UNITED STATES COPYRIGHT ROYALTY JUDGES

The Library of Congress

In re **DETERMINATION OF ROYALTY RATES AND TERMS FOR EPHEMERAL RECORDING AND WEBCASTING DIGITAL PERFORMANCE OF SOUND RECORDINGS (Web-IV)**	**Docket No. 14-CRB-0001-WR (2016-2020)**

ORDER DENYING IN PART SOUNDEXCHANGE'S MOTION FOR REHEARING AND GRANTING IN PART REQUESTED REVISIONS TO CERTAIN REGULATORY PROVISIONS

I. Introduction

On December 31, 2015, SoundExchange, Inc. (SoundExchange) filed a Motion captioned "Petition for Rehearing" (Motion), seeking rehearing of certain findings in the December 16, 2015 Determination (Determination) issued by the Copyright Royalty Judges (Judges). On January 4, 2016, the Judges entered an Order *sua sponte* permitting other parties to respond to the Motion and permitting SoundExchange to reply. On January 12, 2016, the Judges received opposing papers filed by iHeartMedia, Inc. (iHeart), the National Association of Broadcasters (NAB) and Pandora Media, Inc. (Pandora) (iHeart Opposition, NAB Opposition, and Pandora Opposition, respectively). On January 19, 2016, the Judges received a submission from Mr. George Johnson dba GEO Music (GEO) supporting the SoundExchange Motion.[1] On January 19, 2016, SoundExchange filed its Reply.

II. The Legal Standard for Rehearing

Under the Copyright Act (Act), the Judges may order a rehearing after a determination only in "exceptional circumstances." 17 U.S.C. § 803(c)(2). The regulations implementing the statute provide that the Judges may grant a motion for rehearing upon a showing that an aspect of the determination is "erroneous." 37 C.F.R. § 353.1. The moving party must identify the aspects of the determination that are "without evidentiary support in the record or contrary to legal requirements." 37 C.F.R. § 353.2.

The Judges' prior orders provide that they shall grant rehearing only "when (1) there has been an intervening change in controlling law; (2) new evidence is available; or (3) there is a

[1] On January 21, 2016, the Judges also received GEO's separate Motion for Rehearing (captioned as a "Petition") dated January 14, 2016. The Judges shall enter a separate order on GEO's Motion.

need to correct a clear error or prevent manifest injustice." *See, e.g., Order Denying Motion for Rehearing* at 1 (Docket No. 2006-1 CRB DSTRA (Jan. 8, 2008) (*SDARS I Rehearing Order*) (applying standard for federal district courts under *Fed. R. Civ. P.* 59(e) detailed in *Regency Comm., Inc. v. Cleartel Comm., Inc.*, 212 F. Supp. 2d 1, 3 (D.D.C. 2002)).

The Judges have cautioned that a motion for rehearing "must be subject to a strict standard in order to dissuade repetitive arguments on issues that have already been fully considered by the [Judges]." *Order Denying Motions for Reh'g*, Docket No. 2005-1 CRB DTRA, at 1-2 (Apr. 16, 2007). This holding is consistent with the position of the U.S. Supreme Court, which has held that such a motion does not provide a vehicle "to re-litigate old matters, or to raise arguments or present evidence that could have been raised prior to the entry of judgment." *Exxon Shipping Co. v. Baker*, 554 U.S. 471, 485 n.5 (2008) (quoting C. Wright & A. Miller, *Federal Practice and Procedure* § 2810.1 (2d ed. 1995)). In that vein, the Judges have ruled that a party cannot use the rehearing process to seek a "second bite at the apple" by which it "present[s] theories and arguments that could have been advanced earlier." *SDARS I Rehearing Order* at 1-2 (quoting *Fresh Kist Produce, LLC v. Choi Corp.*, 251 F. Supp. 2d 138140 (D.D.C. 2003)); *see Order Denying Motions for Rehearing* at 2, Docket No. 2005-1 CRB DTRA (Apr. 16, 2007) (motions for rehearing not for "change of tactics for a party to present a new theory or evidence after the trial is concluded.").

SoundExchange contends that certain of the Judges' decisions in the Determination constituted "clear error." *See, e.g.*, Motion at 2, 5, and 8-10. Namely, SoundExchange asserts that the Judges erred in (1) "blending" rates appropriate for major record labels (Majors) and independent record labels (Indies); (2) establishing the annual rate escalator; (3) discounting the effect of the statutory rate "shadow" on determining rates that would be negotiated by willing buyers and willing sellers; and (4) adopting certain regulations.

III. SoundExchange Fails to Demonstrate Error in the Majors-to-Indies Ownership Ratio Applied by the Judges.

A. A SoundExchange Exhibit Supports the Ownership Ratio

SoundExchange asserts that the royalty rate the Judges set under section 114 of the Act for noninteractive streaming services is based on an inaccurately determined "blending" of effective rates paid to Majors and Indies under benchmark agreements in the noninteractive market. Motion at 1-2 (citing *Determination* at 200). However, the so-called "blending" to which SoundExchange refers is based upon the Judges' reliance on SoundExchange's own exhibit, which indicated that approximately 65% of sound recordings performed on Pandora, the leading noninteractive streaming service, were owned by one of the three Majors, and approximately 35% were owned by Indies. *See* SX Ex. 269 at 73.

At the hearing, SoundExchange relied successfully on the same document—including the data analysis on the immediately following page (p. 74) of SX Ex. 269—to convince the Judges that the Majors' ownership share of "top spins" was sufficiently great to rebut the argument of Pandora's economic expert, Dr. Carl Shapiro, that the per-play value of the repertoires of all sound recordings in the market should be deemed equal. *See Determination* at 132 and nn.152-53. Further, as the NAB notes, SoundExchange placed particular emphasis on SX Ex. 269. NAB Opposition at 2. More particularly, in closing argument, SoundExchange's counsel stated that SX Ex. 269 was a "very important document that I would encourage you to look at carefully." 7/21/15 Tr. 7750 (attorney Pomerantz).

The relative market shares of the Majors and the Indies was an important issue in the proceeding, affecting the weight the Judges placed on proposed benchmarks. Therefore, when SoundExchange introduced an exhibit that estimated the respective market shares, it was reasonable for the Judges to rely on those percentages in determining appropriate royalty rates. Accordingly, based on that evidence, the Judges established a "zone of reasonableness" that relied on the Indie benchmark rate of $0.[redacted] as the low end of the zone and the Majors benchmark rate of $0.[redacted] as the high end of the zone. The Judges selected an intermediate rate of $0.0017, as the statutory rate, within that zone of reasonableness, giving due weight to the relative market shares of the Majors and Indies.

For these reasons, the Judges reject SoundExchange's attempt to seek rehearing by seeking to diminish the importance of its own exhibit.

SoundExchange asserts it is not merely attempting to diminish, distinguish, or disavow its own exhibit. Rather, according to SoundExchange, "[t]he right measure" is "'distributed' shares, *i.e.*, shares of recordings that [M]ajors and [I]ndies distribute," not "owned" shares. Motion at 2. In the rehearing Motion, SoundExchange argues that when a Major distributes Indie sound recordings to streaming services, the services pay the Majors' royalty rate. *Id.* SoundExchange asserts the evidence indicates that the Majors distribute approximately 85% of sound recordings to noninteractive streaming services, whereas the Indies distribute only 15%. *Id.* at 3. Applying that ratio, SoundExchange argues that the appropriate rate under the Judges' methodology should have been a different rate *within the same zone of reasonableness* that the Judges established based on the totality of the evidence in record of the proceeding: $0.0018 rather than $0.0017, a $0.0001 difference. *Id.* at 3.

Assuming *arguendo* that SoundExchange is not seeking a rehearing by diminishing, distinguishing, or disavowing its own exhibit, the Judges find the remainder of SoundExchange's arguments to be incorrect, and certainly insufficient to satisfy the standard for rehearing.

B. SoundExchange Failed to Argue at the Hearing that Distribution Agreements Affected the Royalty Rates Paid to Indies by Noninteractive Services

In its Opposition, Pandora correctly notes that SoundExchange failed to argue during the hearing that royalty rates for sound recordings owned by Indies, but distributed by Majors, would or should be affected by distribution agreements between Indies and Majors. Specifically, Pandora notes:

> SoundExchange carefully avoided making the argument it now presses.… When SoundExchange critiqued the Merlin agreement as non-representative of a major-label agreement, it did so in terms of ownership, not distribution, arguing that "the Merlin license only covers independently-*owned* sound recordings" and that "sole reliance on the Merlin license only offers information about the value of independently-*owned* sound recordings."

Pandora Opposition at 3 (emphasis in original).

The Judges agree with Pandora. SoundExchange did not argue this point during the hearing.[2] A motion for rehearing is procedurally too late for assertion of a substantive argument.

In its Reply, SoundExchange claims its argument is timely because no party suggested during the proceeding that the Judges should blend a statutory rate as they did in the Determination. Reply at 1. That claim is clearly off the mark. SoundExchange was on notice that the rate-setting process can require the Judges, in their discretion, to identify a statutory rate within a zone of reasonableness, as informed by the parties' evidence and arguments. Identification of that rate within the zone may result from blending, averaging, or other reconciliation of the several benchmarks. More particularly, SoundExchange is well aware that the Judges have consistently applied useful disparate benchmarks to create a "zone of reasonableness" within which they reconcile market evidence to set the statutory rate. *See, e.g., Beethoven v. Librarian of Cong.*, 394 F.3d 939, 948 (D.C. Cir. 2005) (affirming decision under § 114(f)(2)(B) to set sound recording performance rate using both "mid-point" and "blended rate").

Notably, the Judges specifically criticized SoundExchange's benchmark in the preceding webcasting proceeding for failing to account for the "approximately 40% of the music streamed on noninteractive webcasts owned and licensed by independent labels." *Determination of Royalty Rates for Digital Performance Right in Sound Recordings and Ephemeral Recordings,* Docket No. 2009-1 CRB Webcasting III, 79 Fed. Reg. 23102, 23118 (Apr. 25, 2014) *(Web III Remand)*.

Further, SoundExchange's own economic expert, Dr. Daniel Rubinfeld, made adjustments to account for the separate value of Indie recordings in order to blend Major and Indie rates to arrive at a proposed statutory rate. Rubinfeld CWDT at 53 and ¶¶ 220-225. Another SoundExchange economic expert, Dr. Eric Talley, testified that the Judges should look at all the useful benchmarks and identify some central tendency, such as the "mean," to blend those disparate benchmarks. SX Ex. 19 at 34-35 (Talley WRT) ("[O]ne should expect to observe a range of prices from such benchmark transactions, suggesting that an appropriate benchmark is unlikely to consist of a single example or specimen price, but rather *some aggregated assessment of the range of benchmark prices (such as median or mean).* Fixating on a single benchmark … would therefore be imprudent.") (emphasis added).

SoundExchange must have, and reasonably should have, understood that it needed to make all available arguments to diminish the evidentiary value of a benchmark. If SoundExchange believed a benchmark was too low or otherwise deficient, it should have argued for (1) rejection of that benchmark in order to constrict the low end of the zone of reasonableness, (2) blending with other benchmarks to diminish its impact, or (3) inclusion of the challenged benchmark in any other measure of central tendency, such as a mean value, also to blunt its impact. SoundExchange did not advocate use of a distribution ratio at the hearing to

[2] To the extent SoundExchange is asserting that it did raise this issue through the oblique reference to the distribution issue in Dr. Rubinfeld's testimony, that argument is insufficient to support SoundExchange's rehearing Motion. *See* section III(C), *infra*. Even if SoundExchange had raised this point properly during the proceeding, the Judges would have rejected the argument based on the record evidence taken as a whole. *See* sections III(D)-(G), *infra*.

adjust the benchmark rates within a zone of reasonableness. It cannot use the rehearing process to raise this issue for the first time.

In sum, the Judges did not commit any error on this basis, as SoundExchange did not make this argument during the hearing.

C. The Judges Did Not Err in Their Consideration of Dr. Rubinfeld's Testimony on the Topic of Ownership versus Distributional Market Shares

In its Motion, SoundExchange points to Dr. Rubinfeld's testimony to support its claims that it presented an 85:15 distribution ratio during the hearing and that the Judges clearly erred by failing to rely on that ratio in selecting a rate within the zone of reasonableness. Motion at 2 n.3. More particularly, SoundExchange relies on the following excerpt from Dr. Rubinfeld's testimony:

> I note that Nielsen Soundscan indicated that the 2013 market share of independent record companies [Indies] by ownership of sound recordings was nearly 35%. I also note that a substantial portion of those sound recordings were distributed by [M]ajor labels.

SX Ex. 17 ¶ 224 (Rubinfeld CWDT).[3] This testimony does not disclose, let alone support, the 85:15 distribution ratio that SoundExchange urges in its Motion.

SoundExchange attempts via rehearing to demonstrate the percentage of Indie sound recordings distributed by the Majors. Specifically, at page 3 of its Motion, SoundExchange avers that Dr. Rubinfeld relied on "*Billboard* data showing that [I]ndies control 12.3% of sound recordings based on distribution." However, Dr. Rubinfeld never mentioned in his testimony any reliance on that 12.3% figure. Rather, he cited the *Billboard* article only as support for the "nearly 35%" Indie "market share." *Id.* ¶ 224. Moreover, as the NAB notes, the *Billboard* article on which SoundExchange's rehearing argument rests was not in evidence. NAB Opposition at 3.

Further, Dr. Rubinfeld testified that under his proposed benchmark—*and despite the other evidence on which SoundExchange now relies to support its 85:15 ratio argument*—the Indies accounted for 24% of the interactive streams he had examined. Rubinfeld CWDT ¶ 225.[4] Based on that opinion, Dr. Rubinfeld utilized the same 76:24 ratio for the noninteractive market. Inexplicably, in its Motion, SoundExchange ignores this aspect of Dr. Rubinfeld's opinion.[5] If

[3] The first sentence quoted in the accompanying text containing the "nearly 35%" figure was sourced to a Billboard article. *See* SX Ex. 17 n.131. The second sentence asserting that "a substantial portion of those sound recordings were distributed by [M]ajor labels" was unsourced. Dr. Rubinfeld further cited an a2im.org web statement dated September 23, 2014 (also not in evidence), confirming only the Indies' 34.6% market share. *Id.* (a2im is a not-for-profit trade organization representing a coalition of independently owned U.S music labels. *See* SX Ex. 469 at 2.)

[4] Dr. Rubinfeld's CWDT actually states that the Indies accounted for "76%" of those streams. *Id.* However, the Judges understand that figure to be a mistake, and that Dr. Rubinfeld transposed the 76:24 Major-to-Indie ratio that he had determined.

[5] In its Reply at 1, n.2, SoundExchange acknowledges Dr. Rubinfeld's 76:24 ratio, but disavows that figure because it references the non-statutory interactive market where Indies supposedly receive compensation comparable to that received by a Major. As discussed at section (III)(G) *infra*, the fact that the value of the Indies' repertoires was substantially less than the value of the Majors' repertoires *in the noninteractive market* actually undercuts SoundExchange's rehearing argument.

SoundExchange had continued to rely on its expert's opinion on rehearing, rather than create a new 85:15 ratio, a mathematical application of Dr. Rubinfeld's 76:24 Major-to-Indie ratio would have led the Judges to the same statutory rate, $0.0017.[6]

The Judges agree with Pandora: "The proposed [85:15] split is nowhere to be found in SoundExchange's post-trial briefing …." Pandora Opposition at 4. As the NAB similarly points out, although SoundExchange noted during the hearing that the 65% share pertained to Major ownership percentage rather than distribution percentage, "it nowhere sought to quantify the distribution percentage." NAB Opposition at 3. Thus, there was no evidence or argument regarding any pure distribution percentage, let alone an 85:15 ratio. Rehearing is not an opportunity for a party to introduce new tactics, new theories, or new evidence.

Finally, it is important to note that SoundExchange simply ignores the fact that the Judges explicitly found Dr. Rubinfeld had failed to link "logically or evidentially" the percentage of Indie sound recordings distributed by the Majors to the determination of a benchmark royalty rate. *Determination at* 54, n.89; *see* Pandora Opposition at 4. That is, whatever percentage accurately reflects the relative percentages for the distribution of sound recordings, SoundExchange does not argue in its Motion that the Judges "clearly erred" (or that they erred at all) in finding no logical or evidentiary basis for Dr. Rubinfeld's reference to the (unquantified and unsourced) percentage of distributed sound recordings. SoundExchange's failure to challenge this finding is alone sufficient to deny this aspect of its Motion.[7]

D. The Testimony of Darius Van Arman does not Demonstrate Error in the Determination

SoundExchange attempts to rely on the testimony of its witness Darius Van Arman, owner of the Indie, Secretly Group,[8] to support SoundExchange's contention that the Judges should have used distribution share rather than ownership share in deriving the applicable per-play rate.[9] SX Ex. 20 (Van Arman WDT). Mr. Van Arman testified: "*While I cannot say for certain how large that percentage is*, I do know that a substantial portion of independently-owned sound recordings are digitally distributed by one of the three [M]ajors." Van Arman WDT at 7 (emphasis added).[10] Preliminarily, it is notable that in the passage of Van Arman's testimony SoundExchange quotes in its Motion, Mr. Van Arman does not attempt to estimate the percentage of Indie-owned sound recordings distributed by the Majors.

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[6] [$0.[redacted] x .76] + [$0.[redacted] x .24] = $0.001444 + $0.000288 = $0.00173 (or $0.0017 rounded). It is also worthy of note that SoundExchange's proposed 85:15 ratio would result in a rate of $0.0018 only because of a rounding change. That is, [$0.[redacted] x .85] + [$0.[redacted] x .15] = $0.001615 + $0.00018 = $0.001795. Thus, it appears that SoundExchange benefited by ignoring its own expert's ratio and using instead the unsourced, uncited, ambiguous and nested RIAA reference to an 85:15 ratio, which "moved the needle" to the next one-hundredth of a cent through rounding. *See* section III(D), *infra.*

[7] In light of the Judges' finding in the Determination that SoundExchange did not "logically or evidentially" link Dr. Rubinfeld's comment regarding distribution to the valuation issue or to the setting of a particular Major-to-Indie ratio, it is clear that SoundExchange cannot re-argue this issue via rehearing.

[8] Mr. Van Arman was also a member of the a2im Board of Directors.

[9] *See* SoundExchange Motion at 2, n.4.

[10] SoundExchange omitted from its Motion the italicized portion of the quoted testimony.

SoundExchange further quotes Mr. Van Arman's testimony, in which he states that when an Indie uses a Major for distribution, "*generally* it is the terms of the [M]ajor's license with a digital music service that governs the rates and terms for distribution of those sound recordings." *Id.* (emphasis added). Once again, Mr. Van Arman's *general* testimony is not cast in terms of percentages, or even estimates of percentages, so it fails to support SoundExchange's assertion of an 85:15 distribution ratio. At most, it indicates that some Indies use some Majors to distribute some sound recordings.

Moreover, in that same testimony, Mr. Van Arman indicates that the foregoing testimony regarding "rates" relates to the *cost of distribution*. *Id.* at 8 ("[A]n [Indie] may choose to handle its own distribution rights [to] save the [Indie] from paying *a distribution fee to the [M]ajors.*") (emphasis added). The Judges reject any argument that suggests they erred by declining to infer from this testimony that Mr. Van Arman was claiming that an Indie distributing to a Service through a Major receives from the Service the same *royalty rates* that the Major may have established in its direct deal with a Service.

More pointedly, for purposes of the present Motion, SoundExchange never attempted at the hearing to explain if or how the distribution relationship between Indies and Majors affected the royalty rates Indies received in their direct deals (including the Pandora/Merlin Agreement).

Additionally, SoundExchange ignores the fact that Mr. Van Arman's testimony distinguished between physical distribution and digital distribution, noting that Indies were relatively less reliant on the Majors for digital distributions, over which they were more likely to retain digital distribution rights. *See* iHeart Opposition at 2-3 (and record citations therein). Given that a section 114 proceeding establishes rates for the licensing of *digital* sound recordings, this distinction further undercuts SoundExchange's reliance on Mr. Van Arman's testimony.

SoundExchange also seeks to bootstrap testimony by Mr. Van Arman on June 25, 2014, to the U.S. House of Representatives Committee on the Judiciary Subcommittee on Courts, Intellectual Property and the Internet. Motion at 3 (citing SX Ex. 469). In that Congressional testimony, Mr. Van Arman referred to a statistic on an uncited website and in uncited regulatory filings purportedly reported by the Recording Industry Association of America (RIAA) asserting "the three major record companies … create, manufacture and/or distribute approximately 85% of all legitimate recorded music produced and sold in the United States." *Id.* at 5. SoundExchange uses this uncited statistical excerpt of Congressional testimony in its Motion and asserts that the excerpt supports the use of an 85:15 ratio between Major and Indie recordings for purposes of selecting the statutory rate within the zone of reasonableness. Motion at 3.

However, that information hardly supports SoundExchange's request for rehearing. First, the statistical reference does not distinguish between the distribution of digital and physical product or, more specifically, between digital sales and streams, or, even more granularly, between interactive and noninteractive Services. Second, it lumps the "manufacture" and "creat[ion]" of sound recordings with distributions, rendering the statistic unhelpful in confirming a separate percentage for distributed noninteractive digital recordings, the only relevant data for purposes of the calculation that SoundExchange now challenges. Finally, a further review of Mr. Van Arman's Congressional testimony, SX Ex. 469, reveals that Mr. Van Arman testified, generally, when the Majors cite the percentage of sound recordings they *distribute* they are "misrepresenting their market share figures" and "copyright ownership is the only appropriate market share definition." SX Ex. 469 at 5 and n.1 (Van Arman Congressional Testimony at 4 and n.1).

In sum, nothing in Mr. Van Arman's testimony indicates that the Judges erred by utilizing the 65:35 Major-to-Indie ownership ratio, rather than the asserted 85:15 distribution ratio, in selecting a statutory rate within the zone of reasonableness.

E. The Testimony of Dr. Michael Katz does not Demonstrate Error in the Judges' Determination

SoundExchange asserts that Dr. Michael Katz, the NAB's economic expert, confirmed that the Majors distributed approximately 85% of sound recordings. Motion at 3. In support of this assertion, SoundExchange relies on NAB Ex. 4000 ¶ 70 (Katz WDT). In that testimony, however, Dr. Katz clearly was quoting an excerpt from the *Web III Remand*, in which the Judges cited a prior SoundExchange witness, Dr. Michael Pelcovits, for the proposition that, as of 2010 when he testified, the Majors "*owned* approximately 85% of supply (the sound recordings)." *Web III Remand* at 23113 (emphasis added). Dr. Katz's statement in *Web IV* referring to someone else's five year-old testimony regarding then historic *ownership* shares cannot support SoundExchange's assertion that the Judges' 2015 Determination relying on contemporaneous data and evidence was erroneous.

F. The Testimony of Dr. Shapiro does not Demonstrate Error in the Judges' Determination

SoundExchange claims Dr. Carl Shapiro, Pandora's economic expert, "acknowledged" that the 65:35 shares "are not representative of the [M]ajor-[I]ndie split on other services." Motion at 2, n.3 (citing Shapiro WDT at 13, n.19). In that testimony, what Dr. Shapiro actually said was that "[t]he share of performances at Pandora attributable to music from the major record companies is less than their share on *terrestrial radio, and thus also less than their share for simulcasters.*" Shapiro WDT at 13, n.19 (emphasis added). The fact that the Majors' noninteractive share may be less than their share on terrestrial or simulcast services does not diminish the value of the 65:35 figure in the custom noninteractive market. Further, even if the simulcast share is different, SoundExchange offered no evidence of that ratio; rather it relied upon the intermediate 76:24 ratio that its own expert, Dr. Rubinfeld, adopted in his testimony.

This excerpt of Dr. Shapiro's testimony does not support SoundExchange's claim of judicial error.

G. The Alleged Impact of Asserted Contractual Grants of Distribution Rights by Indies to Majors does not Support SoundExchange's Request for Rehearing

In its Motion, SoundExchange relies on certain language in the iHeart/Warner Agreement to support its rehearing assertion that the appropriate Major-to-Indie ratio to use in setting the statutory rate within the zone of reasonableness is 85:15. More particularly, SoundExchange argues that the iHeart/Warner Agreement, SX Ex. 33, is exemplary of the fact that an Indie distributing sound recordings through a Major (or its affiliate) "*generally*" gets paid pursuant to the Majors' deals with such Services. Motion at 2 (emphasis added). In opposition, iHeart asserts: (1) SoundExchange "misconstrues" the iHeart/Warner Agreement because Warner lacks the contractual right to set royalties with regard to "some music that it otherwise distributes"; and (2) SoundExchange fails to note the record evidence that Indies *"often"* do not grant digital distribution rights to Majors. iHeart Opposition at 2-3 and n.3 (and record citations therein) (emphasis added). In its Reply, SoundExchange does not dispute iHeart's assertion that SoundExchange has misconstrued the iHeart/Warner Agreement in this regard.

The Judges find that SoundExchange has not demonstrated a right to rehearing based on its post-hearing interpretation of the iHeart/Warner Agreement. The Judges note that at no time during the proceeding did SoundExchange argue that royalty rates established contractually in direct licenses between Indies and noninteractive services could be, or have been, superseded by the royalty rate contained in the distribution agreements or distribution clauses of contracts between Majors and Services, (such as the iHeart/Warner Agreement). Even assuming *arguendo* that provisions in the iHeart/Warner Agreement allow Indies to exact royalties at Warner's royalty rate, SoundExchange fails to identify any evidence in the record that the provisions upon which SoundExchange relies in the iHeart/Warner Agreement are typical of provisions in agreements between Majors and services. As the NAB correctly notes, "SoundExchange points to no evidence that an independent label whose recordings are distributed by a major label would be unable to enter into its own direct licenses in order to encourage services to steer towards it," and that "Dr. Rubinfeld's testimony indicates that independents that are distributed by major labels have the option to make their own deals." NAB Opposition at 2 (citing Rubinfeld CWDT ¶ 222). Given these evidentiary points, SoundExchange cannot utilize the rehearing process to obtain a "second bite at the apple" by which it "present[s] theories and arguments that could have been advanced earlier." *Id.* at 1-2.[11]

Further, the record of the proceeding does not reveal a basis to calculate or reasonably estimate the difference, if any, between SoundExchange's assertion that Indies *generally* get paid the Major rate when the Major engages in digital distribution on their behalf, and iHeart's position that *some* Indies do not convey to Warner (as a distributor) the right to set royalties, and in fact *often* do not grant digital distribution rights to Majors.

In its Reply, SoundExchange seeks to recast the economic substance of this argument more bluntly. SoundExchange asks: "[W]ould an [I]ndie whose music is distributed … by a [M]ajor opt to have the [M]ajor distribute to streaming services … at the $0.[redacted] rate, or would the [I]ndie opt to distribute itself at the lower $0.[redacted] rate?" SoundExchange Reply at 1. This question is irrelevant (or, to put it colloquially, a "loaded question"), because an Indie would not have such a choice, based on SoundExchange's own contrary economic argument during the proceeding vis-a-vis the relative values of Major and Indie sound recording repertoires.

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[11] Clearly SoundExchange could have made its present contract-based argument regarding the Major to Indie ratio during the proceeding, as it was well aware that there was a need to consider the ratio of Major and Indie sound recordings, and it did apply such a ratio through its economic expert. *See* Rubinfeld CWDT at 53 and ¶¶ 220-225 (noting need for "[a]djustment for independent record company deals and streams."). SoundExchange's failure at the hearing to make this argument regarding the purported impact of distribution agreements on rates is surprising, given SoundExchange's present emphasis on the importance of the issue. For example, SoundExchange certainly could have made an argument as to why the Pandora/Merlin rate supposedly was less consequential than the Services urged, to the extent those rates supposedly were superseded or otherwise "washed out" by the distribution agreements between Indies and the Majors. Moreover, if there was such a "washing out" of direct deal rates such as in the Pandora/Merlin Agreement, it is difficult to understand why Pandora and Merlin would have agreed to incur the expense of negotiating and monitoring such a deal, and of building the architecture to perform their steering deal, if the tradeoff of lower rates could be eviscerated by the Indies' distribution agreements with Majors. These issues were never developed because SoundExchange never made this argument during the hearing. That issue cannot be raised for the first time on rehearing.

Specifically, SoundExchange argued *during the proceeding* that:

(1) the evidence from multiple agreements between record companies and noninteractive streaming services showed that "[i]n direct license situations, the noninteractive service provided *better rates and terms to the [Majors] than the same service provided in direct licenses with [Indies].*" SX PFF ¶ 653 (emphasis added).

(2) [redacted]'s direct licenses demonstrate exactly that: "[redacted], a [M]ajor, has received *better rates … than the [Indies]* who executed direct licenses with [redacted], both before and after the [redacted] [Agreement] … [A] comparison of those licenses … reveals that [redacted] *received better rates and terms than [Indies].*" SX PFF ¶ 654 (emphasis added).

(3) "[T]he evidentiary record concerning Apple's licenses with Sony, Warner, and [Indies] for its iTunes Radio service demonstrates that *[the [M]ajors … receive considerably more consideration than [the Indies].* SX PFF ¶ 655 (emphasis added).

(4) Summing up, SoundExchange concluded that "[t]hose licenses … confirm that *[Majors] receive more consideration than [Indies] when negotiating directly for licenses covering non-interactive services.*" SX PFF ¶ 656 (emphasis added).

See also SX RPFF ¶ 734 (reemphasizing these points and noting they were not disputed by Pandora).

Moreover, SoundExchange relied on the difference in value between the repertoires of Majors, on the one hand, and Indies, on the other, to argue successfully that the statutory rate should not be based merely on the benchmark rate paid by Indies. *See Determination* at 110 (summarizing SoundExchange's argument), 132 (adopting SoundExchange's argument); *see* SX RPFF ¶¶ 745-748. Further, in their Determination, the Judges agreed with SoundExchange (*see, e.g.*, SX RPFF ¶ 733) that the Judges should follow their own prior reasoning in *SDARS II*, in which they distinguished between the lesser value of Indie repertoires and the greater value of Major repertoires, and noted that the statutory rate must reflect both categories of sound recordings. *See SDARS II*, 78 Fed. Reg. at 23063-64.

At no point in this proceeding did SoundExchange advance the argument that it now asserts, *viz.*, if an Indie allowed a Major to distribute its sound recordings to noninteractive services, the Indie would receive the higher Major rate in the hypothetical marketplace. This construct seems to be an attempt—for the first time on rehearing—to make a purported logical or evidentiary connection between distribution ratios and the royalty rate-setting process, a connection the Judges found Dr. Rubinfeld had not made. *See Determination* at 54, n.89 (Dr. Rubinfeld failed "logically or evidentially" to link concept of distribution to statutory rates).

If Dr. Rubinfeld or anyone else on behalf of SoundExchange *had* made such an argument, the Judges nonetheless would have rejected it on the merits, as they do now. As noted above, SoundExchange argued (successfully) that there is a difference in the value of the sound recording repertoires of Majors and Indies. There is no rationale (and certainly nothing in the record) explaining why a sound recording from an Indie repertoire with a market-based royalty value of $0.[redacted] per play when distributed by someone other than a Major, would somehow increase in royalty value *by 63%* to $0.[redacted] per play if a Major distributed sound recordings from that repertoire. SoundExchange's argument is more alchemy than economics.[12]

To come full circle to SoundExchange's blunt question, the foregoing discussion reveals the loaded nature of that query: "Would an [I]ndie … opt to have the Major distribute … at the $0.[redacted] rate, or would the [I]ndie opt to distribute itself at the lower $0.[redacted] rate?" Reply at 1. The correct response to this question is obvious, but it is not the answer SoundExchange proposes: The correct response is that—*based on SoundExchange's own persuasive reasoning during the proceeding*—the Indie could *not* receive $0.[redacted] in royalties for sound recordings from a repertoire in which those sound recordings were valued at $0.[redacted].[13]

For all these reasons, the Judges reject SoundExchange's assertion that, with regard to this issue, the Judges committed "clear error," or that this issue otherwise creates an "exceptional circumstance" sufficient to grant SoundExchange's Motion.[14]

IV. The Judges Reject SoundExchange's Claim of "Clear Error" Regarding the Alleged "Shadow" of the Statutory License.

SoundExchange argues that the Judges clearly erred in their consideration of the so-called "shadow" effects of the statutory license. The Judges reject this argument for several reasons.

SoundExchange is merely reasserting arguments it made during the proceeding based on the opinion of one of its experts, Dr. Talley. He had opined that the existence of this so-called "shadow" obscures certain pairings of willing buyers and willing sellers ("dyads") that would have occurred but for the presence of the statutory license. However, the Judges have already rejected this argument because it was "too untethered from the facts," as exemplified by his failure to consider the effects of potential steering and competitive dynamics, and because his

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[12] SoundExchange's failure to make a "logical and evidential" connection between the Majors' distributional services and the royalty rate left many questions unanswered, which SoundExchange cannot now attempt to re-litigate. For example, *are those distribution costs already accounted for in the benchmarks?* An Indie would certainly know of the cost of distribution. As the Judges noted in the Determination, costs would already be "baked in" to the rate willingly agreed to in the marketplace. *Determination* at 31. Thus, the benchmark rate already incorporates the distribution cost of the willing sellers/licensors. Accordingly, if the statutory rate was increased to account for the distribution costs, that would constitute both a second-guessing of the market participants and a double-counting of those costs. To note a second example, if a Major could provide less costly distribution services, then *why would that lower cost not suggest a lower statutory rate rather than a higher one?* To note a third example of an issue that SoundExchange left unexplored, *would a Major attempt to lump its distribution of Indies with its distribution of its own sound recordings, using its complementary oligopoly power to present that bundle as a "take it or leave it" proposition to the interactive services?* (Moreover, would the Major retain a disproportionate share of the "distribution" fee?) Such a practice would frustrate the effectively competitive market required by the statute. *See id.* at 133-34. Finally, to the extent a Major attempted to use such bundling, *would it constitute a form of price discrimination?* If so, SoundExchange proffered no evidence as to any potentially beneficial aspects of such price discrimination, nor did it afford the Services the opportunity to rebut such an unasserted claim and point out any negative aspects of such discriminatory pricing. These immediate examples of unraised issues underscore the point that rehearing is not the procedure by which such complex economic issues may be raised for the first time.

[13] This point relates to the *hypothetical marketplace*, absent the statutory license, in which two different sets of repertoires, Majors and Indies, have separate values.

[14] SoundExchange also relies on its own PFF ¶ 541 in support of this Major-to-Indie ratio argument. However, that paragraph is devoid of any references to the record; it appears to summarize the arguments based on the foregoing record citations discussed by the Judges. Therefore, paragraph 541 of SoundExchange's PFF does not provide any independent argument in support of the present Motion.

analysis would effectively preclude use of the benchmark approach. *Determination* at 32-35. Thus, SoundExchange is simply seeking a "second bite at the apple" on this issue, which is not a basis for rehearing.[15]

Further, as a matter of substance, SoundExchange fails to address adequately an important reason why the Judges rejected SoundExchange's "shadow" argument. The Judges found that the Pandora/Merlin Agreement and the iHeart/Warner Agreement established rates that were *below* the statutory rates that otherwise controlled for those respective parties. As the Judges noted in the Determination, neither Merlin nor Warner was compelled by the statutory "shadow" to agree to rates below the statutory rate unless such rates were in their economic interest, *i.e.*, their interests as willing sellers/licensors dealing with willing buyers/licensees. They could have defaulted instead to the *higher* statutory rate—the so-called "shadow"—but declined to do so.

To avoid this critical *economic* point, SoundExchange resorts to linguistic ambiguity, asserting that these benchmark rates were "tied" to the statutory rate. *See* Motion at 6. This argument simply ignores the salient economic point summarized above. Indeed, if the benchmark rates were in fact "tied" to the statutory rate, this tying could only suggest that the statutory rate had an *upward* bias on the benchmark rates.[16]

SoundExchange also asserts the Judges clearly erred in their consideration of the "shadow" issue by failing to treat as dispositive the fact that Universal and Sony did not enter into steering-related deals with iHeart. However, in the Motion, SoundExchange fails to note that the Judges found the evidence demonstrated that steering and the threat of steering would be effective in the hypothetical marketplace for rights to the sound recordings of the three Majors as well as the Indies. *See Determination* at 122-23. Indeed, the evidence indicates that rejection of steering deals by Universal and Sony was related to the impact of steering on the statutory rate.[17]

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[15] The Judges also note that SoundExchange's rehearing argument, based on Dr. Talley's critique, would compel rejection of any voluntary noninteractive direct license agreements as benchmarks, because the argument asserts that such direct agreements are *per se* invalid benchmarks, as they hypothetically could be unrepresentative of the noninteractive market. However, the applicable statutory language states that the Judges, "[i]n establishing rates … may consider the rates … for comparable types of digital audio transmission services and comparable circumstances under voluntary license agreements described in subparagraph (A)." 17 U.S.C. § 114(f)(2)(B). An expert cannot foreclose the Judges from considering an entire category of benchmarks that Congress has explicitly identified as pertinent to the establishment of the statutory rate.

[16] This influence is precisely what Pandora's expert economist, Dr. Shapiro, argued, claiming that the statutory rates acted as a "magnet" or "focal point," keeping the consensual benchmark rates even higher than the market rate in the absence of a statutory rate. However, the Judges rejected Dr. Shapiro's argument for the same reason they rejected Dr. Talley's argument: as unsupported by sufficient evidence. *Determination* at 32-33.

[17] For example, Sony claims to have rejected a proposed deal with iHeart, but the comprehensive terms of that proposed deal and all the particulars of the negotiations were not in evidence. Although a Sony witness, Dennis Kooker, stated in conclusory fashion that the proposal made by iHeart was "horrible," there also was insufficient evidence of the particular proposed terms of the negotiation that led him to that conclusion. Moreover, Mr. Kooker indicated in his testimony that Sony resisted a steering agreement with iHeart at least in part because [redacted], and he testified that Sony [redacted] 4/28/15 Tr. 511 (Kooker). Thus, Sony appears to have cut off negotiations with iHeart at least in part [redacted], rather than merely because the economics of the deal under negotiation were unsatisfactory. Further, Universal's witness, Aaron Harrison, candidly admitted that Universal "[redacted] consider[s] [redacted]" as well as the independent business value of any proposed direct agreement. 4/30/15 Tr.

The decision by Sony and Universal not to enter into steering agreements thus would tend to underscore the value of preserving the Majors' complementary oligopoly power, rather than diminish the benchmark value of the steering-based iHeart/Warner Agreement and Pandora/Merlin Agreement.

SoundExchange argues that the Judges clearly erred because they were obligated to set a statutory rate to which "most" licensors and licensees would agree, relying on language from prior webcasting determinations. Motion at 7. That argument hardly suggests any error by the Judges, for several reasons. First, the language from *Web II* upon which SoundExchange relies expressly states that the statutory rate should represent the rate to which most willing parties would agree, "absent special circumstances." *See Web II* at 24087. The concept of steering, as demonstrated in the present proceeding, was not in evidence in those prior proceedings, and the technology of steering did not even exist at the time of those prior determinations. Clearly, steering is a "special circumstance" when considered in the historical context of *Web II* and *Web III*.

Furthermore, the language quoted by SoundExchange does not require the Judges to establish what essentially is the modal rate among pairs of willing buyers and sellers. If it did, then the rates in the more than 14,000 contracts, each pairing Pandora with one of those 14,000 Merlin members, would easily swamp, on a modal basis, all other contract rates. It seems safe to infer that SoundExchange, by its present Motion, does not want the Judges to adopt a purely modal analysis and adopt as the statutory rates only the rates derived from the 14,000-plus agreements between Pandora and (Merlin-member) Indies.

SoundExchange argues as well that the Judges clearly erred because the modal analysis should apply to the Major rate within the Determination, noting that two of the three Majors declined to enter into a similar benchmark agreement with iHeart. Even if the Judges were to give any weight to this argument, which they do not, the Judges note that Universal (one of the two Majors that did not enter into a steering-based agreement) has described Merlin as the equivalent of a "Major." *See Determination* at 127; PAN Ex. 5349 at 9. The fact that Merlin, with the level of commercial sophistication of a Major, embraced a steering-based rate structure, indicates that among those with the capacity to advance licensor interests there was a two-to- two split (Warner and Merlin favoring steering-based agreements), and therefore no literal modal grouping that eschewed a steering-based rate.

V. The Judges Reject SoundExchange's Claim of Error in Adopting an Annual Price Level Adjustment

SoundExchange argues that the Judges "clearly erred" in adopting an annual adjustment of commercial royalty rates to reflect changes in the Consumer Price Index (CPI-U) because no benchmark agreement in evidence included such an automatic increase. Motion at 3-5. The Judges reject SoundExchange's assertion that this annual price level adjustment is clearly erroneous, or otherwise constitutes a basis to grant rehearing.

1164-65 (Aaron Harrison) (emphasis added). This testimony indicates that Universal considered [redacted] in the ordinary course of business.

Contrary to SoundExchange's assertion, one of the adopted benchmarks—the Pandora/Merlin benchmark—*does* include [redacted].[18] PAN Ex. 5022 at 32 (Shapiro WDT). However, in his oral testimony, Dr. Shapiro stated it was his opinion that it would be preferable to adjust rates annually for *actual* price level changes rather than for *forecasted* changes. 5/19/15 Tr. 4608-10 (Shapiro). The Judges based the annual inflation adjustment explicitly and properly upon this benchmark and Dr. Shapiro's oral testimony. *See Determination* at 104; 198; *see also id.* at 82-83 (rejecting Dr. Rubinfeld's proposed annual adjustments as lacking empirical support and noting that, *inter alia*, he admitted his adjustments were not based on anticipated inflation or consumer price index).

The Judges did not commit "clear error" in adopting these rate adjustments. Moreover, there is no basis for a rehearing as to this issue because, again, a motion for rehearing "is not simply an opportunity to reargue facts and theories upon which a court has already ruled …." NAB Opposition at 1.

Relatedly, the fact that this particular price-level adjustment was not included in a benchmark does not preclude the Judges from including an annual price-level adjustment generally recommended by a testifying expert. The Judges are not straitjacketed by the benchmarks submitted by the parties, but rather are guided by all the evidence and testimony. *See* 17 U.S.C. § 114(f)(2)(B) ("In determining … rates … the …Judges shall base their decision on economic, competitive and programming information presented by the parties."); s*ee generally Music Choice v. Copyright Royalty Bd.*, 774 F.3d 1000, 1009 (D.C. Cir. 2014) (Judges permitted by Act to make "adjustments to … benchmarks" or "to look elsewhere for guidance"). The Judges decided this basic point in the Determination and thus this argument is not properly subject to rehearing. *See Determination* at 118, n.39 ("[T]he benchmarking approach, while highly instructive, is not the sole method for ascertaining the statutory rate …. [A] *combination* of benchmarks, experiments and expert economic theorizing ... is actually *more persuasive* to the Judges than a mere benchmark standing alone.") (emphasis in original).

SoundExchange also asserts that the particular benchmarks on which the Judges did rely to set the noninteractive, ad-supported rate contain annual rate escalators other than price-level adjustments. Motion at 3-4. However, as the NAB points out, that is a mischaracterization of those two agreements, because both the Pandora/Merlin Agreement and the iHeart/Warner Agreement [redacted]. NAB Opposition at 6 (and record citations therein). Moreover, to the extent any agreements [redacted], the Judges found in the Determination that there was no evidence or testimony to explain why there were different rates for different years or why such escalation should continue. *Id.* at 82-83; *see* NAB

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[18] Other direct agreements included annual rate increases, although the agreements do not state expressly the basis on which the increases are computed. Thus, the Judges certainly acted in a manner that was generally consistent with those agreements by including an annual adjustment factor in the statutory rate. SoundExchange's disagreement concerns the method of adjustment and the potential size of adjustment, not the concept of a year-over-year adjustment. However, as noted *infra*, the Judges can consider all the evidence and testimony to set appropriate rate adjustments, not merely the benchmark agreements submitted by the parties.

Opposition at 5-6 (no precedent requires Judges to "slavishly adopt every aspect" of benchmark agreement, particularly if other evidence demands different conclusion.).

Although SoundExchange acknowledges the Judges found that annual changes in the hypothetical market royalty rate cannot be predicted, SoundExchange argues the Judges erred because this inability to predict requires protection for the record companies against a supposed "inherent asymmetry" in the statutory license." Motion at 4, citing *Determination* at 83.[19] The Judges find this argument unavailing, both because the Judges rejected the argument when SoundExchange raised it at the hearing, and because, on the substantive merits, SoundExchange's present belated asymmetry argument is incorrect.

Taking the substantive deficiency of SoundExchange's argument first, if willing buyer/willing seller rates in the hypothetical market were to stay constant in 2017 but *increase* above \$0.0017 in 2018—to \$0.0019, for example[20]—then the record companies would lose the ability to negotiate a new deal in which they could attempt to share in the \$0.0002 increase. Of course, if this example were modified so that rates in the hypothetical market were to *decrease* below \$0.0017 in 2018—to \$0.0015, for example—licensors could still insist on receiving the \$0.0017 statutory rate, and avoid the potential loss in a renegotiated deal. There is symmetry, not asymmetry, in these two alternatives, each of which is equally likely given the absence of evidence to the contrary, as found by the Judges. *See Determination* at 83; *see also* Rubinfeld CWDT ¶ 100 (for licensors and licensees "there can be both upside risk (a better-than-expected outcome) and downside risk (a poorer-than-expected outcome).").

SoundExchange, relying on Dr. Rubinfeld's testimony, claims an asymmetry nonetheless exists because, if the hypothetical 2018 market rate decreased below the statutory rate (to \$0.0015 in the above example), the webcasters/licensees might not accept the higher (\$0.0017) statutory rate, but would "have an incentive to negotiate lower rates." Rubinfeld CWDT ¶ 143. This argument ignores the fact that the record companies/licensors do not have to re-negotiate during the rate term, but rather can retain the economic benefit of a statutory rate that exceeds the now lower market rate.[21]

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[19] SoundExchange also asserts that it needs annual rate escalators to protect against "unforeseen marketplace developments" over the next five years. *Id.* However, the Judges have considered and rejected this stand-alone argument, and SoundExchange has presented no basis for the Judges to allow rehearing on this point. *See Determination* at 83 ("[M]arket forces in the future may cause rates to move in either direction, or to stay constant, and the record does not suggest a basis for a credible prediction.").

[20] For simplicity, this example assumes no change in the CPI-U.

[21]As SoundExchange notes, the webcasters/licensees have the option of going out of business, or of capping listenership. Those "options," unattractive as they are, would become even more unattractive under the *higher* statutory rate SoundExchange seeks to correct for the alleged asymmetry. Further, exiting the market or restricting customer usage can hardly be construed as asymmetric "benefits" to a webcaster. If, as SoundExchange implies, licensors felt compelled to lower rates to keep noninteractive services from going out of business, that would constitute a 180-degree turnabout from SoundExchange's position at the hearing, at which it argued vehemently that rates would not be lowered in the market to support the business models of the noninteractive services. *See* SX PFF ¶1188 ("'[T]he rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller,' 17 U.S.C. § 114(f)(2)(B), *cannot be discovered by studying the current or short-term profitability (or unprofitability) of any webcaster or of the webcasting industry."* (emphasis added)).

The Judges, consistent with prior Webcasting decisions, agree that the business models of any of the parties are not pertinent to a benchmark analysis. *Determination* at 31-32. If record companies believed noninteractive services needed to be subsidized with below-statutory rates in adverse market conditions, that approach would signal a sea

Further, to the extent the statutory rate may contain any residual "inherent asymmetry," notwithstanding the foregoing analysis, the asymmetry argument is plagued by procedural deficiencies. SoundExchange has not presented any evidentiary basis on which the Judges could estimate the value of such asymmetry and incorporate that possible value into the rates throughout the rate period. Instead, without any support in the record, SoundExchange has sought via rehearing annual $0.0001 increases over the rate period that would result in a cumulative 23.5% increase in the subscription rate, and a cumulative 17.4% increase in the ad-supported, nonsubscription rate.

Further, as Pandora notes in its Opposition, SoundExchange's rehearing request for this annual $0.0001 increase seeks a 25% larger increase than the $0.00008 annual increase proposed by Dr. Rubinfeld. Pandora Opposition at 6 n.4. The Judges rejected that lower increase in the Determination for lack of evidence to support Dr. Rubinfeld's testimony. Now, by Motion, SoundExchange seeks an even larger annual escalator based on neither evidence nor testimony.

SoundExchange is re-visiting an issue already decided by the Judges in the Determination. Specifically, SoundExchange notes that the Judges' refusal to adopt a "greater-of" rate structure that included a percent-of-revenue rate eliminated the licensors' ability to "protect against future uncertainties …." Motion at 5 n.8. However, the Judges thoroughly considered, and ultimately rejected, the proposal for such a "greater of" rate structure. *See Determination* at 18-24.

Moreover, the citation to which SoundExchange now refers the Judges, post-hearing, on the alleged "asymmetry" issue, SX PFF ¶¶ 321-331, merely catalogs certain agreements. In fact, SoundExchange *did* address the alleged asymmetry issue at SX PFF ¶ 333, in which it argued that the per-play prong protected it against downside risk while the percentage-of-revenue prong allowed it to share in the upside return. SX PFF ¶ 333. However, SoundExchange did not assert until rehearing that the record companies require an annual escalator to prevent an alleged asymmetry if the Judges do not adopt a greater-of structure and establish only a per-play rate. Therefore, SoundExchange cannot raise this issue for the first time on rehearing.[22]

change in a core SoundExchange economic argument. It would also suggest that noninteractive services are not "net substitutional," but rather may be "net promotional," and that the continued market presence of the noninteractive services is necessary for the licensors, to prevent the migration of noninteractive listeners to entities such as terrestrial radio or pirate services. Otherwise, if listeners were to migrate to interactive services and other royalty-bearing listening, licensors would be pleased with the elimination of the noninteractive services. Thus, SoundExchange's rehearing argument on this point would require a significant change in its position that would necessitate, *ceteris paribus*, a *lower* statutory rate. *See* SX PFF § XIII at 370 ("[t]he record shows that consumer use of statutory services interferes with higher-ARPU copyright owner revenue from directly licensed services … [and] fail[s] to support the services' contention that consumer use of statutory services is 'net promotional'"). The pertinent point at this stage of the proceeding is to note that the economic argument made by SoundExchange would open a can of worms regarding issues already determined in its favor at the hearing, further underscoring the impropriety of asserting this issue via the rehearing process.

[22] The Judges also note SoundExchange's argument that the "greater of" structure is necessitated by an "asymmetry" problem based on the assumption that a percentage-of-revenue rate offsets a per-play rate that is set too low. However, the Judges *explicitly* set the per-play rate at the level they found to be proper, even without a percentage-of-revenue rate prong. *Determination* at 23-24 and n.54. Thus, SoundExchange's claim that the asymmetry problem resurfaces in the absence of a "greater of" structure depends on an implicit assumption that the per-play rates set by the Judges are too low, an implication the Judges reject. In the absence of a *bona fide* asymmetry issue, the annual escalator sought by SoundExchange would be a "solution in search of a problem."

Additionally, as a matter of basic economics, the price level adjustment in royalty rates for any given year after 2016 in the rate period should reflect the *real* value of money, rather than a *nominal* rate that fails to reflect increases (or potential decreases) in the price level. Indeed, as the representative of licensors, SoundExchange should prefer a rate that adjusts for annual inflation to one that fails to keep up with inflation.[23] Section 114 of the Act certainly does not require the Judges to set annual rates that assume willing buyers and sellers would suffer from irrational "price illusion," *i.e.*, that they would agree to nominal rates that fail to reflect the real value of their rates after an incorporation of price-level changes.

For all of these reasons, the Judges reject SoundExchange's assertion that, with regard to this issue, the Judges committed "clear error," or that this issue creates an "exceptional circumstance" sufficient to grant SoundExchange's Motion.[24]

VI. The Judges Reject SoundExchange's Assertion of "Error" in the Regulatory Language but Accept in Part Suggestions to Revise that Language

SoundExchange included in its Motion several requests for rehearing regarding the regulatory language resulting from this proceeding. To assure full consideration of the regulatory objections the Judges accepted SoundExchange's offer to specify regulatory language to which it objected. The Licensees objected to the SoundExchange Supplemental Petition (Supplement) as untimely under the Act.[25] As a general rule, the Judges would not and will not permit a party to ignore a statutory time limit or to skirt the rules regarding page limitations, particularly as those requirements pertain to a motion for rehearing after a determination. In the context of this webcasting proceeding, however, the parties proposed technical regulatory changes in writing but produced insufficient evidence and devoted insufficient argument to the specifics of those proposed changes. Even if SoundExchange had not volunteered to supplement its substantive motion with additional regulatory detail, the Judges could have, and likely would have, sought additional submissions from the parties to illuminate the regulatory concerns before issuing the final regulations. The Judges would have been remiss, and might even have erred, had they attempted to resolve regulatory differences without seeking and considering additional argument of the parties. The Judges consider the Supplement and the oppositions thereto as necessary augmentations and reject the Licensees timeliness argument, in this instance.

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[23] Inflation is certainly more likely than deflation. *See generally* U.S. Bureau of Labor Statistics, *One Hundred Years of Price Change: The Consumer Price Index and the American Inflation Experience*, Monthly Labor Rev. (Apr. 2014) (noting overwhelming historic prevalence of inflation over deflation). The Judges recognize that SoundExchange advocated for a likely higher annual nominal increase, based on Dr. Rubinfeld's testimony, but given the Judges' rejection of his opinion in that regard, it is curious that SoundExchange would object to an annual adjustment that would *protect* licensors from the eroding effect of inflation. SoundExchange's argument against the price-level adjusted rates thus appears to be a fresh example of the adage "cutting off one's nose to spite his face."

[24] The Judges agree with SoundExchange that they should clarify the new regulation describing the price-level adjustment, § 380.10, so that the process of rounding to the fourth decimal place is not misunderstood to create a meaningful deviation from the unrounded real rate. None of the Services objected to the substance of this requested clarification in their Oppositions. Accordingly, the Judges shall supplement the new § 380.10 as indicated in "Exhibit A" to this Order. (The Judges note that any rounding process will inevitably lead to an inexact figure. However, no party has suggested that the rounding process be carried beyond the level of precision described in the supplemental regulatory language in "Exhibit A" to this order.).

[25] Section 803(c)(2)(B) requires any motion for rehearing to be filed within 15 days of issuance of the determination.

Having reviewed the SoundExchange "Supplemental Petition" (Supplement) and the Services' responses thereto, the Judges adopt some changes in the regulatory language disseminated as "Exhibit A" to the Determination.[26]

A. The Jurisdictional Licensing Requirement for a Qualified Auditor (§ 380.7–definition of "qualified auditor")

SoundExchange objects to the addition of a requirement that a Qualified Auditor be licensed in the jurisdiction in which it conducts the audit in § 380.7.[27] Motion at 8-9. The NAB requested this additional requirement to qualify an auditor as part of its proposed terms. NAB Proposed Rates and Terms, at 3 (Tab B to NAB CWDS Vol. 1).

SoundExchange argued against the added requirement that a selected auditor be a Certified Public Accountant. The Judges rejected SoundExchange's argument, opting for designation of an auditor that would be subject to the CPA licensure standards. SoundExchange asserts that the additional jurisdictional licensure requirement is not supported by the record. This requirement provides assurance that the auditor will be accountable and amenable to local governance in the jurisdiction in which it operates. Differences in ethical standards and sanctions for CPAs among jurisdictions might be small, but the requirement that the auditor submit itself to the jurisdiction of the local CPA governing bodies and local courts is significant. The NAB suggestion is supported by the testimony of Professor Raymond Weil and, therefore, not without support in the record. *See* Weil WRT at 11-13. The Judges reject SoundExchange's objection.

B. The Three-Year Holding Period for Unclaimed Funds (§ 380.2(e))

The extant regulations contain an internal ambiguity concerning the measurement of the period for holding unclaimed funds. When the Judges suggested reorganization of the Part 380 regulations, they highlighted this issue for the parties. *See Judges' letter to participants dated April 2, 2015.* For example, in § 380.4 of the current regulations, the Collective is required Whold funds if it is "unable to locate a Copyright Owner … within 3 years from the *date of payment by a Licensee* …." 37 C.F.R. § 380.4(g)(2) (emphasis added). If the Collective is unable to locate the rightful payee, then the funds become subject to § 380.8, *id.*, which requires the Collective to retain "unclaimed" funds for "a period of 3 years from the *date of distribution*." *See, e.g.*, 37 C.F.R. § 380.8 (emphasis added). The Collective may apply those funds to offset its costs at the end of the three-year holding period. *Id.*[28] On its face, the "date of payment by a Licensee" is not the same as the "date of distribution," the latter of which is ambiguous, at best.

Despite the Judges' invitation, no party offered explanation for the current regulatory discrepancy or suggested clarifying language to eliminate the ambiguity. In section 380.2(e) of the regulations adopted by the Judges as part of the Determination, the Judges sought to resolve

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[26] The Judges also make clarifying edits to the regulatory section regarding annual rate adjustments discussed in section V of this Order.

[27] It now appears that the Judges included two sections 380.6 in the initial iteration of the regulatory language The Judges shall correct that error and relabel the second (the definitions section) as § 380.7.

[28] Similar language is repeated in subparts B (§§ 380.13(i)(2), 380.17) and C (§§ 380.23(h)(2), 380.27) of the extant regulations.

the ambiguity by specifying that the three-year holding period commences on “the date of final distribution of all royalties.” SoundExchange avers that the Judges’ have introduced uncertainty into the regulation because it is unclear when a “final distribution of all royalties” takes place when a copyright owner cannot be located and the funds that copyright owner may be entitled to cannot be distributed. SoundExchange has requested that the Judges amend the regulation to specify that the three-year holding period commences on the date of the first distribution of royalties from the relevant payment by the service. Motion at 10. No other party has responded to SoundExchange’s requested amendment. The Judges recognize that the language of section 380.2(e) may be unclear, and that the amendment that SoundExchange requests would clarify the regulation in a manner consistent with the Judges’ intent. Therefore, the Judges accept the SoundExchange proposal and clarify the regulatory language accordingly. The three-year escrow period for undistributable royalties shall be three years from the date of first distribution of relevant royalty deposits from a Licensee.

C. Audit Frequency (§ 380.6(b))

SoundExchange argues that the Judges’ newly-revised regulatory language regarding audit frequency included an unintended ambiguity regarding the frequency with which the Collective may audit Licensees. Motion at 10. In its Motion, contends that section 380.6(b) could be interpreted as limiting SoundExchange to a single audit *of a single service* each year. *Id*. SoundExchange asks the Judges to clarify that it is not restricted to auditing only one licensee per year; rather that the limit is one audit per year *for each licensee*. No party responded in opposition to this clarification request. Since SoundExchange’s proposed clarification is consistent with the intent of the language originally adopted by the Judges, but is not subject to misinterpretation, the Judges shall amend the regulatory language accordingly.

D. Royalty Adjustments and Interest Obligations after Audit (§ 380.6(g))

SoundExchange objects to language in section 380.6(g) that gives licensees a credit, with interest, for overpayments that are revealed in an audit, arguing that the provision is inconsistent with the Judges’ rejection of a similar proposal by the services in connection with adjustments based on revised Statements of Account. Motion at 10. In the extant regulations, the provisions regarding audits and audit findings do not address the question of financial adjustment,[29] either restitution for underpayment or recoupment of overpayment. In this proceeding, the Services introduced evidence of the practice of “truing” accounts. *See e.g.,* SX Ex. 33 at 18 (¶4(c) of document) (Licensee to make immediate restitution of any underpayment discovered by audit), IHM Ex. 3351 at 11 (¶ 7(b), p. 10 of document) (Licensee may withhold royalties prospectively in certain circumstances), IHM Ex. 3340 at 3 (¶ 1.b., p. 2 of document) (same). Reconciliation of accounts should be no less a practice in the context of statutory licensing. *See* 17 U.S.C. §114(f)(2)(B)(II) (in establishing terms, Judges may consider “comparable circumstances under voluntary license agreements”).

[29] The only reference to a financial issue in the current audit regulations relates to restitution of an underpayment and allocation of the cost of the audit in the event the auditor finds an underpayment discrepancy of 10% or more. *See, e.g.* 37 C.F.R. §§ 380.6(g), 380.7(g). No regulation addresses underpayment of less than 10% or overpayment at any amount.

The Licensees participating in this proceeding proposed an open-ended term that would permit them to amend SOAs and make concomitant financial adjustments (with interest). The Judges rejected this proposal because of the open-ended nature of the proposal, which could result in an excessive administrative burden on SoundExchange. The Judges concluded, rather, to allocate the burden of accuracy in reporting to the Licensees. *See Determination* at 194.

In allocating that administrative burden, however, the Judges were not opining on the propriety of or need for a balancing of accounts after an audit. SoundExchange may audit Licensees annually, but the period audited may be up to three years. No party offered evidence of past audit practices or results. The Judges are unaware of whether any audit findings have ever resulted in cost-shifting, for example, let alone what remedies, if any, the parties have employed to reconcile under- or overpayments. Further, a sampling of direct license agreements does not reveal a standard regarding recoupment of overpayments detected by audit.

Nonetheless, even if directly contracting parties negotiated reciprocal reconciliation of payments in any circumstance, the Collective is in a different business posture than its members making direct license deals. As SoundExchange points out, it is a non-profit organization that makes distributions directly to a multiplicity of artists and record companies from each royalty deposit. SoundExchange is not in the same position that an individual Licensor might be with regard to management of its funds.

The Judges thus adopt for audit findings the same rationale as that applicable to Statements of Account: the burden of accurate reporting and payment is on the Licensee. Accordingly, the Judges' regulations shall continue to require immediate restitution in the case of underpayment, but not a right of recoupment for overpayment.

As with any untimely payment, a Licensee that is obligated to remedy an underpayment shall be liable to pay reasonable interest thereon.

E. Definition of Commercial Webcaster (§ 380.7–definition of "commercial webcaster")

In the Motion, SoundExchange asked the Judges to change the definition of "Commercial Webcaster." Motion at 10. As written, the definition of Commercial Webcaster excludes "an Educational Webcaster, a Noncommercial Webcaster, or Public Broadcasting Entities …." SoundExchange seeks to change the phrase "Public Broadcasting Entities" to "Covered Entity under Subpart D" to conform the terminology with that adopted in Subpart D of Part 380, pursuant to the settlement SoundExchange reached with The Corporation for Public Broadcasting (CPB) and National Public Radio (NPR). By its terms, the CPB/NPR settlement is by and between SoundExchange on the one hand and, on the other hand, NPR and CPB, on behalf of themselves and on behalf of American Public Media, Public Radio International, and certain public radio stations, together designated the Covered Entities.

No participant in the hearing self-identified as a public broadcasting entity. Presumably, if there is an entity satisfying the statutory definition of a public broadcaster that was *excluded* by agreement from the settlement memorialized in Subpart D of the revamped regulations, that excluded entity would be treated as a noncommercial webcaster or a noncommercial educational webcaster, as the case may be.[30] As the Judges did not define "public broadcaster" in this iteration of their regulations, however, the request from SoundExchange to clarify the reference is well taken.

The Judges shall add a definition of "public broadcaster" to section 380.7, cross-referencing Subpart D.

F. Due Diligence (§§ 380.2(e), 380.4(a)(2))

In this proceeding, the Licensees proposed, and the Judges adopted, additional regulatory language regarding the Collective's duty to locate parties entitled to receive royalty distributions.[31] SoundExchange objected to the added language. A SoundExchange executive testified that the Collective maintains an extensive database and can locate distributees without the due diligence suggested by the new language. *See* SX Ex. 23 at 18-19, SX Ex. 2 at 5-11. As SoundExchange concedes, however, the regulations contain similar language in section 370.5(d) regarding best efforts to find copyright owners in order to make available reports of use.

If SoundExchange is able to make—and amenable to making—records searches to assure proper distribution of reports of use, the Judges should assure that SoundExchange makes no less of an effort to locate copyright owners when the time comes to distribute royalty funds. It would seem even more appropriate for SoundExchange to engage in best efforts when distributing royalties to avoid any appearance of impropriety or conflict of interest, in light of section 380.4(a)(2), which may permit retention of unclaimed funds by SoundExchange. This minimal additional due diligence can do little other than assure the currency and integrity of SoundExchange's distribution database.

Further, SoundExchange outlined its search capabilities, but did not object expressly to the due diligence language proposed by NAB and NRBNMLC. The Judges adopted the proposal of NAB and NRBNMLC.

G. Handling confidential information (§ 380.5(c)(1))

NAB and NRBNMLC proposed, and the Judges adopted, additional verbiage for the regulation (section 380.5(c) (1) in the newly-revised regulations) regarding confidential information shared by participants in webcasting proceedings that: (1) required confidentiality agreements to be in writing; and (2) limited disclosure of confidential information to those performing activities "related directly" to collection and distribution of royalty payments. SoundExchange does not indicate that it ever addressed these proposed changes to the regulations. It was not until SoundExchange sought rehearing that it raised a specific challenge to this added confidentiality language. Supplemental Petition for Rehearing … at 4 (Supplement).

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[30] Under section 118 of the Act, a "public broadcasting entity" means a noncommercial educational webcaster as defined in 47 U.S.C. § 397, *viz.*, "[CPB], any licensee or permittee of a public broadcast station, or any nonprofit institution engaged primarily in the production, acquisition, distribution, or dissemination of educational and cultural television or radio programs." Not all noncommercial webcasters are public broadcasters. Not all educational webcasters are public broadcasters. The appellation "public broadcaster" appears to be reserved to those stations that receive funding by or through the CPB.

[31] In this post-Determination review, the Judges noted that the due diligence language appears to be misplaced in § 380.2(e), regarding payment of royalty fees by Licensees. The Judges have deleted the language from § 380.2.

In their joint opposition to the Supplement, NAB and Pandora object to allowing SoundExchange to raise a new issue on rehearing. *See* NAB and Pandora's Opposition to … Supplement[ ] … at 5 (NAB/Pandora Supp. Opp.). iHeart further points to record evidence to support the additional language relating to handling confidential information during the process of royalty collection and distribution. *See* iHeart Opposition to … Supplement[ ] at 2-3 (iHeart Supp. Opp.). iHeart cites direct license agreements that are in evidence in this proceeding as support for the reasonable addition of requirements for (1) written confidentiality agreements and (2) restriction of use of confidential information to purposes "directly" related to collection and distribution of royalties. *Id*. (citing, *e.g.*, SX Exs 110 at 11 ([redacted] agreement) and 33 at 30 ([redacted]agreement)). iHeart's citation to the record illustrates the Judges' ability to look to "comparable circumstances under voluntary license agreements" in setting rates under section 114.

SoundExchange's objection is too little, too late. The Judges decline to change the confidentiality language.

H. "Distributees" of Confidential Information (§ 380.5(d))

SoundExchange objects to the use of the phrase "distributees of the collective" in section 380.5(d) as creating an uncertain standard, contending that the provision could be interpreted to require recipients of confidential information to "adhere to the unknowable standards employed by SoundExchange's tens of thousands of distributees." Supplement at 4. SoundExchange proposes to clarify that recipients of confidential information are bound by the standard of care that they employ with their own confidential information by substituting the phrase "Person authorized to receive confidential information" for "distributees of the collective." *Id*. No other party raised an issue with the language of the newly-revised regulation; nor did any party object to SoundExchange's requested change.

SoundExchange has correctly discerned the intended meaning of the language that the Judges adopted. The Judges do not view the potential misinterpretation that SoundExchange fears to be a reasonable reading of the section 380.5(d). The Judges also do not view SoundExchange's proposed amendment as likely to clarify the Judges' intent. Nevertheless, to remove all doubt the Judges shall amend section 380.5(d) by deleting everything after the second-to-last comma, and substituting the following: "but no less than the same degree of security that the recipient uses to protect its own Confidential Information or similarly sensitive information."

I. Binding nature of audit results (§ 380.6(d))

NAB proposed the Judges modify the audit regulation by removing the requirement that the Qualified Auditor's results be binding on the parties.[32] SoundExchange objects to the Judges' adoption of the NAB proposal. Supplement at 4. As NAB notes, SoundExchange

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[32] In drafting, the Judges apparently *moved* the modifier ("binding") rather than *removing* it, which was their intention. As issued, the Part 380 regulations provided not that the results of an audit be binding, but that the choice of the Qualified Auditor be binding. The issue NAB raised did not, in this instance, relate to selection of the Qualified Auditor, but to the binding nature of the audit results. The language making the choice of a Qualified Auditor binding was not requested by any party, is unnecessary, and shall be removed.

witness, Dr. Thomas Lys, testified that requiring an audit report be dispositive would be "unreasonable". NAB/Pandora Supp. Opp. at 3, citing 5/4/15 Tr. at 1507-08 (Lys).

The Judges agree that the subject of any audit should be permitted to contest audit results. SoundExchange offers no record support for its proposal that the regulations return to the current language, albeit made reciprocal in nature. The "binding" language shall be excised from the newly-revised regulations.[33]

J. Payment reconciliation terms (§ 380.6(g))

Pandora suggested that Licensees and SoundExchange be permitted to agree on acceptable terms[34] regarding the time for restitution of underpayments by Licensees.[35] SoundExchange did not oppose Pandora's proposal in its Reply PFF/PCL. In its opposition to the SoundExchange Supplement, iHeart suggests that agreed terms for reconciliation are consistent with market terms allowing for agreement on the identity of an auditor and the scope of an audit. iHeart Supp. Opp. at 2, citing, *e.g.,* SX Ex. 38 at 40 (re timing and scope of audit).

The legislative emphasis in the Act on voluntary, negotiated settlements, should, without clear, contrary evidence or authority, extend to permitting agreement regarding the timing for account reconciliation. SoundExchange has failed to show that permission to resolve a conflict by agreement is without evidentiary support or contrary to any legal requirements in the Act. The Judges did not err in adding this provision to the revised regulations. However, the regulatory language the Judges adopted might be construed as requiring, rather than permitting SoundExchange and Licensees to agree on acceptable terms of payment. Accordingly, the Judges shall clarify section 380.6(g) to read as follows:

> (g) Audit results; underpayment or overpayment of royalties. If the auditor determines the payor or distributor underpaid royalties, the payor or distributor must remit the amount of any agreed-upon underpayment to the verifying entity. In the absence of mutually agreed payment terms, which may, but need not, include installment payments with interest at the rate specified in § 380.2(d), the payor or distributor shall remit the underpayment determined by the auditor promptly to the verifying entity.

K. Performance of portion of a single track (§ 380.7–definition of "performance")

SoundExchange objects to the Judges' linguistic changes to the definition of "performance" in section 380.7. Supplement at 5. The Judges accept SoundExchange's concern

[33] Accordingly, any attempt to seek a remedy based upon an auditor's findings, and any attempt to challenge those findings, must be made in a court of competent jurisdiction, or through any private alternative dispute resolution procedure to which the affected parties may have agreed.

[34] The Judges address whether those terms shall include interest in section D, above.

[35] SoundExchange complains that Pandora "sneaked" in these changes. The record does not support SoundExchange's allegation. Pandora included its request for this regulatory change twice--once with its written rebuttal statement and again with its proposed findings of fact and conclusions of law. Pandora First Amended Rates and Terms (Feb. 22, 2015) (submitted concurrently with Pandora Written Rebuttal Statement); Pandora Second Amended Rates and Terms at 3, 13 (Jun. 24, 2015) (submitted concurrently with Pandora PFF/PCL).

that the new language may harbor an ambiguity. No party objected to SoundExchange's request for modification of the definition. The Judges shall make the requested modification.

VII. Conclusion

Upon conclusion of the redaction process, the Judges shall finalize the Determination they issued on December 16, 2015, in accordance with the reasoning and conclusions in this Order and the conclusions they reach regarding GEO's motion for rehearing. The Judges will forward the final Determination to the Register of Copyrights for her statutory review, after which the Librarian of Congress shall cause the Determination and any opinion of the Register to be published in the *Federal Register*.

SO ORDERED.

/s/______________________	**/s/**______________________	**/s/**______________________
Suzanne M. Barnett	**Jesse M. Feder**	**David R. Strickler**
Copyright Royalty Judge	**Copyright Royalty Judge**	**Copyright Royalty Judge**

DATED: February 10, 2016.

EXHIBIT A

§ 380.10 Royalty fees for the public performance of sound recordings and the making of ephemeral recordings.

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(c) Annual royalty fee adjustment. The Copyright Royalty Judges shall adjust the royalty fees each year to reflect any changes occurring in the cost of living as determined by the most recent Consumer Price Index (for all consumers and for all items) (CPI-U) published by the Secretary of Labor before December 1 of the preceding year. The adjusted rate shall be rounded to the nearest fourth decimal place. To account more accurately for cumulative changes in the CPI-U over the rate period, the calculation of the rate for each year shall be cumulative based on a calculation of the percentage increase in the CPI-U from the CPI-U published in November, 2015 (237.336), according to the formula $(1 + (Cy - 237.336)/237.336) \times R_{2016}$, where C_y is the CPI-U published by the Secretary of Labor before December 1 of the preceding year, and R_{2016} is the royalty rate for 2016 (*i.e.*, \$0.0022 per subscription performance or \$0.0017 per nonsubscription performance). By way of example, if the CPI-U published in November 2016 is 242.083, the adjusted rate for nonsubscription services in 2017 will be computed as $(1 + (242.083 - 237.336)/237.336) \times \$0.0017$ and will equal \$0.00173 (\$0.0017 when rounded to the nearest fourth decimal place). If the CPI-U published in November 2017 is 249.345, the rate for nonsubscription services for 2018 will be computed as $(1 + (249.345 - 237.336)/237.336) \times \$0.0017$ and will equal \$0.00179 (\$0.0018 when rounded to the nearest fourth decimal place). The Judges shall publish notice of the adjusted fees in the *Federal Register* at least 25 days before January 1. The adjusted fees shall be effective on January 1.