UNITED STATES COPYRIGHT ROYALTY JUDGES
The Library of Congress

In re DETERMINATION OF ROYALTY RATES AND TERMS FOR TRANSMISSION OF SOUND RECORDINGS BY SATELLITE RADIO AND "PREEXISTING" SUBSCRIPTION SERVICES (SDARS III)	Docket No. 16-CRB-0001 SR/PSSR (2018-2022)

ORDER GRANTING IN PART AND DENYING IN PART SIRIUS XM's MOTION FOR REHEARING and DENYING MUSIC CHOICE's MOTION FOR REHEARING

I. Introduction

The Copyright Royalty Judges (Judges) issued an Initial Determination in the captioned proceeding on December 14, 2017 (*Initial Determination*). On December 29, 2017, Sirius XM Radio, Inc. (Sirius XM) and Music Choice each filed a timely Motion for Rehearing.[1] On January 8, 2018, the Judges entered, *sua sponte*, an Order Permitting Written Response(s) to Motions for Rehearing, which also permitted moving parties to file written replies. On January 18, 2018, SoundExchange, Inc. (SoundExchange) filed separate responses in opposition to the Sirius XM motion and the Music Choice motion.[2] Sirius XM and Music Choice each filed a reply on January 25, 2018.

For the reasons detailed herein, the Judges **DENY** the Music Choice Motion and **GRANT in part and DENY in part** the Sirius XM Motion.

II. The Legal Standard for Rehearing

Under the Copyright Act (Act), the Judges may grant rehearing after a determination in "exceptional cases." 17 U.S.C. § 803(c)(2). 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 Judges' regulations require the moving party to identify the aspects of the determination that are either "without evidentiary support in the record" or "contrary to legal requirements." 37 C.F.R. § 353.2.

[1] All participants, except George Johnson d/b/a GEO Music Group (GEO), had until December 29, 2017, to file motions for rehearing. Mr. Johnson did not have access to the redacted Initial Determination until January 10, 2018. His 15-day period for filing a motion for rehearing ended on January 25, 2018.

[2] Mr. Johnson filed responses in opposition to the Sirius XM and Music Choice rehearing motions, adopting the SoundExchange reasoning.

The Judges' prior orders have further explicated this regulatory standard, providing that rehearing may be granted only when (1) there has been an intervening change in controlling law; (2) new evidence is available; (3) there is a need to correct a clear error; or (4) there is a need to 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*). In the *SDARS I Rehearing Order*, the Judges expressly adopted the standards for reconsideration of an order by 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)). *See SDARS I Rehearing Order* at 1.

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). A rehearing 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)). A party may not use a motion for rehearing erely to effect a change of tactics, to present a new theory, or to introduce new evidence after the trial has concluded. *Order Denying Motions for Reh'g* at 2, Docket No. 2005-1 CRB DTRA (Apr. 16, 2007). In support of their expressed limitations on motions for rehearing, the Judges have previously relied on the holding in *Fresh Kist Produce, LLC v. Choi Corp.*, 251 F. Supp. 2d 138,140 (D.D.C. 2003). *See Order Denying in Part… Motion for Rehearing …*, Docket No. 14-CRB-0001-WR (2016-2020) (Web IV) (Feb. 10, 2016) (citing *Fresh Kist Produce*). In *Fresh Kist*, the district court acknowledged a tension in motions for rehearing between: (1) "disapprov[al] of parties raising arguments that they could have advanced earlier"; and (2) consideration of "the interests of justice and fairness [that] support reviewing the plaintiff's motion." *Fresh Kist*, 251 F. Supp. 2d at 141.

III. Issues Presented in Sirius XM Motion

Sirius XM asserts that rehearing is warranted on the following specific rulings in the *Initial Determination*:

(1) the Judges' choice of a calculation methodology for Gross Revenues, which was used to derive "Average Revenue Per User" (ARPU),[3] which, in turn, was used to derive the applicable royalty rate for SDARS, resulting in an overstatement of that royalty rate;[4]

[3] ARPU is the quotient derived from Gross Revenue ÷ Total Number of Subscribers. *See* SEPFF ¶ 268, n.8 (indicating that the *numerator* in the ARPU calculation is "the revenue that Sirius XM reports to SoundExchange [*i.e.*, "Gross Revenue"] and is the base against which the percentage of revenue rate is applied under the relevant regulations."); SXMPFF ¶ 209 (indicating that the *denominator* in the ARPU calculation is the total number of "Users," which "includes both paid and trial subscribers.").

[4] The royalty rate calculation involves two related formulas: (1) the ARPU formula (ARPU = Gross Revenues ÷ Number of Subscribers) and (2) the royalty rate formula (Opportunity Cost ÷ ARPU = Royalty Rate). A lower Gross Revenues number translates into a lower ARPU. A lower ARPU translates into a *higher* Royalty Rate. In essence, Sirius XM contends that the Gross Revenues methodology that the Judges used resulted in a lower-than-warranted Gross Revenues number, which resulted in a higher-than-warranted royalty rate.

(2) the Judges' imposition of a regulatory "cap" on the Direct License Share that Sirius XM alleges is not mentioned, explained, or justified in the *Initial Determination*; and

(3) the Judges' imposition of a requirement in the regulatory language that deductible fees must be "charged to subscribers" and be "reasonably related to the Licensee's expenses to which they pertain," requirements that Sirius XM alleges are not mentioned or supported in the *Initial Determination*.

Sirius XM Motion for Rehearing (SXM Motion) at 1.

SoundExchange opposes each of these alleged grounds for rehearing.

A. The ARPU Issues

1. The Gross Revenues Definition that Formed the Basis of the Judges' ARPU Measure Was Proper

In the *Initial Determination*, the Judges set a royalty rate of 15.5% of Gross Revenues (as that term is defined for SDARS). *Initial Determination* at 1. The Judges calculated the rate by application of (1) an opportunity cost of $[redacted] per subscriber that the Judges based on credible evidence and (2) a $[redacted] ARPU that the parties agreed was appropriate if the Judges did not change the definition of "Gross Revenues" in the *Initial Determination*. *Id.* at 57.[5]

In its rehearing motion, Sirius XM claims that the $[redacted] ARPU is an incorrect measure, and that the ARPU should have been $[[redacted]], which would have yielded a royalty rate of 14.7%.[6] *Initial Determination* at 57 (cited in SXM Motion at 7). In particular, Sirius XM argues that in calculating the royalty rate the Judges erroneously failed to apply the then-prevailing definition of Gross Revenues, which is in the numerator of the ARPU formula. Sirius XM argues that the alleged change in the Gross Revenues definition had the effect of "expand[ing] the reportable revenue base beyond what Sirius XM reported in 2016." *Id*. at 3. Sirius XM argues, however, that the Judges "failed to recalculate the resulting 'regulatory' ARPU to reflect that change, using instead Sirius XM's 2016 ARPU, calculated from the now-superseded (and in places, previously interpreted) Gross Revenues definition in their percentage-rate derivation." *Id*. According to Sirius XM, "[t]he effect of converting the $[redacted] opportunity cost into a percentage-of-revenue rate using a lower ARPU ($[redacted]) than the ARPU resulting from application of the new Gross Revenues definition is an incorrect and overstated percentage rate." *Id*.

Notably, Sirius XM does not assert that the Judges changed the language of the "Gross Revenues" definition in a manner that would alter the ARPU used to derive the royalty rate. In fact, Sirius XM does not point to any changed definitional language that affected the ARPU

[5] The $[redacted] ARPU was calculated "from Sirius XM's monthly revenue reported to SoundExchange during the first six months of 2016." *Initial Determination* at 72, n. 141.

[6] The revised royalty rate would be derived as follows: [redacted] (opportunity cost) ÷ [[redacted]] (revised ARPU) =14.7% (rounded) (revised royalty rate).

calculation.[7] Rather, Sirius XM argues that the Judges applied a new "interpretation" of the Gross Revenues definition. *See, e.g.*, SXM Motion at 2, 3.[8]

In fact, the Judges adopted the interpretation of Gross Revenues that Sirius XM now claims to be "new" in a January 10, 2017, ruling (*Ruling on Referral*) relating to *SDARS I.*[9] The Judges entered the *Ruling on Referral* and provided it to the affected parties during the *SDARS III* proceeding, *prior to* the parties' filing of rebuttal testimony and *prior* to the hearing in the present proceeding. Clearly, Sirius XM was fully aware and on notice of any potential impact the Judges' interpretation might have on its calculation of ARPU in the present proceeding. Accordingly, the Judges find that their consistent application of the Gross Revenues definition in the *Ruling on Referral* and in the *Initial Determination* was proper.

2. The Judges' Did Not Err in Declining to Adopt An ARPU That Sirius XM Never Proposed

At the hearing in the present proceeding, Sirius XM failed to proffer the $[[redacted]] ARPU which it now contends the Judges should have used in calculating the royalty rate. Rather, Sirius XM acknowledged that the ARPU that should be applied in this proceeding was $[[redacted]], unless the Judges changed the definitional language for Gross Revenues. *Initial Determination* at 72, n.141. Tellingly, in its Reply, Sirius XM does not identify any part of the record in which it had actually proposed that the Judges use the $[[redacted]] ARPU figure it now advances in its Motion.

Sirius XM argues that its failure to proffer the $[[redacted]] ARPU is excusable, claiming that "it was not possible … to provide the Judges with the precise ARPU" because of the "disputed hearing record regarding what should be included and excluded from Gross Revenues." Sirius XM Reply at 1 (SXM Reply); *see* SXM Motion at 3 ("in the event the Judges determined to

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[7] In light of the record evidence, Sirius XM would have been hard-pressed to claim that the Judges substantively changed the definition of Gross Revenues. As SoundExchange correctly notes:

> the Judges did not substantively modify the definition of Gross Revenues. Most importantly, as to whether SXM must include in Gross Revenues the revenue from non-music offerings that are not "offered for a separate charge," the Judges specifically concluded there was "no need to amend the text of the regulatory definition." Determination at 113-14. SXM is likewise incorrect when it asserts that the Judges have meaningfully altered the definition of Gross Revenues with respect to deduction of credit card fee expenses, which have never been excludable from the revenue base.

SoundExchange Opposition at 6.

[8] Sirius XM repeatedly *qualifies* its assertion that the Judges modified or changed the definitional language and uses a parenthetical or other qualifier that suggests it takes issue with the Judges' consistent interpretation of the substantively unchanged definition. *See, e.g.*, Motion at 3 ("The Judges did in fact modify (*and clarify their interpretation of*) the Gross Revenues definition … [with a] now-superseded (*and in places, previously interpreted*) Gross Revenues definition ….") (emphases added); *see also id.* at 5, 6 n. 4.

[9] The Judges issued the January 10 *Ruling on Referral* in response to a primary jurisdiction referral from the United States District Court for the District of Columbia deferring to the Judges' interpretation of the definition of Gross Revenues. *See SoundExchange, Inc. v. Sirius XM Radio, Inc.* 65 F. Supp. 3d 150 (D.D.C. 2014) (D.C. Action). In response to the D.C. action referral, the Judges ruled, *inter alia*, that "Sirius XM's use of a bundled price [for its former Premier package] is inconsistent with the regulatory requirement that premium channels must be priced at a 'separate charge'" and that "Sirius XM was incorrect to claim a revenue exclusion based upon [a] package upcharge, as that … package was not a service offered for a separate charge." Ruling on Referral at 17, 21. The Judges subsequently withdrew and modified the January10th version of that ruling for reasons unrelated to the present issue.

modify the Gross Revenues definition," the Judges would need to modify the ARPU). However, as noted, the Judges did not change the definition or interpretation of Gross Revenues. Therefore, Sirius XM could have calculated an ARPU it believed to be appropriate under that *status quo* but failed to do so. As SoundExchange rhetorically asks: "If $[[redacted]] is so clearly the only correct ARPU number, why didn't [Sirius XM] calculate it for the Judges before their Determination?" SoundExchange Opposition at 5.

3. Sirius XM had the Duty to Propose $[[redacted]] ARPU at the Hearing

Although Sirius XM cannot point to record evidence that it had calculated or argued in support of an ARPU of $[[redacted]], it now contends that the Judges had the responsibility to identify, post-hearing and *sua sponte*, the single document[10] among 511 admitted exhibits from which they might be able to calculate the now-favored ARPU figure and that the Judges erred by not doing so. Sirius XM is wrong on both counts.

A party has an obligation not only to present evidence and testimony, but also to apply that evidence and make arguments that support a specific factual finding that the party asks the Judges to adopt. If a party believes that different strands of evidence and testimony should be analyzed together to establish a particular factual finding or to establish inputs for the calculation of a figure to be applied in making a factual finding, that party must (1) synthesize the disparate portions of the record that would support that finding; and (2) state what it proposes that finding should be. Here, however, Sirius XM for the first time in this rehearing motion (1) proposes its alternative finding of an ARPU of $[[redacted]] and (2) identifies elements in the record Sirius XM claims the Judges should have identified and used to calculate the $[[redacted]] ARPU.

SoundExchange argues that Sirius XM declined to propose an alternative ARPU at the hearing "for purely tactical reasons" because it is challenging the Judges' interpretation of the Gross Revenues definition in the D.C. Action. SoundExchange Opposition at 7. Sirius XM does not deny that its failure to proffer the $[[redacted]] ARPU figure was in fact tactical, but rather suggests that SoundExchange's own witnesses also had tactically decided not to make a similar ARPU calculation. SXM Reply at 4, n.5. SoundExchange's purported decision to refrain from advocating a position for tactical reasons does not offset Sirius XM's decision to do the same. Prior to the closing of the record in the proceeding, Sirius XM had all of the information it needed to propose for the Judges' consideration the ARPU for which it now advocates. Therefore, the responsibility for not having done so must rest on Sirius XM. The Judges' decision not to follow a potential path that Sirius XM chose not to advocate is not grounds for a rehearing.

4. Sirius XM does not Demonstrate Error by the Judges

Sirius XM refers to four paragraphs in its Reply Proposed Findings of Fact (SXMRPFF ¶¶ 391-394), and a revenue summary in Exhibit 149 to support its contention that the Judges

[10] That single document is Ex. 149, discussed *infra*.

should have used an ARPU of $[[redacted]].[11] SXM Motion at 5-6. However, those cited materials do not provide evidence that identifies and supports the monthly ARPU of $[[redacted]] that Sirius XM now contends the Judges should have used in calculating a royalty rate. Rather, those paragraphs purport to support a different monthly ARPU – $[[redacted]]. *See* SXMRPFF ¶ 393. Sirius XM apparently calculated this $[[redacted]] ARPU based on revenue data from the single month – September 2016 – identified in Ex. 149. More particularly, in SXMRPFF ¶ 393, Sirius XM indicates that its calculation relates to "that month," but the reference to "that month" is ambiguous, because no particular month is mentioned in SXMRPFF ¶ 393.[12] Further, in its rehearing Motion, Sirius XM relies on the same exhibit, Ex. 149, to calculate yet another ARPU – $[[redacted]]. SXM Motion at 6-7. Apparently, Sirius XM believes this latest September 2016-based ARPU is more precise than the September 2016 ARPU it proffered in SXMRPFF ¶ 393, which was a "ballpark" measure. *Id*. Nonetheless, neither the $[[redacted]] nor the $[[redacted]] ARPU figure is the ARPU on which Sirius XM relies in the rehearing motion, in which it asks the Judges to adopt the third figure – the proposed $[[redacted]] ARPU.[13]

SoundExchange correctly identifies a flaw in Sirius XM's argument on rehearing: Sirius XM calculates different ARPUs based on two sets of data, proving that ARPU is a moving target, derived from inputs that fluctuate over time. SoundExchange Opposition at 8-9. Sirius XM's painstaking post-hearing analysis, which still leaves ambiguous the calculation of ARPU, only underscores the conclusion that the Judges did not err in declining to adopt an ARPU and a specific analysis that Sirius XM never proposed. The Judges agree with SoundExchange's argument in opposition to this Motion: "The Judges' task here was not to undertake post determination every recalculation that the record would have allowed …." SoundExchange Opposition at 9.

5. The Risk of "Manifest Injustice"

The foregoing analysis makes clear that the Judges did not err in their adoption of the $[[redacted]] ARPU. However, judicial error is not the only criterion that might support SXM's request for rehearing. Sirius XM also asserts that application of the $[[redacted]] ARPU would result in "manifest injustice," one of the itemized bases for granting rehearing. The Judges have expressed "manifest injustice" as an explicit standard for rehearing, separate and apart from a finding of clear error. Sirius XM has alleged that manifest injustice would occur if certain challenged portions of the *Initial Determination* were adopted as final. The Judges therefore

[11] The exhibit on which Sirius XM relies, Ex. 149, was admitted by stipulation, together with many other exhibits, 4/19/17 Tr. 157, and Sirius XM did not describe this exhibit as some sort of "roadmap" by which the Judges could calculate or adjust an ARPU figure.

[12] Two paragraphs prior, at SXMRPFF ¶ 391, Sirius XM does refer to the month of September 2016, the same month whose summary data apparently is contained in Ex. 149.

[13] There are at least two possible reasons why Sirius XM has declined to rely on the higher September 2016 ARPU calculation, which would have benefitted Sirius XM. First, as SoundExchange points out, Sirius XM did not provide evidence of the subscriber count (that is, users—the "U" in ARPU) that corresponded to the ARPU for the month at issue, *i.e.*, September 2016. Opposition at 9. Second, the ARPU to which the parties agreed at the hearing, $[[redacted]], was calculated over the six-month period January through June 2016. So, use of the September 2016 data (even assuming evidence of the subscriber count) would constitute a change in the time frame that the parties agreed would be covered in the ARPU calculation.

examine whether, even in the absence of a finding of clear error, the potential for "manifest injustice" warrants a rehearing in this case.[14]

In determining whether to grant rehearing motions, the Judges have looked to *Fresh Kist Produce,* which applies the "manifest injustice" criterion in a case involving economic rights. In *Fresh Kist Produce,* plaintiff moved for summary judgment, seeking monetary relief, and pre-judgment interest. Plaintiff had requested pre-judgment interest in its motion for summary judgment, but had failed to detail or provide support for this request. Plaintiff moved under Fed.R.Civ.P. 59(e)[15] for an order amending the partial summary judgment, presenting a new argument in support of the request for pre-judgment interest. *Fresh Kist Produce,* 251 F. Supp. 2d at 141. The district court granted the Rule 59(e) motion, after noting the tension between offering a party the proverbial second bite at the apple and preventing "manifest injustice." Accommodating this tension in favor of granting rehearing, the district court held that "[a]lthough the court disapproves of parties raising arguments that they could have advanced earlier, the court recognizes that *the interests of justice and fairness* support reviewing the plaintiff's motion." *Id.* After conducting a rehearing and further review, the district court awarded prejudgment interest to the plaintiff. *Id.*

In the present proceeding, the monetary sum at issue is much larger than was the case in *Fresh Kist Produce*.[16] As Sirius XM asserts, using the same calculation method relied upon by SoundExchange in its Opposition, the amount of royalties at issue is approximately $150 million. Reply at 2. Thus, if the record of the hearing reflects the parties' understanding that a higher, albeit uncalculated, ARPU should have been adopted, the Judges are inclined to grant rehearing, to prevent manifest injustice, notwithstanding that Sirius XM neither calculated this ARPU nor provided the Judges with a clear identification of record evidence that would have permitted such a calculation.

Moreover, the Judges understand that it is their statutory duty to set a rate that is supported by evidence in the record. Here, the Judges used the ratio of per subscriber opportunity cost divided by ARPU to establish a rate of 15.5%. If that ARPU is too low, given the Gross Revenues royalty base established by the Judges, then the percent-of-revenue royalty rate will necessarily be too high. The Judges find it would be manifestly unjust to maintain a royalty rate that was not based on the Gross Revenues calculation methodology that prevailed at the time the record was closed in the current proceeding.[17]

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[14] The Fifth Circuit in *Douglas v. United Services Automobile Assoc.*, observed that, whereas "our court has a solid understanding of 'plain error'…'manifest injustice' is a far more elusive concept [that has not been defined clearly]." 79 F.3d 1415, 1424 (1996).

[15] As noted in the *SDARS I* Rehearing order, the Judges pattern their rehearing standard after the standards pertaining to Fed.R.Civ.P. 59(e).

[16] In *Fresh Kist Produce*, the court was asked to order pre-judgment interest on a disgorgement amount of $59,189.40. 251 F.Supp.2d at 141.

[17] As Sirius XM points out, the alleged mismatch between the ARPU and the Gross Revenues royalty base implies a $[[redacted]] per subscriber "opportunity cost" numerator in the royalty calculation, rather than the $1.66 per subscriber rate determined by the Judges. That is, given the 15.5% royalty rate and the $[[redacted]] ARPU advocated by Sirius XM, the formula utilized by the Judges (and the parties) to calculate the percent-of-revenue royalty rate can be expressed as follows:

Sirius XM has adequately demonstrated that the record could support a finding that the parties' mutual understanding that the ARPU must reflect the Gross Revenues royalty base ultimately adopted by the Judges. SXM Motion at 4-5 and evidence cited therein. Further, Sirius XM argues plausibly that it could not have known that the Judges would maintain the Gross Revenues interpretation set forth in the *Ruling on Referral* when issuing the Determination in the present proceeding. *See* SXM Reply at 3 ("Given the open issues relating to the definition of Gross Revenues, providing the precise number was impossible."). Of course, Sirius XM could have calculated the ARPU based on the reasonable assumption that the Judges would not change their nearly contemporaneous interpretation of the Gross Revenues definition, but that only demonstrates why it was Sirius XM, not the Judges, who erred previously.

In any event, as Sirius XM correctly argues, Sirius XM and SoundExchange each presented evidence from an economist who provided a per-subscriber estimate for his respective royalty rate calculations, each using the same ratio approach as used by the Judges in the *Initial Determination*, to convert those per-subscriber amounts into percentage rates. *See* Shapiro CWRT at 17-18; Orszag AWDT ¶¶ 60; *Initial Determination* at 41-42. As Sirius XM also properly argues, all economists who discussed the issue agreed that, when converting per-subscriber ratios into percent-of-revenue royalty rates, "it was imperative that the ARPU used in the denominator of the calculation be commensurate with the ARPU that would flow from the Gross Revenues definition actually adopted by the Judges going forward …." SXM Motion at 4. Indeed, the relevant economic witnesses are on record to this effect. *See* 4/19/17 Tr. 212-213 (Shapiro); 4/20/17 Tr. 313-315 (Shapiro); 4/25/17 Tr. 1000-1001 (Orszag); Lys WRT ¶ 154.

In its Opposition, SoundExchange does not disagree with the accuracy of the foregoing cited testimony or the relevance of that testimony to the calculation of the royalty rate. *See* Reply at 2. Rather, SoundExchange takes issue with Sirius XM's failure to acknowledge the impact of the Judges' *Ruling on Referral* and its failure to provide a calculation based on the reasoning in that ruling. SoundExchange Opposition at 7 ("If Sirius XM thought the Judges' interpretation of the Gross Revenues definition required a different ARPU number, it should have said so (and calculated that number) before the Judges issued their Determination, not after.").

The Judges do not disagree with SoundExchange's argument, but it does not address the substantive point – which appears to remain undisputed – that the ARPU used in the royalty rate ratio must be commensurate with the Gross Revenues definition that the Judges applied. That undisputed and important principle outweighs any dereliction by Sirius XM in its presentation of the evidence, and must be adopted in order to prevent manifest injustice.

The Judges therefore conclude that they should reconsider -- in the face of unrebutted arguments -- whether the 15.5% royalty rate is based on an ARPU that is not commensurate with the Gross Revenues definition actually adopted. Reconsideration of the 15.5% royalty rate does not imply that the Judges should simply adopt the 14.7% royalty rate calculated by Sirius XM.

15.5% = X÷$[[redacted]] ("X" is the implied per subscriber "opportunity cost")
X = $1.75 "opportunity cost" per subscriber.

Rather, the Judges must reconsider the record supporting each proposal and determine what conclusion is better supported by evidence in the record.

Accordingly, by this order, the Judges grant Sirius XM's motion for a rehearing on this issue and will re-evaluate whether the royalty rate should remain at 15.5%, or be reduced to a rate not lower than 14.7% – the rate requested by Sirius XM on rehearing. *See* SXM Motion at 8 ("The Judges … should reset the rate at the properly calculated 14.7%.").

Each party shall provide the Judges with additional submissions, limited in scope and size and according to the following schedule.

No later than May 15, 2018, each party shall simultaneously submit:

> A brief, limited to no more than 7,500 words (excluding exhibits), identifying the ARPU and the resulting royalty rate (between 14.7% and 15.5% inclusive) that the party alleges to be appropriate, and the reasons therefor. The proffered ARPU must be supported by cited evidence in the record.[18]

No later than May 29, 2018, each party shall simultaneously submit:

> An opposition brief, limited to no more than 5,000 words (excluding exhibits), responding to the adverse party's initial rehearing brief.

The Judges do not intend currently to accept additional submissions or to schedule a hearing. However, they reserve the right to require additional submissions or to schedule a hearing or both.

B. The Direct License "Cap"

In its rehearing motion, Sirius XM also seeks rehearing on regulatory language the Judges adopted with respect to section 382.23(a)(2), which deals with adjustments to the royalty fee for directly licensed recordings (Reduction for Direct License Share). Sirius XM refers to section XI ("Terms") of the *Initial Determination* in which the Judges described certain changes to the regulatory language effectuating the rates and terms resulting from the hearing. SXM Motion at 8-9. Sirius XM states that "[c]ertain changes that appear in the Terms…are neither identified nor explained in the Determination." *Id*. at 9. In particular, Sirius XM points to changes to section 382.23(a)(2) relating to a royalty fee reduction for the direct license share.

The new section 382.23(a)(2) reads:

> To arrive at the percentage allocable to the Direct License Share for each month, the Licensee shall divide the Internet Performances of Directly-Licensed Recordings on the Reference Channels by the total number of Internet Performances of all sound recordings on the Reference Channels. In no event

[18] This rehearing process is limited to the issues discussed in this Order. For the sake of clarity, the Judges are not allowing, *inter alia*, any briefing or exhibits related to the calculation of the $1.66 per-subscriber figure, or related to any alternative methodology for the calculation of ARPU or the statutory rate.

> shall the Direct License Share be an amount greater than the result of dividing the number of plays of Directly-Licensed Recordings on the SDARS by the total number of plays of all sound recordings on the SDARS.

Sirius XM argues that the new provision imposes a cap on the Direct License Share which would create a disincentive to direct licensing by causing Sirius XM effectively to pay twice for the portion of Performances exceeding the satellite play cap. Motion at 10.

According to SoundExchange, "until such time as actual satellite listenership data is used to calculate the direct license exclusion, the direct license share should be capped based on plays on the satellite service." SXPFF at ¶ 1745. SoundExchange notes that unlike almost all other statutory licensees, Sirius XM does not currently provide to SoundExchange listenership data that could be used for distributing SDARS royalties. 5/10/17 Tr. 3221:10-12 (Bender). At the same time, because SoundExchange is required to "distribute royalties on a basis that values all performances by a Licensee equally based upon the information provided under the reports of use requirements," 37 C.F.R. § 382.13(f)(1), it must distribute on the basis of plays on Sirius XM's satellite radio service. Trial Ex. 25 at ¶ 285 (Lys Corr. WDT); Trial Ex. 29 at 8 (Bender WDT); Trial Ex. 49 at 9 (Bender WRT). By contrast, the methodology used to calculate the direct license exclusion is based on webcast performances, and, SoundExchange represents, [[redacted]] Sirius XM's direct licenses [[redacted]]. Trial Ex. 25 at ¶ 287 (Lys Corr. WDT). SoundExchange notes that while the Judges determined in *SDARS II* that the total amount Sirius XM deducts from its payment to SoundExchange should be determined based on the webcasting proxy, the Judges did not order Sirius XM to do the same.[19]

SoundExchange represents that the difference between Sirius XM's payment methodology and SoundExchange's distribution methodology has created an incentive for labels to sign direct licenses with Sirius XM if they "over-index;" that is, if their share of performances on Sirius XM's webcasting service is greater than their share of plays on Sirius XM's SDARS. Trial Ex. 4 at ¶¶ 26-27 (White WDT); Trial Ex. 25 at ¶¶ 286, 289 (Lys Corr. WDT); Trial Ex. 42 at ¶ 85 (Lys WRT); Trial Ex. 48 at 6-7 (Bender WRT). According to SoundExchange, [[redacted]] Trial Ex. 42 at ¶ 89 (Lys WRT); *see* 5/17/17 Tr. 4290-91 (White). SEPFF at ¶ 1748.

SoundExchange represents that [redacted]] Trial Ex. 25 at ¶ 300 (Lys CWDT); 4/27/17 Tr. 1553 (Lys). This is because Sirius XM gets a more-than-offsetting increase in the size of the direct license exclusion from its statutory royalty obligation. Lys CWDT at ¶ 300; *see* Trial Ex. 42 at ¶ 96 (Lys WRT). That exclusion, as SoundExchange points out, is calculated based on performances using the webcasting proxy, not plays on the SDARS. *See* 37 C.F.R. § 382.12(d); Lys CWDT ¶ 300; Lys WRT ¶ 96. SoundExchange represents that the increased exclusion

[19] SoundExchange points to no authority in the Copyright Act that would authorize the Judges to impose payment terms in private agreements.

decreases the pool of royalties available to artists and copyright owners whose works are used under the statutory licenses. Lys CWDT ¶ 301; *see* SEPFF at ¶ 1749.

According to SoundExchange, over-indexing has not been an issue to date. SoundExchange argues, however, that there is an incentive for Sirius XM to encourage such behavior and therefore there is a need for a mechanism to mitigate Sirius XM's incentives to engage in such regulatory arbitrage to the detriment of artists and copyright owners whose works are used under the statutory license. SEPFF at ¶ 1751. Therefore, SoundExchange proposed capping the direct license share based on plays on the SDARS until Sirius XM provides actual satellite usage data. SEPFF at ¶ 1752. According to SoundExchange, the way to avoid this potential concern is to migrate calculation of the direct license exclusion to actual satellite listenership data because that would eliminate the opportunity for arbitrage between the statutory license exclusion and distribution methodologies. SEPFF at ¶ 1754.

The Judges note that the fairest way to assess a licensee's royalty obligations is by assessing the actual number of performances on the licensee's service. The Judges have made certain accommodations for services such as Sirius XM that have represented that they do not have the technological ability to determine performances; that is, how many subscribers are actually listening to the transmitted plays on the service. The Judges also are aware, however, that as technology advances Sirius XM's capability to track satellite performances may become more feasible. Evidence in future proceedings might better inform the Judges about when that technology will become available and at what cost. Until that time, however, the Judges conclude that it is necessary to avoid any unintended consequences that the Internet proxy accommodation might have on artists whose works are made available under the compulsory license. The record reflects that SoundExchange has identified a plausible unintended consequence of the Internet proxy accommodation and has proposed an appropriate and reasonable means of addressing it, which the Judges adopted. Therefore, the Judges see no reason to review that decision in a rehearing.

The Judges **DENY** Sirius XM's rehearing request with respect to Section 382.23(a)(2).

C. Gross Revenues Definition

A second regulatory concern expressed by Sirius XM is changes in the new Section 382.22(b)(5). The Judges changed the extant definition of Gross Revenues for SDARS by adding a requirement that the fees identified in that clause (credit card, invoice, activation, swap and early termination fees) be "charged to subscribers" and be "reasonably related to the Licensee's expenses to which they pertain." SXM Motion at 9. Sirius XM states that it opposed the addition of the "reasonably related" language relating to underlying expenses because, in Sirius XM's view, the phrase is "tremendously vague and will almost assuredly lead to litigation between Sirius XM and SoundExchange over whether a fee sufficiently 'relates' to underlying expenses." *Id*. Sirius XM asserts that SoundExchange's witness testimony on this issue failed to explain how the relation between a fee and an expense would be established or measured and to provide justification for the relation in the first place. *Id*.

With respect to the "charged to subscribers" requirement, Sirius XM asserts that the requirement will force Sirius XM to include in revenue sums it never collects (chiefly processing fees withheld by credit card companies and associated entities before sending payments). *Id*. at 9-10. Moreover, Sirius XM asserts that this new requirement is "at odds with prior acceptance of this deduction in *SDARS II*." *Id*. at 10.

SoundExchange counters that the evidence and testimony it presented to the Judges at the hearing provide ample support for the regulatory changes the Judges adopted. SoundExchange Opposition at 10. In proposing the "reasonably related" language that the Judges adopted, SoundExchange noted that while it agreed that certain miscellaneous fee revenue can be deducted from Gross Revenues,

> that does not mean that any amount paid by a subscriber and called a special fee should be deductible regardless of the size of the fee…To ensure that the deduction for miscellaneous subscriber fees remains true to its purpose of relating the royalty to the value of the sound recordings used, this proposal does two things. First, it specifies more clearly which miscellaneous subscriber fee revenue is deductible, to permit reasoned consideration of which fees are or are not related to the use of sound recordings and avoid future disputes. Second, it specifies that for a miscellaneous subscriber fee to be properly deductible from subscriber revenue, it must be related to the purpose unrelated to the use of recordings for which that fee is charged.

SXPFFCL at ¶ 1691, citing Trial Ex. 29 at 21 (Bender WDT); 5/10/17 Tr. 3183-84 (Bender).

The Judges find that the changes SoundExchange proposed to Section 382.22(b)(5) are reasonable and appropriate in that they clarify the types of fees that may be excluded from Gross Revenues and help to prevent those excluded fees from reducing revenues that are more properly attributable to the value of the sound recordings that Sirius XM uses in its service. The Judges disagree with Sirius XM that the language the Judges adopted in this section is "tremendously vague." The Judges find the language to be sufficiently clear to address the concern that SoundExchange expressed about miscellaneous fees being used as a way to avoid certain revenues from being included in Gross Revenues for purposes of calculating royalties. In fact, the adopted language should help to provide added clarity with regard to fees Sirius XM receives that may be deductible from Gross Revenues. Should interpretive issues arise with respect to the adopted changes to section 382.22(b)(5), the Judges will address those issues accordingly.

Therefore, the Judges **DENY** Sirius XM's request for rehearing related to Section 382.22(b)(5).

IV. Music Choice Motion for Rehearing

In the *Initial Determination*, the Judges concluded that Music Choice's provision of music streaming over the Internet constituted a different service offering that is ineligible for the royalty rates for preexisting subscription services determined in this proceeding. *Initial Determination* at 37. In reaching their conclusion, the Judges referred to and relied upon the legal opinion they sought from the Register of Copyrights.[20] *See Memorandum Opinion on Novel Questions of Law*, Nov. 20, 2017 (Register's Opinion).

In its Motion for Rehearing Regarding PSS Internet Transmissions Available Outside the Home (MC Motion), Music Choice contended that "there is no evidentiary support in the record for a finding that transmissions made outside of the home exceed the scope of the PSS license by differing from the cable TV industry's common practices." MC Motion at 10. Music Choice contends that to the extent there is a dispute between SoundExchange and Music Choice as to whether transmissions that may be accessed outside the home "are sufficiently different from cable and satellite television industry norms to exclude them from the PSS license under the Register's legal test, that dispute should be resolved either in federal court or in a later rate proceeding, in which an adequate factual record may be developed." MC Motion at 10. Music Choice's effort to reframe the issue of Internet transmissions as one of the cable TV industry's common practices misses the mark. A more apt framing of the issue is whether Music Choice's service offering, to the extent it allows users to stream sound recordings over the Internet outside their homes through mobile devices, is sufficiently similar to Music Choice's residential television cable service for purposes of the Section 114 grandfathering provisions. After carefully reviewing the evidence in the record the Judges concluded that it was not.

Music Choice states correctly that the Register's Opinion "made no factual finding relating to whether subscribers' ability to access Internet transmissions of network content outside the home would render those transmissions ineligible for the PSS license." MC Motion at 3. The Register did conclude, however, as a matter of law, that by using the Internet as a transmission medium, as Music Choice's streaming service does, the streaming service must either be an "expanded service offering" (which is within the scope of the PSS license) or a "different service offering" (which is outside the scope of the PSS license). Register's Opinion at 19. The service offering at issue cannot qualify as an existing service offering. In assessing whether a service offering is an expanded service offering "a comparison must be made between the service offering in question and the existing service offering to see if it is sufficiently similar" at the time of the comparison. Register's Opinion at 21. The Judges made such a comparison based on the characteristics of those services as presented in the proceeding. The Register provided a non-exhaustive list of six factors that aided the Judges in making the comparison:

(1) Whether the service offering has a similar effect on displacing or promoting sales of phonorecords.

(2) Whether the quantity and nature of the use of sound recordings by the service offering is similar.

(3) Whether the service offering provides similar content to similar user groups.

[20] In the course of deliberations, the Judges identified a novel material question of substantive law, *i.e.*, a question concerning the interpretation of provisions of the Copyright Act (Act) that had not been determined in any prior decision, determination, or ruling. *See* 17 U.S.C. § 802(f)(1)(B). Referral to the Register is mandatory for a "novel material question of substantive law concerning an interpretation of those provisions of [the Act] that are the subject of the proceeding …." 17 U.S.C. § 802(f)(1)(B).

(4) Whether the service offering is consumed in a similar manner, provides a similar user experience, and has similar form, feel, and functionality.

(5) Whether and to what degree the service offering relates to the pre-July 31, 1998 investments Congress sought to protect.

(6) Whether and to what degree the service offering takes advantage of the capabilities of the medium through which it is transmitted (*i.e.*, whether and the extent to which differences between the service offerings are due to limitations in the existing service offering's transmission medium that are not present in the other service offering's transmission medium).

Register's Opinion at 21-22.

According to Music Choice, it has made numerous technological contributions to its service since it launched, each designed to increase the exposure of sound recordings to new and larger audiences and enhance the promotional value of the service to the record labels. Del Beccaro WDT at 38. Examples include: improvements to the on-screen displays containing promotional information about the song and artist and improvements to the digital playback system to improve the programmers' flexibility to provide "deeper music lists and more interesting mixes on more channels." *Id*. at 38-39. These improvements appear consistent with the Register's assessment of the types of changes that are permissible to expand and grow an existing service offering within the same transmission medium (*i.e.*, cable and satellite). Nevertheless, the Judges did not find conclusive evidence in either direction to determine whether the service offering (*i.e.*, the 75 Internet channels that may be streamed outside the home) has a similar effect to the residential cable-based television service in displacing or promoting sales of phonorecords.[21]

Other changes that Music Choice cites strongly suggested that they are more consistent with a "different service offering." For example, Music Choice cites its efforts "to integrate our residential audio service with various social networking platforms, such as Twitter and Facebook, as well as texting, all to improve customer engagement." *Id*. These technological enhancements are consistent with Music Choice's planned expansion of its service, which is focused primarily on its Internet channels. Indeed, apparently all of the 25 Internet-only channels were added since the last rate period. 5/18/17 Tr. 4666-67 (Del Beccaro). Substantially all of Music Choice's planned expansion from the last rate period (most of which did not materialize) would have been through additional Internet-only channels. 5/18/17 Tr. 4667 (Del Beccaro). With reference to the Register's six-factor list of criteria, the Judges find that the addition of 25 Internet-only channels constitutes a change in the quantity and the nature of the use of the sound recordings by Music Choice. Many of the technological improvements that Music Choice attributes to its Internet-based channels significantly change the manner of consumption and nature of the user experience from its existing residential audio cable television service. By making channels available on mobile devices and through a website and by

[21] In addition to the 50 Music Choice channels of audio music programming that are delivered to subscribers' televisions, Music Choice also provides 25 additional channels that are made available to "authenticated television subscribers through Music Choice's website and a mobile app." Del Beccaro WDT at 4.

integrating those channels with social media providers such as Facebook and Twitter, Music Choice is allowing consumption in a different manner, and providing a different user experience from its residential audio cable television service. Music Choice does so by utilizing technological capabilities only available with the advent of the Internet and the wireless capabilities that it allows, which are not the type of pre-July 31, 1998 investments Congress sought to protect when it adopted the grandfathered rate provisions for PSS.

Consistent with the Register's Opinion, the Judges conclude that a Music Choice channel available to a subscriber outside the home (*e.g.*, through a smart phone, tablet, or other mobile device) is part of a different service offering. This conclusion is consistent with evidence in the record dealing with the way in which Music Choice customers consume Music Choice services. Notably, [[redacted]] viewers watch (or listen to) Music Choice channels on their TVs and in their own homes. Music Choice Viewership Study, Trial Ex. 443, at 31. In Q3 2016, however, [[redacted]]% of viewers stated that they also typically watch (or listen) at work, [[redacted]]% in a school dorm, and [[redacted]]% in a car. *Id*. Television was still the most used device for viewing (or listening), but [[redacted]]% (in Q3 2016) also indicated watching (or listening) online, and [[redacted]]% on cell phones. *Id*.

These emerging consumption patterns strongly suggest that a PSS channel that offers users the capability to consume that service outside the home will likely alter their traditional consumption patterns in a way that makes those channels part of a different service, which is outside the scope of the PSS license. The fact that Music Choice offers (at least) 25 music channels that are only available outside its residential television audio service indicates that Music Choice was not merely intending to replicate that residential television service offering over the Internet. Opening the service to the Internet allows an opportunity to offer new channels, new genres, and new formats, unfettered by limitations on the number of channels a cable system is willing to dedicate to the service. These facts support the conclusion that the service is a different service rather than a mere expansion of the existing service.[22]

Finally, Music Choice argues that the Judges' decision on this issue would create a manifest injustice because, according to Music Choice, it cannot track individual performances and therefore would not be able to comply with existing webcasting royalty requirements. MC Motion at 9. This assertion is undercut by Music Choice's CEO who clarified that it is not technologically impossible to know how many listeners are listening to each performance on Music Choice's Internet transmissions; rather that Music Choice chooses not to track those performances because it believes it would be prohibitively expensive to do so. 5/18/17 Tr. 4651, 4652 (Del Beccaro).

Music Choice also argues that ceasing to provide its Internet streaming service would cause Music Choice to breach its affiliate agreements and therefore would cause market

[22] According to Music Choice, each channel offers a distinct musical genre or sub-genre. Trial Ex. 55, at 4 (Del Beccaro WDT). Music Choice channels offered over the Internet through a web site or app would also offer video on demand, which is beyond the scope of the PSS service. Trial Ex. 57, at 29 (Del Beccaro WRT). The Judges agree with SoundExchange's assessment that "[t]here is little or no relationship between Music Choice's current Internet service and its pre-1998 investments in the PSS cable radio service." SoundExchange Opposition at 6. Music Choice did not begin providing any video-on-demand until 2004. Trial Ex. 55, at 28 (Del Beccaro WDT). Music Choice began providing access to its service through personal computers, a precursor to mobile devices and apps, in 2004 or 2005. Trial Ex. 926.

disruption contrary to Section 801(b)(1)(D) of the Copyright Act. First, the Judges did not prohibit Music Choice from providing a streaming service; the choice to do so would be Music Choice's alone. Second, the Judges did not conclude that the Music Choice Internet service offering must comply with existing webcasting royalty requirements. The Judges noted that sound recording royalties for the Internet service offering "must be determined by reference to existing rate regulations covering that type of service offering, in a separate, future proceeding under the willing buyer/willing seller standard, or through voluntary negotiations." *Initial Determination* at 36. Music Choice's conclusion of what rate structure and terms would apply to the streaming service is premature as is Music Choice's assertion that the applicable rate structure would be disruptive.

For these reasons, the Judges **DENY** the Music Choice motion for rehearing.

SO ORDERED.

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Date: 2018.04.18 15:37:48 -04'00'

Suzanne M. Barnett
Chief Copyright Royalty Judge

Dated: April 18, 2018