

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

In the Matter of

Determination of Rates and Terms for
Business Establishment Services

Docket No. 2007-1 CRB DTRA-BE
(2009-2013)

In the Matter of

Determination of Rates and Terms for
Business Establishment Services

Docket No. 2012-1 CRB
Business Establishments II
(2014-2018)

MUSIC CHOICE'S REPLY BRIEF RE: BES GROSS PROCEEDS REFERRAL

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INTRODUCTION

The “Gross Proceeds” definition at issue in this referral is clear—it explicitly calls for the inclusion of only those revenues derived from copies of sound recordings that are made “for the sole purpose of facilitating a [BES] transmission . . .” 37 C.F.R. § 384.3(a)(2) (2019). As Music Choice explained in its Opening Brief, long-established principles of regulatory interpretation make clear that limiting language in a regulation, such as this “sole purpose” language, must be given effect. The language cannot simply be ignored or read out of the regulation. MC Opening Br. at 24-27. As Music Choice also explained, the plain meaning of the Gross Proceeds definition is fully supported by the unique nature of the BES license, the historical context in which it was created, prior findings of both the Register and the Judges, and even arguments SoundExchange has successfully made in other proceedings. *Id.* at 27-34.

Despite all of the foregoing, SoundExchange continues to press its untenable position that the “sole purpose” limiting language is effectively meaningless and that, despite this clear language, Music Choice must nevertheless include *all* of its BES revenues in the Gross Proceeds royalty pool. While SoundExchange acknowledges that all words in a regulation must be given effect, it nevertheless fails to offer any credible explanation for what the “sole purpose” limiting language at issue is meant to accomplish. Instead, it attempts to dance around that language by making a series of tortured linguistic arguments and resorting to misdirection.

SoundExchange first attempts to create an ambiguity in the Gross Proceeds definition where none exists, including by incorrectly asserting that there is an inconsistency between the Gross Proceeds definition at issue and the prior subsection of 37 C.F.R. § 384.3(a), which sets forth the percentage of revenue rates to be applied against the Gross Proceeds royalty pool. Next, SoundExchange attempts in vain to show that the plain meaning of the Gross Proceeds royalty pool produces “absurd results.” And finally, SoundExchange presents an irrelevant and

incomplete discussion of a twenty-year old CARP decision—one that was based on a limited record, flawed and outdated understanding of technology as well as subsequent developments in the copyright treatment of that technology, and that engaged in a benchmarking analysis that would never withstand scrutiny today. As Music Choice demonstrates, all of these arguments are meritless and in no way undermine the plain meaning of the Gross Proceeds definition at issue.

Music Choice has offered a straightforward and simple reading of the regulatory language at issue—one that is not only clear, but is also fully consistent with the unique nature of the BES license and the historical context in which it was created. SoundExchange, on the other hand, has offered no credible reading of the regulation at issue and has provided no explanation for the “sole purpose” limiting language that can possibly withstand scrutiny. Between these two options, the choice is clear. The Judges should confirm Music Choice’s interpretation of the definition of Gross Proceeds.

ARGUMENT

I. SoundExchange’s Effort to Manufacture an Ambiguity Regarding the Meaning of Gross Proceeds Does Not Withstand Scrutiny

As demonstrated in Music Choice’s Opening Brief, the provision at issue in this referral—the definition of Gross Proceeds—is clear. The Gross Proceeds royalty pool against which the applicable percentage-of-revenue rate is to be applied must capture fees and payments “that are derived from the use of sound recordings subject to protection under title 17, United States Code, during the License Period pursuant to 17 U.S.C. 112(e) *for the sole purpose of facilitating a transmission to the public of a performance of a sound recording under the [BES] limitation on exclusive rights.*” 37 C.F.R. 384.3(a)(2) (emphasis added). The emphasized “sole purpose” language unquestionably imposes a limitation on the revenues that must be included in Gross Proceeds. Were that not the case, the language would serve no purpose. And the only plausible

interpretation of this limiting language is that BES providers need to include in the Gross Proceeds revenue pool *only* those revenues that are attributable to BES transmissions where copies are made *solely* for the purpose of facilitating transmissions by the BES provider. MC Opening Br. at 24-27.

Unable to provide any plausible alternative explanation for the meaning of this limiting language, SoundExchange resorts to linguistic sleight-of-hand in an effort to create ambiguity where none exists. To do so, it starts by combining two separate provisions—both of which are unambiguous when read on their own—by “[p]lugging the definition of Gross Proceeds from paragraph (a)(2) into the place in paragraph (a)(1) where that term is used.” SX Opening Br. at 21. SoundExchange then goes on to characterize its own mashed-together and newly-minted provision as “ungrammatical” and “difficult to parse.” *Id.*

But this re-imagined provision is only “ungrammatical” and “difficult to parse” because SoundExchange has created it by mashing together two distinct provisions that were drafted to be read separately. The BES regulations do not contain such a mashed-up provision, and this fictional provision is not the one at issue in this referral. When read separately—as they actually exist—the two provisions make complete sense and the alleged problems that SoundExchange raises disappear. Section (a)(1) sets forth the royalty formula to be used—multiplying specified percentage-of-revenue rates against a royalty pool—and then states the rates that are to be used during each year of the license period. Section (a)(1) also explains that only revenues that are attributable to “musical programs” need to be considered. As a result, this language makes clear that any revenues associated with non-music offerings or services also provided by a BES need not be considered. Section (a)(2) plays a different role. It defines the “Gross Proceeds” royalty pool against which the rates set forth in the prior subsection are applied. It begins with the

revenues associated with BES music offerings and then carves out from those revenues, among other things, revenues—if any—derived solely from dual-use copies.¹

That the regulation is structured in this way does not create any ambiguity or raise any difficulties. Indeed, this is precisely how the Judges regularly craft regulations, with one provision addressing the royalty formula and the specified percentage-of-revenue rates and a separate provision defining the precise royalty pool against which those rates are to be applied. *See, e.g., 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), 83 Fed. Reg. 65,210, 65,269 (Dec. 19, 2018) (Section 382.21(a) stating that “Licensees must pay royalty fees for all Eligible Transmissions of sound recordings at the rate of 15.5% of Gross Revenues” and then separately defining the “Gross Revenues” royalty pool in section 382.22, including specifying revenues that are to be included and those that are to be excluded); *Phonorecords III*, 84 Fed. Reg. 1918, 2033-36 (Feb. 5, 2019) (similarly setting forth the royalty formula and rates in a separate provision from that which defines the royalty pool).

Moreover, these other sets of regulations further demonstrate the absurdity of the mash-up exercise that SoundExchange has engaged in here. Were one to take the same approach with any of these other sets of regulations, and plug the definition of the royalty pool into the other provision that sets forth the royalty formula and rates, the result would similarly be an “ungrammatical” and “difficult to parse” Frankenstein’s uber-regulation.

All this being said, even if there were some merit to SoundExchanges’s linguistic contortions, there still is not the ambiguity that SoundExchange claims. SoundExchange argues

¹ Section 384.3(c) then provides that such dual-use copies must be paid for pursuant to any royalty obligation applicable to the non-BES use of such copies, as discussed *infra*, pp. 13.

that there are “two difficult linguistic and interpretive challenges” that emerge from its combination of the two provisions. SX Opening Br. at 21. First, it raises the question of “how to read the word ‘including.’” *Id.* According to SoundExchange, the question is “whether the lengthy matter that follows the word ‘including’ in paragraph (a)(2) is a list of illustrative examples, just one illustrative example, or one or more illustrative examples plus some words that relate back to the ‘all fees and payments’ at the beginning of the definition.” *Id.* at 22. But there is no ambiguity here. The only reading of the term “including” that makes any sense in this context is the obvious and natural reading—that it simply clarifies that “all fees and payments” *include* not only direct monetary payments, but also payments “made in kind” such as barter and other non-cash exchanges of value. SoundExchange simply ignores this obvious reading to try and create ambiguity where none exists.

SoundExchange’s proposed two “alternative” readings of the term “including” are both clearly wrong.² First, SoundExchange suggests that what follows “including” in the Gross Proceeds definition is just a non-exhaustive list of examples of types of “fees and payments.” SX Opening Br. at 22-23. As an initial matter, this reading is ungrammatical. According to SoundExchange, the list of types of “fees and payments” includes two items, those “made in kind” and those “received from any source before, during or after the License Period that are derived from the use of copyrighted sound recordings during the License Period pursuant to 17 U.S.C. 112(e) for the sole purpose of facilitating a transmission to the public of a performance of a sound recording under the limitation on exclusive rights specified in 17 U.S.C. 114(d)(1)(C)(iv).” *Id.* at 22-23. The first problem with this interpretation is that there is no “and”

² Tellingly, SoundExchange is not willing to stand behind either of its “alternative” interpretations, stating that it “does not press the position that either of the [two] interpretations is the best or most plausible interpretation of (a)(2).” SX Opening Br. at 24.

or other connecting language between the only two items contained in this asserted list of different types of “fees and payments.” SoundExchange makes no effort to explain this glaring grammatical problem away.

Moreover, this supposed list of examples of “fees and payments” makes no sense. If “all fees and payments” must be included, as SoundExchange claims, then it is difficult to fathom why the regulations only specify that in kind payments and payments attributable only to single-use copies must be included. More to the point, if all fees and payments must be included, it makes no sense to call out payments attributable to just single-use copies and remain silent as to dual-use copies. It would have been far simpler to leave out the “sole use” language if the intent of the regulations truly were to capture payments attributable to both single-use and dual-use copies, as SoundExchange claims. SoundExchange offers no explanation for why it makes any sense to specifically call out the need to include revenues associated with single-use copies when the regulation, according to SoundExchange, in fact calls for the inclusion of the revenues associated with both single-use *and* dual-use copies. This proposed reading, to use SoundExchange’s own words, is “ungrammatical” and “difficult to parse.” It is also nonsensical and makes far less sense than the straightforward and natural reading of the definition that Music Choice has proposed.

SoundExchange’s second alternative reading of the term “including” is even more bizarre. It claims that everything that follows “including those made in kind” simply “specif[ies] what sorts of ‘in kind’ consideration” must be included. SX Opening Br. at 23. According to SoundExchange, when read this way, the definition first establishes that all fees and payments must be included and then “goes on to specify what kinds of ‘in kind’ consideration count as well—those that come from ‘any source,’ before or after the license period, provided that the

consideration was offered ‘for the sole purpose’ of facilitating a BES transmission.” *Id.*

According to this alternative interpretation offered by SoundExchange, it is only the “in kind” payments that are subject to the “sole purpose” limiting language. This unnatural reading, like SoundExchange’s prior effort, is a grammatical mess. Worse, it contradicts itself. If it is really true that “all fees and payments” must be included, then it cannot also be the case that only a subset of “in kind” consideration—those “offered ‘for the sole purpose’ of facilitating a BES transmission”—must be included.

In addition to being internally inconsistent, SoundExchange’s proposed interpretation of the definition fails for another reason—it is nonsensical. According to SoundExchange’s reading, the “‘for the sole purpose’ of facilitating a BES transmission” language was meant to refer to payments, and not ephemeral copies. *Id.* But payments cannot “facilitate” a transmission. It is copies that facilitate transmissions of sound recordings. Like its other effort to parse the definition of Gross Proceeds, this reading is incoherent and, accordingly, makes far less sense than the natural reading noted above—that “including” simply makes clear that the fees and payments at issue include not only cash payments, but also those made in kind.

Lest there be any doubt, earlier in its brief, SoundExchange makes it abundantly clear that this natural reading of the word “including” is the right one. In its discussion of the Librarian’s review of the *Web I* determination, SoundExchange asserts that the “RIAA persuaded the Librarian that the CARP’s regulatory language ‘does not necessarily appear to capture in-kind payments of goods, free advertising or other similar payments for use of the license.’” SX Opening Br. at 11. As a result, the phrase “including those made in kind” was incorporated to explicitly address the concern raised by the RIAA. *Id.* In other words, the history of the regulation that SoundExchange discusses at some length makes it clear that the “including those

made in kind” language was only ever intended to clarify that in kind payments also fall within the definition of Gross Proceeds—nothing more.

The second “difficult linguistic and interpretive challenge[.]” that SoundExchange alleges is that there are two instances of the term “derived from” in section 384.3(a)—one in the definition of Gross Proceeds and one in the prior provision that sets forth the royalty formula and the rates to be used. SX Opening Br. at 21-22. According to SoundExchange, these two uses of “derived from” create “incoherence” between the two provisions. *Id.* at 24. SoundExchange’s claim is that the plain meaning of Gross Proceeds—one that calls for the inclusion of only revenues that are derived from copies made for the sole purpose of facilitating a transmission—is “totally undermined” by the language in the prior provision because the prior provision does not have the same limitation found in the definition of Gross Proceeds. *Id.* at 24-25. SoundExchange is wrong.

As previously discussed, the two provisions that use the term “derived from” are separate and have distinct roles. There is only the appearance of an inconsistency because SoundExchange has inexplicably mashed the two provisions together. Section 384.3(a)(1) sets forth the formula for calculating royalties and the specified percentage-of-revenue rates to use in that formula. Section 384.3(a)(2) defines with specificity what is to be included in the royalty pool against which the rates are to be applied. As also noted above, this approach of spelling out the royalty formula and rates in a provision that is separate from the provision that precisely defines the royalty pool is regularly used by the Judges in regulations governing statutory royalty rates. And, while section (a)(1) provides that only revenues attributable to musical programs that use copyrighted sound recordings are to be included, that is not in conflict with the different limitations provided in the definition of Gross Proceeds. The limitation in section (a)(1) excludes

revenues that are unrelated to music programming, such as those earned by a BES providers for supplying non-music products. The limitation included in Section(a)(2) operates to exclude, among other things, revenues from musical programs that are attributable to copies made other than for the sole purpose of facilitating a BES transmission, such as dual-use copies. In short, there is no inconsistency between the two provisions.

II. SoundExchange’s Assertion that the Plain Meaning of the Gross Proceeds Definition Produces “Absurd Results” is Meritless

SoundExchange next asserts that the plain meaning of the Gross Proceeds definition “produces absurd results when viewing the statutory license system as a whole.” SX Opening Br. at 26. SoundExchange’s entire argument in this regard hinges on the fact that the PSS regulations in effect from 2013-2017 “similarly used the word ‘solely’ with reference to use of ephemeral recordings in those services.” *Id.* From this unremarkable proposition, SoundExchange leaps to the conclusion that if Music Choice’s interpretation of Gross Proceeds is correct, then “the only copies for which it would owe royalties are those used in *either* its BES or its PSS, *but not in both.*” *Id.* at 27. In other words, according to SoundExchange, if Music Choice were able to use only dual-use copies (copies used for both its BES and PSS services), those copies “would not generate any BES or PSS royalties.” This claim is patently false.

As an initial matter, and as SoundExchange itself acknowledges, the “BES and PSS licenses are separate and distinct.” SX Br. at 27. How the “separate and distinct” PSS regulations are relevant for interpreting the definition of Gross Proceeds for BES is never explained. Nor does it make any sense to look to “separate and distinct” regulations to attempt to understand what the word “solely” means in the definition of Gross Proceeds for BES providers. “Solely” is not a term of art used by the Judges when crafting regulations—its ordinary dictionary definition is well understood.

But even if the PSS regulations during one past rate period were relevant to the task at hand, they do not say anything close to what SoundExchange claims. A closer look at those regulations makes it abundantly clear that the regulations applicable to PSS and BES are not at all analogous. The PSS regulations state that “the monthly royalty fee to be paid by a [PSS] Licensee for the public performance of sound recordings pursuant to 17 U.S.C. 114 and the making of any number of Ephemeral Recordings to facilitate such performances pursuant to 17 U.S.C. 112(e) shall be a percentage of monthly Gross Revenues resulting from residential services in the United States as follows: for 2013, 8%; and for 2014 through 2017, 8.5%.” *Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services*, 78 Fed. Reg. 23,054, 23,096-23,097 (Apr. 17, 2013) (“*SDARS II*”). To be analogous to the BES regulation at issue, Gross Revenues (as defined in the *SDARS II* regulations) would have to limit the revenues in the royalty pool to just those that are derived from copies of sound recordings that are made for the sole purpose of facilitating a PSS transmission. But the applicable Gross Revenues definition contained no such limitation. In contrast to BES Gross Proceeds, Gross Revenues for PSS are defined as “all monies derived from the operation of the programming service of the Licensee and shall be comprised of” eight specified categories of revenues. *Id.* at 23,096. There is nothing in the Gross Revenues definition that allows a PSS to make the sort of carve-out that SoundExchange is suggesting.

Moreover, SoundExchange is also incorrect when it suggests that the use of the word “solely” in the PSS regulation it cites allowed Music Choice to reduce its PSS royalties. Like all other statutory sound recording licenses other than that applicable to BES providers, the PSS license has always been priced based upon the value of the sound recording performance rights. And, like with all those other statutory sound recording licenses, 5% of the PSS sound recording

performance royalties are attributed to ephemeral royalties, solely for the purpose of SoundExchange's distributions to its members. As a result, the provision quoted by SoundExchange has no impact whatsoever on the amount of royalties paid by Music Choice. Whether 0% or 5% of Music Choice's PSS royalties were ultimately attributed to ephemeral copies for distribution purposes, Music Choice would still pay the same total amount—its total royalty obligations cannot be diminished by the use of the word “solely” in the 2013-2017 PSS regulations. In short, the plain reading of the Gross Proceeds definition cannot produce the “absurd results” that SoundExchange is claiming.

III. SoundExchange's Preferred Reading of the Definition of Gross Proceeds is at Odds With its Own Discussion of Canons of Regulatory Interpretation

As noted above, SoundExchange's efforts to create an ambiguity in the meaning of Gross Proceeds all fail, as does its effort to suggest that the plain meaning of Gross Proceeds leads to absurd results. But there is another fundamental problem with SoundExchange's Opening Brief. Its preferred reading of Gross Proceeds is at odds with its own discussion of the canons of regulatory interpretation. As SoundExchange rightly notes, there is an “endlessly reiterated principle of statutory construction...that all words in a statute are to be assigned meaning, and that nothing therein is to be construed as surplusage.” SX Opening Br. at 25 (quoting *Qi-Zhuo v. Meissner*, 70 F.3d 135, 139 (D.C. Cir. 1995)). SoundExchange goes on to explain that this “surplusage canon” requires that “if it can be prevented, no clause, sentence, or word shall be superfluous, void or insignificant.” *Id.* at 25 (quoting *TRW Inc. v. Andrews*, 534 U.S. 19, 31 (2001)). SoundExchange further argues that “[c]ourts have invalidated interpretations of both statutes and regulations by regulatory agencies on the basis that those agencies' interpretations did not heed the rule against surplusage.” *Id.* at 25-26. Yet, despite discussing at some length the importance of the “surplusage canon,” SoundExchange inexplicably asks the Judges to violate it.

Nowhere in its Opening Brief does SoundExchange provide any plausible meaning for the “sole purpose” limiting language that is at the heart of this referral. Instead, it asks that, notwithstanding this limiting language, that the Judges “issue an order clarifying that 37 C.F.R. § 384.3(a) requires BES providers to calculate royalties using their total gross proceeds derived from the use of copyrighted recordings in a BES, regardless of whether operation of the BES involves copies or channels that are also used as part of a PSS.” SX Opening Br. at 35-36. In other words, SoundExchange is asking the Judges to read out the limiting language—a clear violation of the “surplusage canon.”

The single halfhearted effort that SoundExchange appears to make to provide some meaning to the “sole purpose” language is its assertion that the Gross Proceeds definition calls for the inclusion of all fees and payments, and “then goes on to specify what kinds of ‘in kind’ consideration” must be included. *Id.* at 23. SoundExchange’s claim appears to be that it is only “in kind” consideration that is limited by the “sole purpose” language, and that the “sole purpose” language does not apply to any other form of consideration. *Id.* But as noted above, this interpretation of the Gross Proceeds definition is internally inconsistent and makes no sense. It strains credulity to suggest that “all fees and payments” must be included, but, at the same time, that only certain kinds of “in-kind” payments—a subset of all fees and payments—must be included. And it makes no sense to suggest, as SoundExchange does, that in-kind payments can “facilitate a transmission.” The Gross Proceeds definition at issue is clearly referring to copies of sound recordings that facilitate transmissions of those recordings, and not certain “in kind” payments. Accordingly, the one effort SoundExchange makes to give some meaning to the “sole purpose” language utterly fails. In the absence of any plausible alternative meaning of the language at issue in the Gross Proceeds definition, the plain meaning of the text must stand.

Were that not enough, there is a second way in which SoundExchange’s preferred interpretation is at odds with its own discussion of canons of regulatory interpretation. SoundExchange points out that “the ‘surplusage canon’ applies with particular force ‘when the intersection of subsections becomes so great that one subsection renders another meaningless.’” SX Opening Br. at 25 (quoting *S.E.C. v. Familant*, 910 F. Supp. 2d 83, 95 (D.D.C. 2012)). But that is precisely what SoundExchange’s preferred reading of Gross Proceeds does. It not only reads out the “sole purpose” limiting language found in 37 C.F.R. 384.3(a)(2), but it also renders 37 C.F.R. 384.3(c) meaningless.

The “Other [R]oyalty [R]ates and [T]erms” provision—section 384.3(c)—states that “[f]or ephemeral recordings other than those governed by paragraph (a) of this section [e.g., those not made for the sole purpose of facilitating a BES transmission], persons making such ephemeral recordings must pay royalties, to the extent (if at all) applicable, under 17 U.S.C. § 112(e) or as prescribed by other law, regulation, or agreement.” 37 C.F.R. § 384.3(c). In other words, to the extent a BES provider is making dual-use copies—copies that are not governed by section 384.3(a)—royalties for those other copies, if required at all, are to be paid pursuant some other law, regulation or agreement. SoundExchange’s preferred reading of section 384.3(a) cannot be squared with this provision. If a BES provider is required to pay for all ephemeral copies, whether made solely to facilitate a transmission by a BES or not, then all copies made by a BES would be covered by section 384.3(a) and there would be no copies left for section 384.3(c) to address, rendering it meaningless. Indeed, the very existence of section 384.3(c) further underscores that exclusions of revenue derived from certain BES ephemeral copies must be allowed by the applicable BES regulations.

IV. Flawed Fact-Finding and Analysis From the Decades-Old CARP Proceeding Are Irrelevant, But In Any Event Are Not Inconsistent With the Plain Meaning of Gross Proceeds

A. SoundExchange improperly continues to ask the Judges to engage in fact-finding

The Judges have repeatedly ruled that fact-finding related to a royalty payment dispute, including in connection with a legal referral from a district court, is beyond their jurisdiction and outside the scope of such a referral. Order Reopening Two Proceedings and Scheduling Briefing, Doc. No. 26360, p. 2; Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services, 82 Fed. Reg. 56,725, 56,727 (Nov. 30, 2017) (rejecting the argument that the Judges’ “continuing jurisdiction to interpret, or their ability to provide ‘interpretive guidance,’ somehow endows them with jurisdiction to resolve factual disputes relating to application of those regulations.”); *id.*, at 56,726 (“the District Court could not have referred to the Judges resolution of the ultimate issues of fact presented by the SoundExchange litigation. The District Court is the forum in which resolution of the factual dispute lies. . . . Notwithstanding language or rhetoric regarding the application of the CRB regulations to the facts of the District Court matter, the narrow question referable to the Judges was one of interpretation.”).

Indeed, in this very proceeding, the Judges have already rejected SoundExchange’s attempt to vastly expand the scope of the referral to include extensive discovery and fact-finding, holding:

The Judges agree with Music Choice that the issue referred is narrow. . . . The Judges are tasked with interpreting their regulations. Whatever that interpretation, the parties shall pursue remedies or relief in the underlying District Court action, to the extent permitted by that court.

The Judges therefore **GRANT in part** SoundExchange’s motion to the extent its seeks to permit briefing on questions of statutory interpretation. Pursuant to the District Court’s referral, the Judges

hereby reopen two of the three captioned proceedings . . . for the limited purpose of addressing the meaning of “Gross Proceeds” as defined in 37 C.F.R. 384.3(a). The Judges **DENY** SoundExchange’s Motion in all other respects.

Order Reopening Two Proceedings and Scheduling Briefing, Doc. No. 26360, p. 2. This clear ruling is consistent with prior rulings of the Judges cited above, and also with the District Court’s referral, which merely asked the Judges to provide an advisory opinion on their legal interpretation of the Gross Proceeds definition. *SoundExchange, Inc. v. Music Choice*, 2021 WL 5998382, at *3, 12 (D.D.C. Dec. 20, 2021).

Notwithstanding the Judges’ clear ruling, SoundExchange refuses to take “no” for an answer. In a mockery of that ruling, SoundExchange submits a fifty-six page declaration including ten exhibits and spends most of its Opening Brief asking the Judges—yet again—to rely upon SoundExchange’s own distorted spinning of disputed facts related to the underlying audit dispute and cherry-picked factual evidence and analysis from the record of a CARP proceeding that took place over twenty years ago. Declaration of Mary Marshall (“Marshall Decl.”). The Judges should again reject SoundExchange’s attempt to have them resolve disputed facts or otherwise engage in fact-finding in connection with this limited legal referral.

1. Improper fact-finding from District Court pleadings

SoundExchange asks the Judges to make factual determinations regarding Music Choice’s BES royalty calculations and features of its BES service based upon faulty inferences it draws from cherry-picked sections of Music Choice’s Answer in the underlying District Court action. SX Opening Br. at 15, 17. As noted above, these allegations are irrelevant to the Judges’ sole task in this proceeding: advising the District Court on the Judges’ legal interpretation of the applicable Gross Proceeds definition.

Moreover, SoundExchange distorts the cited pleadings in order to mislead and distract the Judges. Not surprisingly, over the past twenty-plus years, both the technology and distribution channels for Music Choice's BES have changed in several ways. With respect to the one quoted statement from Music Choice's Answer concerning its BES royalty calculation, Music Choice was responding to specific allegations in SoundExchange's Complaint in the District Court, referencing a specific time period covered by one "audit" SoundExchange conducted. Consequently, it reflects the methodology that Music Choice used in calculating those specific payments to reflect the more generally-applicable rule that it must only include in Gross Proceeds those revenues derived from transmissions where ephemeral copies were made solely for the purpose of facilitating those transmissions. It does not necessarily reflect any number of other ways that the sole-purpose limitation could be implemented, depending on the many different ways that a given BES might transmit or distribute its service offering.

Similarly, SoundExchange cites Music Choice's statement that the number of channels it offered during certain specific time periods at issue in the underlying District Court proceeding has varied, depending both on the time period and the particular subscribers. SX Opening Br. at 17. From this fairly mundane fact, SoundExchange bizarrely asks the Judges to infer that Music Choice has underpaid its BES Royalties. Again, whether Music Choice has underpaid its BES royalties is the ultimate question for the District Court to resolve. Moreover, SoundExchange's claim does not even make sense. There is nothing inherent in offering "in some instances and at certain times, nearly one hundred channels to certain of its" BES subscribers that would render Music Choice's royalty payments—which are not even in the record of this proceeding—insufficient. *Id.*

It would be inappropriate for the Judges to draw from these isolated statements from Music Choice's Answer in the District Court proceeding any conclusions at all, and certainly none that would be relevant to the Judges' purely legal determination in this proceeding. This is particularly true with respect to facts relating only to the features and royalty payment calculations that have changed over time and only apply to one particular BES. As with all disputed facts, it will be the District Court's job to oversee the finding of those facts. SoundExchange's attempt to inject these distractions into this proceedings should be rejected.

2. Improper fact-finding from unrelated Copyright Office proceedings

SoundExchange seeks to further distract the Judges by mischaracterizing statements made by Music Choice in other regulatory proceedings to support SoundExchange's present factual allegations regarding Music Choice's BES. SX Opening Br. at 14-15. In particular, SoundExchange claims that in connection with the Copyright Office's music licensing study, Music Choice somehow acknowledged that it was "necessary" to make "server, cache, buffer, and other intermediate copies." *Id.* at 15. As a preliminary matter, in the section of Music Choice's submission selectively quoted by SoundExchange, Music Choice was not discussing how its BES in particular functioned. In an earlier section discussing the many problems inherent in the section 112 ephemeral license generally, Music Choice noted that these problems created a particularly absurd result for BES because they risked requiring a BES effectively to pay for the very performance rights from which Congress exempted them. However, the specific language quoted by SoundExchange comes from Music Choice's discussion of the problem of intermediate copies generally, including as made by internet transmissions. It was not even referring to its own services (much less its BES service). Nor did it say that such "cache, buffer, and other intermediate copies" were "necessary," as SoundExchange misrepresents. Music Choice merely made the uncontroversial statement that such copies "are actually used."

Comments of Music Choice in Copyright Office Docket No. 2014-03 at 13.³ Moreover, as demonstrated below, the law has developed to recognize that such intermediate copies do not require licenses to avoid infringement liability.

In any event, it is wholly unnecessary—and would be inappropriate—for the Judges to make factual findings regarding the manner and extent to which Music Choice actually makes various types of intermediate copies of data in connection with its BES. In addition to the limited nature of the District Court’s referral, the applicable Gross Proceeds definition must be interpreted in a way that applies fairly to all BES, not just Music Choice.

3. Improper fact-finding from unreliable and unauthenticated website printouts and unsupported assertions

Notwithstanding the Judges’ clear ruling that they would not engage in fact-finding, SoundExchange goes so far as to submit many pages of purported “evidence,” including several printouts of website pages that it seeks to attribute to Music Choice.⁴ Marshall Decl., Exs. D-J. The Judges should not reward SoundExchange’s tone-deaf defiance of the spirit—if not the letter—of the Judges’ prior ruling by even considering its purported fact evidence. Moreover, the content of those web pages is not relevant to any rational interpretation of the Gross Proceeds definition. It is not clear exactly what point SoundExchange is attempting to make when it cites these various purported web page printouts. At most, it seems to argue that they support a fact-finding that Music Choice offered approximately 50 channels in its BES offering for several

³ Available at

https://www.copyright.gov/policy/musiclicensingstudy/comments/Docket2014_3/Music_Choice_MLS_2014.pdf

⁴ SoundExchange notes that in the pending *SDARS III* remand proceeding, Music Choice objected to similar attempts by SoundExchange to introduce and rely upon unreliable and unauthenticated printouts from the “Wayback Machine” website. Although it claims generally that some courts have accepted Wayback Machine printouts in a handful of cases, SoundExchange fails to address the limited circumstances and requirements for authentication of such printouts, which it has not met in this case. Moreover, two of the web pages, Exhibits D & J, purport to be from web pages that are not controlled by Music Choice. Instead, they are web pages controlled by an independent distributor of Music Choice’s BES.

years, and recently may have increased the number of channels. SX Opening Br. at 16-17 & n.13. It does not explain why—even if true—this fact would be relevant to the purely legal question referred to the Judges: the meaning of the Gross Proceeds definition. Notably, none of the exhibits purport to be from years where any payments were actually “audited” by SoundExchange. Marshall Decl. Exs. E-J (purporting to be from 2008, 2009, 2018, and the present, while the only BES years “audited” by SoundExchange to date were 2014-2017).

In addition to these unreliable and irrelevant exhibits, SoundExchange goes so far as to ask the Judges to find facts without any support at all. In particular, SoundExchange asks the Judges to find that it “has no way to know what calculations Music Choice actually performed” in connection with Music Choice’s BES royalty payments, SX Opening Br. at 16, and that Music Choice “has hid the details of its allocation methodology from SoundExchange for years.” *Id.* at 19. SoundExchange does not even attempt to provide any support for these bald accusations, which are false. Nor does SoundExchange identify any requirement in the reporting or audit provisions of the regulations that Music Choice failed to fulfill. These baseless and entirely irrelevant attacks on Music Choice should be ignored.

As Music Choice explained in its Opening Brief, SoundExchange purported to audit Music Choice’s BES payments for 2014 through 2016. MC Opening Br. at 5-6. In connection with that examination, which was not actually an independent audit as required by the regulations, Music Choice fully cooperated with SoundExchange’s forensic consulting accountant and answered any questions he had regarding Music Choice’s calculations. *See id.* This non-audit obviously disclosed Music Choice’s calculations for that royalty period because it was the basis for the underlying District Court litigation.

This argument is nothing more than a rehash of the strategy used by SoundExchange in the *SDARS III* remand proceeding in which it, and its consulting forensic accountant Mr. Stark who testified about the very same royalty examination that included both PSS and BES royalties, falsely claimed that Music Choice had refused to provide various information about its calculation of PSS royalty payments. *See* Music Choice’s Responsive Brief on Remand, 16-CRB-0001-SR/PSSR (2018-2022) (Remand), Doc. No. 25713, pp. 28-32. Indeed, SoundExchange made an exactly analogous false claim in that proceeding, namely that Music Choice had refused to explain how revenues were allocated between PSS and non-PSS for the purpose of computing Gross Revenues under the PSS regulations. *Id.* at 32. Music Choice demonstrated that the work papers provided to Mr. Stark expressly disclosed the methodology for those allocations. *Id.* Yet SoundExchange seeks to rely on the same misrepresentations in this proceeding.

In any event, SoundExchange’s audit rights provide a full opportunity to examine any allocation methodologies used to calculate Gross Proceeds—the very information it wrongly claims that Music Choice has been “hiding.” SoundExchange’s dissatisfaction with the results of such an allocation cannot justify its attempt to erase the plain meaning of the text of the Gross Proceeds definition from the BES regulations.

4. Improper fact-finding from CARP proceeding

If it were not bad enough to ask the Judges to engage in fact-finding based upon website printouts and pleadings from the underlying District Court action, SoundExchange also asks the Judges to make factual determinations based upon cherry-picked excerpts from the record of a CARP proceeding that took place over twenty years ago. SX Opening Br. at 6-9, 27-34. As demonstrated above, fact-finding is outside the scope of this legal referral. As demonstrated in detail below, even if factual determinations were appropriately within the scope of this

proceeding, the record of the CARP proceeding could not possibly provide a reasonable basis for supporting SoundExchange's preferred interpretation of Gross Proceeds.

- B. The CARP's analysis was the product of a minimal record reflecting the operations of only one BES among many and is inconsistent with subsequent factual and legal developments, including settled ratemaking principles employed by the Judges

As noted above, SoundExchange cannot possibly provide any rational interpretation of the actual text of the Gross Proceeds definition that would require Music Choice to include in those Gross Proceeds revenues that were not derived from its use of ephemeral copies made for the sole purpose of facilitating a BES transmission. Faced with this immutable and fatal problem, SoundExchange seeks to distract the Judges by pointing to various testimony, fact-findings, and analyses from the CARP proceeding that produced the first rates and terms for the BES license. That proceeding occurred over twenty years ago, at a time when digital transmission technologies, copyright law related to those technologies, and ratemaking and benchmarking principles surrounding the statutory licenses were all in their infancy. Moreover, only one BES licensee participated in the proceeding, resulting in a limited fact record that did not reflect the variety of BES in operation at that time, much less the significant changes that have occurred in the intervening decades. Nothing in that ancient CARP proceeding can provide useful guidance in this proceeding, much less support SoundExchange's request that the Judges ignore the plain meaning of the actual text in the Gross Proceeds definition.

1. The Judges are not bound by the CARP's ruling where subsequent factual and legal developments support different analyses and conclusions

Even if this proceeding were a full rate proceeding—rather than the limited legal referral to the Judges—it is well established that the Judges are not required to follow the same reasoning, accept the same benchmarks, or otherwise bind themselves to the analyses or fact record in that early proceeding. Indeed, the D.C. Circuit has held that the Judges are free to

depart from CARP precedent so long as they provide a reasoned explanation for doing so. *Music Choice v. Copyright Royalty Bd.*, 774 F.3d 1000, 1014 (D.C. Cir. 2014) (citing *Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd.*, 574 F.3d 748, 762 (D.C. Cir. 2009)). See also *SDARS II*, 78 Fed. Reg. 23,054, 23,055.

In *SDARS II*, Music Choice relied in part on the first PSS CARP proceeding, in which the CARP used the PSS' musical works performance licenses as a benchmark to set the original PSS rates. Music Choice argued that in the absence of any more comparable marketplace licenses, the Judges were required to follow that CARP precedent and again use those benchmarks. The Judges rejected that argument on a number of grounds. Among them was that benchmarking is inherently based upon a factual record regarding the relevant marketplace, and fact-finding in any particular proceeding is not precedential. *Id.* The Judges further held that the historical context of the original CARP proceeding, when the PSS market was in its infancy and the statutory license was brand new, resulted in an evidentiary record before the CARP that was significantly different from that in the later *SDARS II* proceeding, and that difference alone was sufficient to deprive the CARP proceeding of any binding precedential effect. *Id.* The Judges then rejected entirely the use of Music Choice's PRO benchmarks on the ground that the rights licensed in the PRO licenses were different from the rights included in the statutory PSS license and therefore were not sufficiently comparable to be useful. *Id.* at 23,058.

On appeal, the D.C. Circuit upheld the Judges' ruling on this point, finding that even to the extent that the CARP's decision (and subsequent Librarian's decision in the same proceeding) included legal rulings that might be precedential, the Judges were free to depart from such rulings because they provided an adequate explanation for doing so. *Music Choice*, 774 F.3d at 1014. In particular, the appellate court held that the differences in "historical

context” and the evidentiary records between the CARP and the SDARS II proceedings were sufficient justifications for the Judges to come to different conclusions than those reached by the CARP and Librarian. *Id.*

In this limited referral on a narrow question of purely legal interpretation, SoundExchange points to various testimony and rulings in the Webcasting/BES CARP in an attempt to persuade the Judges to ignore the plain meaning of the language used in the Gross Proceeds definition. As demonstrated in greater detail below, there are even stronger grounds to depart from any of the analysis or rulings in the Webcasting/BES CARP than there were with respect to the PSS CARP.

2. The factual record before the CARP was limited and flawed

The CARP proceeding upon which SoundExchange seeks to rely was instituted—over twenty years ago—to determine the initial rates and terms for both the webcasting statutory license and the BES license in one consolidated proceeding. In contrast to the webcasting portion of the proceeding, which included seventeen different webcasting licensees as active participants, the BES portion of the proceeding included only one participant: DMX/AEI Music Inc. (“DMX”). *See* Report of the Copyright Arbitration Royalty Panel, *Rate Setting for Digital Performance Right in Sound Recordings and Ephemeral Recordings*, Interim Public Version, Docket No. 2000-9 CARP DTRA 1 & 2, at 2-3 (Feb. 20, 2002) [“*Web I CARP Rept.*”].⁵ That sole participant, DMX, which also operated a PSS for some time, subsequently was dissolved in bankruptcy and certain assets related to the DMX service were acquired out of the bankruptcy

⁵ Three BES petitioned to participate: DMX Music, Inc., AEI Music Network, Inc., and Music Choice. Music Choice, having endured significant expense litigating the first PSS proceeding, could not afford to litigate and subsequently withdrew. By the time of the CARP hearing, DMX and AEI merged into a single entity. *See Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings and Ephemeral Recordings*, Docket No. 2000-9 CARP DTRA 1&2, 67 Fed. Reg. 45,240, 45,263 & n.38 (July 8, 2002) [“*Web I Librarian’s Determination*”].

estate. *See Designation as a Preexisting Subscription Service*, Docket Nos. RF 2006-2 & RF 2006-3. 71 Fed. Reg. 64,639, 64,641 (Nov. 3, 2006). As the Judges are aware from subsequent PSS proceedings, that new company operating a new version of the DMX service is not the same entity and therefore no longer has PSS status.

Given that only one licensee participated in the proceeding, it is not surprising that the evidentiary record was very limited and only reflected the operations of that participant. Thus, the record regarding the technical functioning, market, and business operations of the BES available to the CARP was limited to that of DMX. The resulting fact-findings, which informed the CARP's (and Librarian's) analysis and resulting determination were inherently flawed, even with respect to the BES market as it existed back in 2001. Indeed, after the CARP issued its Report based upon various fundamental misapprehensions regarding the scope and functioning of the BES and their use of ephemeral copies driven by the limited record available to it, Music Choice attempted to intervene and inform the CARP and Register that other BES—including Music Choice—operated quite differently from DMX and made significantly less use of ephemeral copies than DMX claimed to make. *See Motion to Accept Petition and Petition for Clarification*, 2000-9 CARP DTRA 1 & 2, eCRB Doc. No. 7314, at 3-7 (Mar. 6, 2002); *Order*, 2000-9 CARP DTRA 1 & 2, eCRB Doc. No. 12801, at 2 (March 25, 2002). The Register of Copyrights denied Music Choice's petition to modify the CARP Report on the ground that Music Choice was not a participant in the proceeding and therefore lacked standing. *Order*, at 3.

One perennial problem with rate proceedings before the CARP and Copyright Royalty Board is that they are extremely costly, both in dollars and disruption. It is therefore a recurring issue that many licensees (and even smaller independent copyright owners) cannot bear those

costs and, as a result, their interests are not represented in these proceedings.⁶ The CARP nonetheless was required to issue a determination. But that does not mean that the Judges are foreclosed from deviating from what the CARP did, so long as there is good reason for doing so. And here, because the record in that proceeding was so incomplete, it makes imminent sense to do so, and it would be erroneous to compound the problems created by the first BES CARP proceeding by relying upon fact-finding or analysis based upon that flawed record, even with respect to issues relating to the BES market and license as they existed in 2001.

Reliance on the CARP record would be even more erroneous when applied to the BES market and license as they exist today. Indeed, relying upon the CARP's understanding and analysis of the use of ephemeral copies for the purpose of construing the BES regulations today would be akin to using primitive cave drawings as anatomical illustrations to guide modern-day laser surgery procedures. The CARP proceeding took place at a time when the technology used for digital music transmissions, the market for BES using such digital transmissions, legal precedent addressing the copyright treatment of various types of data copying inherent in those transmissions, and even benchmarking approaches for setting rates for statutory copyright licenses, were all in their respective infancies. As noted above, even in 2001, the technology used by DMX was not representative of that used by other BES. It certainly bears no relation to the technologies used by BES today. Blindly following the CARP's fact-finding, analysis, and reasoning as if the intervening twenty years had not happened would be a mistake. And as demonstrated in more detail below, subsequent legal developments have been based upon better understandings of digital transmission technologies, and the Judges have significantly refined

⁶ Indeed, this is the reason that the BES rates and terms have never been subject to another proceeding. The market is so marginally profitable and the revenues so low that even the absurdly high rates contained in the current regulations cannot rationally support the cost of litigation necessary to correct them.

their approaches for engaging in benchmarking analyses to determine reasonable rates for the various statutory licenses they oversee. The CARP’s reasoning and analysis are inconsistent with these more recent advancements, rendering that reasoning and analysis unhelpful to any modern ratemaking exercise.

3. The legal analysis employed by the CARP is inconsistent with modern precedent and fundamental ratemaking principles employed by the Judges

The CARP’s entire analysis of the benchmarking and legal principles applicable to its determination of rates and terms for the BES license was riddled with legal errors. While perhaps defensible at the time due to the limited record available in that proceeding, the analysis can no longer withstand scrutiny.

- (a) The CARP’s use of “on-premise” distribution license benchmarks was inconsistent with the Judges’ well-established rulings on benchmarking

In the intervening decades since the time of the CARP, the Judges have developed consistent and well-established principles to evaluate marketplace benchmarks. The Judges have consistently held that the *sine qua non* of benchmarking is comparability. *See, e.g., Determination of Rates and Terms for Digital Performance or Sound Recordings and Making of Ephemeral Copies to Facilitate Those Performance (Web V)*, Docket No. 19-CRB-0005-WR (2021-2025), 86 Fed. Reg. 59,452, 59,569-70 (Oct. 27, 2021) [“*Web V*”] (noting that only “comparable” marketplace evidence may be considered by the Judges pursuant to section 114 and that “[t]he Judges have long acknowledged that comparability is a key consideration in determining the usefulness of a proffered benchmark.”); *SDARS II*, 78 Fed. Reg. at 23,058.

The proponent of a benchmark bears the burden of establishing its comparability with the target license and market. And to the extent there are differences, that participant bears the further burden of making reasoned adjustments to the benchmark to account for those

differences. *Web V*, 86 Fed. Reg. at 59,569-70; *SDARS II*, 78 Fed. Reg. at 23,058. The D.C. Circuit has consistently upheld this comparability requirement. *See, e.g., SoundExchange v. Copyright Royalty Bd.*, 904 F.3d 41, 50-51 (D.C. Cir. 2018); *Music Choice*, 774 F.3d at 1012.

The only benchmarks used by the CARP in setting the initial rates and terms for BES were a handful of major-label “on-premises” background music service licenses. *Web I CARP Rept.* at 122-26. These on-premise services were typical of the way commercial background music was delivered prior to the advent of digital performance technology, and the sole CARP participant—DMX—had provided such on-premise services for many years prior to the CARP. To deliver its on-premise background music service, such a provider would make physical copies of hours of music programming, comprising all of the sound recordings to be performed by each business location receiving the service, including on tape, compact disc, and hard drives, and distribute those copies to each such location. *See Web I CARP Rept.* at 112. *See also* Testimony of Barry Knittel, Docket No. 2000-9 CARP DTRA 1 & 2, Sept. 5, 2001 Hearing Transcript, at 8363:4–19; 8364:5–18; 8365:12-18; 8366:17–8367:9; 8368:18–8369:21; 8414:16–8416:1 [“Knittel Testimony”] (Fakler Decl., Ex. 1) (describing how, for each business location, four hours of music programming is copied onto cassette, compact disc, or hard drive and those physical copies are distributed to each business location where they are played for between 30 days and fourteen months, depending on the preferences of the business); Testimony of Douglas Talley, Docket No. 2000-9 CARP DTRA 1 & 2, Sept. 6, 2001 Hearing Transcript at 8631:9–15; 8640:6–19; 8643:5–12; [“Talley Testimony”] (Fakler Decl., Ex. 2).⁷

⁷ SoundExchange submitted incomplete excerpts from the CARP testimony of these witnesses. Music Choice submits the full testimony of these witnesses for the Judges’ convenience, without intending to waive its position that SoundExchange’s submission and reliance on this testimony is improper.

The copying and distribution rights necessary to operate such an on-premise service are fundamentally different from the ephemeral recording right in the BES license. The CARP acknowledged that these proposed benchmark agreements provided a different kind of reproduction right than that involved in the ephemeral recording right and that a public distribution right that is not in any way included in the BES license. *Web I CARP Rpt.* at 122. The CARP nonetheless used those agreements as the sole benchmarks, without even attempting to adjust them or explain how licenses for different rights could be comparable, stating merely that the on-premise licenses “were effectively intended to permit the licensees to utilize sound recordings in operating the [on-premise] background music services in question.” *Id.*

Moreover, the CARP even acknowledged that the on-premise benchmark license agreements included additional rights and “benefits beyond the use of the sound recordings.” *Id.* at 124. Yet it treated the licenses as though they were comparable and did not even attempt to adjust them to account for these non-sound recording benefits that were obviously not included in the BES license. Instead, the CARP merely stated that it was “clear” that the most important rights conveyed in the benchmarks were the sound recording reproduction and distribution rights, and therefore “it is thus reasonable to infer” that all of the consideration in those license agreements was attributable to the sound recording reproduction and distribution rights. *Id.*

Additionally, the very testimony cited by SoundExchange shows that those benchmark agreements contained various deductions, including deductions for the on-premise service’s musical composition mechanical and performance license payments to ASCAP, BMI, SESAC, and Harry Fox.⁸ Knittel Testimony, at 8384:4-14. The fact that the CARP did not separately

⁸ Further demonstrating how fundamentally different the on-premise distribution right is from the rights needed for a BES, the on-premise services require mechanical licenses to reproduce and distribute copies of the musical works embodied in the sound recordings. In contrast, neither Music Choice nor any other non-interactive digital music service have ever had to obtain mechanical licenses for those services.

incorporate these specific deductions into the BES royalty structure provides yet another example of its improper benchmarking practice and, as a result, provides further support for the need to ensure that the plain meaning of the limitations in the language of the Gross Proceeds definition be given full effect and not read out of the BES regulations as SoundExchange suggests.

Music Choice respectfully submits that the CARP's total failure to address the lack of comparability of the benchmark on-premise agreements with the target market would be unacceptable to the Judges under their well-established benchmarking precedent. Were they confronted with these on-premise benchmarks, the Judges simply would not—and could not, consistent with that precedent—use the on-premise benchmarks as the CARP did. Those benchmarks were for a different type of service (on-premise vs. broadcast) and contained different rights (broad reproduction rights, completely different distribution rights, and additional rights unrelated to the sound recordings themselves in the benchmarks vs limited ephemeral reproduction rights only in the BES license). These fundamental differences are exactly the kinds of differences that have led the Judges to reject proffered benchmarks.

For example, in *SDARS II*, the Judges rejected Music Choice's proffered musical works performance license benchmarks, even though they were for the exact same service, because they included different rights. *SDARS II*, 78 Fed. Reg. at 23,058. In that same proceeding, the Judges rejected SoundExchange's proffer of 2,000 different license agreements, on the grounds that those agreements covered different types of services and other rights, including the very same public distribution rights contained in the on-premise background music benchmarks used by the CARP. *Id.* (Ringtone and download licenses rejected as benchmarks, *inter alia*, because they granted "rights separate and apart from the right to publicly perform sound recordings in the

context of this proceeding.”). If the Judges would not use these benchmarks to determine the rates and terms for the BES in the first instance, they certainly should not reach back in time to use them or the reasoning and analysis employed by the CARP and Librarian based upon them, to interpret the plain language of the current BES Gross Proceeds definition.

- (b) The CARP’s analysis of ephemeral copies is inconsistent with the weight of subsequent precedent concerning the copyright status of cache, buffer, and other transitory “copies”

In addition to its fatally flawed benchmarking, the CARP’s analysis (and subsequent Librarian’s determination based on that analysis) was further infected by its fundamental misunderstanding of the types of data copying used for digital transmissions and the copyright treatment of that copying. Those errors may be forgiven in the context of the limited record before the CARP and the paucity of legal precedent at that time, but there is no excuse over twenty years later to make the same mistakes. With the benefit of hindsight, we can clearly see that the CARP labored under a confused and overly-broad view of what ephemeral copies are and which types of copies potentially required a license, which is inconsistent with contemporary understandings of the Copyright Act. In particular, the CARP relied on a belief that Congress intended copyright owners to be paid for not only full server copies of sound recordings, but also all fleeting buffer copies of small packets of data that are made during any digital transmission or other performance of a sound recording. This is inconsistent with the legislative history of the section 112 license, as well as intervening precedent, which establishes that these “copies” do not require a license in the first place because they are either not sufficiently “fixed” to implicate the reproduction right, or are privileged under the fair use doctrine.

At the time of the CARP proceeding, the section 112 “ephemeral” license was new, and there was considerable confusion as to what an ephemeral copy was. The confusion was not helped by the testimony in that proceeding. Neither of the two witnesses who testified on behalf

of DMX in the CARP proceeding were attorneys, and they both testified that they did not actually know what an ephemeral copy was, despite using the term throughout their testimony. Knittel Testimony at 8400:20-8401:5; 8410:4-10; Talley Testimony at 8672:5-18; 8680:16-8681:19. Due to this confusion, the record contains testimony regarding DMX's need to make many millions of "ephemeral" copies, when the witnesses were actually discussing miniscule, transitory data buffer copies that are made in the course of not only digital transmissions, but even when a consumer played a compact disc in a CD player.

Mr. Talley, who provided the only testimony relied upon by the CARP to support its findings relating to the nature of the ephemeral copies supposedly made by BES, was an engineer. He separated the types of "copies" made for the purpose of both the on-premise and BES services offered by DMX into "cache" and "buffer" categories. He viewed buffer copies as copies of small bits of data made for the purpose of transmitting or using digital data where those copies are constantly overwritten as they are used. As an example, he noted that when a consumer plays a CD, 32-bit chunks of data are read from the CD 44,000 times per second and copied into a buffer to be converted into an analog signal, such that in a four-minute song over 10 million "buffer copies" are made. Talley Testimony, at 8637:2-8638-12. Mr. Talley testified that throughout the process of providing DMX's BES, millions of these types of buffer copies are made inherently by the functioning of digital technology. *Id.* at 8639:7-21.

Mr. Talley contrasted buffer copies with "cache" copies, which he used to describe full copies of an entire recording that would be used for repository or playback purposes and would be retained in their full form for some significant period of time. The only examples of cache copies he gave were server copies of the sound recordings that were made (1) in a digital repository from which further copies would be made onto physical media to be distributed for

the on-premise service and (2) to create additional server copies on 120 playback servers—one for each channel offered—from which the BES channels would be transmitted only to BES customers. *Id.* at 8658:21-8660:19. Based on Mr. Talley’s testimony, the CARP concluded that DMX—and therefore by assumption all BES—needed to make many millions of ephemeral copies covered by the section 112 license, and therefore the 112 license must have significant value. *Web I CARP Rpt.* at 117-18. This analysis was clearly wrong and in any event inconsistent with the legislative history of section 112(e), the Register of Copyright’s interpretation of the ephemeral license, and intervening legal precedent concerning the copyright status of buffer and other intermediate copies.

As demonstrated in greater detail in Music Choice’s Opening Brief, the legislative history of the section 112(e) license only references coverage for multiple server copies used for the purpose of making digital music transmissions, and the Register of Copyright has consistently stated that the license was only meant to cover server copies, not buffer copies, and that neither server nor buffer nor cache copies have any independent economic or copyright policy value from the performances they enable. *MC Opening Br.* at 15-18. As the courts have grappled with copyright issues related to the internet and other digital technologies, they have agreed with the Register’s assessment and even gone farther.

It is now well established that buffer copies, consisting of small chunks of digital data that persist for only short periods of time before being overwritten, do not even constitute “copies” as that term is used in the Copyright Act and therefore do not require a license. As the D.C. Circuit has explained:

The Copyright Act defines ‘copies’ as ‘material objects . . . in which a work is fixed’ and considers a work ‘fixed’ in a tangible medium of expression when its embodiment in a copy . . . is sufficiently permanent or stable to permit it to be perceived,

reproduced, or otherwise communicated for a period of more than transitory duration. 17 U.S.C. § 101. We agree with the district court that this definition of copy does not include ‘ephemeral transmission of a picture across the internet.’ Instead, the copy becomes ‘fixed’ when the picture is reproduced for a viewer.

IMAPizza, LLC v. At Pizza Ltd., 965 F.3d 871, 877 (D.C. Cir. 2020). Other courts have agreed.

The Second Circuit has held that:

The [Copyright Act] provides that a work is “‘fixed’ in a tangible medium of expression when its embodiment . . . is sufficiently permanent or stable to permit it to be . . . reproduced . . . *for a period of more than transitory duration.*” . . . We believe that this language plainly imposes two distinct but related requirements: the work must be embodied in a medium, i.e., placed in a medium such that it can be perceived, reproduced, etc., from that medium (the “embodiment requirement”), and it must remain thus embodied “for a period of more than transitory duration” (the “duration requirement”). . . . Unless both requirements are met, the work is not “fixed” in the buffer, and, as a result, the buffer data is not a “copy” of the original work whose data is buffered.

Cartoon Network LP, LLLP, v. CSC Holdings, Inc., 536 F.3d 121, 127 (2d Cir. 2008)(citations omitted). In *Cartoon Network*, the Second Circuit held that buffer copies made to transmit performances of audiovisual works were not infringing where data resided in the buffer for no more than 1.2 seconds before being overwritten, because the copyrighted works were not embodied in the buffer copies for more than a transitory duration and therefore were not “fixed.” *Id.* at 130. In the examples given by DMX at the CARP, Mr. Talley discussed buffer copies that were overwritten 44,000 times per second. Talley Testimony at 8638:2-12. Though he mistakenly referred to these as ephemeral copies, they could not possibly be considered “copies” at all as that term is used in the Copyright Act. *See also CDK Global LLC v. Brnovich*, 16 F.4th 1266, 1276 (9th Cir. 2021) (holding digital embodiment of copyrighted work must persist for more than a transitory duration to constitute an infringing “copy” and noting that “embodiments in a computer’s memory may perform some useful function despite being transitory. . . . But the

Copyright Act does not provide copyright owners the exclusive right to *use* their works.”); *Costar Group, Inc., v. Loopnet, Inc.*, 373 F.3d 544, 550-51 (4th Cir. 2004) (“While temporary electronic copies may be made in this transmission process, they would appear not to be ‘fixed’ in the sense that they are ‘of more than a transitory duration,’ and the ISP therefore would not be a ‘copier’ to make it directly liable under the Copyright Act.”).

Moreover, as the Register noted, even if any intermediate copies are embodied for a sufficiently long duration as to make them more than transitory, such intermediate copies made solely to facilitate an otherwise lawful purpose—especially a purpose that Congress has decided should be outside the scope of the copyright owner’s exclusive rights—are non-infringing fair use and therefore similarly do not require a license. *See, e.g., Sony Comput. Ent., Inc. v. Connectix Corp.*, 203 F.3d 596, 603-08 (9th Cir. 2000) (creation of intermediate copies of computer code solely for the lawful purpose of reverse engineering held to be fair use where end result of the use was not infringing); *Sega Enterp. Ltd. v. Accolade, Inc.*, 977 F.2d 1510, 1520-27 (9th Cir. 1992) (intermediate copies made for purpose of non-infringing use held to be fair use). Indeed, in the analogous state common-law copyright context applicable to pre-1972 sound recordings, courts have held that where no public performance right exists for such sound recordings—as is the case for all sound recordings transmitted by a BES—any server, cache, or other copies made to facilitate those transmissions are non-infringing:

The Supreme Court of Florida likewise foreclosed Flo & Eddie’s claim that Sirius infringed on its exclusive right of reproduction by creating back-up or buffer copies of Flo & Eddie’s recordings on its servers and satellites. The court held that even if Florida common law recognized an exclusive right of reproduction in pre-1972 sound recordings, Sirius did not infringe on that right by creating back-up or buffer copies for internal use. Thus, the district court properly granted summary judgment in favor of Sirius on both of Flo & Eddie’s copyright claims.

Flo & Eddie, Inc. v. Sirius XM Radio, Inc., 709 F. App'x. 661, 663 (11th Cir. 2018). *See also Flo & Eddie, Inc. v. Sirius XM Radio, Inc.*, 849 F.3d 14, 16-17 (2d Cir. 2017) (reversing district court's denial of summary judgment on copyright infringement claims for server copies and other reproductions of sound recordings on fair use grounds because they were made for the purpose of performances exempt from copyright).

That the CARP's most basic understanding of the need and value of the BES license was fundamentally flawed and led to the imposition of an absurdly high and unjustified nominal royalty rate provides yet another reason why the Judges should not look to any analysis, fact-finding, or other material from the CARP proceeding to interpret the current Gross Proceeds definition.

- C. Even if the CARP's flawed fact-finding and analysis were properly considered, they are not inconsistent with the plain meaning of the Gross Proceeds definition

As demonstrated above, SoundExchange's attempt to distract the Judges from the plain meaning of the text of the Gross Proceeds definition with arguments based upon the record and analysis in the twenty-year old CARP proceeding should be rejected because they are irrelevant and unreliable. But even were one to consider the findings and analysis from that proceeding, when properly viewed, they are not inconsistent with the plain meaning of Gross Proceeds.

- 1. The CARP did not hold that BES licensees must pay based upon revenue from transmissions where no ephemeral copies are made solely to facilitate those transmissions.

SoundExchange argues that the exclusion of revenues where no copies were made for the sole purpose of facilitating BES transmissions would be inconsistent with the CARP's adoption of a "blanket license" structure for the BES license and insinuates that the CARP somehow expressly rejected an argument that revenue generated from BES transmissions where only dual-use ephemeral copies were made can be excluded from the Gross Proceeds royalty pool. SX

Opening Br. at 28-31. SoundExchange is again wrong. As a preliminary matter, the “blanket license” structure for the BES license—like all section 114 and 112 licenses—is dictated by the Copyright Act itself, which established the ephemeral and performance licenses as broad limitations on the sound recording digital performance right when that exclusive right was first created. Moreover, there is nothing about a blanket license that is inconsistent with allowing deductions from the revenue pool to which a percent of revenue royalty rate is applied. As noted *supra*, p. 4, other section 112 and 114 licenses overseen by the Judges are “blanket licenses” and allow for various exclusions from their respective royalty pools. The same is true of licenses granted by the PROs, which routinely allow deductions from the royalty pool. *See, e.g., In re Petition of Pandora Media, Inc.*, 6 F. Supp. 3d 317, 326 & n. 17 (S.D.N.Y. 2014) (“The rate for Music Format Stations was set at 1.70% of all revenue, including revenue derived from new media uses... The agreement provided for a deduction of 12% for gross revenues from ‘Radio Broadcasting’ and a 25% deduction for gross revenues from ‘New Media Transmissions,’ subject to a cap.”), *aff’d*, 785 F.3d 73 (2d Cir. 2015).

Nor is it true that the CARP specifically considered and rejected any request to exclude revenues from BES transmissions where only dual-use ephemeral copies were made. In the sections of the CARP Report and Librarian’s Determination cited by SoundExchange, the CARP and Librarian rejected an argument made by DMX that they should set separate rates for what it was calling “cache” and “buffer” copies and set no rate for the copies in its “digital repository.” The CARP and Librarian rejected the argument that the rates and terms should set different rates in that manner, noting that the rates and terms needed to be generally applicable to all BES and should not be tailored to the specific technological and licensing choices made by DMX. *Web I Librarian’s Determination*, 67 Fed. Reg. 45,240, 45,263-64. In doing so, the Librarian

specifically noted that other BES should be free to set up their operations as they see fit, including in a way to minimize or eliminate entirely the use of the BES license. *Id.* at 45,264.

Moreover, the CARP could not possibly have foreclosed Music Choice’s reading of the Gross Proceeds definition because unlike Music Choice, DMX did not actually make any BES transmissions that did not require the use of server copies made solely for those transmissions. Although the copies in DMX’s digital repository were used for both on-premise and BES services, DMX’s BES service also required the use of server copies on 120 different playback servers that were used to program and transmit the channels *only* to the BES recipients. Talley Testimony at 8658:21-8660:12.

2. The plain language of the Gross Proceeds definition is not inconsistent with the CARP’s analysis of on-premise service benchmarks or the Librarian’s review and modification of the CARP’s Gross Proceeds definition

As noted above, the on-premise benchmarks used by the CARP were unreliable, non-comparable, and included vastly different rights. They are also ancient, and not in the record before the Judges in this proceeding, so they can hardly be used to alter the plain meaning of the Gross Proceeds definition. But SoundExchange points to no specific term in them that is inconsistent with that plain meaning. Indeed, there would be no reason for these old licenses for on-premise services to deal with the specific issue raised in this proceeding, because, as demonstrated above, the only on-premise service provider that was also providing a BES—DMX—did not have any revenue from BES transmissions where only dual-use ephemeral copies were made. Nor is it true that these benchmarks required the on-premise service providers to pay royalties based on all revenues—as SoundExchange claims. SoundExchange misleadingly quotes a portion of DMX testimony discussing the benchmark royalty pools as being “gross revenue of music sales.” SX Opening Br. at 32. SoundExchange deceptively left out the rest of Mr. Knittel’s

testimony on that point, which made clear that there were a variety of deductions from those revenues allowed in the benchmark agreements, including deduction of all PRO and mechanical license payments. Knittel Testimony at 8384:4-14 (“that amount is reduced by other royalties, ASCAP, BMI, SESAC, Harry Fox, et cetera.”). Thus, even the fatally flawed benchmark agreements allowed for various deductions from Gross Revenue.

Nor did the Librarian decide the issue before the Judges when he modified the Gross Proceeds definition on review of the CARP Report. SoundExchange focuses on the Librarian’s decision that the Gross Proceeds definition needed clarification to make clear that “in kind” payments were included within Gross Proceeds, and therefore added “including those made in kind” to the description of “fees and payments” included in Gross Proceeds. *Web I Librarian’s Determination*, 67 Fed. Reg. at 45,268. This has nothing to do with the question presented in this referral. SoundExchange’s non sequitur argument that this somehow demonstrates that the Librarian did not intend to allow any deductions from BES revenue in the Gross Proceeds definition is belied by the Librarian’s own explanation of that definition. One of the very reasons he created the Gross Proceeds definition as a separate provision was in rejection of RIAA’s proposed definition that included revenue from equipment rental, maintenance service, advertising, and revenues “from any source in connection with the licensee’s [BES].” *Id.* The Librarian credited Mr. Knittel’s testimony—quoted above—in which he described the benchmark agreements’ revenue pool, including various deductions, and noted that the Gross Proceeds revenue pool concept in those agreements was sufficiently understood not to include all revenue as RIAA requested. None of this is inconsistent with excluding from Gross Proceeds revenue derived from BES transmissions where no ephemeral copies are made solely to facilitate those transmissions.

CONCLUSION

For the foregoing reasons, and for those detailed in Music Choice's Opening Brief, the Judges should confirm Music Choice's interpretation of the definition of Gross Proceeds.

Dated: June 6, 2022

Respectfully submitted,

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Proof of Delivery

I hereby certify that on Monday, June 06, 2022, I provided a true and correct copy of the Music Choice's Reply Brief Re: BES Gross Proceeds Referral to the following:

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Sirius Satellite Radio, represented by Matthew J. Astle, served via US Mail

XM Satellite Radio Inc., represented by R. Bruce Rich, served via US Mail

Signed: /s/ Paul Fakler