined that the digital audio subscription services should pay a royalty fee of 5% of gross revenues resulting from U.S. residential subscribers. Report ¶¶ 196, 200. This rate represents the midpoint of the range of possible license rates that the Panel considered appropriate (but not the midpoint of the parties' proposals). The Panel further concluded that there was no reason to impose a minimum license fee on the Services at this point, and consequently, it rejected RIAA's proposal to set a minimum fee based on a flat rate. Report ¶ 204.

In making this determination, the Panel followed the precedent set in prior rate adjustment proceedings conducted by the former Copyright Royalty Tribunal and other CARP panels which, as a first step, determined a range of possible rates after considering different proposed rates based on negotiated licenses or analogous marketplace models. Report ¶ 123. *See also,* 1980 Adjustment of the Royalty Rate for Coin-Operated Phonorecord Players, 46 FR 884 (January 5, 1981), and the 1997 Rate Adjustment of the Satellite Carrier Compulsory License Fees, 62 FR 55742 (October 28, 1997). Each party offering a ''benchmark'' rate contends that the rate it offers represents the cost for similar products in analogous markets. The Panel considered three benchmarks, weighing each in light of the record evidence to determine whether the proposed models shed light on how the marketplace would value a performance license in sound recordings. Once the Panel identified the useful models, it used the corresponding rate information to craft a range of potential royalty rates for the section 114 license, then chose the rate within the range which would further the stated statutory objectives.

RIAA and the Services proposed rates based on three distinct marketplace models in which rates are set through arms-length negotiations. Report ¶ 124. The Services proposed two benchmarks for consideration by the Panel: Negotiated license fees for a sound recording performance right and the license fees the Services pay the performing rights organizations for use of the underlying musical works. RIAA put forth a single model for the Panel's consideration: Cable television network license fees. The Panel found the Services' models helpful in setting the rate for the digital performance right, but rejected the RIAA model for the reasons stated herein.

Both RIAA and the Services seemed to agree that the best proxy for reasonable compensation is a marketplace rate. The Panel, however, noted that the DPRSRA instructs the CARP to set reasonable rates, which need not be the same as rates set in a marketplace unconstrained by a compulsory license. In support of its interpretation, the Panel cited the statutory factors which must be considered in setting the rate. *See* Report ¶¶ 10, 124.

The Panel's Evaluation of the RIAA Benchmark

The benchmark proposed by the recording industry analogizes the cost of programming for cable television networks with the cost of procuring the right to perform the sound recordings. The analogy, however, did not withstand scrutiny by the Panel, which reasonably found that the cable television network license fees model did not represent rates for an analogous product in a comparable marketplace. Its conclusion rested on a number of findings which described analytical deficiencies in the two studies offered in support of the 41.5% proposed royalty rate. Report ¶¶ 126–150.

The RIAA model proposed using the purchase price of programming for cable television networks to determine the price the Services would pay for the right to publicly perform sound recordings, if negotiated in a free market. RIAA's Proposed Findings of Fact and Conclusions of Law (PF) ¶ 62; RIAA Proposed Conclusions (PC) ¶ 18. RIAA presented two studies that illustrate the amount of money cable television networks pay for their programming: (1) The Kagan study,[4] and (2) the Wilkofsky Gruen Associates[5] study. RIAA Exhibits (Exs.) 14 and 15, respectively. Both studies argued that the analogy between cable television networks and the digital audio services was apt because the digital audio services and the cable television networks compete head-to-head for carriage on cable and DBS systems, and for consumer time and discretionary income. Report ¶ 130.

The Kagan study analyzed data concerning the revenues and programming expenses of 31 basic cable television networks from the 1985–96 period. It concluded that a cable television network spends, on average, approximately 40% of its gross revenues for programming. RIAA Exhibit (Ex.) 14 at 7. The Panel, however, discounted the 40% figure because it represented the costs of license fees to all copyright owners, and it included the costs of programming during the start-up years, when a new cable television network may pay more than 100% of its revenues in programming costs. Report ¶¶ 127, 129, 149. Failure to adjust for these factors made it impossible for the Panel to assess the costs for the right to publicly perform the sound recordings apart from the costs of the other copyrighted works which make up the program.

Their second study, prepared by Wilkofsky Gruen Associates (WGA), analyzed only cable movie networks because Wilkofsky, the expert for the study, claimed that the ''pricing characteristics and dynamics'' of the cable movie networks were comparable in three fundamental ways: The lack of commercials, the generation of revenues through subscriptions, and the purchase of programming from third parties. Wilkofsky Written Direct Testimony (W.D.T.) at 3–5. This study concluded that the cable movie networks pay a weighted average of 41.5 % of their revenues for programming that they acquire from outside sources and by analogy, the Services should pay the same. *Id.* at 3.

The Panel rejected the conclusion of the WGA study because it ignored the following fundamental differences in market demand and cost characteristics between the cable movie networks and the digital audio services. Report ¶¶ 133–145.

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[3] (1) to make determinations concerning the adjustment of reasonable copyright royalty rates as provided in sections 114, 115, and 116, and to make determinations as to reasonable terms and rates of royalty payments as provided in section 118. The rates applicable under section 114, 115, and 116 shall be calculated to achieve the following objectives:

(A) To maximize the availability of creative works to the public;

(B) To afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions;

(C) To reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk, and contribution to the opening of new markets for creative expression and media for their communication;

(D) To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices.

17 U.S.C. 801(b)(1).

[4] The Kagan study was prepared by Paul Kagan Associates, a media research company that tracks and publishes financial data concerning the media and entertainment industries.

[5] Wilkofsky Gruen Associates is an economic consulting firm that specializes in the communications and entertainment industries.

1. The study provided no evidence to show that any of the movie networks directly compete with digital audio services. In fact, when people watch a movie, they devote their entire attention to the film for a period of time, and generally, do not repeat the experience with the same movie. On the other hand, subscribers to digital audio services choose to listen to the same music again and again while engaged in other activities. In other words, the subscriber chooses each service for different reasons, and therefore, they do not represent choices in the same market. Report ¶¶ 143, citing Rosenthal Written Rubuttal Testimony (W.R.T). at 13, Transcript (Tr). 1251 (Rubinstein).

2. The cable movie networks compete against other cable and broadcast stations for exclusive rights to motion pictures. Exclusive rights are highly prized, and consequently, command a premium price, but they are not implicated in the market for digital audio transmissions. Consequently, the Panel found that RIAA's failure to adjust for this aspect grossly overstated the value of programming costs in its cable movie network analogy. Report ¶¶ 137–142.

3. The Panel further discounted the analogy because RIAA ignored the promotional benefit that flows to the record companies from the constant airplay of their sound recordings. Report ¶¶ 144–145. *See also discussion infra.*

The Panel's Determination of Reasonable Terms

In addition to establishing a reasonable rate for the sound recording performance license, the Panel must also establish reasonable terms for implementing the license. The Senate Committee Report makes clear that terms include ''such details as how payments are to be made, when, and other accounting matters.'' S. Rep. No. 104–128, at 30 (1995).

RIAA and the Services proposed specific terms concerning minimal fees, payment schedules, late fees, statements of account, and audits. From these, the Panel adopted the following terms:

1. RIAA shall have sole responsibility for the distribution of the royalty fees to all copyright holders. Report ¶¶ 184, 205.

2. The license fee payments shall be due on the twentieth day after the end of each month, beginning with the month succeeding the month in which the royalty fees are set. Report ¶¶ 185, 206.

3. The Services shall make back payments over a 30-month period. The first back payment, 1/30th of the total arrearage, shall be delayed for six months. Report ¶¶ 187, 206(a).

4. A Service shall be subject to copyright liability if it fails to make timely payments. Liability for copyright infringement shall only come about for knowing and willful acts which materially breach the statutory license terms. Report ¶¶ 188, 206(b).

5. A late fee of 1.5% per month or the highest lawful rate, whichever is lower, will be imposed from the due date until payment is received. Report ¶¶ 189, 206(a).

6. Services shall submit monthly statements of accounts and payment to RIAA. Only information to verify the royalty payments need be provided on the monthly statements of account. Report ¶¶ 190, 205, 207.

7. Safeguards must be established to protect against disclosure of confidential financial and business information, which includes the amount of the royalty payment. Access to this information shall be limited to employees of RIAA, who are not employees or officers of the copyright owners or the recording artists, for the purpose of performing their assigned duties during the ordinary course of employment, and to independent auditors acting on behalf of RIAA. Report ¶¶ 191, 208.

8. The digital audio services shall maintain accurate records on matters directly related to the payment of the license fees for a period of three years. Report ¶¶ 192, 209.

9. Interested parties may conduct only one audit of a digital audio service during any given year. Report ¶¶ 193, 210(c).

- Interested parties must file a Notice of Intent to Conduct an Audit with the Copyright Office. Such notice shall be published in the **Federal Register**. Report ¶¶ 193, 210(a)–(b).
- RIAA must retain an auditor's report for a period of three years. Report ¶¶ 193, 210(d).
- An audit, including underlying paperwork, which was performed in the ordinary course of business according to generally accepted auditing standards by an independent auditor, may serve as an audit for all interested parties. Report ¶¶ 194, 210(e).
- Interested parties shall pay for the cost of the audit, unless an independent auditor concludes that there was an underpayment of five (5) percent or more. Report ¶¶ 195, 210(f).

The Panel chose not to adopt RIAA's minimum fee proposal and the Services' proposed payment schedule for the distribution of royalties to the featured artists and the nonfeatured musicians and vocalists. The Panel found that the timing of payments to the performing artists was not within the scope of the proceeding. Report § 204; Report at 56 n.21.

The Panel's Evaluation of the RIAA Proposal To Adopt a Minimum Fee

RIAA proposed the imposition of a minimum fee as a means to insure a fair return to the copyright owners in light of business practices that might erode the value of the statutory license fee. RIAA PF ¶¶ 126–147. Specifically, RIAA sought a minimum fee to minimize the effect of discounts or credits, to address shifts in business models, and to avoid diluting the value of the sound recording when audio digital services add new channels to their offerings. *Id.* The Panel ultimately rejected this suggestion because it found that the rationale for a minimum fee was based on unsupported speculation about the business structure of the Services. Report ¶ 204.

III. The Parties' Reaction to the Determination of the Panel

The regulations governing the CARP proceedings allow parties to file petitions to modify or set aside the determination of the Panel within 14 days of its filing date. The petition must state the reasons for the petition, including relevant references to the parties' proposed findings of fact and conclusions of law. Parties who wish to file replies to a petition may do so within 14 days of the filing of such petition. See 37 CFR 251.55(a), (b).

Accordingly, on December 12, 1997, RIAA filed a Petition to Reject the Report of the CARP (Petition), contending that the Panel acted both contrary to the Copyright Act and arbitrarily in reaching its determination. In its petition, RIAA requests the Librarian to set aside the Panel's determination and set a new rate that should not be less than double the Services' 1996–2001 payments for the public performance of the underlying musical works.

RIAA contends that the Panel's determination was arbitrary and contrary to law for the following reasons:

1. The Panel disregarded precedent set by the former Copyright Royalty Tribunal (CRT or Tribunal) in applying the statutory criteria for determining a reasonable rate for the public performance right. Petition at 6, 14–15.

2. The Panel used the rates set in a corporate partnership agreement as a benchmark for establishing the new compulsory license rate. This was inappropriate because the public performance in sound recordings

license agreement was not negotiated independently, but as part of a larger complex agreement. *Id.* at 20–27.

3. When the Services publicly perform a sound recording, two groups of copyright owners receive royalties: The copyright owners in the underlying musical works, and for the first time, the record companies and performers. The Panel determined that the record companies and performers were not entitled to more royalties for their public performance right than those received by the copyright owners in the underlying musical works for the public performance of their works. RIAA contends that CRT precedent supports a determination that just the reverse is true. *Id.* at 14–15.

4. The compulsory license allows the Services to perform sound recordings publicly without infringing copyright prior to the setting of the royalty rate, so long as the Services agree to pay their accumulated royalty obligation once the rates are determined. The Panel created a payment schedule that allows the Services to pay these fees over a three year period. RIAA contends that this payment schedule is contrary to law. *Id.* at 7 n.1.

5. RIAA also contends that the CARP failed to provide a reasoned explanation for proper review, made conclusions inconsistent with its findings, made findings without record support, and failed to make findings in support of conclusions. *Id.* at 2.

RIAA, however, does not suggest that the Librarian disregard all the findings of the Panel. Instead, it recommends adopting the Panel's approach ''to determine a reasonable rate—provided that the Librarian makes the necessary adjustments to account for the precedent and considerations that the Panel ignored.'' Petition at 51–52. RIAA further allows that the Librarian need not consider the cable network benchmark in its analysis, since the Panel's analysis of the remaining benchmarks supports an upward adjustment of the 5% rate of gross revenues set by the CARP. Petition at 52 n.9.

On December 29, 1997, in response to the RIAA petition to reject the CARP report, the Services filed a reply to RIAA's Petition to Reject the CARP Report (Reply to Petition). The crux of the Services' argument in support of adopting the Panel's report is that ''[w]hen examined as a whole, the Panel's Report is eminently reasonable and amply supported by the record.'' Reply to Petition at 12. Specific arguments of the Services in support of the Panel's report are discussed below in conjunction with RIAA's arguments to reject the report.

IV. The Librarian's Scope of Review of the Panel's Report

The Copyright Royalty Tribunal Reform Act of 1993 (the Reform Act), Public Law 103–198, 107 Stat. 2304, created a unique system of review of a CARP's determination. Typically, an arbitrator's decision is not reviewable, but the Reform Act created two layers of review that result in final orders: the Librarian of Congress (Librarian) and the United States Court of Appeals for the District of Columbia Circuit. Section 802(f) of title 17 directs the Librarian either to accept the decision of the CARP or to reject it. If the Librarian rejects it, he must substitute his own determination ''after full examination of the record created in the arbitration proceeding.'' 17 U.S.C. 802(f). If the Librarian accepts it, then the determination of the CARP becomes the determination of the Librarian. In either case, through issuance of the Librarian's Order, it is his decision that will be subject to review by the Court of Appeals. 17 U.S.C. 802(g).

The review process has been thoroughly discussed in prior recommendations of the Register of Copyrights (Register) concerning rate adjustments and royalty distribution proceedings. Nevertheless, the discussion merits repetition because of its importance in reviewing each CARP decision.

Section 802(f) of the Copyright Act directs that the Librarian shall adopt the report of the CARP ''unless the Librarian finds that the determination is arbitrary or contrary to the applicable provisions of this title.'' Neither the Reform Act nor its legislative history indicates what is meant specifically by ''arbitrary,'' but there is no reason to conclude that the use of the term is any different from the ''arbitrary'' standard described in the Administrative Procedure Act (APA), 5 U.S.C. 706(2)(A).

Review of the case law applying the APA ''arbitrary'' standard reveals six factors or circumstances under which a court is likely to find that an agency acted arbitrarily. An agency action is generally considered to be arbitrary when:

1. It relies on factors that Congress did not intend it to consider;

2. It fails to consider entirely an important aspect of the problem that it was solving;

3. It offers an explanation for its decision that runs counter to the evidence presented before it;

4. It issues a decision that is so implausible that it cannot be explained as a product of agency expertise or a difference of viewpoint;

5. It fails to examine the data and articulate a satisfactory explanation for its action including a rational connection between the facts found and the choice made; and

6. Its action entails the unexplained discrimination or disparate treatment of similarly situated parties.

Motor Vehicle Mfrs. Ass'n. State Farm Mutual Auto. Insurance Co., 463 U.S. 29 (1983);

Celcom Communications Corp. v. *FCC,* 789 F.2d 67 (D.C. Cir. 1986); *Airmark Corp.* v. *FAA,* 758 F.2d 685 (D.C. Cir. 1985).

Given these guidelines for determining when a determination is ''arbitrary,'' prior decisions of the District of Columbia Circuit reviewing the determinations of the former CRT have been consulted. The decisions of the Tribunal were reviewed under the ''arbitrary and capricious'' standard of 5 U.S.C. 706(2)(A) which, as noted above, appears to be applicable to the Librarian's review of the CARP's decision.

Review of judicial decisions regarding Tribunal actions reveals a consistent theme: while the Tribunal was granted a relatively wide ''zone of reasonableness,'' it was required to articulate clearly the rationale for its award of royalties to each claimant. See *National Ass'n of Broadcasters* v. *Copyright Royalty Tribunal,* 772 F.2d 922 (D.C. Cir. 1985), *cert. denied,* 475 U.S. 1035 (1986) *(NAB* v. *CRT*); *Christian Broadcasting Network* v. *Copyright Royalty Tribunal,* 720 F.2d 1295 (D.C. Cir. 1983) (*Christian Broadcasting* v. *CRT*); *National Cable Television Ass'n* v. *Copyright Royalty Tribunal,* 689 F.2d 1077 (D.C. Cir. 1982) (*NCTA* v. *CRT*); *Recording Indus. Ass'n of America* v. *Copyright Royalty Tribunal,* 662 F.2d 1 (D.C. Cir. 1981) (*RIAA* v. *CRT*). As the D.C. Circuit succinctly noted:

> We wish to emphasize * * * that precisely because of the technical and discretionary nature of the Tribunal's work, we must especially insist that it weigh all the relevant considerations and that it set out its conclusions in a form that permits us to determine whether it has exercised its responsibilities lawfully * * *.

Christian Broadcasting v. *CRT,* 720 F.2d at 1319 (D.C. Cir. 1983), quoting *NCTA* v. *CRT,* 689 F.2d at 1091 (D.C. Cir. 1982).

Because the Librarian is reviewing the CARP decision under the same ''arbitrary'' standard used by the courts to review the Tribunal, he must be presented by the CARP with a rational analysis of its decision, setting forth specific findings of fact and conclusions of law. This requirement of every CARP report is confirmed by the legislative history to the Reform Act which notes that a ''clear report setting forth the panel's reasoning and findings will greatly assist the Librarian of Congress.'' H.R. Rep. No. 103–286, at 13 (1993). This goal cannot be reached by ''attempt(ing) to distinguish apparently inconsistent awards with simple, undifferentiated allusions to a 10,000 page record.'' *Christian Broadcasting* v. *CRT*, 720 F.2d at 1319.

It is the task of the Register to review the report and make her recommendation to the Librarian as to whether it is arbitrary or contrary to the provisions of the Copyright Act and, if so, whether, and in what manner, the Librarian should substitute his own determination. 17 U.S.C. 802(f).

V. Review and Recommendation of the Register of Copyrights

The law gives the Register the responsibility to review the CARP report and make recommendations to the Librarian whether to adopt or reject the Panel's determination. In doing so, she reviews the Panel's report, the parties' post-panel motions, and the record evidence.

After carefully reviewing the Panel's report and the record in this proceeding, the Register finds that the Panel's adoption of the DCR negotiated license fee as the starting point for making its determination is arbitrary. This conclusion compels the Register to set aside the Panel's final determination and reevaluate the record evidence before making a recommendation to the Librarian.

Section 802(f) states that ''(i)f the Librarian rejects the determination of the arbitration panel, the Librarian shall, before the end of that 60-day period, and after full examination of the record created in the arbitration proceeding, issue an order setting the royalty fee or distribution of fees, as the case may be.'' During that 60-day period, the Register reviewed the Panel's report and made a recommendation to the Librarian not to accept the Panel's report, for the reasons cited herein. The Librarian accepted this recommendation, and on January 27, 1998, issued an order stating that the Panel's report was still under review. See Order, Docket No. 96–5 CARP DSTRA (January 27, 1998).

The full review of the Register and her corresponding recommendations is presented herein. Within the limited scope of the Librarian's review of this proceeding, ''the Librarian will not second guess a CARP's balance and consideration of the evidence, unless its decision runs completely counter to the evidence presented to it.'' Rate Adjustment for the Satellite Carrier Compulsory License, 62 FR 55757 (1997), citing 61 FR 55663 (October 28, 1996) (Distribution of 1990, 1991 and 1992 Cable Royalties). Accordingly, the Register accepts the Panel's weighing of the evidence and will not question findings and conclusions which proceed directly from the arbitrators' consideration of factual evidence.

The Register also adopts the Panel's approach in setting reasonable rates and terms for the digital performance license in sound recordings pursuant to 17 U.S.C. 114(f)(2), but sets aside those findings and conclusions that are arbitrary or contrary to law.

a. Methodology for Making Rate Determination

Use of a Marketplace Standard in Setting the Royalty Rate

The standard for setting the royalty rate for the performance of a sound recording by a digital audio subscription service is not fair market value, although CARPs and the Copyright Royalty Tribunal (CRT or Tribunal) in prior rate adjustment proceedings under sections 115 and 116 considered comparable rates negotiated under marketplace conditions when making their determinations.

In light of this practice, the Panel followed the same approach established in prior rate adjustment proceedings conducted by the Tribunal and the CARPs in making its determination. Namely, the Panel considered the parties' presentations of different rates negotiated in comparable marketplace transactions and first determined whether the proposed models mirrored the potential market transactions which would take place to set rates for the digital performance of sound recordings. Report ¶ 123. These benchmarks were then evaluated in light of the statutory objectives to determine a reasonable royalty rate. *Id.*

The Panel noted that RIAA and the Services ''seem to agree that the best proxy for reasonable compensation is to look to marketplace rates.'' Report ¶ 124. The parties also agreed that the rates should be based on gross revenues and further agreed on the definition of ''gross revenues.'' Report ¶ 125; RIAA PF ¶ 55; Services Joint Reply to RIAA's Proposed Findings of Fact and Conclusions of Law (Services' RF) ¶ 51.

While the Panel agreed with the parties on these two points, it noted that the statute requires the Panel to adopt reasonable rates and terms, and that reasonable rates and terms are not synonymous with marketplace rates. Report ¶ 124. Unlike a marketplace rate which represents the negotiated price a willing buyer will pay a willing seller, *see* Rate Adjustment for the Satellite Carrier Compulsory License, 62 FR 55742 (1997) (applying a fair market standard, as set forth at 17 U.S.C. 119(c)(3)(D), in setting royalty rates for the retransmission of broadcast signals by satellite carriers), reasonable rates are determined based on policy considerations. *See RIAA* v. *CRT*, 662 F.2d 1.[6] Congress granted the record companies a limited performance right in sound recordings in order to ''provide [them] with the ability to control the distribution of their product by digital transmissions,'' but it did so with the understanding that the emergence of new technologies would not be hampered. S. Rep. No. 104–128, at 15 (1995). Consequently, Congress specified that the terms were to be reasonable and calculated to achieve the following four specific policy objectives:

1. To maximize the availability of creative works to the public;
2. To afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions;
3. To reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk, and contribution to the opening of new markets for creative expression and media for their communication; and
4. To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices. 17 U.S.C. 114(f)(2) and 801(b)(1).

RIAA takes exception to this interpretation and argues that the Panel failed to follow CRT precedent that ''interpreted the Section 801(b)(1) factors as requiring it to establish a market rate.'' Petition at 33. In support of its position, RIAA relies upon the 1982 CRT rate adjustment proceeding to determine reasonable rates and terms for the statutory noncommercial broadcasting license, 17 U.S.C. 118, where the CRT stated:

> The Tribunal has consistently held that the Copyright Act does not contemplate the Tribunal establishing rates below the

[6] In reviewing how the Tribunal analyzed the statutory criteria, the court noted that ''other statutory criteria invite the Tribunal to exercise a legislative discretion in determining copyright policy in order to achieve an equitable division of music industry profits between the copyright owners and users.'' *Id.* at 8.

reasonable market value of the copyrighted works subject to a compulsory license.

1982 Adjustment of Royalty Schedule for Use of Certain Copyrighted Works in Connection with Noncommercial Broadcasting: Terms and Rates of Royalty Payments, 47 FR 57924 (December 29, 1982). RIAA further contends that the Panel not only ignored the CRT precedent requiring it to set marketplace rates, but improperly shifted the emphasis to ensure the financial viability of the copyright users. Petition at 33.

In response, the Services contend that the Panel's analysis comports with CRT precedent on both points, noting that the CRT did consider evidence on how a proposed rate would affect the user industry in its proceedings to set rates under sections 111 and 116. Reply to Petition at 26. For example, in the 1980 rate adjustment proceeding to set the royalty rate for jukeboxes, the CRT considered the evidence and found ''only that marginal jukebox owners would be threatened by the new rate.'' *Id.* In fact, the Tribunal stated that it was ''satisfied that adequate attention (had) been given to the small operator, * * * (and adopted) an amendment to the proposed fee schedule that was proposed for the benefit of such (small) operators.'' 1980 Adjustment of the Royalty Rate for Coin-Operated Phonorecord Players, 46 FR 888 (1981).

The Register finds that the Panel correctly analyzed how to determine a reasonable rate under section 114. Section 801(b)(1) states that one function of a CARP is to determine reasonable rates ''as provided in sections 114, 115, and 116, and to make determinations as to reasonable terms and rates of royalty payments as provided in section 118.'' The provision further states that the CARP must determine the rates under sections 114, 115, and 116 to achieve the four statutory objectives. The law does not state that these objectives are applicable in a rate adjustment proceeding to determine rates under sections 111 or 118. Therefore, RIAA's reliance on CRT precedents for setting rates under section 118 is without merit. Furthermore, the Panel's analysis is consistent with the prior CRT determinations establishing rates for the section 115 and 116 licenses.

In the 1980 jukebox rate adjustment proceeding, the CRT set the rate ''[o]n the basis of the marketplace analogies presented during the proceeding, taking the record as a whole, and with regard for the statutory criteria. * * * That rate takes account both of what is paid for music elsewhere under similar circumstances and, since it is a flat rate, of the Tribunal's concern for the smaller, less profitable operators.'' 46 FR 889 (1981). To recognize that this rate was not a negotiated marketplace value, one need only read Commissioner James's dissent admonishing the majority for setting a rate on ''an ability to pay theory.'' He characterized the majority's actions as follows:

> In essence, the majority reached a conclusion on the premise that a true market value would result in too large an increase in fees. The majority was set on course by what they deemed were the guiding standards of the statute which referred to minimizing the disruptive impact on the economic structure of the industries involved. It was the majority view and opinion that a large increase in fees would be oppressive to the industry and would ''impact on small operators.''

Id. at 891 (footnote omitted).

The Court of Appeals upheld the Tribunal's approach in its 1980 jukebox rate adjustment proceeding, stating that:

> In its decision, the Tribunal acknowledged that the rate which it approved could not be directly linked to marketplace parallels, but it found that such parallels served as appropriate points of reference to be weighed together with the entire record and the statutory criteria. Although we agree with ASCAP that the analogous marketplace evidence is significant, we do not believe that the Tribunal was bound by that evidence to select a fee rate within the $70–$140 ''zone'' which, according to ASCAP, governs this case. The Tribunal carefully weighed the evidence derived from the marketplace analogies and other evidence specifically in light of the four statutory criteria of section 801(b) and arrived at a royalty rate for coin-operated phonorecord players of $50 per machine.

Amusement and Music Operators Ass'n v. *Copyright Royalty Tribunal,* 676 F.2d 1144, 1157 (7th Cir. 1982), *cert. denied,* 459 U.S. 907 (1982) (*AMOA* v. *CRT*). The D.C. Court of Appeals engaged in a similar analysis when it considered the Tribunal's determination to raise the royalty rate for making and distributing phonorecords of copyrighted musical works from 2 cents to 4 cents. In that case, the copyright owners argued that Congress intended the Tribunal to set a high royalty rate under a bargaining room theory, which would create a rate ceiling for stimulating future negotiations outside the license. The D.C. Circuit found that while Congress had considered this possibility, it chose not to codify this approach, but rather to express its will through specific statutory criteria and allow the Tribunal to interpret and apply these objectives to the record evidence in a rate adjustment proceeding. *RIAA* v. *CRT,* 662 F.2d at 8–9. Furthermore, the Court ascertained that Congress did not rank the criteria in order of importance so that the Tribunal, and subsequently, the CARP, could:

> To the extent that the statutory objectives determine a range of reasonable royalty rates that would serve all these objectives adequately but to differing degrees, * * * choose among those rates, and courts are without authority to set aside the particular rate chosen by the Tribunal if it lies within a ''zone of reasonableness.''

Id. at 9. *See also Permian Basin Area Rate Cases,* 390 U.S. 747, 767 (1968); *Federal Power Commission* v. *Natural Gas Pipeline Co.,* 315 U.S. 575, 585–586 (1942); *Hercules, Inc.* v. *Environmental Protection Agency,* 598 F.2d 91, 107 (D.C. Cir. 1978).

b. Benchmarks

The Panel's Disposition of the Proposed Benchmarks

The Register has reviewed the analysis of the Panel and its disposition of the three benchmarks and finds that the Panel's primary reliance on and manipulation of the DCR negotiated license fee was arbitrary. The Register also finds that the record evidence does not support the Panel's calculation of a specific range of fees for the public performance of the musical compositions. These flaws compel the Register to reexamine the record evidence and propose a rate based on her analysis while providing deference, where appropriate, to the findings of the Panel.

The Register, however, did not evaluate further the record evidence concerning either the cable television network fee or the proposed minimum fee in her deliberations to determine the appropriate rate because no party to the proceeding challenged either of these findings or continued to rely upon these matters in presenting its arguments to the Librarian.[7] Therefore, the Register forgoes a review of the Panel's analysis in these areas. This does not mean, however, that the Register and the Librarian will always forego an independent review of a Panel's actions. See, *e.g.* Distribution of the 1992, 1993, and 1994 Musical Works Funds, 62 FR 6558 (February 12, 1997)

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[7] ''RIAA strongly disagrees with the CARP's conclusion that the Services should devote a smaller percentage of their revenues to license fees than do other cable networks. While the range of percentages is large, there are no cable networks that consistently spend as little as 5 percent. Nevertheless, RIAA has not challenged the CARP's decision to reject the cable network analogy.'' Petition at 52 n.9 (citations omitted). Furthermore, RIAA did not raise any challenge to the Panel's decision not to grant a minimum fee.

(recommending an upward adjustment to one party's award, although no party made a request for the adjustment); Rate Adjustment for the Satellite Carrier Compulsory License, 62 FR 55742 (1997) (recommending the adoption of a zero rate for local retransmission of network signals to unserved households).

The Panel's Adoption of the DCR Negotiated License Fee and its Subsequent Manipulations of This Rate to Establish a Range of Potential Royalty Rates was Arbitrary [8]

The Panel found that the digital performance license negotiated as part of a larger partnership agreement between DCR and its two record company partners, Warner Music and Sony Music, was a useful benchmark for determining the section 114 royalty fee because it provided a ''useful precedent,'' although there were problems with using the rate for this license fee since only 60% of the industry engaged in the negotiations setting the rate.[9] Report ¶¶ 166, 200. To address this problem the panel adjusted the figure upward to reach a base rate figure arguably applicable to 100% of the recording industry market. *Id.* The Panel then doubled this number to account for the statutory provision which requires an equal distribution of the royalties collected pursuant to the compulsory license between the record companies and the recording artists. *Id.; also* 17 U.S.C. 114(g). While recognizing that a pure doubling of the base rate was inappropriate, the Panel determined that these manipulations of a ''freely negotiated rate'' set a reasonable range of rates for further consideration in light of the statutory criteria. *Id.*

RIAA opposes the use of the negotiated license fee as a benchmark for setting the compulsory license fee for the following reasons: (1) It was merely one provision in a complex transaction involving eleven interrelated agreements, RIAA PF ¶ 92; Petition at 22; Wildman [10] W.R.T. at 12–15; Transcript (Tr.) 2213–14 (Wildman); (2) the record companies interested in investing in the digital audio service would share the cost of a higher rate, thereby creating a strong incentive to create a low rate; (3) the license fee was not for the right to perform sound recordings publicly, but for the acknowledgement that a right should exist, RIAA PF ¶ 84; Tr. 2102 (Vidich); [11] (4) the record companies never viewed the established rate as precedential, citing the license provision that the rate will be superseded if Congress establishes a performance right in sound recordings, DCR Exs. 7, 8 & 15 at ¶ 9; Vidich W.R.T. at 7; Tr. 2106–2107 (Vidich); Del Beccaro [12] W.D.T. at 9, and the most favored nations clause, DCR Exs. 7, 8 & 15 at ¶ 6; (5) the record companies did not enjoy the degree of leverage in setting the rate that the Services imply in their proposed findings; (6) the fee did not represent an industry-wide agreement on the value of the performance right; instead, only three record companies, ''collectively responsible for only about 35% of the sound recordings performed by DCR,'' negotiated the rates, RIAA's Reply to Proposed Findings and Conclusions of Law (RIAA RPF)] 39; Tr. 1014 (McCarthy); [13] and (7) the DCR digital performance license differed in significant ways from the statutory license. For example, the DCR license requires the company to pay royalties on its revenues from international sources which are not recoverable under the DPRSRA, RIAA PF ¶ 83; Tr. 965 (Del Beccaro); Tr. 1014 (McCarthy); Tr. 2137 (Vidich), and it did not contemplate a distribution of a portion of the royalties to recording artists as required under the new law, RIAA PF ¶ 82.

In response, the Services assert that the Panel ''did not rely on the DCR license rate in isolation,'' and argue that its determination was informed by testimony from the parties who participated in the negotiations. Reply to Petition at 20. More specifically, the Services argue that the inclusion of the performance license within a larger, complex commercial agreement makes it more meaningful, because DCR did not purchase a license for the public performance of sound recordings. Rather, in exchange for a partnership agreement, DCR acknowledged that the right should exist for a particular rate. The Services neglect, however, to discuss why this observation is important in their initial findings. Services RF ¶ 75–77. Later, the Services argue that the Panel's decision to use the DCR license fee as an appropriate benchmark rested on a weighing of the evidence and invoke the Panel's discretion to evaluate the testimony and fashion its decision accordingly. Reply to Petition at 20–21. The Services, however, fail to address RIAA's additional concerns about the negotiated license, except to note that the partner record companies never operated a joint advertising venture nor took advantage of the provisions which gave them some measure of control over programming. Services RF ¶¶ 80–81.

While the Register agrees with the Services that the Panel carefully considered the rationale for and the circumstances surrounding the negotiations setting the DCR license rate, she finds the Panel's adoption of this benchmark and its subsequent adjustments arbitrary. In the first instance, the benchmark offered by the Services cannot represent a license for a right to perform sound recordings, because no such legal right existed at the time of the negotiations. Woodbury [14] W.D.T. at 12; RIAA PF] 84; Tr. 2102 (Vidich). DCR allowed that, in fact, it did not negotiate for a performance license in sound recordings; and instead, characterized the transaction as selling ''to its record company partners the recognition they sought 'that the right existed for a particular rate.' '' Services PF ¶ 102. To underscore this distinction, DCR insisted on a clause which stated that the United States law did not require DCR to pay a fee or royalty for the public performance of any sound recording, even though DCR agreed, as part of a complex commercial transaction, to pay its partner record companies what it calls a public performance license fee. Services PF ¶¶ 111, 136. An article in the press announcing the deal echoed this distinction. It noted that not only did the transaction allow DCR use of the record companies' repertoire, it also required DCR to support a performance right in sound recordings. DCR Ex. 27 (Paul Verna, *Time Warner Breaks New Cable Ground; Enters Cable Radio Venture With Sony,* Billboard, Feb. 6, 1996, at 1).

Consequently, the Register rejects the Panel's premise that the rate set for a nonexistent right would represent accurately the value of the performance right once it came into existence, especially where the parties

[8] Negotiated license fees and certain business information, which the Register has considered throughout her review, are not being published in the Register's review because the information is subject to a protective order. See Order Docket No. 96–5 CARP DSTRA (September 18, 1996).

[9] Sony Music and Warner Music signed a partnership agreement with DCR in January 1993. A third record company, EMI, joined the partnership in April 1994, under substantially the same terms. Report ¶ 164.

[10] Associate Professor of Communications Studies at Northwestern University and Director of Northwestern's program in Telecommunications Studies, Management, and Policy.

[11] Senior Vice-President of Strategic Planning and Business Development at Warner Music Group and a member of the Board of Directors of Digital Cable Radio Associates.

[12] President and Chief Executive Officer of Digital Cable Radio Associates.

[13] Senior Vice-President and Chief Financial Officer of Digital Cable Radio Associates.

[14] A vice-president at the economic consulting firm of Charles River Associates, Inc.

acknowledge that the agreement encompassed more than the purported value of the coveted right, namely the recognition from the audio service that a performance right in sound recordings should exist. RIAA PF ¶¶ 94–95; Tr. 2209–12 (Wildman); Wildman W.R.T. at 9–12. Arguably, that recognition was more valuable consideration to the record companies than the license fee itself.

The conclusion that the DCR license fee may serve as the benchmark for setting the section 114 rates is undermined further by the very nature of the partnership agreement. All parties agree that the agreement concerning the performance right was merely one of eleven interdependent co-equal agreements which together constituted the partnership agreement between DCR and the record companies. Such strong ties between provisions in a negotiated document raise the question of how much give-and-take occurred in negotiating the final terms. Courts recognize that complex transactions encourage tradeoffs among the various provisions and lead to results that most likely differ from those that would result from a separately negotiated transaction.[15] While DCR freely entered into the partnership agreement, the record contains no evidence that it would have freely entered into a separate performance license for sound recordings. To the contrary, the Service's own witness admits that it is unlikely that a stand-alone performance license would have been negotiated. Woodbury W.D.T. at 15. Accordingly, the Register concludes that it was arbitrary for the Panel to rely on a single provision extracted from a complex agreement where the evidence demonstrates that the provision would not exist but for the entire agreement. Under similar circumstances, the Southern District Court of New York found that ''plucking one term out of the contract is likely to yield a fairly arbitrary result.'' *American Society of Composers Authors and Publishers* v. *Showtime/The Movie Channel, Inc. (ASCAP)*, published at 912 F.2d 572, 590 (S.D.N.Y. December 20, 1989) (No. 13–95 (WCC)) (rejecting proposal to rely upon provisions in guild agreement concerning payment of revenues where such provisions were part of a set of terms governing compensation, benefits, and working conditions).[16]

Another problem with adopting the DCR license fee is that it is not an industry-wide agreement, but rather the product of negotiations among only three record companies, which together account for approximately 35% of the sound recordings performed by DCR. RIAA PF ¶ 82; RIAA RPF ¶ 39. The arbitrators understood the limited nature of the negotiations and made an adjustment to the license fee based on the mistaken assumption that the DCR license fee represented the value of the sound recordings owned by the three record companies party to the agreement, which purportedly represented 60% of the record industry. Report ¶¶ 166, 200. This assumption arose from a statement made by the Services in the summary statement contained in the Services' joint reply to RIAA's proposed findings.[17] The statement, however, has no support in the record. See Petition at 21 n.3; Reply to Petition at 21–22. Consequently, the Panel's upward adjustment of the base figure on the merits of this assertion was arbitrary.

This is not to say that the fact that the DCR license fee was negotiated with companies owning rights to only 35% of the relevant works renders that license fee irrelevant. It is, however, a further deficiency which in combination with the other deficiencies discussed herein, renders the Panel's reliance on the DCR license fee as its exclusive benchmark inappropriate.

Furthermore, the Panel's decision to rely on the DCR license fee deviates from CRT precedent where that agency refused to adopt, as an industry-wide rate, a set of rates negotiated by only certain of the affected parties as part of a general understanding involving issues in addition to the rate of compensation. Use of Certain Copyrighted Works in Connection with Noncommercial Broadcasting, 43 FR 25068 (June 8, 1978). While no Panel need slavishly adhere to the past practices of the CRT, it must articulate a reasoned explanation for its deviation from past precedent. Distribution of 1990, 1991, and 1992 Cable Royalties, 61 FR 55653, 55659 (October 28, 1996). Otherwise, its actions may be construed as arbitrary or contrary to law.[18]

The Register also finds that even if the 60% figure had record support, it would be arbitrary to adjust a negotiated license fee that purports to represent the market value of the digital performance right in sound recordings. Under the license agreement, DCR agreed to pay a percentage of its gross revenues for the right to perform sound recordings digitally, but only a portion of these fees were paid to each of DCR's three record company partners, allocated on the basis of the DCR playlist.[19] Tr. 2123–24 (Vidich); Services PF ¶ 111. Therefore, the license fee—to the extent that it was a license fee—already accounted for all copyright fees owed to the record industry, and it was inappropriate for the Panel to make any further adjustment. The Services seem to realize the Panel's error in this respect and note that the Panel was under no obligation to make an upward adjustment, since the license fee reflected the value of the sound recording and not the sum of the percentage amount each partner record company negotiated for use of its works. Reply to Petition at 22.

Furthermore, the Register finds that the Panel's conclusion that the DCR license fee ''provides a useful precedent for setting a royalty rate in this proceeding'' was arbitrary. Report ¶ 200. The only support for this finding was Woodbury's testimony that the trade article announcing the deal between DCR and its new record company partners, Sony and Warner, illustrated its precedential value, at least for the record companies. Woodbury W.D.T. at

[15] For example, in resolving a dispute between ASCAP and Showtime/The Movie Channel, Inc. over the fee for a ''blanket'' license, the Southern District Court of New York stated that:

it is fair to assume that in any negotiation that encompasses as many disparate issues as do the guild agreements, the negotiators will agree to tradeoffs, among the various negotiated items, ... The process of negotiation is thus likely to yield a complex pattern of results, most of which would have been different if the individual issue had been negotiated entirely separately from the others. Accordingly, plucking one term out of the contract is likely to yield a fairly arbitrary result.

ASCAP v. *Showtime/The Movie Channel, Inc.*, published at 912 F.2d 572, 590 (S.D.N.Y. Dec. 20, 1989) (Civ. No. 13–95 (WCC) (footnote omitted).

[16] This is not to say that in any case in which a CARP relied on a license fee that was part of a larger agreement containing a number of provisions unrelated to the license fee, such reliance would necessarily be arbitrary. But in light of the other deficiencies in the CARP's reliance on the DCR license, discussed herein, and especially in light of the fact that the license fee was for the exercise of a nonexistent right, the Register is compelled to conclude that in this case, the CARP's reliance on the DCR license fee as its exclusive benchmark was arbitrary.

[17] ''DCR entered into a performance license with three record companies that represent approximately 60% of all recorded music sold in the United States.'' Services RF at 2.

[18] Section 802(c), of the Copyright Act, directs the CARP to ''act on the basis of a fully documented written record, prior decisions of the Copyright Royalty Tribunal, prior copyright arbitration panel determinations, and rulings by the Librarian of Congress under section 801(c).''

[19] For example, if the DCR license fee had been 5% of gross receipts (equaling $100,000) and 40% of the sound recordings on DCR's playlist were owned by DCR's record company partners, then DCR would pay 40% of the license fees ($40,000) on a prorata basis to these partners. The remaining 60% ($60,000) represents the value of the digital performance of works owned by non-partnership record companies performed during the relevant time period—a sum that DCR would not actually pay under the terms of its license agreement.

The 5% license fee value does not represent the actual value of the negotiated fee because this information is subject to a protective order. *See* n.8 *supra.*

16. Mr. Woodbury's statements on the precedential value of the agreement, however, are full of qualifications, and he readily acknowledged that ''a successful negotiation may have required that Warner and Sony compensate Music Choice for including the performance rights payments as part of the partnership agreement. The effect of this compensation may have restrained Warner and Sony in their choice of a higher fee level.'' *Id.*

In addition, the partnership agreement itself fails to support the Panel's finding. It includes material redacted subject to the protective order, DCR Exs. 7, 8 & 15 at ¶ 6, and a provision that the rate will be superseded if Congress establishes a performance right in sound recordings. DCR Exs. 7, 8, & 15 at ¶ 9. Vidich W.R.T. at 7; Tr. 2106–2107 (Vidich); Del Beccaro W.D.T. at 9. Because the partnership agreement included language that undermined any precedential value of the digital performance license included therein, the Register finds that the Panel's reliance on the DCR license fee as precedent was an arbitrary action. *See Motor Vehicle Mfrs. Ass'n* v. *State Farm Mutual Auto. Insurance Co.,* 463 U.S. 29 (1983) (agency action is arbitrary where the agency offers an explanation for its decision that runs counter to the record evidence).

In setting a range of possible rates for the section 114 license, the Panel made further adjustments to the base figure to account for the payments to the recording artists. Under the DPRSRA, recording artists are entitled to half of the royalties collected under the compulsory license. 17 U.S.C. 114(g). RIAA argues that the DCR license fee must be adjusted to account for this provision in the law that entitles recording artists to a share of the royalties, because the record companies were under no obligation to share the royalties. RIAA RPF ¶ 40; Petition at 28. RIAA also argued for additional upward adjustments of the benchmark to compensate the record companies for certain differences between the DCR license and the compulsory license, including compensation for loss of royalties generated from foreign and commercial subscribers, and loss of revenue due to a shift in how the Services offer their product to subscribers.

RIAA anchors its arguments for these requested adjustments on the presumption that the responsibility of the Panel was ''to determine the royalty [rate] that would be produced through free market negotiations, absent the compulsory license.'' RIAA RPF ¶ 41. This presumption, however, misrepresents the Panel's duty, which is to establish reasonable rates and terms. See discussion *supra* concerning the use of a marketplace standard in setting the royalty rate. While RIAA may have a reasonable expectation that a Panel would make appropriate adjustments to a marketplace benchmark that the Panel adopts for further consideration in light of the statutory objectives, and that is not to say that the requested adjustments are appropriate, there is no justification for making the adjustments where the benchmark value does not fulfill that function. Therefore, having found that the DCR license fee does not represent the marketplace value of sound recordings, the Register need not consider further arguments on adjusting the rate.

For the reasons cited above, the Register finds that the Panel was arbitrary in relying on the DCR license fee for the purpose of establishing an accurate evaluation of the marketplace value for the performance right.

The Panel's Determination of a Specific Range of Fees for the Public Performance of the Musical Compositions Was Arbitrary

The Services pay separate license fees to Broadcast Music, Inc. (BMI), the American Society of Composers, Authors, and Publishers (ASCAP), and SESAC, Inc. for the public performance of the underlying musical works in the sound recordings. The Services introduced evidence on what they pay the performing rights organizations for the public performance of the musical works to illustrate the industry practice that ''licensing rates ordinarily paid in the recording and music industries for the use of copyrighted works are far less than 41.5%, and generally are within the low single digit range for use of copyrighted music and sound recordings.'' Rosenthal [20] W.R.T. at 3; Tr. 1646, 1669–70, 1674 (Massarsky).[21]

Using the license fees DMX and DCR [22] pay for the right to perform musical compositions in the BMI and SESAC repertories and the anticipated payments that ASCAP will receive upon resolution of a rate dispute between itself and the Services, and not the interim rates that the Services currently pay ASCAP, which are usually lower than the final determination of the rate court, the Panel set an upper limit on the value of the performance right for the musical compositions. Report ¶¶ 167(B)–(G). In making this determination, the Panel accepted Massarsky's testimony that ASCAP license fees are ''generally greater than, but at least no less than, BMI license fees,'' and made its calculations accordingly. Report ¶ 167(E); see also RIAA PF ¶¶ 106–108.[23] In addition to setting an upper limit on the amount the Services would pay for these performance licenses, the Panel announced a lower limit for this benchmark but provided no discussion on how it arrived at this figure.

RIAA accepts the Panel's determination for an upper limit valuation for the performance right in musical works, but challenges the Panel's determination of the lower limit of this value. Petition at 16–20. RIAA contends that because the Panel had actual figures upon which to base its calculation, it was arbitrary to set a lower limit. *Id.* at 17.

From an examination of the record, the Register cannot determine how the Panel derived the lower limit figure, but she has identified at least one way that the Panel could have settled upon the lower figure. It entails the use of the interim rates which the Services pay ASCAP currently, instead of relying on a figure equal to or greater than the rate paid to BMI. Tr. 1669 (Massarsky), Tr. 1028–1029 (McCarthy). Use of such an approach, however, is expressly

[20] An attorney with the law firm of Berliner, Corcoran & Rowe, L.L.P., in Washington, D.C., who represents recording artists, writers, production companies, record companies, and multimedia companies.

[21] An economic consultant with the firm of Barry M. Massarsky Consulting, Inc.

[22] The Services pay an interim rate set in 1989 to ASCAP for the performance of the musical works in its repertoire. Tr. 1029 (McCarthy); Tr. 1656 (Massarsky). DCR also pays an interim rate to BMI. These rate disputes are currently the subject of adjudication before the ''rate court'' in the Southern District of New York. Services RF ¶¶ 52–53; 100–105. Pending the outcome of the rate cases, DCR has agreed to pay BMI the same contractual rate that DMX pays for the musical works performance license. Tr. 1653 (Massarsky).

[23] CRT and judicial precedent supports the Panel's premise that ASCAP usually receives slightly higher royalty fees for the public performance of its works than does BMI. In *American Society of Composers, Authors, and Publishers* v. *Showtime/The Movie Channel,* 912 F.2d 563 (2nd Cir. 1990), the court affirmed the rate court decision that a ''blanket'' license rate for use of ASCAP works should be set slightly higher than the rate the cable network pays for a BMI license. This result reflected the agreed upon 55–45 ratio that ASCAP and BMI adopted in dividing their share of the royalties for compulsory licenses paid by cable system operators for retransmissions of broadcast signals. See also 1978 Cable Royalty Distribution Determination, 45 FR 63026 (Sept. 23, 1980) (CRT determined that of the 4.5% royalty share awarded to the music claimants' group in the 1978 cable distribution proceeding, ASCAP would receive 54%, BMI, 43%, and SESAC, 3% of the royalties.); 1987 Cable Royalty Distribution Proceeding, 55 FR 11988 (March 30, 1990) (CRT again adjusted the distribution percentages for cable royalties so that ASCAP received a 58% share of the disputed royalties and BMI received the remaining 42% share).

disavowed by two of the Services' own expert witnesses who agree that it is inappropriate to rely on interim rates to determine competitive market rates. Woodbury W.R.T. at 19 n.70; Tr. 2710–2711 (Woodbury); Tr. 1029 (McCarthy). The Register concurs with these witnesses's assertions, and therefore rejects any figure which uses an interim rate in calculating a value when specific evidence exists in the record discounting this methodology and nothing supports its use.

Nor could the Panel consider just the individual license fees which the Services pay to a single performing rights organization in setting the lower limit, having rejected a similar argument when the Services initially proposed making this comparison. Report ¶ 168. A single license fee covers only those musical works under the control of the individual performing rights organization granting the license. Therefore, a Service must obtain a ''blanket'' license from every performing rights organization in order to have the freedom to play virtually any musical composition without infringing its copyright. Hence, the total value attached to the performance of the underlying musical works would be the sum of the license fees paid to each of the performing rights organizations, just as the value of the digital performance right in sound recordings would be the fees paid to all record companies. See Report ¶ 168.

The Register perceives no rational connection between the Panel's factual conclusions and its decision to set a lower limit for this benchmark. Where the record provides clear evidence of what the Services actually pay for the performance licenses, and the witnesses agree that the interim rates which are currently being paid represent *de minimis* value for these licenses, the Panel need not look beyond this information to determine the value of the benchmark. For the reasons discussed above, the Register does not consider the Panel's lower limit on the performance license fees for musical compositions when proposing a royalty rate for the section 114 license.

Use of Benchmarks Approximating Marketplace Value in Setting the Section 114 Rate

A benchmark is a marketplace point of reference, and as such, it need not be perfect in order to be considered in a rate setting proceeding. In the 1980 rate adjustment proceeding for coin-operated phonorecord players, the Tribunal considered different marketplace models and found that each analogy had distinguishing characteristics, but nevertheless considered them in conjunction with the record evidence and the statutory objectives. 1980 Adjustment of the Royalty Rate for Coin-Operated Phonorecord Players, 46 FR 884, 888 (1981) (''While acknowledging that our rate cannot be directly linked to marketplace parallels, we find that they serve as an appropriate benchmark to be weighed together with the entire record and the statutory criteria''). The U.S. Court of Appeals for the Seventh Circuit approved the Tribunal's approach, stating that:

> We think that the Tribunal could properly take cognizance of the marketplace analogies while appraising them to reflect the differences in both the respective markets (*e.g.*, with respect to volume and industry structure) and the regulatory environment. It is quite appropriate and normal in this administrative rate determination process to find distinguishing features among various analogous situations affecting the weight and appropriate thrust of evidence rather than its admissibility. No authority cited by AMOA would require the Tribunal to reject the ASCAP/SESAC analogies. Comparable rate analogies have been repeatedly endorsed as appropriate ratemaking devices.

AMOA v. *CRT*, 676 F.2d at 1157. See also *San Antonio* v. *United States*, 631 F.2d 831, 836–37 (D.C. Cir. 1980), *clarified*, 655 F.2d 1341 (D.C. Cir. 1981); *Burlington Northern, Inc.* v. *United States*, 555 F.2d 637, 641–43 (8th Cir. 1977).

When setting the rates for the statutory performance license in sound recordings, the benchmarks are merely the starting point for establishing an appropriate rate. The deciding body uses the appropriate marketplace analogies,[24] in conjunction with record evidence, and with regard for the statutory criteria, to set a reasonable rate.

In this proceeding, the Register finds that both the negotiated DCR license fee and the marketplace license fee for the performance of the musical works are useful at least in circumscribing the possible range of values under consideration for the statutory performance license in sound recordings. While the DCR license fee purports to represent a negotiated value for a right to which, by law, the record companies were not entitled (in addition to the recognition that the right should exist), the Register acknowledges that the value of the DCR license provides minimal information as to the value of the performance right ultimately granted in the DPRSRA, although it does provide some guidance for assessing the proposed rate. See Adjustment of Royalty Payable Under Compulsory License for Making and Distributing Phonorecords; Rates and Adjustment of Rates (115 Rate Adjustment Proceeding), 46 FR 10466, 10483 (Feb. 3, 1981) (''We find that the foreign experience is relevant—because it provides one measure of whether copyright owners in the United States are being afforded a fair return'').

On the other hand, the second reference point—the negotiated license fees for the performance of music embodied in the sound recordings—offers specific information on what the Services actually pay for the already-established performance right of one component of the sound recording. The Panel recognized this reference point's usefulness and used it to further support its choice of a royalty rate. Report ¶ 201. The question, however, is whether this reference point is determinative of the marketplace value of the performance right in sound recordings; and, as the Panel determined, the answer is no. Report ¶¶ 169, 201.

Initially, neither the Services nor RIAA placed much weight on this marketplace reference point, although RIAA has consistently argued that the value of the performance right in sound recordings is greater than the value of the performance right in the underlying musical works. RIAA RPF ¶ 16, Petition at 10–16. On the one hand, the Services argue that the musical composition is the key to a successful recording, Services RF ¶ 10–12, citing Tr. 1664 (Massarsky), and on the other hand, RIAA contends that a song lacks feeling until the recording artist breathes life into the song. Morris[25] W.D.T. at 1–2; Petition at 12–13. Because neither side presented conclusive evidence on this point, the Panel observed only that both groups are ''parents of the music.'' Report ¶ 169.

RIAA faults the Panel for its lack of discussion on the question of whose rights in the phonorecord are more valuable. Petition at 10–16. While the Register agrees that the Panel did not make specific citations to record evidence, its finding that ''[t]here was insufficient and conflicting evidence to make a determination that the

[24] A Panel is free to reject a proposed benchmark that does not reflect accurately the characteristics and dynamics of the industries subject to the proposed rate. *See e.g.*, Use of Certain Copyrighted Works in Connection with Noncommercial Broadcasting, 43 FR 25068–69 (1978) (CRT found voluntary license between BMI, Inc. and the public broadcasters, Public Broadcasting System and National Public Radio, of no assistance in setting rate for use of ASCAP repertoire); Adjustment of the Royalty Rate for Cable Systems; Federal Communications Commission's Deregulation of the Cable Industry, 47 FR 52146 (November 12, 1982).

[25] A country music artist who has recorded 14 albums, including five number one songs.

performers and record companies deserve a larger percentage from the Services than granted to the music works,'' was supported by the record evidence. Report ¶ 169.

To make its point, RIAA presented an analysis of revenues from record sales in support of its argument that the marketplace values the contributions of the record companies and the performing artists more than it values the contributions of the copyright owners in the musical compositions. RIAA's PF ¶¶ 112–120; Petition at 10–16. This evidence showed that copyright owners of the musical composition receive between 5–20% of the wholesale price for the sound recordings based on sales of CDs and cassette tapes—approximately 5% from the average wholesale price for an average CD and 12% from an average cassette.[26] RIAA PF ¶¶ 115, 119. Recording artists, on the other hand, receive 7–10% of the average wholesale price for a typical CD and 15–20% for a typical cassette, leaving approximately between 56–88% of the revenues from sales for the record companies. RIAA ¶ PF 116.

The Services disagreed with RIAA's interpretation of the marketplace data, contending that the reason the ''(r)ecord companies receive a bigger percentage of revenues from the sale of sound recordings (is) because they have a bigger monetary investment in the record production costs, as well as the leverage to minimize the royalties paid to songwriters, music publishers, and recording artists.'' Services RF ¶¶ 118–120. They also oppose RIAA's implication that the record companies should receive more value from the performance right in sound recordings than the songwriters receive for a similar right because the record companies garner more revenue from the use of the mechanical license than do the songwriters and composers.

The Services accurately note that the mechanical license and the digital performance license represent different and distinct rights to the copyright holders under the law, and they make no attempt to tie the value of the rights associated with the mechanical license to the value of the digital performance right, a right newly recognized with the passage of the DPRSRA. Even RIAA, the proponent of the assertion, fails to explain why the relative value of the mechanical license to the various owners and users has any application to the determination of the value of a digital performance license in sound recordings. Consequently, where no clear nexus exists between the values of different rights, the model serves no practical purpose in computing the value of the digital performance right.

Hence, RIAA's contention that the data supports its assertion that the marketplace places a higher value on the contributions of the record companies and the recording artists in the creation of the phonorecord fails, because it does not discuss the constraining effect the mechanical license has on the copyright owners in setting a value on their reproduction and distribution right. Record companies pay the copyright owners of the musical compositions no more than the statutory rate for the right to reproduce and distribute the musical composition in a phonorecord. The record company then, in turn, sells the phonorecord at a fair market price. Because both groups do not share equal power to set rates in an unfettered marketplace, it is unreasonable to compare the value of the reproduction and distribution right of musical compositions—a rate set by the government at a level to achieve certain statutory goals—with the revenues flowing to record companies from a price set in the marketplace according to the laws of supply and demand, and then to declare that the marketplace values the sound recording more than the underlying musical composition. Consequently, RIAA's evidence sheds no light on the relative value of the sound recording performance right and the musical works performance right.[27]

In addition to the foregoing discussion, the Register notes that Congress did not intend for the license fees paid under the new digital performance license to ''*diminish* in any respect the royalties payable to copyright owners of musical works for the public performance of their works.'' S. Rep. No. 104–128, at 33 (1995) (emphasis added). See also 17 U.S.C. 114(i). Although this statement does not express Congress' intent that the license be set below the value of the public performance right in the musical works, it indicates that Congress considered the possibility that such would be the outcome, and sought through express legislation to protect the current value of the performance right in musical works.

Based on a review of the record evidence, the Register concurs with the Panel's conclusion that there was insufficient evidence to determine that the performers and record companies deserve a larger percentage from the Services than that received by the copyright holders in the musical works. That being so, the Register finds no basis for making an upward adjustment to the musical works performance license fees to establish a broader range of potential rates.

c. Statutory Objectives

Section 801(b)(1) of the Copyright Act states that the rates for the section 114 license shall be calculated to achieve certain statutory objectives. The Panel evaluated each statutory objective and made a finding as to whether the Services or RIAA furthered that objective. If the Services contributed more to furthering the objective, the Panel gave more consideration to setting a rate at the lower end of the possible range, and conversely, if the record companies made the more significant contribution, the Panel found this to favor a rate toward the upper end. Report ¶ 19((A)–(D).

The Panel's analysis led it to set a rate toward the low end of its range, because a rate set toward the high end would thwart the statutory objectives under current market conditions. *Id.* The Panel expressly noted that a future Panel may reach an entirely different result based on the then-current economic state of the industry and new information on the Services' impact on the marketplace. Report ¶ 202.

RIAA contends that the Panel's findings that all factors favor setting a low rate is contrary to CRT precedent. Petition at 32. This contention relies on a statement from the D.C. Court of Appeals, which upon reviewing the CRT's 1980 Mechanical Rate Adjustment Proceeding concluded that the factors ''pull in opposing directions.'' *Id.*, citing *RIAA* v. *CRT*, 662 F.2d at 9. But in making this statement, the court merely made an observation that the statutory objectives required the Tribunal to weigh opposing factors in determining how best to achieve each objective. It went on to say that the Tribunal had the responsibility of reconciling these factors in setting a reasonable rate, but the court did not preclude the possibility that the Tribunal might find that the application of the factors to the evidence consistently supported either a high rate or a low rate. *RIAA* v. *CRT*, 662 F.2d at 9.

[26] Interested parties are free to negotiate a rate below the statutory rate for the mechanical license and often do. Tr. 1660 (Massarsky).

[27] Even if there was some value to the comparison, RIAA does not appear to factor into its calculations the value of the sound recordings in those phonorecords that do not show a profit. According to the record, ''approximately 85 percent of all sound recordings do not recoup the costs that are spent to make and to market those recordings. Indeed, over two-thirds of all sound recordings sell less than 1,000 copies.'' Report ¶ 105.

The Register approves the Panel's basic approach in utilizing the factors to determine its rate for the digital performance right and adopts the Panel's findings where the evidence supports its conclusions.

The Panel's determination that the statutory objectives supported setting a rate favoring the Services was not arbitrary

The Panel's ultimate conclusion that the best way to achieve the four statutory objectives was to set a low rate favoring the Services is supported by the evidence presented in this proceeding. How much weight to accord each objective is within the discretion of the Panel, which may accord more weight to one objective over the others so long as all objectives are served adequately. See *RIAA* v. *CRT*, 662 F.2d at 9. In *RIAA* v. *CRT*, the court reviewed the Tribunal's decision to raise the rate for making and distributing phonorecords from two cents to four cents. It found the copyright users' argument that the Tribunal failed to give adequate consideration to certain factors over others unavailing. In discussing the impact of the statutory objectives on the ratemaking process, the court stated:

> (T)he Tribunal was not told which factors should receive higher priorities. To the extent that the statutory objectives determine a range of reasonable royalty rates that would serve all these objectives adequately but to differing degrees, the Tribunal is free to choose among those rates, and courts are without authority to set aside the particular rate chosen by the Tribunal if it lies within a ''zone of reasonableness.''

Id. at 9 (citations omitted). Hence, the Panel was free to find that a rate on the low end was reasonable so long as that rate fell within the ''zone,'' and the ''zone'' was calculated to achieve the statutory objectives.

The Panel's analysis and application of the statutory objectives, however, are not without problems. The Register finds that on occasion, the Panel either did not perceive or misinterpreted the precedential underpinnings of the statutory objective.

A full discussion of the Panel's deliberations and the parties' responses concerning the evaluation and application of the four statutory objectives follows.

A. Maximize the Availability of Works. (17 U.S.C.801(b)(1)(A)).

The Panel found that the digital audio services ''substantially increase the availability of recordings by providing many channels of uninterrupted music of different genres,'' noting the diversity of the music offered by the Services. Report ¶¶ 121–122. Based on this finding, the Panel concluded at the end of its report that ''[t]o maximize the availability of creative works to the public * * * the rate should be set on the low side. A lower rate will hopefully ensure the Services' continued existence and encourage competition so that the greatest number of recordings will be exposed to the consumers.'' *Id.* ¶ 198(A).

RIAA alleges that the Panel misinterpreted this statutory objective because it focused on ''whether the Services promote the sale of sound recordings,'' rather than ''whether the proposed rate will maximize the availability of sound recordings.'' RIAA RPF ¶ 43; Petition at 37–41. In support of its position, RIAA recalls the 1980 jukebox rate adjustment proceeding, where the CRT concluded, in its discussion of section 801(b)(1)(A), that jukeboxes were not crucial to assuring the public of the availability of creative works. 1980 Adjustment of the Royalty Rate for Coin-Operated Phonorecord Players, 46 FR 884, 889 (1981). The Tribunal, however, did find that ''reasonable payment for jukebox performances will add incrementally to the encouragement of creation by songwriters and exploitation by music publishers, and so maximize availability of musical works to the public.'' *Id.* On the strength of past CRT precedent and the courts' recurring observation that compensation to the author or artist stimulates the creative force,[28] RIAA disputes the Panel's conclusion, contending that the best way to maximize the availability to the public is to ensure that copyright owners receive fair compensation for their works. Petition at 38.

The Services support the Panel's findings and conclusion but offer no legal support for their position except to note that ''[t]he Courts have long held that under copyright law, reward to copyright owners is a 'secondary consideration' that ultimately serves the cause of promoting public availability of copyrighted works.'' Reply to Petition at 27 (citations omitted). The Services assert rightfully that the primary rationale for the copyright law is to stimulate the creation of artistic works for the benefit of the public. *Twentieth Century Music* v. *Aiken*, 422 U.S. 151, 156 (1975), citing *Fox Film Corp.* v. *Doyal*, 286 U.S. 123, 127 (1932) (''The sole interest of the United States and the primary object in conferring this monopoly * * * lie in the general benefits derived by the public from the labors of authors''). But in underscoring the primary purpose for the copyright law, the Court in *Aiken* acknowledges that this aim is achieved by allowing the copyright owners to receive a fair return for their labor, the position advanced by RIAA. *Id.* (''The immediate effect of our copyright law is to secure a fair return for an 'author's' creative labor. But the ultimate aim is, by this incentive, to stimulate artistic creativity for the general public good''). *See also Sony Corp. America* v. *Universal City Studios, Inc.*, 464 U.S. 417 (1984); *United States* v. *Paramount Pictures*, 334 U.S. 131 (1948). The positive interplay between compensation and creation is a basic tenet of copyright law, and as such, its contribution to stimulating the creation of additional works cannot be set aside lightly.

In such matters where the Panel failed to discuss any relevant case law or past precedent construing the statutory objective before rendering its determination, the Register finds the Panel acted in an arbitrary manner. The finding is based on the Panel's failure to consider CRT precedent and to provide a rational basis for its departure from prior proceedings construing the same statutory objective. *See Pontchartrain Broad.* v. *FCC*, 15 F.3d 183, 185 (D.C. Cir. 1994) (''an unexplained departure from Commission precedent would have to be overturned as arbitrary and capricious''). *Motor Vehicle Mfrs. Ass'n* v. *State Farm Mutual Auto. Insurance Co.*, 463 U.S. 29 (1983); *Celcom Communications Corp.* v. *FCC*, 789 F.2d 67 (D.C. Cir. 1986); *Airmark Corp.* v. *FAA*, 758 F.2d 685 (D.C. Cir. 1985).

There is no record evidence to support a conclusion that the existence of the digital transmission services stimulates the creative process. Instead, the Panel made observations concerning the development of another method for disseminating creative works to the public—a valid and vital consideration addressed in the statutory objective concerning relative contributions from each party—but fails to discuss how the creation of a new mode of distribution will itself stimulate the creation of additional works.

[28] *Sony Corp. of America* v. *Universal City Studios, Inc.*, 464 U.S. 417, 429 (1984), quoting *United States* v. *Paramount Pictures*, 334 U.S. 131, 158 (1948). ('''[R]eward to the author or artist serves to induce release to the public of the products of his creative genius.'''); *Twentieth Century Music Corp.* v. *Aiken*, 422 U.S. 151, 156 (1975) (compensating authors ''serve[s] the cause of promoting broad public availability of literature, music, and the other arts''); 115 Rate Adjustment Proceeding, 46 FR 10479 (1981) (In discussing section 801(b)(1)(A), the CRT looked to the purpose of the section 115 license which was ''intended to encourage the creation and dissemination of musical compositions.'' Therefore, the Tribunal set the rate to ''afford songwriters a financial and not merely a psychic reward for their creative efforts'' as a way to maximize the availability of creative works).

Because the Panel failed to reconcile its determination with past CRT precedent and case law, the Register rejects both the Panel's findings and conclusions on this point as arbitrary. Instead, the Register concludes that the record companies and the performers make the greater contribution in maximizing the availability of the creative works to the public, a conclusion consistent with past CRT precedent.

B. Relative Roles of the Copyright Owners and the Copyright Users in Making Product Available to the Public. (17 U.S.C. 801(b)(1)(C)).

The statutory objective addressing the relative roles of the parties contains five different factors, which the Panel evaluated independently. In analyzing the first component of this objective, the relative creative contribution, the Panel found that both the recording companies and the performers make substantial creative contributions to the release of a sound recording. Report ¶ 87. Its determination credited the performers and the record companies for their work in making the musical work come alive. *Id.* ¶¶ 81–83. The Services were found to make no such significant contribution to the creation of the sound recording. Instead, their contribution was seen as more limited, since it merely enhanced the presentation of the final work through unique programming concepts. *Id.* ¶¶ 84–86. On balance, the Panel found ''that the artists and the record companies provide greater creative contributions to the release of sound recordings to the public than do the Services,'' *id.* ¶ 87, a finding supported by CRT precedent.[29]

The Panel continued its consideration of the relative contribution of the owners vis-a-vis the users in making the product available to the public and determined that the Services made the greater contribution with respect to the four remaining factors: technological contributions, capital investment, costs and risks to industry, and the opening of new markets. Report ¶¶ 88, 93, 94, 97, 98, and 109.

In making this determination, the Panel focused on the technological developments made by the Services in opening a new avenue for transmitting sound recordings to a larger and more diverse audience, including the creation of technology to uplink the signals to satellites and transmit them via cable; technology to identify the name of the sound recording and the artist during the performance; and technology for programming, encryption, and transmission of the sound recording. *Id.* ¶¶ 89–92. In contrast, the Panel found that the record companies made no contributions in these areas. *Id.* ¶ 93.

The Panel also weighed the evidence presented in support of the parties' relative roles in making capital investments in equipment and technology, the third factor. The Panel determined that the Services made a substantial showing of their $10 million investment in equipment and technology, Report ¶ 95 and cites therein, whereas RIAA did not suggest that any capital investment was required on its part. *Id.* ¶ 97.

And finally, the Panel found that the fourth factor, the relative costs and risks incurred by the parties in making the product available to the public, was greater for the Services than for the record companies and the performing artists, even though the record companies do incur substantial costs and risks in producing the product used by the Services. *Id.* ¶¶ 98–108. In making its determination, the Panel balanced the costs and risks involved in producing the sound recordings against the cost and risks associated with bringing the creative product to market in a new and novel way. *Id.* ¶¶ 99–107. In support of its findings, the Panel noted that the Services have invested significant start-up costs and are currently undergoing a shift in how they market their services. *Id.* ¶¶ 55, 73–78, 99, and 102. In addition, the Services contend, and the Panel agrees, that the Services face new competition from the internet and digital radio. Consequently, it is far from clear whether the Services can survive. *Id.* ¶¶ 72, 99.

The Panel also found that record companies face tremendous risks when producing new sound recordings, citing the record companies' submissions showing that record companies fail to recover the production costs for approximately 85% of sound recordings, much less show a profit. *Id.* ¶ 105. The Panel, however, went on to find that the record companies have adapted to the vagaries of the music business, and as an industry, have shown consistent growth in units shipped and dollar value of records, CDs, and music videos from 1982–1996. *Id.* ¶ 108.

The Panel's key finding from its analysis of the third objective was that the Services contribute more to the opening of new markets for creative expression through the development of the digital audio services. *Id.* ¶ 109. The Panel credited the Services with opening new markets for creative expression because they expose the public to a broader range of music than does traditional over-the-air radio. Unlike traditional radio, the Services offer multiple channels for classical, jazz, traditional, alternative, and ethnic formats. *Id.* ¶ 110. Because subscribers frequently purchase new music heard for the first time on the service, the Panel found that record companies arguably benefit directly from the expanded musical formats offered by the Services. *Id.* ¶ 112. The Panel also found that the Services' future plans to offer subscribers an opportunity to purchase the sound recordings directly will ''undoubtedly'' open new markets for the record companies. *Id.* ¶¶ 114–115.

The record companies do not accept the Panel's findings concerning this statutory objective, and once again, take issue with the Panel's interpretation, positing that the Panel impermissively focused on ''whether recording companies had made a particular contribution to the *Services* operations—and wholly ignored the contributions that the recording industry had made to the sound recordings themselves.'' Petition at 45–46. RIAA's predicate for its argument is its interpretation that the statutory phrase, ''in the product made available to the public,'' 17 U.S.C. 801(b)(1)(C), refers only to the creation of the sound recordings and not to the Services' creation of a new means for bringing the sound recordings to the listener. Petition at 46.

In addition to this alleged fundamental flaw in interpretation, RIAA contends that the Panel ''improperly collapsed (its cost/risk analysis) into a risk only (analysis)'' and ignored empirical evidence in the record discounting the promotional value of the Services' offerings. *Id.* at 47–48. RIAA, however, fails to note that the Panel did acknowledge that the record companies incur significant costs and risks in their business. Report ¶¶ 105–107. But the Panel also found that the Services presented no additional risk to the record companies ''*unless* the customers of the Services record the sound transmissions in lieu of purchasing these products at a retail store.'' Report ¶ 107 (emphasis added). Because the record companies introduced no evidence showing decreased overall sales of records and CDs, the Panel reasonably found that the record companies did not incur additional risk from lost sales due to the Services' activities. Report ¶¶ 107, 111.

[29] The CRT refused to award broadcasters a share of the cable royalties for their role in formatting radio stations. The Tribunal construed the claim as one for compilation which had a *de minimis* value. The U.S. Court of Appeals for the D.C. Circuit upheld the Tribunal's determination. *NAB* v. *CRT*, 772 F.2d at 931.

If anything, the Panel believed that the Services decreased the risk to the recording companies because the digital audio services have substantial promotional value. The promotional value comes from the constant airplay of new types of music not readily accessible in the marketplace, which in turn stimulates record sales. Report ¶ 110. In making this finding, the Panel relied on Simon's and Rubinstein's testimony that ''subscribers frequently purchase new music precisely because they heard it on one of the Services,'' Report ¶ 112 citing Simon [30] W.D.T. at 1; Rubinstein W.D.T. at 34; Tr. 1442 (Rubinstein), and on the record industries' practice of supplying complimentary copies of their products to the Services for use on the air to promote the sales of an album. Tr. 1291 (Rubinstein); Tr. 1182–83, 1201 (Talley) [31]; DMX Ex. 3. *See also* Tr. 2248 (Wildman) (''Is there a benefit to the record company from getting music exposed that might become a hit that wouldn't get exposed otherwise? Of course there is'').

Furthermore, RIAA's reliance on the preliminary DCR survey for the proposition that the Services do not promote sound recording sales is untenable where the record clearly shows that the record companies provide promotional copies to the Services. In fact, RIAA's own expert acknowledges ''there (are) promotional benefits to recording companies from having their music played on radio stations or the digital music services.'' Tr. 2220 (Wildman).

In contrast to RIAA's fundamental objection to the Panel's interpretation of this statutory objective, the Services contend that the Panel made a reasonable determination that the phrase, ''the product made available to the public,'' applied to both the sound recordings and the entire digital music service. Reply to Petition at 29. This finding is consistent with the 1980 rate adjustment proceeding for the mechanical license, where the CRT credited the record companies, the users of the musical compositions for purposes of the mechanical license, with developing new markets through technological innovations, and through the creation of record clubs, mail order sales, and television advertising campaigns. 46 FR 10480–81 (1981).

In making her determination on this point, the Register reflects on the statutory responsibilities of the Panel which is to set reasonable rates and terms for the public performance of sound recordings by *certain digital audio services.* (emphasis added). ''In deciding to grant a new exclusive right to perform copyrighted sound recordings publicly by means of digital audio transmission, the Committee was mindful of the need to strike a balance among all of the interests affected thereby.'' S. Rep. No. 104–128, at 15–16 (1995). By its very nature, the section 114 license contemplates weighing the contributions of the users in creating and expanding the market for the performance of the sound recording in a digital technological environment. Without dispute, the evidence reveals a large investment of capital by the Services to create a new industry that expands the offerings of the types of music beyond that which one receives over the radio, through live performances, and other traditional means of public performance. Report ¶¶ 44, 49, 52, 99, 102–104, 110, 113; Simon W.D.T. at 3–4; Rubinstein W.D.T. at 13–14; Tr. 853–54 (Del Beccaro); Tr. 1237–40 (Rubinstein); Tr. 1476–78 (Funkhouser); DMX Ex. 32. Conversely, the record companies offered little or no evidence on their contributions relating to the key factors. Report ¶¶ 93, 97, 111.

From the foregoing analysis, the Panel concluded that the record companies contributed more in only one of the five areas under consideration in evaluating this statutory objective, and consequently, the rate should be set at a minimum level in favor of the Services. Report ¶ 198(C).

C. To Minimize Any Disruptive Impact on the Structure of the Industries Involved. (17 U.S.C. 801(b)(1)(D)).

The Panel determined that a rate set too high could cause one or all of the Services to abandon the business. Report ¶¶ 117–118; Troxel [32] W.R.T. 1, 5–6; Tr. 2553–2554; DMX Ex. 49(b). The Panel considered the nature of the Services' business, noting its need to increase its subscriber base just to reach a break-even point without the added obligation of paying an additional fee for a digital performance right. *Id.* ¶¶ 119(a)–(d). The Panel also calculated that the record companies would receive substantially less than a 1% increase in their gross revenues even if the rate were set at the highest proposed level (41.5% of gross revenues), underscoring the lesser impact of the license fees on the record industry. *Id.* ¶ 119.

RIAA implies that a low statutory rate for the digital performance right will have a negative impact on their future negotiations with other digital services. RIAA RPF ¶¶ 58, 105; Petition at 43. They also object to the Panel's constant reference to revenues generated from the distribution and reproduction rights and its alleged lack of consideration of CRT precedent. Petition at 43–44.

In support of the Panel's evaluation, the Services note that RIAA failed to introduce any evidence concerning the impact a low rate would have on the record companies and performing artists, in direct contrast to the abundance of financial information submitted by the Services in support of their assertion that a high rate could devastate the industry. Reply to Petition at 28.

While RIAA correctly states that the Panel considered the record companies' revenues generated from the exercise of other rights granted to them under the Copyright Act, the Panel's purpose was merely to demonstrate the financial health of the industries. The Panel never implied that the record companies should receive anything less than reasonable compensation under the DPRSRA, nor that their revenues from the exercise of the distribution and reproduction rights are meant to compensate them for the use of their creative works under the new statutory license. Rather, it determined that a reasonable rate for the digital performance right should be set at a level to allow the three companies currently doing business to continue to do so. This balance in favor of the Services supports both the statutory objective to consider the impact on the industries and Congressional intent not to hamper the arrival of new technologies. S. Rep. No. 104–128, at 15–16 (1995). The law requires the Panel, and ultimately the Librarian, to set a reasonable rate that minimizes the disruptive impact on the industry. It does not require that the rate insure the survival of every company. See 115 Rate Adjustment Proceeding, 46 FR 10486 (1981) (''We conclude that while the Tribunal must seek to minimize disruptive impacts, in trying to set a rate that provides a fair return it is not required to avoid all impacts whatsoever'').

The Register acknowledges RIAA's uneasiness with the possibility that the rate which is ultimately adopted may have precedential value for their negotiations with other digital services, but such concern is misplaced. The rate under consideration applies only to the non-interactive digital audio subscription services, provided, of

[30] Senior Vice-President of Programming at Digital Cable Radio Associates.

[31] Executive Vice-President and Chief Technical Officer of Digital Music Express who oversees research and development, and technical operations worldwide.

[32] Chief Executive Officer and President of Digital Music Express since July 1997.

course, that they are eligible under the law and comply with all legal requirements. See 17 U.S.C. 114(d)(2). Congress, fully recognizing the threat that interactive services pose to the record companies, crafted the law so that they were ineligible for the compulsory license. The result of this decision is that record companies have an opportunity to negotiate an appropriate marketplace rate for a digital performance license with these services.

> Interactive services, which allow listeners to receive sound recordings ''on-demand,'' pose the greatest threat to traditional record sales, as to which sound recording copyright owners (of sound recordings) must have the right to negotiate the terms of licenses granted to interactive services.

S. Rep. No. 104–128, at 24 (1995). Congress also included provisions in the DPRSRA to establish different rates for different types of digital audio subscription services. Section 114(f)(1) states that ''(s)uch terms and rates shall distinguish among the different types of digital audio transmissions then in operation.'' This language gives the Panel and the parties broad discretion in setting rates for different types of digital audio services, when such distinction is warranted. Nor must the record companies accept the final rate from this determination for a new type of digital audio service which emerges before the next regularly scheduled rate adjustment proceeding. The law expressly allows for another rate-setting proceeding upon the filing of a petition. 17 U.S.C. 114(f)(4)(A)(i). Together, these provisions provide an opportunity to the record companies to make their case for a higher rate, where circumstances support such a determination.

In addition, as the market conditions change and the industry shows significant growth and profitability, another Panel will have an opportunity to make adjustments to the rate, and may well find that the changed circumstances favor an upward adjustment. In any event, the Register must make her recommendation based on the evidence in the current record before the Panel, which supports the Panel's determination that the best way to minimize the disruptive impact on the structure of the industries is to adopt a rate from the low range of possibilities. Report ¶ 198(D).

D. To afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions. (17 U.S.C. 801(b)(1)(B)).

Usually this balance is struck in the marketplace through arms-length negotiations; and even in the case of a statutory license, Congress encourages interested parties to negotiate among themselves and set a reasonable rate which inevitably affords fair compensation to all parties. 17 U.S.C. 114(f)(1), (4); 115(c)(3); 116(b); 118(b); and 119(c). A statutory rate, however, need not mirror a freely negotiated marketplace rate—and rarely does—because it is a mechanism whereby Congress implements policy considerations which are not normally part of the calculus of a marketplace rate. See 115 Rate Adjustment Proceeding, 46 FR 10466 (1981) (determining that the mechanical license regulates the price of music to lower the entry barriers for potential users of that music).

The creation of the digital performance right embodied similar considerations. It affords the copyright owners some control over the distribution of their creative works through digital transmissions, then balances the owners' right to compensation against the users' need for access to the works at a price that would not hamper their growth.

In the current proceeding, the Panel considered proposed marketplace benchmarks, including all the economic data, and weighed the record evidence in light of the statutory objectives. This process is structured so that it affords the copyright owners reasonable compensation and the users a fair income—the purpose of the second statutory objective. See 17 U.S.C. 801(b)(1)(B). Accordingly, a recommended rate so calculated achieves this final statutory objective, in that it reflects the balance between fair compensation for the owners and a fair return to the users. As fully discussed above, the Register supports the Panel's methodology in reaching its determination (although she rejects as arbitrary the Panel's application of that methodology in some respects) and has adopted the Panel's overall approach in making her recommendation to the Librarian.

d. The Register's Recommended Rate

Rate setting is not a precise science. National Cable Television Assoc. Inc., 724 F.2d 176, 182 (D.C. Cir. 1983). (''Ratemaking generally 'is an intensely practical affair.' The Tribunal's work particularly, in both ratemaking and royalty distributions, necessarily involves estimates and approximations. There has never been any pretense that the CRT's rulings rest on precise mathematical calculations; it suffices that they lie within a 'zone of reasonableness' ''). It requires evaluating the marketplace points of reference and tempering the choice of any proposed rate with the policy considerations underpinning the objectives of Congress in creating the license. Because this process requires the consideration of numerous factors, the CARPs, as the Tribunal before them, have considerable discretion in setting rates designed to achieve specific statutory objectives. *See* RIAA v. *CRT*, 662 F.2d at 9 (''To the extent that the statutory objectives determine a range of reasonable royalty rates that would serve all these objectives adequately but to differing degrees, the Tribunal is free to choose among those rates, and courts are without authority to set aside the particular rate chosen by the Tribunal if it lies within a 'zone of reasonableness' '').

Discretion in setting rates, however, assumes that the underlying rationale for making a determination is sound—a finding which the Register could not make in this proceeding because the Panel's undue reliance on the rate in the DCR license agreement, and its subsequent manipulation of the license fee, were arbitrary actions. *See Permian Basin Area Rate Cases,* 390 U.S. 747 (1968) (Rate setting agency allowed to use a variety of regulatory methods in setting rates provided that the result is not arbitrary or unreasonable). Consequently, the Register recommended that the Librarian reject the Panel's determination, which he did, and set a new rate.

In formulating her recommendation as to the appropriate rate for the digital performance license, the Register, like the Panel, considered the relevant marketplace points of reference offered into evidence.[33] These reference points guided the Register in her task of setting a reasonable rate for the performance of digital sound recordings. But unlike the Panel, the Register gave more consideration to the rates paid for the performance right in the musical compositions, because these rates represent an actual marketplace value for a public performance right in the digital arena, albeit not the digital performance right in sound recordings. The Register took this approach after finding that the DCR negotiated license fee could not reflect accurately the

[33] The values of the relevant marketplace reference points, the DCR negotiated license fee and the license fee for the performance of the musical works, are subject to a protective order, and hence, their numerical values have been omitted. Nevertheless, the values of the performance rights embodied in these licenses figure prominently in the determination of the value for the digital performance right in sound recordings. In fact, the sum of these license fees establishes the outer boundary of the ''zone of reasonableness'' for this proceeding.

marketplace value of the digital performance right since no such legal right existed at the time the rate was negotiated, and the negotiating parties were unwilling to enter a licensing agreement for the digital performance right absent a partnership agreement.

Nevertheless, the Register did take into account the negotiated value of the digital performance right in the DCR license in making her determination that the statutory rate should be less than the value of the performance rights of the musical compositions. This determination followed from a review of the evidence on the relative value of the sound recording component and the musical works component of a phonorecord, which failed to support the record industry's assertion that the marketplace valued the sound recording component more than the musical works component. This being so, the Register evaluated the only other relevant marketplace point of reference, the negotiated DCR license fee. Because this fee is considerably lower than the total value of the marketplace license fees which each Service pays for the right to publicly perform the musical works, and while not a true marker for the value of the digital performance right, it supports a determination that the value of the performance right in the sound recording does not exceed the value of the performance right in the musical works.

In addition to these factors, the Register considered the statutory criteria and Congress' intent in creating the license. Unlike the Panel, which found that all four factors support a low rate, the Register found that the copyright owners did more ''[t]o maximize the availability of creative works to the public,'' see 17 U.S.C. 801(b)(1)(A), and should receive fair compensation for their contributions in this area. However, the three remaining factors, especially the fourth factor, which requires that the rate be set ''[t]o minimize any disruptive impact on the structure of the industries involved,'' see 17 U.S.C. 801(b)(1)(D), compels the Register to consider the economic health of the digital audio transmission industry.

The evidence clearly shows that the Services have been facing an uphill battle in their struggle to achieve profitability. At this time, the digital audio industry is still struggling to create a sustainable subscriber base, and as yet, no digital audio transmission service has shown a profit nor does any service expect to reach profitability in the near future. Unfortunately, the actual state of financial health within the industry is difficult to ascertain from the projected budgets put forward by the Services. Nevertheless, the 5% rate proposed by the Panel did not draw an objection from the Services, indicating a reasonable state of financial health to absorb at least a rate set at this level.

For the foregoing reasons, the Register recommends a rate that will not harm the industry at this critical point in its development and finds that a 6.5% rate achieves this aim and meets all other statutory objectives. This rate reflects the deference the Register accorded the value of the performance right in the musical works, the consideration of the financial health of the industry, and the recognition that copyright owners contribute the lion share's to the creation of new works for the public's enjoyment.

e. Terms

On June 2, 1997, the Services submitted general comments concerning proposed terms and conditions for the digital performance license pursuant to the March 28, 1997, Order of the Copyright Office. They later proposed specific terms concerning how the Services would make payment, how often they would pay, and procedures for verifying the accuracy of those payments, including terms on confidentiality, recordkeeping, and audits. Services PF ¶¶ 122–128; 284–304. Included in their submissions were proposed terms establishing a payment schedule for the distribution of royalties to the featured artists and the nonfeatured musicians and vocalists. Services PF ¶¶ 287–289. The Panel refused to adopt these terms because the Services failed to present any evidence or testimony to support their proposal, but more importantly, because the Panel found that ''the issue of the timing of payments from the RIAA Collective to artists and other performers is not within the scope of this proceeding.'' Report at 56 n.21.

RIAA made similar proposals on how to administer the royalty payments, but offered two additional considerations, a minimum fee ''equivalent to the rate adopted in this proceeding'' and a late fee for untimely payments. RIAA PF ¶¶ 125–160. The Panel rejected the proposal to impose a minimum fee, see discussion supra, but accepted the RIAA proposal to impose a 1.5% late fee.

The Register supports and adopts the Panel's decision to reject the Services' proposed terms concerning further distribution of royalties to certain copyright owners by RIAA on the grounds that no evidence was introduced in support of the terms. Because this is a sufficient ground on which to reject the Services' proposed term, the Register need not address the Panel's determination that it lacked the authority to consider a payment schedule for the performing artists. The Register also need not address the Panel's rejection of the minimum fee because no party chose to challenge the Panel's decision. *See* n. 7, *supra.*

The parties' reactions to the terms adopted by the Panel

The Services did not file a post-panel motion to modify or set aside the Panel's determination, thereby signaling their acceptance of the Panel's resolution of any conflict between the parties concerning the terms. However, RIAA has raised two key items for further review by the Librarian: The adoption of a term which defines when copyright infringement occurs for purposes of the statutory digital performance license and the creation of a payment schedule that allows the Services to spread out their payment for the performances made between February 1996, the effective date of the Act, and November 1997, the month the Panel filed its report with the Librarian of Congress.[34] Petition at 7 n. 1.

The Panel's adoption of two of its terms was either arbitrary or contrary to law

The Register has determined that the Panel had no authority to set terms which attempt to delineate the scope of copyright infringement for the digital performance license, or alter a payment schedule already set by law. See Report ¶¶ 187–189, 206(a), (b).

1. *Payment of arrears.* The Panel adopted a term which allowed the Services to make back payments over a 30-month period for use of the sound recordings between February 1, 1996, and the end of the month in which the royalty rate is set and to delay the first payment for six months. Report ¶¶ 187, 206(a). The Register has determined, however, that adoption of this term is contrary to law.

Section 114(f)(5)(B) of the Copyright Act states that ''(a)ny royalty payments in arrears shall be made on or before the twentieth day of the month next succeeding the month in which the royalty fees are set.'' The ''arrears'' referenced in the statute refers to the copyright liability that accrued to the Services for those performances made since February 1, 1996, the effective date of the Act, and the end of the month in which the royalty rate is set.

[34] RIAA did not object to the Panel's refusal to grant its request for a minimum fee in its petition, nor does the Register find any reason to question the Panel's determination. As discussed supra, the Register finds the Panel's disposition on this issue to be well reasoned and supported by the evidence.

In spite of the express statutory language, the Panel fashioned a payment schedule to ease the burden on the Services in meeting this obligation.

The Panel found support for its action in the 1980 jukebox rate adjustment proceeding, in which the CRT raised the rate from $8 to $50, but did so in a progressive fashion. Report ¶ 186. The determination required the jukebox operators to make the first increased payment of $25 per jukebox per year on January 1, 1982, and a second $25 annual payment the following year. The CRT did not require the full $50 annual rate to be paid until January 1, 1984, approximately three years after setting the rate. 46 FR 884, 888, 890 (1981). The Tribunal adopted the phase-in payment schedule relying on its duty to set rates in accordance with the statutory objectives. It found that the gradual increase in payments furthered the objective concerned with minimizing the disruptive impact on the industries. *Id.* at 889. The Panel relied upon this CRT decision in adopting its phase-in program for payment of the arrears over a 30-month period.

The Services embrace the Panel's reliance on past CRT precedent for the inclusion of the phase-in payment term and claim that RIAA also agreed to allow the Services to make the "back payments" over a period of time. Reply to Petition at 14 n. 5. This assertion, however, is inaccurate. RIAA agreed that a phase-in schedule would be appropriate for the minimum fee, but never posited such a payment schedule for the arrears. See Tr. 2829 (RIAA closing argument). By comparing RIAA's statement on the proposal for making payments of a minimal fee,

> The recording industry proposes that the minimum fee be phased in to help minimize any disruptive effect from the fact that, for the first time, the services are going to be paying a fair fee—in fact, any fee at all for the performance of sound recordings,

Id. at 2829, see also RIAA PF ¶¶ 150–152, with its statement concerning the timing of the payment of arrears,

> In terms of the timing of the back payment, the statute leaves absolutely no question as to when the back payment from the services is due for the period from the Act's effective date through the date on which the Panel issues its decision.
>
> Section 114(f)(5)(B) says that "any royalty payment in arrears shall be made on or before the 20th day of the month next succeeding the month in which the royalty fees are set."

Id. at 2829–2830, see also RIAA PF ¶ 157, it is absolutely clear that RIAA never agreed to a payment scheme for the arrears that would allow the Services to make partial payments over a 30-month period.

In another attempt to support the Panel's conclusion, the Services construe the statutory provision broadly and argue that arrears refers to "any royalty payment in arrears" and "does not specifically cover the back payment for the extended period between the 1995 Act's February 1, 1996, effective date and the time the Panel sets the performance rate." Services RF ¶ 157. This assertion, however, is inconsistent with the legislative history and the plain language of the statute.

Thus, the Panel had no authority to create a graded payment schedule for the payment of the arrears because the statute expressly stated when payment was to occur. Section 114(f)(5)(B) states, without qualification, that "[a]ny royalty payments in arrears shall be made on or before the twentieth day of the month *next succeeding the month in which the royalty fees are set.*" (emphasis added). It is a well-established principle that, in interpreting the meaning of a statute, the language of the law is the best evidence of its meaning. *United States* v. *Ron Pair Enterprises, Inc.*, 489 U.S. 235, 241 (1989); Norman S. Singer, Sutherland Statutory Construction sec. 46.01 (5th ed. 1992 rev.) Because the statutory language is clear on its face, the Register finds that the Panel's and the Services' reliance on the CRT 1980 jukebox decision is arbitrary and contrary to well-established principles of law. And even if the statutory language were ambiguous, the legislative history supports the Register's and RIAA's interpretation of section 114(f)(5)(B).[35]

Because the Panel's action exceeded its authority, the Register recommends that the Librarian reject the proposed term because its adoption would be contrary to law.

2. *Copyright infringement.* The Panel adopted a term which stated that "[i]f a Service fails to make timely payments, it will be subject to liability for copyright infringement. Such liability will only come about, however, for knowing and willful acts which materially breach the statutory license terms." Report ¶ 206(b). The Register has determined that this term is contrary to law.

RIAA contends that the Panel "usurped the authority of Article III courts by attempting to define the circumstances where the Services are liable for copyright infringement." Petition at 7 n.1. In response, the Services argue that the DPRSRA supports the Panel's suggestion that minor technical violations should not result in an infringement action. Services Reply to Petition at 14 n.5. Specifically, the Services point to section 114(j)(7)(B) which limits complement to the performance of sound recordings from a single album, which Congress included "[t]o avoid imposing liability for programming that unintentionally may exceed the complement." S. Rep. No. 104–128, at 35 (1995).

The Register acknowledges that Congress made provisions to protect users from copyright liability for programming that unintentionally exceeds the complement, see 17 U.S.C. 114(j)(7), but she finds it impermissible to expand a particular provision of the copyright law which limits copyright liability under one set of circumstances to include additional limitations not contemplated by Congress. *Fame Publishing Co.* v. *Alabama Custom Tape, Inc.*, 507 F.2d 667, 670 (5th Cir.) *cert. denied*, 423 U.S. 841 (1975) ("We begin by noting that the compulsory license provision is a limited exception to the copyright holder's exclusive right to decide who shall make use of his composition. As such, it must be construed narrowly, lest the exception destroy, rather than prove, the rule. Thus we should neither expand the scope of the compulsory license provision beyond what Congress intended in 1909, nor interpret it in such a way as to frustrate that purpose").[36]

But more importantly, in examining the legislative history, it is clear that Congress meant for the CARP to have limited authority in adopting reasonable terms.

> By terms, the Committee means generally such details as how payments are to be made, when, and other accounting matters (such as are prescribed in section 115). In addition, the Librarian is to establish related terms under section 114(f)(2). Should additional terms be necessary to effectively implement the statutory license, the parties may negotiate such provisions or the CARPs may prescribe them.

S. Rep. No. 104–128, at 30 (1995). This language clearly indicates that the CARP had authority to set reasonable terms only so far as those terms insured the smooth administration of the license. There is no indication in the statutory language or in the legislative history that the scope of the terms should go

[35] S. Rep. No. 104–128, at 30 (1995) ("If the royalty fees have not been set at the time of performance, the performing entity must agree to pay the royalty fee to be determined under this subsection by the twentieth day of the month following the month in which the rates are set").

[36] Congress defined the scope of the digital performance right granted to the copyright owner and under what circumstances a digital audio service infringes that right. *See,* e.g., 17 U.S.C. 114 (d) and (e)(5).

beyond the creation of a workable administrative system and reach substantive issues, such as defining the scope of copyright infringement for those availing themselves of the statutory license.

Congress carefully delineated the scope of the digital performance right and the limitations on that right within the provisions of the statute. Section 114(d), entitled ''Limitations on Exclusive Right,'' states with specificity when a performance by means of a digital audio transmissions is not an infringement, just as section 114(f)(5) defines when a public performance of a sound recording by means of a nonexempt subscription digital transmission is not an infringement. For the Panel to fashion a term further delineating the issue of copyright infringement when Congress has already acted is an improper exercise of authority beyond that granted under the statute.

Accordingly, the Register finds that the Panel had no authority to set a term construing the meaning of copyright infringement for purposes of section 114. See Report ¶¶ 188, 206(b). Because the Panel's action exceeded its authority, the Register recommends that the Librarian reject the proposed term because its adoption would be contrary to law.

f. Other Issues

1. *Effective date.* Section 114(f)(5)(B) states that payments in arrears for the performance of sound recordings prior to the setting of a royalty rate are due on a date certain in the month following the month in which the rate is set. Both the Panel and RIAA assume that the ''date the royalty rate is set'' is the date the Panel submits its report to the Librarian of Congress. See Report ¶ 186; Petition at 7 n.1. The Register disagrees with this assessment.

Section 802(g) governs judicial review of the Librarian's decision with respect to CARP determinations. The section allows an aggrieved party 30 days to file an appeal with the United States Court of Appeals for the District of Columbia Circuit, but does not relieve a party of his or her obligation to make royalty payments during the pendency of the appeal. In the event that no appeal is taken, the section states that ''the decision of the Librarian is final, and the royalty fee * * * shall take effect as set forth in the decision.'' 17 U.S.C. 802(g). Neither section 114 nor chapter 8 makes further reference to the possible effective date of royalty rates.

As discussed in an earlier order setting a rate for the satellite compulsory license, 17 U.S.C. 119, the Register interprets the decision referenced in section 802(g) ''to mean the decision of the Librarian, and not the decision of the CARP, since section 802(g) only refers to the decision of the Librarian. Consequently, the Register concludes that only the Librarian of Congress has the authority to set the effective dates of the royalty rates in this proceeding.'' Rate Adjustment for the Satellite Carrier Compulsory License, 62 FR 55754 (1997). See also *RIAA* v. *CRT,* 662 F.2d at 14 (''When the statute authorizing agency action fails to specify a timetable for effectiveness of decisions, the agency normally retains considerable discretion to choose an effective date'') (footnote omitted). This reasoning applies equally to the current proceeding, since no other guidance for setting the effective date is to be found in the statute or the legislative history.

The Register has pondered the question of an appropriate effective date and believes that the Panel's concern with minimizing the disruptive impact on the structure of the industries involved was well founded. See discussion supra concerning the economic health of the Services. Consequently, the Register proposes an effective date of June 1, 1998, which would require the Services to make full payment of the arrears on July 20, 1998, in addition to the payment for the month of June 1998, with subsequent payments to RIAA on the 20th day of each subsequent month. This date provides the Services with a measured amount of time to provide for any necessary adjustments in their business operations to meet their copyright obligations.

The Tribunal took a similar course when it set the effective date for implementing the rate increase for making and distributing phonorecords approximately six months after publication of its final rule. Section 115 Rate Adjustment Proceeding, 46 FR 10486 (1981). The Tribunal chose not to implement the rate change immediately in order to minimize the effect of the upward adjustment on the copyright users. The United States Court of Appeals for the District of Columbia Circuit upheld the Tribunal's decision to postpone the effective date because:

> The Tribunal's opinion demonstrates its concern ''to minimize disruptive impacts'' on the recording industry, and its view that the effective date of a royalty adjustment should be arranged so as to be ''less disruptive to the industries.'' Although the Tribunal concluded that a single increase to the full four-cent rate would not be unduly disruptive, it was within the Tribunal's discretion to give the industry adequate lead time to prepare for the increase.

RIAA v. *CRT*, 662 F.2d at 14 (citations omitted).

2. *Value of an individual performance of a sound recording.* The Register notes that the Panel stopped prematurely in its consideration of the value of the public performance of a sound recording. Its entire inquiry focused on the value of the ''blanket license'' for the right to perform the sound recording, without once considering the value of the individual performance—a value which must be established in order for the collecting entity to perform its function not only to collect, but also to distribute royalties. Consequently, the Register has made a determination that each performance of each sound recording is of equal value and has included a term that incorporates this determination.

To do otherwise requires the parties to establish criteria for establishing differential values for individual sound recordings or various categories of sound recordings. Neither the Services nor RIAA proposed any methodology for assigning different values to different sound recordings. In the absence of an alternative method for assessing the value of the performance of the sound recording, the Register has no alternative but to find that the value of each performance of a sound recording has equal value. Furthermore, the structure of the statute contemplates direct payment of royalty fees to individual copyright owners when negotiated license agreements exist between one or more copyright owner and one or more digital audio service. To accommodate this structure in the absence of any statutory language or legislative intent to the contrary, each performance of each sound recording must be afforded equal value.

This determination does not alter the statutory provision that specifies how the copyright owner of the right to publicly perform the sound recording must allocate the statutory fees among the recording artists. See 17 U.S.C. 114(f)(2).

3. *Audit of the designated collective.* Although the membership of the collective represented by RIAA includes over 275 record labels which create more than 90 percent of all legitimate sound recordings sold in the United States, it does not represent the record companies responsible for the creation of the remaining 10% of the sound recordings. Report ¶ 20. Nevertheless, the Panel found, and the Register concurs, that the parties' suggestion to designate a single entity to collect and to distribute the royalty fees creates an efficient administrative mechanism. Report ¶ 184.

It is common practice, however, for the government body making such designations to implement safeguards to monitor the functions of the collective.[37] To this end, the Register recommends new terms that afford the copyright holders a right to audit the collective's practices in handling the royalty fees. The Register takes this step to insure copyright holders access to the records of the organization charged with the fiduciary responsibility of making an equitable distribution among those entitled to receive a portion of the funds, while at the same time preserving the confidentiality of the organization's business records. These terms mirror those formulated by the parties and adopted by the Panel which allow the collective to audit the business records of the Services to insure proper payment of the royalties.

4. *Deduction of administrative costs.* Neither the parties nor the Panel gave any consideration to the manner in which the collecting entity would deduct from payments to copyright owners its costs of administering the funds it receives and disburses. Nevertheless, the Panel should have addressed this key term of the compulsory license. Therefore, the Register finds it necessary to establish an additional term that permits the collecting entity to deduct from the royalties it pays to copyright owners the costs it incurs in administering the funds, so long as the costs deducted are reasonable and are no more than the actual costs incurred by the collecting entity.

5. *Unknown copyright owners.* The digital audio services will pay royalties on all sound recording performances without regard to the further disbursement of these fees to the numerous copyright holders. The collective will have little difficulty in identifying and locating the overwhelming majority of the copyright holders entitled to receive a portion of the fees, since the membership of the collective represents the interests of the copyright holders in over 90% of all sound recordings. Problems may arise, however, as RIAA attempts to identify and locate the copyright holders to the remaining 10% of the sound recordings. In anticipation of the likelihood that RIAA will not be able to locate all copyright holders, the Register recommends the adoption of a term that segregates the fees for unknown copyright owners into a separate trust account for future distribution to the rightful owner, or in the event that the owner is not found, allows the collective to use the funds after a period of three years, see 17 U.S.C. 507(b), to offset its administrative costs associated only with the collection and distribution of royalty fees collected under the statutory license.

6. *Rates for other types of digital audio services.* The rates and terms announced in this notice apply to DCR, DMX, and Muzak, the three digital audio transmission services participating in this proceeding, and to any other digital audio transmission service that avails itself of the compulsory license, provided that the service is of the same type. The Register raises this point to avoid any confusion over the Panel's statement which implies that the rates and terms set in this proceeding ''shall be binding on all copyright owners of sound recordings and entities performing sound recording[s].'' Report ¶ 1, citing 17 U.S.C. 114(f)(2). A general provision, however, must be read in conjunction with more specific statutory language; in this case, section 114(f)(4)(A), which provides for additional rate adjustment proceedings upon petition from any copyright owner or entity performing sound recordings when a new type of digital audio transmission becomes or is about to become operational.

VI. Conclusion

In considering the evidence in the record, the contentions of the parties, and the statutory objectives, the Register of Copyrights recommends that the Librarian adopt a statutory rate for the digital performance of sound recordings, pursuant to 17 U.S.C. 114, of 6.5% of gross revenues from subscribers residing within the United States.

In addition, the Register recommends that the Librarian adopt the reasonable terms propounded by the Panel except for those terms concerning the payment schedule for arrears and potential limitations on the scope of copyright infringement. The Register also recommends setting June 1, 1998, as the effective date for implementing the new rate and terms in order to ease the burden on each Service on meeting its initial obligations under the statutory license.

VII. The Order of the Librarian of Congress

Having duly considered the recommendations of the Register of Copyrights regarding the Report of the Copyright Arbitration Royalty Panel in the matter to set reasonable terms and rates for the digital performance right in sound recordings, 17 U.S.C. 114, the Librarian of Congress fully endorses and adopts her recommendation to set the rate for the statutory license at 6.5% of gross revenues from U.S. residential subscribers. This rate shall apply to those digital audio services represented in this proceeding and any other eligible digital audio service of the same type that subsequently enters the market and makes use of the statutory license. The Librarian of Congress also adopts the Register's recommendation to reject the terms concerning potential limits on what constitutes copyright infringement and the proposed schedule for the payment of the arrears.

For the reasons stated in the Register's recommendation, the Librarian is exercising his authority under 17 U.S.C. 802(f) and is issuing this order which adopts new Copyright Office regulations setting reasonable terms and rates for the digital performance right in sound recordings.

List of Subjects in 37 CFR Part 260

Copyright, Digital Audio Transmissions, Performance Right, Sound Recordings

Final Regulation

In consideration of the foregoing, part 260 of 37 CFR is added to read as follows:

PART 260—USE OF SOUND RECORDINGS IN A DIGITAL PERFORMANCE

Sec.

Authority: 17 U.S.C. 114, 801(b)(1).

§ 260.1 General.

(a) This part 260 establishes terms and rates of royalty payments for the public performance of sound recordings by nonexempt subscription digital transmission services in accordance with the provisions of 17 U.S.C. 114 and 801(b)(1).

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[37] A government's general policy toward the regulation of collective administration should be to limit government intervention to only ''that which is necessary to facilitate the effective operations of the collective administration organization, consistent with the private character of the rights involved, while checking possible abuses by that collective in the least intrusive manner possible within'' the overall context of the society involved. David Sinacore-Guinn, Collective Administration of Copyrights and Neighboring Rights, 544 (1993).

(b) Upon compliance with 17 U.S.C. 114 and the terms and rates of this part, a nonexempt subscription digital transmission service may engage in the activities set forth in 17 U.S.C. 114.

§ 260.2 Royalty fees for the digital performance of sound recordings.

(a) Commencing June 1, 1998, the royalty fee for the digital performance of sound recordings by nonexempt subscription digital services shall be 6.5% of gross revenues resulting from residential services in the United States.

(b) A nonexempt subscription digital transmission service (the ''Licensee'') shall pay a late fee of 1.5% per month, or the highest lawful rate, whichever is lower, for any payment received after the due date. Late fees shall accrue from the due date until payment is received.

(c)(1) For purposes of this section, *gross revenues* shall mean all monies derived from the operation of the programming service of the Licensee and shall be comprised of the following:

(i) Monies received by Licensee from Licensee's carriers and directly from residential U.S. subscribers for Licensee's programming service;

(ii) Licensee's advertising revenues (as billed), or other monies received from sponsors if any, less advertising agency commissions not to exceed 15% of those fees incurred to recognized advertising agency not owned or controlled by Licensee;

(iii) Monies received for the provision of time on the Programming Service to any third party;

(iv) Monies received from the sale of time to providers of paid programming such as infomercials;

(v) Where merchandise or anything or service of value is received by licensee in lieu of cash consideration for the use of Licensee's programming service, the fair market value thereof or Licensee's prevailing published rate, whichever is less;

(vi) Monies or other consideration received by Licensee from Licensee's carriers, but not including monies received by Licensee's carriers from others and not accounted for by Licensee's carriers to Licensee, for the provision of hardware by anyone and used in connection with the Programming Service;

(vii) Monies or other consideration received for any references to or inclusion of any product or service on the programming service; and

(viii) Bad debts recovered regarding paragraphs (c)(1) (i) through (vii) of this section.

(2)Gross revenues shall include such payments as are in paragraphs (c)(1) (i) through (viii) of this section to which Licensee is entitled but which are paid to a parent, subsidiary, division, or affiliate of Licensee, in lieu of payment to Licensee but not including payments to Licensee's carriers for the programming service. Licensee shall be allowed a deduction from ''gross revenues'' as defined in paragraph (c)(1) of this section for affiliate revenue returned during the reporting period and for bad debts actually written off during reporting period.

(d) During any given payment period, the value of each performance of each digital sound recording shall be the same.

§ 260.3 Terms for making payment of royalty fees.

(a) All royalty payments shall be made to a designated agent(s), to be determined by the parties through voluntary license agreements or by a duly appointed Copyright Arbitration Royalty Panel pursuant to the procedures set forth in subchapter B of 37 CFR, part 251.

(b) Payment shall be made on the twentieth day after the end of each month for that month, commencing with the month succeeding the month in which the royalty fees are set.

(c) The agent designated to receive the royalty payments and the statements of account shall have the responsibility of making further distribution of these fees to those parties entitled to receive such payment according to the provisions set forth at 17 U.S.C. 114(g).

(d) The designated agent may deduct reasonable costs incurred in the administration of the distribution of the royalties, so long as the reasonable costs do not exceed the actual costs incurred by the collecting entity.

(e) Commencing June 1, 1998, and until such time as a new designation is made, the Recording Industry Association of America, Inc. shall be the agent receiving royalty payments and statements of accounts.

§ 260.4 Confidential information and statements of account.

(a) For purposes of this part, confidential information shall include statements of account and any information pertaining to the statements of account designated as confidential by the nonexempt subscription digital transmission service filing the statement. Confidential information shall also include any information so designated in a confidentiality agreement which has been duly executed between a nonexempt subscription digital transmission service and an interested party, or between one or more interested parties; *Provided* that all such information shall be made available, for the verification proceedings provided for in §§ 260.5 and 260.6 of this part.

(b) Nonexempt subscription digital transmission services shall submit monthly statements of account on a form provided by the agent designated to collect such forms and the monthly royalty payments.

(c) A statement of account shall include only such information as is necessary to verify the accompanying royalty payment. Additional information beyond that which is sufficient to verify the calculation of the royalty fees shall not be included on the statement of account.

(d) Access to the confidential information pertaining to the royalty payments shall be limited to:

(1) Those employees of the designated agent who are not also employees or officers of a sound recording copyright owner or performing artist, and who, for the purpose of performing their assigned duties during the ordinary course of business, require access to the records; and

(2) An independent and qualified auditor who is not an employee or officer of a sound recording copyright owner or performing artist, but is authorized to act on behalf of the interested copyright owners with respect to the verification of the royalty payments.

(e) The designated agent shall implement procedures to safeguard all confidential financial and business information, including but not limited to royalty payments, submitted as part of the statements of account. Confidential information shall be maintained in locked files.

(f) Books and records relating to the payment of the license fees shall be kept in accordance with generally accepted accounting principles for a period of three years. These records shall include, but are not limited to, the statements of account, records documenting an interested party's share of the royalty fees, and the records pertaining to the administration of the collection process and the further distribution of the royalty fees to those interested parties entitled to receive such fees.

§ 260.5 Verification of statements of account.

(a) *General.* This section prescribes general rules pertaining to the verification of the statements of account by interested parties according to terms promulgated by a duly appointed copyright arbitration royalty panel, under its authority to set reasonable terms and rates pursuant to 17 U.S.C.

114 and 801(b)(1), and the Librarian of Congress under his authority pursuant to 17 U.S.C. 802(f).

(b) *Frequency of verification.* Interested parties may conduct a single audit of a nonexempt subscription digital transmission service during any given calendar year.

(c) *Notice of intent to audit.* Interested parties must submit a notice of intent to audit a particular service with the Copyright Office, which shall publish in the **Federal Register** a notice announcing the receipt of the notice of intent to audit within 30 days of the filing of the interested parties' notice. Such notification of intent to audit shall also be served at the same time on the party to be audited.

(d) *Retention of records.* The party requesting the verification procedure shall retain the report of the verification for a period of three years.

(e) *Acceptable verification procedure.* An audit, including underlying paperwork, which was performed in the ordinary course of business according to generally accepted auditing standards by an independent auditor, shall serve as an acceptable verification procedure for all parties.

(f) *Costs of the verification procedure.* The interested parties requesting the verification procedure shall pay for the cost of the verification procedure, unless an independent auditor concludes that there was an underpayment of five (5) percent or more; in which case, the service which made the underpayment shall bear the costs of the verification procedure.

(g) *Interested parties.* For purposes of this section, interested parties are those copyright owners who are entitled to receive royalty fees pursuant to 17 U.S.C. 114(g), their designated agents, or the entity designated by the copyright arbitration royalty panel in 37 CFR 260.3 to receive and to distribute the royalty fees.

§ 260.6 Verification of royalty payments.

(a) *General.* This section prescribes general rules pertaining to the verification of the payment of royalty fees to those parties entitled to receive such fees, according to terms promulgated by a duly appointed copyright arbitration royalty panel, under its authority to set reasonable terms and rates pursuant to 17 U.S.C. 114 and 801(b)(1), and the Librarian of Congress under his authority pursuant to 17 U.S.C. 802(f).

(b) *Frequency of verification.* Interested parties may conduct a single audit of the entity making the royalty payment during any given calendar year.

(c) *Notice of intent to audit.* Interested parties must submit a notice of intent to audit the entity making the royalty payment with the Copyright Office, which shall publish in the **Federal Register** a notice announcing the receipt of the notice of intent to audit within 30 days of the filing of the interested parties' notice. Such notification of interest shall also be served at the same time on the party to be audited.

(d) *Retention of records.* The party requesting the verification procedure shall retain the report of the verification for a period of three years.

(e) *Acceptable verification procedure.* An audit, including underlying paperwork, which was performed in the ordinary course of business according to generally accepted auditing standards by an independent auditor, shall serve as an acceptable verification procedure for all parties.

(f) *Costs of the verification procedure.* The interested parties requesting the verification procedure shall pay for the cost of the verification procedure, unless an independent auditor concludes that there was an underpayment of five (5) percent or more; in which case, the entity which made the underpayment shall bear the costs of the verification procedure.

(g) *Interested parties.* For purposes of this section, interested parties are those copyright owners who are entitled to receive royalty fees pursuant to 17 U.S.C. 114(g), or their designated agents.

§ 260.7 Unknown copyright owners.

If the designated collecting agent is unable to identify or locate a copyright owner who is entitled to receive a royalty payment under this part, the collecting agent shall retain the required payment in a segregated trust account for a period of three years from the date of payment. No claim to such payment shall be valid after the expiration of the three year period. After the expiration of this period, the collecting agent may use the unclaimed funds to offset the cost of the administration of the collection and distribution of the royalty fees.

Dated: April 17, 1998.

Marybeth Peters,

Register of Copyrights.

James H. Billington,

The Librarian of Congress.

[FR Doc. 98–12266 Filed 5–7–98; 8:45 am]

BILLING CODE 1410–33–U

ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 52

[FRL 325–6]

Approval and Promulgation of State Implementation Plans

CFR Correction

In title 40 of the Code of Federal Regulations, part 52 (§ 52.1019 to end), revised as of July 1, 1997, in appendix D to part 52, on page 610, in the first and second columns, equations d–1 and d–2 were inadvertently omitted. Additionally, the second line in the legend for Equation D–2 was incorrectly printed. The missing equations and corrected line should read as follows:

Appendix D to Part 52—Determination of Sulfur Dioxide Emissions From Stationary Sources by Continuous Monitors

* * * * *

$$\bar{X} \; \frac{\sum_{i=1}^{n} x_i}{n} \qquad \text{Equation D-1}$$

* * * * *

$$\mathrm{C.I.}_{95} = \frac{t_{.975}}{n\sqrt{n-1}} \sqrt{n\left(\sum \chi_i^{2}\right) - \left(\sum \chi_i\right)^2}$$

Equation D-2

* * * * *

$t_{.975} = t_{1-a/2}$, and

* * * * *

BILLING CODE 1505–01–D

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 648

[Docket No. 980318066–8066–01; I.D. 022698A]

Fisheries of the Northeastern United States; Northeast Multispecies Fishery; Framework Adjustment 25; Correction

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Final rule; correction.

SUMMARY: This rule removes regulatory language inadvertently added, clarifies the raised footrope requirement for Small Mesh Area 1 & 2, and corrects an