PUBLIC VERSION

Before the
COPYRIGHT ROYALTY BOARD
LIBRARY OF CONGRESS
Washington, D.C.

In re DETERMINATION OF ROYALTY RATES AND TERMS FOR MAKING AND DISTRIBUTING PHONORECORDS (Phonorecords III)	Docket No. 16–CRB–0003–PR (2018-2022) (Remand)

COPYRIGHT OWNERS' RESPONSE TO JUDGES' JULY 27, 2022 ORDER SOLICITING RESPONSES REGARDING REGULATORY PROVISIONS

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National Music Publishers' Association ("NMPA") and Nashville Songwriters Association International ("NSAI") (together, "Copyright Owners" or "COs") respectfully submit the following response to the Judges' July 27, 2022 Order Soliciting Responses Regarding Regulatory Provisions (eCRB Docket No. 27051; the "July 27 Order"). The July 27 Order directed the participants to address (a) their adversary's arguments regarding their differing proposed regulatory provisions submitted on July 18, 2022 pursuant to the Initial Ruling and Order After Remand (eCRB Docket No. 26938; the "Ruling"), and (b) the issue of former subpart C per-subscriber minima referenced in an omitted footnote. COs address these issues below.

I. The Services' rate proposal on remand is not a "benchmark"

The Services repeatedly argue that their joint rate *proposal* on remand *is* the "PR II-based benchmark" that is to be adopted pursuant to the Ruling. *See, e.g.*, Joint Submission of Regulatory Provisions (eCRB Docket No. 27005; the "Services' Joint Submission") at 2; unauthorized letter to the Judges (eCRB Docket No. 27022; the "July 22 Letter") at 12. This argument is factually and logically baseless. Under no precedent or standard is a party's request for relief in a litigation a "benchmark." Indeed, the Judges have explained that proposals are not benchmarks, and that the usefulness of benchmarks comes from their being marketplace agreements which might "bake in" different contributions and value, and thereby approximate a market result.[1]

The argument is also inconsistent with the Ruling, which states, for example, that "[t]he PR II-based benchmark was the product of an industrywide negotiation, with the music publishers

[1] *See, e.g.*, *Determination of Royalty Rates and Terms for Transmission of Sound Recordings by Satellite Radio and Preexisting Subscription Services (SDARS III)*, 83 Fed. Reg. 65210, 65210, 65212-13 (December 19, 2018) (noting that the Judges considered "proposals" from the participants as "guideposts rather than as benchmarks," and explaining the Judges' benchmarking process as involving "marketplace benchmarks"); *Digital Performance Right in Sound Recordings and Ephemeral Recordings (Web II)*, 72 Fed. Reg. 24084, 24095 (May 1, 2007) (explaining that "[b]ecause we adopt a benchmark approach to determining the rates," various considerations would have been factored into the "negotiated price[.]").

represented by the NMPA and the interactive streaming services represented by DiMA, their respective trade associations." (Ruling at 92 (emphasis removed).) By contrast, the Services' rate proposal on remand is an aspirational wish list concocted for litigation purposes that was never the subject of any negotiation, let alone a marketplace agreement.[2] Moreover, no evidence was ever presented on the Services' remand rate proposal, as it was presented for the first time on remand, and the scope of the remand was limited to taking evidence only on the question of expanding the uncapped TCC rate prong. (*See* Order Regarding Proceedings on Remand, eCRB Docket No. 23390, at 1-2.) In short, the Services' position that their remand rate proposal is to be adopted *in toto*, with the exception of the *Johnson*-affirmed 15.1% revenue rate, is not consistent with the Ruling or with due process.

II. The Ruling is silent on the implementation of student and family discounts, and they are inconsistent with core reasoning in the Ruling

A. Student and family discounts are not *Phonorecords II* terms, and are inconsistent with the Ruling's reasoning and the roll back of the TCC rate level calculation that was affirmed by *Johnson*

In addition to the 15.1% revenue rate, the Ruling notes two other holdings from the Board's original Final Determination from 2019 (*see* 84 Fed. Reg. 1,918 (2019); the "Original FD") that were affirmed by *Johnson*: (i) the 26.2% TCC rate level calculation and (ii) student and family discount plan rate reductions. (Ruling at 19-20, 74, 112.) Despite these three specific findings expressly affirmed in *Johnson*, the directive in the Ruling appears to call for rolling back the TCC rate level calculation in the Original FD, even though that runs expressly counter to another

[2] The Services' position is also inconsistent with the Ruling's directive to the participants to confer towards joint regulatory provisions, or else submit separate proposals. (Ruling at 114.) If the Ruling was simply adopting the Services' rate proposal *in toto*, there would have been no need to have the participants present regulatory language to implement the Ruling.

holding in the Ruling acknowledging that the Judges cannot change the Original TCC rate level calculation:

> [B]ecause the identical analysis was performed by the Judges to derive **the 26.2% TCC rate** as was done to derive the 15.1% revenue rate, the Majority's finding with regard to the *derivation and calculation* of the TCC rate likewise **is not subject to further consideration on remand by the Judges**.

Ruling at 20 (added emphasis in bold).

Thus, while *Johnson* would foreclose this tribunal from changing the 26.2% TCC rate level calculation and the student and family plan discounts, the Ruling rejects the affirmed TCC rate level calculation and does not state that it is implementing the affirmed student and family plan discounts. Moreover, the reasoning set forth in the Ruling is at odds with implementation of the student and family discounts while, at the same time, rolling back the TCC rates.

For one, the rejection of the affirmed TCC rate levels, noted above, cannot be reconciled with implementation of the affirmed student and family discounts. *See Masonry Masters, Inc. v. Thornburgh*, 742 F. Supp. 682, 687-88 (D.D.C. 1990) (agency acted arbitrarily and abused its discretion "[b]y reaching diametrically opposed results" on questions that were "for all practical purposes, identical").

Moreover, implementation of those discounts is at odds with the Ruling's holdings that rely on the negotiated terms of *Phonorecords II* to provide protection from revenue diminution. The Ruling reaffirms the Original FD's findings that revenue diminution is both a reality and a threat to COs' royalty payments, findings also affirmed by *Johnson.* (*See* Ruling at 81-83.) Indeed, *Johnson* specifically tied the Board's implementation of the uncapped TCC prong to harm from student and family discount programs, noting that:

> By pegging the mechanical license royalties to an **uncapped** total content cost prong, **the Board sought to ensure** that owners of musical works copyrights were neither undercompensated relative to sound recording rightsholders, nor **harmed**

> **by** the interactive streaming services' revenue deferral strategies (such as **student and family discount programs**).

Johnson v. CRB, 969 F.3d 363, 372 (D.C. Cir. 2020) (emphasis added).

The Ruling, in eliminating the Original FD's uncapped TCC rate structure, repeatedly emphasizes that subsequent to the Ruling the protections that COs will have from revenue diminution are to be the protections set forth in the *Phonorecords II* rates and terms:

> [T]he Judges emphasize that **the rate structure of the PR II-based benchmark provides protection *sought by Copyright Owners* against revenue diminution** by the Services—*protection they would otherwise lose*—because in this Initial Ruling the Judges are not adopting the vacated uncapped TCC prong for which Copyright Owners are now advocating, and which they claim would have protected them in that regard. (Ruling at 58 (emphasis added in bold).)
>
> [T]he foregoing analysis demonstrates the economic reasonableness and appropriateness of the price discriminatory *Phonorecords II rate structure* and its **negotiated safeguards to address the real possibility of revenue diminution**. (Ruling at 78 (emphasis added in bold).)

(*See also id.* at 84 (holding that "there is no sufficient reason in the record to depart from the bargained-for multi-tiered rate structure in *Phonorecords II*" and its minima and floors); 65 n.98 ("There is no sufficient basis for the Judges to substitute their own blunt conception of the appropriate form and extent of price discrimination for the structure generated in negotiations by the market participants.").)[3]

[3] The Ruling employs the same reasoning with respect to the revenue mismeasurement problem connected to the bundle revenue definition. As the Ruling observes, the Board found there was evidence that the *Phonorecords II* bundle revenue definition often led to "an inappropriately low revenue base." (*Id*. at 95.) Nevertheless, the Ruling readopts the *Phonorecords II* bundle revenue definition, holding that COs are to receive the protections from the "negotiated alternative royalty provisions" in the *Phonorecords II* rates and terms—which do not include rate reductions for student and family discounts. (*See e.g.*, Ruling at 96 n.140, 111 n.161; *see also id*. at 113; Dissent in Part as to Section IV of the Initial Ruling and Order at 4 n.9.)

Implementing the affirmed student and family discounts would substantially diminish the negotiated alternative royalty provisions in *Phonorecords II*, and would directly lead to a loss of royalties due to revenue diminution. According to those discounts, the subscriber-based royalty provision for student plans is reduced by 50%. The subscriber-based royalty provision for family plans is reduced by up to 75% (when 6 subscribers are using a family plan, which is counted as 1.5 users). *See* 37 C.F.R. §§ 385.2, 385.22 (2019). These discounts had a significant real-world impact when they were implemented—notwithstanding the percentage rate increases set forth in the Original Final Determination, and notwithstanding the "uncapping" of the TCC, [redacted]. (*See* Remand Written Rebuttal Testimony of Jeffrey A. Eisenach, PhD ¶¶ 81-82 (rounded).)

The Ruling does not addresses the financial impact to COs of rolling back the TCC rate to *Phonorecords II* rates (despite *Johnson'* affirmance of the Original FD's increase of those rates) combined with re-capping the TCC prong (at a per-subscriber rate originally agreed to in 2008 that does not come close to correlating to the rate percentages affirmed by *Johnson*) and then *reducing* the *Phonorecords II* mechanical floors in the case of student and family plans, which, while affirmed by *Johnson*, are not part of the *Phonorecords II* settlement. Nor does the Ruling address how doing so would be consonant with the 801(b)(1) standard.

B. Student and family discounts have never extended to the TCC caps

Johnson's affirmance of student and family plan discount terms is solely in connection with the mechanical floor.[4] Neither the Original FD nor *Johnson* contemplated applying those discounts to the TCC caps. There have never been student or family plan royalty reductions in connection with the TCC caps, whether under *Phonorecords I, II*, the Original FD, the Dissent to the Original FD, or otherwise.

The Services claim that extending the student and family plan discounts to the TCC caps would be "consistent with . . . the conclusions reached in *Johnson* and by the Judges throughout the Initial Ruling regarding the many benefits of price discrimination." (Services' Joint Submission at 2-3.) This is simply incorrect. *Johnson* recognized that these user discounts are part of the Services' revenue diminution strategies. *See Johnson*, 969 F.3d at 372.[5] And, as COs show above, the student and family reductions cannot be reconciled with the reliance of the Ruling on the bargained-for *Phonorecords II* royalty protections, which did not include those reductions.

Importantly, the TCC cap levels set forth in *Phonorecords II* already equate to heavily discounted pricing, including through student and family discount plans. The highest of the TCC caps, for standalone portable subscription services, is a mere 80-cents per subscriber per month,

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[4] *See* 84 Fed. Reg. at 1962 (adopting such discounts "[f]or purposes of calculating a Mechanical Floor rate"); *Johnson*, 969 F.4d at 373 ("Second, the Board concluded that, **in setting the mechanical floor**, student and family plans should be counted differently for purposes of computing the number of subscribers to a streaming service."), 375 ("The Board also maintained the counting of family plans as the equivalent of 1.5 subscribers and student accounts as the equivalent of 0.5 subscribers **when calculating the mechanical floor**."), 392 ("The Copyright Owners take exception to the Board's definition of "Subscribers" as applied to student and family streaming plans, **which affects the computation of the mechanical floor**.") (emphases added).

[5] The Services cite *Johnson* at 392-94 in support of their position, but that section merely summarized the testimony that Service witnesses offered related to the purported lower willingness to pay of students and families and concluded that "[t]he Board's finding about the willingness (and ability) of students and families to pay is grounded in substantial record evidence." That is not a conclusion regarding the purported "benefits of price discrimination."

all-in. *See* 37 C.F.R. § 385.13(a)(3) (2017). The other TCC caps are even lower, at 50-cents per subscriber per month, all in. *See* 37 C.F.R. § 385.13(a)(1)-(2) (2017). Those cap levels are thus 8% and 5%, respectively, of the standard $9.99 premium subscription price point, nowhere remotely close to the 15.1%. (*See e.g.*, Hearing Tr. 225:1-15 (Levine) ([redacted]); Tr. 394:16-25 (Phillips) (same); Tr. 1801:23-1802:16 (Page) (same).)[6] Without any student and family discounts, these cap levels equate to a consumer price discount of nearly 50% in the case of the 80-cent cap and over 65% in the case of the 50-cent cap (at the affirmed and implemented 15.1% revenue rate). Put another way, these rates are already so low that they would not bind unless a Service drops its average pricing by at least 50% relative to the standard $9.99 price point. To apply student and family discounts *again* to these already uncorrelated low caps would magnify the losses from these revenue diminution strategies.

III. Under the Ruling, the *Phonorecords II* Subpart C provisions should be included in the rates and terms

A. Under the holdings of the Ruling, the *Phonorecords II* Subpart C all-in per-subscriber rates are to be included

The Judges direct the parties to address a point in an omitted footnote from the Ruling concerning Copyright Owners assertion "that the Services have inexplicably omitted from their proposed subpart C rates a portion of the Phonorecords II rates, to Copyright Owners' detriment."[7]

As COs explained in the submission cited in the omitted footnote, the Services' rate proposal on remand eliminates all-in per-subscriber rates that were present in the *Phonorecords II*

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[6] Professor Marx admitted [redacted] (Hearing Tr. 1900:13-1902:15; 5578:8-5579:21.) Of course, the 80 cents [redacted] because it was set years before Spotify even entered the US market. *See* 37 C.F.R. § 385.13(a)(3) (2009); Original FD at 1921 (". . . Spotify . . . launched in the United States in 2011.").

[7] July 27 Order at 1. This issue was anticipated and addressed at page 14 of Tab A of COs' July 18, 2022 submission.

structure for limited offerings and paid locker services. *See* 37 C.F.R. § 385.23(a)(3)-(4) (2017) (setting forth 18-cent and 17-cent per-subscriber floors for limited offerings and paid locker services, respectively). The Services had included these rates in their original *Phonorecords III* rate proposals, and have never provided a basis for dropping them on remand while continuing to pursue *Phonorecords II*-based rates and terms.

Moreover, the Ruling quite clearly holds that these rates are to be included. The Ruling provides that "the alternative rates (identified in subpart C as 'minima' and 'subminima') rates **shall remain unchanged**." (Ruling at 94 (emphasis added)), and observes that those minima included *both* "per-subscriber and TCC minima," which includes the all-in per-subscriber minima for limited offerings and paid locker services. (*Id*. at 93; *see also* 37 C.F.R. § 385.23(a)(3) and (4) (2017).)[8] Copyright Owners therefore included these all-in per-subscriber minima in their submitted regulations implementing the Ruling.

The Services' argument that those minima must be excluded under law of the case has no basis. The Board only excluded those minima in the Original FD as part of the "regulatory overhaul" in which it uncapped the TCC. (Amended Order on Motions for Rehearing at 12-13.) The Judges *explicitly* tied the removal of the *Phonorecords II* subpart C all-in per-subscriber rates to the removal of the all-in per-subscriber caps on the TCC for standalone offerings, quoting the Services' argument that:

[8] Not only were these minima part of the *Phonorecords II* rate structure, they were also included as part of the Services' original rate proposals from the underlying *Phonorecords III* proceeding. (*See* Amazon Digital Services LLC Proposed Rates and Terms (Nov. 1, 2016) (at proposed § 385.23); Google Inc.'s Proposed Terms (Nov. 1, 2016) (same); Proposed Rates and Terms of Pandora Media, Inc. (Nov. 1, 2016) (same); Proposed Rates and Terms of Spotify USA Inc. (Nov. 1, 2016) (indicating no changes from § 385.23).)

> the Copyright Owners offer no reason for reinserting per-subscriber minima for these service categories, but continuing to discard the other per-subscriber minima from the prior regulations that benefited the Services.

(*Id*.) But of course, the Ruling has reinserted the "caps" (*i.e.*, the per-subscriber minima) on the TCC, and so there is no logic to the Services' omission of the *Phonorecords II* subpart C all-in per-subscriber rates that the Ruling explicitly says "shall remain unchanged."

B. Under the holdings of the Ruling, the *Phonorecords II* definition of revenue for subpart C bundles should also remain in place

Consistent with the express contemplation of the Ruling, COs' submitted regulations maintain *Phonorecords II*'s bundle revenue definition for the Subpart C offering category of Mixed Service Bundles. This is another *Phonorecords II* term that the Services included in their original *Phonorecords III* rate proposals, but opportunistically abandoned on remand without explanation, while continuing to argue for *Phonorecords II*-based rates and terms.

Bundles falling under *Phonorecords II* subpart C (*i.e.*, mixed service bundles) did not have any per-subscriber floor. Instead, they had a definition of bundle revenue with a floor based upon the standalone published subscription price. That definition is a greater-of calculation between (i) revenue under the definition that the Ruling readopted for bundled subscription offerings, and (ii) either 40% or 50% of the standalone published price of the licensed music component of the bundle, depending on the number of subscribers to the mixed service bundle. See 37 C.F.R. 385.21 (2017) ("Subpart C service revenue," subparagraph 5).

The Services omit this definition without any explanation. COs submit that this revenue definition is necessary if the Judges are going to reimplement the old Subpart C rates and terms. The only basis for implementing these terms is that they were part of settlement, and so the bare minimum must include the protections that were part of that settlement, which include this stronger revenue definition. The Services have submitted no evidence at all to support their proposal to

modify Subpart C to omit this definition. Moreover, the Ruling appears to intend to adopt "the parties' negotiated definition of Bundled Revenue for purposes of calculating royalties on bundled interactive offerings." (Ruling at 111.) The Judges decision to re-implement the old Subpart C offering types means that there are *two* negotiated definitions for bundle revenue: the one for the old subpart B bundles and the one for the old subpart C bundles. It would be arbitrary and capricious to adopt the subpart C terms but not the associated bundle revenue definition, particularly where the Services proposed including it in the original proceeding, and have offered no argument or evidence why it should not be included. Again, the Services' *post hoc* changes to the PR II rate structure, in every instance to the detriment of COs, creates the very post-hearing problems of a lack of evidence in the record that the Services successfully complained of to the D.C. Circuit on appeal.

IV. The Services' unexplained removal of the royalty floor terms language that has been in place since *Phonorecords I* must be rejected

The Services inexplicably propose deleting § 385.22 in its entirety and replacing it with a table of rates. But § 385.22 has been in place with largely unchanged language since *Phonorecords I*, and there has been absolutely no evidence adduced about the potential effects of such a significant change in language in such a critical term. Indeed, this restructuring was offered for the first time on remand, when the record was not even open to taking new evidence on this issue (or any issue other than the expansion of the uncapped TCC rate structure). The Ruling does not, nor could it, explain a reasoned basis for making such a change without any discussion in the record concerning the proposed language. Moreover, the proposed change is simply unnecessary. The Services purport to be maintaining the § 385.22 royalty floors, and so there is no need or basis to eliminate the language describing these floors, which makes clear how they involve the application of the floor based upon features of offerings.

Dated: August 5, 2022

Respectfully submitted,

PRYOR CASHMAN LLP

By: /s/ Benjamin K. Semel

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In re DETERMINATION OF ROYALTY RATES AND TERMS FOR MAKING AND DISTRIBUTING PHONORECORDS (Phonorecords III)	Docket No. 16–CRB–0003–PR (2018–2022) (Remand)

DECLARATION OF BENJAMIN K. SEMEL
REGARDING RESTRICTED INFORMATION

1. I am a partner at Pryor Cashman LLP, counsel for the National Music Publishers' Association ("NMPA") and the Nashville Songwriters Association International ("NSAI" and, together with the NMPA, the "Copyright Owners") in the above-captioned proceeding (the "Proceeding").

2. Pursuant to Section IV.A of the Protective Order issued in the above-captioned Proceeding on July 28, 2016 (the "Protective Order"), I submit this declaration in connection with the Copyright Owners' Response to Judges' July 27, 2022 Order Soliciting Responses Regarding Regulatory Provisions (the "Response").

3. I have reviewed the Response. I am also familiar with the definitions and terms set forth in the Protective Order. Each of the redactions that the Copyright Owners have made to the publicly-filed version of the Response is necessitated by the designation of that information as "Confidential Information" under the Protective Order by either one of the participants in this proceeding or by a non-party Producing Participant, as that term is defined in the Protective Order. Because the Copyright Owners are bound under such Order to treat as "Restricted" and to redact information designated "Confidential Information" by Participants and Producers, they are doing

so. Copyright Owners reserve all rights and arguments as to whether any such information is, in fact, "Confidential Information."

Pursuant to 28 U.S.C. § 1746, I hereby declare under penalty of perjury that the foregoing is true and correct to the best of my knowledge, information and belief.

Dated: August 5, 2022
New York, New York

/s/ Benjamin K. Semel

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Proof of Delivery

I hereby certify that on Friday, August 05, 2022, I provided a true and correct copy of the Copyright Owners' Response to Judges' July 27, 2022 Order Soliciting Responses Regarding Regulatory Provisions [PUBLIC] to the following:

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Signed: /s/ Benjamin K Semel