

**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)**

**[PUBLIC]**

**AMENDED**

**ORDER GRANTING IN PART AND DENYING IN PART  
MOTIONS FOR REHEARING**

On January 27, 2018, the Copyright Royalty Judges (Judges) issued their Initial Determination of Royalty Rates and Terms (*Initial Determination*) in the captioned proceeding. Participants are permitted to file a motion for rehearing within 15 days of the date of issuance of a determination. 17 U.S.C. 803(c)(2)(B). The Judges received motions for rehearing from the Copyright Owners<sup>1</sup> ([Owners' Motion](#)), from three of the streaming services participating in the proceeding<sup>2</sup> ([Services' Motion](#)), and from George Johnson d/b/a/ George Johnson Music Publishing ([GEO](#)). The Judges ruled on the GEO motion by separate order. [Order Denying Johnson Motion for Rehearing](#) (June 6, 2018).

Judge Strickler did not join in the *Initial Determination* and issued a *Dissenting Opinion*. The Judges issued the *Initial Determination* and the *Dissenting Opinion* only to counsel for participants, pending redaction of privileged or confidential information. The Judges issued a [redacted, public version of the Initial Determination and the Dissenting Opinion](#) on March 19, 2018. Judge Strickler does not join in this Order, and takes no position with regard to its reasoning and rulings. Rather, he respectfully reaffirms his *Dissenting Opinion*, which will be made final and issued together with the Final Determination. References to “the Judges” in this Order are references to the authors of the Majority Opinion only. The Copyright Owners styled their motion as one for technical corrections: Motion for Clarification or Correction of Typographical Errors and Certain Regulatory Terms. In particular, the Copyright Owners do not request rehearing, but submit their motion “pursuant to the general motion procedures of 37 CFR §§ 350.3 and 350.4 to put before the Judges certain questions” concerning the regulatory terms attached to the Initial Determination. Owners Motion at 1. The Services Motion was for Rehearing to Clarify the Regulations.

<sup>1</sup> The Copyright Owners filing the motion are the National Music Publishers' Association and the Nashville Songwriters Association International.

<sup>2</sup> The streaming services filing the motion are Amazon Digital Services, LLC; Pandora Media, Inc.; and Spotify USA Inc.

The Services take exception to the Owners’ styling their Motion as something other than a motion for rehearing. The Services assert that the Owners do so to “help themselves to additional pages for their Motion” and “to skirt the standard governing motions for rehearing—a standard that the Copyright Owners have not even attempted to meet.” [Services’ Opposition to Owners Motion](#) at 1-2. The Judges do not speculate on the Owners’ motivation for styling their Motion as something other than a motion for rehearing, but agree that, no matter the styling, the Motion would not and does not meet that exceptional standard for granting rehearing motions.<sup>3</sup> Similarly, the Services’ Motion seeks clarification, rather than rehearing or reconsideration of the substance of the Initial Determination.

Because of the nature of the requests in the Owners’ Motion and Services’ Motion, the Judges solicited responses and replies to join the issues. See [Order Permitting Written Response\(s\) to Motions for Rehearing ...](#) (Feb. 21, 2018). Following submission of the papers, the Services and the Copyright Owners reached agreement on some of the items raised in the motions, some of which the Judges adopt. The Judges reviewed all of the requests in the motions, the responses, and the replies and determined that some of the requests are for technical corrections, some are for substantive relief, and some are a conflation of the two. Given the scope of the participants’ issues, the Judges’ resolutions of those issues have resulted in pervasive changes to the regulatory language the Judges promulgated initially.

The Judges conclude that although the moving parties have failed to make even a *prima facie* case for rehearing under the applicable standard, in the interests of enhancing the clarity and administrability of the regulatory terms accompanying the *Phonorecords III* final determination, it is appropriate for the Judges to resolve the issues that the parties have raised. To the extent the Judges’ action could be considered a rehearing under 17 U.S.C. § 803(c)(2), the Judges further resolve these motions on the papers without oral argument.

By this Order, the Judges **GRANT** in part and **DENY** in part the motions of the Copyright Owners and the Services.

## I. Stipulated Changes

The moving parties agree to changes needed for assorted section titles, paragraph numbers, and internal cross-references. These are set forth in the Copyright Owners Response to the Services’ Motion ([Owners’ Response](#)). The Judges agree and incorporate those editorial changes. The Judges decline to adopt one agreement of the parties relating to the definitions of “applicable consideration” and “performance royalties.” The Judges’ reasoning on this compromise is detailed in section II.A below.

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<sup>3</sup> 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 DSTR (Jan. 8, 2008) (*SDARS I Rehearing Order*) (applying federal district court standard under *Fed. R. Civ. P.* 59(e)).

## II. Overlapping Issues

The Copyright Owners and the Services each raised issues with regard to certain regulatory provisions, though their issues were not always identical. While the parties exchanged ideas regarding preferred amendments, they did not always reach agreement. For economy of presentation, the Judges deal with the provisions with shared concerns in this section.

### A. Definitions of Applicable Consideration and Performance Royalties

In a compromise, the parties agreed that the Judges should add the defined term “applicable consideration” to the promulgated regulations and delete the defined term “performance royalties.” Each party included an identical “Attachment A” to its response, including agreed language. With regard to this compromise, the parties “respectfully request that if the Copyright Royalty Judges are inclined to enter one of these changes, but not the other, the applicable party be given the opportunity to submit further written argument addressing the other party’s proposed changes.” Attachment A at 3.

For the reasons detailed below, the Judges include the essence of the definition of “applicable consideration” but decline to delete the definition of “performance royalties.” The Judges deny the parties’ request for further briefing on this resolution.

#### 1. Applicable Consideration

The Copyright Owners note that the definition of Total Cost of Content that the Judges promulgated in the Initial Determination is based on section 385.13(b) of the existing regulations and contains the phrase “which amount shall equal the applicable consideration for such rights at the time such applicable consideration is properly recognized as an expense under GAAP.” Owners’ Motion at 5. The Copyright Owners contend that the term “applicable consideration” is an important term of art that is defined in current section 385.11 but was likely inadvertently omitted from the new regulatory terms. The Copyright Owners note that the definition of applicable consideration was added in *Phonorecords II* to ensure “TCC integrity” and avoid the undermining of the TCC prong. Owners’ Motion at 5. The Copyright Owners propose reinstating the current definition of applicable consideration.

Because of the parties’ negotiated compromise, the Services did not address this issue in their Motion.

The Judges accept that the term “applicable consideration” is a term of art in these proceedings. The Judges note, however, that the term appears only one other time in the extant regulations, *viz.*, in the definition of Total Cost of Content or TCC. Consequently, the Judges specify the meaning of the term “applicable consideration” in the definition of TCC.

#### 2. Performance Royalties

The Services ask that the Judges delete the definition of “performance royalties” noting that it was a defined term that was not used anywhere in the promulgated regulations. After the review of the promulgated regulations, which the Judges undertook both in response to the present motions and *sua sponte*, the Judges determined that the term Performance Royalties could and should be used in section 385.21 describing the necessary steps to calculate applicable royalties.

The Judges, therefore, decline to delete the definition of Performance Royalties, but rather retain the defined term and put it to use in section 385.21.

### **B. Family Plan Definition and Proration**

The Copyright Owners note that the regulatory terms in the *Initial Determination* provide for modifications to the monthly royalty floors for student and family plans and that these modifications are to be prorated for partial calendar months.<sup>4</sup> The proration for family plans states:

A Family plan shall be treated as 1.5 subscribers per month, prorated in the case of a Family plan end user who subscribed for only part of a calendar month.

See Owners' Motion at 6, citing promulgated regulations.

The Copyright Owners assert, and the Services and the Judges agree, that this language appears to create an ambiguity "since family plans allow for more than one end user to make plays, and thus a family plan has *multiple* end users for *one* subscription." Owners' Motion at 6; accord Services' Motion at 8. The Copyright Owners offer an alternative definition stating that family plans are "prorated in the case of a Family plan subscription in effect for only part of a calendar month" to remove this perceived ambiguity. *Id.* at 6-7.

The Judges agree that the proffered amendment relating to the inclusion of the term End User is appropriate and consistent with the record and therefore adopt it.

In their Motion, the Services ask the Judges to strike the word "discounted" from the definition.<sup>5</sup> The Services contend that the use of the word "discounted" is confusing and unnecessary because family plans may be discounted as compared against multiple subscriptions for multiple family members but will be more expensive than a single subscription. Services' Motion at 8.

The Copyright Owners "vigorously disagree" with the Services' proposal to remove the word "discounted" from the definition of Family Plan or Family Account. Owners' Response at 6. The Copyright Owners argue that doing so would "gut the provision and enable the Services to pay Copyright Owners based on 1.5 times an individual subscription rate while charging higher rates to Families." *Id.*

The Copyright Owners contend that the Initial Determination "explicitly bases its allowance of discounts to the mechanical floor for family and student plans on the allegations by the Services that these plans serve customers with low willingness to pay." *Id.* at 7. Although the Copyright Owners aver that the record evidence did not support this conclusion, the Copyright Owners state that

the [Initial] Determination put faith in the Services' unsupported claims that they were targeting low-WTP groups and allowed for discounts to the mechanical floors for these "discounted service users." Now the Services seek to remove the

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<sup>4</sup> The Owners also identify an unrelated typographical error in the Family Plan section of the Initial Determination, which incorrectly states that "Family accounts are to be counted as one subscriber" rather than 1.5 subscribers. Owners' Motion at 7, n.4. The Judges correct this error in the attached amended regulations.

<sup>5</sup> The Judges *sua sponte* eliminate as surplus the phrases "Family Account" and "Student Account" from the definitions of both "Family Plan" and "Student Plan."

“discounted” requirement for which they argued so strenuously, which would allow them to sell subscriptions to these high-value groups even at higher or full rates while paying at a reduced royalty rate to the Copyright Owners.

*Id.*

The Copyright Owners contend that “[a]t a minimum, the 1.5x subscriber Family Plan mechanical floor cap should require that the Services charge no more than 1.5x individual subscription price. If they do, the 1.5x cap should correspondingly go up as well.” *Id.* at 7-8. The Copyright Owners also assert that family plans should be limited to six people, as two of the Services had proposed. The Copyright Owners therefore assert that the Services’ proposed removal of the word “discounted,” if adopted, should be accompanied by the inclusion of a six-user limit on the number of people that could use the plan. *Id.* at 8.

In response, the Services contend, among other things, that the Copyright Owners’ concern is “nonsensical” because the Copyright Owners would benefit if the Services increased prices for Family Plans under a greater-of revenue and TCC rate. [Services’ Reply](#) at 4. The Services also contend that the Copyright Owners’ proposed changes to the Family Plan definition are inconsistent with the Initial Determination and “are nothing more than a transparent effort to undermine the ability of the Services to engage in certain forms of flexible price discrimination.” *Id.*

The Judges reject both parties’ requests to further amend the definition of Family Plan; neither is supported by record evidence.

### **C. Definition of Play**

The Services and the Copyright Owners each identified concerns with the definition of “Play” that the Judges promulgated in the Initial Determination. The Services contend that the phrase “limited download of 30 seconds or more” could be misconstrued as referring to limited downloads of sound recordings that are only 30 seconds or more in duration, rather than a *play* of a limited download of a sound recording that lasts 30 seconds or more. The Services propose to fix this purported ambiguity by replacing the current phrase “limited download of 30 seconds or more” with one that states “Interactive Stream or play of a Limited Download of 30 seconds or more.” Services’ Motion at 7. The Services also contend that the final reference to “30 second” in the current definition should be struck because a track under 30 seconds cannot be played for 30 seconds or more. *Id.* In its entirety the Services’ proposed definition would read:

*Play* means an Interactive Stream or play of a Limited Download of 30 seconds or more, except a track that lasts in its entirety under 30 seconds and the End User streams the entire duration of the track. A Play excludes Fraudulent Streams.

The Copyright Owners also seek a revised definition of the term “Play” to “clarify how the definition would apply to tracks of less than 30 seconds in duration.” Owners’ Response at 5 and Attachment A at 1-2. The Copyright Owners propose as the definition:

*Play* means (1) with respect to a track that lasts in its entirety 30 seconds or more, an Interactive Stream or play of a Limited Download of 30 seconds or more and (2) with respect to a track that lasts in its entirety under 30 seconds, an Interactive Stream or play of a Limited Download of the entire duration of the track. A Play excludes Fraudulent Streams.

Owners' Response, Attachment A at 1-2.

The parties appear to agree on the substance of a revised definition. The Judges find that the substance of each proposed definition is appropriate and adopt it, with some stylistic modifications, as detailed in Amended Attachment A.

#### **D. Definitions of Licensed Activity and Offering**

Both the Copyright Owners and the Services raised issues with the promulgated definitions of the terms "Licensed Activity" and "Offering."

##### **1. Licensed Activity**

The Copyright Owners note that the Initial Determination revises the definitions of "Licensed Activity" and "Offering" to include new subpart B products (physical phonorecords, permanent digital downloads, and ringtones), in addition to interactive streams and limited downloads, which the current regulations already included. The Copyright Owners continue that the Licensed Activity definition also "pulls New Subpart B products into definitions and provisions that are not applicable to New Subpart B products." Owners' Motion at 3. For example, the Copyright Owners note that the term Licensed Activity is used in the definition of "Promotional Offering," but, according to the Copyright Owners, new subpart B products have never been the subject of promotional uses entitled to a zero rate. Thus, according to the Copyright Owners, the new regulations inadvertently alter the approved settlement that the Copyright Owners reached with the Services and the newly published regulations effectuating that settlement. *Id.*

The Copyright Owners contend that the use of the term "Licensed Activity," to the extent that it now inadvertently includes new subpart B products in the definition of "Bundled Subscription Services" (section 385.22 in the regulations promulgated with the Initial Determination) and in the rate calculation methodologies in section 385.21, raises the same ambiguity. The Copyright Owners propose certain revisions to the definition of "Licensed Activity" to address their concerns. *Id.* at 4 and Exhibit A at 4-5.

The Services also identified alleged infirmities in the new "Licensed Activity" definition but contend that the Copyright Owners' proposal would not fix the perceived problems. The Services contend that the Copyright Owners' proposed revised definition of "Licensed Activity" would remain ambiguous because it includes the phrase "Licensed Activity includes but is not limited to." According to the Services, this phrase could be read to include not only new subpart B, but also old subpart C products and services, which, the Services contend, "would render the [revised] definition incompatible with other portions of the regulations." Services' Opposition at 7-8. As an example, the Services point to the "Bundled Subscription Service" prong "in new § 385.29 [*sic.*]"<sup>6</sup>, which refers to Licensed Activity. According to the Services, retaining the phrase "includes but is not limited to" in the "Licensed Activity" definition renders this prong ambiguous and potentially incoherent because the definition of "Bundled Subscription Service"

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<sup>6</sup> There is no section 385.29 in the new regulations. Perhaps the Services are referring to new section 385.22 (Royalty floors for specific types of services) which has a subparagraph (a)(4) dealing with bundled subscription services, which does refer to licensed activity.

also references “products or services **subject to other subparts.**” Services’ Opposition at 8 (emphasis added).

The Services opine that if the “Licensed Activity” definition were left open to include new subpart B and old subpart C products and services, then the addition of “subject to other subparts” would be meaningless. According to the Services, all subparts would be incorporated in Licensed Activity and no such other subparts would exist. *Id.* Accordingly, the Services conclude that the Judges must not have intended to include both new subpart B and old subpart C products and services in the definition of Licensed Activity. Thus, the Services conclude, the Judges should correct this ambiguity by adopting the language the Services proposed in their Motion and reject the Copyright Owners’ proposal. *Id.*

The Services proffered an alternative definition for “Licensed Activity” as “Interactive Streams or Limited Downloads of musical works subject to [s]ubparts C and D of this title (*sic.*), and licensed pursuant to 17 U.S.C. 115.” Services’ Motion at 4. The Copyright Owners oppose (and request that the Judges reject) the Services’ proffered alternative definition because, they contend, it would “result in a change to the way royalties are calculated that is not supported by the evidentiary record and is not consistent with the [Initial] Determination.” Owners’ Response at 3. The Copyright Owners are concerned that the Services’ proffered alternative definition would “carve out direct licensing deals from the definition,” which, the Copyright Owners argue, is “improper and confuses how the defined term Licensed Activity is used in the Regulatory Terms.” *Id.*

The Copyright Owners assert that the use of “licensed activity” in new section 385.21(a) is already expressly limited to licensed activity “covered by this subpart pursuant to 17 U.S.C. 115.” Owners’ Response at 3. The Copyright Owners interpret this limitation to address “any concern about direct deals being overridden by statutory rates.” *Id.* According to the Copyright Owners, “[t]he royalty calculations of subpart C do not work if the limitation is also baked into the definition of Licensed Activity itself because the Step 4 calculation of which royalties are payable for works licensed under the Section 115 compulsory license requires the inclusion of all streaming activity involved in an Offering in order to make the per song/per stream allocation required by Step 4.” *Id.*

In their reply, the Services contend that

[t]he Copyright Owners appear to misunderstand the intent of [the Services’] proposed clarification [to the Licensed Activity definition], surmising that the purpose of the change is ‘to carve out direct licensing deals.’ This is incorrect, and their concern is easily addressed.

Services’ Reply at 2. To address the Copyright Owners’ purported concern with the alternative definition that the Services proposed, the Services offer a second alternative definition: “Interactive Streams or Limited Downloads of musical works subject to subparts C and D of this title, and *licensable* [as opposed to *licensed*, per the Services’ initial proffered alternative definition] pursuant to 17 U.S.C. 115.” *Id.* at 2-3.

Based on the Services’ Motion and the [Owners’ Reply](#), it appears that neither party would interpret the definition of “Licensed Activity” to impose a royalty obligation for activities that are not licensed or licensable under section 115, either under the compulsory license or a

directly negotiated license. Therefore, the Judges find that the concerns the parties raise are purely speculative and not compelled by evidence in the record in this proceeding. Nonetheless, for other reasons described below, the Judges amend the “Licensed Activity” definition.

In their reply, the Copyright Owners observe that the Services do not oppose removing new subpart B products from the “Licensed Activity” definition. Owners’ Reply at 1. The Copyright Owners, however, oppose the additional change the Services propose (*i.e.*, removal of the phrase “includes but is not limited to”) because they contend the argument the Services make in support of removing it makes no sense. *Id.* With regard to the “includes but is not limited to” language, the Judges agree with the Services’ logic. The Judges will excise that phrase from the definition.

With regard to the inadvertent inclusion of new subpart B activities where they should be excluded, the Judges have modified the language of the definition. Section 115 of the Copyright Act establishes a compulsory license for uses that are exceptions to a copyright owner’s exclusive rights to make and distribute phonorecords of their musical works. Production and distribution of physical phonorecords, permanent digital downloads, and ringtones are subject to the section 115 compulsory license and are, therefore, licensed activity, albeit an activity different in nature from digital transmissions. To resolve the issue, the Judges amend the definition of “Licensed Activity” by applying a different interpretation of the term depending upon its usage: Licensed Activity, as used in subpart B refers only to subpart B uses and as used in subparts C and D refers only to subparts C and D uses.

## **2. Offering**

The Copyright Owners raise the same concern with respect to the term Offering to the extent it inadvertently includes new subpart B products in the definition of “Relevant Page” (which is used in the “Service Revenue” definition and relates to interactive streaming services). *Id.* at 3-4.

The Services complain that the definition of “Offering” (“activity requiring a license under 17 USC 115”) in the Initial Determination is vague in light of language in § 385.1(c) regarding direct licensing and § 385.20(b) (“[n]either this subpart nor the act of obtaining a license under 17 U.S.C. 115 is intended to express or imply any conclusion as to the circumstances in which any of the exclusive rights of a copyright owner are implicated or a license, including a compulsory license pursuant to 17 U.S.C. 115, must be obtained.”). Services’ Motion at 4.

Moreover, the Services “do not believe the Judges intended to include revenue related to the sale of physical phonorecords in the calculation of royalties under subpart C. However, as written, both the definitions of ‘Relevant Page’ and ‘Service Revenue’ reference the defined term ‘Offering,’ which incorporates ‘physical and general’ deliveries.” *Id.* at 5. According to the Services, “[t]his leaves open the possibility that ad revenue derived from webpages for physical phonorecord sales could be included in Subpart C revenue calculations.” *Id.* The Services aver that “[b]ecause a separate royalty rate exists under Subpart B for physical phonorecords, and because the terms Service Revenue and Relevant Page are only used in the calculation of Subpart C royalties...the inclusion of [the word] ‘physical’ in the definition of Offering is an apparent error.” *Id.*

The Copyright Owners concur that “former Subpart A products (‘physical phonorecords, Permanent Digital Downloads, Ringtones’) should not be included in the definition of Offering.” Owners’ Response at 3. The Copyright Owners object to the revised definition of “Offering” that the Services proffer, however, asserting that it raises some of the same concerns that the Copyright Owners raised with respect to the Services’ proffered definition of “Licensed Activity” (discussed above). *Id.* at 3.

The Copyright Owners also complain that the Services’ proffered definition of “Offering” would result in a change in the way royalties are calculated that is not supported by the evidentiary record, is inconsistent with the Initial Determination, and would be confusing. *Id.* at 4. The Copyright Owners stress that, like Licensed Activity, Offering is a part of the determination of the payable royalty pool in § 385.21 and therefore must not be limited only to activity for which a compulsory license has been obtained. The concern the Copyright Owners raise relates to direct licenses. According to the Copyright Owners,

[w]here a Service provides a subscription streaming service to End Users, and a portion of the musical works streamed via this service are [*sic.*] licensed under direct deals, the compulsory per work royalty cannot be computed unless the payable royalty pool first includes all works so that the per work royalty payable for works licensed under the compulsory license can be properly allocated.

Owners’ Response at 4.

The Copyright Owners proffer their own definition of “Offering” (*i.e.*, “Offering means a Service’s engagement in Licensed Activity.”). *Id.* at 4, n.5.

The Judges accept the parties’ agreement that the definition of “Offering” should not include references to physical phonorecords and other former subpart A products. With the Judges’ changes to the definition of “Licensed Activity,” however, the Copyright Owners’ proffered definition does not address this issue. The Judges therefore amend the definition of “Offering” to clarify that an offering is a streamed digital product subject to the regulations in subparts C and D.

#### **E. Locker Service provisions**

The Services note that the definition of “Locker Service” in the regulations the Judges promulgated contains a typographical error and is “missing one or more clauses.” Services’ Motion at 8.<sup>7</sup> The Copyright Owners “agree with fixing the typographical error in this definition.”<sup>8</sup> The Judges also agree; correction of the typographical error is noncontroversial.

The Copyright Owners raised other, more substantive issues, which the Judges discuss in section III.D

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<sup>7</sup> In their proposed amendment to the definition of “Locker Service,” the Services proffer a change to correct the typographical error but do not add or identify any allegedly “missing” clauses. *See* Services’ Motion, Att. A 4.

<sup>8</sup> The Copyright Owners are presumably referring to missing punctuation after “Ringtone” and the change in case of the following word.

### III. Copyright Owners' Proposed Changes

In their Motion the Copyright Owners request clarification or correction in ten areas. The areas not analyzed in the foregoing discussion of overlapping issues are: (1) definitions of Service and Offering Service; (2) omission of the two subpart C subscriber-based all-in royalty floors; (3) definitions of Locker Service and Purchased Content Locker Service; (4) definitions of Promotional Offering and Free Trial Offering; and (5) definition of Service Revenue from Bundle Offerings.

#### A. Definitions of Service and Offering Service

The Copyright Owners note that the term Service is used often in the Regulatory Terms but is not defined, while the term Offering Service is defined but not used in the Regulatory Terms. Owners' Motion at 2. According to the Copyright Owners, the definition of "Offering Service" is derived from the definition of "Service Provider" in section 385.11 of the current regulations. The Copyright Owners continue, however, that in the promulgated regulatory terms, the definition has been expanded to include the licensees (*e.g.*, record labels) of permanent downloads, physical phonorecords and ringtones. The Copyright Owners opine that because Offering Service is not a term that is used in the new subpart B (formerly subpart A), it is not necessary for the definition of "Offering Service" to be revised to include new subpart B licensees. Owners' Motion at 2. The Copyright Owners contend that the term "Licensee," which is a separately defined term, suffices to provide the terms for the new subpart B licensees. The Copyright Owners continue that "defining New subpart B licensees as Offering Services as well as Licensees is problematic, as it pulls the New subpart B licensees into other provisions that are intended to apply to interactive streaming services rather than New subpart B licensees." *Id.* To remedy these concerns, the Copyright Owners propose that the Judges change the defined term Offering Service to Service and delete subparagraph (1) of that definition covering the new subpart B licensees (who, according to the Copyright Owners, are already defined as Licensees). *Id.*

The Services do not object to the changes the Copyright Owners propose. *See* Owners' Reply at 1.

The Judges acknowledge the inconsistencies in the definitions of "Licensee" and "Offering Service" in the promulgated regulations. To resolve the inherent ambiguity, the Judges omit the term "Offering Service," opting for the clearer term "Service" and limiting that term to entities engaged in using musical works in subparts C and D configurations.

#### B. Definition of Student Plan<sup>9</sup>

The Copyright Owners state that the Initial Determination purports to adopt the Services' proposal (as articulated by Spotify) for student plans. However, the definition in the regulatory terms of "Student Plan" does not include the language that Spotify (or the other Services) proposed and does not define what constitutes a student. Owners' Motion at 5. The Copyright Owners opine that

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<sup>9</sup> The term "student account" is not used in the regulations as promulgated. The Judges, therefore, delete the surplus verbiage.

[i]t appears clear that the [Initial] Determination intended to provide a discounted mechanical floor for subscription plans offered to college students, as articulated by the Services, who provided generally similar definitions of their requested “student account,” namely “an individual subscription that meets at least the following criteria: the individual is enrolled in at least one course at a college geographically located in the United States.”

Owners’ Motion at 5-6. The Copyright Owners assert that the definition in the Initial Determination (“a discounted subscription available on a limited basis by a Service”) “does not appear to be what the [Initial] Determination intended. The language might wrongly imply that family plans are also student plans, and that anyone can get a student plan, whether or not a student.” *Id.* at 6. The Copyright Owners assert that using the language that Spotify and the other Services proposed more faithfully implements what was intended in the Initial Determination. *Id.*

The Services oppose changing the definition of “Student Plan” in the manner that the Copyright Owners propose. The Services suggest that to add additional clarity the Judges could add the words “to students” in the definition so that it would read “a discounted subscription available to students on a limited basis by a Service.” Opposition at 10. In their Reply, the Copyright Owners contend that the scope of a student plan must be defined and limiting the definition of “Student Plan” to college students is consistent with the Services’ argument that discounted plans should be directed toward groups with a low willingness to pay (which includes college students). Owners’ Reply at 1-2 & n.3.

The Judges agree with the Services that inserting the words “to students” in the “Student Plan” definition will provide sufficient clarity to assure that a student plan is one that is made available to students. The Judges find that further clarity or limitation of the scope of the definition is unnecessary and unsupported by the current record. The Judges leave it to each Service to define, in good faith, the term “student” in its terms of service, while being mindful that the rationale behind a student plan should be “aimed at monetizing a segment of the market with a low WTP (or ability to pay) that might not otherwise subscribe at all” with the ultimate goal of getting those subscribers “into the ‘funnel’ for full-price subscriptions.” Initial Determination at 92.

### **C. Omission of Royalty Floors for Paid Locker Services and Limited Offerings**

In the Initial Determination, the Judges noted that “the existing subscriber-based royalty floors shall remain in effect during the new rate period.” Initial Determination at 1. In their Motion, the Copyright Owners note that “[t]wo of the five former subpart C offerings [have] subscriber-based royalty floors: paid locker services (17 cents all-in) and limited offerings (18 cents all-in). However, these royalty floors were omitted from the Regulatory Terms, although the [Initial] Determination does not hold that they should be omitted. It thus appears an oversight....” Owners’ Motion at 7.

In response, the Services contend that the Initial Determination is clear that “it is only the subscriber-based mechanical-only royalty *floors*, *i.e.*, the per-subscriber rates applied *after* the deduction of performance rights royalty payments from the total royalty pool, that the Judges intended to remain in effect, *not* the per-subscriber minima.” Services’ Response at 6. According to the Services, “there have never been mechanical-only floors for locker services and

limited offerings.... As a result, there are no floors to roll over.” *Id.* at 6-7. The Services aver that the Copyright Owners do not propose to add a mechanical-only floor for locker services and limited offerings but rather “propose to reinsert the per-subscriber minima for those service categories that applied *prior* to the deduction of performance royalties.” *Id.* at 7. The Services concede that “Pandora, Amazon, and Spotify did propose maintaining the existing per-subscriber minima for limited offerings and locker services as part of their proposals, but the Judges did not adopt their proposals.” *Id.* According to the Services,

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. The Judges should reject this cherry-picking and the unnecessary and confusing conflation of the analytically distinct concepts of floor fees (which have never applied to limited offerings or paid locker services) and minima (which have).

*Id.*

It their reply, the Copyright Owners dispute the Services’ contention that there is a distinction between “minima” and “floors.” Owners’ Reply at 2. The Copyright Owners contend that the terms “floor” and “minimum” are synonyms and “the general use of the term ‘mechanical-only floor’ accurately signals that the term ‘floor’ alone encompasses more than mechanical-only floors.” *Id.* at n.5. According to the Copyright Owners, the title of the current regulation that created these floors calls them “subscriber-based royalty floors” as do the rate proposals that the Services submitted. The Copyright Owners contend that there is nothing in the Initial Determination indicating an intention to “omit these floors (and neither Amazon, Spotify [n]or Pandora requested removal of these floors in their rate proposals).” *Id.* at 2.

In the present proceeding, the Judges did not set a royalty floor for Paid Locker Services or Limited Offerings. The Copyright Owners seek to reintroduce the minimum royalties for Paid Locker Services (\$.017 per subscriber per month) and Limited Offerings (\$.18 per subscriber per month) that applied over the prior rate period. The Copyright Owners argue that the Judges’ failure to carry over per subscriber minimums or floors was clearly inadvertent but they provide no support for that assertion, except to point out that the Judges continued royalty floors for certain other services but not for Paid Locker Services and Limited Offerings.

In setting the rates and terms for the service offerings at issue, the Judges weighed the evidence in the record before them and set the rates and terms that they found were warranted for those services. Based on the record, the Judges revamped the entire mechanical rate structure. In that process, they attempted to anticipate negative consequences that might result from the structural overhaul. For subscriber-based services, the Judges introduced an external rate comparison factor (TCC). The Judges addressed the Copyright Owners’ concerns regarding revenue manipulation in a percent-of-revenue rate structure. Further, the Judges acknowledged, without fully accepting, the potential for consolidation or integration of sectors of the music industry that might result in manipulation of the TCC factor. The Judges accepted mechanical floors for those licenses that enjoyed mechanical floors under the previous rate scheme as an additional backstop against this unknown potential.

Paid Locker Services and Limited Offerings are licensed uses that are of a nature totally different from other streaming services. The existing regulations treated them differently and

afforded them an alternative minimum royalty. The existing minimum for these services was not a mechanical floor. The Judges adopt the reasoning of the Services and incorporate it as an enhanced explication of their reasoning in the Initial Determination. The Judges' choice not to establish a minimum for Paid Locker Services and Limited Offerings was not inadvertent; it was a feature of the regulatory overhaul so necessary for these mechanical licenses.

**D. Definitions of Locker Service and Purchased Content Locker Service**

According to the Copyright Owners, beyond the typographical error, “additional points ... need to be clarified in [the Locker Service] definition, and in the related definition of Purchased Content Locker Service.” Owners' Response at 6.

The Copyright Owners note that the Initial Determination distinguishes between the two types of locker services: paid locker services and purchased content locker services, and simplifies the definitions of *Locker Service*, *Paid Locker Service*, and *Purchased Content Locker Service*. Owners' Motion at 7, citing Initial Determination at 77, 92. According to the Copyright Owners, two apparently unintentional ambiguities now exist in the regulatory terms that merit clarification. *Id.* The Copyright Owners note that the promulgated regulatory terms contain language that “could be viewed as inadvertently conflating paid locker services with regular portable streaming service offerings. Since the two offerings have different subscriber-based royalty floors, the distinction is material.” *Id.* at 8.

According to the Copyright Owners:

What distinguishes a paid locker service from a standard subscription service is that the paid locker service streams only works that the service has reasonably determined have been purchased by or are otherwise in possession of the end user. If a user can stream all works, even those that he or she did not already possess, that is a standard subscription service, not a paid locker service, and is properly subject to the higher subscriber-based royalty floor. The new definition of *Locker Service* omits language that makes this distinction which the Copyright Owners believe was not intended by the Judges.

*Id.*

According to the Copyright Owners, a similar concept appears in the new “Purchased Content Locker Service” definition, but not in the new “Paid Locker Service” or the new general “Locker Service” definition. *Id.*

The Copyright Owners propose the following revised definition:

*Locker Service* means an Offering providing digital access to sound recordings of musical works in the form of Interactive Streams, Permanent Digital Downloads, Restricted Downloads or Ringtones where the Service has reasonably determined that phonorecords of the applicable sound recordings have been purchased by the End User or are otherwise in the possession of the End User prior to the End User's first request to access such sound recordings by means of the Service, but does not mean any part of a Service's products otherwise meeting this definition, but as to which the Service has not obtained a section 115 license.

[Owners' Proposed Order Granting Motion for Clarification](#) at 4.

The Judges agree that the additional language the Copyright Owners suggest is supported by the record in this proceeding and necessary to the completeness and clarity of the definition of “Locker Service.”

### **E. Definitions of Promotional Offering and Free Trial Offering**

The Copyright Owners note that the Initial Determination “accept[s] the agreed definitions in the extant regulations and the agreed zero rate for promotional streams.” Owners’ Motion at 9. Nevertheless, according to the Copyright Owners, the new definition of “Promotional Offering” “introduces material changes to the agreed definition in the extant regulations, and thus appears inadvertent.” *Id.* The Copyright Owners further assert that “[t]he definitional change would also sweep in New Subpart B products and have the unintentional consequence of changing the New Subpart B settlement and recently published regulations effectuating that settlement.” *Id.* at 9-10. Moreover, the Copyright Owners opine that the “Promotional Offering” definition also introduces “an ambiguity by including promotion by a label or Service for which the label or Service receives no consideration other than ‘in-kind promotional consideration’, which is undefined and unclear.” *Id.* at 10.

The Copyright Owners contend that “the maintenance of the existing promotional offering provision at 37 CFR § 385.14 [Promotional royalty rate] is appropriate for the holding in the [Initial] Determination to maintain the existing terms and associated zero rate.” *Id.* According to the Copyright Owners, “the modification of the definition of promotional activities [sic], while maintaining the zero rate, could lead to a mistaken assumption that there was an unintentional expansion of the scope of activities subject to a zero rate, and would conflict with the accepted settlement of the parties on New Subpart B.” *Id.*<sup>10</sup>

The Copyright Owners assert that

the intention of the [Initial] Determination to carry forward the zero royalty rate for promotional and free trial streams “as they are defined in the regulations” would not be achieved by creating the separate and new definitions....The existing § 385.14 language...sets forth the complete set of (and important limitations on) the promotional activities for which a zero rate might apply (and includes 30-day free trial periods for all types of interactive streaming and limited download offerings), carrying forward the promotional terms that exist, which is the [Initial] Determination’s stated intent.

*Id.* at 10-11. To remedy their concerns, the Copyright Owners propose to replace the new definitions of “Promotional Offering” and “Free Trial Offering” with a definition of Promotional Offering “tied to a Promotional Royalty Rate that carries forward the terms of the existing Section 385.14 regulation into the new Section 385.31.” *Id.* at 11.<sup>11</sup>

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<sup>10</sup> The Copyright Owners also state that retaining the terms of the existing § 385.14 as the new § 385.31 would allow for the removal of the “Free Trial Offering” definition because “all interactive streaming offerings are covered under § 385.14, which also covers free trial offerings.” Owners’ Motion at 10.

<sup>11</sup> The Copyright Owners also argue that retaining the existing section 385.14 would solve the perceived problem of a lack of a definition of “in-kind promotional consideration” in the new “Promotional Offering” definition. Owners’ Motion at 11 n.5. While advocating for its adoption, the Owners acknowledge that existing section 385.14, which

The Services oppose this proposal, arguing that it “misunderstands both the reasoning of the [Initial] Determination and the Judges’ stated goal of simplifying the regulations.” Services’ Opposition at 8. The Services opine that the Judges created new subpart D because there is a basis to distinguish promotional or other non-revenue producing offerings from revenue-producing offerings. *Id.* at 9. According to the Services, “[t]his finding expressly removes zero-rate products from old Subpart C, a change that can hardly be ‘inadvertent.’” *Id.* The Services assert that “[r]everting to the complex and ‘admittedly long-winded’ old Subpart C regulations is inconsistent with the [Initial] Determination.” *Id.* The Services contend that the language in the “Promotional Offering” definition is “nearly identical to old § 385.14(a)(1)(i), with minor wording changes consistent with the Judges’ goal of redrafting the regulations in ‘simple English.’” *Id.* The Services argue that this “welcome improvement” should not fall victim to the Copyright Owners’ “generalized claims of harm.” *Id.* The Services further contend that the Copyright Owners’ assertion that the new regulations conflict with the new subpart B and expand the scope of promotional offerings “lacks any basis.” *Id.* Other than correcting a typographical error in the “Promotional Offering” definition, the Services argue that the Judges should reject the Owners’ Motion on this point.<sup>12</sup>

In their reply, the Copyright Owners accuse the Services of trying to “exploit inadvertent definitional implications in the [Initial] Determination, contradicting their own proposals in effort to snare a ‘freebie.’” Owners’ Reply at 3. The Copyright Owners assert that the Services concede that the Judges expressed a clear intent not to change the extant regulations on promotional streams, but that the Services inconsistently and disingenuously argue that the new “Promotional Offering” definition is nearly identical to extant § 385.14 with minor word changes. According to the Copyright Owners, no such identity exists. *Id.* In addition to merely restating the arguments in support of their proffered changes to the “Promotional Offering” definition in their Motion, the Copyright Owners also point out that there were many limitations on promotional offerings in the extant regulations that are absent from the new definition, “significantly changing a definition regarding zero-rate activities that the Judges explicitly intended to not change.” *Id.*

As a preliminary matter, the Judges did not intend to change the substance of the regulations dealing with promotional streams and stated as much in the Initial Determination. Initial Determination at 93 (“No party in this proceeding offered evidence or argument against continuing the zero royalty rate for promotional streams, as they are defined in the regulations. The Judges accept the agreed definition in the extant regulations and the agreed zero rate for promotional streams.”). It was in that spirit that the Judges promulgated a new definition of “Promotional Offering” that was intended to codify and simplify the prior definition of “Promotional royalty rate” (extant regulation section 385.11) and the related provision of Promotional royalty rate in extant section 385.14.

In the amended regulations in Attachment A to this Order, the Judges opt to include the necessary operative language from former section 385.14 in the definition of “Promotional

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fills four pages of regulatory text in the CFR, is “long-winded” and could perhaps stand the insertion of an additional clause to enhance clarity. Owners’ Motion at 10, 11 n.5.

<sup>12</sup> The Judges agree with the Services that the “Promotional Offering” definition, which states in relevant part “neither the Record Company nor the Service receives no consideration” should not include the underlined “no.”

Offering,” but decline to incorporate all of the (almost) four printed pages of that former section. The language in the former section expressly provides: “[t]his section is based on an understanding of industry practices and market conditions at the time of its development, among other things. The terms of this section shall be subject to de novo review and consideration (or elimination altogether) in future proceedings before the Copyright Royalty Judges.” 37 C.F.R. 385.14(a)(4) (2017).<sup>13</sup> Based upon the record in the present proceeding, the Judges have considered section 385.14 and have determined that the clarifications added to the definition of “Promotional Offering” in this Order are sufficient and are the limits of what the record supports.

#### **F. Definition of Service Revenue from Bundle Offerings**

The Copyright Owners assert that the definition of “Service Revenue” in the regulatory terms as it relates to bundles (which are not explicitly discussed in the Initial Determination) was not intended and warrants revision to be consistent with the Determination and the Judges’ holdings in *Web IV* and the *SDARS III* proceedings. Owners’ Motion at 11. The Copyright Owners refer specifically to subparagraph 5 of the “Service Revenue” definition, which addresses “instances in which a Service provides an Offering to End Users as part of the same transaction with one or more other products or services that are not Licensed Activities.” *Id.* The Copyright Owners contend that the adoption of this definition was not discussed in the Initial Determination and “appears inadvertent and is inconsistent with reasoning of the Judges on fairness as explained in both *Web IV* and *SDARS III.*” *Id.*

The Copyright Owners note that under this definition, for a bundle that includes an interactive streaming service plus one other item, the attributed price for streaming would be the total price minus the “standalone published” price of the other item. According to the Copyright Owners, the Judges “explicitly discussed the unfairness of this precise approach in *Web IV.*” *Id.* (referring to the Judges’ hypothetical example of a vendor selling one ice cream cone for \$1 and two cones for \$1.06 and the purported absurdity of concluding that the true market price of an ice cream cone is the incremental six cents). The Copyright Owners contend that it was undisputed

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<sup>13</sup> At the hearing in this proceeding, the Judges made clear that they were determining *de novo* both the royalty rates and the regulatory terms.

The current regulations are fragmented tremendously because there are five or six different types of Services that are dealt with separately. There are also ... regulations about promotional uses and free trials. And the current regulations include that de novo determination provision and lots and lots of definitions.

Just because there are current regulations in subparts B and C does not mean that they will automatically roll over, because this is a contested proceeding. Those were put in by agreement.

And if we don't have evidence to adopt new regulations, new terms, then we will be unable to complete this. It is not enough for us to set the rates. It is not enough for us to determine the rate structure and what goes into that. The regulations have a full complement of terms and those will be decided de novo, the same as the rates.

So we need evidence. ... [A]nd, I mean, something other than arguments of counsel in the proposed findings and conclusions, just so you are aware.

04/05/18 Tr. at 5195-96 (Barnett, J.). A thorough review of the parties’ written submissions, the transcripts of the proceeding, and the parties’ proposed findings and conclusions revealed no evidence supporting wholesale adoption of section 385.14. Some participants included the language of former section 385.14 in their proposed terms, but without analysis or citation to the record.

at the hearing that services have allocated zero revenues from bundles for royalty purposes despite generating massive bundle revenues while sending billions of streams to millions of users. *Id.* The Copyright Owners argue that this is the type of accounting that was considered absurd in *Web IV*. *Id.* at 13. The Copyright Owners further note that in *SDARS III*, the Judges disallowed any exclusion from bundle revenue, counting total bundle revenue towards the royalty revenue base. *Id.*

To address their concerns, the Copyright Owners proffer an alternative “Service Revenue” definition that would state that the revenue attributed to a particular offering in a bundle is the standalone price of the offering (or comparables). *Id.*

The Services counter that “[f]ar from being unintentional or inadvertent (as the Copyright Owners suggest), the Judges’ definition of “Service Revenue” was based on the record, thoroughly analyzed by the Judges, and plainly deliberate.” Services’ Opposition at 3. The Services contend that the Copyright Owners’ proffered definition of “Service Revenue,” if adopted, would lead to “unpredictable and potentially incongruous results.” *Id.* The Services note that the Copyright Owners never proposed any definition of “Service Revenue” during the proceeding and that their “late-proposed” definition violates the basic requirements that a determination of the Judges be supported by the written record. *Id.* at 4-5. The Services contend that the Copyright Owners’ proffered definition of “Service Revenue” is contrary to the Judges’ endorsement of the classic price discrimination enabled by bundling strategies. *Id.* at 5. The Services also dispute the Copyright Owners’ contention that the definition that the Judges promulgated is inconsistent with the Judges’ holdings in *Web IV* and in *SDARS I* and *III*. *Id.* In particular, the Services assert that those proceedings “involved different circumstances, different economics, different rights, different licenses, and (in the case of *Web IV*) a different legal standard” than the current proceeding and therefore are improper comparisons for evaluating the “Service Revenue” definition in the current proceeding. *Id.*

In their reply, the Copyright Owners contend that the Initial Determination “contains no reasoning to justify the extant definition, which appears to have been inadvertently included and which conflicts deeply with the Judges’ general reasoning.” Owners’ Reply at 4. The Copyright Owners note that there is an “economic indeterminacy problem inherent in bundling” which they “repeatedly called out” throughout the hearing, “objecting to this precise definition that allowed such absurd results.” *Id.* at 5. The Copyright Owners argue that “the Services must bear the burden of providing evidence that might mitigate the acknowledged economic indeterminacy problem inherent in bundling” and they have failed to do so. *Id.* As an alternative to the definition that the Copyright Owners proffer, the Copyright Owners contend that “the Judges can at least use the Services’ own market price (or comparables) for the music product for bundle allocation purposes.” *Id.* According to the Copyright Owners, “less than this is not an economically justifiable definition.” *Id.*

The parties have presented the Judges with diametrically-opposed approaches to valuing bundle revenues. Neither party presented evidence adequate to support the approach it advocates. The 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. However, the “‘economic indeterminacy’ problem inherent in bundling” is common to all three proceedings. *SDARS III* at 113. The Judges, therefore, are informed in their approach to this problem by those prior rulings. In *SDARS III*, the Judges noted that “bundling was undertaken to increase Sirius XM’s revenues and it would be reasonable to assume that Sirius XM has information relevant to the economic allocation of the bundled revenue.” *Id.* The Judges determined that Sirius XM, as the party in possession of the relevant information, bore the burden of “providing evidence that might mitigate the acknowledged ‘economic indeterminacy’ problem inherent in bundling.” *Id.* In the absence of that evidence, the Judges did not accept Sirius XM’s proposal.

In the present case it is the Services—not the Copyright Owners—that are in a position to provide evidence of how they price bundles and value the component parts thereof. *See, e.g., Initial Determination* at 21-22 (and record citations therein) (discussing [REDACTED]). Consequently the Services, like Sirius XM, bore the burden of providing evidence concerning the proper economic allocation of bundled revenue. Having failed to do so, the Judges are unable to reduce the bundled revenue (for purposes computing the revenue base for royalty calculations) as proposed by the Services.

By default, that means that the Judges must adopt an approach to valuing bundled revenue that is in line with what the Copyright Owners have proposed. That is, licensees must use either the revenue for the entire bundle, or the standalone price for the music component(s), for purposes of computing the revenue base upon which they calculate their section 115 royalties. The Judges evaluate these two approaches with reference to the statutory factors set forth in section 801(b)(1).

Both approaches could potentially further the goal of maximizing the availability of works to the public, but in different ways. The former approach (including the entire price of the bundle in the revenue base) would result in higher royalties to copyright owners, thus providing greater economic incentives to songwriters and publishers. The latter approach (including the standalone price of the music component of the bundle in the revenue base), however, better accommodates beneficial price discrimination by services, which increases access to music services by customers with low willingness to pay.

The former approach is in tension with the goals set forth in subparagraph (B) of section 801(b)(1). Including the entire price of the bundle in the revenue base provides a potential windfall (*i.e., unfair return*) to Copyright Owners and imposes a potentially unjustified burden on (and thereby denies a fair income to) the Services. By contrast the latter approach, by tying royalties to the Copyright Owner’s contribution to the bundle (albeit indeterminate), better serves the goals of section 801(b)(1)(B). For the same reasons, the latter approach better reflects the relative roles of Copyright Owners and Services as required by section 801(b)(1)(C).

Finally, the Judges find that by avoiding imposing a potentially unjustified burden on Services, the latter approach minimizes any disruptive impact on the structure of the industries involved, consonant with the goal of section 801(b)(1)(D). For the foregoing reasons the Judges will adopt the latter approach: Services 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.

As a consequence of the Judges' adoption of the foregoing approach, the Judges will also dispense with the separate royalty floor for Bundled Service Offerings. Because the applicable revenue will be the same as though the bundle were a standalone music offering, the royalty floor will be the royalty floor that would apply to the music component of the bundle if it were offered on a standalone basis.

#### **IV. Services' Proposed Changes**

The Services' Motion is broken into two separate parts: (1) typographical and clerical errors and (2) definitional issues. In the first section, the Services identify four categories of "apparent errors and illustrative examples" that they recommend the Judges fix. Services' Motion at 2-3. The Services cite outdated section headings, incorrectly numbered subsection paragraphs, incomplete or incorrect cross references, and other typographical corrections. In the second section, the Services identify three categories of "definitional issues" that they aver need addressing, *viz.*, defined terms that are not used, capitalized terms that are used but not defined, and unclear language in certain definitions. *Id.* at 3-4. The Judges acknowledge the nonsubstantive errors in the Initial Determination and incorporate corrections in the amended regulatory language detailed in Attachment A to this Order.

Most of the Services' Motion deals with the second section, in which the Services analyze purported issues that they have identified with certain terms that are defined or used in the Initial Determination. In addition to the issues the Judges address in section II of this Order, the Services assert issues relating to the promulgated definitions of fraudulent stream and a purported ambiguity relating to the royalty due date. *Id.* at 4-10.

##### **A. Fraudulent Stream Definition**

In the Initial Determination the Judges defined the term Fraudulent Stream as:

a Stream that has not been initiated or requested by a human user. If a single End User plays the same track more than 50 straight times, all plays after play 50 shall be deemed Fraudulent Streams.

The Services contend that the definition "should be clarified to take into account both 'Streams' and 'Plays' (using the defined term 'Play' rather than the undefined 'play') as the latter also includes streams of Limited Downloads ...." Services' Motion at 8.<sup>14</sup> The Services' proposed revised definition would read: *Fraudulent Stream* means a Stream or a Play that has not been initiated or requested by a human user. If a single End User plays the same track more than 50 straight times, all Plays after Play 50 shall be deemed Fraudulent Streams.

*See* Services' Motion, Attach. A at 3.

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<sup>14</sup> Limited Downloads are not streamed; they are downloaded, then played. The Judges assume that the Services meant "plays" of Limited Downloads.

In response, the Copyright Owners state that the Services' proposed edit to the definition of Fraudulent Stream, *i.e.*, using Play in the definition instead of Stream, would capture as fraudulent,

plays of limited downloads as well as streams. This raises an issue that should also be clarified in the Regulatory Terms. Does 50 "straight" plays include a situation where a track is played by limited download 50 straight times, even where there may be interactive streams of other tracks interspersed?

Owners' Response at 5.

The Copyright Owners also note that the Services' proposed definition "invites [the Services] to unilaterally exercise discretion in making a determination as to whether the 'Play' was 'not initiated or requested by a human user' and hence omit all such uses from royalty calculations." *Id.* To address these perceived concerns with the Services' proposed revised definition, the Copyright Owners "submit that, in addition to the edit proposed by the Services to Fraudulent Stream, the Recordkeeping section [of the regulations should] be clarified to ensure that records are kept of Fraudulent Streams that are omitted from royalty calculations in the same way as records of other 'zero rate' uses." *Id.* at 6.

The Services counter that there is no basis in the record for imposing the Copyright Owners' proposed new recordkeeping requirement and, as a procedural matter, "it is improper to propose new record-keeping requirements for the first time in opposition to a motion for rehearing." Services' Reply at 1. The Services also contend that the record-keeping change that the Copyright Owners propose is unnecessary because the Services have no financial incentive to over- or under-count fraudulent streams. *Id.* at 2.

The Judges conclude that, as plays of Limited Downloads are included in the definition of "Play," fraudulent plays of Limited Downloads should be excluded from the definition of "Play" just as fraudulent streams are excluded. The Judges, however, reject the Service's specific proposal. Adding the term "Play" to the definition of "Fraudulent Stream" creates a circularity, because the definition of "Play" expressly excludes any "Fraudulent Stream." The Judges will, instead, eliminate the definition of "Fraudulent Stream" (which is only used in the definition of "Play"), and include the elements of the definition of "Fraudulent Stream" in the definition of "Play."

The Judges acknowledge the Copyright Owners' request that the Judges clarify whether plays of Limited Downloads interspersed with streams of the same work count as plays of the same track. The regulation, as presented in Attachment A, does not distinguish between streams and plays of Limited Downloads for purposes of counting plays of the same track. No clarification is necessary.

The Judges do not find sufficient persuasive evidence in the present record to support imposing the recordkeeping requirement the Copyright Owners propose. Therefore, the Judges will adopt the definition as the Services propose and decline to adopt the Copyright Owners' proposed recordkeeping requirement with respect to fraudulent streams.

## **B. Ambiguity in Due Date/Late Payments Provision**

The Services raise two concerns with the promulgated late payments section, which states:

A Licensee shall pay a late fee of 1.5% per month, or the highest lawful rate, whichever is lower, for any payment received by the Copyright Owner after the due date. Late fees shall accrue from the due date until payment is received by the Copyright Owner.

Promulgated section 385.3.

The Services contend that as currently drafted, the “due date” for payments is not clear. The Services reason that the new late-fee language mirrors the late fee language in 37 C.F.R. § 385.4 of the current subpart A regulations, “except it deletes the provision, appearing in the current regulations, which provides that the ‘due date’ is that ‘set forth in § 210.16(g)(1).”

The Copyright Owners object to the cross-reference to 37 C.F.R. § 210.16(g)(1) that the Services proffer as “unnecessary and confusing.” Owners’ Response at 9. The Copyright Owners state that part 210 applies to all compulsory royalty payments and addresses due dates and the payment of agents of copyright owners. According to the Copyright Owners, “selectively invoking one portion of Part 210 for Section 385.3 and not for all of the other royalty provisions to which Part 210 equally applies (and only invoking part but not all of Part 210) could be interpreted as excluding application of other parts of Part 210.” *Id.*

The Services reply that the reference to section 210.16(g)(1) they propose would remove the possibility of disputes arising or late fees being unjustly assessed before monthly payments and annual true-up payments are actually due. Services’ Reply at 5.

No party concerned with a section 115 license need resort to regulatory language. The statute provides: “Royalty payments shall be made on or before the twentieth day of each month and shall include all royalties for the month next preceding.” 17 U.S.C. § 115(c)(5). With regard to the particularities of tendering or receiving royalty payments, the parties must refer to part 210 of title 37, C.F.R. The regulations in part 210 are not the Judges’ regulations. Part 210 is promulgated by the Register of Copyrights. The Judges will not refer to any specific section or subsection of part 210 because the provisions of part 210 might change, rendering a specific citation erroneous. The Judges amend promulgated section 385.3 to include citation to the statute and to the Register’s regulations in part 210, as it is currently or may be amended hereafter.

## **V. Additional Changes to Regulations**

In deliberating on the parties’ motions, the Judges have determined that certain additional changes or stylistic improvements to the promulgated regulatory language are appropriate and necessary for ease of administration.<sup>15</sup>

### **A. Incidental Deliveries**

The Judges have determined that the definition of “Incidental Delivery” in section 385.2, and the provision setting a rate for Incidental Deliveries in section 385.31 of the promulgated regulations attached to the Initial Determination, are unnecessary and could lead to confusion.

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<sup>15</sup> Section 102(d) of the Hatch-Goodlatte Music Modernization Act, Pub. L. No. 115-264, \_\_\_ Stat. \_\_\_ (Oct. 11, 2018) requires the Judges to amend the regulations in Part 385 “to conform the definitions of the same terms described in section 115(e) of title 17, United States Code, as added by” section 102(a). The Judges will do so through a separate rulemaking.

The Judges have deleted both provisions from the regulations in Attachment A, and have added language to the Final Determination addressing the royalty rates attributable to incidental DPDs.

**B. Bundles**

The regulations attached to the Initial Determination included a definition of “Bundle,” that combined definitions for “Music Bundle” and “Mixed Service Bundle” from the extant regulations. Upon further consideration, the Judge have determined that combining the definitions could have unintended consequences. The Judges have eliminated the definition of Bundle in the regulations in Attachment A, and have included separate definitions for “Music Bundle” and “Mixed Service Bundle.”

**C. Bundled Subscription Offerings**

Like the extant regulations, the promulgated regulations attached to the Initial Determination defined “Bundled Subscription Offerings” in the substantive provision establishing the royalty floor for that type of offering. The Judges have determined that it would be more appropriate to define “Bundled Subscription Offering” in section 385.2 (the definitional provision), and refer to it in section 385.22 (the provision setting royalty floors), and have done so in the regulations in Attachment A.

**VI. Final Determination**

The Judges will incorporate into the Final Determination the reasoning and rulings in this Order and Attachment A to this Order. The Final Determination is subject to statutory review by the Register of Copyrights and approval by the Librarian of Congress.

**SO ORDERED.**

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Suzanne M. Barnett  
Copyright Royalty Judge

DATED: January 4, 2019.

**Regulatory Terms**

**PART 385—RATES AND TERMS FOR USE OF NONDRAMATIC MUSICAL WORKS IN THE  
MAKING AND DISTRIBUTING OF PHYSICAL AND DIGITAL PHONORECORDS**

**Subpart A – Regulations of General Application**

- §385.1 General
- §385.2 Definitions
- §385.3 Late Payments
- §385.4 Recordkeeping for non royalty-bearing uses

**Subpart B – Physical Phonorecord Deliveries, Permanent Digital  
Downloads, Ringtones, and Music Bundles**

- §385.10 Scope
- §385.11 Royalty Rates

**Subpart C – Interactive Streaming, Limited Downloads, Limited  
Offerings, Mixed Service Bundles, Bundled Subscription Offerings,  
Locker Services, and Other Delivery Configurations**

- §385.20 Scope
- §385.21 Royalty Rates and Calculations

**Subpart D – Promotional and Free-to-the-User Offerings**

- §385.30 Scope
- §385.31 Royalty Rates

**Subpart A—Regulations of General Application**

**§385.1 General.**

(a) *Scope.* This part 385 establishes rates and terms of royalty payments for the use of nondramatic musical works in making and distributing of physical and digital phonorecords in accordance with the provisions of 17 U.S.C. 115. This subpart A contains regulations of general application to the making and distributing of phonorecords subject to the section 115 license.

(b) *Legal compliance.* Licensees relying on the compulsory license detailed in 17 U.S.C. 115 shall comply with the requirements of that section, the rates and terms of this part, and any other applicable regulations. This part 385 describes rates and terms for the compulsory license only.

(c) *Interpretation.* This part 385 is intended only to set rates and terms for situations in which the exclusive rights of a Copyright Owner are implicated and a compulsory license

pursuant to 17 U.S.C. 115 is obtained. Neither the part nor the act of obtaining a license under 17 U.S.C. 115 is intended to express or imply any conclusion as to the circumstances in which a user must obtain a compulsory license pursuant to 17 U.S.C. 115.

(d) *Relationship to voluntary agreements.* The rates and terms of any license agreements entered into by Copyright Owners and Licensees relating to use of musical works within the scope of those license agreements shall apply *in lieu* of the rates and terms of this part.

## **§385.2 Definitions.**

*Accounting Period* means the monthly period specified in 17 U.S.C. 115(c)(5) and any related regulations.

*Affiliate* means an entity controlling, controlled by, or under common control with another entity, except that an affiliate of a record company shall not include a Copyright Owner to the extent it is engaging in business as to musical works.

*Bundled Subscription Offering* means a Subscription Offering providing Licensed Activity consisting of Streams or Limited Downloads that is made available to End Users with one or more other products or services (including products or services subject to other subparts) as part of a single transaction without pricing for the subscription service providing Licensed Activity separate from the product(s) or service(s) with which it is made available (e.g., a case in which a user can buy a portable device and one-year access to a subscription service providing Licensed Activity for a single price),

*Copyright Owner(s)* are nondramatic musical works copyright owners who are entitled to royalty payments made under this part 385 pursuant to the compulsory license under 17 U.S.C. 115.

*Digital Phonorecord Delivery or DPD* has the same meaning as in 17 U.S.C. 115(d).

*End User* means each unique person that (a) pays a subscription fee for an Offering during the relevant Accounting Period or (b) makes at least one Play during the relevant Accounting Period.

*Family Plan* means a discounted subscription to be shared by two or more family members for a single subscription price.

*Free Trial Offering* means a subscription to a Service's transmissions of sound recordings embodying musical works when

(1) Neither the Service, the Record Company, the Copyright Owner, nor any person or entity acting on behalf of or *in lieu* of any of them receives any monetary consideration for the Offering;

(2) The free usage does not exceed 30 consecutive days per subscriber per two-year period;

(3) In connection with the Offering, the Service is operating with appropriate musical license authority and complies with the recordkeeping requirements in section 385.4;

(4) Upon receipt by the Service of written notice from the Copyright Owner or its agent stating in good faith that the Service is in a material manner operating without appropriate license authority from the Copyright Owner under 17 U.S.C. 115, the Service shall within 5 business days cease transmission of the sound recording embodying that musical work and withdraw it from the repertoire available as part of a Free Trial Offering;

(5) The Free Trial Offering is made available to the End User free of any charge; and

(6) The Service offers the End User periodically during the free usage an opportunity to subscribe to a non-free Offering of the Service.

*GAAP* means U.S. Generally Accepted Accounting Principles in effect at the relevant time, except that if the U.S. Securities and Exchange Commission permits or requires entities with securities that are publicly traded in the U.S. to employ International Financial Reporting Standards in lieu of Generally Accepted Accounting Principles, then that entity may employ International Financial Reporting Standards as “GAAP” for purposes of this subpart.

*Interactive Stream* means a Stream, where the performance of the sound recording by means of the Stream is not exempt from the sound recording performance royalty under 17 U.S.C. 114(d)(1) and does not in itself, or as a result of a program in which it is included, qualify for statutory licensing under 17 U.S.C. 114(d)(2).

*Licensee* means any entity availing itself of the compulsory license under 17 U.S.C. 115 to use copyrighted musical works in the making or distributing of physical or digital phonorecords.

*Licensed Activity*, as the term is used in subpart B of this part 385, means delivery of musical works, under voluntary or statutory license, *via* physical phonorecords and Digital Phonorecord Deliveries in connection with Permanent Digital Downloads, Ringtones, and Music Bundles; and, as the term is used in subparts C and D of this part 385, means delivery of musical works, under voluntary or statutory license, *via* Digital Phonorecord Deliveries in connection with Interactive Streams, Limited Downloads, Limited Offerings, mixed Bundles, and Locker Services.

*Limited Download* means a transmission of a sound recording embodying a musical work to an End User of a digital phonorecord under 17 U.S.C. 115(c)(3)(C) and (D) that results in a Digital Phonorecord Delivery of that sound recording that is only accessible for listening for—

(1) An amount of time not to exceed one month from the time of the transmission (unless the Licensee, *in lieu* of retransmitting the same sound recording as another limited download, separately and upon specific request of the End User made through a live network connection, reauthorizes use for another time period not to exceed one month), or in the case of a subscription plan, a period of time following the end of the applicable subscription no longer than a subscription renewal period or three months, whichever is shorter; or

(2) A number of times not to exceed 12 (unless the Licensee, *in lieu* of retransmitting the same sound recording as another Limited Download, separately and upon specific request of the End User made through a live network connection, reauthorizes use of another series of 12

or fewer plays), or in the case of a subscription transmission, 12 times after the end of the applicable subscription.

*Limited Offering* means a subscription plan providing Interactive Streams or Limited Downloads for which—

(1) An End User cannot choose to listen to a particular sound recording (*i.e.*, the Service does not provide Interactive Streams of individual recordings that are on-demand, and Limited Downloads are rendered only as part of programs rather than as individual recordings that are on-demand); or

(2) The particular sound recordings available to the End User over a period of time are substantially limited relative to Services in the marketplace providing access to a comprehensive catalog of recordings (*e.g.*, a product limited to a particular genre or permitting Interactive Streaming only from a monthly playlist consisting of a limited set of recordings).

*Locker Service* means an Offering providing digital access to sound recordings of musical works in the form of Interactive Streams, Permanent Digital Downloads, Restricted Downloads or Ringtones where the Service has reasonably determined that the End User has purchased or is otherwise in possession of the subject phonorecords of the applicable sound recording prior to the End User's first request to use the sound recording via the Locker Service. The term Locker Service does not mean any part of a Service's products otherwise meeting this definition, but as to which the Service has not obtained a section 115 license.

*Mixed Service Bundle* means one or more of Permanent Digital Downloads, Ringtones, Locker Services, or Limited Offerings a Service delivers to End Users together with one or more non-music services (*e.g.*, Internet access service, mobile phone service) or non-music products (*e.g.*, a telephone device) of more than token value and provided to users as part of one transaction without pricing for the music services or music products separate from the whole Offering.

*Music Bundle* means two or more of physical phonorecords, Permanent Digital Downloads or Ringtones delivered as part of one transaction (*e.g.*, download plus ringtone, CD plus downloads). In the case of Music Bundles containing one or more physical phonorecords, the Service must sell the physical phonorecord component of the Music Bundle under a single catalog number, and the musical works embodied in the Digital Phonorecord Delivery configurations in the Music Bundle must be the same as, or a subset of, the musical works embodied in the physical phonorecords; provided that when the Music Bundle contains a set of Digital Phonorecord Deliveries sold by the same Record Company under substantially the same title as the physical phonorecord (*e.g.*, a corresponding digital album), the Service may include in the same bundle up to 5 sound recordings of musical works that are included in the stand-alone version of the set of digital phonorecord deliveries but not included on the physical phonorecord. In addition, the Service must permanently part with possession of the physical phonorecord or phonorecords it sells as part of the Music Bundle. In the case of Music Bundles composed solely of digital phonorecord deliveries, the number of digital phonorecord deliveries in either configuration cannot exceed 20, and the musical works embodied in each configuration in the Music Bundle must be the same as, or a subset of, the musical works embodied in the configuration containing the most musical works.

*Offering* means a Service's engagement in Licensed Activity covered by subparts C and D of this part 385.

*Paid Locker Service* means a Locker Service for which the End User pays a fee to the Service.

*Performance Royalty* means the license fee payable for the right to perform publicly musical works in any of the forms covered by subparts C and D this part 385.

*Permanent Digital Download or PDD* means a Digital Phonorecord Delivery in a form that the End User may retain on a permanent basis and replay at any time.

*Play* means an Interactive Stream, or play of a Limited Download, lasting 30 seconds or more and, if a track lasts in its entirety under 30 seconds, an Interactive Stream or play of a Limited Download of the entire duration of the track. A Play excludes an Interactive Stream or play of a Limited Download that has not been initiated or requested by a human user. If a single End User plays the same track more than 50 straight times, all plays after play 50 shall be deemed not to have been initiated or requested by a human user..

*Promotional Offering* means a digital transmission of a sound recording, in the form of an Interactive Stream or Limited Download, embodying a musical work, the primary purpose of which is to promote the sale or other paid use of that sound recording or to promote the artist performing on that sound recording and not to promote or suggest promotion or endorsement of any other good or service and

(1) a Record Company is lawfully distributing the sound recording through established retail channels or, if the sound recording is not yet released, the Record Company has a good faith intention to lawfully distribute the sound recording or a different version of the sound recording embodying the same musical work;

(2) for Interactive Streaming or Limited Downloads, the Record Company requires a writing signed by an authorized representative of the Service representing that the Service is operating with appropriate musical works license authority and that the Service is in compliance with the recordkeeping requirements of section 385.4;

(3) for Interactive Streaming of segments of sound recordings not exceeding 90 seconds, the Record Company delivers or authorizes delivery of the segments for promotional purposes and neither the Service nor the Record Company creates or uses a segment of a sound recording in violation of 17 U.S.C. 106(2) or 115(a)(2);

(4) the Promotional Offering is made available to an End User free of any charge; and

(5) the Service provides to the End User at the same time as the Promotional Offering stream an opportunity to purchase the sound recording or the Service periodically offers End Users the opportunity to subscribe to a paid Offering of the Service.

*Purchased Content Locker Service* means a Locker Service made available to End User purchasers of Permanent Digital Downloads, Ringtones, or physical phonorecords at no incremental charge above the otherwise applicable purchase price of the PDDs, Ringtones, or physical phonorecords acquired from a qualifying seller. With a Purchased Content Locker

Service, an End User may receive one or more additional phonorecords of the purchased sound recordings of musical works in the form of Permanent Digital Downloads or Ringtones at the time of purchase, or subsequently have digital access to the purchased sound recordings of musical works in the form of Interactive Streams, additional Permanent Digital Downloads, Restricted Downloads, or Ringtones.

A qualifying seller for purposes of this definition is the entity operating the Service, including affiliates, predecessors, or successors in interest, or—

(1) In the case of Permanent Digital Downloads or Ringtones, a seller having a legitimate connection to the locker service provider pursuant to one or more written agreements (including that the Purchased Content Locker Service and Permanent Digital Downloads or Ringtones are offered through the same third party); or

(2) In the case of physical phonorecords,

(A) The seller of the physical phonorecord has an agreement with the Purchased Content Locker Service provider establishing an integrated offer that creates a consumer experience commensurate with having the same Service both sell the physical phonorecord and offer the integrated locker service; or

(B) The Service has an agreement with the entity offering the Purchased Content Locker Service establishing an integrated offer that creates a consumer experience commensurate with having the same Service both sell the physical phonorecord and offer the integrated locker service.

*Record Company* means a person or entity that

(1) Is a copyright owner of a sound recording embodying a musical work;

(2) In the case of a sound recording of a musical work fixed before February 15, 1972, has rights to the sound recording, under the common law or statutes of any State, that are equivalent to the rights of a copyright owner of a sound recording of a musical work under title 17, United States Code;

(3) Is an exclusive Licensee of the rights to reproduce and distribute a sound recording of a musical work; or

(4) Performs the functions of marketing and authorizing the distribution of a sound recording of a musical work under its own label, under the authority of the Copyright Owner of the sound recording.

*Relevant Page* means an electronic display (for example, a Web page or screen) from which a Service's Offering consisting of Streams or Limited Downloads is directly available to End Users, but only when the Offering and content directly relating to the Offering (e.g., an image of the artist, information about the artist or album, reviews, credits, and music player controls) comprises 75% or more of the space on that display, excluding any space occupied by advertising. An Offering is directly available to End Users from a page if End Users can receive sound recordings of musical works (in most cases this will be the page on which the Limited Download or Interactive Stream takes place).

*Restricted download* means a Digital Phonorecord Delivery in a form that cannot be retained and replayed on a permanent basis. The term Restricted Download includes a Limited Download.

*Ringtone* means a phonorecord of a part of a musical work distributed as a Digital Phonorecord Delivery in a format to be made resident on a telecommunications device for use to announce the reception of an incoming telephone call or other communication or message or to alert the receiver to the fact that there is a communication or message.

*Service* means that entity governed by subparts C and D of this part 385, which might or might not be the Licensee, that with respect to the section 115 license

(1) Contracts with or has a direct relationship with End Users or otherwise controls the content made available to End Users;

(2) Is able to report fully on Service Revenue from the provision of musical works embodied in phonorecords to the public, and to the extent applicable, verify Service Revenue through an audit; and

(3) Is able to report fully on its usage of musical works, or procure such reporting and, to the extent applicable, verify usage through an audit.

*Service Revenue.* (1) Subject to paragraphs (2) through (5) of this definition and subject to GAAP, *Service Revenue* shall mean:

(i) All revenue from End Users recognized by a Service for the provision of any Offering;

(ii) All revenue recognized by a Service by way of sponsorship and commissions as a result of the inclusion of third-party "in-stream" or "in-download" advertising as part of any Offering, *i.e.*, advertising placed immediately at the start or end of, or during the actual delivery of, a musical work, by way of Interactive Streaming or Limited Downloads; and

(iii) All revenue recognized by the Service, including by way of sponsorship and commissions, as a result of the placement of third-party advertising on a Relevant Page of the Service or on any page that directly follows a Relevant Page leading up to and including the Limited Download or Interactive Stream of a musical work; provided that, in case more than one Offering is available to End Users from a Relevant Page, any advertising revenue shall be allocated between or among the Services on the basis of the relative amounts of the page they occupy.

(2) Service Revenue shall:

(A) include revenue recognized by the Service, or by any associate, affiliate, agent, or representative of the Service *in lieu* of its being recognized by the Service; and

(B) include the value of any barter or other nonmonetary consideration; and

(C) except as expressly detailed in this part 385, not be subject to any other deduction or set-off other than refunds to End Users for Offerings that the End Users were

unable to use because of technical faults in the Offering or other bona fide refunds or credits issued to End Users in the ordinary course of business.

(3) Service Revenue shall exclude revenue derived by the Service solely in connection with activities other than Offering(s), whereas advertising or sponsorship revenue derived in connection with any Offering(s) shall be treated as provided in paragraphs (2) and (4) of this definition of Service Revenue.

(4) For purposes of paragraph (1) of this definition of Service Revenue, advertising or sponsorship revenue shall be reduced by the actual cost of obtaining that revenue, not to exceed 15%.

(5) In instances in which a Service provides an Offering to End Users as part of the same transaction with one or more other products or services that are not Licensed Activities, then the revenue from End Users deemed to be recognized by the Service for the Offering for the purpose of paragraph (1) of this definition of Service Revenue shall be the lesser of the revenue recognized from End Users for the bundle and the aggregate standalone published prices for End Users for each of the component(s) of the bundle that are Licensed Activities; provided that, if there is no standalone published price for a component of the bundle, then the Service shall use the average standalone published price for End Users for the most closely comparable product or service in the U.S. or, if more than one comparable exists, the average of standalone prices for comparables.

*Stream* means the digital transmission of a sound recording of a musical work to an End User—

(1) To allow the End User to listen to the sound recording, while maintaining a live network connection to the transmitting service, substantially at the time of transmission, except to the extent that the sound recording remains accessible for future listening from a Streaming Cache Reproduction;

(2) Using technology that is designed such that the sound recording does not remain accessible for future listening, except to the extent that the sound recording remains accessible for future listening from a Streaming Cache Reproduction; and

(3) That is subject to licensing as a public performance of the musical work.

*Streaming Cache Reproduction* means a reproduction of a sound recording embodying a musical work made on a computer or other receiving device by a Service solely for the purpose of permitting an End User who has previously received a Stream of that sound recording to play the sound recording again from local storage on the computer or other device rather than by means of a transmission; provided that the End User is only able to do so while maintaining a live network connection to the Service, and the reproduction is encrypted or otherwise protected consistent with prevailing industry standards to prevent it from being played in any other manner or on any device other than the computer or other device on which it was originally made.

*Student Plan* means a discounted Subscription to an Offering available on a limited basis to students.

*Subscription* means an Offering for which End Users are required to pay a fee to have access to the Offering for defined subscription periods of 3 years or less (in contrast to, for example, a service where the basic charge to users is a payment per download or per play), whether the End User makes payment for access to the Offering on a standalone basis or as part of a Bundle with one or more other products or services.

*Total Cost of Content* or *TCC* means the total amount expended by a Service or any of its affiliates in accordance with GAAP for rights to make interactive streams or limited downloads of a musical work embodied in a sound recording through the Service for the accounting period, which amount shall equal the applicable consideration for those rights at the time the applicable consideration is properly recognized as an expense under GAAP. As used in this definition, “applicable consideration” means anything of value given for the identified rights to undertake the Licensed Activity, including, without limitation, ownership equity, monetary advances, barter or any other monetary and/or nonmonetary consideration, whether that consideration is conveyed via a single agreement, multiple agreements and/or agreements that do not themselves authorize the Licensed Activity but nevertheless provide consideration for the identified rights to undertake the Licensed Activity, and including any value given to an affiliate of a record company for the rights to undertake the Licensed Activity. Value given to a Copyright Owner of musical works that is controlling, controlled by, or under common control with a Record Company for rights to undertake the Licensed Activity shall not be considered value given to the Record Company. Notwithstanding the foregoing, applicable consideration shall not include in-kind promotional consideration given to a Record Company (or affiliate thereof) that is used to promote the sale or paid use of sound recordings embodying musical works or the paid use of music services through which sound recordings embodying musical works are available where the in-kind promotional consideration is given in connection with a use that qualifies for licensing under 17 U.S.C. 115.

### **§385.3 Late payments.**

A Licensee shall pay a late fee of 1.5% per month, or the highest lawful rate, whichever is lower, for any payment owed to a Copyright Owner and remaining unpaid after the due date established in 17 U.S.C. 115(c)(5) and detailed in part 210 of this title 37, or any amendments to or replacements of that part. Late fees shall accrue from the due date until the Copyright Owner receives payment.

### **§385.4 Recordkeeping for promotional and non royalty-bearing uses.**

(a) *General.* A Licensee transmitting a sound recording embodying a musical work subject to section 115 and subparts C and D of this part 385 and claiming a Promotional or Free Trial zero royalty rate shall keep complete and accurate contemporaneous written records of making or authorizing Interactive Streams or Limited Downloads, including the sound recordings and musical works involved, the artists, the release dates of the sound recordings, a brief statement of the promotional activities authorized, the identity of the Offering or Offerings for which the zero-rate is authorized (including the Internet address if applicable), and the beginning and end date of each zero rate Offering.

(b) *Retention of Records.* A Service claiming zero rates shall maintain the records required by this section 385.4 for no less time than the Service maintains records of royalty-bearing uses involving the same types of Offerings in the ordinary course of business, but in no event for fewer than five years from the conclusion of the zero rate Offerings to which they pertain.

(c) *Availability of Records.* If a Copyright Owner or agent requests information concerning zero rate Offerings, the Licensee shall respond to the request within an agreed, reasonable time.

**Subpart B – Physical Phonorecord Deliveries,  
Permanent Digital Downloads, Ringtones, and Music Bundles.**

**§385.10 Scope**

This subpart establishes rates and terms of royalty payments for making and distributing phonorecords, including by means of Digital Phonorecord Deliveries, in accordance with the provisions of 17 U.S.C. 115.

**§385.11 Royalty rates.**

(a) *Physical phonorecord deliveries and Permanent Digital Downloads.* For every physical phonorecord and Permanent Digital Download the Licensee makes and distributes or authorizes to be made and distributed, the royalty rate payable for each work embodied in the phonorecord or PDD shall be either 9.1 cents or 1.75 cents per minute of playing time or fraction thereof, whichever amount is larger.

(b) *Ringtones.* For every Ringtone the Licensee makes and distributes or authorizes to be made and distributed, the royalty rate payable for each work embodied therein shall be 24 cents.

(c) *Music bundles.* For a Music Bundle, the royalty rate for each element of the Music Bundle shall be the rate required under paragraph (a) or paragraph (b), as appropriate.

**Subpart C—Interactive Streaming, Limited Downloads, Limited Offerings,  
Mixed Service Bundles, Bundled Subscription Offerings, Locker Services, and Other  
Delivery Configurations**

**§385.20 Scope.**

This subpart establishes rates and terms of royalty payments for Interactive Streams and Limited Downloads of musical works, and other reproductions or distributions of musical works through Limited Offerings, Mixed Service Bundles, Bundled Subscription Offerings, Paid Locker Services, and Purchased Content Locker Services provided through subscription and nonsubscription digital music Services in accordance with the provisions of 17 U.S.C. 115, exclusive of Offerings subject to subpart D.

**§385.21 Royalty Rates and Calculations**

(a) *Applicable royalty.* Licensees that engage in Licensed Activity covered by this subpart pursuant to 17 U.S.C. 115 shall pay royalties therefor that are calculated as provided in this section, subject to the royalty floors for specific types of services described in §385.22.

(b) *Rate calculation.* Royalty payments for Licensed Activity in this subpart shall be calculated as provided in paragraph (b) of this section. If a Service includes different Offerings, royalties must be calculated separately with respect to each Offering taking into consideration Service Revenue and expenses associated with each Offering.

(1) *Step 1*: Calculate the All-In Royalty for the Offering. For each Accounting Period, the all-in royalty shall be the greater of the applicable percent of Service Revenue and the applicable percent of TCC set forth in the following table.

**2018-2022 All-In Royalty Rates**

<b>Royalty Year:</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>
<b>Percent of Revenue</b>	11.4%	12.3%	13.3%	14.2%	15.1%
<b>Percent of TCC</b>	22.0%	23.1%	24.1%	25.2%	26.2%

(2) *Step 2*: Subtract Applicable Performance Royalties. From the amount determined in step 1 in paragraph (b)(1) of this section, for each Offering of the Service, subtract the total amount of Performance Royalty that the Service has expensed or will expense pursuant to public performance licenses in connection with uses of musical works through that Offering during the Accounting Period that constitute Licensed Activity. Although this amount may be the total of the Service’s payments for that Offering for the Accounting Period, it will be less than the total of the Performance Royalties if the Service is also engaging in public performance of musical works that does not constitute Licensed Activity. In the case in which the Service is also engaging in the public performance of musical works that does not constitute Licensed Activity, the amount to be subtracted for Performance Royalties shall be the amount allocable to Licensed Activity uses through the relevant Offering as determined in relation to all uses of musical works for which the Service pays Performance Royalties for the Accounting Period. The Service shall make this allocation on the basis of Plays of musical works or, where per-play information is unavailable because of *bona fide* technical limitations as described in step 3 in paragraph (b)(3) of this section, using the same alternative methodology as provided in step 4.

(3) *Step 3*: Determine the Payable Royalty Pool. The payable royalty pool is the amount payable for the reproduction and distribution of all musical works used by the Service by virtue of its Licensed Activity for a particular Offering during the Accounting Period. This amount is the greater of

- (i) The result determined in step 2 in paragraph (b)(2) of this section, and
- (ii) The royalty floor (if any) resulting from the calculations described in §385.22.

(4) *Step 4*: Calculate the Per-Work Royalty Allocation. This is the amount payable for the reproduction and distribution of each musical work used by the Service by virtue of its Licensed Activity through a particular Offering during the Accounting Period. To determine this amount, the Service must allocate the result determined in step 3 in paragraph (b)(3) of this section to each musical work used through the Offering. The allocation shall be accomplished by dividing the payable royalty pool determined in step 3 for the Offering by the total number of Plays of all musical works through the Offering during the Accounting Period (other than Plays subject to subpart D of this part 385) to yield a per-Play allocation, and multiplying that result by the number of Plays of each musical work (other than Plays subject to subpart D of this part 385) through the Offering during the Accounting Period. For purposes of determining the per-work royalty allocation in all calculations under this step 4 only (*i.e.*, after the payable royalty pool has been determined), for sound recordings of musical works with a playing time of over 5 minutes, each Play shall be counted as provided in paragraph (c) of this section. Notwithstanding the foregoing, if the Service is not capable of tracking Play information because of *bona fide* limitations of the available technology for Offerings of that nature or of devices useable with the Offering, the per-work royalty allocation may instead be accomplished in a manner consistent with the methodology used by the Service for making royalty payment allocations for the use of individual sound recordings.

(c) *Overtime adjustment.* For purposes of the calculations in step 4 in paragraph (b)(4) of this section only, for sound recordings of musical works with a playing time of over 5 minutes, adjust the number of Plays as follows.

- (1) 5:01 to 6:00 minutes—Each play = 1.2 plays
- (2) 6:01 to 7:00 minutes—Each play = 1.4 plays
- (3) 7:01 to 8:00 minutes—Each play = 1.6 plays
- (4) 8:01 to 9:00 minutes—Each play = 1.8 plays
- (5) 9:01 to 10:00 minutes—Each play = 2.0 plays
- (6) For playing times of greater than 10 minutes, continue to add 0.2 plays for each additional minute or fraction thereof.

(d) *Accounting.* The calculations required by paragraph (b) of this section shall be made in good faith and on the basis of the best knowledge, information, and belief of the Licensee at the time payment is due, and subject to the additional accounting and certification requirements of 17 U.S.C. 115(c)(5) and part 210 of this title. Without limitation, a Licensee's statements of account shall set forth each step of its calculations with sufficient information to allow the Copyright Owner to assess the accuracy and manner in which the Licensee determined the payable royalty pool and per-play allocations (including information sufficient to demonstrate whether and how a royalty floor pursuant to §385.22 does or does not apply) and, for each Offering the Licensee reports, also indicate the type of Licensed Activity involved and the number of Plays of each musical work (including an indication of any overtime adjustment applied) that is the basis of the per-work royalty allocation being paid.

### **§ 385.22 Royalty Floors for Specific Types of Offerings.**

(a) *In general.* The following royalty floors for use in step 3 of §385.21(b)(3)(ii) shall apply to the respective types of Offerings.

(1) *Standalone non-portable Subscription—streaming only.* Except as provided in paragraph (a)(4) of this section, in the case of a Subscription Offering through which an End User can listen to sound recordings only in the form of Interactive Streams and only from a non-portable device to which those Streams are originally transmitted while the device has a live network connection, the royalty floor is the aggregate amount of 15 cents per subscriber per month.

(2) *Standalone non-portable Subscription—mixed.* Except as provided in paragraph (a)(4) of this section, in the case of a Subscription Offering through which an End User can listen to sound recordings either in the form of Interactive Streams or Limited Downloads but only from a non-portable device to which those Streams or Limited Downloads are originally transmitted, the royalty floor for use in step 3 of §385.21(b)(3)(ii) is the aggregate amount of 30 cents per subscriber per month.

(3) *Standalone portable Subscription Offering.* Except as provided in paragraph (a)(4) of this section, in the case of a Subscription Offering through which an End User can listen to sound recordings in the form of Interactive Streams or Limited Downloads from a portable device, the royalty floor for use in step 3 of §385.21(b)(3)(ii) is the aggregate amount of 50 cents per subscriber per month.

(4) *Bundled Subscription Offerings.* In the case of a Bundled Subscription Offering, the royalty floor for use in step 3 of §385.21(b)(3)(ii) is the [aggregate amount of 25 cents per month][the royalty floor that would apply to the music component of the bundle if it were offered

on a standalone basis] for each End User who has made at least one Play of a licensed work during that month (each such End User to be considered an “active subscriber”).

(b) *Computation of royalty rates.* For purposes of paragraph (a) of this section, to determine the royalty floor, as applicable to any particular Offering, the total number of subscriber-months for the Accounting Period, shall be calculated by taking all End Users who were subscribers for complete calendar months, prorating in the case of End Users who were subscribers for only part of a calendar month, and deducting on a prorated basis for End Users covered by an Offering subject to Subpart D, except in the case of a Bundled Subscription Offering, subscriber-months shall be determined with respect to active subscribers as defined in paragraph (a)(4) of this section. The product of the total number of subscriber-months for the Accounting Period and the specified number of cents per subscriber (or active subscriber, as the case may be) shall be used as the subscriber-based component of the royalty floor for the Accounting Period. A Family Plan shall be treated as 1.5 subscribers per month, prorated in the case of a Family Plan Subscription in effect for only part of a calendar month. A Student Plan shall be treated as 0.50 subscribers per month, prorated in the case of a Student Plan End User who subscribed for only part of a calendar month.

### **Subpart D – Promotional and Free-to-the-User Offerings**

#### **§385.30 Scope.**

This subpart establishes rates and terms of royalty payments for Promotional Offerings, Free Trial Offerings, and Certain Purchased Content Locker Services provided by subscription and nonsubscription digital music Services in accordance with the provisions of 17 U.S.C. 115.

#### **§385.31 Royalty Rates.**

(a) *Promotional Offerings.* For Promotional Offerings of audio-only Interactive Streaming and Limited Downloads of sound recordings embodying musical works that the Record Company authorizes royalty-free to the Service, the royalty rate is zero.

(b) *Free Trial Offerings.* For Free Trial Offerings for which the Service receives no monetary consideration, the royalty rate is zero.

(c) *Certain Purchased Content Locker Services.* For every Purchased Content Locker Service for which the Service receives no monetary consideration, the royalty rate is zero.

(d) *Unauthorized use.* If a Copyright Owner or agent of the Copyright Owner sends written notice to a Licensee stating in good faith that a particular Offering subject to this subpart D differs in a material manner from the terms governing that Offering, the Licensee must within 5 business days cease Streaming or otherwise making available that Copyright Owner's musical works and shall withdraw from the identified Offering any End User's access to the subject musical work.