46 FR 10466-02
46 FR 10466-02, 1981 WL 115839 (F.R.)
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RULES and REGULATIONS

COPYRIGHT ROYALTY TRIBUNAL

37 CFR Part 307

[Docket No. 80-2]

Adjustment of Royalty Payable Under Compulsory License for Making and Distributing Phonorecords; Rates and Adjustment of Rates

Tuesday, February 3, 1981

***10466** AGENCY: Copyright Royalty Tribunal (CRT)

ACTION: Final Rule Findings.

SUMMARY: Copyright Royalty Tribunal has adopted rule adjusting the rates of royalty payable under compulsory license of 17 U.S.C. 115 for making and distributing phonorecords embodying nondramatic musical works. The rule also provides for possible subsequent adjustment of the royalty rates. This document contains the detailed findings to accompany the rule as required by 17 U.S.C. 803(b).

EFFECTIVE DATE: January 31, 1981.

FOR FURTHER INFORMATION CONTACT:

Clarence L. James, Jr., Chairman Copyright Royalty Tribunal, (202) 653-5175.

SUPPLEMENTARY INFORMATION: The Copyright Royalty Tribunal published in the Federal Register of January 5, 1981 (46 FR 891) its final rule concerning the adjustment of the royalty payable under compulsory license for making and distributing phonorecords. It was stated in that publication that the detailed findings to accompany the rule, as required by 17 U.S.C. 803(b), would be published within thirty days.

Introduction and Chronology

17 U.S.C. 804(a)(1) directs the Copyright Royalty Tribunal (Tribunal) to publish on January 1, 1980 in the Federal Register notice of commencement of proceedings concerning possible adjustment of the royalty rates established in 17 U.S.C. 115 concerning the compulsory license for the use of nondramatic musical works in the making of phonorecords. The required notice appeared in the Federal Register of January 2, 1980 (45 FR 63).

Parties to the proceeding included both copyright owners and copyright users. Copyright owners were represented by (either by witnesses or written submissions) the National Music Publishers Association, Inc. (NMPA), Church Music Publish-

ers Association, the Association of Independent Music Publishers, the American Guild of Authors and Composers (AGAC), the Nashville Songwriters Association International and Songwriters Resources and Services. Copyright users were represented by the Recording Industry Association of America (RIAA). CBS Inc. made various written submissions in addition to oral testimony by its officers and employees. The Amusement and Operators Association (AMOA), a trade association representing operators of jukeboxes and other machines, and the American Society of Music Arrangers (ASMA) also made written submissions.

In its notice of January 2, 1980 the Tribunal directed parties to submit motions concerning jurisdictional or legal questions by March 3, 1980, and reply comments by March 20. The Tribunal also directed that economic or other studies be submitted by April 1, 1980, with reply comments by April 21, 1980. Studies were submitted by NMPA, AGAC and RIAA.

After receiving various filings by the parties, a pre-hearing conference was held on March 10, 1980. On March 25 the Tribunal heard oral argument on the motion of RIAA that the Tribunal lacked jurisdiction to adjust the royalty rate to ***10467** provide for the fixing of the royalty rate as a percentage of the price of the phonorecord. On March 27 the Tribunal denied the motion of RIAA.

On April 21, 1980 RIAA moved that the Tribunal request NMPA to provide "evidence concerning the financial condition of the publishing industry". On April 23, 1980 NMPA moved that the Tribunal request RIAA and Cambridge Research Institute to submit the underlying input data for its economic study. The Tribunal on April 24, after considering the views of parties, issued an order stating that the Tribunal "at the present time takes no action on the subject matter of the motion of the Recording Industry Association of America" and requesting RIAA and the Cambridge Research Institute to submit the requested input data, including the individual responses to questionnaires. On April 29, RIAA moved the Tribunal to reconsider its request for the production of input data. This motion was denied on April 30.

On May 2, 1980 the Tribunal requested legal memoranda on the relevance of profitability to an adjustment of the mechanical royalty. Memoranda were submitted by NMPA, AGAC and RIAA.

The evidentiary hearing commenced on May 7, 1980 and included 46 days of hearings, 35 witnesses, over 6,000 pages of transcript and hundreds of additional pages of documents, financial tables and economic charts.

On July 15, 1980 AGAC moved to strike the Cambridge study, reply Comments and all testimony dependent upon the input data. The Tribunal denied AGAC's motion on October 14, 1980.

On August 6, 1980 the Tribunal issued an order declaring "that representative aggregate data concerning the financial condition of the music publishers may be relevant to the determination * * * of the mechanical royalty rate" and requesting NMPA and music publishers to assemble and present data in certain specified areas. On October 1, NMPA submitted Aggregate Data Concerning the Financial Condition of Music

Publishers to the Tribunal.

The Tribunal heard closing argument in this proceeding on November 19, 1980. The Tribunal considered its final determination in this proceeding at public meetings on December 18 and 19. The Tribunal's final regulation was adopted on December 19, docketed by the Federal Register on December 31, and published in the Federal Register of January 5, 1981 (46 FR 891).

Summary of Evidentiary Positions of Parties

Music Publishers and Songwriters:

The Music Publishers and Songwriters presented cases that were complementary, the difference being that while the music publishers argued for the rate to be set at six percent of the suggested retail list price, the songwriters argued that it be set at eight percent. In support of their position the music publishers presented a study by Nathan Associates and the songwriters one by Rinfret Associates. Both parties relied upon the study of the other as well as their own during the course of the proceedings.

Music Publishers

The music publishers argued that the mechanical royalty should be raised to six percent of the suggested list price, or, as an alternative, that the flat rate be raised to 5 cents and adjusted annually for inflation by the Consumer Price Index. [FN1]

FN1 Proposed Findings of Fact and Conclusions of NMPA, Nov. 17, 1980, p. 186- 187.

A principal claim by the music publishers in arguing for such as increase, was that over the last decade the mechanical royalty has eroded while record company profits have increased. [FN2] In real purchasing terms the two cent statutory rate of 1909 had the equivalent in 1978 of 14.5 cents. [FN3] From January 1978 to February 1980, the period during which the current mechanical rate has been in effect, the Consumer Price Index increased more than 20% and record prices increased 10%, but the purchasing power of the 2 [FN34] cent rate declined 18%. [FN4] According to the music publishers, the historical effective mechanical royalty rate was six percent of the suggested list price and 8.5 percent of the actual price paid by consumers. [FN5] The benchmark the music publishers chose from which to begin historical comparison was 1948; this was when the L.P. was first introduced, and marked the beginning of the modern recorded music industry. [FN6] Starting in this period the price of an album stabilized at $3.98 and contained twelve songs; with a two cent mechanical rate the total royalty per record was 24 and therefore equalled six percent of the suggested list price. [FN7] If the excise tax which was imposed at the time is taken into consideration, the music publishers claimed, the royalty as a percentage of suggested list price was even higher. [FN8] This rate, according to the music publishers, remained in effect from 1948 to 1966, the period during which monaural L.P.'s were dominant [FN9] and during which the industry as a whole was stable. [FN10] It is since this period that the rate has eroded. [FN11] From 1965 until

the final revision of the Copyright Act, the mechanical royalty rate fell to little more than half its value, against a rise in the Consumer Price Index of 76%. [FN12] In order to maintain the value of the two cent 1965 royalty, the rate would have to be raised to 5.34 cents. [FN13] In the argument of the music publishers, the very least that should be done would be an adjustment of the rate to compensate for inflation since 1974, which was the last year Congress had financial data for when it established the current rate at 2 [FN34] cents. [FN14] Such a rate would be 4 cents, but because it would fail to take into account the erosion before 1974 the music publishers considered that it would still be unfair. [FN15] In addition to an erosion of the rate with respect to inflation, it has also eroded with respect to record prices and to all other costs record companies bear, the music publisher claimed. [FN16] The rate has effectively further decreased because of the reduction in the number of songs per album, from twelve in 1965 to ten in 1979. [FN17] And in comparison with the erosion of the value of the mechanical royalty, the royalties of recording artists appearing on the same records have substantially increased. [FN18] The result, according to the music publishers, has been that the compulsory license has enabled record companies to buy music at a rate that is unfairly cheap. [FN19]

FN2 Ibid, p. 25 and Nathan Study, pp. 27-28.

FN3 Ibid, p. 32 and Rinfret Study, Vol. 1, p. 27.

FN4 Ibid, p. 33 and Ibid, p. 35.

FN5 Proposed Findings of Fact and Conclusions of NMPA, Nov. 17, 1980, p. 119.

FN6 Ibid, p. 119.

FN7 Ibid, p. 119 and Post-Hearing Brief of NMPA, p. 2.

FN8 Ibid, p. 120.

FN9 Ibid, p. 120 and Post-Hearing Brief of NMPA, p. 9.

FN10 Post-Hearing Brief of NMPA, p. 12.

FN11 Proposed Findings of Fact and Conclusions of NMPA, p. 122.

FN12 Ibid, p. 124 and Post Hearing Brief, pp. 22 and 23.

FN13 Post-Hearing Brief of NMPA, p. 67.

FN14 Ibid, p. 68.

FN15 Proposed Findings of Fact and Conclusions of NMPA, p. 125.

FN16 Facts and Conclusions of NMPA, p. 167 and Post Hearing Brief, p. 14.

FN17 Facts and Conclusions of NMPA, p. 23.

FN18 Ibid, p. 127.

FN19 Ibid, p. 63.

As for the contention that the increase in record sales has compensated for the reduction in the effective royalty rate, the music publishers claimed that this is not true. [FN20] Increase in volume has only resulted in a slight increase in the number of songs available to the ***10468** public; [FN21] and compensation to the composer is not to be considered in the aggregate, but on a per-unit basis. [FN22] The music publishers also claimed that the increase in volume has been much smaller than the increase in record prices, [FN23] and smaller than the increase in inflation as measured by the CPI. [FN24] Record prices, not volume, in the music publisher' judgment, have been responsible for the profitability of the record industry. [FN25] It is on those albums that do achieve high volume that, in comparison with mechanical royalties, the record companies make their highest profits. [FN26] In Australia the Copyright Tribunal there determined that volume in sales did not compensate for inflation, [FN27] and the music publishers argued that the contention by the Francis Report in England that a lower royalty rate can to some degree be compensated for by volume does not apply to the United States because the rate in England is expressed as a percentage of retail price and can fluctuate on an individual basis with record prices. [FN28]

FN20 Ibid, p. 24 and 131 and Post Hearing Brief, p. 3 and 31.

FN21 Ibid, p. 24.

FN22 Ibid, p. 25.

FN23 Ibid, p. 25 and 134 and Post Hearing Brief, p. 31.

FN24 Ibid, p. 134.

FN25 Post Hearing Brief, p. 27.

FN26 Ibid, p. 29.

FN27 Facts and Conclusions of NMPA, p. 132.

FN28 Facts and Conclusions of NMPA, p. 132.

The music publishers considered that mechanical royalties abroad are an important point of comparison [FN29] and stressed that they are much higher than they are in the United States. [FN30] They are also expressed not as a flat rate, but as a percentage of price, [FN31] and in many countries are eight percent of retail list. [FN32] The position of the copyright owners is therefore much weaker here than it is abroad. [FN33] The music publishers disputed that higher rates in Europe are due to lower sales volume and pointed out that on a per capita basis volume in Europe is higher. [FN34] Furthermore, American records receiving the lower royalty in the United States receive the higher royalty in Europe, [FN35] and the reverse is true, European composers receiving less in the United States than they do for the same music in Europe. [FN36] The music publishers considered that it was inconsistent of the record companies to reject comparisons with practices abroad, because they rely

upon foreign practices themselves when arguing for performance royalties. [FN37]

FN29 Ibid, p. 129.

FN30 Ibid, p. 26.

FN31 Ibid, p. 26.

FN32 Post-Hearing Brief, p. 4 and 5.

FN33 Facts and Conclusions of NMPA, p. 128.

FN34 Post-Hearing Brief, p. 40.

FN35 Ibid, p. 43.

FN36 Ibid, p. 39.

FN37 Ibid, p. 37-38.

The music publishers claimed that under the current 2 [FN34] cent statutory rate the copyright owners are not able to negotiate in a fashion that reflects market values. [FN38] For negotiations to occur that will insure the proper function of the free market the statutory rate must be sufficiently high; [FN39] although it must also enable record companies to invoke the compulsory license if negotiations should fail. [FN40] Therefore, the music publishers argued that the rate should be set at the high end of the negotiating range. [FN41] The fact that little negotiation now take place confirms that even with the rate set under the 1976 Statute the ceiling is too low. [FN42] The record companies have no economic incentive to negotiate. [FN43] Moreover, record companies rarely invoke the compulsory license. [FN44] When the mechanical rate was equal to six percent in the past, bargaining did occur, and licenses were granted at a level below that set by statute. [FN45]

FN38 Facts and Conclusions of NMPA, p. 103.

FN39 Facts and Conclusions of NMPA, p. 103.

FN40 Ibid, p. 103.

FN41 Ibid, p. 103.

FN42 Ibid, p. 21.

FN43 Ibid, p. 104.

FN44 Ibid, p. 104.

FN45 Ibid, pp. 169-170.

The music publishers emphasized that the songwriter and his creative talents are basic to the record industry. [FN46] For the industry to have its few successful hits a large pool of songwriting talent must be available. [FN47] Nevertheless the

difficulties, particularly financial, of being a songwriter are great [FN48] especially in areas of special music like jazz. [FN49] Relying on the Rinfret study to demonstrate the hardship and risk associated with being a songwriter, [FN50] the music publishers argued that the object of any rate increase should be the modest songwriter, not those who will be wealthy under any circumstances. [FN51] Other than performance royalties, mechanical royalties provide the major share of songwriters' income. [FN52] Moreover, at issue is not what songwriters receive as a group, but what they receive individually. [FN53] And this must be viewed in light of the fact that other traditional sources of income such as print sales have diminished. [FN54]

FN46 Ibid, p. 52.

FN47 Ibid, p. 114.

FN48 Ibid, p. 56.

FN49 Ibid, p. 58.

FN50 Ibid, pp. 29-30.

FN51 Ibid, p. 59.

FN52 Ibid, p. 31.

FN53 Post-Hearing Brief, p. 27.

FN54 Facts and Conclusions of NMPA, p. 114.

The music publishers argued that the Tribunal should not take into account the phenomenon of the singer-songwriter. [FN55] The issue of just how widespread the phenomenon is, is in doubt, [FN56] but above all they are not subject to the compulsory license. [FN57] Their releases are principally recorded by themselves, [FN58] and the royalties are negotiated as a total package. [FN59] They can therefore compensate for lower mechanical royalties by receiving higher artist royalties. [FN60] Conversely, if the mechanical rate is increased, both the artist and the record company can negotiate lower artist royalties. [FN61] With singer-songwriters who own their own publishing companies, the issue is where they wish to retain their profits. [FN62] In the case of those who reported in the Praeger and Fenton survey, most chose to leave them with their publishing companies. [FN63] Furthermore, because artist royalties are used to recoup the costs of recording, the effect of lower mechanical royalties and higher artist royalties has been to shift the financial risk of production on to the singer-songwriter. [FN64] The music publishers felt that it was proof that singer-songwriters are not affected by the mechanical rate and should not be taken into consideration in that none appeared at the proceeding. [FN65] Finally it was suggested that as a phenomenon singer-songwriter may ultimately have a deleterious effect upon the development of music. [FN66]

FN55 Post-Hearing Brief, pp. 33 and 37.

FN56 Facts and Conclusions of NMPA, p. 60.

FN57 Post-Hearing Brief, pp. 4 and 35.

FN58 Ibid, p. 35 and Facts and Conclusions of NMPA, p. 61.

FN59 Post-Hearing Brief, p. 35.

FN60 Ibid, p. 35.

FN61 Ibid, p. 36.

FN62 Ibid, p. 34.

FN63 Ibid, p. 34.

FN64 Ibid, p. 36 and Facts and Conclusions of NMPA, p. 61.

FN65 Post-Hearing Brief, pp. 36 and 37.

FN66 Facts and Conclusions of NMPA, p. 61.

The music publishers considered that it was not the role of the Tribunal to evaluate the relationship between the songwriter and music publisher. [FN67] The relationship is a commercial one and freely negotiated on a free-market basis. [FN68] Nevertheless, music publishers argued that they play a significant role in the creation and dissemination of music [FN69] and that close collaboration exists between the publisher and ***10469** songwriter [FN70] both creatively and in promotion. [FN71]

FN67 Ibid, p. 147.

FN68 Ibid, p. 68.

FN69 Ibid, p. 74.

FN70 Ibid, pp. 148-150.

FN71 Ibid, pp. 69-73.

The music publishers considered that the question of their own profitability is irrelevant. [FN72] Congress did not intend it to be considered, [FN73] and it is not related to the reasonable return for a song. [FN74] Nevertheless, at the request of the Tribunal the music publisher submitted "Aggregate Data Concerning the Financial Condition of Music Publishers" prepared by Praeger and Fenton. [FN75] According to this data, traditional music publishers had a modest return on revenue of between 5.17 percent in 1977 and 8.46 percent in 1979. [FN76] Their financial success also depends heavily on revenues from foreign mechanicals. [FN77]

FN72 Ibid, p. 47.

FN73 Ibid, p. 47.

FN74 Ibid, p. 47.

FN75 Ibid, p. 136.

FN76 Post-Hearing Brief, pp. 4 and 32.

FN77 Ibid, p. 33.

The profits of the record industry, the music publishers argued, on the other hand, are relevant and have been substantial. [FN78] The prospects for the industry also continue to be strong in spite of 1979, when profits fell and which was an aberration [FN79] due to bad management. [FN80] Much fat exists in the industry [FN81] especially in sales, promotion, and general and administrative expenses. [FN82] And the record industry claims concerning the effect a royalty increase would have are exaggerated. [FN83] If the mechanical rate is increased to six percent of the suggested list price, at most the record companies would have to absorb or pass on 2.8 cents per song. [FN84] The music publishers also questioned the record companies' concern for the consumer. [FN85] Reductions in cost in the past have not been accompanied by a decrease in prices. [FN86] The repeal of the excise tax in 1965 [FN87] and the increase in the price of monaural albums through 1967 were cited as examples. [FN88] There is no difference between the increase in the mechanical rate and the increase of other costs. [FN89] Prices and other costs have risen in the past, while mechanicals have risen only slightly. [FN90] The rate of increase of all other record company costs from 1965-1980, according to the music publishers, was ten times as great as the increase in the mechanical royalty. [FN91]

FN78 Facts and Conclusions of NMPA, pp. 138 and 140.

FN79 Ibid, p. 23.

FN80 Ibid, pp. 23 and 144.

FN81 Post-Hearing Brief, p. 19.

FN82 Post-Hearing Brief, pp. 19 and 20.

FN83 Ibid, p. 52.

FN84 Ibid, p. 16.

FN85 Ibid, pp. 6 and 50.

FN86 Ibid, p. 52.

FN87 Ibid, p. 53.

FN88 Ibid, p. 54.

FN89 Ibid, p. 51.

FN90 Ibid, p. 90.

FN91 Facts and Conclusions of NMPA, p. 167.

The music publishers considered that a rise in the rate to six percent is fully consistent with the statutory criteria. The Tribunal above all must base its judgment on what is reasonable, [FN92] and, according to the music publishers, because the rate increase they propose is reasonable, it is therefore by definition consistent with the statutory criteria. [FN93]

FN92 Ibid, p. 102.

FN93 Ibid, p. 102.

As to the criteria specifically:

In the case of the first criteria, the music publishers argued that only an increase in the rate would provide sufficient economic incentive to maximize the availability of creative works to the public, [FN94] which the current 2 [FN34] cent rate does not do. [FN95] With respect to the second criteria, the music publishers argued that the chief concern in evaluating return must be fairness [FN96] and that only with a rate of six percent could the copyright owners achieve a fair return on the basis of rates for music elsewhere. [FN97] Also, insuring a fair return to copyright owners and a fair income to copyright users does not require profits to be balanced. [FN98] The request to raise the copyright mechanical royalty is not to be confused with the burden of proof requirements in utility rate cases. [FN99] The music publishers contended that because profitability is not related to a fair return to copyright owners, their own profitability is irrelevant. [FN100]

FN94 Ibid, p. 109.

FN95 Ibid, p. 111.

FN96 Ibid, pp. 116 and 117.

FN97 Post-Hearing Brief, p. 8.

FN98 Facts and Conclusions of NMPA, p. 116.

FN99 Ibid, p. 117.

FN100 Ibid, p. 135.

Concerning the third criteria, the relative roles of the copyright owner and the copyright user, the music publisher argued that in terms of risk and time the greatest cost is borne by the songwriter. [FN101] Furthermore, in the case of the singer-songwriter there is direct financial investment because artist royalties are used to recover recording costs. [FN102] Financial risk is also borne by the music publisher. [FN103] By increasing the rate new markets would be opened to music. [FN104]

FN101 Ibid, p. 155.

FN102 Ibid, p. 160 and Post-Hearing Brief, p. 36.

FN103 Ibid, pp. 156-157.

FN104 Ibid, pp. 162-3.

With respect to the fourth criteria, the music publishers contended that the record industry has absorbed cost increases in the past without suffering substantial disruption. [FN105] The Tribunal has the obligation to minimize disruptive impacts, but it is not required to avoid them altogether. [FN106] Neither the music publisher preferred proposal nor an increase in the flat rate with an annual CPI adjustment would have an impact that would be disruptive. [FN107] The industry could convert easily to a percentage system, [FN108] and such a system already exists with respect to artist royalties. [FN109] Furthermore, in acknowledging the need for an increase in their own proposal, the record industry has admitted that an increase per se would not be disruptive. [FN110]

FN105 Ibid, p. 166.

FN106 Post-Hearing Brief, p. 44.

FN107 Facts and Conclusions of NMPA, p. 171 and Post Hearing Brief, p. 49.

FN108 Facts and Conclusions of NMPA, p. 178

FN109 Ibid, p. 178.

FN110 Post-Hearing Brief, p. 60.

The music publishers considered that a rate based upon percentage is preferable to a flat rate with an annual inflationary adjustment, first of all, because a percentage rate does not lag behind the acutal change in inflation, [FN111] and, second, because the rate applies to records individually. [FN112] In terms of lower priced records it would be the record companies who would benefit. [FN113] The Tribunal is not limited in its authority to institute a percentage based method, [FN114] and such a rate would assist the government in extricating itself further from having to adjust the rates of compulsory licenses. [FN115] It would also insure that the rate would remain reasonable until the next rate review in 1987, [FN116] and the percentage system already exists with respect to recording artists. [FN117]

FN111 Facts and Conclusions, p. 28 and post Hearing Brief, p. 75.

FN112 Post Hearing Brief, p. 73.

FN113 Ibid, p. 73.

FN114 Ibid, p. 55-57 and Facts and Conclusions, p. 14-15.

FN115 Ibid, p. 58.

FN116 Facts and Conclusions, p. 186.

FN117 Post Hearing Brief, p. 45.

The most appropriate basis on which a percentage rate should be applied, according to the music publishers, is the suggested list price. [FN118] It is well-entrenched, [FN119] and changes in the royalty rate would be related to changes in price. [FN120] Also, the suggested list price will last because it must be maintained ***10470** for artist royalties. [FN121] A rate based upon a percentage of the suggested list price would be self-administering [FN122] and would relieve the Tribunal of any continuing burden as a monitor. [FN123]

FN118 Facts and Conclusions, p. 189.

FN119 Post Hearing Brief, p. 80.

FN120 Facts and Conclusions, p. 193-194.

FN121 Post Hearing Brief, p. 81.

FN122 Ibid, p. 78.

FN123 Ibid, p. 77.

According to the proposal submitted by the music publishers, the six percent royalty would be allocated on the basis of units of time. [FN124] Works under one minute would receive one-third unit; works between one and five minutes would receive one unit; and works over five minutes would receive one-fifth unit per minute of playing time or fraction of a minute. [FN125] The share of each work would be the number of units assigned to it divided by the number of units on the record assigned to all works. [FN126] This would be its fraction of six percent of the suggested list price. The only requirement would be that the industry maintain bona fide suggested list prices. [FN127] The music publishers foresaw only one difficulty in that the record companies might not maintain their royalty files completely accurately. [FN128] The music publishers expressed concern that the Tribunal's regulation apply to the date upon which phonorecords have been made and distributed, and not simply to the date upon which they have been released. [FN129]

FN124 Facts and Conclusions, p. 197-201.

FN125 Ibid, p. 198.

FN126 Ibid, p. 198 and 211.

FN127 Post Hearing Brief, p. 82.

FN128 Ibid, p. 48.

FN129 Ibid, p. 71.

As an alternative, although not preferred, to the percentage rate, the music publishers proposed that the flat rate should be raised to 5 cents, and then be adjusted annually for inflation according to the Consumer Price Index. [FN130] A five

cent flat rate would be approximately equivalent to six percent of current suggested list prices. And the CPI could serve as an adjustment mechanism because increases in the CPI have paralleled increases in record prices. [FN131] The adjustment procedure would consist only of an annual announcement by the Tribunal, a practice it has already followed. [FN132] The strength of the CPI is that it is the most widely used basis for adjustments for inflation. [FN133] The music publishers felt that the record industry destroyed the basis for its argument against the use of the CPI, because in its original objection the record industry opposed, not just the CPI, but any index for inflation, and yet later in its own proposal did introduce an inflationary index. [FN134]

FN130 Facts and Conclusions, p. 202-203.

FN131 Ibid., p. 207.

FN132 Post Hearing Brief, p. 83.

FN133 Facts and Conclusions, p. 209.

FN134 Post Hearing Brief, p. 56.

Songwriters

The arguments of the songwriters were those of the music publishers. The mechanical royalty rate is too low. [FN135] As a percentage of suggested list price it has declined from over 8% in the 1940's and 6% in the 1950's and early 60's to a level that presently is 3.1%. [FN136] In comparison with artist royalties, mechanical royalties are disproportionately low. [FN137] There has been great erosion due to inflation, [FN138] which has been aggravated further by the decrease in the number of songs per album. [FN139] Contrary to the claim by the record industry, the erosion in the rate has not been compensated for by the increase in the volume of sales. [FN140]

FN135 Post-Hearing Brief of American Guild of Authors and Composers and Nashville Songwriters Association International, Nov. 17, 1980, p. 7 and 18.

FN136 Ibid, p. 32.

FN137 Ibid, p. 22.

FN138 Ibid, p. 2 and 29.

FN139 Ibid, p. 37.

FN140 Ibid, p. 29.

The mechanical rate in Japan and most European countries is double that in the United States, [FN141] and on a per capita basis in several European countries volume of sales is higher. [FN142] This discrepancy is due to the fact that in the United States the royalty rate is fixed while abroad it is a percentage of price and therefore can fluctuate. [FN143]

FN141 Ibid, p. 27.

FN142 Ibid, p. 28.

FN143 Ibid, p. 28 and 29.

The current level of the royalty rate has eliminated bargaining. [FN144] The songwriters argued that the decline in bargaining has accompanied the decline in the statutory ceiling as a percentage of record prices [FN145] and has been caused by inflation. [FN146] Bargaining would allow the copyright owner a fair return, [FN147] and the royalty rate should be set to encourage it, [FN148] therefore at the high end of the negotiating range. [FN149] The proof that little bargaining now exists is that licensing is organized for administrative convenience. [FN150] Recording artists, on the other hand, are free to bargain, [FN151] as are singer-songwriters and their controlled publishers. [FN152]

FN144 Ibid, p. 2.

FN145 Ibid, p. 40.

FN146 Ibid, p. 41.

FN147 Ibid, p. 18.

FN148 Ibid, p. 2.

FN149 Ibid, p. 14 and 73.

FN150 Ibid, p. 45.

FN151 Ibid, p. 23.

FN152 Ibid, p. 56-57.

In comparison with the income of artists, the income of songwriters is small, [FN153] and income from other sources such as print sales should not be considered because it is outside the bounds of the mechanical royalty. [FN154]

FN153 Ibid, p. 25.

FN154 Ibid, p. 21.

The singer-songwriter is not relevant to the proceeding. [FN155] Their compensation, as well as that of the singer-songwriter-controlled publisher, is the result of free negotiation. [FN156]

FN155 Ibid, p. 4.

FN156 Ibid, p. 53 and 54.

Publishers' profits are equally irrelevant, [FN157] in that the publisher is the assignee of the songwriter, [FN158] and the relation between them are determined by

free negotiation, [FN159] which is shown by the fact that the split has evolved over the years in favor of the songwriter. [FN160]

FN157 Ibid, p. 3.

FN158 Ibid, p. 51.

FN159 Ibid, p. 52.

FN160 Ibid, p. 52.

An increase in the mechanical rate will not have the serious effects the industry claims; in 1978 the mechanical increased and there were none. [FN161] The effects of the 1979 recession are past. [FN162] In comparison with other costs, mechanical royalties are trivial. [FN163] An increase will not have the effect upon the consumer the industry claims. [FN164] It can be counterbalanced by the reduction of other expenses, such as general and administrative costs, and these are already swollen and would not increase automatically with an increase in the mechanical anyway. [FN165] Retailers would not necessarily have to include any increase in the mechanical in their percentage markups. [FN166] Their flexibility in this regard is already proved by the existence of discounting. [FN167] Price increases have taken place in the past, and they have not been due to an increase in the mechanical. [FN168]

FN161 Ibid, p. 12 and 74.

FN162 Ibid, p. 52.

FN163 Ibid, p. 5 and 73.

FN164 Ibid, p. 77.

FN165 Ibid, p. 77.

FN166 Ibid, p. 79.

FN167 Ibid, p. 80.

FN168 Ibid, p. 78.

The claims of financial woe on the part of the recording industry, according to the songwriters, are not justified. [FN169] The figures submitted by the industry do not reflect profits accurately. [FN170] There is no reliable profit information available, [FN171] and industry revenues have not been matched to industry ***10471** costs. [FN172] The picture is further clouded, the songwriters contended, by the tax advantages of leaving profits in foreign subsidiaries. [FN173] The songwriters questioned the industry's breakeven analysis, especially as it applied to small companies. [FN174]

FN169 Ibid, p. 5.

FN170 Ibid, p. 62.

FN171 Ibid, p. 58.

FN172 Ibid, p. 64 and 69.

FN173 Ibid, p. 66.

FN174 Ibid, p. 81.

In order to satisfy the first statutory criterion and encourage the development of the necessary pool of creative musical talent there must be an increase in the rate. [FN175] The reduction of the number of good tunes that has occurred can be attributed to its current low level. [FN176] The songwriters considered that the most important criterion is the one requiring the Tribunal to afford the copyright owner a fair return. [FN177] The songwriters felt that as for affording the copyright user a fair income there was no guidance, [FN178] especially since in comparison with other costs the mechanical royalty is insignificant. [FN179] Only a rate that is high enough to produce bargaining will reflect adequately the relative roles of the copyright owner and copyright user. [FN180] In respect to such elements as investment and risk the relative roles cancel each other out. [FN181] The Tribunal should minimize disruptive impacts, but it should not avoid all impact whatsoever if fair return is at stake. [FN182]

FN175 Ibid, p. 9.

FN176 Ibid, p. 44.

FN177 Ibid, p. 13.

FN178 Ibid, p. 57.

FN179 Ibid, p. 57.

FN180 Ibid, p. 86.

FN181 Ibid, p. 88.

FN182 Ibid, p. 88.

The rate should be set as a percentage of suggested retail list price. [FN183] The administrative problems are not that great [FN184] and artist royalties are currently already calculated in that fashion. [FN185] The best base for any percentage rate is the suggested retail list price. [FN186] In its absence, the Tribunal should adopt an adjustment for the cost of living. [FN187]

FN183 Ibid, p. 90.

FN184 Ibid, p. 91.

FN185 Ibid, p. 94.

FN186 Ibid, p. 32 and 33.

FN187 Ibid, p. 95.

According to the songwriters, the percentage of the suggested retail list price should be set at 8%. [FN188] This would return the rate to the level that existed in the 1940's when bargaining was common, [FN189] and a 6% rate would not achieve this. [FN190] An 8% rate would approach the range at which royalties are paid in Europe but would still not achieve it. [FN191]

FN188 Ibid, p. 48.

FN189 Ibid, p. 48.

FN190 Ibid, p. 59.

FN191 Ibid, p. 51.

Recording Industry

The recording industry argued that no increase in the rate was appropriate now. [FN192] In retaining the compulsory license and creating the Tribunal, [FN193] Congress intended for the Tribunal, not the marketplace, to set the rate, [FN194] and in doing so, the Tribunal must adhere to the statutory criteria. [FN195] According to these criteria no increase is presently justified. [FN196] The compulsory license itself maximize the availability of creative works to the public. [FN197]

FN192 Proposed Findings of Fact and Conclusions of Law of the Recording Industry Association of America, Nov. 17, 1980, p. 6.

FN193 Ibid, p. 193.

FN194 Ibid, p. 190-191 and Summary of Proposed Findings of Fact and Conclusions of Law of the Recording Industry of America, Nov. 17, 1980, p. 35.

FN195 Summary, p. 1

FN196 Findings, p. 293.

FN197 Ibid., p. 175 and CBS Inc. Findings of Fact, p. 4-7.

According to the recording industry, copyright owners are already doing extremely well under the current rate [FN198] and, including the traditional publishers, are doing better than copyright users. [FN199] Singer-songwriters who receive 50% to 60% of all mechanical royalties, [FN200] dominate the industry, [FN201] and non-singer-songwriters, but composers who are successful are also doing well. [FN202] The recording industry argued that the Tribunal must consider "fair return" in terms of fair profit [FN203] and considered that the studies submitted by both the songwriters and the music publishers were lacking as a basis on which to do so because they did not fully report all income. [FN204]

FN198 Summary, p. 3 and Findings, p. 41.

FN199 Summary, p. 16.

FN200 Findings, p. 10.

FN201 Ibid, p. 7.

FN202 Ibid, p. 27.

FN203 Ibid, p. 27.

FN204 Ibid, pp. 35 and 81-89.

According to the recording industry, mechanicals on a per-tune basis have increased twice as fast as inflation [FN205] and when taken in the aggregate have kept pace with, or exceeded, inflation in every year for which the recording industry has data. [FN206] The recording industry stressed that in the Francis Report in England the importance of sales volume was recognized in the consideration of an equitable royalty rate. [FN207] According to the recording industry, the issue is income, not the royalty rate in the abstract. [FN208] As a result, it is necessary to consider all income related to the recording of a song, such as performance rights, synchronization, and print sales, [FN209] because the recording of a song is what its earning power is dependent upon. [FN210] These sources of income have increased and between 1974 and 1979 outpaced inflation. [FN211]

FN205 Summary, p. 6 and Findings, p. 16.

FN206 Findings, p. 14 and Summary, p. 6.

FN207 Findings, p. 26.

FN208 Ibid, p. 25.

FN209 Ibid, pp. 20 and 24.

FN210 Ibid, p. 21.

FN211 Ibid, p. 18.

The recording industry stressed that any examination of the financial situation of the copyright owners must take into account the fact that mechanical royalties are concentrated in the hands of a few [FN212] and argued also that in the arts skewed income distribution is to be expected. [FN213] The recording industry considered that the incomes of successful composers are both good [FN214] and higher than those of the general populations. [FN215] The Tribunal should not consider the income of poor songwriters, the industry argued, [FN216] and criticized the survey submitted by the songwriters as too biased towards them, [FN217] because no matter how much the royalty rate is increased the poor songwriter will not be helped. [FN218] The difficulty affecting the poor songwriter is the fact that his songs don't sell, not the royalty rate. [FN219] Those who would benefit most from an increase are the

singer-songwriter [FN220] and they are already thriving. [FN221]

FN212 Ibid, p. 10.

FN213 Ibid, p. 38.

FN214 Summary, p. 12.

FN215 Ibid, p. 13.

FN216 Findings, p. 30.

FN217 Ibid, pp. 31 and 32.

FN218 Summary, p. 13.

FN219 Findings, p. 39.

FN220 Ibid, p. 158.

FN221 Summary, p. 4.

The recording industry considered also that music publishers are very profitable, [FN222] even when they serve only as administrators for singer-songwriters. [FN223] Their income has kept pace with inflation, [FN224] and the health of the industry is shown by their own survey. [FN225] This is true not only for controlled publishers but also for traditional publishers as well. [FN226] The recording industry suggested that the usual split between the songwriter and the publisher should therefore be reexamined. [FN227] The recording industry argued that under the statutory criteria ***10472** it is the music publishers' profitability that the Tribunal must consider. [FN228] An increase in the mechanical would only provide them unearned windfall profits. [FN229] Comparing incomes from 1974 to 1979, [FN230] music publishing has been more profitable than the recording industry. [FN231] The profits of even traditional publishers have increased while recording industry profits have declined. [FN232] The recording industry argued that this comparison of profitability was one the Tribunal must take into consideration under the second criterion. [FN233] Music publishers earned money regardless of whether or not the record company losses [FN234] or breaks even [FN235] and, continues to earn over a long period of time without any additional effort. [FN236]

FN222 Findings, p. 41 and Summary, p. 4.

FN223 Findings, p. 13.

FN224 Ibid, p. 42.

FN225 Summary, p. 11.

FN226 Findings, pp. 11 and 12; and Summary, p. 6.

FN227 Findings, p. 40.

FN228 Ibid, p. 27.

FN229 Ibid, p. 159.

FN230 Ibid, p. 76.

FN231 Ibid, pp. 72 and 79.

FN232 Ibid, p. 73.

FN233 Findings, p. 70.

FN234 Ibid, p. 135.

FN235 Summary, p. 22.

FN236 Findings, p. 136.

The reliability of the financial data submitted by the music publishers was brought into question by the recording industry, [FN237] in particular concerning the small amount of royalties distributed to controlled publishers. [FN238] The recording industry argued that because income from foreign sources has become increasingly important to music publishers, [FN239] if record companies must account for foreign license income, music publishers must also account for the foreign mechanical income from those same masters. [FN240]

FN237 Ibid, pp. 81-89.

FN238 Ibid, p. 90.

FN239 Ibid, p. 20.

FN240 Ibid, p. 44.

According to the recording industry, the songwriter continues to make a significant contribution, but the role of the music publisher has declined, [FN241] and this has been caused by the growing importance of the singer-songwriter [FN242] and the controlled publisher. [FN243] Today, publishers are simply administrators, [FN244] have minimal costs, [FN245] and leave the promotion of a song up to the record company. [FN246] Publishers rarely give advances to artists according to the recording industry, [FN247] or spend significant sums to make music available to the public. [FN248] They therefore no longer fill their original role as discoverers of new talent. [FN249] Music publishers bear little risk, [FN250] and the relationship of their risk to their return is out of balance. [FN251] Their investment is minimal, [FN252] and the investment as well as risk even of artists is greater because they at least recover recording costs with their royalties. [FN253]

FN241 Ibid, p. 101.

FN242 Ibid, p. 103.

FN243 Ibid, p. 111.

FN244 Findings, p. 110 and Summary p. 21.

FN245 Findings, p. 125.

FN246 Ibid, pp. 104-107 and 124.

FN247 Ibid, p. 124.

FN248 Ibid, p. 123.

FN249 Summary, p. 20.

FN250 Findings, pp. 134 and 136.

FN251 Ibid, p. 137.

FN252 Ibid, p. 139.

FN253 Ibid, p. 135.

On the other hand, the recording industry fails to receive a fair income. [FN254] Its pre-tax return has been below that of the Fortune 500, [FN255] and its profitability has declined. [FN256] The recording industry presented a study by the Cambridge Research Institute upon which to base its judgment about the industry, [FN257] and the respondents to the study represent approximately 60% to 70% of domestic sales. [FN258] In the view of the recording industry the study, if anything, overstates industry profits. [FN259]

FN254 Ibid, p. 43.

FN255 Ibid, pp. 46-47.

FN256 Ibid, p. 45.

FN257 Ibid, p. 91.

FN258 Ibid, pp. 92-94.

FN259 Ibid, p. 94.

The recording industry considered that it was important to take into account the year 1979 because it was a year in which the industry suffered severe losses. [FN260] These were due to spiraling costs, [FN261] large volumes of returns, [FN262] consumer price resistance, [FN263] the reduction in the number of albums sold per customer, [FN264] sensitivity to price distributors as well as by customers, [FN265] and privacy, counterfeiting, and home taping. [FN266] The losses were not due to bad management. [FN267] The heavy expenditures on sales that occurred was a decision that was based on experience, [FN268] and it is always a gamble. [FN269] In many instances the expenditures were demanded by the artists themselves. [FN270]

FN260 Ibid, p. 43.

FN261 Ibid, p. 47.

FN262 Ibid, pp. 47-48.

FN263 Ibid, p. 48.

FN264 Ibid, p. 50.

FN265 Ibid, p. 50.

FN266 Ibid, p. 51.

FN267 Ibid, p. 56.

FN268 Ibid, p. 57.

FN269 Ibid, p. 57.

FN270 Ibid, p. 58.

The significance of 1979 was that it caused the industry to institute many changes which altered its character. [FN271] Costs were cut, [FN272] employees laid off, [FN273] artist roster and new signings reduced, [FN274] stricter policies adopted with regard to distributors and retailers, [FN275] the number of releases cut, [FN276] and prices lowered. [FN277] Measures to combat counterfeiting were considered, but were found to be too costly. [FN278] Artists agreed to accept lower royalties, [FN279] but music publishers were not approached to do so because on the basis of its experience the recording industry did not expect the music publishers to agree. [FN280] The present is a period of transition according to the recording industry, [FN281] and the industry stressed the significance of the structural changes that have occurred. [FN282]

FN271 Findings, p. 59 and Summary p. 15.

FN272 Findings, pp. 59 and 64.

FN273 Ibid, p. 60.

FN274 Ibid, p. 60.

FN275 Ibid, p. 61.

FN276 Ibid, pp. 64-69.

FN277 Ibid, p. 65.

FN278 Ibid, p. 64.

FN279 Ibid, p. 66.

FN280 Ibid, p. 67.

FN281 Ibid, p. 67.

FN282 Ibid, p. 53.

Against this background the recording industry argued that in comparison with the copyright owner its role has expanded. [FN283] The third statutory criterion requires that the relative contributions of the copyright owners and copyright user be compared, and the recording industry presented evidence to show its contribution is greater. [FN284] Its role is vital in finding and producing talent, [FN285] and continued to remain important in spite of the rise of the independent producer. [FN286] Record companies develop artists' careers, [FN287] introduce new technology, [FN288] L.P.'s, stereo, tapes, [FN289] reduce manufacturing costs, [FN290] and bear the risk if new technologies don't succeed. [FN291] Recording companies make substantial capital investment, [FN292] bearing most costs, [FN293] and these costs have risen faster than inflation. [FN294] The risk borne by the recording industry [FN295] can be measured by the fluctuation in profit levels, [FN296] the volatility of returns, [FN297] the ***10473** wide variation in recording costs, [FN298] and the number of firms leaving the industry. [FN299] The riskiness of demand is increased because of the dependence for success upon a few albums, [FN300] eighty percent (80%) of which don't break even. [FN301] Finally the recording industry claimed that it bears the responsibility for opening new markets. [FN302]

FN283 Summary, p. 21.

FN284 Findings, p. 149.

FN285 Ibid, p. 97.

FN286 Ibid, p. 99.

FN287 Ibid, p. 100.

FN288 Ibid, p. 140.

FN289 Ibid, p. 141-142.

FN290 Ibid, p. 143.

FN291 Ibid, p. 144.

FN292 Ibid, p. 137-140.

FN293 Ibid, p. 111-118.

FN294 Ibid, p. 121.

FN295 Ibid, p. 126.

FN296 Ibid, p. 127.

FN297 Ibid, p. 127.

FN298 Ibid, p. 127.

FN299 Ibid, p. 128.

FN300 Ibid, p. 130-131.

FN301 Ibid, p. 95, 96, and 131.

FN302 Ibid, p. 146.

The recording industry argued that the mechanical royalty rate should not be changed because copyright owners are already earning a fair return, [FN303] and the criteria under the statute are already satisfied. [FN304] The current rate, according to the recording industry, maximizes the availability of creative works to the public. [FN305] An increase in the rate would reduce this availability [FN306] because it would cause the consumer to pay more, and the copyright owners would be those harmed. [FN307] According to the recording industry, there is already an imbalance between the supply and demand of tunes, [FN308] with the registration of tunes increasing [FN309] and the number of releases declining. [FN310] No evidence exists that the number of tunes will increase if the rate is increased, [FN311] but an increase in their price will reduce therecording industry's demand for them. [FN312] Artist rosters would be reduced [FN313] and only those artists would be released who are already proven. [FN314] The most hurt would be smaller companies [FN315] and specialized music such as jazz. [FN316] The industry claimed that its marketing strategy would be jeopardized. [FN317] An increase in the mechanical rate, according to the recording industry, would therefore reduce the availability of creative works, [FN318] and from the standpoint of fair return, an increase in the rate would increase music publishers' profits without their being any economic need shown. [FN319]

FN303 Ibid, p. 6 and 80.

FN304 Ibid, p. 293.

FN305 Summary, p. 25.

FN306 Findings, p. 161-167.

FN307 Ibid, p. 157.

FN308 Ibid, p. 174.

FN309 Ibid, p. 177 and 179.

FN310 Summary, p. 26.

FN311 Findings, p. 179.

FN312 Ibid, p. 180-181.

FN313 Ibid, p. 181.

FN314 Ibid, p. 182.

FN315 Ibid, p. 184.

FN316 Ibid, p. 183.

FN317 Summary, p. 32.

FN318 Findings, p. 182.

FN319 Ibid, p. 158-159 and CBS Findings, p. 22.

The recording industry claimed that an increase in the rate on the order of that proposed by the music publishers would produce a staggering impact and cost upon the industry. [FN320] Cost increases have been supported in the past, but not of such a sudden magnitude. [FN321] Volume would drop, [FN322] and there would be a reduction in the number of releases. [FN323] The increase could not be financed out of G & A expense, the industry claimed, [FN324] manufacturing costs, [FN325] or by negotiating reductions in artist royalties. [FN326] The artist rather than bargain could go elsewhere. [FN327] Higher prices would further stimulate piracy. [FN328] According to the recording industry the cost could be as much as .83 cent per album, [FN329] and the consumers pay $335 million per year. [FN330] There would also result a successive series of price rises. [FN331] Finally, the industry argued that as for the impact of an increase being lessened by bargaining this would not occur. [FN332]

FN320 Ibid, p. 150 and Summary, p. 27.

FN321 Findings, p. 151.

FN322 Ibid, p. 152.

FN323 Summary, p. 28.

FN324 Findings, p. 153.

FN325 Ibid, p. 154.

FN326 Ibid, p. 154.

FN327 Ibid, p. 155.

FN328 Ibid, p. 156.

FN329 Ibid, p. 167.

FN330 Ibid, p. 170.

FN331 Ibid, p. 171.

FN332 Ibid, pp. 206-208.

The industry also opposed the concept that the mechanical rate should be set high enough so that it would encourage bargaining. [FN333] The rate must be reasonable in order to meet the criteria, and if it is high enough to encourage bargaining, by definition it would be unreasonable. [FN334] The recording industry argued that bargaining would still not occur even if the rate were increased. [FN335] It does not occur on first releases now [FN336] and the full rate is paid in the schlock market. [FN337] The large majority of licenses are at the statutory rate the recording industry claimed, [FN338] and language in licenses specifying the statutory rate has already been incorporated in them. [FN339] In the past, rate reductions have been refused by music publishers, [FN340] and it is to the statutory rate that the contracts of singer-songwriters are tied. [FN341] When the rate went up to 2 [FN34] cents, that was what the rate became. [FN342] The recording industry claimed that administratively tune-by-tune bargaining is impossible, [FN343] and from the publishers' point of view makes no sense. [FN344] The recording industry has no bargaining power because licenses traditionally are requested after a recording has already been made, [FN345] and composing often takes place in the studio. [FN346] It has been the Harry Fox Agency itself which has perpetuated the practice of not licensing until after a recording has been made. [FN347] According to the recording industry bargaining on a tune-by-tune basis doesn't occur anywhere in the world. [FN348]

FN333 Ibid, p. 190.

FN334 Ibid, pp. 190-191 and Summary, p. 36.

FN335 Ibid, p. 194 and Ibid, p. 36.

FN336 Findings, 195.

FN337 Ibid, p. 196.

FN338 Ibid, p. 197.

FN339 Ibid, p. 198.

FN340 Ibid, p. 157.

FN341 Ibid, p. 198.

FN342 Summary, p. 38.

FN343 Findings, p. 200.

FN344 Ibid, p. 202.

FN345 Ibid, p. 203.

FN346 Ibid, p. 204.

FN347 Ibid, p. 205.

FN348 Ibid, p. 202.

The recording industry argued that a historically effective rate has never existed. [FN349] Rates today, according to the recording industry, range from 3.7% to 4.6% of suggested list price, [FN350] and during the period 1955- 1966 were approximately 4.6% to 5.2%, at no time reaching 6%. [FN351] As a percentage the rate has been further clouded by discounting. [FN352] The period 1955-1966 which, according to the recording industry, the publishers used on which to lose their historical comparisons bears no relationship with the industry today. [FN353]

FN349 Ibid, p. 209 and Summary, p. 39.

FN350 Findings, p. 210.

FN351 Ibid, pp. 212-213.

FN352 Ibid, p. 211.

FN353 Ibid, p. 213 and CBS Findings, p. 37.

The recording industry objected to the songwriters' proposal to increase the rate to 8% on the grounds that there is no basis for it. [FN354] The true incidence of the Biem rate in Europe is not 8% [FN355] but, according to the recording industry, significantly less. [FN356] The recording industry objected further on the grounds that no study was made of the impact such a rate would have. [FN357]

FN354 Ibid, p. 186 and Summary p. 33.

FN355 Findings, p. 187.

FN356 Ibid, pp. 187-188.

FN357 Ibid, p. 189.

The recording industry opposed changing the mechanical rate to a percentage. [FN358] First of all, because there is the question as to the Tribunal's authority to do so, [FN359] and second, because, a percentage rate would violate the statutory criteria. [FN360] A ***10474** percentage rate would disrupt the industry and be unpredictable. [FN361] Royalty costs could not be predicted, [FN362] and the rate would be inflationary because royalties would be related to costs that are unrelated. [FN363] To the extent the impact would be disruptive technological innovations would be discouraged. [FN364] The cost to implement and administer would be great, [FN365] involving new computer systems and increased input data; [FN366] and all of these costs would have to be borne by the recording industry. [FN367] the impact would be particularly great on small companies. [FN368] The old flat rate would continue to exist with the new percentage rate, and therefore two systems would have to be maintained simultaneously. [FN369]

FN358 Ibid, p. 217 and CBS Findings, pp. 9-12.

FN359 Ibid, p. 258 and Summary, p. 48, and CBS Findings, pp. 9-12.

FN360 Findings, p. 217.

FN361 Ibid, pp. 217-218.

FN362 Ibid, p. 220.

FN363 Ibid, p. 221.

FN364 Ibid, p. 223.

FN365 Ibid, pp. 227-245.

FN366 Ibid, pp. 229-230.

FN367 Ibid, p. 245.

FN368 Ibid, p. 242.

FN369 Ibid, p. 243.

The recording industry argued that there is no comparison between a percentage rate for mechanicals and the practice of calculating artist royalties as a percentage.

FN370 Ibid, p. 224.

FN371 Ibid, p. 224.

FN372 Ibid, p. 224-225.

FN373 Ibid, p. 225.

FN374 Ibid, p. 225.

FN375 Ibid, p. 244.

FN376 Ibid, p. 245.

The recording industry claimed that there is no relationship between the percentage rate proposed by the music publishers and practices in Europe. [FN377] European mechanical royalties on a given record are not divided according to the time on that record a tune occupies, [FN378] and in Europe the cost of administering the mechanical royalty system is born by the copyright owners. [FN379] Complications have also arisen in establishing a base upon which the percentage can be calculated, [FN380] and a flat rate system is currently being contemplated. [FN381] The recording industry denied that there was any contradiction in its opposing a percentage mechanical royalty and at the same time advocating performance rights, in that the impact upon the American recording industry of introducing percentage mechanical royalty is dissimilar from that which would result if performance rights were adopted. [FN382]

FN377 Ibid, p. 220.

FN378 Ibid, p. 220.

FN379 Ibid, p. 248.

FN380 Ibid, p. 252.

FN381 Ibid, p. 248.

FN382 Ibid, p. 226.

The recording industry argued that the suggested list price would not be practical as a base. [FN383] The increase of discounting and the issues raised concerning its legality cause it to be questionable that the suggested list price will still be in existence in 1987. [FN384] According to the recording industry, wholesale prices would not serve as an alternative substitute. [FN385] They vary between and within companies, and they change frequently. [FN386] Because of the difficulty of determining what actual selling prices are, they also would not be a substitute. [FN387]

FN383 Ibid, p. 252.

FN384 Ibid, p. 252.

FN385 Ibid, p. 254.

FN386 Ibid, p. 254-255.

FN387 Ibid, p. 257.

The recording industry opposed equally adjusting the mechanical royalty rate according to the Consumer Price Index, [FN388] because changes in record prices were considered the fairest basis for any adjustment, not the CPI. [FN389] No relationship exists between the CPI and record prices [FN390] and with a cost of living adjustment no consideration would be given to the benefit to copyright owners of sales volume. [FN391] As a result, with a cost of living adjustment, the increase of mechanicals in the aggregate would be faster than inflation. [FN392] An increase in prices would be caused [FN393] and this in turn would hamper industry growth. [FN394] The recording industry questioned whether the CPI was an accurate measure of inflation, [FN395] and argued finally that there is no relationship between it and the statutory criteria. [FN396]

FN388 Ibid, p. 264.

FN389 Ibid, p. 264.

FN390 Ibid, p. 265.

FN391 Ibid, p. 266.

FN392 Ibid, p. 269.

FN393 Ibid, p. 269.

FN394 Ibid, p. 270.

FN395 Ibid, p. 272.

FN396 Ibid, p. 273.

Because the recording industry acknowledged that incertainties do exist concerning the future and inflation, a proposal was presented which was intended to meet these concerns. [FN397] Under it, no change at present would take place with the current rate, but subsequent adjustments would occur in 1982 and 1985, [FN398] proportional to the change in the average suggested list price of leading albums since 1980. The average price would be computed on the basis of the prices appearing during the year in Billboard, Record World, and Cashbox, and any disputes concerning the calculations would be resolved by a mutually acceptable public accountant. [FN399] In the event suggested list prices are eliminated, other adjustments would be calculated on the basis of changes in average wholesale prices. [FN400] The strength of this proposal, in the recording industry's judgments, was that, while not changing the current rate, it allowed for adjustments for inflation in the future. [FN401] Also, adjustments would be linked, not to an external index, but to one that reflects the condition of the industry. [FN402] The flat rate would be retained. [FN403] The system would be self-executing. [FN404] And no unlawful delegation of the Tribunal's authority, in the judgment of the recording industry would occur. [FN405] The recording industry considered that, as the year of the Tribunal's initial determination, the most appropriate base year was 1980. [FN406] The lag in adjustment between the years would be compensated by sales volume. [FN407]

FN397 Ibid, p. 274.

FN398 Ibid, p. 274.

FN399 Ibid, p. 275.

FN400 Ibid, p. 276.

FN401 Ibid, p. 276.

FN402 Ibid, p. 277.

FN403 Ibid, p. 281.

FN404 Ibid, p. 279.

FN405 Ibid, p. 284.

FN406 Ibid, p. 287.

FN407 Summary, p. 61.

Economic Submissions of the Parties

Introduction

During the course of the mechanical royalty proceedings certain financial evidence was submitted by the parties. The evidence included six studies. The songwriters through AGAC and NSAI presented a study from Rinfret Associates, Inc., an economic consulting firm. The publishers presented studies by Robert Nathan Associates, an economic consulting firm and Praeger & Fenton, a certified public accounting firm. The RIAA representing the recording industry submitted a study of financial and operating performance. The Study was conducted by the Cambridge Research Institute, a management and economic research ***10475** firm for the RIAA. The RIAA also submitted a study of Average Retail Prices of L.P.'s Tapes, and Singles, and a study of Album Content and Tune Length.

Songwriters (AGAC and NSAI)

Rinfret Study

The Study by Rinfret Associates, Inc. (Rinfret Study) recommended an immediate upward adjustment of the statutory rate to at least eight percent of the suggested retail list price of phonorecords. [FN408] The study rejected expressing the mechanical royalty as a flat cent rate, concluding that such rate is and would be unable to maintain its purchasing power under inflationary pressure. [FN409]

FN408 Rinfret Study, vol. 1, pp. 37-38.

FN409 Ibid, vol. 1, p. 35.

The Rinfret Study was based on economic data relating to inflation from 1909 to the present and on a survey of income data provided for the period 1974-1979 by 1017 songwriters in response to a questionnaire distributed to AGAC and NSAI members. Rinfret Associates conducted the survey in accordance with the Tribunal's Rules of Procedure. The underlying questionnaire responses were subsequently made available to counsel and the Tribunal for review. The questionnaire sought information with respect to the following categories: creative production of works; publishing history; recording history; recording sales success; songwriting income flow; songwriter publishing ownership interest; songwriter mechanical royalty share; sources of music related and other income; inflation protection; insurance benefits; and retirement provisions. [FN410]

FN410 Rinfret Study, vol. 1, pp. 4-5.

According to the study, in 1979 about 73 percent of the respondents received $11,500 or less from music related sources of income, while 47.5 percent of respondents received up to $11,500 total income from music and non-music related sources. [FN411] Only 20 percent of the respondents claim to be able to support themselves as full-time songwriters, and 59 percent describe their income from songwriting as "completely unpredictable." [FN412]

FN411 Ibid, vol. 1, pp. 11-13.

FN412 Ibid, vol. 1, pp. 6, 10, 15.

The Rinfret Study reports that the historical split of mechanical royalties among copyright owners has increased in favor of the songwriter's share. About 21 percent of respondents have complete ownership rights to the royalties generated by their copyrights; another 16 percent of respondents have more than a 50 percent interest. [FN413]

FN413 Ibid, vol. 1, p. 10.

The Rinfret Study shows that in real purchasing terms, the two cent statutory rate in 1909 had the equivalence of 14.5 cents of purchasing power in 1978 dollars based on the Consumer's Price Index. [FN414] The study also indicated that the 2 [FN34] cent interim rate has also seriously eroded under inflationary pressure. In the period January 1978 (the effective date of the interim increase) to February 1980, the Consumer Price Index increased more than 20 percent; record and tape prices increased more than 10 percent; and the purchasing power of the price-fixed mechanical royalty decreased 18 percent. [FN415]

FN414 Ibid, vol. 1, p. 27.

FN415 Ibid, vol. 1, p. 35.

The Rinfret Study contains data which show that while record companies are able to raise prices during periods of inflation, songwriters receive an ever-decreasing rate of return for their creative efforts. [FN416]

FN416 Rinfret Study, vol. 1, pp. 22-34.

The study recognizes that indexing a flat cent rate to changes in the cost of living would maintain some of the purchasing power of the intended adjustment. However, it regards the use of an index as less equitable than expressing the rate payable as a percentage of price. Under a cost-of-living adjustment, increases in the rate will always lag behind actual increases in inflation, thus perpetuating a built-in inequity. [FN417]

FN417 Ibid, vol. 1, p. 38.

The Rinfret Study concluded that data currently available strongly support an upward adjustment of the statutory rate and that the statutory royalty should be expressed as a percentage of the suggested retail list price of phonorecords in order to ensure a reasonable rate of return under existing economic conditions. The Study concluded that despite the availability of multiple sources of income, both music and non-music related, songwriting is a high risk occupation, deriving very low economic rewards, with few fringe benefits, and few protections against economic, financial and social adversity. [FN418] The Rinfret Study further concludes that a flat cent royalty is completely incapable of resisting inflationary pressure. [FN419]

FN418 Ibid, vol. 1, pp. 1, 35.

FN419 Ibid, vol. 1, p. 1.

Publishers (NMPA)

Praeger & Fenton Study

The Tribunal requested NMPA and music publishers to assemble and present data for the years 1977, 1978, and 1979 in the following areas: (a) Domestic and foreign revenues from mechanical royalties, performance fees, print license revenues, and revenues for administrative service to controlled publishers; (b) Expenses for mechanical, performance and print license payments; selling and promotion; general and administrative; and (c) Printing and miscellaneous income and total profit before tax. The Tribunal further directed "that the survey sample be structured so as to reflect the distinct roles of traditional and controlled publishers."

NMPA continues to maintain that the profitability of copyright owners is irrelevant to a fair determination under the criteria governing this proceeding. NMPA complied with the Tribunal's request for aggregate financial data and commissioned a financial survey of NMPA's 204 members and of 73 non-member music publishers considered to be associated with singer-songwriters for a total of 277.

The Survey of music publishers was conducted on behalf of NMPA by Praeger and Fenton, a certified public accounting firm. On October 1, 1980, NMPA submitted Aggregate Data Concerning the Financial Condition of Music Publishers to the Tribunal. Such data were based on the responses of 116 music publishers, 96 of which provided financial information. Accounting methods and reporting periods differed from response to response. The conclusion of the survey was that annual aggregate pre-tax income of traditional music publishers, based on revenues, ranged from 5% to 8.5%. Uncontroverted testimony demonstrated that even the modest return on revenues enjoyed by U.S. music publishers would be substantially lower if foreign-earned mechanicals were paid at the American rate. Based on the financial data submitted and allowing for market share and rate differentials, foreign royalties account for approximately 16 percent of U.S. publisher total revenues, 60 percent of which is paid out to songwriters. Foreign mechanical royalties would account for only seven percent of U.S. music publisher revenues if they were paid at the 2 [FN34] cent U.S. rate. [FN420]

FN420 Tr. 10/9/80, Strauss, pp. 74-75.

Analysis of the data submitted also shows that in 1979, U.S. music publishers would have earned not 8.5 but five percent return on revenues if foreign mechanicals has been paid at the American rate; in 1978, the seven percent return on revenues ***10476** would have been reduced to 3.5 percent; and, in 1977, the 5.17 percent return on revenues would have been reduced to less than two percent. [FN421]

FN421 Tr. 10/9/80, Strauss, p. 76.

Robert R. Nathan Associates, Inc. Study (Nathan)

Robert R. Nathan Associates, Inc. (Nathan) submitted analysis and data for the period 1909 to date on behalf of NMPA in accordance with the Tribunal's Rules of

Procedure. [FN422]

FN422 Nathan Study, pp. 1, 6.

The Nathan Study concluded that the statutory rate, historically equivalent to an effective rate of six percent of the suggested retail list price of phonorecords, has deteriorated to a level of little more than three percent of list price. The study further concludes that the compulsory license system no longer accommodates the proper function of the free market and denies copyright owners their right to negotiate royalties at a rate which fairly reflects the market value of their musical compositions. [FN423]

FN423 Nathan Study, p. 13.

The Nathan Study indicates that during the period 1963-1974, record company gross revenues increased substantially, while the mechanical royalty rate declined as a percentage of record sales. [FN424] The data presented illustrates that from 1963 to 1974, sales of recorded music increased from $361 million to $1,172 million. [FN425] Those data further show that in the period from 1964 through 1974, aggregate royalties actually paid to copyright owners declined from an average of about 11.2 percent of record sales at wholesale to about 7.2 percent. [FN426]

FN424 Ibid, p. 14.

FN425 Ibid, p. 14.

FN426 Ibid, p. 14.

The study indicates that in the period from 1964 through 1974, royalties paid by record companies to recording artists far outpaced mechanical royalties, rising to an average of 16.8 percent of record sales at wholesale. [FN427]

FN427 Ibid, p. 14.

The study shows that between 1973 and 1979, the record industry experiences phenomenal sales growth, with record sales almost doubling, from $2 billion to nearly $4 billion at retail list price. [FN428] It attributes such growth to two factors: an increase in unit sales (which may result in higher aggregate mechanical royalties and an increase in the suggested retail list price of records (which does not). Unit sales of albums rose by 22 percent in the 1973-78 period, while the average suggested retail list price of albums and tapes rose 54 percent, and that of singles, 65 percent. [FN429] Further, accompanying the increase in record prices was a continued decline in the number of songs per album, from twelve in 1965 to ten in 1979. [FN430]

FN428 Ibid, Table 1.

FN429 Nathan Study, p. 15.

FN430 Ibid, Table 2.

The Nathan Study indicated the impact of inflation by stating that the original two-cent royalty of 1909 commands little more than one-tenth of its purchasing power today. Further, the study states that the 2 [FN34] cent royalty presently in effect purchases today what the 2 cent royalty purchased in 1976. The study indicates a steady reduction in the number of songs per album. The volume of songs sold increased on average only two percent per annum in the period 1974-1979. [FN431]

FN431 Ibid, Table 11.

The Nathan Study further shows that the market position of copyright owners has deteriorated relative to that of others in the economy, including music arrangers, nonsymphony musicians, and industrial workers. [FN432] It shows that the market position of copyright owners has also deteriorated relative to that of performing artists. Available data show that average artist royalties range between ten and as high as twenty percent of list price. [FN433]

FN432 Ibid, Table 9.

FN433 Ibid, Table 10.

The Nathan Study does not regard increasing sales volume as an acceptable adjusting factor for inflation. The study shows that the increase in record sales volume has resulted in a mere two percent increase per annum in the volume of copyright songs sold to the public. Further, that aggregate mechanical royalties paid have not kept pace with record sales. [FN434]

FN434 Ibid, p. 44.

The Nathan Study shows that mechanical royalties are paid at a higher rate abroad than in the United States. Moreover, in all countries (other than Canada and the Soviet Union), the royalty payable is expressed as a percentage of price. [FN435]

FN435 Nathian Study, pp. 40-41.

The Nathan Study concluded that the statutory royalty should be expressed as six percent of the suggested retail list price of phonorecords, to ensure that the royalty payable maintains its purchasing power under inflationary pressure. [FN436] As stated in the Nathan report the royalty rate at the inception of the Copyright law was "at its ceiling rate of two cents per song thus came out to 24 cents per record * * * or six percent of the suggested retail list price." [FN437]

FN436 Ibid, p. 45.

FN437 Ibid, p. 10.

The Nathan Study strongly disapproves expressing the royalty as a flat cent rate, for such rate would quickly reduce to a mere fraction of its intended purchasing power. [FN438]

FN438 Ibid, Table 12.

The Nathan Study recognizes that indexing a flat cent rate to changes in the cost of living would maintain some of the purchasing power of the intended adjustment, but regards the use of an index as less equitable than a rate expressed as a percentage of price: Under a cost-of-living adjustment, increases in the rate payable always lag behind actual changes in inflation, thus perpetuating a built-in inequity.

In contrast, it finds that a royalty expressed as a percentage of price ensures that the compensation of songwriters and music publishers keeps pace not only with the price of records but also with the gross revenues generated by record sales. [FN439]

FN439 Nathan Study, pp. 48-49.

RIAA

Cambridge Research Institute Study (CRI)

CRI submitted data on behalf of RIAA covering the U.S. recording industry financial and operating performance. The CRI Study complements data derived from CRI's prior financial survey data of the recording industry which extends as far back as the 1950's. The current CRI Study updates the financial information for the period from 1977 through 1979 and also obtains information on current industry operations.

CRI's sample included label companies, which release top albums in the fields of pop, rock, jazz, folk, and classical. The sample included some major vertically integrated manufacturers, as well as a few very small and very large companies. In addition, the sample included representatives of some of the distribution patterns that exist in the industry.

The questionnaire was distributed in the summer of 1979 to all 66 RIAA member companies of which 14 recording companies responded. Not all companies supplied data for all the years requested. [FN440]

FN440 CRI Study, p. 5.

The CRI "Estimated Financial Statistics for the U.S. Recording Industry (1974-1979)" was based on the RIAA total industry sales figures which are generated by RIAA's Market Research Committee. The committee is composed of major recording companies executives. CRI used the committee's figures as a foundation, to expand its sample results to produce industry-wide aggregate financial figures.

***10477** The CRI Study produced an estimate of industry-wide profits which is more heavily weighted with larger firms.

To assemble a financial picture of the U.S. recording industry, CRI used estimation techniques to account for certain data that were not reported by individual respondents. The sample generated by the CRI Study produced an estimate of industry-wide profits.

The study shows that in terms of pre-tax profits (and losses), 1979 was the worst year for the recording industry in recent history. The CRI Study included a consolidated industry-wide income statement which was shown in two formats--one as a breakdown of each component in total dollars and the other format had the same components and totals expressed as a percentage of net sales. These formats excluded license income from U.S. masters licensed abroad. [FN441] Both statement formats were subsequently connected because of tabulation error. [FN442]

FN441 CRI Study, Exhibits 1, 2, pp. 4-9.

FN442 Fitzpatrick letter, July 17, 1980.

The CRI Study contained data showing that for the years 1977-1979, the largest expense for the recording industry was production and manufacturing expenses (30.8%) and the second largest was artist and recording expenses (29.9%). [FN443]

FN443 CRI Study, pp. 4-10.

CRI produced data on break-even points. It showed that more than 80% of most recordings fail to break even. CRI data on the profitability of artists' royalty accounts, showed that approximately 80% of the artists had unprofitable royalty accounts.

The CRI Financial and Operations Survey also included information on pricing of records; profile of recording sales; sales returns; and, personnel, artist, and singer/songwriters.

In addition to the Financial and Operations Survey, CRI conducted a survey of mechanical royalties on all tunes released by two respondent companies in 1978. The survey shows that the mechanical royalty rates are set at the statutory amount or a standard variation thereof for record club and budget/economy tunes.

Average Retail Prices Study

RIAA also submitted data reporting average retail selling prices of LP's, tapes, singles by type of distribution outlet for the period 1974-1979.

The retail price data in this study are based on information from a nationwide Consumer Panel maintained by an independent testing institute for CBS Records.

The Consumer Panel consists of approximately 7,150 individuals, representing a sample of the record and tape buying public in the United States. Record and tape purchases of Panel members are monitored on a daily basis and the results are projected to national levels.

Each year, the reports of the Panel members are consolidated to produce average retail prices for that year by configuration and type of outlet. [FN444] The Study shows that the suggested retail list price and also the actual selling price of LP's, tapes and singles has increased over the last six years. It showed that during the period 1974-1979, the average actual selling price of LP's increased from

$4.05 to $5.79.

FN444 Ibid, Exhibits 1, 2, 3.

Album Content and Tune Length Study

RIAA submitted a Study of the top 150 albums listed in Billboard magazine's best-seller charts in order to obtain information about the composition and tune lengths of record albums. [FN445] For purposes of the Study, RIAA selected at random the Billboard charts in the issues dated March 31, 1979 and January 19, 1980. [FN446] The Study shows that the average number of songs per disk has continued to decline, from twelve tunes in 1965 to ten tunes in 1973, to nine tunes in 1979 [FN447] and that the majority of mechanical royalties on these 150 albums were paid at the statutory rate. [FN448]

FN445 Study, Appendix C.

FN446 Ibid, Appendix A, B.

FN447 Album Content and Tune Length Study, p. 3, line item 5.

FN448 Study, p. 5.

The Study further shows that increased record sales volume has not compensated copyright owners for the increased length of their songs. Most recorded songs (77%) have an average playing time of less than five minutes. [FN449]

FN449 Ibid, p. 4, line item 12.

Legal Issues

Petition of the Music Arrangers

The American Society of Music Arrangers submitted to the Tribunal a petition on January 31, 1980 requesting a hearing on a proposal to require record companies to provide compensation to arrangers "in the form of a royalty to the arranger for every record sold, subject to the usual industry allowances for returns, promotion, etc." [FN450] The Tribunal invited the parties to this proceeding to comment on this petition. Comments were submitted by AGAC, NMPA, and RIAA. [FN451] Each of these comments asserted that consideration of the petition would be beyond the jurisdiction of the Tribunal. After considering these comments and reply comments of ASMA, [FN452] the Tribunal rejected the petition. [FN453] The Tribunal stated:

FN450 Letter of Eddy L. Manson, President, American Society of Music Arrangers, Jan. 31, 1980.

FN451 Letter of Alvin Deutsch, counsel for AGAC, Feb. 26, 1980; letter of Morris B. Abram, counsel for NMPA, Feb. 29, 1980; memorandum of RIAA, March 3, 1980.

FN452 Reply Memorandum of American Society of Music Arrangers In Opposition To Memoranda Filed By the Recording Industry Association of America, the National Music

Publisher's Association, and the American Guild of Authors and Composers, March 26, 1980.

FN453 Letter of Chairman Mary Lou Burg to Harris E. Tulchin, counsel, ASMA, April 7, 1980.

The Tribunal interprets 17 USC 115 as providing that the compulsory license royalty is to be paid only to the copyright owner of the original musical composition. Congress did not grant the Tribunal the statutory authority to create a new compulsory license. Rather the Congress, 17 USC 801(b)(1), expressly limited the Tribunal to the adjustment of reasonable copyright royalty rates as provided in Section 115.

The Mechanical Royalty Percentage Formulas Issue

The Tribunal on March 25, 1980 heard oral argument by the parties on a motion of RIAA requesting the Tribunal to issue an order declaring that any adjustment of the mechanical royalty rate to provide for the fixing of the royalty rate as a percentage of the price of the phonorecord would be beyond the jurisdiction of the Tribunal. We issued an order on March 27, 1980 stating in part:

The Tribunal has not found the arguments in support of the motion to be persuasive and the motion is therefore denied. The Tribunal will receive and consider evidence on proposed "mechanical royalty" percentage formulas.

The Tribunal has not in this proceeding adopted a royalty rate fixed as a percentage of the price of the phonorecord, therefore, it is unnecessary for the Tribunal now to further discuss this issue. We observe that our determination to retain a flat rate indexed to increases in record prices is not subject to RIAA's jurisdictional objections, and indeed, was urged upon us by RIAA.

The Issue of Burden of Proof

Our jurisdiction to provide for an adjustment of the mechanical royalty rate is derived from the same statutory authorization as our jurisdiction to adjust the royalty rate paid by operators of coin-operated phonorecord players (jukeboxes). [FN454] We have analyzed the ***10478** issue of burden of proof in the opinion accompanying our final determination in the jukebox proceeding. [FN455]

FN454 17 USC 801(b).

FN455 46 FR 887, Jan. 5, 1981.

17 USC 804(a)(1) mandated the institution of this proceeding. No party to this proceeding was required to sustain any general or specific burden of proof. Since it was obviously not possible for the Tribunal to hear simultaneous presentations of the direct cases of the parties, the Tribunal determined an order of presentation. In doing so, the Tribunal rejected any suggestion that the order of presentation implied any relationship to a burden of proof.

Likewise, the statutory language and the legislative history of the copyright revi-

sion bill excludes any presumptions concerning the "reasonableness" of the existing rate. Nor is the existing rate to be accorded precedential weight in the Tribunal's proceedings. The task of the Tribunal in this proceeding was to determine a "reasonable" royalty rate on the basis of the record before us and calculated "to achieve" the statutory objectives. Our findings and conclusions on these matters are set forth in considerable detail elsewhere in this document.

"Bargaining Room" Theory

It has been suggested during this proceeding that the Tribunal should adopt a royalty rate at the high level of a range within which there would be marketplace bargaining. RIAA has maintained that such action by the Tribunal would be contrary to law, as well as contrary to prevailing industry practice. [FN456]

FN456 RIAA Proposed Findings of Fact and Conclusions of Law, pp. 190-208.

The statute requires the Tribunal to establish a "reasonable" royalty rate calculated to achieve the statutory objectives. We adopt the view of RIAA that:

A rate that is deliberately fixed above the level that the market can bear--so that a lower rate can be negotiated in the marketplace--cannot be 'reasonable'. Such a rate would yield more than the 'fair return' to copyright owners mandated by the statute. [FN457]

FN457 Ibid, p. 191.

In adjusting the mechanical rate, we excluded any consideration of the "bargaining room" theory.

The AGAC Motion To Strike

AGAC on July 15, 1980 filed a motion moving the Tribunal to strike from the record of this proceeding the economic study of the recording industry prepared by the Cambridge Research Institute, the reply comments of April 21, 1980 prepared by the Institute for RIAA, and the May 5, 1980 statement of David B. Kiser. AGAC subsequently expanded the basis for the motion because of the lack of access to certain Touche Ross market research information.

AGAC maintained that the refusal of RIAA to submit requested input data, including individual questionnaire responses, "violates the rules of the Tribunal (37 CFR 301.51), denies other parties the ability to conduct such cross examination as is necessary to disclose the facts fully and truthfully, and deprives the Tribunal of the ability to determine the accuracy, reliability, and truthfulness of the statements made in the CRI documents." [FN458]

FN458 AGAC Motion To Strike, p. 2.

Section 301.51(h) of the Tribunal's Rules of Procedure states in part that:

If requested, tabulations of input data shall be made available to the Tribunal.

AGAC has argued that it is impossible to establish whether statements contained in the Cambridge documents are reliable or accurate simply by questioning the author of the document. AGAC mentioned that it "is well settled that such studies should not be admitted in administrative proceedings unless the underlying questionnaires are made available." [FN459]

FN459 Ibid, p. 5.

The Tribunal on October 14, 1980 denied the motion of AGAC. [FN460] We were not persuaded that the granting of the motion was required by the Administrative Procedure Act, the case law, the Tribunal's Rules of Procedure or procedural fairness. The inability or failure of RIAA to disclose "confidential" input information in our view goes to the weight we should accord their evidence, not to its admissibility. This is particularly relevant to our proceedings since the Congress has not accorded the Tribunal subpoena power.

FN460 Tr. Oct. 14, 1980, pp. 270-271.

Determination of Royalty Rate

Preliminary Statement

The Tribunal held 46 days of hearings on the adjustment of the mechanical royalty rate. On the basis of the record in this proceeding, the Tribunal determined that an adjustment was appropriate.

Congressional Purpose

When Congress enacted the Copyright Revision Act of 1976 it specifically acknowledged the unfairness of the existing mechanical royalty rate: "(Although) a compulsory licensing system is still warranted as a condition for the rights of reproducing and distributing phonorecords of copyrighted music * * * the present system is unfair and unnecessarily burdensome on copyright owners, and * * * the statutory rate is too low." [FN461]

FN461 H.R. Rep. No. 94-1476, 94th Cong., 2d Sess. 107 (1976).

Congress mandated that the Tribunal commence rate adjustment proceedings on January 1, 1980 and publish its determination of a reasonable rate by year's end. [FN462] From review of the legislative history of the Act we find that Congress delegated plenary authority to this Tribunal to effect a reasonable rate payable under a compulsory license, and calculated to achieve the statutory objectives.

FN462 17 U.S.C. § 804.

Congress increased the statutory rate to 2 3/4 cents per musical work made and distributed, or 1/2 of one cent per minute of playing time, or fraction thereof, effective January 1, 1978.

We find that the legislative history of the Act is clear that Congress did not find

that the existing rate was fair as of 1976 or any other date. We further find that Congress did not intend the rate to be a precedent for the Tribunal nor to bind the Tribunal in any way.

The 1975 Senate Judiciary Committee Report on the copyright law revision stated:

The Committee does not intend that the rates in this legislation shall be regarded as precedents in future proceedings of the Tribunal. [FN463]

FN463 S. Rep. No. 94-473, 94th Cong., 1st Sess. p. 155 (1975).

The House took the opposite view. The last sentence of section 801(b)(1) of the House amendment of the bill stated that the Tribunal's determinations adjusting mechanical royalty rates "shall be based upon relevant factors occurring subsequent to the date of the enactment of this Act." [FN464]

FN464 H.R. Rep. No. 94-1476, p. 41 (1976).

In conference, the House abandoned its position and the Senate view prevailed. The language in section 801(b)(1) restricting the Tribunal's consideration to events after 1976 was deleted, and the present criteria were inserted. The conference report stated:

The House receded on its language appearing in the last sentence of section 801(b)(1), and the conference agreed to a substitute for the language. [FN465]

FN465 H.R. Conf. Rep. No. 94-1733, p. 82 (1976).

From our review of the legislative history of the Act we conclude that Congress resolved the split between the House and the Senate to favor the Senate view that the rate of 2 3/4 cents was not a precedent for the Tribunal, ***10479** and that the Tribunal was not to limit its consideration to events after enactment of the Act. It is our opinion and we therefore find, that the legislative history of the Act shows that Congress delegated to the Tribunal sufficient authority to effect a de novo adjustment of the statutory rate, uninhibited by prior Congressional action, consistent with Section 801 of the Act.

Statutory Objectives

Our review of the legislative history of the Act indicates that the statutory criteria in section 801(b) originated with the suggestion of Professor Ernest Gellhorn and the Register of Copyrights that more definite criteria than "reasonableness" should be provided, in order to avoid a constitutional challenge to the Tribunal. [FN466] Subsequently, the House Judiciary Committee included criteria in its report. [FN467] The Conference Committee then included a revised version of the criteria in section 801. [FN468]

FN466 2nd Supp. Rep. of the Register of Copyrights (draft), Ch. XV, pp. 29, 31 (1975); 1975 Hearings, Part 3, pp. 1914, 1921-25.

FN467 H.R. Rep. 94-1476, p. 174 (1976).

FN468 H.R. Conf. Rep. No. 94-1733, p. 82 (1976).

We therefore conclude that Congress drafted the criteria in the broadest terms that it could, consistent with its intent to prevent a challenge to the constitutionality of the Tribunal.

We also conclude, consistent with its Congressional mandate, that this Tribunal's adjustment must set a "reasonable" mechanical royalty rate designed to achieve four objectives, set forth in Section 801 of the Act:

(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. [FN469]

FN469 17 U.S.C. §801(b)(1)(A)-(D).

Based on our review of the entire record in this proceeding and the legislative history of the Act, we have determined that a reasonable adjustment of the statutory rate must look to the application and operation of the regulatory system of which it is an integral part. We conclude from the record in this proceeding and the legislative history of the Act, that the regulatory system was designed to remedy a perceived market deficiency, namely, attempts at monopolization by copyright users. [FN470] We therefore find that the application of Section 115 is limited by the market deficiency which justifies its existence.

FN470 Knight Report, June 30, 1969, pp. 5-8.

It is our opinion that the term reasonable in the statute is of dominating importance in reaching a final determination in this proceeding. Further we find by the express terms of Section 115 of the Act, that the compulsory license system is applicable only in the absence of a negotiated license. [FN471]

FN471 17 U.S.C. § 115(b)(2).

We conclude that the Tribunal's authority to adjust the statutory rate payable under the compulsory license system is only limited by the fact that Section 115 of the Act operates on an individual and not an industry-wide basis. The legislative history of the Act makes it clear that Section 115 of the Act contemplates the com-

pulsory use of an individual song, by an individual record manufacturer, after voluntary negotiation with an individual copyright owner has failed. Further that in exchange for that compulsory use, the Act contemplates a per-unit rate of compensation payable to the copyright owner on an individual basis by a copyright user.

Based on the entire record of this proceeding and the legislative history of the Act, we are of the opinion that the market then determines the total amount of royalties paid to each copyright owner for all uses. We thus conclude that under Section 115, the statutory royalty is designed to provide a reasonable rate of return on an individual per-use basis.

Further, consistent with the anti-monopoly purpose of the compulsory license system, a reasonable adjustment of the statutory rate should work to ensure the full play of market forces, while affording individual copyright owners a reasonable rate of return for their creative works.

To Maximize the Availability of Works

Section 801(b)(1)(A) of the Act mandates that the statutory rate payable under the compulsory license system be calculated "to maximize the availability of creatives works to the public."

Under Section 115 of the Act, incorporated by reference in Section 801, the term "creative work" applies to the copyrighted non-dramatic musical composition subject to compulsory use. In our opinion the adjustment of the statutory rate payable under Section 115 of the Act is intended to encourage the creation and dissemination of musical compositions. This encouragement we find takes the form of an economic incentive and the prospect of pecuniary reward--royalties payable at a reasonable rate of return. The evidence shows that under the statutory objectives governing a reasonable adjustment of the statutory rate, the Tribunal must afford songwriters a financial and not merely a psychic reward for their creative efforts. [FN472]

FN472 Tr. 7/31, p. 107.

RIAA argues that if the Tribunal were to grant a rate increase, recording companies would have to take serious steps to deal with these new costs, like reducing the number of releases, thereby reducing the quantity of creative works available to the public. [FN473] They also argued that a rate increase might lead record companies to issue releases only by artists with a proven record of "home-run" albums, thereby reducing the variety of creative works available to the public. [FN474] The Tribunal was not persuaded by these arguments.

FN473 RIAA Findings and Conclusions, p. 181.

FN474 Ibid, p. 182.

The evidence in this proceeding shows that 2 [FN34] cent statutory ceiling does not maximize the availability of commercially viable musical compositions to the public. [FN475] It further shows that the 2 [FN34] cent rate does not permit songwriters to maximize their creative outputs. We find nothing in this record which would justi-

fy any reasonable concern that the rate we have adopted will deprive the public of access to music.

FN475 Tr. 7/8, pp. 44-46.

Fair Return to the Copyright Owner and Fair Income for the Copyright User

Section 801(b)(1)(B) of the Act mandates that the statutory rate payable under the compulsory license system be calculated "to afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions."

We find that the copyright owner's right to receive a fair rate of return for the compulsory use of his song derives from Congress' decision to afford commercial protection to the author of a creative work. [FN476] The evidence shows that in most instances, the rate of return afforded the copyright owner is determined on the free market. It further shows that in the case of the composer of non-dramatic musical composition, however, the rate of return from recordings is fixed under Section 115 of ***10480** the Act. The statutory rate thus regulates the price of music.

FN476 17 U.S.C. § 102.

The evidence shows that the copyright user's right to fair income under the compulsory license system derives from Congress' decision to permit entry into the music market by a potential copyright user. [FN477] Accordingly, the statutory rate--triggered only after voluntary negotiations have failed--should work to permit any record companies to enter the market at will. Thus, Section 115 of the Act fixes a statutory rate as a royalty of reasonable resort. [FN478]

FN477 Tr. 6/18, p, 21.

FN478 Tr. 5/14, pp. 36-37.

In our view, taking the entire record of this proceeding into consideration, including the available economic data and the relevant benchmarks of fairness, demonstrates that the statutory royalty payable under the compulsory license system should be adjusted upward to a rate of four cents, with an annual adjustment. The evidence shows that the current rate does not afford songwriters and music publishers, as copyright owners, a fair return for their creative work. [FN479] The evidence also shows that adjustment of the mechanical royalty rate to four cents with annual adjustment will permit entry into the music market by a potential copyright user and will afford record companies the opportunity to earn a fair income. [FN480]

FN479 Nathan Study, pp. 45-50; Tr. 5/7, p. 108.

FN480 Nathan Study, pp. 7-23.

In our view the evidence did not demonstrate that a rate increase would prevent entry by record companies into the music market or that such an adjustment would fail to afford copyright users a fair income. We find the proponderance of the

evidence was to the contrary. The evidence presented in our opinion confirms that the record industry flourished during the past decade. The evidence shows that during the past decade, the record industry developed into a four billion dollar enterprise, and sustained a high level of profitability, in every year but 1979. [FN481]

FN481 Ibid, p. 21.

It is our opinion, and we so find, that the evidence has failed to prove that a four cent rate will impede the industry's future growth or fail to afford its members an opportunity to earn a fair income.

Relative Roles of Owners and Users

The evidence shows that upward adjustment of the statutory rate to four cents with annual adjustment will best reflect the relative roles of the copyright owner and the copyright user in the product made available to the public.

The evidence shows that the songwriter is the provider of an essential input to the phonorecord: The song itself. The music publisher collaborates with the songwriter in the creative process. [FN482] Sometimes the music publisher's role involves matching up a composer with a suitable lyricist, [FN483] and sometimes matching up the singer and the song. [FN484] The evidence shows that when independent producers are used, the role of the record company in the creative process is reduced. [FN485]

FN482 Tr. 5/8, p. 50.

FN483 Tr. 6/12, pp. 89-115, 139-152, 155-158.

FN484 Tr. 6/26, pp. 118-119; Tr. 5/8, p. 63.

FN485 Tr. 5/8, pp. 49-77.

The record reflects that the role of music publishers and record companies is somewhat different is dealing with singer-songwriters--recording artists who record their own songs. We note that in that situation, sometimes it is the music publisher who finds and develops the singer-songwriter, [FN486] and sometimes it is the record company. We find, however, that singer-songwriters are not subject to the mechanical royalty rate for the compulsory license, and instead negotiate total packages for their copyright performance package.

FN486 Ibid, pp. 32-33.

We determined from the evidence in this record, that on recordings which may be subject to the compulsory license, (i.e. not including singer-songwriter's recordings of their own songs) the creative contributions are made sometimes by the songwriter and music publisher, the copyright owners, as well as by the independent producer, and sometimes by the record company, the copyright user.

The evidence also shows that record companies also make a vital contribution to the production of a sound recording. They are engaged frequently in finding and signing the right talent; deciding on the material; directing the recording sessions; and in the development of artists' careers. In addition record companies' personnel are involved in packaging, graphics, marketing and promotion.

The evidence shows that record companies have substantial risks and cost. The evidence also shows that they have often succeeded in minimizing their risks and costs by transferring them to others. The evidence also shows that while the record company advances the money for recording costs, if the album achieves even moderate success, these recording costs are paid back to the record company, by the recording artist, before the artist receives any actual royalties. The evidence also shows that once a recording artist has had one successful record, the record company has limited risk on subsequent records, because record company contracts with recording artist typically provide for cross-collateralization of recording artist royalties between different records. [FN487] The evidence shows that record companies can cross-collateralize mechanical royalties with recording artist royalties--and charge recording costs against both types of royalties.

FN487 CBS Artist Contract, A-D, Tr. 7/22, p. 6.

The evidence shows that at the manufacturing and distribution levels, record companies can minimize their risks through distribution systems which allow them to manufacture a very small number of records of a new release, before receiving indication of whether the release will have commercial success. [FN488]

FN488 Tr. 7/1, pp. 72-73.

It is our opinion and we so find that although the amount of money advanced by record companies as part of the recording process is significant, record companies have often succeeded in transferring the risk and cost of record production.

The evidence shows that new markets for creative expression and media for their communication may be opened through technological innovation, and through development of new types of music.

The evidence in the record shows that the development of different types of music is related to the geograpahic distribution of songwriters and music publishers, who are dispersed across the United States--unlike record companies which tend to concentrate in Los Angeles and New York City. A witness testified:

NMPA COUNSEL: So it's, in fact, important to have independent music publishers located across the nation; isn't that right

THE WITNESS: Oh, I think so and they are, thank goodness. I think that we see music now coming from all over America. You('ve) got * * * publishers in various sections of the country. (You've) got the music industry located in Miami. It's in Memphis. It's in Muscle Shoals, Alabama. It's in Birmingham, Alabama. It's in New Orleans, Louisiana. I'm talking South because I'm for the South. But I know

it's in San Francisco, California; it's in Philadelphia, Pennsylvania. It's all over this country. [FN489]

FN489 Tr. 6/2, pp. 114-115.

The record reflects that the copyright owners rarely make any significant contributions in the way of technological innovation.

The record also reflects that record companies make contributions to the ***10481** opening of new markets through record clubs, mail order sales and television advertising campaigns. The record also reflects that the record companies make unique and distinctive contribution concerning technology, cost, risk and creativity.

We determined, however, that upward adjustment of the mechanical royalty rate to four cents, would best reflect, based on the evidence in the entire record, the relative contribution of copyright owners and copyright users, with respect to each of the criteria set forth in the Act: "creative contribution, technological contribution, capital investment, cost, risk, and contribution to the opening of new markets for creative expression and media for their communication."

Disruption of the Industries

We determined that upward adjustments of the statutory rate payable under Section 115 of the Act to four cents with annual adjustment, will not have any disruptive impact on the structure of the industries involved or on generally prevailing industry practices.

We reject the contention that any immediate increase in the mechanical royalty payable to copyright owners, would be disruptive on the record industry. The record in this proceeding clearly shows that an increase in the compulsory license is necessary to afford copyright owners a fair return. We reject the argument that it would be difficult to pay that rate. [FN490] We find the record void of any probative evidence to support that argument. On the basis of the record in this proceeding, we find that the record industry has been able to absorb other cost increases without any disruptive impact on the structure of the industries involved or on generally prevailing industry practices.

FN490 RIAA Summary of Proposed Findings of Fact and Conclusions, p. 28.

The record reflects that the record industry's ability to absorb other cost increases is demonstrated by comparison of record company costs in 1965 with record company costs in 1980. In 1965, evidence was submitted to Congress which stated that on a record listed at $3.98, the record companies' total cost was $1.26, of which 24 cents was attributable to the mechanical royalty rate (two cents x 12 songs). [FN491] In 1980, evidence was submitted to this Tribunal that on a record listed at $7.98, the record companies' total cost was $2.79, of which 27.5 cents was attributable to the mechanical royalty rate (2 [FN34] cents x 10 songs). [FN492] Thus, between 1965 and 1980, all other record company costs went up from $1.02 to $2.51--an increase of 146 percent. At the same time, the mechanical royalty

payments went up from 24 cents to 27.5 cents, an increase of 14.5 percent. The evidence shows that the rate of increase of all other record company costs during this fifteen-year period is ten times as great as the increase in the mechanical royalty rate. [FN493]

FN491 1965 CRI Report.

FN492 MPA Exh. 54; RIAA Exh. BB.

FN493 MPA Findings and Conclusions, pp. 167-168.

We determined that an increase in the mechanical royalty rate to four cents would produce a 40 cent royalty on a record listed at $7.98. That would raise the mechanical royalty cost from 24 cents in 1965 to 40 cents in 1981--a 67 percent increase over fifteen years, during which time all other costs will have risen 147 percent. We note that if the record industry chose to absorb this 12.5 cent increase in mechanical royalties by reducing its profit margin from $1.20 to 107.5 cents, the record company profit margin would still be 144 percent higher today than in 1965. This is 77 percent higher than the increase in mechanical royalties which would result from adjusting the rate to four cents.

We determined that the amount of the mechanical royalty increase to be absorbed or passed on by the record companies would not be disruptive of the industry. The evidence clearly shows that it would be substantially less than other cost increases which the record industry has been able to absorb, or pass on.

Erosion of the Statutory Rate

The evidence in this proceeding shows that the statutory rate has been seriously eroded by inflation, and does not afford copyright owners a reasonable return for their creative efforts. The evidence reflects that despite the astounding growth in market demand for music in the period 1974 to date, the return afforded copyright owners, as a proportion of record sales, has steadily declined.

The evidence shows that during the period 1963-1974, record company gross revenues increased substantially. [FN494] The evidence also shows that in the period 1963 through 1974, sales of recorded music increased from $361 million to $1,172 million or 202 percent. [FN495]

FN494 athan Study, p. 13

FN495 Ibid, p. 14.

The evidence also shows that in the period 1964 through 1974, aggregate royalties actually paid to copyright owners declined from an average of about 11.2 percent of record sales at wholesale to about 7.2 percent, thus relegating copyright owners to a substantially weakened economic position vis-a-vis the users of their creative works. [FN496]

FN496 Ibid.

The evidence further shows that in the period 1964 through 1974, royalties paid by record companies to recording artists, negotiated on the free market, far outpaced mechanical royalties, rising to an average of 16.8 percent of record sales at wholesale. [FN497]

FN497 Ibid.

The record reflects that the available evidence shows that between 1973 and 1979, the record industry experienced growth, with record sales almost doubling, from $2 billion to nearly $4 billion at retail list price. [FN498]

FN498 Ibid, p. 16.

The evidence shows that the increase in record sales volume has resulted in a two percent increase per annum in the volume of copyrighted songs sold to the public. Further aggregate mechanical royalties paid have not kept pace with record sales. [FN499]

FN499 Ibid, p. 44.

The evidence in this record shows that all parties agree that the purchasing power of the statutory rate has seriously eroded under inflationary pressure. This erosion has become more severe since the 1950's, as inflation began to reach new levels. [FN500] The evidence further shows that during the twelve-year period of copyright revision, the Consumer Price Index rose by 76 percent, thus reducing the purchasing power of the two cent flat fee to little more than half its value in 1965 dollars. [FN501] The record reflects that to restore the purchasing power which two cents had in 1965, when the Congressional hearings began, it would be necessary to set the mechanical royalty rate at more than five cents today. [FN502]

FN500 MPA Chart A; Rinfret Study, Vol. 1, p. 22; Tr. 7/23, p. 90.

FN501 MPA, Table 6.

FN502 MPA Post-Hearing Brief, pp. 22-23.

The evidence shows that the current rate has suffered a similar erosion. Congress enacted the 2 3/4 cent interim rate on the basis of evidence describing conditions through the year 1974. In our opinion, and we so find, that even if the Tribunal were to ignore Congress' instruction that the existing rate have no precedential weight in the current proceeding, the evidence in this proceeding demands an immediate upward adjustment of the royalty to not less than four cents merely to restore the 2 3/4 cents existing rate today to its effective purchasing power in 1974 dollars.

***10482** Copyright Users

We note that the record industry claims that an increase in the statutory mechanical rates will bankrupt great record companies, will force others to drastically cut their operations, and will force increases of 300-700 million dollars to con-

sumers. We reject all of these claims as we find no probative evidence in the record to support them.

The evidence in this record is clear that mechanical royalties are a small part of record industry costs; that when the mechanical royalty rate increased in 1978, the record industry did not reduce its other expenses, did not reduce the scope of its operations, and did not increase prices because of the change in mechanical royalties; and that the record industry has increased prices whenever it felt the market would bear it, even though mechanical royalties were frozen. The evidence shows that the impact of mechanical royalties on both the industry and consumers is trivial, compared to the effects of expenditures such as artists' royalties, promotional expenses, and general and administrative expenses, which are within the industry's control.

We have previously discussed our conclusions that the evidence indicates that any effect of changes in the mechanical rate are insignificant compared to the effects of costs within the industry's control, such as artists' royalties or selling, general and administrative expenses, or compared to the effects of general economic conditions. This is apparent from comparison of mechanical royalties to other record industry costs, from analysis of changes in various record industry costs, and from the events of 1978.

It is our opinion and we so find that the evidence also demonstrates that the adverse consequences of the 1979-80 recession were temporary and most of them have already been overcome.

The record shows that the record industry has introduced two kinds of evidence concerning its economic condition. The first was pessimistic testimony provided by representatives of the major companies. The evidence shows, however, that the testimony was contradicted by equally optimistic statements issued by the same companies (and in one instance by the same individual) to other audiences, such as stockholders, securities analysts and trade groups. [FN503] We note that it is not unknown for corporations to plead poverty to regulatory agencies while simultaneously making optimistic profit projections to their stockholders.

FN503 Post-Hearing Brief of AGAC, p. 58.

The second form of evidence introduced by the record industry, the CRI Economic Study, was subject to such deficiences that it does not provide full data concerning the revenues, return on investment and the level of profit of the record industry. The record reflects that CRI's principal document was its revised Exhibit 1, attached to Mr. James Fitzpatrick's letter of July 7, 1980.

In our opinion the first major omission and uncertainty in this document is its starting figure for industry net sales, which is simply 50% of the RIAA estimate. The evidence shows that the estimate is produced by the RIAA Marketing Committee, which consists of a dozen representatives of large record companies. The evidence shows that they take an aggregate sales figure for the major record companies reported to them by Touche Ross, and adjust it by adding a guess at the sales of all oth-

er record companies. [FN504] Without knowing either the figures reported by Touche Ross or the amount of the RIAA Marketing Committee "adjustment", one cannot know whether the estimates are based on Touche Ross' figures, or primarily reflect the "horseback guesses" of the marketing committee.

FN504 Tr. 7/24, pp. 36-42; Tr. 7/29, pp. 9-12.

The record reflects that notwithstanding a request therefor, no evidence was submitted regarding the Touche Ross reports which purportedly underlay the net sales estimates reported in CRI Exhibit 1 for the years 1974-79. [FN505] The evidence shows that there can be nothing confidential about the Touche Ross figures. They are aggregate figures, not individual company figures; [FN506] they have been shown to representatives of the major competitors in the industry, who serve on the RIAA Marketing Committee.

FN505 Tr. 7/25, pp. 42-43.

FN506 Ibid.

The testimony of the record industry is consistent that their current practice is to request licenses from publishers only after an album has been recorded. [FN507] The evidence shows that there is nothing in the process of recording albums that makes it impossible to decide upon a group of compositions in advance of recording, and to bargain with copyright owners for the most favorable rates on those compositions.

FN507 Ibid.

The evidence shows that at the present time, CBS artists' contracts require the artist to inform CBS of the compositions to be recorded several weeks in advance of recording. [FN508] One witness testified that compositions are selected before arrangements and instrumentation are chosen, before a studio is selected, before musicians are selected, and before recording begins. [FN509]

FN508 Tr. 7/30, pp. 106-109; CBS Artist Contracts, A-D, Tr. 7/22, p. 6.

FN509 Tr. 6/26, pp. 31, 34; RIAA Exh. G.

The evidence in the record shows that copyright users rarely invoke Section 115 of the Act. Further they exploit the statutory rate payable under a compulsory license to keep their mechanical royalty costs as low as possible, fixing the 2 [FN34] cent royalty as a ceiling in all negotiations with copyright owners, even for first releases. [FN510]

FN510 Tr. 6/18, pp. 22-23, 145; Tr. 6/19, pp. 78, 88; Tr. 6/25, p. 15.

The record reflects that RIAA initially proposed that the Tribunal maintain the statutory rate at its current level, urging that increases in record sales, with consequent increases in total royalties payable to copyright owners as a group, compensate for the eroding effects of inflation. [FN511] The Tribunal finds the record

is void of any useful evidence to support that position.

FN511 Tr. 7/30, p. 122.

The evidence shows that a copyright user who invokes the compulsory license for phonorecords pays the mechanical royalty rate directly to the individual copyright owner. What mechanical royalty fees are paid by the same copyright users, or other copyright users, to other copyright owner obviously has no effect on whether the individual copyright owner is receiving a fair return for the individual uses of his songs.

We conclude that it makes no difference to the songwriter, whose song is subject to the compulsory license for use on an album which sells 50,000 copies, that songwriters of best-selling albums receive more royalties, in the aggregate. In our view the fair return required by the statute is not to songwriters as a group but as individuals.

The evidence shows that from the standpoint of investment, risk, and technological innovation the record industry activities do often benefit the copyright owners. All these factors were taken into consideration in determining that the rate should be four cents and not higher.

The Tribunal concluded that while it was valuable for us to be aware of the financial status of both the recording industry and the copyright owners, the financial information received provided no clear guidance as to how to balance fair return as against fair income.

***10483** The Tribunal also concluded that while the rate must be viewed as payment on the individual basis and in principle royalty payments should not be considered in the aggregate, the size of the American market and the volume of records sold do constitute an advantage to the copyright owner. Therefore, although not on a one-for-one basis, volume can be taken into consideration when setting the rate, and for this reason the rate was not set as high as it is in Europe.

Copyright Owners

The record of this proceeding contains detailed analyses of the legislative history of Section 115. Our review of this history persuades us that Congress enacted the compulsory license as part of the Copyright Act of 1909 because it feared that the Aeolian Piano Roll Company would monopolize the music industry by entering into exclusive contracts with copyright owners. Accordingly, the Copyright Act provided that once a song was recorded, any record company--as a matter of right--could obtain a license at a statutory rate and record its own rendition of the musical composition.

As originally enacted, the compulsory license was thus intended to govern the relationship among copyright users--and not the relationship between copyright users and copyright owners. The compulsory license was intended to prevent formation of a "music monopoly" by guaranteeing to all mechanical producers full access to copy-

right music.

The evidence shows that the recorded music industry has experienced significant growth in the five-year period since Congress concluded its hearings on the compulsory license. It further shows that during that period, however, songwriters and music publishers, the copyright owners, have been limited to a mechanical royalty rate worth only a fraction of its former purchasing power, and yielding aggregate royalties equal to a decreasing percentage of record sales at the suggested retail list price. Further, that copyright owners have thus been relegated to a substantially weakened economic position.

The record reflects that between 1973 and 1979, sales of recorded music in the Untied States almost doubled, from $2 billion to nearly $4 billion. We note that sales growth was especially large in 1977, with a spectacular rise of 28 percent. Further, that in 1978, the industry enjoyed another huge growth increase--18 percent.

In our opinion, based on the evidence in this proceeding, the fortunes of the record companies, the copyright users, have been enhanced in the last decade. The evidence shows that at the same time, the fortunes of songwriters and music publishers, the copyright owners--subject to a price-fixed mechanical royalty in a period of great inflation--have dwindled. We find that:

The value of the fixed rate mechanical royalty has decreased under inflationary pressure. The 2 3/4 cent royalty enacted by Congress in 1976 is now worth only two cents in 1976 dollars. Thus, the entire current increase has already been eroded by inflation.

The 2 3/4 cent ceiling rate is not paid to copyright owners across-the-board.

The 2 3/4 cent mechanical royalty, as a rate of compensation, has not kept pace with the afforded performing artists, musicians, arrangers, and industrial workers.

The 2 3/4 cent mechanical royalty rate is far less than comparable rates in England, Australia, Japan and Western Europe.

Mechanical royalties paid in the period 1974-79 did not keep pace with record company gross revenues. [FN512]

FN512 Nathan Study, p. 27.

The evidence shows that in order to purchase today the same amount of goods which could have been purchased in 1909 for two cents, the copyright owner now needs 17.3 cents. The songwriter must have six songs recorded--if he is paid the full statutory rate of 2 [FN34] cents--to earn the same purchasing power per song per record that Congress afforded his predecessors in 1909. [FN513]

FN513 Ibid, p. 28.

We note that nothing in the statute compels copyright owners to give any discounts

to record companies. Nevertheless, the evidence shows that the copyright user in the past has successfully bargained for discounts from the statutory rate. The evidence shows that a majority of licenses are today issued at the statutory ceiling. The record reflects that pressures on copyright owners arising from the rampant inflation in the economy and the realization that their levels have fallen relative to those of other participants in the music industry, have made copyright owners more insistent on receiving ceiling and near-ceiling mechanical royalty rates for their musical compositions.

The Tribunal concurs with RIAA, that the NMPA Survey is not a reliable indicator of the financial condition or profitability of the music publishing industry. The survey may not include all income sources and the results may be distorted because NMPA may have aggregated noncomparable data. [FN514]

FN514 Tr. 10/19, pp. 36-37, 95-96, 117-118, 171-173.

The record reflects that each exhibit of the study constitutes a separate study. Because each of the respondents did not fill out the entire questionnaire, there are inconsistencies and discrepancies from exhibit to exhibit. In addition, the number of total respondents to each exhibit differs; [FN515] the identities of the respondents differ from exhibit to exhibit; [FN516] and it is not possible to trace the financial statements from one exhibit to another for a single group of companies. [FN517]

FN515 Ibid, pp. 122b-123a.

FN516 Ibid, pp. 124-125.

FN517 Ibid, pp. 123a-124.

As discussed above, we conclude that while it was valuable for the Tribunal to be aware of the financial status of copyright owners and users, the information we did receive provided us with no clear guidance as to how to balance fair return as against fair income.

International Comparison

The evidence shows that mechanical royalties are paid at a higher rate abroad than in the United States. Further, that mechanical royalties per album in most European countries and Japan are approximately double the royalties paid in the U.S. [FN518] The Nathan Study found no economic or policy justification for this disparity. Moreover, in all countries (other than Canada and the Soviet Union), the royalty payable is expressed as a percentage of price, to ensure that the statutory or negotiated rate maintains its purchasing power under inflationary pressure. [FN519]

FN518 NMPA, Table 20.

FN519 Nathan Study, pp. 40-41.

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.

The record reflects that the foreign comparison is relevant for a number of other reasons. First, rights of mechanical reproduction for sound recordings are licenses through most of the world as they are in the U.S., with copyright owners granting phonorecords nonexclusive rights to exploit copyright works in return for compensation in the form of royalties. [FN520] Second, large record producers are predominant in Western Europe and other parts of the world, as in the United States. [FN521] Third, music publishers play a similar role abroad as in the United States--as "the one hundred percent associate of the writer. ***10484** He is the one that gets an assignment from the writer * * * and * * * performs the duty of exploiting the work by all means and not only nationally but internationally." [FN522] Fourth, both here and abroad, the recorded music industry is dependent upon copyright owners for an essential input. The evidence in this proceeding shows that despite these substantial similarities, the market position of the copyright owner in the United States is much weaker than his colleagues abroad.

FN520 Tr. 6/3, pp. 13-14.

FN521 RIAA Exhibit, 1, 2.

FN522 Tr. 6/31, pp. 37-38.

The evidence also shows that the actual royalty payable to copyright owners whose songs are used in each of the BIEM member nations provides a benchmark against which to judge the 2 [FN34] cent rate--equivalent to a royalty of 27 [FN13] cents per L.P, assuming ten songs on a disc. The evidence was clear that against that benchmark, American copyright owners do not receive a fair return for the use of their creative efforts in their native land. [FN523]

FN523 NMPA Table 20; Tr. 7/10 , pp. 47-66; Tr. 6/4 , p. 69.

In reaching our determination in this proceeding, we found that an increase in the rate is justified in order to make the price paid for a tune in the United States comparable with what is paid elsewhere. There are differences between the markets in Europe and in the United States. Nevertheless, in Europe the rate is set by market forces, and this was seen as an indication that the U.S. rate has been too low.

Singer-Songwriter

The record industry has sought to make some point of the apparent earnings of the publishers controlled by singer-songwriters. [FN524] That position ignored the fact that singer-songwriters, who usually record the first and only use of their own songs, are not subject to the compulsory license in a legal or practical sense. The evidence shows that they can freely negotiate their entire royalty packages, including both artist royalties and mechanical royalties. As discussed above, by its terms the compulsory license system does not apply to the first release of a musical composition, and is triggered only in the absence of a negotiated license. [FN525]

FN524 RIAA Exh. VV.

FN525 17 U.S.C. § 115.

The evidence and history of the Act clearly shows that mechanical royalties received by singer-songwriters and their controlled publishers are not governed by the compulsory license. The evidence also shows that they are set by the contracts between singer-songwriters and record companies, and are entirely the product of bargaining.

The Tribunal thus concluded that because mechanical royalties are only a small part of the total contractual package between record companies and singer-songwriters, and these packages are the result of free negotiation, the amount of royalties singer-songwriters receive was not considered an issue.

Interest of the Consumer

We reject the claim that increasing the mechanical royalty rate would automatically force record companies to raise suggested retail list price. That claim is not supported by any probative evidence in the record.

The record industry argued that increases in royalties are different from other costs. They also argued that cost increases at the wholesale level are passed through, with a multiplier effect, to the retail level. The Tribunal finds that these arguments are not supported by any evidence in the record.

As noted above, increases in mechanical royalties are no different than increases in other record company costs. The evidence shows that since 1965, record companies have been able to absorb or pass on other cost increases totaling $1.49 per LP--during a time when mechanical royalties per LP increased only 3.5 cents, from 24 cents to 27.5 cents. The fact is, as a witness testified:

No specific cost results in a (price) increase. It's the aggregate of all of these costs that will generally contribute to a price increase. [FN526]

FN526 Tr. 81, p. 44.

It was claimed that increasing the mechanical royalty rate would be multiplied by the distribution chain, increasing cost to the consumer. [FN527] The evidence shows that increases at wholesale do not have an automatic multiplier effect through the distribution chain to the retail level. The evidence also shows that between 1965 and 1980, record companies increased their average margin per LP from 44 cents to $1.20--an increase of 76 cents. The record does not show why a 76 cent increase in the average profit margin cost the consumer $2.28 per album.

FN527 RIAA Exh. DD.

The evidence also shows that reductions in record company costs have not had a reverse multiplier effect, reflected in lower consumer prices. The record reflects what happened when 10 percent federal excise tax, levied on the wholesale price of

phonograph records, was repealed by Congress in 1965. In 1965, the tax came to about 19 cents per album--10 percent of the $1.90 wholesale price. The evidence shows that when Congress repealed the tax, its primary rationale looked to consumer protection, i.e. the tax was a regressive measure which had a disproportionate impact on low income consumers. [FN528]

FN528 H.R. Rep. No. 433, 89th Cong., 1st Sess. 25 (1965); S. Rep. No. 324, 89th Cong., 2d Sess. 29 (1965).

The evidence also shows that after repeal of the excise tax, according to RIAA's own analysis, record companies should have been able to lower the suggested retail list price by between 38 and 57 cents--based on RIAA's claims of a "multiplier" effect. The evidence shows that the industry did not pass the "multiplied" saving on to the consumer. Further that for a short time after repeal of the excise tax in June 1965, $3.98 suggested retail list prices were reduced by precisely the amount of the cost deduction, 19 cents, to $3.79.

The record reflects that there is not always an economic reason to increase suggested retail list price. [FN529] Stan Cornyn, of Warner Bros. Records testified:

FN529 NMPA Exh. 67; Tr. 8/6, pp. 89-90.

Well, we have raised some prices. It's an obvious answer and in my experience records that were once $3.98 or $4.98 when I started buying albums, it seems that over the years they have gone up a magic dollar every once in awhile.

And I find something remarkably different happening at this time. Usually when they have gone up, one manufacturer has announced it and somehow within 48 hours, the whole industry seems to be at that next level almost like the raising or lowering of the prime rate.

Somehow every bank in the country gets on that very quickly. And that happened when it went from $4.98 to $5.98. And clearly the viability of $7.98 was on the table for us a year or year-and-a-half ago. [FN530]

FN530 Tr. 7/1, p. 89-90.

The evidence further shows that if record companies raise their prices, there is no reason to expect that distributors and retailers will add on their percentage markups to such increases, so as to multiply the amount passed on to customers. Further that distributors' and retailers' markups cover their operating expenses and their profits. The evidence shows that their operating expenses are principally labor and space charges, which do not change as the prices of their goods increase. [FN531] Further that the same is true for retailers. The evidence also shows that like any businessmen, distributors and retailers increase their profits to the extent that competition and consumer price resistance will allow. [FN532]

FN531 Tr. 7/30, pp. 91-94.

FN532 Ibid, p. 94.

We find that there is no evidence in this record and no reason to believe that ***10485** record company price increases are dependent upon increases in mechanical royalties. Further it is clear that distributors and retailers do not automatically add a "markup" or "multiplier" to record company general price increases.

Determination of the Amount of the Royalty Adjustment

We determine that the evidence before this Tribunal conclusively demonstrates that there should be an immediate substantial increase in the mechanical royalty rate--to at least four cents per song--and that the rate should be adjusted annually to reflect increases in record prices.

The evidence shows that a comparison of evidence submitted to Congress during the period of copyright revision with evidence submitted to this Tribunal demonstrates that between 1955 and 1979 the "ceiling" of mechanical royalty payments--assuming that the statutory rate is paid on every song--declined. The record reflects that all parties agree that the purchasing power of the statutory rate has seriously eroded under inflationary pressure. Further that this erosion has become more severe since the 1950's, as inflation began to reach new levels. [FN533]

FN533 NMPA Chart A; Rinfret Study, Vol. 1, p. 22; Tr. 7/23, p. 90.

The evidence shows the market position of copyright owners has drastically deteriorated in absolute as well as relative terms. Likewise, the mechanical royalty rate has deteriorated relative to other record company costs. Evidence submitted shows that record company sales and promotion and general and administrative expenses have increased. [FN534]

FN534 Glober Report, pp. 47-48; James Fitzpatrick letter 7/17/80, Exh. 3.

Although we have concluded that aggregate statistics are less meaningful-- because the rate must be fair on an individual basis--industrywide statistics confirm the deteriorating market position of the copyright owner. Evidence in the record shows that in 1955, mechanical royalties were $11.04 million, slightly more than recording artist royalties of $10.21 million. The evidence also shows that by 1979, mechanical royalties were $117.7 million, barely one-fourth of recording artist royalties, which totalled $466.2 million. [FN535]

FN535 NMPA Table 10; NMPA Chart G.

The Tribunal concurs with Mr. Nathan's conclusion that increases in record sales volume do not compensate for the erosion of the mechanical royalty as a rate of return afforded copyright owners for the individual use of their songs by record manufacturers. [FN536]

FN536 Tr. 5/14, p. 61.

The record reflects that as a matter of economic fact, volume has not compensated for the erosion of the mechanical royalty rate. First, increases in sales volume in the period 1974 to 1979 have not kept pace with increases in the suggested retail

list price of phonerecords. During that period, average list prices increased from $4.91 to $7.09--or 44 percent. Likewise, average actual consumer prices increased from $4.05 to $5.79--or 43 percent in the five-year period. [FN537] Further shows that during the same five-year period, the number of songs sold increased from 4.5 billion in 1974 to 5.071 billion in 1979--barely two percent on average per annum. [FN538]

FN537 NMPA Table 15, 16.

FN538 Nathan Reply Comments, Table 13.

Second, the evidence shows that increases in sales volume in the period 1974 to 1979 have not kept pace with increases in the Consumer Price Index, which in that same five-year period increased from 147.7 to 217.4--or 47 percent. [FN539] The evidence also shows that although the volume of songs sold increased on average only two percent per annum over the last five years, record prices and the Consumer Price Index increased on average nine percent.

FN539 NMPA Table 15, 16.

The record reflects that an increase in the mechanical royalty rate as determined will have none of the dire effects predicted by the record industry. Further evidence is what happened in 1978 and 1979. The evidence shows that in 1978 the statutory rate increased for the first time in 69 years; the increase was approximately 40%. In 1979, a general recession began. The evidence shows that in 1979 there were budget cuts, firings, and reductions in the signing of new acts. In 1978 none of these things happened; indeed the evidence in this proceeding shows no adverse events at all in 1978. [FN540]

FN540 Cornyn, 7/1, pp. 21-22, 35-36, 54-55, 62-64; 7/2, 52-54; Butler, 6/26, pp. 72, 83, 88-90, 141-142; McCracken, 7/15, pp. 25-26, 75-77.

The record reflects the reason why the mechanical rate increase had no effect when compared to other industry expenses. The evidence shows that in 1979, after the statutory mechanical rate increase had become fully effective, other record industry expenses stood in the following relation to mechancial royalties;

Artists' royalties were 4 times as large.

Production and manufacturing expenses were 5 times as large.

Selling and promotion expenses were 4 2/3 times as large.

General and administrative expenses were 2 times as large. [FN541]

FN541 CRI Exhibit 1-3.

The evidence further shows that even a comparison of changes from 1977 to 1979, which gives undue emphasis to the single increase in the mechanical rate, indicates how trivial was that increase compared to other record industry expenses. [FN542]

Taking the entire record of this proceeding into consideration, we find there is no reason for this Tribunal to consider that future increases in mechanical royalty rates would be any more significant to the record companies than was the 1978 increases.

FN542 AGAC Cross Exh. 2.

The Adjusted Rate

The Tribunal has determined that the application of the statutory criteria to the evidence in this proceeding demonstrates that the mechanical royalty rate must be adjusted to either four cents, or three-quarters of one cent per minute of playing time or fraction thereof, whichever amount is larger, for every phonorecord made and distributed on or after July 1, 1981. We further determined that in order that the rate shall remain reasonable until this Tribunal may next convene rate adjustment proceedings in 1987, it is necessary to set the rate in a manner that will respond to changes in record prices.

A review of the entire record also shows that there is no evidence to support; no logic behind, and certainly no equity in, a rate which does not approach a reasonable rate. We, therefore, determined that any adjustment to the rate should and must be directly related to the retail list price of records, now and in the future.

Taking the entire record in this proceeding into consideration, we have determined to adjust the mechanical royalty upward from the rate adopted by Congress. The record shows that evidence was submitted to this Tribunal relating to changes in record prices since the last year for which Congress apparently had data to date.

We have determined that from the time that Congress apparently had such data, record prices increased substantially; we further determined that the 2 [FN34] cent existing rate has also seriously eroded under inflationary pressure. [FN543]

FN543 Economic Study of Average Retail Prices of LP's, Tapes and Singles from 1974-1979, submitted by RIAA, date April 7, 1980. Economic Study of the Record Industry for the Section 115 Rate-making Proceeding, prepared by Cambridge Research Institute for RIAA, April 7, 1980. NMPA Table 15. NMPA Table 2, NMPA's Dec. 15, 1980 letter to Commissioners Brennan and Coulter.

***10486** The Tribunal recognizes that Congress intended that the rates in the Act should not be regarded as precedents in future proceedings of this Tribunal. We have not in our determination, considered the rates established by Congress as precedential but we have taken them into consideration as a " benchmark of reasonableness."

We thus determined under the governing criteria of the statute and the evidence in this record, that the rate of 2.75 cent or 1/2 cent per minute of playing time, thereof established by Congress must be adjusted upward to either four cents, or three-quarters of one cent per minute of playing time or fraction thereof. The new rates shall become effective July 1, 1981 for every phonorecord made and distributed

after that date.

We further determined that in order to ensure the copyright owners a continuous fair return, the above rate must be adjusted annually. The adjustment shall only take place if the record industry increases, during any 12 month period, the average suggested retail list price of records.

On December 1, of each year, beginning in 1981, the Tribunal shall publish in the Federal Register a notice of any further changes in the rate which shall be directly proportionate to the change, if any, in the average suggested retail list price of albums between the twelve-month period ending October 31, of the preceding year and the twelve-month period ending October 31 of the year in which the notice is published.

We determined from the evidence in this record that the use of suggested retail list price is a "total prevailing" industry practice in the United States record industry. [FN545] The evidence before us did not disclose a single example of a single phonorecord made and distributed in the United States without a suggested retail list price.

FN545 Tr. 6/19, pp. 18-19.

The evidence shows that most record companies in the United States, including all of the major companies with the exception of CBS and Capitol, use suggested retail list price as the basis for computing royalties payable to recording artists and procedures. [FN546] The evidence also shows that many record companies are currently obliged, by existing contracts, to maintain suggested retail list price at a fair level, consistent with its accepted meaning in the industry.

FN546 Tr. 7/2, pp. 86-89.

The record shows that the question has been raised regarding the possibility that suggested retail list price will be abandoned in this country. The evidence shows, however, that the extensive use of suggested retail list price in artist royalty contracts and in marketing practices, makes that prospect highly unlikely. The record also shows that the record industry would disrupt its own industry practices if it chooses to abolish suggested retail list price.

The Tribunal determined that if a particular record company abandons suggested retail list price, the annual adjustment shall be based on change in the average wholesale price of albums for the corresponding periods.

We further determined that in the event a different configuration of phonorecords becomes the predominant configuration of phonorecords made and distributed in the United States, changes in the average suggested retail list price or average wholesale price of that configuration shall be used as the basis of the adjustment.

We further determined that the average suggested retail list price or average wholesale price shall be determined by the Tribunal from Tribunal conducted surveys and/or studies. Further, that persons affected by an adjustment will have the op-

portunity to submit comments, surveys, studies, or recommendations to the Tribunal for consideration. In addition, voluntary agreement on an adjusted rate by parties affected, can be submitted for the Tribunal's consideration.

The Tribunal determined that the transitional provision followed by Congress equitably balanced the interests of copyright owners and copyright users. We found that to apply the new rates to phonorecords made and distributed after the effective date of any royalty adjustment is less disruptive to the industries and is in accordance with current generally prevailing industry practices.

Conclusion

In considering a reasonable adjustment of the mechanical royalty rate for the compulsory license, the Tribunal considered all the relevant evidence in the record. We recognized that a still raging inflation has occurred since the last year for which Congress apparently had financial data.

We find that the record companies, the copyright users, are able to increase the price of their products to insure theirselves a fair income. On the other side, however, the songwriters and their music publishers, the copyright owners, suffer an unreasonably low mechanical royalty, payable at an ever diminishing rate in real dollars. We, therefore, conclude that as a matter of substantial evidence of record, the 2 3/4 cent statutory rate is unreasonably low and does not implement the statutory criteria.

Based on our consideration of the entire record of this proceeding: our consideration of the evidence which has occurred since the last year for which Congress apparently had financial data; our consideration of the average retail list price evidence; and our consideration of the inflationary rate evidence, we conclusively find that an adjustment of the royalty to four cents with annual adjustment is warranted as of July 1, 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 fact that an increase in the rate will increase costs is not per se an argument against raising the rate. There have been benefits to others from cost and price increases in the past without any benefit to the copyright owner.

We further conclude that under the controlling criteria and substantial evidence of record that an upward adjustment to four cents with annual adjustment as adopted by this Tribunal in its final determination on December 19, 1980 and published in the Federal Register of January 5, 1981 (45 FR 891) is warranted.

Note.--Commissioners James, Brennan, Coulter and Garcia concurred in the above opinion. Commissioner Burg has written minority views.

Clarence L. James, Jr.,

Chairman, Copyright Royalty Tribunal.

January 29, 1981.

Minority Views of Commissioner Burg

I disagree with and dissent in the decision to adjust the rate of royalty payable under compulsory license for making and distributing phonorecords to four cents for each work embodied in the phonorecord, or three-quarters of one cent per minute of playing time or fraction thereof, subject to annual adjustments based on the change, if any, in the average suggested retail list price of albums.

In my opinion an increase in the flat rate of this magnitude, more than 45% over a rate that has been in effect for three years, coupled with a yearly adjustment which in all probability will have an immediate multiplier effect, ignores the statutory criteria, particularly 17 U.S.C. 801(b)(1)(B) which admonishes the Tribunal "to afford the copyright owner a fair return for his creative work and the copyright user a fair income under existing economic conditions." I do not believe the function of this Tribunal, the 1980 royalty rate review as mandated by Congress, is to redress inequities, real or imagined retroactively. I am persuaded that ***10487** when Congress enacted the 37 1/ 2 % increase in the mechanical rate in 1976 it was aware of and took into consideration the 1978 effective date of the revised legislation, and the subsequent review by the Tribunal in 1980. The evidence in this proceeding is incontrovertible that Congress reviewed the financial data of the record industry through calendar year 1974, and set the 2 3/4 cents rate accordingly.

Therefore, my initial preference was to designate 1978 or 1980 as the base year, increase the mechanical rate to 3.25 cents per tune effective January 1, 1982 and provide upward adjustments in 1984 and 1986. Consequently in an effort to embrace the resolution I indicated I would accept 1975 as the base year, a year which also can be supported by the evidence in this proceeding, and a year which would have produced a rate of 3.6 cents per tune. I would have accepted periodic adjustments reflecting the change in record prices. However I am opposed to annual adjustments as being unavoidably disruptive on generally prevailing industry practices, which in my opinion ignores the statutory criteria, 17 U.S.C. 801(b)(1)(D).

Furthermore the package increase adopted by the majority will without question be borne by the consumer, triggering a substantial and unnecessarily excessive cost impact.

To conclude I strongly believe this mechanical rate increase to 4 cents per tune with yearly adjustments cannot be supported by the record in this proceeding and is indefensible in the light of commercial realities.

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