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

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

TESTIMONY OF

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PUBLIC VERSION

Witness for SoundExchange, Inc.

BACKGROUND

1. I am Senior Vice President, Business & Legal Affairs, Global Digital Business, UMG Recordings, Inc. ("UMG Recordings"), a position I have held since 2013. UMG Recordings, Inc. is the primary recorded music company in the United States for the Universal Music Group. Universal Music Group (hereafter, "Universal") is the colloquial name for the group of music related companies owned by Vivendi S.A. Together, these companies comprise the world's largest recorded music company. Along with other members of the Business & Legal Affairs team in the Global Digital Business department, I negotiate deals with various digital music services that use Universal's repertoire of sound recordings. Such services include on-demand and customized streaming services, download and ringtone stores, locker services, and various types of subscription services. I have negotiated deals on Universal's behalf for the past nine years. During that time, I have negotiated more than 100 agreements with digital music services.

2. Prior to assuming my current position, I was Vice President, Business & Legal Affairs, eLabs, UMG Recordings. I began my employment with UMG Recordings in 2005 as Director, Business & Legal Affairs, eLabs. Prior to joining UMG Recordings, I was an attorney with the law firm Manatt, Phelps & Phillips, LLP, where my practice focused primarily on talent representation and advising companies in the acquisition of intellectual property and branded entertainment rights. I started my career as an attorney at Munger, Tolles & Olson, LLP in 1999. I received a J.D. from Yale Law School and a B.A. in Economics from Pomona College. I am licensed to practice law in California.

3. I previously testified before the Copyright Royalty Board in 2012 in connection with the rate-setting proceeding for certain satellite and cable television services.

DISCUSSION

I. Universal's Position In The U.S. Music Industry

4. Universal's share of the U.S. recorded music market is approximately 38%. This includes the recorded music repertoire of UMG Recordings, as well as the recorded music assets previously owned by EMI Music. Universal acquired EMI's recorded music assets in 2012, and today our department handles agreements related to the online dissemination of all of this content.

5. Universal's recorded music holdings are comprised of an extensive and diverse collection of record labels, including A&M Records, Blue Note Records, Capitol Records, Capitol Christian Music Group, Caroline, Decca, Def Jam Recordings, Deutsche Grammophon, Geffen Records, Interscope Records, Island Records, MCA Nashville, Motown Records, Republic Records, Show Dog–Universal Music, Universal Music Latino, Verve Music Group, and Virgin Records. The artists who record for Universal labels include the best known and most popular recording artists in the world, including, among others, U2, Imagine Dragons, Maroon 5, The Black Eyed Peas, Drake, Bon Jovi, Mariah Carey, Ariana Grande, Dr. Dre, Kanye West, Alan Jackson, Tim McGraw, Keith Urban, Norah Jones, The Killers, Lady Gaga, Madonna, Lorde, Lionel Richie, Sting, George Strait, and Stevie Wonder. Universal's extensive catalog of sound recordings includes music by some of the most influential and legendary artists in the history of music, including Louis Armstrong, The Beach Boys, The Beatles, James Brown, Eric Clapton, Patsy Cline, Ella Fitzgerald, Marvin Gaye, Guns N' Roses, The Jackson Five, Lynyrd Skynyrd, Bob Marley, Nirvana, The Rolling Stones, Kenny Rogers, Frank Sinatra, and The Who.

6. Universal also has an extensive international presence, operating through affiliated companies, joint ventures, and other entities authorized to disseminate its content in more than 70 countries worldwide.

II. Universal's Approach To The Market For The Distribution Of Recorded Music

A. The Shift From Ownership Model To Access Model

7. The market for recorded music continues to change at an extraordinary pace. This change has accelerated greatly within the last five years. That change likely will continue even more rapidly over the next five years. In particular, we are in the midst of a highly accelerating transition from the traditionally dominant "ownership" model of consumers acquiring recorded music to a model that will be predominantly "access."

8. The "ownership" model is one in which the consumer purchases a copy of a particular piece of recorded music, traditionally an album (whether on vinyl, cassette, or CD) or, in more recent times, a permanent download through an online retailer such as the iTunes Store. Once purchased, the copy of the music would reside in the consumer's music "library," either in a record collection, on a hardware device (such as an iPod), in a cloud collection on a locker service's remote servers (such as iTunes Match), or some combination of the three. For a full album permanent download sold on iTunes, the range of return to Universal is between [redacted], after paying the expense of music publishing rights for between ten and twelve songs on the album. When the consumer purchases a single permanent download track, the return to Universal generally would be around [redacted] or [redacted], after paying the expense of music publishing rights, for single tracks with a retail price of $0.69, $0.99, or $1.29.

9. In contrast, in an "access" model, consumers do not obtain permanent copies of sound recordings, but instead utilize services that play recordings for listeners. Over the last

decade numerous services that digitally stream music to consumers have come into being and gained in popularity. These services provide materially different types of access to musical content. A number of these services are "on-demand," meaning that, among other features offered, the service allows users (or subscribers) to choose the immediate next song that they will hear and create playlists of songs in the exact order in which they want to listen to them. Some well-known on-demand services are Spotify and Rhapsody. Other such services offer programmed, customized, or personalized webcasting. Examples include Pandora, Slacker, and iHeartRadio.

10. For purposes of understanding the shift to an access model from an ownership model, a particularly important development is the deployment by webcasting services of customized, or personalized, offerings. Customized webcasting services transmit individual recordings to individual users. In addition, customized services utilize computer algorithms to respond to the preferences of individual users, so that, although the user may not be able to select the precise track that will be streamed to his or her device, the user can significantly narrow, or "fine tune," the music that he or she will hear. This can be done in a variety of ways, including expressing "likes" or "dislikes," such as "thumbs up," or "thumbs down," or using interface controls that ask the service to play certain music more, or less, like the track the service is streaming to the user at that moment. If a user has "customized" her or his preferences through a streaming service, the user knows they have a good chance of hearing songs they like, or others like them, and thus see a diminished need to own the particular recording.

11. Over the past few years, we have grown to understand that neither on-demand nor customized streaming services promote sales of recorded music. To the contrary, our observations of the market, especially over the last year, have been that these services are

drawing consumers and revenue away from the sale of permanent downloads and CDs. The most visible example of this and the market's transition away from an ownership model to an access model is the rapid decline in permanent download sales. January is typically our biggest month for download sales because iTunes gift cards are a common holiday gift. In January 2014, however, we saw a 20% decline in download sales from the prior January. Since January, the rate of decline has decreased somewhat from the prior year, but it is still 18% year-to-date. Conversely, the number of listener hours on customized and on-demand streaming services rose substantially over the same period. This imbalance—with higher streaming hours and significantly reduced download sales—has provided further confirmation to us that on-demand and customized streaming services do not promote sales of downloads. Rather, the widespread access to such streaming music services has helped to accelerate the decline in purchases of permanent downloads. As a result, Universal is depending more and more on revenues from all types of streaming services.

B. The Importance Of Revenue-Generating Access Services To Universal's Ability To Recover Its Substantial Investments In Recorded Music

12. As a consequence of this shift from an ownership model to an access model, revenues from streaming services have become increasingly important to Universal's ability to recover the substantial investments it makes in the discovery and development of recording artists, and the production and marketing of recorded music. Going forward, we will not be able to rely on revenues from the sale of permanent downloads or CDs. Thus, revenues obtained from streaming services will need to increase to ensure Universal receives a fair return on its investment in the creation of music. This is not only fair, it is sound economics. Universal's repertoire (along with other music) serves as the foundation upon which each of these services is built—without the music, these services would not exist.

13. In our experience, a service's ability to return sufficient value to Universal depends on the amount of average revenue per user ("ARPU") the service can generate. In particular, we have found that streaming services cannot generate sufficient ARPU through advertising alone. This is in part because streaming services are reticent to play advertisements at the same frequency as terrestrial radio. Most streaming services play an average of 3 minutes of advertising per hour, compared to the 10-15 minutes per hour for terrestrial radio. According to publicly available information, Pandora plays only an average of 1.5 minutes per hour. Publicly available statements from streaming services reflect the services' predictions that advertising revenues will grow as advertisers become more comfortable with the audience that the services reach. However, webcasting services have been slow to increase advertising inventory because they are currently focusing on growth in number of users and listener hours, rather than monetization and profit. Therefore, we have not yet seen advertising generate substantial revenues for services and, in turn, substantial revenues to Universal. For this reason, we require minimum advertising loads in our direct deals for ad-supported services, as well as a path to conversion to paid subscription. For example, in our agreement with [redacted], we require the service to play a number of advertisements per hour that increases with the number of months the user has been listening to the service. For a user that has been listening to the advertising-supported service for [redacted] months, the service plays a minimum of [redacted] of advertising per listener hour with at least [redacted] within the first [redacted] of the session. For users on the service from [redacted] months, the requirement increases to [redacted] and for users on the service longer than [redacted] months, the requirement increases to [redacted].

14. Subscription offerings, in contrast, can generate a higher ARPU. In Universal's direct deals, it shares in this higher ARPU. Consumers are willing to pay for a subscription to a streaming service for multiple reasons: subscriptions can allow users to avoid advertising, to access streams at a higher level of sound quality, to listen to music offline, or to be able to hear a song or album on-demand. Advertisers, on the other hand, do not necessarily pay higher rates for the additional features that come with a subscription; rather, they pay for traffic numbers and time spent listening. Universal prefers to do deals with services that drive toward subscription versus non-subscription services because the former are able to generate monetary value, in the form of higher ARPU than non-subscription services, and accordingly generate more significant returns to Universal in exchange for the right to exploit Universal's repertoire. As explained more fully below, Universal generally negotiates conversion incentives or other structural mechanisms that ensure the service encourages users to subscribe.

15. On-demand subscription services generally return an ARPU in excess of [redacted] per month to Universal, or [redacted] per year. Subscription services also pay much higher effective per-play rates, averaging more than [redacted] per play for on-demand services and close to [redacted] per play for those programmed services with which we have direct licenses. Thus far, the most prominent webcasters have operated predominantly non-subscription services. Those that do have subscription services, such as Pandora, appear to have made a business judgment not to encourage users to subscribe. Even if statutory services did encourage subscriptions, Universal and other rightsholders would not share in this revenue because the statutory rates are only a per performance fee, not a greater-of per performance and share of revenue.

16. Our approach to the terms on which we will authorize subscription streaming services to use our repertoire continues to evolve. In prior years, Universal was willing to authorize the right to stream its repertoire to a substantial number of services without significant restriction. As revenue from streaming services becomes much more important to Universal's overall revenue, growing from [redacted] to [redacted] of Universal's digital revenue over the last five years, we have become more deliberate than in prior years about the terms on which we will authorize the use of our repertoire for such purposes. In particular, we seek to ensure that services to which Universal grants the right to use sound recordings will generate revenue and not just divert revenues from other forms of exploitation, including from higher ARPU subscription streaming services. For example, although revenues received through SoundExchange from Pandora make it [redacted] source of revenues in the United States, its ARPU is particularly weak. To Universal, this suggests that Pandora is streaming music to users who might otherwise pay for a subscription or use a higher ARPU streaming service. For this reason alone, Universal would never do a deal with Pandora at the rates it currently pays.

III. <u>Influence Of The Statutory License On Universal's Deals With On-Demand Streaming Services</u>

17. Most of Universal's directly negotiated agreements with streaming services are for services that want to offer "on-demand" streaming. The statutory rates have less of an influence on Universal's negotiations with on-demand subscription services than Universal's negotiations with webcasting services. I believe these agreements therefore are a better proxy for market rates than agreements with services whose functionality either makes them eligible for the statutory license, or that could be changed to become eligible for the statutory license without significant disruption to the service's mode of operation.

18. Nonetheless, the statutory rates are always in the background of our negotiations with on-demand services and have had a downward influence on the rates over the last few years. These negotiations are anchored by the statutory license because on-demand subscription services compete with statutory services for large portions of the same base of users. Because on-demand services like Spotify compete directly with statutory webcasters like Pandora, our directly negotiated rates have fallen over the past few years in response to the low statutory rates. Unless the statutory rates are set closer to the market rate for streaming services generally, on-demand rates will likely continue to fall to bring about parity in the market. As a result, I believe the statutory rates need to increase over the next rate term to reflect the fact that customized webcasting services are becoming more and more personalized and competing directly with the on-demand services.

19. Notably, many services offer both on-demand and programmed or customized streaming. While such services may have the ability to elect the statutory license for the latter under 17 U.S.C. § 114, companies offering both services frequently negotiate with Universal for authorization to stream Universal sound recordings on both services. It has been our experience in negotiations that on-demand subscription services whose consumer offering feature an ad-supported, customized webcasting "tier" strongly resist rates for such tiers that are higher than the statutory rates. It also has been Universal's experience that such services will seek rates for their customized webcasting tiers that are *lower than* the statutory rates, both because the services provide Universal with additional consideration through other deal terms such as usage data and marketing analytics and because the customized webcasting tier is used as a tool to convert free users to the paid on-demand service. For example, during negotiations with

[redacted], the service took the position that its rates should be discounted because it intended to use the webcasting tier of service to upsell users to the subscription tiers.

20. In addition, parties with whom Universal negotiates can and do use the threat of transforming their operations to fall within the statutory license as grounds for seeking reductions in the rates or other forms of consideration provided to Universal. An example of this phenomenon can be found in Universal's recent negotiation with Slacker Radio. Slacker Radio currently offers three tiers of service:

- **Slacker Basic Radio:** an ad-supported tier, the functionality of which closely approximates the functionality found in services operating under the statutory license;
- **Slacker Radio Plus:** a subscription tier for $3.99 per month that has no advertising, no limit on the number of skips, and permits users to play stations offline;
- **Slacker Radio Premium**: a subscription tier for $9.99 per month that has all the features of the Plus tier, but also permits on-demand plays and allows users to create their own playlists.

[redacted] This threat was made after Last.fm did in fact opt to go through SoundExchange after the direct deal with Universal expired.

21. In sum, based on Universal's experience, the availability of the statutory license has a significant effect on the rates that Universal will receive for streaming services' exploitation of its repertoire.

IV. Important Terms In Universal's Direct Deals With On-Demand Streaming Services

22. In this section, I explain how Universal approaches its negotiations for direct deals with on-demand streaming services and what Universal aims to receive in consideration through those negotiations. I also provide examples from concluded agreements of how Universal has been able to achieve some of these objectives. It is important to emphasize at the outset that, although we have clear priorities in negotiating, Universal is not rigid in its approach to deal-making. Through negotiations with our streaming service partners, Universal attempts to achieve an optimal overall return to Universal for the use of its repertoire.

23. Universal's goal is to create meaningful strategic partnerships. In this endeavor, we look for a service that has a strong business plan for growing ARPU. Before we go forward with any direct negotiations with new services, we ask them to fill out a "new partner questionnaire" which allows us to better evaluate their business plan. We ask about their funding sources, their management, their business model, plans for scaling the service and increasing revenues over time, as well as how they will distinguish their service from others on the market. I have attached a copy of our questionnaire as Exhibit 1 to my testimony. We also conduct diligence on the business model and financial stability of the prospective partner. We view the value to Universal of our direct deals based on the entirety of the agreement. In particular, the stated royalty rates alone do not capture the full value that Universal receives from these deals.

24. In the sections that follow, I will describe some of the types of monetary consideration that Universal receives from its direct deals, then I will describe some of the non-monetary terms that provide substantial value to Universal.

A. Universal Obtains Substantial Monetary Value From Its Direct Deals With On-Demand Services.

25. In general, Universal's direct deals share several key features that are important to understanding the overall consideration that Universal receives. First, we work to obtain rate structures that not only ensure a minimum level of compensation to Universal, but also a potential to share in the upside of services that are built on our repertoire. Second, Universal ties the rates to advances, minimum guarantees, flat fees, and shortfall payments that set expectations for the service's performance. Third, Universal seeks marketing and promotional guarantees that ensure that the service compensates Universal proportionately to its market share.

(a) Rate Structure and Rates

26. One of the most important aspects of our direct deals is that they provide a rate structure based on the "greater-of" several different methods of calculating rates. Universal almost always requires a greater-of rate structure because it both guarantees a minimum level of compensation for the use of Universal's music and it gives us a chance to share in the upside of a successful service. Within the greater-of structure, one or two of the tiers are "floor" rates, either a minimum per play or a minimum per subscriber. Per play fees in particular compensate Universal for the intrinsic value of our music and the fact that consumption of music on any platform takes away from consumption of music elsewhere. The per play fee is crucial to an ad-supported or otherwise free-to-the-consumer service to ensure that the service has an incentive to monetize its user base. For the subscription tier of a service, Universal has moved away from requiring per-play fees. However, Universal insists on a minimum share of per-subscriber revenue that results in an effective per play rate.

27. The other component of the greater-of rate structure is Universal's proportionate share of the service's gross revenue. If the service is successful, we believe that we are entitled

to share in that success, because music is the single most important ingredient on which the service builds its business. Universal's deal with [redacted] illustrates a typical rate structure for an on-demand subscription service with a free-to-consumer offering and a premium mobile offering. This deal also offers an annual discount and a discounted family plan, which are aspects of several of our deals. The rate structure is as follows:

[redacted]

[redacted]

[redacted]

[redacted]

I have included a copy of this agreement as Exhibit 2 to my testimony.

28. In the United States, Universal does not have a single agreement with an audio streaming service that does not include a greater-of rate structure. If we negotiated a deal on a pure percentage of revenue, we would require a substantial minimum guarantee to ensure adequate compensation for Universal's music. Likewise, if we did not have the opportunity to

share in the upside of a successful service, we would seek higher per subscriber or per play compensation.

29. Closely tied to the rate structure are conversion incentives for subscription services that offer a free-to-the-consumer tier. If the service wants to offer a free-to-the-consumer tier, we require built-in conversion incentives to ensure the service pushes consumers toward the higher ARPU service. For example, as mentioned above, our deal with [redacted] includes certain conversion incentives as follows:

[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]

[redacted]

30. Universal also requires a per play or per user minimum to protect against the risk that the service would defer revenue from these free users while actively seeking to gain market share. For example, [redacted] I have attached this agreement as Exhibit 3 to my testimony. These free-to-the-consumer rates must be viewed in conjunction with the higher per subscriber minimum. Universal would never offer such rates on a stand-alone basis. When Universal did enter into deals with streaming services without a subscription component, the per play rate was between [redacted] and [redacted] per play. Today, these services typically do not generate sufficient

ARPU, and, as a result, Universal prefers to focus on subscription services that provide a greater return on its investment.

31. Within the greater-of rate structure, Universal generally seeks the following rates: First, for the per play floor, Universal generally seeks a per play minimum of [redacted] for on-demand subscription services and above [redacted] for non-subscription services. Second, for the revenue share, Universal generally seeks its share of [redacted] of revenue. This share of revenue is purposeful. It roughly approximates the percentage of revenue that Universal receives for the sale of a permanent download. Third, for the per subscriber floor, Universal generally seeks a per subscriber minimum tied to the consumer price, usually Universal's share of a [redacted] label pool per subscriber for a $10 per month subscription service. These numbers also reflect the labels' collective share of the service's revenue. For example, when the revenue share for a service is [redacted] the per subscriber minimum is generally [redacted] and when the revenue share is [redacted] the per subscriber minimum is [redacted]. Occasionally, Universal will combine the per subscriber share with a non-pro rata per-subscriber minimum to ensure that the royalty reflects Universal's market share. For example, Universal's agreement with [redacted]

> [redacted]
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> [redacted]
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> [redacted]
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> [redacted]
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> [redacted]

[redacted]

32. These stated rates are not how we ultimately value the consideration received. Rather, we calculate "effective" rates that incorporate these rates, but also all the other consideration to achieve an overall value that is generally higher. On an effective rate basis, virtually all subscription services pay Universal more than [redacted] per play.

(b) Advances, Minimum Guarantees, Flat Fees, and Shortfall Payments

33. Universal seeks compensation in the form of advances, minimum guarantees, shortfall payments, and flat fees. These terms mitigate the risk that a service will fail, underperform, or try to "game" the contract. We calibrate these payments so they are both achievable for the service but also enough of a stretch to ensure the company will invest and grow their streaming business. To set the appropriate advance or minimum guarantee, we use the service's own projections of future revenue. The amounts of these payments therefore are calibrated to what we and the service expect it will pay over the term of the agreement. Sometimes, we allocate a specific minimum guarantee to a service offering to ensure that the partner will invest in growing that business. For example, our agreement with [redacted] allocated [redacted] that was only recoupable against the [redacted] offering in 2012 and [redacted] for 2013. In the case of the [redacted], this allocation reflected the offering's actual performance.

34. Overall, these guarantees have proven to be successful forms of consideration for both parties. When these tools are not successful, we often work with partners to allow an advance to be recouped over a longer term. For example, [redacted]

[redacted] For Universal, the most important aspect of these forms of consideration is having it upfront and guaranteed which minimizes our risk in the partnership.

35. Universal's effective rate calculation takes into account the total value, including these upfront and true-up payments. Because the statutory license does not come with any advance or minimum guarantee of payment, the statutory rates must be higher to match the market value for this form of guaranteed consideration.

(c) Marketing and Promotional Guarantees

36. Universal also derives significant value from enhanced marketing and promotion of Universal artists. Although not as easily quantifiable as direct cash payment, enhanced marketing and promotion is quite valuable consideration for the use of Universal's content.

37. Enhanced marketing commitments can take a number of forms. Some commitments ensure promotional commitments for Universal artists relative to promotion the services provide to other rights owners. For example, our agreement with [redacted] Provisions such as this provide significant value to Universal, vis-à-vis support that a service might otherwise use in favor of Universal's competitors. In the physical space, Universal used to pay retail stores co-op advertising fees to ensure better placement of our music and increased promotion of our

artists, but we now obtain those commitments directly in our agreements with streaming services.

38. Universal will often negotiate for mandatory spends on marketing the service itself. For example, [redacted] For a new or emerging service, this is an investment that is mutually beneficial because it reduces the likelihood that the service will fail and creates additional opportunities for showcasing Universal artists.

39. Ultimately, these marketing and promotional guarantees have monetary value because Universal does not need to buy advertisements on the service or otherwise target the service's users. For example, [redacted] The market price for this advertising, [redacted] Accordingly, Universal considers this to be additional monetary consideration not available under the statutory license.

B. Universal Obtains Substantial Non-Monetary Value From Its Direct Licenses.

40. In addition to the monetary consideration received, Universal obtains substantial benefits in the form of non-monetary consideration from its direct deals with on-demand services. Although we cannot easily assign a value to these benefits, without many of them—most notably, holdback rights, user data and security precautions—we would not authorize the use of Universal's sound recordings. None of these benefits inheres in the statutory license.

Because any compliant service can obtain a statutory license for Universal's sound recordings, the rates should be higher to compensate for the lack of these common benefits generally included in our direct deals.

(a) Short Deal Terms

41. Universal's direct deals average in duration from one to three years. Generally, we seek a two-year term or less to ensure that we can adapt as the market evolves. We would never risk a five-year deal term—the length of the statutory rate period, except in extraordinary circumstances. It is important that the statutory rates account for the risk that Universal and other content owners would face if the rates were set too low. If the rates are set too low, Universal has no ability to opt-out of the statutory license. This would put both Universal and the interactive streaming services with which it partners in a very difficult place until royalty rates could be reset to match the market price. However, if the rates are too high, services have the option of opting-out of the statute and doing direct deals at market rates. Although a statutory rate above market rates would give us some negotiating leverage, ultimately, it would be in our interest to find a rate that enabled the service to grow and be profitable.

(b) Holdback Rights

42. [redacted] As we see the market evolving, we see holdback rights becoming a more important aspect of our partnerships. One clear way to drive users to a service is to offer an exclusive release on that service. Moreover, we could help a service encourage subscriptions by offering specific content to subscribers only. Unfortunately, statutory services can gain near immediate access to sound recordings once we

have publicly distributed phonorecords of those sound recordings, thereby undermining the effectiveness of either strategy.

43. [redacted] For example, our agreement with [redacted]

(c) User Data

44. Increasingly, we have found that user data is one of the single most important benefits of our partnerships with streaming services. Among other sources of information, we are able to obtain user data that shows the geographic regions in which specific artists are popular or are gaining popularity. We can also see which artists appeal to certain demographics (by age, gender, type of device used, etc.). The data that partners provide to us can indicate when a track from an album is gaining in popularity such that Universal should consider releasing it as the next single. Information regarding user behavior is crucial to helping Universal and our artists understand how their music is being received by their fans and decide where to target marketing efforts and where to tour.

45. Universal employs a full analytics team of approximately forty people. This team devotes their time to analyzing the data for trends that help us make well-informed decisions

regarding how to promote certain artists. To illustrate how important user data is to Universal, we have entered into a strategic partnership with [redacted] In that deal, we agreed to waive our standard [redacted] per track content delivery fee in exchange for the data, which amounts to more than [redacted] for our full catalog. Although statutory services are required to report the tracks that they have played so the royalties are properly distributed, they do not report any user data information. Accordingly, this is a benefit that Universal regularly receives in the market but that is not available under the statutory license.

(d) Security Guarantees

46. Security precautions are potentially priceless because they protect Universal's single most valuable asset: its catalog of sound recordings. Security guarantees are especially crucial for Universal to be willing to authorize the use of its content given that unscrupulous online companies have spent more than a decade enabling the mass pirating of our content. Before we finalize any agreement, we ask the service to submit a technical white paper on their security protocols. Our Advanced Technology staff of four engineers and computer scientists spends weeks investigating each streaming service's ability to protect our content on its servers and to deliver content to users in a way that prevents capture or download. Adherence with these protocols then becomes a condition of the agreement.

47. We have extensive security requirements. By way of example:

- We require that services not partner with peer-to-peer sharing services;
- We require services to take active steps to stop piracy, including by using encrypted streaming or true streaming;

- We also require our partners to use territorial filtering that prevents individuals from accessing a service if it is not offered in their territory;
- We require services to have an anti-hacking policy and to monitor their system for any security breaches and immediately inform Universal if one has occurred; and
- We require the service to implement an end user agreement that requires users to comply with all security measures and agree to not make any infringing use of the music as a term of use.

48. While the statute prohibits any affirmative act to facilitate reproduction of phonorecords, it does not prevent webcasting services from keeping files in insecure locations or from delivering those files to users as unencrypted progressive downloads, which are much easier to capture than true streams or encrypted progressive downloads (our minimum requirement in direct deals). The statute is also silent on other security protocols that are standard in our direct deals, such as territorial filtering. We recently became aware that a number of NPR digital stations are available outside the United States, but Universal has no recourse to limit the streaming because there is no contractual relationship with NPR.

49. To remedy some of these security risks, Universal has entered into agreements with statutory services to provide them content directly in exchange for a relatively small content delivery fee and security guarantees. For example, iHeartRadio stations must comply with our security and territorial filtering requirements to maintain access to our direct United States content feed. Although we have directly negotiated for security guarantees and content delivery fees with certain statutory webcasters, the statutory license does not mandate that we will receive this benefit.

(e) Fan Engagement

50. Universal also looks for ways to engage fans through the services. In addition to the marketing guarantees described above that require the service to include Universal artists in

its promotional materials, we also seek to access fans directly. Several of our agreements include a term that gives Universal access to the email addresses of users. For example, [redacted] We spend over [redacted] per year to maintain our email database. In addition, Universal seeks to include label-specific pages or playlists on services. These pages and playlists allow Universal's record labels to directly reach fans and give exposure to up-and-coming artists.

V. Universal's Direct Deal with Nokia Mix Radio Is Unique

51. In 2012, Universal entered into a direct agreement with Nokia for a customized webcasting service that would be bundled with Nokia devices. The idea was for Nokia to have a brand-specific music streaming service to help differentiate its phones. The service launched with a free-to-the-consumer streaming service available to each user owning a Nokia device. As a requirement of our deal, [redacted] The premium subscription service, known as MixRadio Plus, launched in 2013. The consumer price for the premium service is $3.99 a month for unlimited skips, unlimited offline listening and higher sound quality.

52. Although Nokia's webcasting offering is similar to that offered by statutory licensees, our deal was unique and very different from a statutory license for a number of

reasons, including that the fees Nokia pays Universal are [redacted], and we authorized Nokia to provide limited caching of sound recordings. The fees that we receive from Nokia are as follows: For the Basic MixRadio service, we receive [redacted] For MixRadio Premium service, we receive [redacted] I have attached this agreement as Exhibit 4 to my testimony.

53. Earlier this year Microsoft purchased the Nokia service and has recently spun it off into a separate company. We are currently negotiating the terms of a new deal.

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

Date: October 6, 2014

Aaron Harrison

Exhibits Sponsored By Aaron Harrison

Exhibit No.	Sponsored By	Description
SX EX. 003-DR	Aaron Harrison	Exhibit 1 - New Partner Questionnaire
SX EX. 004-DR	Aaron Harrison	[redacted]
SX EX. 005-DR	Aaron Harrison	[redacted]
SX EX. 006-DR	Aaron Harrison	[redacted]

SX EX. 003-DR

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

SX EX. 004-DR

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

SX EX. 005-DR

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

SX EX. 006-DR

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