

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
Library of Congress
Washington, D.C.

_____)	
<i>In re</i>)	
)	
DETERMINATION OF ROYALTY)	DOCKET NO. 14-CRB-0001-WR
RATES AND TERMS FOR)	(2016-2020)
EPHEMERAL RECORDING AND)	
DIGITAL PERFORMANCE OF SOUND)	
RECORDINGS (<i>WEB IV</i>))	
_____)	

TESTIMONY OF
RON WILCOX
Executive Counsel, Business Affairs, Strategic and Digital Initiatives
Warner Music Group

Witness for SoundExchange, Inc.

TESTIMONY OF RON WILCOX

BACKGROUND

My name is Ron Wilcox. I am Executive Counsel, Business Affairs, Strategic and Digital Initiatives for Warner Music Group (“WMG”). In that position, I lead the business affairs efforts for WMG’s major strategic and digital initiatives, and I work closely with WMG’s digital legal affairs lawyers and WMG’s Digital Strategy and Business Development department. Recently, I added oversight of WMG’s digital legal affairs team to my responsibilities. I am one of the WMG attorneys primarily responsible for developing WMG’s relationships and negotiating agreements with digital music services, including agreements that authorize the transmission of WMG’s labels’ repertoire through streaming services. I joined WMG in the spring of 2009.

I have worked in the music business for more than 30 years. Before joining WMG, I worked as an independent consultant from 2008 through early 2009. During this time, I was retained by Sony Music Entertainment (“Sony”) (my immediate past employer) to negotiate, among other matters, a complex digital agreement for a bundled music-wireless service, Nokia’s “Comes With Music.” I also was retained by digital services, including digital music services such as Songza, and by recording artists, record companies and management companies to advise them on various transactions, including recording and other agreements. Before that, I worked in a variety of positions with Sony, ultimately serving as Executive Vice President and Chief Business and Legal Affairs Officer of Sony BMG Music Entertainment (“Sony BMG”). Sony BMG was a joint venture that combined the recorded music assets of Sony Corporation of America and Bertelsmann AG. In that position, I oversaw Sony BMG’s business and legal affairs activities, including the negotiation of deals with digital music services and the

development of Sony BMG's policies concerning the dissemination of its content through online service providers. Prior to the formation of the Sony BMG, I was Executive Vice President, Business Affairs and New Technology at Sony. Between 1990 and 2000, I was Senior Vice President, Business Affairs & Administration at Sony. From 1983 to 1990, I worked in Business Affairs for Sony's predecessor, CBS Records, and prior to that, I was an attorney for CBS Inc.

I graduated from the College of Wooster in 1975 and the University of Michigan Law School in 1978.

DISCUSSION

I. Warner Music Group's Position in the Recorded Music Industry

WMG includes a collection of some of the best-known record labels in the music industry, including Atlantic, Bad Boy, Elektra, Lava, Maverick, Nonesuch, Reprise, Rhino, Sire, Warner Bros. and Word. These labels feature a comprehensive roster of recording artists and a large catalog that includes some of the world's most popular sound recordings by some of the most iconic and celebrated recording artists of today and in recorded music history. WMG repertoire includes sound recordings by, to name just a few, Prince, Linkin Park, Bruno Mars, the Eagles, James Taylor, Led Zeppelin and Phil Collins.

In addition, WMG operates Alternative Distribution Alliance (ADA), which for many years has been a leading distributor for independent record labels. WMG's Warner Music International, a leading company in national and international recorded music repertoire, operates through numerous international affiliates and licensees in more than 50 countries. WMG also includes Warner/Chappell Music, one of the world's leading music publishers, with a catalog of more than a million musical compositions.

WMG was publicly traded on the New York Stock Exchange prior to its acquisition in July 2011 by an affiliate of Access Industries, Inc. WMG is now privately held.

II. WMG's Approach to the Digital Distribution of Music

WMG has long been an industry leader in the digital marketplace. WMG's innovative tradition traces all the way back to its origin, in 1929, when the Warner Bros. movie studio first entered the music business. WMG has always striven to find better ways of connecting artists and fans by embracing the latest delivery technologies and the most innovative product, sales and distribution strategies. Today, WMG is at the forefront of the record industry's transition from physical distribution to digital distribution. WMG manages a variety of music-based content that is marketed, promoted and distributed over a wide array of online and mobile platforms.

WMG believes that digital distribution is the key to new growth in the record industry. WMG has incorporated digital distribution as a central part of its business strategy. Sales of CDs and other physical media have continued to decline in recent years, as they have for more than a decade. Revenues from digital distribution—including from sales of permanent downloads through iTunes and other online retailers and from online streaming services—have become a critical component of WMG's business. In WMG's last reported financial quarter (the quarter ending June 30, 2014), WMG's digital revenues had grown to 58.9% of its total U.S. recorded music revenues, up significantly from 37.0% of its total U.S. recorded music revenues for the same financial quarter in 2009. WMG's digital revenues will continue to comprise a greater and greater share of its total revenues in the coming years. It is imperative, therefore, that WMG increase its digital revenues in order to compensate artists appropriately, discover new musical talent, produce the highest quality recordings, and market and promote artists to the widest possible public audience.

Over the past decade, technological developments have enabled music lovers to enjoy music in many new ways and have provided more immediate access to music than ever before.

The rise of digital services has fundamentally altered WMG’s view of how to generate revenues from distributing its sound recordings. Whereas in the past WMG was primarily concerned about the sales of physical products, such as CDs, WMG now views each potential distribution model in terms of its impact on all other distribution channels. The wide range of digital services appeal to different consumers, but all have the potential to substitute for one another. A key component of WMG’s digital strategy therefore is to negotiate marketplace agreements so as to maximize overall return to the company. Each business that WMG authorizes to exploit its content needs to provide a distinct revenue stream that either contributes meaningfully to WMG’s bottom line, or that has the realistic potential to develop a business model that, over time, is likely to make such a contribution. It is WMG’s goal to execute deals only at prices that are designed to generate sustainable revenues over the long term.

WMG’s overarching strategy for digital agreements is to find and exploit all potential avenues for monetizing the experience of listening to its recorded music. WMG is not interested in allowing its sound recordings to be used for free in the name of “promotion” alone. The fact is that, in 2014, the ubiquity and high quality of digital distribution have fundamentally transformed the concept of “substitution.” Prospective consumers can obtain free access through streaming services—including many that operate pursuant to the statutory license—to a wide range of music whose selection is customized to her or his musical tastes, or that is contained on playlists curated by friends or popular tastemakers. The idea that such unlimited access—without some additional element to incentivize music purchasing—promotes sales is fanciful. For WMG, authorizing the use of its music on services that will be “free to the listener” must be a means to an end of trying to stimulate listeners to pay for the core product they consume. Such payment may come, for example, in the form of subscription payments that allow for streaming

without advertisements, that allow listeners to skip through songs without limitation and/or that enable streaming on mobile devices.

III. Overview of WMG's Marketplace Agreements with Digital Distribution Services

WMG has entered into numerous agreements with various digital distribution services. Its digital group now negotiates upwards of 190 deals each year—including new agreements, amendments to existing agreements, extensions, and renewals—with a wide variety of digital service providers. WMG's agreements evidence the terms to which willing buyers and willing sellers agree in the marketplace. Many of WMG's agreements are with sophisticated parties operating a number of different music services. Through free market negotiations, WMG is able to obtain significantly higher rates and/or significantly more valuable overall deal terms than WMG receives through the statutory license. It is important to note, however, that the existence of the statutory license and compulsory statutory rates affects the marketplace rates that directly licensed services are willing to pay. Because statutory services compete with directly licensed services, the statutory rates act as a constraint on the rates WMG can negotiate with those directly licensed services.

In Section A below, I provide a very brief summary of the relevant general terms that WMG works to obtain in agreements with streaming services. In Section B, I discuss some of the unique features of WMG's 2013 agreement with iHeart Media, Inc. formerly known as Clear Channel Communications, Inc.

A. WMG's General Framework for Agreements with Streaming Services

As noted, WMG has negotiated numerous deals for the digital exploitation of WMG's extensive catalog of copyrighted sound recordings.

In marketplace deals, there are a few significant elements that are of particular value to WMG and are important components of WMG's negotiating strategy. WMG is not able to secure any of these elements under the statutory license and existing statutory rate structure:

[REDACTED] The single most important aspect of WMG's negotiated agreements is that they almost all feature a payment structure based on [REDACTED]

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

[REDACTED]. This [REDACTED] approach ensures that WMG is paid revenues that reflect the value that its sound recordings provide to the applicable service.

Without the music, these services—whether ad-supported, free-to-the-listener, or paid subscription—simply would not exist. This [REDACTED] structure ensures that if the service is tremendously successful and has significant revenues driven by its ability to deliver WMG content, WMG shares in that success. It also ensures that if the service is not successful, the value of WMG content is still protected.

[REDACTED] WMG's agreements with streaming services generally require [REDACTED]

[REDACTED]. WMG seeks these commitments to ensure that its digital partners will invest their time and resources to make their service offerings succeed. Such financial commitments also comprise a critical component of the consideration WMG requires for the use of its music.

Access to data. WMG's agreements generally require its streaming service partners to provide it with data and/or analytics about music consumption and user preferences. Such data help WMG refine and improve its A&R, production and marketing efforts.

Security provisions. WMG requires directly licensed streaming services to satisfy specific and detailed security requirements to protect the security of WMG content.

Holdback rights. WMG negotiates the right to withhold content for a number of reasons, including artist relations and limitations imposed by agreement, and also negotiates for holdback rights that allow WMG to provide certain content exclusively to other services or on other platforms, and thereby maximizing the value to WMG.

Reporting requirements and audit rights. WMG requires extensive reporting information from digital partners so WMG can report to publishers and artists accurately. WMG also secures meaningful rights to conduct audits to ensure that partners are meeting their technological and monetary commitments.

Short-term licenses. Given the evolving nature of the digital space in general, and the streaming space in particular, WMG generally does not enter into direct licenses with terms longer than two or, in rare cases, three years. The relatively short terms of these agreements allow WMG the opportunity to negotiate extensions, amendments, or new agreements that reflect marketplace developments.

B. WMG's Agreement with Clear Channel

One of WMG's recently concluded streaming agreements has been the focus of considerable media commentary and discussion, and I discuss some of its key terms here. In October of 2013, WMG entered into a trial agreement with iHeart Media, Inc. formerly known as Clear Channel Communications, Inc. relating to Clear Channel's internet simulcast and non-

simulcast transmissions. I will use the name Clear Channel in this testimony, since that is how the company is still commonly referred to.

Clear Channel is uniquely positioned as a streaming service. Clear Channel has an established record as one of the premiere nationwide media companies providing terrestrial broadcasts, internet simulcast of those broadcasts, and non-simulcast webcasts, as well as concert promotions and music video services. Clear Channel controls a massive share of the terrestrial broadcast market. It owns or operates more than 800 radio channels in more than 150 markets nationwide. It streams internet simulcasts from a large number of its channels. WMG has enjoyed a close, positive relationship with Clear Channel for many years.

Prior to the October 2013 agreement, Clear Channel paid SoundExchange for internet simulcasts and non-interactive streams of WMG music at per-play rates established by the NAB settlement negotiated pursuant to the Webcaster Settlement Act. Over a long period extending through 2012 and 2013, Clear Channel and WMG negotiated an agreement for WMG to directly license Clear Channel's internet simulcast and non-simulcast streams of WMG music. The resulting agreement between WMG and Clear Channel strikes a compromise that, from WMG's perspective, provided sufficient overall consideration to make a trial agreement attractive. (The agreement—which is Exhibit 1 hereto—is entitled a “Trial and Experimental Internet Simulcast and Webcasting Agreement.”) WMG and Clear Channel entered into an Amendment No. 1 to that agreement as of March 31, 2014 (Exhibit 2 hereto). Except as otherwise noted, the matters I discuss here relate to the October 2013 agreement.

WMG entered into the Clear Channel agreement because it perceived significant value in various contractual commitments—a number of which I describe below—that WMG believed Clear Channel would not be able to replicate in deals with other sound recording owners. WMG

thus believed the agreement provided it with very significant and unique economic advantages because WMG was the first major recorded music company to conclude a direct license with Clear Channel. The agreement also has provisions that ensure WMG will not be disadvantaged by being the first, or potentially the only, major recorded music label to have a direct deal with Clear Channel for internet simulcast and non-simulcast performances. The agreement has an initial term of three years, with a separate provision delineating WMG’s right to extend the agreement for a three-year renewal term under certain circumstances.

Several features of WMG’s agreement with Clear Channel deserve special mention and discussion here.

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] There is no right under federal copyright law for sound recordings publicly performed over terrestrial radio. The amount of the [REDACTED] [REDACTED]—is substantial. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] *for non-interactive webcasts*. Clear Channel has an active and growing service called “iHeart Radio,” which provides, among other things, “user influenced” or “customized” webcasting, *i.e.*, streams of music programming to listeners that are influenced by and tailored to individual listener preferences. By definition, these streaming transmissions are not simulcast with terrestrial radio transmissions. For these transmissions, Clear Channel pays

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] This is an important concept that I return to below.

[REDACTED]

[REDACTED] Clear Channel is contractually obligated to pay WMG [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]. This is a particularly valuable right for WMG. WMG's share of usage on any particular digital platform generally ranges between 15% and 20%, depending on the particular usage being measured (*e.g.*, individual track downloads or track-equivalent albums). If Clear Channel were to stream WMG's music roughly in proportion to WMG's general market share, WMG would expect its tracks to comprise around 15-20% of Clear Channel plays. [REDACTED]

[REDACTED] As a result, if Clear Channel [REDACTED]

[REDACTED]. In order to [REDACTED]

[REDACTED]

[REDACTED] The agreement also guarantees that WMG's royalties for the initial three-year term will be at least [REDACTED].

[REDACTED] Clear Channel also guarantees that, [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]. The [REDACTED] is defined by formula in the

comparable advertising. These commitments thus provide WMG substantial additional consideration as part of the overall deal.

Payments for [REDACTED]. Clear Channel also pays WMG for streams of [REDACTED] [REDACTED]. This is another piece of valuable consideration to WMG in the entire deal.

In sum, WMG agreed to enter into the Clear Channel agreement because it believed the deal provided a unique opportunity for WMG to obtain far greater consideration for the use of WMG content than WMG would obtain if Clear Channel used that content pursuant to the statutory license. At the same time, WMG ensured through the [REDACTED]

IV. General Principles Regarding Defining “Revenue”

As discussed above, many of WMG’s agreements with streaming services use a [REDACTED]

[REDACTED] In these agreements, the definition of “revenue” is an important issue. For WMG, it is critical that the agreement define “revenue” with sufficient breadth to encompass all income that the streaming service generates as the result of exploiting WMG’s repertoire. To implement this concept, the agreements generally take care in delineating several components of the “revenue” definition.

First, the agreements generally define “revenue” [REDACTED]

[REDACTED]

Second, the agreements generally provide that [REDACTED]

[REDACTED]

Third, [REDACTED]

[REDACTED]

Whether this deduction is permitted and the terms of any such deduction depend on the specific circumstances of the agreement being negotiated as well as the service's business model.

If a directly licensed streaming service has income streams attributable to a combination of WMG's music and some other product or service, [REDACTED]

[REDACTED] For example, the service may offer consumers a bundle of items, such as access to music combined with a wireless phone plan. Or, the service may receive advertising income for ads that appear in connection with music offerings as well as other offerings. In these circumstances, [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

V. Fees for Ephemeral Rights

In agreements with streaming services, WMG does not separately negotiate royalty rates for the performance of sound recordings and the making of ephemeral copies of sound recordings—*i.e.*, server copies. Rather, because licenses for both activities are required for the operation of a digital service, WMG negotiates a single bundled royalty rate that includes both rights as part of the license. In my experience, directly licensed services have not generally negotiated with WMG to obtain any specific allocation of royalties between the two license grants. This is most likely because directly licensed streaming services are not affected in any way by a specific allocation between the two rights, so long as they receive the full bundle of rights necessary to operate their service.

VI. Audit Rights

As noted, WMG’s agreements with streaming services generally provide WMG with important rights to audit a service’s compliance with its contractual commitments, including

payment and other obligations. While WMG has found that its partners generally aim to be diligent and accurate in their reporting, there are a number of factors that can cause a partner to fall short, including inadvertence, technical error, or the partner reads the agreement's requirements differently than WMG does.

WMG's agreements generally do not require that a certified public accountant ("CPA") perform royalty audits with its digital partners. Auditors who conduct royalty audits of digital services generally do not draw on the set of skills required to pass the CPA exam. Rather, royalty auditors must be able to understand the technical systems that WMG's partners use, to interpret data those systems maintain and generate, and the like. For example, a royalty auditor may have to examine a streaming service's server logs and content databases to determine the accuracy of the service's statement of performances and royalty payments. This could require understanding how the service's systems record digital performances, how those records are retained, and how those records are used to generate royalty statements. In addition, royalty auditors must be familiar with some of the unique conventions and jargon in the music industry as well as the royalty terms applicable to each service provider. For instance, auditors need to understand how to calculate a pro-rata share from a label pool, how performances are defined in the relevant contracts, and how to account for non-royalty-bearing plays.

Because royalty audits require extensive technical and industry-specific expertise, in WMG's experience a CPA certification is not generally a requirement for conducting such audits. To my knowledge, some of the most experienced and knowledgeable royalty auditors in the music industry are not CPAs.

VII. Role of the Collective for Statutory Licensing

WMG strongly believes that in the interest of efficiency for both the services involved in this proceeding and those who receive revenues from the statutory license, there should be one unified licensing collective, and that SoundExchange should be that collective.

SoundExchange is a nonprofit organization governed by an equally weighted coalition of artists (and representatives of artist organizations) and representatives of recorded music organizations. It takes a significant amount of time and effort for the interested constituencies to oversee and provide support (*e.g.*, Board and Board committee service) to SoundExchange. It would be very difficult for all interested constituents to provide comparable services in connection with more than one licensing collective.

SoundExchange has been repeatedly designated as the collective for statutory royalties and has done a commendable job in this role. It collects and distributes royalties from and to countless parties and persistently seeks out artists and record labels that may not be aware of monies being held for them.

For these reasons, and based on its track record, SoundExchange should maintain its position as the sole licensing collective.

I declare under penalty of perjury that the foregoing testimony is true and correct.

Date: 6 October 2014

Ron Wilcox
Ron Wilcox

Exhibits Sponsored By Ron Wilcox

Exhibit No.	Sponsored By	Description
SX EX. 001-DR	Ron Wilcox	Exhibit 1 - Trial and Experimental Internet Simulcast and Webcasting Agreement with Clear Channel Communications, Inc. dated October 1, 2013
SX EX. 002-DR	Ron Wilcox	Exhibit 2 - First Amendment to Trial and Experimental Internet Simulcast and Webcasting Agreement with Clear Channel Communications, Inc. dated March 31, 2014

SX EX. 001-DR

**RESTRICTED — Subject to Protective Order in
Docket No. 14-CRB-0001-WR (2016-2020) Webcasting**

SX EX. 002-DR

**RESTRICTED — Subject to Protective Order in
Docket No. 14-CRB-0001-WR (2016-2020) Webcasting**