Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
THE LIBRARY OF CONGRESS
Washington, D.C.

In the Matter of	)	
DETERMINATION OF ROYALTY RATES FOR DIGITAL PERFORMANCE IN SOUND RECORDINGS AND EPHEMERAL RECORDINGS (WEB IV)	)	**Docket No. 14-CRB-0001-WR (2016-2020)**

INTRODUCTORY MEMORANDUM TO THE WRITTEN DIRECT CASE OF iHEARTMEDIA, INC.

iHeartMedia, Inc. respectfully submits its written direct evidence for the consideration of the Judges. As the Judges will see, we propose a searching reexamination of the statutory rates, based on economic evidence, to the end of establishing rates that reflect what willing buyers and sellers would set in an actual, functioning market.

What we seek is a reset: the current rates, set by prior panels, were based not merely on limited or non-existent economic evidence, but on *bad* economic evidence. As the Judges have observed in recent orders, a linchpin of a prior proceeding – the testimony of Dr. Michael Pelcovits presented by SoundExchange – is indefensible and obviously wrong. Yet it was that testimony that justified high per-play rates that have afflicted webcasters and inhibited the growth of the webcasting industry, as the enclosed testimony of iHeartMedia's CEO Robert Pittman and venture capitalist David Pakman explains.

It is plain that the current rates are too high. As the Judges will see in the enclosed written testimony of Professors Daniel R. Fischel and Douglas G. Lichtman, the

current rate is higher than the rate that would maintain full compensation for copyright owners if webcasting *eliminated* all their other revenues. That is, current rates pay those owners *as if* internet radio were a complete substitute for purchasing music, attending concerts, and all other sources of revenue for the labels.

But in fact we know that this is not the case. As the testimony of Professor Brett Danaher demonstrates, the webcasting services at issue in this proceeding *promote* sales, thereby *producing* sales (and revenues) for copyright owners rather than taking them away. As the testimony of iHeartMedia's Tom Poleman and Bob Pittman proves, exposure through "spins" is the critical element that drives music sales, and artists and record labels exert enormous energy to place their works before the public on iHeartMedia's stations for that reason. Copyright holders want to have their cake and eat it too: the indisputable promotional benefits of spins *and* the highest possible payment rate they can gain.

It is time for a fresh and more penetrating look, based on substantial new evidence that was not available to prior Judges. We now have, for the first time, actual evidence of a market negotiation between a major record label (Warner) and a leading webcaster (iHeartMedia). The result of that recent negotiation established, in economic substance, two rates: a rate of $0.0023 to $0.0025 – that is, the statutory rate – for the spins of Warner music that iHeartMedia would have performed in the absence of any agreement with Warner; and a rate of **$0.0005** for the *additional* spins iHeartMedia agreed to give Warner as a result of their agreement. This latter rate actually shows what market actors, unconstrained by flawed statutory rates, agree upon as fair per-performance compensation, as Professors Fischel and Lichtman explain in detail in their testimony.

Other economic evidence strongly supports the conclusion that $0.0005 per performance is the market rate. The independent label deals that iHeartMedia has struck set a rate for additional spins that is below $0.0005 per performance. The satellite rate, set by the CRB, likewise supports the $0.0005 per-performance rate. And a careful analysis of the economics of the internet radio business is yet another vector pointing to the reasonableness of this rate – as well as the crippling excess of the rate to which broadcasters are now subject and will be subject through 2015. These vectors are all described in detail in the report of Professors Fischel and Lichtman.

Ultimately, as the Judges will see, the evidence of the promotional benefits of spins is overwhelming, as the testimony of iHeartMedia's Pittman and Poleman, and the data provided by Professor Danaher, demonstrate. Since the days of illegal "payola," copyright holders have competed with each other for the obvious benefits of broad exposure through broadcasting. In a functioning market – without a monopolist SoundExchange, and without a mandatory, artificially high rate the copyright holder can insist upon – buyers and sellers would in fact agree upon a per-performance rate of $0.0005, and indeed they have agreed upon that rate when recent contracts are properly analyzed.

Summary of the Written Testimony of iHeartMedia's Witnesses[1]

A. Expert Witnesses

Daniel R. Fischel and Douglas G. Lichtman are both affiliated with the economic consulting firm of Compass Lexecon, where Professor Fischel serves as President and Professor Lichtman as Senior Consultant. Professor Fischel is also the Lee and Brena

[1] Pursuant to the Interim Protective Order entered on October 2, 2014, iHeartMedia is filing both Restricted and public versions of certain of its written direct statements.

Freeman Professor of Law and Business Emeritus at The University of Chicago Law School, and Professor Lichtman is also a Professor of Law at the University of California Los Angeles. Their joint testimony supports iHeartMedia's rate proposal.

Professors Fischel and Lichtman first consider the license agreements that iHeartMedia has signed with 28 different record labels, including one of the three major record labels, Warner. These agreements are recent, cover precisely the statutory webcasting services at issue here, and were negotiated on both sides between entities with an important stake in establishing market rates. Most importantly, these are the first and most comprehensive agreements of which iHeartMedia is aware that provide a way to determine the rate to which a willing buyer and willing seller would agree for the statutory webcasting services at issue here, in a free market unconstrained by government regulation or interference. Professors Fischel and Lichtman conclude that iHeartMedia's agreements provide a reliable basis to determine a range of rates that meet the statutory criteria applicable in this proceeding, and that iHeartMedia's proposed rate is within this range (indeed, at the high end).

Professors Fischel and Lichtman also perform several additional analyses, each of which provides further confirmation that the current statutory rates are excessive and that the range of rates derived from the iHeartMedia agreements is reasonable. First, they perform a financial analysis of broadcast radio stations to determine the maximum amount such broadcasters would be able to pay for copyright royalties on the simulcasting of their radio broadcasts. Second, they analyze the royalty rates established for satellite digital audio radio services and, using those rates as a benchmark, make appropriate adjustments to determine a reasonable range of rates for the webcasting

services at issue here. Third, they perform a "thought experiment" to demonstrate that the current rates are so excessively high that they would far over compensate copyright holders even under the extreme and unrealistic scenario in which webcasting substituted for *all* other forms of music consumption. Finally, they demonstrate that the previous methodology used to establish rates – the benchmark analysis of SoundExchange's expert, Dr. Pelcovits – is highly flawed and, when corrected, provides further support for iHeartMedia's rate proposal.

Brett Danaher, Ph.D, is an assistant professor of Economics at Wellesley College. His research focuses on digital music and other digital media.

Dr. Danaher's testimony uses data from an Internet consumer panel tracking company to perform an empirical analysis of the effect of the webcasting services at issue here on other forms of music consumption. This analysis demonstrates to a high degree of statistical certainty that non-interactive webcasting services have a significantly greater promotional effect (and/or less substitutional effect) than interactive webcasting services. Dr. Danaher's analysis also provides strong evidentiary support that non-interactive webcasting services have a net promotional effect, whereas interactive webcasting services have a net substitutional effect.

David B. Pakman is a partner at venture capital firm Venrock, and a former founder and investor of a digital music service, with more than 14 years of experience in digital music. His testimony provides support for iHeartMedia's rate proposal and for seeking a fundamental rethinking of the current statutory rates. He demonstrates that, under the current rates, the industry has fared poorly, as demonstrated by the high failure

rate for webcasting services and the lack of investment in these services, relative to other digital industries.

B. Fact Witnesses

Robert Pittman is the Chief Executive Officer and Chairman of the Board of Directors of iHeartMedia. His testimony supports iHeartMedia's rate proposal and its request for a fundamental rethinking of the current statutory rates. He provides background of iHeartMedia's operations and business and establishes the foundation for understanding iHeartMedia's recent licensing agreements with Warner and more than two dozen independent record labels.

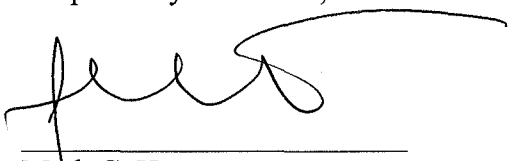
Steven Cutler is the Executive Vice President for Business Development and Corporate Strategy at iHeartMedia. His testimony describes iHeartMedia's efforts to reduce its music licensing costs for its Internet radio services. He provides details regarding iHeartMedia's agreements with Warner and the independent labels, including the assumptions and expectations of iHeartMedia's management and Board at the time these agreements were negotiated and entered. He also describes iHeartMedia's efforts to lower its royalty payments by substituting music content to which high rates apply with other content.

Tom Poleman is the President of National Programming Platforms for iHeartMedia. Drawing on his three decades in the radio industry, Mr. Poleman describes the significant ability of live radio to break new artists and songs and drive music sales – regardless of whether it is transmitted via broadcast radio or simulcast. He explains how iHeartMedia's promotional programs for new music enhance iHeartMedia's stations'

natural role as music discovery platforms for listeners, and increase music sales, to the benefit of artists and record labels.

Jeffrey L. Littlejohn is the Executive Vice President for Engineering and Systems Integrations at iHeartMedia. His testimony describes the technology that iHeartMedia has developed to replace the music content played on terrestrial broadcast radio with other content when that radio is simulcast over the Internet.

Respectfully submitted,



Mark C. Hansen
John Thorne
Evan T. Leo
Scott H. Angstreich
Kevin J. Miller
Caitlin S. Hall
Igor Helman
Leslie V. Pope
Matthew R. Huppert
KELLOGG, HUBER, HANSEN, TODD,
EVANS & FIGEL, P.L.L.C.
1615 M Street, NW, Suite 400
Washington, DC 20036
Telephone: (202) 326-7900
Facsimile: (202) 326-7999
mhansen@khhte.com
jthorne@khhte.com

Robert H. Walls, Jr.
Donna Schneider
iHeartMedia, Inc.
125 West 55th Street
New York, NY 10018
robwalls@iheartmedia.com
donnaschneider@iheartmedia.com

Counsel for iHeartMedia, Inc.

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