

UNITED STATES COPYRIGHT ROYALTY JUDGES
The Library of Congress

In re

**DETERMINATION OF ROYALTY RATES AND
TERMS FOR MAKING AND DISTRIBUTING
PHONORECORDS (Phonorecords III)**

**Docket No. 16-CRB-0003-PR
(2018–2022) (Remand)**

**DISSENT IN PART AS TO SECTION IV OF THE INITIAL RULING AND ORDER
AFTER REMAND BY JUDGE DAVID R. STRICKLER¹**

I. The Contours of this Partial Dissent

I respectfully Dissent from Section IV of the Initial Ruling and Order after Remand (Initial Ruling). As explained herein, I conclude that the D.C. Circuit’s rulings in *Johnson* preclude the Judges from engaging in “new “agency action.””² See *Johnson v. Copyright Royalty Board*, 969 F.3d 363, 386 (D.C. Cir. 2020). Accordingly, I cannot join with the present Majority in its determination that this remand proceeding constitutes “new ‘agency action’” consistent with *Johnson*. That argument is circular and renders useless the D.C. Circuit’s careful analysis of the procedures that are and are not available to the Judges after they have issued their Initial Determination.

As further explained herein, the argument is *circular* because it begins with the D.C. Circuit’s ruling that the Determination³ was improper because it invented a new procedure to

¹ I am concurring in the Majority’s *substantive* re-adoption of the Bundled Service Revenue definition from the Initial Determination. As explained herein, I disagree with the Majority regarding the *procedural* manner in which the Judges may reach this result. Thus, it would be more accurate to describe this “Dissent” as a “Concurring Opinion”, or an “Opinion Concurring in Part and Dissenting in Part.” However, the Copyright Act does not expressly authorize Judges to issue a “concurring opinion,” but rather references the issuance of a “dissenting opinion.” See 17 U.S.C. § 803(a)(3). Accordingly, I identify this opinion as a “Dissent in Part as to Section IV of the Initial Ruling and Order after Remand.”

² I place the phrase *agency action* within quotation marks inside the broader phrase *new agency action* to avoid potential ambiguity and inconsistency with the directives in *Johnson*. There, the D.C. Circuit held that the Judges cannot assert “plenary authority to revise [their] determinations whenever [they] thought appropriate,” because such a power grab would render “a nullity ... the lines drawn by the authorizing statute ... to confine ... post hoc amendments” to statutorily identified circumstances.” *Johnson* at 392. So, “new” means the new application of an *existing* statutorily available “agency action” that had not previously been invoked—not “new” in the sense of a form of action conjured up to meet the moment. (When this phrase is used in a quotation I do not use the double quotation marks.) This distinction is important because the Majority and Copyright Owners advance new *forms* of (extra-statutory) agency action, not merely new applications of statutorily-authorized agency actions.

³ *Determination of Royalty Rates and Terms for Making and Distributing Phonorecords (Phonorecords III)*, 84 Fed. Reg. 1918 (Copyright Royalty Board Feb. 5, 2019) (final rule and order) (“Determination”); See also Final Determination, 16-CRB-0003-PR (2018-2022) (Nov. 5, 2018) (citations to the Determination and to the Dissent in this Dissent in Part are found in this document). The Dissent is appended to and part of the same document as the Determination.

change the Bundled Revenue definition that was in the Initial Determination⁴, only to circle back to where it started by creating—through the D.C. Circuit’s own remand no less—a further and extra-statutory “new ‘agency action’”.

The Majority also renders Johnson *useless*, by adopting a process by which—after the D.C. Circuit has remanded an issue because the Judges lacked procedural authority to rule—the procedural error is essentially honored in the breach, because the remand neuters the effect of the D.C. Circuit’s ruling.⁵

I join with the Majority though on its *substantive* decision to re-adopt the definition of Bundled Revenue set forth in the Initial Determination. As explained *infra*, I too find that it is clearly preferable to the definition that was swapped into the (Final) Determination. But as explained herein, I reconcile the procedural and substantive points differently. I apply what I believe to be the proper understanding of the D.C. Circuit’s ruling—finding, contrary to the Majority, no avenue for “new ‘agency action’” post-remand. Rather, the Judges must *revert* to the original – and substantively appropriate – definition of Bundled Revenue in the Initial Determination.

To explicate the bases of this Dissent, my opinion as to this issue is set forth below.

II. Introduction

The Majority and I analyze the definition of “Service Revenue” from “Bundled Offerings” (henceforth “Bundled Revenue” definition) in the context of our partial adoption of the PR II-based benchmark. As discussed *supra*, the Remand Majority found that the PR II-based benchmark is a useful benchmark, particularly because of its features that incentivize beneficial downstream price discrimination and generate more listeners, revenues, and royalties. As explained below, the Bundled Revenue definition—itsself an element within the PR II-based benchmark—also embodies such price discriminatory incentives. Thus, the Judges’ analysis of the PR II-based benchmark and the Bundled Revenue definition are connected.

In the Determination, the earlier Majority likewise found the issues relating to the PR II-based benchmark to be bound-up with the question of the appropriate Bundled Revenue definition. But because that earlier Majority *rejected* the PR II-based benchmark, it likewise rejected the Bundled Revenue definition contained in the Initial Determination. The definition in the Determination thus eliminated the royalty-based incentive to engage in price discrimination via bundling.

In the interregnum between the Initial Determination and the (Final) Determination, the Judges considered Copyright Owners’ post-hearing motion which sought, *inter alia*, to strike the Bundled Revenue definition in the Initial Determination. The Majority agreed with Copyright Owners that the definition in the Initial Determination should be replaced. An important rationale—highly relevant in the present context—was as follows: “The Judges have ... declined to rely on the 2012 ... benchmark ... as the basis for the rate structure, or, therefore, as

⁴ Initial Determination, 16-CRB-0003-PR (2018-2022) (Jan. 27, 2018).

⁵ The Initial Ruling suggests that the Judges *could* have utilized a “further explanation” for the switched Bundled Revenue definition, as opposed to using “new ‘agency action.’” I do not dissent from that general point. However, even though the Majority did not utilize this alternative approach on remand, I dissent to the extent that section could be read to allow a fuller explanation that would conflict with *Johnson*.

regulatory guidance.” Amended Order Granting in Part and Denying in Part Motions for Rehearing at 17 (Jan. 4, 2019) (Clarification Order).⁶

Unlike in the Determination, in this Initial Remand Ruling the Judges *do* rely on the PR II-based benchmark in part because of its price discriminatory aspects. More particularly, because the bundling of interactive services also constitutes a form of price discrimination, the Judges find the PR II-based benchmark definition of Bundled Revenue set forth in the Initial Determination to be substantively reasonable and otherwise consistent with the four itemized factors in section 801(b)(1).

As a *procedural* matter though, I can neither: (1) offer any further or fuller explanation for why the Majority made this change in the Bundled Revenue definition nor (2) identify any “new ‘agency action’” that would permit this definitional switch. And contrary to present Majority on remand, I also cannot identify a “new ‘agency action’” that the Judges can now take to return to the definition in the Initial Determination. But, as explained *infra*, the Judges need not identify such action, because the absence of a justification for the definitional switch requires the Judges to *revert back* to the definition in the Initial Determination.

As a *substantive* matter though, the Judges unanimously agree to replace the post-hearing definition of Bundled Revenue in the Determination and reinstate the definition set forth in the Initial Determination.

III. Background

In this remand proceeding, the parties propose two starkly different definitions of Bundled Revenue. Each has a dramatically different impact on the use of the royalty structure and levels to incentivize price discrimination in the downstream market.

The Services argue in favor of the language contained in the Initial Determination, *i.e.*, in their PR II-based benchmark, which defines Bundled Revenue, in pertinent part, as

the revenue recognized from End Users [*i.e.*, consumers] for the Bundle less the standalone published price for End users for each of the other component(s) of the Bundle

Initial Determination, Attachment A at 7 (section 382.2 therein).

By contrast, Copyright Owners support the Majority’s substituted language contained in the Determination, which defines Bundled Revenue, in pertinent part, as

the lesser of the revenue recognized from End Users [*i.e.*, consumers] for the bundle and the aggregate standalone published prices for End Users for each of the component(s) of the bundle that are License Activities

⁶ This January 4, 2019 Order was issued in response to two motions; the Services’ “Joint Motion for Rehearing to Clarify the Regulations” and Copyright Owners’ “Motion for Clarification or Correction of Typographical Errors and Certain Regulatory Terms.” As explained *infra*, Copyright Owners did not style their motion as a “rehearing” motion and expressly declined to argue that their motion met the statutory and regulatory requisites for rehearing. This remand issue pertains only to the post-hearing switch in the Bundled Revenue definition sought and obtained by Copyright Owners via their motion. Accordingly, it is clearer to refer herein to the Judges’ January 4, 2019 Order as the “Clarification Order,” rather than as a “Rehearing Order,” because the semantic distinction carries substantive overtones. (I had dissented from the Initial Determination and the Determination, and thus did not join in the Clarification Order.)

Determination, Attachment A at 8 (section 382.2 therein).

In *Johnson*, the D.C. Circuit succinctly summarized these conflicting definitions as follows:

In its Initial Determination, the [Judges] directed that the revenue from streaming services that are included in bundled offerings would generally be measured by the value remaining after subtracting the prices attributable to the other products in the bundle.

When the Copyright Owners objected to the substance of that definition in their motion for “clarification,” the Board adopted an entirely new definition of Service Revenue for bundled offerings. ... This new definition generally measured the value of the streaming component of a bundle as the standalone price of the streaming component.

Johnson at 389.⁷

In the Clarification Order, the Judges succinctly summarized the parties’ respective positions. *Id.* at 17. They noted that Copyright Owners had presented evidence that the PR II-based benchmark definition contained in the Initial Determination “led *in some cases* to an inappropriately low revenue base,” although the Judges “agree that there is *no support for any sweeping inference that cross-selling has diminished the revenue base.*” *Id.* at 17, 21 (emphasis added). The Judges further noted the Services’ assertion that the Bundled Revenue definition in the Initial Determination is consistent with the Judges’ “endorsement of the classic price discrimination enabled by bundling strategies.” *Id.*⁸

The Majority resolved this issue in the Clarification Order in favor of Copyright Owners. Specifically, the Majority found that, because of the “indeterminacy problem”⁹ inherent in bundling, “the Services—not the Copyright Owners – ... are in a position to provide evidence of how they price bundles and value the component parts thereof.” *Id.* at 17-18. However, according to the Majority, although the Services “bore the burden of providing evidence concerning the proper economic allocation of bundled revenue,” they “failed to do so,” and “[b]y default ... the Judges must adopt an approach to valuing bundled revenue that is in line with what the Copyright Owners have proposed.” *Id.* at 18.

IV. The Rulings in *Johnson* Regarding the Bundled Revenue Definition

⁷ As explained *infra* (including by way of an example), the Bundled Revenue definition in the Initial Determination aligns with and incentivizes price discrimination in the downstream market, but the definition in the Determination does not.

⁸ The parties’ substantive arguments are discussed in more detail *infra*.

⁹ The “economic indeterminacy arises when “the input supplier ... is paid as a percent of retail revenue, and the bundled revenue consists of some revenue attributable to the royalty base and other revenue excluded from the royalty base, the economic indeterminacy of the revenue attributable to each bucket creates a measurement problem, absent further information regarding the WTP [Willingness-to-Pay] of buyers/subscribers to the bundle.” *SDARS III*, 83 Fed. Reg. at 65264. As explained *infra*, the PR II-based benchmark addresses this informational uncertainty with the parties’ negotiated alternative rate prongs and floors that guarantee royalties are paid, whereas the definition in the Determination eliminated the alignment of royalties to price discriminatory bundles designed to increase downstream access to musical works.

The Services appealed the Majority’s abandonment of the Bundled Revenue definition in their Initial Determination. Their appeal “challenge[s] both the legal authority and the substantive soundness” of this switch.

First, the Services argued that the Majority failed to identify and explain the *procedural* basis for making the switch after the hearing had concluded. Second, the Services argued that, *substantively*, the replacement definition in the Determination “was arbitrary, capricious, or unsupported by substantial evidence.” *Johnson* at 389, 392.

The D.C. Circuit agreed with the Services regarding the *procedural* issue and therefore vacated and remanded that aspect of the Bundled Revenue definitional switch. In light of its procedural ruling, the D.C. Circuit explicitly declined to rule on the Services’ *substantive* argument relating to the definitional switch. *Id.* at 392. (“Because the Board failed to explain the legal authority for its late-breaking rewrite, we vacate and remand that aspect of the decision [and] we have no occasion to address the Streaming Services’ separate argument that the definition was arbitrary, capricious, or unsupported by substantial evidence.”).

The D.C. Circuit’s rulings in *Johnson* pertaining to this Bundled Revenue Definition were clearly articulated. The D.C. Circuit found that the Majority “failed to explain under what authority” it made a material change to the definition “so late in the game.” *Johnson* at 389, 392. The D.C. Circuit noted that the Judges expressly declined to treat the Clarification Motion as a motion for rehearing; consequently, the motion did not request and the Judges did not reconsider either evidence or legal argument. *Id.* at 390. Although appellate counsel offered rationales, the D.C. Circuit rejected counsel’s *post hoc* reasoning. *Id.* and 391-92. Ultimately, the D.C. Circuit remanded the adopted regulation “either to provide ‘a fuller explanation of the [Judges’] reasoning at the time of the agency action[,] or to take ‘new agency action’ accompanied by the appropriate procedures.” *Id.* at 392, citing *Dep’t of Homeland Sec. v. Regents of Univ. of Cal.* 140 S.Ct. 1891, 1908 (2020).

To be precise, I take note of the following specific rulings in *Johnson*:

1. “The problem is that the [Majority] has completely failed to explain under what authority it was able to materially rework that definition so late in the game.” *Id.* at 389.
2. “The [Majority] did not treat Copyright Owners’ motion to have the definition changed as a motion for rehearing ... [because] Copyright Owners’ motion did not request a literal rehearing of evidence or legal argument.” *Id.* at 390 (cleaned up).
3. “The [Majority] nowhere in its order or the [] Determination explains the source of its power to make “fundamental” changes under the authorizing statute” *Id.* at 392. [same as #1]
4. “[I]t should go without saying that we may not sustain the Board's action based on its attorney's theorizing at oral argument ... vacillating gestures to uninvoked authority will not do.” *Id.* at 391-92 (the D.C. Circuit alluding to its rejection of arguments also

made only by appellate counsel in support of the Majority’s rejection of the PR II-based benchmark earlier in the decision).¹⁰

“We must vacate the [] Determination’s bundled offering Service Revenue definition and remand for the [CRB Judges] either to provide ‘fuller explanation of the agency’s reasoning at the time of the agency action[,]’ or to take ‘new agency action’ accompanied by the appropriate procedures.” *Id.* at 392.

V. Remand Procedure Regarding Bundled Revenue Definition

Post-remand, the Judges stated their understanding, as well as the parties’ understanding, of the issue on remand with respect to the Bundled Revenue definition:

The Services and Copyright Owners agree that the proceedings on remand should be limited to three issues: * * * [3] the adoption of a revised definition of “service revenue” for bundled offerings between issuing their Initial Determination and [their] Determination.

Order Regarding Proceedings on Remand at 1 (Dec. 15, 2020) (Remand Order).

The parties proposed, and the Judges agreed, that the record would not be re-opened with regard to the Bundled Revenue definitional issue. Rather, the Remand Order permitted the parties only to provide further briefing on this matter. *Id.* Specifically, the Judges subsequently permitted each party to file simultaneous Initial Remand Submissions and simultaneous Reply Remand Submissions. *See* Order Adopting Schedule for Proceedings on Remand (Dec. 20, 2020). Thereafter, seeking further analysis on the question of “new agency action,” the Judges solicited, and received, further briefing on this issue. *See* Notice and *Sua Sponte* Order Directing the Parties to Provide Additional Materials (Dec. 9, 2021) (Feb. 9, 2021); *Sua Sponte* Order Regarding Additional Briefing (Feb. 9, 2021).

VI. The Parties’ Submissions Regarding Bundled Revenue Definition

In their respective briefing, Copyright Owners and the Services made arguments relating to: (1) the *procedural* issue, *i.e.*, the Judges’ authority, *vel non*, to switch to a new Bundled Revenue definition in the Determination; and (2) the *substantive* issue, *i.e.*, the relative merits of the two conflicting Bundled Revenue definitions. *See* Initial Remand Submission of Copyright Owners at 7-10 (Apr. 1, 2021) (CO Initial Submission); Services’ Joint Opening Brief (in Services’ Joint Written Direct Remand Submission at Tab D) at 64-76 (Apr. 1, 2021) (Services’ Initial Submission); Copyright Owners’ Reply Brief on Remand (in Reply Remand Submission of Copyright Owners, Vol. 1) at 64-88 (CO Reply); Services’ Joint Reply Brief at 52-63 (Services’ Reply).

A. The Procedural Issue

1. Copyright Owners’ Arguments

Copyright Owners assert first that the Judges can preserve their post-hearing switch of the Bundled Revenue definition by sidestepping the D.C. Circuit’s holding and rationale

¹⁰ Going beyond the Majority’s actual rulings, the CRB Judges’ appellate counsel argued that the Majority’s authority for this definitional switch fell under either or both of the “inherent” statutory powers of the Judges or their “rehearing power.” *Id.* at 392. (The D.C. Circuit rejecting appellate counsel’s argument that it was unnecessary “for this Court to address which one it is because ... it could properly be understood as both.”).

in *Johnson*. That is, Copyright Owners maintain that this remand proceeding itself constitutes the necessary form of “new ‘agency action’” that *Johnson* invites, while also liberating the Judges from the consequences of the procedural infirmities identified by the D.C. Circuit. More particularly, Copyright Owners argue:

[T]he new agency action here is a determination after remand proceedings[.] [T]he [Judges are] largely free to chart [their] own procedural course, and [they] ha[ve] done so in [their] [Remand] Order. The [Judges are] not required to undertake any of the procedural steps set forth in 17 U.S.C. § 803(b) in order to take such “new agency action.” See 17 U.S.C. § 803(d)(3) (requiring only that on remand further proceedings be taken “in accordance with subsection (a)”); 37 C.F.R. § 351.15; *Intercollegiate Broad. Sys., Inc.*, 796 F.3d at 125 (“[N]either the Copyright Act nor the [Judge’s] regulations prescribe any particular procedures on remand.”) The Circuit’s instruction that the action be “accompanied by the appropriate procedures[.]” *Johnson*, 969 F.3d at 392, does not dictate what those “appropriate procedures” must be but instead plainly refers to these flexible rules. See also *Oceana, Inc.*, 321 F. Supp. 3d at 136 (explaining that when remanding to an agency, a court generally “may not dictate to the agency the methods, procedures, or time dimension, for its reconsideration”).

CO Initial Submission at 71 n.33.

Copyright Owners reject the Services’ position that the asserted procedural error is an “absence of authority” that can never be cured. *Id.* at 74 (citing Services’ Proposal for Remand Proceedings at 10). They note that the D.C. Circuit did not say the Judges lacked the authority to revisit the service revenue definition from bundles on remand. Nor, they observe, did it say the Judges have no authority to review the record evidence and the parties’ arguments and reach the same conclusion or a different conclusion on remand.

Copyright Owners further opine that if the only possible outcome were for the Judges to reinstate a definition that lacked any explanation or evidentiary support solely because it was present in the Initial Determination, then the D.C. Circuit would not have remanded the issue but would have simply reversed and reinstated the Initial Determination definition. But instead, they note, the D.C. Circuit remanded and said the Judges could take “new agency action” precisely to cure the asserted procedural defect. Copyright Owners assert that the remand allowed the parties to present the record evidence and their arguments so that the Judges can address the definition “afresh” in the remand determination. *Id.* at 74.

Further, Copyright Owners argue that 17 U.S.C. § 803(d)(3) states only that proceedings on remand must be in accordance with 17 U.S.C. § 803(a). They contend that remand proceedings need not be confined to procedures the Services claim are too late in the game for the Judges to follow, again relying on the holding in *Intercollegiate Broad. Sys., supra*, that “neither the Copyright Act nor the Board’s regulations prescribe any particular procedures on remand.” *Id.* at 125. Accordingly, they argue, the Judges can reaffirm the adopted bundled service revenue definition following their review of the parties’ submissions without invoking section 803(c)(2) or 803(c)(4) that were ruled inapplicable in *Johnson*. CO Reply at 65-66.

Also, Copyright Owners argue that the Judges may properly justify the changed definition under section 803(c) as a fuller explanation of the agency’s reasoning at the time it was made. They urge that the Judges could explain that, especially in light of the evidence of

how (in Copyright Owners' characterization) the Services misused the prior definition to make service revenue completely disappear, the Judges carry-over of the prior Bundled Revenue definition from *Phonorecords II* into the Initial Determination was unintended and inadvertent.¹¹ CO Reply at 69.

Copyright Owners also assert that, on remand, the Judges could explain that Copyright Owners had, in their Motion for Clarification, identified an "exceptional case" under section 803(c)(2) because the prior definition failed to comport with Judges' precedent and economic principles, and was unsupported by evidence. In addition, the Judges reheard the evidence and legal arguments as presented in the parties' briefs on the issue and, as a result, chose to adopt the revised definition. Copyright Owners maintain that for the Judges to do so would not be impermissible *post-hoc* reasoning. They note that the D.C. Circuit remanded precisely because the Judges did not provide any reason in the Determination for revising the Bundled Revenue definition. Copyright Owners note that it was the Services, not Copyright Owners, who appealed the Judges' modification of the bundled service revenue definition; thus, Copyright Owners cannot be penalized for not making every possible argument for affirmance. CO Reply at 70.

Further, and again notwithstanding the holding in *Johnson*, Copyright Owners argue that the Judges have the authority to engage in new agency action in this remand proceeding through a recasting of the Motion for Clarification as a motion for rehearing, pursuant to 17 U.S.C. § 803(c)(2)(A) and 37 C.F.R. § 353.1. In this regard, Copyright Owners dismiss the point, raised by the D.C. Circuit, that their Motion for Clarification could not be recast as a motion for rehearing because Copyright Owners had explicitly disavowed that their motion sought rehearing under the statute, and that the Judges agreed. Rather, Copyright Owners maintain that the foregoing is not the same as a finding that the standard could not have been met. In Copyright Owners' view, the Judges could revisit on remand the question of whether the rehearing standard has now been met, and find that Copyright Owners have satisfied the "exceptional case" standard for granting rehearing motions under section 803(c)(2).¹² Copyright Owners add that if the Judges do engage in new agency action that reconsiders the Motion for Clarification as a motion for rehearing, the Judges should fully explain their reasoning. *Id.* at 8-10.

However, Copyright Owners urge that proceeding in that fashion would add an entirely unnecessary and complicating step. They again suggest that there is no need to reconsider or

¹¹ Copyright Owners assert that the definition in the Initial Determination conflicted with the CRB Judges' finding in the Initial Determination that the adopted rates and terms would afford Copyright Owners a fair return for their creative works, thereby satisfying Factor B of the 801(b) standard. Thus, they maintain that the definitional switch was necessary so as to not "frustrate the proper implementation of" the Determination. CO Reply at 69 (*citing* 17 U.S.C. §§ 801(b) and 803(c)(4)).

¹² The Majority set forth the rehearing standard in the *Clarification Order*:

According to the Copyright Act, the Judges may grant a motion for rehearing in exceptional circumstances, provided the moving party shows that an aspect of the determination is "erroneous." *See* 17 U.S.C. 803(c)(2); 37 C.F.R. § 353.1. The moving participant must identify the aspects of the determination that it asserts are "without evidentiary support in the record or contrary to legal requirements." 37 C.F.R. § 353.2. In general, the Judges grant rehearing only "when (1) there has been an intervening change in controlling law; (2) new evidence is available; or (3) there is a need to correct a clear error or prevent manifest injustice." *See, e.g.,* Order Denying Motion for Reh'g at 1, Docket No. 2006-1 CRB DSTRA (Jan. 8, 2008) (*SDARS I* Rehearing Order) (applying federal district court standard under Fed. R. Civ. P. 59(e)).

Clarification Order at 2, n.3.

recharacterize the Motion for Clarification as a motion for rehearing because the remand itself affords the opportunity for the Judges to take new agency action, which, as in a rehearing, permits them to reconsider evidence and arguments, but, unlike a rehearing, is not limited by the constraints of section 803(c)(2). *See* Copyright Owners’ ... Additional Briefing on New Agency Action ... Question, etc., Tab B at 7-8 (Feb. 24, 2021).

2. The Services’ Arguments

The Services’ arguments are based on the reasoning of the D.C. Circuit in *Johnson*. Specifically, they assert that the D.C. Circuit found only “three ways in which the [Judges] can revise Initial Determinations” via “new agency action,” and the Judges failed to establish that the change to the service revenue definition fit any of those three categories. Services’ Initial Submission at 64-65 (citing *Johnson* at 390).¹³

According to the Services, the first statutory way the Judges may revise an Initial Determination is to “order rehearing ‘in exceptional cases’ in response to a party’s motion, 17 U.S.C. § 803(c)(2)(A).” Services’ Initial Submission at 65 (citing *Johnson* at 390). The Services argue that the D.C. Circuit held in *Johnson* that the Judges’ “material revision of the ‘[Bundled] Revenue’ definition ... does not fall within the [Judges’] rehearing authority under section 803(c)(2)(A)” because “the [Judges] [themselves] . . . w[ere] explicit that [they] ‘did not treat the [Copyright Owners’] motion[]’ ... ‘as [a] motion[] for rehearing under 17 U.S.C. § 803(c)(2).’” *Id.* The D.C. Circuit also noted that “as the [Judges] found, ... Copyright Owners’ motion did ‘not meet [the] exceptional standard for granting rehearing motions’ under section 803(c)(2).” *Id.* (citing *Johnson* at 390). The Services assert, quoting *Johnson* once more, that the Judges were not able to make “a volte-face” and justify on appeal their revision to the definition as an exercise of rehearing authority. As the D.C. Circuit held, agency action must be justified by “reasons invoked by the agency at the time it took the challenged action,” and post-hoc rationalizations are insufficient. *Id.* (citing *Johnson* at 390).

The Services add their view that the Judges cannot revisit the decision to deny rehearing without engaging in impermissible *post-hoc* reasoning. They note the Supreme Court has explained that, while an agency may “elaborate later” on its “initial explanation” of the reason (or reasons) for its action, it “may not provide new ones.” Services’ Initial Submission at 66, citing *e.g.*, *Regents at 1908*. The Services offer that the Judges, having stated that they did not consider the Copyright Owners’ motion to revise the definition to be a motion for rehearing, cannot now conclude that the motion qualified as one for rehearing and that the Judges in fact engaged in rehearing. *Id.*¹⁴

The Services next argue, relatedly, that the Judges cannot simply recast the Services Motion for Clarification as a rehearing motion in an attempt to satisfy the rehearing standard. In this regard, they maintain that Copyright Owners did not argue before the Judges or the D.C. Circuit that their Motion for Clarification satisfied the “exceptional cases” standard, and have therefore waived that argument. *Id.*

¹³ The Services acknowledge that the Judges could alternatively have attempted to provide on remand a fuller explanation of their prior reasoning (in lieu of engaging in “new ‘agency action’”). That issue is considered *infra*.

¹⁴ In fact, the issue of whether to characterize Copyright Owners’ Motion for Clarification as a motion for rehearing is not one raised by Copyright Owners, but rather by the Judges *sua sponte*.

The Services assert that the second statutory way the Judges may revise an Initial Determination, *viz.* taking “new agency action” to correct a technical or clerical error under section 803(c)(4), cannot be used to justify the modification of the Bundled Revenue definition in the Initial Determination. The Services note that the D.C. Circuit held specifically that the Judges’ change in the Bundled Revenue definition could not be construed as correcting a technical or clerical error because it involved a substantive rewrite of the Service revenue definition. *Id.* at 67 (citing *Johnson* at 391).

The Services argue that the third and final statutory justification for the Judges to engage in “new agency action” is to revise the terms in an Initial Determination is in response to “unforeseen circumstances” that would frustrate the proper implementation of the determination. *Id.* at 67. The Services note that the D.C. Circuit held in *Johnson* that this authority did not justify the Judges’ change to the Bundled Revenue definition because the Judges did not invoke this authority and “the need to ground the original definition in the record” could not credibly be described as “an unforeseen circumstance.” *Id.* (citing *Johnson* at 391).

The Services also note that the D.C. Circuit rejected the argument that the Judges have an “inherent authority” – unmentioned in the statute – to make changes to the Initial Determination. The D.C. Circuit explained that the specific restrictions Congress placed on the [Judges’] authority in section 803 “would be a nullity if [they] also had plenary authority to revise [their] determinations whenever [they] thought appropriate.” *Id.* (citing *Johnson* at 391-92). The Services add that even if the Judges offered a new source of authority capable of justifying substantive changes to the [Bundled] Revenue definition now, the Judges would be unable to rely on this “uninvoked authority” without engaging in impermissible *post-hoc* reasoning. *Id.*

The Services also reject Copyright Owners’ position that the Judges may sidestep the D.C. Circuit’s ruling by issuing a new determination on remand and simply arguing that *any* ruling after remand qualifies as new agency action pursuant to *Johnson*. The Services argue that failure to address the legal and factual issues on which the court remanded would violate the D.C. Circuit’s decision and would result in yet another remand. The Services emphasize that the issue of authority to make the changes to the Initial Determination are especially important in this context, because the D.C. Circuit recognized that the Copyright Act places limits on the Judges’ authority to alter an initial determination by defining conditions for rehearing and the types of changes that are permitted absent a rehearing. In this regard, the Services maintain that the Judges cannot do on remand what they lacked authority to do in the first instance. The Services assert that the Judges must resolve the legal question of whether authority exists to alter the revenue definition in the Initial Determination. Services’ Reply at 52-54.¹⁵

The Services also take note of the alternative path available to the Judges: to provide a “fuller explanation” of the prior conclusion that the Judges had legal authority to revise the Service Revenue definition. The Services maintain that if the Judges pursue the “fuller explanation” path, the Judges are limited to elaborating on what they said previously, and that they cannot add new reasons they did not initially provide. *Id.* at 54-55; *see also* Services’ Joint Rebuttal Brief Addressing the Judges’ Working Proposal at 38-42 (Feb. 24, 2022) (“Services’ Additional Submission”).

¹⁵ In The Services agree that this remand proceeding qualifies as a “new agency action” but do not maintain that a ruling on remand that is inconsistent with *Johnson* would be the type of “new ‘agency action’” that *Johnson* permits. *See* Services Additional Submission at 38-42.

The Services address Copyright Owners’ position that if the only possible outcome were for the Judges to reinstate a definition that lacked any explanation or evidentiary support solely because it was present in the Initial Determination, then the D.C. Circuit would not have remanded the issue but would have simply reversed and reinstated the Initial Determination definition. The Services urge that the D.C. Circuit could not reverse because the CRB’s appellate counsel had raised—for the first time on appeal—new justifications for the Judges’ decision to change the Initial Determination. Instead, the Services maintain, the D.C. Circuit had to remand and give the Judges the opportunity to address appellate counsel’s new justifications in the first instance, as the D.C. Circuit could not rule them out given the posture of the appeal. Services’ Reply at 56.

VII. Analysis and Decision

A. The Procedural Issue: Is there “New Agency Action” Available to the Judges?

Having considered the parties’ arguments, I conclude that the rulings in *Johnson*, which clearly rejected all of the Majority’s procedural arguments seeking to justify their switch in the Bundled Revenue definition, foreclose any avenue for procedurally justifying this definitional switch. More particularly, I conclude that none of the procedural avenues proffered by Copyright Owners would constitute “new ‘agency action’” consonant with the holdings in *Johnson*. Further, I cannot identify any other procedural device (*i.e.*, an extra-statutory form of agency action) that would permit the switched definition in a manner consistent with *Johnson*.¹⁶ In addition, I cannot identify any further or fuller explanation that might support the Majority’s procedural reasoning for swapping out the Bundled Revenue definition in the Initial Determination and substituting the definition in the Determination.

In reaching this conclusion, I take note of the following specific language in *Johnson*:

Section 803 identifies three ways in which the Board can revise Initial Determinations. It can (i) order rehearing “in exceptional cases” in response to a party’s motion; (ii) correct “technical or clerical errors,”; and (iii) “modify the terms, but not the rates” of a royalty payment, “in response to unforeseen circumstances that would frustrate the proper implementation of [the] determination.”

Johnson at 390 (citations omitted). After identifying these three alternatives, the D.C. Circuit concluded that the CRB Judges “rollout of an entirely new manner for calculating the streaming service revenue from bundled offerings fit none of those categories.” *Id.*

First, I consider whether in the present case they can engage in “new ‘agency action’” pursuant to 17 U.S.C. § 803(c)(2)(A) by recasting Copyright Owners’ Motion for Clarification as a Motion for Rehearing. I conclude that this avenue has been unambiguously cut-off by *Johnson* and, indeed (as noted in *Johnson*), by the Judges’ own prior ruling:

¹⁶In this section, Copyright Owners’ arguments regarding recasting their Motion for Clarification as a request for rehearing, a correction for technical or clerical errors, or for unforeseen circumstances would constitute a new application of an *existing* “form of agency action” that the D.C. Circuit had rejected. But Copyright Owners’ argument in favor of the Judges’ supposed “inherent authority” to enlarge their post-hearing jurisdiction is an argument creating a *new form* of agency action, not an argument in favor of new application of an existing form of authority. Likewise, the next approach proffered by Copyright Owners, *i.e.* construing the remand itself as generating the requisite agency action, which is also the Majority’s approach, is an example of an agency action that is not statutorily specified and, as explained *infra*, is inconsistent with section 803(a).

The [CRB Judges’] material revision of the Bundled Revenue definition ... does not fall within [their] rehearing authority under Section 803(c)(2)(A). We have that on no less an authority than the [CRB Judges themselves], [who were] explicit that [they] “did not treat the Copyright Owners’ motion” to have the definition changed “as a motion] for rehearing under 17 U.S.C. § 803(c)(2). That is because the Copyright Owners’ motion did not “request[] a literal rehearing of evidence or legal argument.”

Nor could they have because, as the [CRB Judges] found, the Copyright Owners’ motion did “not meet [the] exceptional standard for granting rehearing motions” under Section 803(c)(2). ... [The CRB Judges] explain[ed] that ... Copyright Owners “failed to make even a *prima facie* case for rehearing under the [rehearing] standard”.

Johnson, 369 F.3d at 390.

Further cutting off this “rehearing” approach, *Johnson* also expressly holds that it is a “forceful” principle that the D.C. Circuit “cannot sustain action on grounds that the agency itself specifically disavowed. *Id.* Moreover, in this Initial Remand Ruling I echo the Majority’s ruling in the Clarification Order that Copyright Owners had failed to present “even a *prima facie* case for rehearing under the applicable standard”. Clarification Order at 2.¹⁷

Next, I consider whether the Judges can engage in “new ‘agency action’” by recharacterizing their switch of the Bundled Revenue definition as an attempted correction of “technical or clerical errors,” pursuant to their “continuing jurisdiction” under section 803(c)(4). Once again, they cannot, and the D.C. Circuit has effectively explained why this is so:

The [Judges] do[] not even try to squeeze [their] substantive rewrite of the Service Revenue definition into that [§ 803(c)(4)] category. Quite the opposite, the [Judges] admit[] that the new definition “represent[s] a departure” from the definition in the Initial Determination, and was a substantive swap designed to “mitigate” the alleged “problem” of the original definition leaving the interactive streaming service providers free to “obscure royalty-based streaming revenue by offering product bundles that include music service offerings with other goods and services[.]” ... To that same point, the order itself labels the initial and new definitions “diametrically-opposed approaches to valuing bundled revenues.” Nothing technical or clerical about that.

Johnson at 391.

On remand, I am unable to ascertain any basis for describing or justifying the changed Bundled Revenue definition as a technical or clerical correction. Thus, I conclude that the Judges cannot engage in “new ‘agency action’” pursuant to this section.

¹⁷ The first two bases for rehearing under the statute, *viz.*, change in the controlling law and the availability of new evidence, clearly do not apply. The third basis, *i.e.*, to correct a clear error or prevent manifest injustice, also does not apply. As explained herein, the substantive difference between the conflicting Bundled Revenue definitions should be resolved consistent with the Judges’ adoption of the PR II-based benchmark and the parties’ negotiated compromise of the “price discrimination vs. revenue diminution” dilemma. This resolution does not constitute an “error,” let alone a “clear error,” and maintaining the parties’ rate architecture from the Initial Determination does not generate any “injustice,” “manifest” or otherwise.

Next, I consider whether the Judges can engage in “new ‘agency action’” – by trying to squeeze the square peg of their definitional swap into the round hole that is the “unforeseen circumstances” clause in § 803(c)(4). That provision permits the Judges to exercise “continuing jurisdiction” if necessary to modify a regulatory term in a determination in response to “unforeseen circumstances,” if the absence of modification would frustrate the proper implementation of the determination. Once again, *Johnson* shuts the door:

Come oral argument, the [Judges] attempted to explain that the unforeseen circumstances would be that [they] initially adopted a definition that was not supported by the record, and that was in fact substantively unreasonable and would frustrate the proper implementation of their determination.” ... It is hard to see how the need to ground the original definition in the record was an unforeseen circumstance. That is Administrative Law 101. *See also* 17 U.S.C. § 803(c)(3) (“A determination of the [Judges] shall be supported by the written record.”).

Johnson at 391 (cleaned up). I agree. The present panel of Judges is bound by the D.C. Circuit’s ruling that the overlooking of the need to ground in the factual record the Bundled Revenue definition in the Initial Determination cannot constitute an “unforeseen circumstance.” Accordingly, I am unable to ascertain any basis for describing or justifying the changed Bundled Revenue definition as an “unforeseen circumstance” that would justify their invocation of “continuing jurisdiction.”

I further consider the argument (made by the Judges’ appellate counsel and by Copyright Owners) that the Judges have the “inherent authority *sua sponte* to make any ‘appropriate’ substantive ... or ‘fundamental changes after the Initial Determination ... that [they] believe[] serve ‘the interests of enhancing the clarity and administrability of the regulatory terms accompanying the [] Determination.’” *Johnson* at 391. The D.C. Circuit made short work of this argument as well, stating that, although the CRB Judges have “considerable freedom” with regard to determining their own procedures

that flexibility must be exercised within the lines drawn by the authorizing statute. Congress’s decision to limit rehearing to “exceptional cases,” and to confine other *post hoc* amendments to cases involving “technical or clerical errors,” would be a nullity if the [Judges] also had plenary authority to revise [their] determinations whenever [they] thought appropriate. The [Judges] nowhere in [their] order or the [] Determination explain[] the source of [their] power to make “fundamental” changes under the authorizing statute ... any time [they] deem such changes “appropriate” ... even after the Initial Determination.

Johnson at 392.¹⁸

As with regard to the proffered rationales discussed *supra*, I cannot identify any authority that would allow the Judges to declare for themselves in the present factual and legal context an “inherent” authority to override the Copyright Act and declare their right to engage in “new ‘agency action.’”

Finally, I consider Copyright Owners’ suggestion that the *remand itself* by the D.C. Circuit permits the Judges, pursuant to the Copyright Act, to engage in any procedure necessary

¹⁸ By the same reasoning, *Johnson* also rejected the Judges’ explanation in the *Determination* that they were permitted to treat Copyright Owners’ request as a general motion under § 350.4) of their regulations. *Id.*

to support their switch in the Bundled Revenue definition. The present Majority essentially adopts this procedural approach. However, I reject that argument as meritless.

The argument begins with a correct premise but seriously veers off course. Copyright Owners correctly note (and the Services do not disagree) that this remand proceeding constitutes “new ‘agency action.’” Copyright Owners then maintain that, because the Copyright Act does not provide for procedures that govern remand proceedings, the Judges are statutorily unconstrained with regard to the procedures they may adopt. This premise, although perhaps correct in other contexts, is most definitely incorrect in this specific context, given the clear holding in *Johnson*.

Here, the D.C. Circuit has been unequivocal in identifying the statutory limitations that precluded the Judges from switching out the Bundled Revenue definition in their Initial Determination and replacing it with a different definition in the Determination that was, to use the Majority’s phrase, “diametrically opposed” to the prior definition, in that it would eliminate the royalty-based incentive to price discriminate via bundling.¹⁹ *But Copyright Owners assert that the remand itself clothes the Judges with the procedural authority to make the very switch that Johnson forbids!* I do not understand the D.C. Circuit to have admonished the Majority for its failure to respect the boundaries of its jurisdiction, only to provide them, via remand, with a back-door through which they may circle-back and exceed those very boundaries.

A reading of section 803(a), upon which Copyright Owners rely, provides a further demonstration of the error in this argument. This subsection lists the authorities whose pronouncements the Judges must “act in accordance with,” including, quite unsurprisingly, “the decisions of the court of appeals under this chapter.” 17 U.S.C. § 803(a). In the instant case, the D.C. Circuit has unambiguously held that the Judges lacked the statutory authority to make the definitional switch at issue. For the Judges to construe that clear ruling as an implicit invitation to create new extra-statutory remand procedures that contradict the D.C. Circuit’s rationale for the remand would be inexplicable and would render useless the procedural ruling in *Johnson*.²⁰

In sum, I cannot and do not understand that the D.C. Circuit intended in *Johnson* simply to write a meaningless procedural opinion that the Judges could not merely ignore, but use to cleanse the very procedural error the D.C. Circuit had condemned.²¹

¹⁹ This substantive impact of the definitional switch is discussed *infra*.

²⁰ In fact, this argument is dangerous. The CRB Judges or any administrative agency, could willfully engage in extra-statutory procedures to obtain a particular substantive result. If there is no appeal, the extra-statutory procedure would be successful. But if the extra-statutory procedure was the subject of a successful appeal resulting in a remand, the CRB Judges (or any agency) could declare the remand as license to engage once more in extra-statutory procedures in order to obtain the same substantive result. This is a “heads-I-win, tails-you-lose” strategy.

²¹ Copyright Owners also argue that if the D.C. Circuit had intended in *Johnson* to prohibit the Judges from engaging in “new ‘agency action’” on remand, they would have reversed and reinstated the Initial Determination, rather than vacated and remanded that aspect of the Determination. But that argument confuses prudence with uncertainty. The D.C. Circuit prudently allowed the Judges, who are presumed to have particular knowledge of their duties, to consider whether there exist further explanations of their reasoning or “new ‘agency actions’” they could invoke to support their definitional switch. That prudence hardly suggests that the D.C. Circuit was sanguine about the existence of further explanations or additional actions that might support the switch.

Also, 17 U.S.C. § 803(d)(3) explicitly allows the D.C. Circuit to “vacate [a] determination of the ... Judges and remand the case to the ... Judges for further proceedings,” but only expressly allows the court to “enter its own determination” in connection with “the amount or distribution of royalty fees and costs, and order the repayment of any excess fees, the payment of any underpaid fees and the payment of interest pertaining respectively thereto”

Accordingly, the Bundled Revenue definition in the Initial Determination should be reinstated. As explained in the portion of the Initial Remand Ruling in which I join, this reinstatement is harmonious with the entirety of the Judges' findings and conclusions regarding the other remanded issues.

B. The Substantive Issue: The Dueling Definitions of Bundled Revenue

1. Introduction: The Issue as Framed in the Clarification Order

Regarding the definition of "Service Revenue" from bundled offerings, the Judges summarized the parties' competing arguments:

Copyright Owners presented evidence that the existing approach led, *in some cases*, to an inappropriately low revenue base—but did so in service to their argument that the Judges should reject revenue-based royalty structures. *They did not present evidence to support a different measure of bundled revenue* because their rate proposal was not revenue-based.

The Services rely on the fact that the approach to bundled revenue in the extant regulations is derived from the 2012 Settlement. The Judges have, however, *declined to rely on the 2012 Settlement as a benchmark*, as the basis for the rate structure, or, therefore, as regulatory guidance. The Services have observed *correctly* that the evidentiary records in *Web IV* and *SDARS III* differ from the record in this proceeding.²²

Clarification Order at 17 (emphasis added).

Despite these arguments, the Judges found that neither party presented evidence adequate to support the approach advocated in post-determination filings, because “the ‘economic indeterminacy’ problem inherent in bundling” remained unresolved.” *Id.* The Judges stated that the Services were the party in possession of the relevant information, and concluded that the Services bore the burden of providing evidence that might mitigate the “indeterminacy problem” inherent in bundling. Because the Judges concluded that the Services had not met that burden, they ruled that they must adopt an approach to valuing bundled revenue that is in line with what the Copyright Owners proposed. As a result, the Judges discarded the formula in the Initial Determination and ruled, instead, that streaming service providers will use their own standalone price (or comparable) for the music component (not to exceed the value of the entire bundle) when allocating bundled revenue. *Id.* at 16-18.

On remand, the parties have made the following arguments regarding the substance of the Bundled Revenue definition:

2. Copyright Owners

According to Copyright Owners, the prior Bundled Revenue definition in the Initial Determination failed to address the “‘economic indeterminacy’ problem inherent in bundling” appropriately and in a way consistent with Judges' precedent. CO Initial Submission at 75 (citing Clarification Order at 16-18). Copyright Owners proceeded to cite several portions of testimony

Id. Thus, it is hardly clear that the D.C. Circuit understood it had any choice upon vacating, save to remand for further proceedings. .

²² In *Web IV* and *SDARS III*, unlike under the Phonorecords II-based benchmark, there were no minima or floors to provide licensors with royalties in the event bundled offerings would otherwise fail to generate royalties.

from the Services' economic experts who acknowledged this problem. *Id.* They then point to hearing testimony in which Copyright Owners repeatedly raised the "economic indeterminacy" problem and demonstrated what they characterized as the absurd results to which the prior definition had led. *Id.* at 76. They pointed out that under the Initial Determination, the first step in computing Bundled Revenue was to identify revenues recognized from the entire bundle (*i.e.*, the price paid by the subscriber). The second step was to subtract "the standalone published price" for all non-music components of the bundle. According to Copyright Owners,

Id. at 76, 83.

Copyright Owners point out that the Judges already found with respect to other licenses that such an approach is not only fundamentally unfair, but "absurd." *Id.* (citing *Web IV*, 81 Fed. Reg. 26316, 26382 (May 2, 2016) (webcaster licenses); *see also SDARS III*, 83 Fed. Reg. 65210, 65264 (Dec. 19, 2018) (SDARS licenses) (rejecting proposed deductions by service from bundle revenues because of the "acknowledged 'economic indeterminacy' problem inherent in bundling"). Copyright Owners concur with the Judges' conclusion that the same reasoning applies to *Phonorecords III*. *Id.* at 76-77 (citing Clarification Order at 18 ("the 'economic indeterminacy' problem inherent in bundling is common to all three proceedings.")). Copyright Owners offer that Spotify conceded to this flaw in the definition in the Initial Determination, but offered an alternative that contained the same loophole. *Id.* at 77-78.

Copyright Owners also point out that the proponent of a term bears the burden of proof as to adoption. The Judges made clear that the licensee who wishes to offer bundles must bear the burden of providing evidence that might mitigate the acknowledged economic indeterminacy problem inherent in bundling, because any such evidence would be in its possession, not in the possession of the licensors. *Id.* at 79 (citing *SDARS III*, 83 Fed. Reg. at 65264 ("bundling [is] undertaken to increase [the Services'] revenues and it would be reasonable to assume that [the Services have] information relevant to the economic allocation of the bundled revenue.")). Copyright Owners contend they presented un rebutted evidence showing the unreasonableness of the Services' proposed definition while the Services offered no evidence to support their definition. *Id.* at 78, 79 (citing Clarification Order at 18). Copyright Owners maintain that no Service offered evidence concerning the separate values of the constituent parts of the bundles, or any other evidence concerning the economic allocation of bundled revenue, let alone the reasonableness of the definition in the Initial Determination. *Id.* at 80. Copyright Owners assert that in the absence of evidence to support the proposed definition, the Judges may adopt or fashion a definition of service revenue for bundled offerings that comports with the record evidence, which is precisely what the Judges did and, through new agency action, do again. *Id.* at 81.

They further argue that the hearing record and the Judges' precedent and reasoning further explain the unreasonableness of the prior definition and support the adopted bundle revenue definition. *Id.* at 82. Copyright Owners offer that in contrast to the Services' evidentiary failure, they have provided sufficient evidence showing the unreasonableness of the Services' proposed definition. They maintain that the definition adopted by the Judges in the Determination was consistent with the statutory factors and the evidence in the proceeding

showing how the prior definition had been manipulated and “led, in some cases, to an inappropriately low revenue base.” *Id.* at 83 (citing Clarification Order at 17-18).

Copyright Owners dispute the Services’ assertion that there is support for the *Phonorecords II* approach to bundles in the record of this proceeding. Instead, Copyright Owners argue, the Services’ purported evidence at most supports the benefits of the practice or strategy of bundling. They maintain that the strategy of bundling covered music services with other products or services has nothing to do with [REDACTED]. They offer that the definition in the Initial Determination has nothing to do with such benefits, and that those benefits may be equally served by a definition that ensures value is apportioned to the music component in the bundle. CO Reply at 73-76.

3. The Services

The Services argue that the evidence in the existing written record addressing bundles shows both that this definition is supported by the *Phonorecords II* benchmark and that it has proven industry-wide benefits. Services’ Initial Submission at 68. They emphasize that Copyright Owners did not propose an alternative definition of service revenue until after the Judges issued the Initial Determination and that any definition they propose now would fail the basic requirement that the Judges must adopt rules “on the basis of a written record.” *Id.* (citing 17 U.S.C. §§ 803(a)(1) and § 803(c)(3)).

Addressing the merits of the definition contained in the Initial Determination, the Services argue that it best serves the goals of the Copyright Act; that as a bright-line, easily administered rule, it continues the broad industry agreement from *Phonorecords II*, which was negotiated voluntarily between the Services and ... Copyright Owners – strong evidence that its terms are mutually beneficial.” Services’ Initial Submission at 69.

The Services contend the prior negotiated definition increases output and incentivizes beneficial price discrimination to reach casual and passive listeners who would otherwise not pay for music and thus would not generate revenue from which royalties could be paid. With regard to [REDACTED] *Id.* at 71 (and record citations therein).

They further state that the definition of Bundled Revenue in *Phonorecords II* also enabled funneling of many of listeners into full-priced, full-catalog services. The Services allege that Copyright Owners also ignore the extensive royalties that were generated. They add that, for casual/passive listeners and those who may be funneled to subscription services, the per-subscriber minimum guarantees that the Copyright Owners will still be paid a fair royalty. The Services then cite several portions of testimony from various Services’ economic experts who point out the realization of an expanded royalty pool, which the Services offer as proving a functioning marketplace. *Id.* at 68-74.²³

²³ The Services’ Reply reiterates this point and offers that the testimony cited by the Copyright Owners also shows why the Initial Determination’s Service Revenue definition works for bundles and grows royalties. Services’ Reply at 57-58.

The Services maintain that while neither the Services nor Copyright Owners submitted evidence specifically addressing the way that customers, Services, or Copyright Owners might value the component parts of bundles, such subjective valuations are unnecessary – given that the parties’ negotiated handling of the bundling issues provides the Judges with ample support for the PR II-based benchmark definition in the Initial Determination. See *id.* at 75-76.

The Services also argue that while the Judges’ decision in SDARS III did involve valuation of the music and non-music components of a bundle, the resolution in SDARS III is inapposite because, here, the rate structure has a way of ensuring that Copyright Owners are fairly compensated from bundles: the statutory minimum payment. Services’ Reply at 62.

C. Analysis and Decision

The fundamental difference between the impact of the two alternative definitions is simply stated:

Under the Initial Determination:

downstream bundling and its price discriminatory effect *would* be incentivized by a royalty structure that reflects the lower WTP of consumers who subscribe by paying for a Bundle;

Under the (Final) Determination:

downstream bundling and its price discriminatory effect *would not* be incentivized by a royalty structure that reflects the lower WTP of consumers who subscribe by paying for a Bundle.

To explain this difference, the Judges find it helpful to describe (as in the Determination and Dissent) how bundling facilitates price discrimination and how lower royalties for bundled streaming services incentivize such bundling.

Price discrimination occurs when a seller offers different units of output at different prices. See, e.g., H. Varian, *Intermediate Economics* at 462 (8th ed. 2010). The benefit to the seller arises from attempting to “charge each customer the maximum price that the customer is willing to pay for each unit bought.” R. Pindyck & D. Rubinfeld, *Microeconomics* at 401 (8th ed. 2013). For all goods, and intellectual property goods such as copyrights in particular,²⁴ the social benefit is that price discrimination more closely matches the quantity sold with the competitive quantity as the seller or licensor better aligns the price with the WTP of different categories of buyers or licensees. See W. Fisher, *Reconstructing the Fair Use Doctrine*, 101 Harv. L. Rev. 1659, 1701 (1988).

A seller can engage in price discrimination in several ways. One form is known as “second-degree price discrimination,” by which buyers self-sort the packages and quantities they purchase.²⁵ See W. Adams & J. Yellen, *Commodity Bundling and the Burden of Monopoly*, 90 Q. J. Econ. 470, 476 (1976) (the profitability of bundling “stem[s] from its ability to sort

²⁴ Streamed copies of intellectual property, such as musical works and sound recordings, have a marginal production cost of essentially zero, making price discrimination particularly beneficial, because charging any positive price, even to a buyer with the lowest WTP, still exceeds the zero marginal production costs. See Dissent, *passim*.

²⁵ “First-degree” price discrimination is a hypothetical construct by which a seller can identify the WTP of every buyer. “Third-degree” price discrimination occurs when the seller offers different prices to buyers based on their different characteristics (e.g., a senior citizen discount). See Pindyck & Rubinfeld, *supra*, at 402, 404-05.

customers into groups with different reservation price [WTP] characteristics.”). Bundling, *i.e.*, the “practice of selling two or more products as a package,” *Pindyck & Rubinfeld, supra* at 419, is thus a type of second-degree price discrimination. *See* A. Boik & H. Takahashi, *Fighting Bundles: The Effects of Competition on Second Degree Price Competition*, 12 *Am. Econ. J.* 156, 157 (2020).

The applicability of these basic economic principles was understood and explained by the parties’ experts at the hearing. *See, e.g.*, 3/15/17 Tr. 1224-25 (Leonard) (Google’s economic expert testifying that price discrimination through bundling is “very, very common ... even by pretty competitively positioned firms ... to sort out customers into willingness-to-pay groups.”); 3/30/17 Tr. 3983 (Gans) (Copyright Owners’ economic expert acknowledging that bundling is a form of price discrimination); *see also* Dissent at 69 (same).

How does this downstream (retail level) benefit of price discrimination impact the setting of upstream royalty rates? As the Majority explained (in summarizing the Services’ expert testimony) the linkage is explained by the economic concept of “derived demand”:

[M]ultiple pricing structures necessary to satisfy the WTP and the differentiated quality preferences of downstream listeners relate directly to the upstream rate structure to be established in this proceeding. Professor Marx opines that the appropriate *upstream* rate structure is derived from the characteristics of downstream demand. 3/20/17 Tr. 1967 (Marx) (rate structure upstream should be derived from need to exploit WTP of users downstream via a percentage of revenue). This upstream to downstream consonance in rate structures represents an application of the concept of “derived demand,” whereby the demand upstream for inputs is dependent upon the demand for the final product downstream. *Id.*; *see* P. Krugman & R. Wells, *Microeconomics* at 511 (2d ed. 2009) (“[D]emand in a factor market is ... *derived demand* ... [t]hat is, demand for the factor is derived from the [downstream] firm’s output choice”).

Determination at 19; *accord* Dissent at 32 (noting that “the upstream demand of the interactive streaming services for musical works (and the sound recordings in which they are embodied) – known as “factors” of production or “inputs” – is derived from the downstream demand of listeners to and users of the interactive streaming services ... This interdependency causes upstream demand to be characterized as “derived demand.”).

In the present proceeding, the PR II-based benchmark embodies the parties’ negotiated definition of Bundled Revenue for purposes of calculating royalties on bundled interactive offerings. This is the definition in the Initial Determination. Copyright Owners’ preferred definition for Bundled Revenue – the Determination’s definition – would not only ignore this agreed-upon definition, but would also de-link the royalty rate from the WTP of purchasers of bundles.²⁶ The Judges recognize that Copyright Owners have expressed concern the Services

²⁶ To see the incentivizing effect of the link between the royalty level and variable WTP, consider the following example. Assume a hypothetical bundle consists of a subscription to the “Acme” interactive music streaming service and the sports service NFL Sunday Ticket. Assume also that Acme and NFL Sunday Ticket have standalone monthly subscription prices of \$9.99/month and \$149.99/month respectively, so that purchasing both separately would cost \$159.98/month. But assume the bundle price is only \$140/month. Acme’s purpose in bundling its interactive music streaming service subscription offering with NFL Sunday Ticket would be to attract customers

could use such bundling in order to diminish revenue otherwise payable on a higher royalty tier. However, the Majority noted that the evidence indicated such diminishment only occurred “in some cases” and that such practices were not “sweeping.” Clarification Order at 17, 21. Thus, the Judges find that eliminating the incentive for price discrimination via bundling would be a disproportionate response and inconsistent with the broad price discriminatory PR II-based benchmark they find useful in this proceeding.

Expert testimony in this regard is “substantial evidence” on which the Judges can rely. For example, the D.C. Circuit also relied in *Johnson* on the testimony of the same witness, Spotify’s economic expert witness, Professor Marx, to affirm the inclusion of the price discriminatory structure for student and family plans. *Johnson*, 969 F.3d at 392-94. Professor Marx explained how a downstream “lower willingness (or ability) to pay” among some cohorts of consumers supports definitional terms, for student and family subscribers, that lower royalty rates in order to further “economic efficiency” in a manner that “still allows more monetization of that provision of that service.” *Johnson* at 392-93. Broadening her lens, Professor Marx also explained that this price discriminatory approach is appropriate “across all types of services and subscribers,” as in “[t]he current law [and in the PR II-based benchmark]” which “accommodates ... ad-supported services ... and ‘bundled services’ through different rate provisions.” Marx WRT ¶ 41 (emphasis added). See also 3/21/17 2182-83 (Hubbard) (Amazon’s expert witness testifying that “Prime Music, which is *bundled* with an Amazon Prime service ... sort[s] out customers’ willingness to pay, with an idea of trying to maximize the number of customers,” and agreeing that this approach constitutes “sorting by way of bundling.”) (emphasis added). Further, Professor Hubbard opined that, given the revenue attribution “measurement problem” associated with bundled products, the “Phonorecords II” approach “with the different categories and the minima” ... address this sort of problem [in] a very good way.” 3/15/17 Tr. 1221 (Hubbard).

As in the case of family and student price discrimination, the beneficial effect of such differential pricing was supported by industry witnesses as well as expert witnesses. See, e.g., Mirchandani WDT ¶ 71 (Amazon executive citing the Phonorecords II-based benchmark provisions regarding bundling that “allowed Amazon to bundle Prime Music with Amazon Prime, enabling Amazon to bring a limited catalog of music [REDACTED]”). In sum, the same type of witness testimony that the D.C. Circuit found sufficient to support price discriminatory student and family plans also supports the use of the price discriminatory bundled definition contained in the Initial Determination.

Given the overall benefits from price discrimination, at first blush it is curious that Copyright Owners would risk “leaving money on the table” by seeking to remove the royalty-based incentive for price discrimination via bundling. The Judges have identified this problem

who had a WTP for the standalone Acme service below \$9.99/month, but a WTP at or above the \$140/month for the bundle.

Under the definition in the Determination, royalties would be paid on the standalone \$9.99/month Acme price. But the purpose of the bundling was to attract subscribers *who would not pay the standalone \$9.99/month price*, so no such would-be subscribers would sign-up, and *no royalties would be generated by them*.

By contrast, under the Initial Determination, the standalone price of NFL Sunday Ticket, \$159.98/month, would be subtracted from the \$140/month bundle price. Although that would preclude a payment of royalties on a *revenue prong*, *royalties still would be paid, under a different tier or on the mechanical floor*.

earlier in this Initial Remand Ruling, in connection with the broader issue of the overall beneficial price discriminatory structure of the PR-based benchmark. As the Judges noted in that general price discrimination context, Copyright Owners’ own expert economic witnesses acknowledged that they would not irrationally leave money on the table. In fact, Copyright owners’ aim, according to that testimony, is to create an unregulated space—per the Bargaining Room theory—and to use their complementary oligopoly power to negotiate price discriminatory rates (in bundles or otherwise), which would free them from the section 801(b)(1) requirements of reasonableness and fairness.

The Judges further find that their prior ruling on this issue in *SDARS III* is distinguishable. There, a proffered bundled revenue definition eliminated the payment of any royalty at all. Copyright Owners quite correctly describe that result as “absurd,” but that is not the result here. Rather, in the present case, the parties’ negotiated an approach that the Judges adopted in the Initial Determination requiring royalties to be paid on interactive services bundled with other products or services.

Even more distinguishable is Copyright Owners’ assertion that *Web IV* provides support for their preferred definition of service revenue. The argument is immediately suspect, because *Web IV* involved per-play royalty rates – not percent-of-revenue rates, making the definition of revenue wholly inapposite. Further, the discussion of the price of an “ice cream cone” in *Web IV*—on which Copyright Owners rely—had nothing to do with bundling or isolating the WTP for different products or services. Rather, there the Judges criticized a bizarre argument made by a licensee (who had a quantity discount for plays steered in its direction), that was tantamount to arguing that if a vendor sells one ice cream cone for \$1.06 but a buyer could buy two for \$1.06, that the market price of an ice cream cone is thus only \$.06. This argument was indeed fallacious, because the price of an ice cream cone would be reasonably identified as the average of the total cost for the two cones, *i.e.*, \$.53/cone, and never as \$.06 per cone.

Here, the issue, is how to address the WTP of different classes of buyers with heterogeneous WTP, not the pricing of a quantity discount. The parties addressed this issue by utilizing the Bundled Revenue definition contained in the PR II-based benchmark (and in the Initial Determination) to address the indeterminacy inherent in the variable WTP among purchasers of the bundles, by setting floors and minima, rather than attempt to sort out the WTP of individual (or individual blocs) of subscribers. The “ice cream cone” issue in *Web IV* is wholly unrelated, and the *SDARS III* situation, as explained *supra*, is also distinguishable.²⁷

²⁷ The foregoing analysis also explains why Copyright Owners’ assertion that the Services did not satisfy their burden of proof with regard to the Bundled Revenue definition misses the point. The Services’ burden was to show the reasonableness of utilizing the Bundled Revenue definition in the PR II-based benchmark, not to show that their proffered approach measured the WTP of individual subscribers (or blocs of subscribers). Such an alternative approach might have had merit but no alternative approach was presented to the Judges.

To be clear, the Judges are not declaring that an alternative Bundled Revenue definition and/or alternative rates and structures for bundle, might not have been preferable. *See* 4/15/17 Tr. 5056-58 (Katz) (“[I]f someone had a proposal [with] a specific reason why we should adjust this minimum that’s something I would have examined.”). *See also* 3/15/17 Tr. 1227-28 (Leonard) (Google’s economic expert testifying that “if somebody had ... suggest[ed] ... a different sort of bucket that should be created ... that’s a good idea.”). But Copyright Owners did not propose such alternatives at the hearing, and the alternative in their Motion for Clarification simply eviscerated the “derived demand”-based link between royalties and bundled offerings. As the Judges have noted *supra*, in the words of Judge Patricia Wald, all judges are cabined by the record evidence introduced by the parties. Therefore (in the absence of a way in which to synthesize the parties’ proposals in a manner that does not “blindsides” the parties) the Judges must choose between the proposals that are in the record, not potentially superior proposals that are not in the

For the foregoing reasons, I find that – even if the Judges had a procedural mechanism by which to support the switch in the Bundled Revenue definition – I would decline to utilize it in this Initial Remand Ruling, because the definition in the Initial Determination (unlike the definition in the Determination) is consistent with the Judges’ other substantive rulings herein. That is, just as the Majority abandoned its Bundled Revenue definition in its Initial Determination because it refused to credit the PR II-based benchmark (even as “guidance”), the Judges here do partially rely on the PR II-based benchmark, and thus find that it supports the Bundled Revenue definition contained in the Initial Determination.

VIII. Application of the Four Itemized Statutory Factors

As the forgoing analysis explains, bundling is a form of price discrimination. Accordingly, the Judges’ explanation of how price discriminatory rates in the PR II-based benchmark interrelate with the Factor A through D objectives in section 801(b)(1) are equally applicable here. Accordingly, the Judges incorporate by reference here their discussion of those four factors set forth *supra* in connection with the PR II-based benchmark, and find that there is no basis pursuant to those four factors to adjust the PR II-based benchmark definition of Bundled Revenue.

IX. Conclusion

This Dissent in part is issued as a RESTRICTED document. Within 30 days of the date of issuance, the participants shall file a version of this Dissent with agreed redactions to permit viewing by the public.

David R. Strickler,
Copyright Royalty Judge

Dated: July 2, 2022.²⁸

record. Here, the Judges favor the Bundled Revenue definition in the Initial Determination that was negotiated by the parties, incentivizes price discrimination and pays royalties on the bundled music, over the substituted definition in the Determination pursued by Copyright Owners that would eliminate price discrimination, except under the terms Copyright Owners could impose via their complementary oligopoly power, and without regard to the statutory requirements of a “reasonable rate” and a “fair income” for the Services.

²⁸ Technical difficulties on July 1 caused the delay in filing of this Dissent until July 2.

Proof of Delivery

I hereby certify that on Monday, August 01, 2022, I provided a true and correct copy of the Dissent in Part as to Section IV of the Initial Ruling and Order after Remand by Judge David R. Strickler (PUBLIC) to the following:

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Signed: /s/ Scott Angstreich