INTERNET, SOUND RECORDINGS AND ROYALTY PAYMENTS: RECENT DEVELOPMENTS

Introduction

The purpose of this article is to discuss recent developments in Internet, sound recordings and royalty payments. This article analyzes the changes resulting from those developments and the measures taken by the different media actors to adapt to those changes.[1]

I. Challenges to the Music Industry's Traditional Structure and the Development of 360 Deals

One of the first direct consequences of the changes in the distribution networks is the now well publicized drop in CD's sales and of the revenues that were traditionally attached to it such roles. Labels have relied upon CD sales for income almost exclusively for years and are therefore primarily affected by the cut in CD sales. This has resulted in a shake-up of the base on which the music industry had traditionally been functioning, with labels now looking for new sources of revenue, and artists regaining a degree independence.

A. The Traditional Label/Artist Model

Traditionally, artists would sign exclusive contracts with record labels. The terms of a typical recording contract usually gave the label the exclusive right to represent the artist's music, which included selling CDs and generating income from song placement in movies, TV shows, advertising and other licensing. However, the economics of an

[1] This article is adapted from a "recent developments" panel presentation by the International Association of Entertainment Lawyers ("IAEL") at MIDEM, January 2008 in Cannes, France in which Richard Idell of Idell & Seitel LLP participated. This article was written by Aïda Kane, a French lawyer and Idell & Seitel LLP Intern (2007-2008) and a Masters of Law candidate at Golden Gate University School of Law in San Francisco, California.

artist/label contract substantially revolved around the CD sales. Seven album cycles were the standard time frame for those deals, so that in practice, most artists were obligated to a particular record label for their entire career. In exchange for exclusivity, artists were usually granted a signing bonus, monies to record their music and tour support, all of which were usually recoupable against future income. Once the records began to sell, the artist would earn a fraction of the income generated. However, for most of the artists, additional sources of income included touring and merchandising in which the labels did not take part.

Therefore, the traditional business model was characterized by a distinction between the record sales on the one hand, which the record label shared in to a significant degree, and other ancillary revenues, such as merchandising or touring, for which artists worked with tour promotion, management agencies and merchandising entities.

B. The Search For New Channels by Artists

Obviously, the above described structure can longer exist in a context in which CD sales do not provide substantial and constantly growing revenues. Proof of the growing dysfunctionality of this system in the digital age can be found in the fact that artists and labels are looking for new solutions and paradigms. To some extent, the drop in record sales, coupled with the cheap and fast ability to record studio-quality songs in home studios using laptop computers, has provided artists with a new level of independence. The number of alternative types of deals or channels of distribution, not involving the labels, sought by artists in 2007 is illustrative of this newly acquired independence. Examples include Prince's new album which was given away in the UK with the Mail on Sunday (a U.K. newspaper). The artist acknowledged that he had been

deriving most of his revenues from live performance rather than from CD sales for years. Radiohead began distributing digital versions of its new album inviting fans to pay as much or as little as they wanted while the Eagles are selling their new album exclusively and directly to Wal-Mart stores. Other artists such as Beck and the Dave Matthews Band also released one-off singles not slated for inclusion on an album on iTunes. And of course, the most significant example of a challenge to the traditional record contract model is the $120 million deal entered by Madonna with Live Nation, a concert promoter, walking away from her long-time label Warner (see *infra*).

C. The Record Companies and the Emergence of 360 Deals as a New Business Model

360-degree deals have increasingly been considered as an alternative business model in order for the labels to remain relevant in a changing music industry landscape. The general idea behind any 360 deal is to give the record company (or other entity) a share in all the revenues generated by the artist, rather than a mere share in record sales. Therefore, under a 360 deal, the record label or other entity a share in income generated by touring, merchandising and other entertainment industry endeavors. In practice, a label might finance a publishing deal for the artist's songs, pay the costs of launching a clothing line or finance infrastructure and staff. These types of deals aim at changing the role of labels from mere record makers to full artist developers involved in all aspects of an artist's career. The label thus would take the entire career of the artist into its hands, investing anywhere that they might be able to recoup with revenues. In exchange for a piece of those ancillary revenues, the label usually gives more money up front and often touring subsidies. Although no "standard" or "typical deal" has emerged, a breakdown of participation in a 360 deal for a band might be as follows:

- Percentage of record sales
- Percentage of touring income
- Percentage of merchandise income
- Percentage of publishing
- Percentage of other endeavors (i.e. clothing line, fragrance, etc.)

A survey of various practitioners reveals that the variety of terms in such deals is quite remarkable and that as noted no "typical" terms are emerging as yet.

The major record companies have already started signing new artists to 360-style contracts or at least expressed interest in their development. Indeed, Universal has already started including shares in image rights and merchandising in addition to the usual recorded music and publishing rights. Warner Music announced the formation of Brand Asset Group, an artist management joint venture with Violator Management, a firm that negotiates roles for rappers in films, advertisements, video games and TV programmes along with licensing their names and images to promote drinks, books and clothes. Likewise, Sony BMG and EMI have laid out plans to sign more 360-degree deals with new artists.

The record companies are not the only ones contemplating 360-degree deals and engaging in them. The companies that currently own touring, merchandising and management revenues are not eager to give up their traditional revenue streams. As a consequence, promoters and others are trying to move closer to the artists by also developing 360-degree deals. Companies such as Ticketmaster and Live Nation therefore appear to be potential competitors in the 360 deal field. The Madonna/Live Nation deal is very significant of this potential. Madonna walked away from her long-time record

label Warner Music Group to sign a multi-album, touring and merchandising deal with concert promoter Live Nation Inc. This ten year contract would pay her about $120 million in exchange for at least 3 albums and the exclusive rights to ancillary revenues. The deal encompasses all of Madonna's future music and music-related businesses including the exploitation of the Madonna brand, new studio albums, touring, merchandising, fan club/website, DVDs, music-related television and film projects and associated sponsorship agreements. Another particularity of this deal is that under the terms of the contract, ownership of her new recordings would remain with her, while Warner still owns the rights to Madonna's catalog of earlier recordings. Live Nation recently announced a similar structure with Jay-Z. Meanwhile, Ticketmaster's parent company struck a deal with Irving Asoff's Frontline Management. Thus, even this traditional ticketing company is changing its economic model.

Are companies like Live Nation and Ticketmaster really likely to become serious competitors to major record labels? It appears so. Although it is too early to say how all of these changes will turn out, it is to be acknowledged that the record companies still play a fundamental role in the music industry. For example, specifically, the power of aggregation, which is sharing resources among many groups, allows the labels to put good money into marketing and get the bands substantial exposure. Also, they can ensure that the artist's music is available through every possible download service in order to reach the broadest audience possible. They also have the advantage of access, which others may not be ready to compete with yet. Notwithstanding, it appears that all of the traditional lines between label, tour promoter, ticketing and management are blurring as these deals develop and continue to emerge.

D. The Efficiency of the 360 Deal Model

As of today, although only a few established artists have accepted 360 deals, musicians with small fan bases and little business experience are much more receptive to the idea of a 360 deal. There are some exceptions such as Pussycat dolls, Robbie Williams, Korn, Jay-Z and of course Madonna. It is speculated that more and more established artists will do similar deals with Live Nation and others.

One may wonder what the benefits of those deals are from an artist's point of view. The benefits to the record companies are obvious. As mentioned above, those deals try to make up for the slide in CD sales on which labels relied almost exclusively for years. However, when the main source of income for the majority of bands is usually touring and merchandise, it may not make sense for them to give a slice of this pie to the label. Record companies argue that their public relations and promotional engines can help break new bands. The labels also give artists more money up front, and provide a steady, comfortable income, which is very appealing to new talent. It has also been argued that these deals allow an more time for artists to develop with less pressure to make back the label's money immediately. The strongest argument is probably that with the substantial decrease in the money generated for labels, these 360 deals would provide an incentive for labels to still risk investment in new talent.

On the other hand, the real potential of a 360 deal does not emerge until an artist is popular enough to attract either loyal fans who regularly buy tickets or attention from business partners who might help market spin-offs like a fragrance, clothing or sneaker line. 360 deals are still at an early stage, and it will take a couple of years before anyone can determine whether a group's ancillary income can offset the continuing slide in

album sales. Indeed, as the sale of CDs decline, live music and merchandising also will grow. Evidence of the growth in live music can be found in the increase in concert ticket sales in North America from $1.7 billion in 2000 to over $3.1 billion in 2007. The growth of live music was originally driven by large arena shows and the boom of music festivals across the United States and Europe. Certainly, the 360 deal is a developing paradigm that will be front and center in the coming years.

II. The Inadequacies of the Current Licensing System in the Digital Distribution World

Another concept called into question by the development of new networks of distribution is the protection of songwriters and publishers' rights through the payment of royalties where perfect reproduction has become so simple. For years, compulsory licensing has been used as a way to ensure the artists were paid the appropriate royalties for use of their work. However, this system has been challenged in the digital age, putting its adequacy into question.

A. Compulsory License Under Section 115 as Applied to the Downloads of Sound Recordings

The current version of Section 115 provides for compulsory license for "making and distributing phonorecords". Section 115 of the Copyright Act of 1976 originally did not apply to downloads, but set out a compulsory license mechanism applicable to "phonorecords" of nondramatic musical works, defined as a physical object in which sounds are fixed, such as a compact disc. Under this scheme, a compulsory license was triggered when phonorecords of the nondramatic musical work were distributed to the public under the authority of the Copyright owner. Once distributed, a licensee could obtain a compulsory license by complying with the requirements of the section. The

procedure for the acquisition of a compulsory license started with providing a notice of intention to obtain a compulsory license to the Copyright owner and was subject to a finding that the licensee's primary purpose in making phonorecords was to distribute them to the public for private use. Failure to give notice foreclosed any possibility of obtaining a compulsory license. Once the Copyright owner was identified in the Copyright Office, a royalty determined by the Copyright Judges was payable. A licensee was then allowed to make and distribute phonorecords of a musical work.

In 1995, Congress created the Digital Performance Right in Sound Recordings Act in response to the inadequacy of then existing copyright law to address new technologies regarding digital transmission of sound recordings. This act extended the mechanical compulsory license to digital phonorecord deliveries. A digital phonorecord delivery was defined in the Act as each individual delivery of a phonorecord by digital transmission of a sound recording which results in a specifically identifiable reproduction by or for any recipient of a phonorecord of that sound recording. However, real-time, non-interactive subscription transmission of a sound recording where no reproduction of the sound recording is made from the inception of the transmission through to its receipt by the transmission recipient in order to make the sound recording audible is not included in the definition. In other words allowing a subscriber to download a song is a digital phonorecord delivery, while the mere streaming of the song, in a non-interactive environment does not qualify as a digital phonorecord delivery. Under the current compulsory license scheme, an artist gets 9.1 cents per song or 1.75 cents per minute of

playing time or fraction thereof, whichever is greater, on any phonorecord manufactured and distributed or legally downloaded in the U.S.[2]

B. The Need for a Reform of Section 115

The need for reform arose from the observation that Section 115 does not comport with the realities of the digital environment in which music creators, distributors and users now operate. In particular, the inefficiencies and confusion spawned by the modern application of Section 115 have been blamed for the inability of legitimate businesses to combat the widespread proliferation of music piracy. Therefore, a number of parties joined together and tried to reform Section 115. Particularly, the Digital Media Association ("DiMA"), a national trade organization devoted to innovative digital media opportunities, especially protecting the rights the online audio and video industries, strongly support a reform. The DiMA, among whose members are online media giants such as AOL, Apple, Microsoft and Yahoo, has criticized the administrative requirements mandated by the statute and the Copyright Office which they see as being "dysfunctional". Indeed, with only 20% of musical works registered with the Copyright Office and about 25% of the copyright owners who can not be located, legitimate startup online digital music providers face a real challenge in trying to give notice and obtain a so-called compulsory license. The procedure seems even more dysfunctional given the competition of the black market where there is no licensing fees or registration forms and where songs can be made available immediately, rather than spending weeks filling out forms and searching for copyright owners.

Another issue pointed out by the DiMA was the fact that the license does not apply to reproductions necessary to the digital distribution process but which are not

[2] These rates are currently being revised on infra Section III.

themselves distributed. This refers to server, cache and buffer copies, so that online digital music providers would necessarily infringe on the rights of copyright owners who have not licensed nor been paid royalties for the use of such incidental copies.

Other interested parties include the National Music Publishers Association ("NMPA") and the Harry Fox Agency ("HFA"). The NMPA, as the largest music publishing trade association in the U.S., represents the interests of songwriters and took a different view. In particular, the NMPA relies on the success of iTunes to argue that Section 115 is not an impediment to consumer demand for online music. They also point out that the HFA does bulk electronic licensing with a turnaround time of four hours upon license request, thus rebutting the dysfunctional aspect argument.

The NMPA ultimately supported reform but took a much less drastic approach than the DiMA. Additional parties weighing in favor of a reform included the Songwriters Guild of America ("SGA"), a songwriter's organization, and the Recording Industry Association of America ("RIAA"), a trade organization representing record companies.

C. The Section 115 Reform Act within the Copyright Modernization Act ("SIRA")

In May 2006, the NMPA worked closely with the DiMA to propose its own discussion draft, known as "SIRA". SIRA was introduced in the last session of Congress and referred to the Committee on the Judiciary on September 12, 2006 by Representative Lamar Smith of Texas. The legislation governed "the making and distribution of general and incidental streams, and any other form constituting a digital phonorecord delivery or hybrid offering…". In other words, SIRA provided that the license would cover incidental reproductions such as cached, network and RAM buffer copies for digital

deliveries. To facilitate noninteractive streaming or terrestrial radio analog broadcast, SIRA also provided for an exemption from copyright infringement when the providers make server or incidental reproductions. However, this exemption did not apply if the digital music provider took affirmative steps to allow an end user to make reproductions of the musical works for future listening. More importantly, SIRA addressed three principal concepts. First, SIRA created an all repertory or "blanket" license that allowed digital music providers access to the entire catalogue of copyrighted music, thus ending the current song-by-song process. Second, SIRA allowed the Copyright Royalty Judges to initiate ratemaking proceedings for any activity licensable under the legislation but did not specify the type of rate to be used, leaving open the possibility of a penny-rate royalty as under current legislation or the flexibility to move to a percentage of revenue based system. Finally, in order to administer the license, SIRA created a General Designated Agent (the Harry fox Agency) and allowed for additional Designated Agents. The General Designated Agent would be the default agent responsible for administrating the license and collecting and distributing royalties to copyright owners. Only digital music providers would have been eligible to receive a blanket license from the General Designated Agent and the other Designated Agents and could assume the General Designated Agent represented any works found not to be in control of any of the Designated Agents.

SIRA, however, did not progress beyond judiciary committee. The failure of this bill to leave committee can be attributed to a host of issues upon which the parties could not reach an agreement. Despite its support in the industry, SIRA was met with hostility by many online commentators. The root of the controversy seemed to revolve around

what many of these organizations see as the deterioration of fair use. In essence, these groups contested the limited exemption for server, cache, and other incidental copies and resisted the characterization of a stream as a "delivery”. On September 27, 2006, Lamar Smith withdrew the SIRA from Judiciary Committee consideration.

D. Reforming Efforts After SIRA?

After the Democrats gained control of the House of Representatives and Howard Berman replaced Lamar Smith as chair of the subcommittee, Berman acknowledged the need for 115 Reform. On March 22, 2007, the House Judiciary Subcommittee on Courts, the Internet, and Intellectual Property held a hearing on “Reforming Section 115 of the Copyright Act in the Digital Age” during which Marybeth Peters, the Register of Copyrights, made a statement. She pointed out the key issues in reviewing the possible options for reform of Section 115, which are:

(1) The scope of the license and clarification of rights;

(2) The collection and distribution of royalty fees;

(3) The efficiency of the licensing process; and

(4) The rate setting procedures.

Ms. Peters also suggested two options: either create a Section 114 style blanket license or provide for wholesale sublicensing with a safe harbor provision for the sublicensors. NMPA is also working with other creators groups to draft what they call “fair legislation”. According to NMPA, it is crucial to music publishers that any new legislation establishes a collective licensing system for mechanical rights and a better system for collecting and distributing mechanical royalties. Legislation must also ensure that music publishers and songwriters are fairly compensated for their creative works and

confirm that interactive streaming (where the user controls what he or she is listening to) requires a mechanical license under Section 115 of the Copyright Act. However, SIRA has not been re-introduced in this term of congress. Neither the House nor the Senate has introduced legislation regarding music licensing. Per the chairman of the house judiciary committee, the legislative priority seems to be elimination of the exemption that allows the radio industry to transmit sound recordings without payment.

III. 2008 Mechanical License Rate Proceedings

The Copyright Royalty Board has jurisdiction to establish the rates for all compulsory licenses provided in the Copyright Act (17 U.S.C. 801 (b) (1)). The former schedule of mechanical rates (9.1 cents or 1.75 cents per minute of playing time or fraction thereof whichever is greater) was set to expire at the end of 2007, and the Copyright Royalty Board proceedings began in January 2006 to determine the next schedule of rates. Along with setting rates for physical products, the CRB will for the first time set rates for digital downloads, interactive streaming, limited downloads and ringtones - each of which require a separate license and generate separate payments. On January 28, 2008 the Copyright Royalty Board began 4 weeks of hearings, where it heard testimony from interested parties on both sides. The Recording Industry Association of America (“RIAA”) and the Digital Media Association (“DiMA”), representing record labels and digital music services such as Yahoo, Napster, and Apple, are arguing to reduce royalty rates while the National Music Publishers Association (“NMPA”), representing copyright owners, is fighting to preserve existing rate structure and increase royalties.

As to physical phonorecords, the NMPA, the Songwriters Guild of America ("SGA") and the Nashville Songwriters Association International ("NSAI") have proposed penny rates for physical phonorecords (12.5 cents per song or 2.4 cents per minute of playing time) and permanent downloads (15 cents per song or 2.9 cents per minute of playing time). The justification of a higher rate for a permanent download, according to a statement filed with the Copyright Royalty Board, is that the majority of digitally downloaded music is done so as a single, compared to the album sales that account for the majority of music sold as physical product. The NMPA, SGA and NSAI also proposed that the rate for tethered downloads, interactive streaming and ringtones be the greater of (1) 12.5% of revenue, (2) 27.5% the costs paid for the sound recording, or (3) a penny rate (the greater of $0.00275 per use or $0.00053 per minute).

On behalf of sound recording owners the RIAA has proposed that the penny rate method be abolished for all uses of musical compositions. They have proposed that the value of the musical composition be 7.8% of revenues directly attributable to sound recordings for permanent downloads as well as physical phonorecords, temporary downloads, and ringtones. The RIAA has also proposed that the value of the underlying musical composition in interactive streams would be 9.6% of the applicable performance royalty rate payable to the performance royalty organizations (ASCAP, BMI and SESAC).

Finally, the DiMA has proposed a royalty rate for permanent digital downloads of 4.1% of applicable revenue and 4% of applicable revenue for tethered downloads. DiMA has proposed that the royalty rate cover "all reproductions necessary to engage in activities covered by the license," including server copies and reproductions made "by

and for the end user." They did not offer a rate for interactive streams or for physical phonorecords. Interestingly, DiMA made a motion on January 7, 2008 to the CRB arguing that an interactive stream of music through internet based media services is not a digital phonorecord delivery and, according to DiMA, should therefore not require a mechanical license or payment of mechanical royalties to songwriters and music publishers. However, the CRB sided with music publishers and denied DiMA's motion on February 5. This denial was mostly based on the CRB noting that copyright law does not define "interactive".

Until a decision is reached, the old rates will remain in effect. At the conclusion of the initial hearing, more discovery followed. A rebuttal hearing will be held in May, and a final decision is expected on October 2.

IV. Developments in Internet Service Providers (ISP) liability for hosting infringing content

Another one of the questions triggered by the development of new distribution channels is the risk of copyright infringement on the Internet generally and in user-generated content particularly, and whether the online service provider may be held liable for those infringements.

A. The Digital Millenium Copyright Act 1995

The Copyright law was modified in 1995 to specifically address the issue of ISP liability. Section 512 of the statute identified safe harbors for five specific categories of online service providers ("OSP"):

(a) those involved in "transitory digital network communications;"

(b) those providing "system caching" services;

(c) those providing space on their systems or networks for the storage of digital material "at the direction of users;"

(d) those providing "information location tools;"

(e) and nonprofit educational institutions providing such services to its faculty and graduate students.

In order to qualify for any of the safe harbors, any OSP is required to satisfy two requirements laid out in section 512(i). First, the OSP must have adopted and published a policy of terminating users guilty of repeat infringement. Second, its systems must be able to accommodate "standard technical measures" when implemented by copyright owners.

In defining these categories, Congress recognized that OSPs in the first category, acting as "mere conduits" for their users' activities, presented a set of liability issues that were quite distinct from those of the OSPs falling into the other four categories, and therefore approached them differently. The key difference in treatment is that OSPs qualifying for the "mere conduit" safe harbor of section 512(a) are effectively immunized with no requirement of further action on their part beyond the eligibility requirements set out in section 512(i). OSPs seeking the protection of one of the other safe harbors, however, must cooperate with content owners in the "notice and takedown" procedures described in section 512(c)(3).

In essence, this procedure requires OSPs seeking to make use of the safe harbors to publicly designate an agent to receive notices from copyright owners. This contact information must be provided to the Register of Copyrights, which is in turn charged with maintaining a publicly available directory of designated agents. Finally, upon receipt

from a copyright owner of a signed, written notification clearly identifying an allegedly infringing work, the OSP must "act expeditiously to remove or disable access to the infringing material." The safe harbors were made even safer by the addition of a provision expressly immunizing OSPs for any liability to the owners of material removed in good-faith compliance with the section 512(c) takedown procedures. This immunity applies even in cases where an OSP removed materials later found to be non-infringing on its own initiative, rather than as a result of receipt of a takedown notice from a copyright owner. Congress also provided for both a "counternotification" or "put back" procedure whereby the owner of material claimed to be infringing can notify the OSP, who is then required to replace it, and a right of action enabling either OSPs or copyright owners to recover damages for injuries sustained as a result of an OSP's reliance on knowing misrepresentations by any party making use of the notice and takedown or put back procedures.

B. Section 230 of the Communication Decency Act 1996, 47 USC § 230

Section 230 of the Communications Decency Act (CDA) of 1996 also has provided OSPs with a defense. The section provides immunity from liability for providers and users of an "interactive computer service" who publish information provided by others, so that they “shall [not] be treated as the publisher or speaker of any information” provided by others. In analyzing the availability of the immunity offered by this provision, courts generally apply a three-prong test. A defendant must satisfy each of the three prongs to gain the benefit of the immunity. First, the defendant must be a "provider or user" of an "interactive computer service." Second, the cause of action asserted by the plaintiff must "treat" the defendant "as the publisher or speaker" of the

harmful information at issue. Third, the information must be "provided by another information content provider," meaning that the defendant must not be the "information content provider" of the harmful information at issue. On the other hand, website operators are not protected by Section 230 if they created the content in question, rather than merely publishing third-party content. In addition, Section 230's coverage is not complete since it excepts federal criminal liability and intellectual property law.

Section 230 has been interpreted broadly by the Courts, virtually providing complete immunity for ISPs with regard to the torts committed by their users over their systems. In *Zeran v. AOL*, 524 U.S. 937 (1998), the Court of Appeals for the 4th Circuit held that Section 230 "creates a federal immunity to any cause of action that would make service providers liable for information originating with a third-party user of the service." In *Michelangelo Delfino v. Agilent Technologies*, 145 Cal. App. 4th 790 (2006), a California Appellate Court unanimously concluded that an employer that provides Internet access to its employees is a provider of an interactive service under section 230, and is protected from state tort claims arising from am employee's use of the employer's e-mail system to send threatening messages. Courts across the country have upheld Section 230 immunity in a variety of factual contexts and on numerous legal theories, including posting defamatory information, private information, false information, pornographic information and discriminatory housing ads.

In 2007, the Courts generally further upheld Section 230 immunity. For instance, in *Universal Communication Systems, Inc. v. Lycos, Inc.*, 478 F.3d 413 (2007), Lycos' activities in operating RagingBull.com, which hosts financially-oriented message boards, including ones designed to allow users to post comments about publicly-traded

companies, were held protected by the Section 230 immunity when Plaintiff, UCS (a publicly traded company), alleged that a number postings disparaging the "financial condition, business prospects and management integrity" of the company were "false, misleading and/or incomplete." In *Perfect 10, Inc. v. CCBill LLC*, 488 F.3d 1102 (2007), CCBill and CWIE (webhosting and related Internet connectivity services providers) were held to be eligible for CDA protection when perfect10.com, an adult entertainment subscription site, alleged their users were infringing on Perfect10's copyrights on its content.

However, one case took the opposite view and held the ISP contributorily liable. In *Fair Housing Council of San Fernando Valley v. Roommate.com, LLC*, 489 F.3d 921, (2007), the Ninth Circuit issued an opinion restricting Section 230 immunity for postings that violate the Fair Housing Act. The Defendants were Roommate.com, LLC ("Roommate") which operates an online roommate matching website at www.roommates.com. As part of the registration membership process, the users must fill out a questionnaire about themselves and a "my roommate preferences" form. The latter includes blank text box, allowing users to personalize their profile. The responses to this query produce the most provocative and revealing information in many users' profiles. For example, some state that they "prefer white male roommates," while others declare that they are "not looking for black Muslims". The action was brought on Fair Housing Act violation grounds. In its analysis, the Court was concerned in particular about online forms that structure data input and search results, and found that those structured forms constitute significant contributions from the service provider that are not immune from liability.

In traditional defamation jurisprudence, courts draw a distinction between "publishers" of information and "distributors." The former is liable for defamatory content it publishes, but the latter is generally liable only if it is on notice of the defamatory nature of the material. Section 230 of the CDA had been largely seen as a way of categorizing online service providers as "distributors," as opposed to "publishers," in the online world until *Barett v. Rosenthal* (2006) where California's Supreme Court declined to take that approach. In that case, plaintiff Stephen Barrett sued defendant Ilena Rosenthal, contending that Rosenthal posted defamatory statements about Barrett on Internet news groups. Rosenthal was not the original author of the statements, but Barrett argued that she was liable as a distributor because she posted them after he had put her on notice regarding their allegedly defamatory nature. The Appeals Court agreed with Barrett, but the State Supreme Court overturned it, finding that the CDA language simply did not support this result. It pointed to precedent indicating that "the publisher/distributor distinction makes no difference for purposes of section 230 immunity." Under this reading of the law, online service providers are free to publish defamatory statements, even once they have been informed that the statements are libelous.

Although Section 230 of the CDA had provided broad immunity for online service providers, that does not mean that there are no legal risks inherent in the business of providing online services on the web. As noted above, the Ninth Circuit Court of Appeals concluded in the *Fair Housing Council of San Fernando Valley* case that the website Roommates.com did not qualify for immunity under Section 230 for violation of the Fair Housing Act. Far from being just a passive conduit for information,

Roommates.com was actively involved in the content collected, since it required individuals to answer the questions at issue before proceeding to use the service. Addressing the scope of Section 230, the Court stated, “If it is responsible, in whole or in part, for creating or developing information, it becomes a content provider and is not entitled to CDA immunity.” En banc rehearing was granted on October 12, 2007. However, the holding was adhered to on rehearing by an 8-3 majority on April 3rd, 2008.

Interestingly, the 2d circuit recently took the opposite view. In *Chicago Lawyers' Committee for Civil rights Under Law Inc. v. Craigslist, Inc*, 2008 U.S. App. LEXIS 5472 (2008), Plaintiffs alleged that Craigslist violated the Fair Housing Acrt as a result of certain discriminatory housing and rental postings on its website. The Court of Appeals found that the defendants did not cause the discriminatory notices to be posted and did nothing that would take them out of the protection of Section 230. The committee could not sue the defendants- the messenger- just because the message revealed a 3rd party's plan to engage in unlawful discrimination. Section 230 was therefore held to protect online information systems from being treated as the publisher or speaker of any information provided by someone else, including in cases where a fundamental right is at issue.

C. The User Generated Content Principles

As to UGC platforms providers in particular, a consortium comprised of leading players in the digital content arena, including Disney/ABC, CBS, NBC/Universal, Fox Entertainment, Viacom (MTV Networks/ Paramount Pictures), MySpace, Veoh and Dailymotion, collectively issued their “User Generated Content Principles” on October

18, 2007. Among other things, the UGC Principles provide that the service provider should:

(1) provide conspicuous notice to users that they may not post infringing content and set forth prohibition in terms of use for the website,

(2) implement "identification technology", which is content filtering technology, to automatically block infringing content that users attempt to upload to their website,

(3) provide content owners with reasonable search capability to locate infringing content on the website,

(4) conduct manual review of user submitted content if necessary to determine if such content is infringing, and

(5) expeditiously take down infringing UGC and block and/or terminate users who repeatedly post infringing UGC.

The UGC Principles also provide some "to do's" for the content owners:

(1) provide "reference materials," that is, data that would enable a service provider to cross reference submitted UGC with the content owner's content,

(2) cooperate with the service providers to implement workable filtering technology with the goals of blocking infringing content, allowing uploads of original or authorized content and accommodating fair use, and

(3) refrain from making claims against service providers that comply with the UGC Principles.

D. Rise in Litigation Activity Involving User Generated Content ("UGC") and the Viacom v. Google Case

There has been an increase in litigation activity involving UGC. Primarily, those cases involve media companies and other individuals alleging direct or secondary copyright infringement against online service providers featuring UGC. Examples of these lawsuits include the two cases filed by Universal Music Group in the California Central District Court against Veoh (filed Sept. 4, 2007) and MySpace (filed Nov. 17, 2006). More importantly, Viacom filed a copyright infringement lawsuit against YouTube and Google in the Southern District of New York on March 13, 2007. Viacom alleges that "YouTube appropriated the value of creative content on a massive scale for YouTube's benefit without payment or license". In its complaint, it alleges that over 160,000 unauthorized clips of Viacom's entertainment programming have been available in Youtube and seen over 1.5 billion times by YouTube Viewers and is seeking $1 billion in damages. In its answer, Google essentially raised, among other defenses, the DMCA Safe Harbor Provision and fair Use.

Discovery has started and is expected to last until the end of 2008, with a potential trial taking place after that. On February 8, 2008, Viacom moved to amend its complaint to seek punitive damages against Google beyond the initial complaint. However, the motion was denied on March 7, 2008 after U.S. district judge Louis Stanton ruled that "punitive damages are not available under the Copyright Act of 1976". However, this should not affect the original suit.

Of importance to the lawsuit, while the lawsuit was pending Google also launched the beta of its "highly complicated" YouTube copyright tool called "YouTube Video Identification" in October. This tool allows copyright owners to identify their content

more easily and manage how it is made available on YouTube. This case should be closely watched as it moves forward to trial.

V. Issues Relating to Satellite/ Digital Radio and the Performance Rights

The development of high-quality radio in general and Internet radio, in particular, has brought attention to the issue of royalty payment over radio transmissions and the need for legislation. Under the Copyright Act of 1976, a different treatment was given to songs (i.e. the notes and lyrics of a piece of music) and to sound recordings (i.e. the particularly recorded version of a song) in terms of performance rights. Performance rights were originally granted to the owners of songs while no such rights were granted to the owners of sound recordings. However, the Digital Millennium Copyright Act ("DMCA") gave copyright owners and performers of a sound recording a performance right when a song is publicly performed by means of a digital transmission. Therefore, the DMCA established a scheme according to which traditional over-the-air broadcasters do not have to pay any performance royalty for sound recordings while cable satellite and internet broadcasters have to pay such a cost. The DMCA also allows for a compulsory license for some digital transmissions of sound recordings, while other digital transmissions such as downloads and podcasts do not qualify for it, so that webcasters would have to obtain a license from and negotiate royalties with the copyright owner directly who is free to charge any royalty rate it desires. As a result of the inconsistencies of the current scheme, there's been a move to introduce legislation to harmonize the legislation for airplay and digital transmission, resulting in the Platform Equality and Remedies for rights Holders in Music Act of 2007. In addition, the current rate scheme for compulsory licensing technically expired at the end of 2005 and the rate

determination process for the 2006-2010 period resulted in the very controversial March 2007 decision of the Copyright Royalty Board, currently under appeal.

A. Platform Equality and Remedies for Rights Holders in Music Act of 2007 (Perform Act): Creating a Single Process for Setting Rates and Terms for the Statutory Licensing of all Transmissions

In response to the onset of high quality digital radio signals transmitted through satellite, cable or Internet radio and consumers being able to become the owners of perfect copies of any song they choose without proper payment, the NMPA has joined together with a coalition in the music industry to ask Congress to draft legislation to protect their content. They are pursuing legislation through both the Commerce and the Judiciary committees in the House and the Senate. On January 11, 2007, Senator Dianne Feinstein, introduced the Perform Act, legislation to protect songwriters and music publishers while encouraging the growth of digital radio. The stated purpose of the bill is "to harmonize rate setting standards for copyright licenses under section 112 and 114 of title 17, United States Code". In essence, the bill requires the Copyright Royalty Judges to establish rates for a statutory license for the transmission of sound recordings by organizations that most clearly represent the fair market value of the rights licensed. First, the Perform Act would replace the different processes for setting rates and terms of royalty payments for subscription transmissions by preexisting subscription services, satellite digital radio services, and eligible non-subscription transmission services with one process for all such transmissions. When setting such rates and terms, the Copyright Royalty Judges would have to consider the fair market value of the rights licensed and the degree to which reasonable recording affects the potential market for sound recordings and the additional fees that are required to be paid by services for

compensation. Furthermore, the Act would condition statutory licensing of transmissions on the use by the transmitting entity of technology that is reasonably available, technologically feasible, and economically reasonable to prevent the making of copies or phonorecords embodying the transmission, except for reasonable recording. Finally, the act requires the Register of Copyrights to convene a meeting among affected parties to discuss whether to recommend creating a new category of limited interactive services within certain statutory licenses for subscription transmissions.

The Perform Act has been referred to the Senate Judiciary Committee.

B. The Copyright Royalty Judges March 2, 2007 Decision and Internet Radio

On March 2 2007, US Copyright Royalty Board ("CRB") announced new royalty rates to be paid to artists and record labels for the public performance of their works by Internet radio broadcasters from 2006-2010.

Under the prior scheme, the royalty rates paid by webcasters under the compulsory license were originally set by a panel of arbitrators selected by the Copyright Office. As of January 2006, the rates are set by the Copyright Royalty Board, who adjusts royalty rates for compulsory licensing every five years. The royalty rates were first set in 2002 and modified by settlement agreements between the recording industry and various groups of webcasters. That scheme technically expired at the end of 2005 but webcasters paid royalties at these rates through 2006, and continued to do so until the implementation of the board's new changes on July 15, 2007. Under this scheme, all commercial webcasters who did not qualify as "small commercial webcasters" could calculate royalties in one of two ways:

- a "per performance" option, which allowed them to pay per song per listener at $0.000762 per performance

- an "aggregate tuning hours" method whereby one listener who listens for one hour would constitute one ATH, two listeners who listen each for half an hour also would be one ATH, and so on, the fee for each ATH being $0.0117

Strong protest led to the small Webcasters Settlement Act of 2002, which created an option allowing any webcaster with less than $1.2 million in revenue to pay the higher of 10% of its revenue on the first $250,000 of its revenue and 12% thereafter, or 7% of the entity's expenses. Additionally, noncommercial webcasters paid a minimum of $500 a year, allowing them to stream 146,000 aggregate monthly tuning hours. Nonmusic webcasters paid a reduced rate of $0.000762 per ATH.

The March 2, 2007 decision changed both the royalty rates and the methodology for the 2006-2010 period. All commercial webcasters including those previously categorized as "small commercial webcasters" or "nonmusic webcasters" must now calculate royalties on a per-performance basis at a uniform rate. New rates force webcasters to pay for each song streamed to each user, and increase over the next few years:

- 2006: $0.0008 (to stream one song to one listener)
- 2007: $.0011
- 2008: $.0014
- 2009: $.0018
- 2010: $.0019

Minimum fee: $500 per year and per channel

Therefore, these rates reflect a significant increase over a five-year period. Non-commercial webcasters are still treated as a separate category under the new scheme instituted by the CRB, but the basis on which they pay royalties has changed. They must pay a minimum annual fee of $500 per channel or station, which allows them to conduct digital audio transmissions of up to 159,140 ATH per month. In case a webcaster exceeds this limit, it must pay additional royalties for digital audio transmissions in excess of the cap at the same rate as that paid by commercial webcasters.

The Royalties will be paid to SoundExchange, a non-profit corporation with a Board made of representatives of artists and the record companies. The royalty goes to the copyright holders in sound recordings (usually the record label) and performers on those recordings. Royalties are split 50% to the copyright owner and 50% to artists further split 45% to the featured artist and 2.5% to the American Federation of Musicians for non-featured musicians and 2.5% to the American Federation of Radio and Television Artists for non-featured vocalists.

The previous rate had been unchanged from 1998 to 2005 and had been $0.000768. Radio and Internet Newsletter calculates that assuming that the average station plays 16 songs per hour, large webcasters would have to pay "about 1,28 cents per listener per hour using the 2006 rate and would owe this retroactively in addition to licensing fees going forward", while tiny sites will owe a minimum of $500 per channel per year. Online music streamers banded together with traditional broadcasters to complain that the royalties were nearly equal or even exceeded their revenues.

In April 2007, the CRB issued an Order denying motions for rehearing. However, the CRB made changes to its own decision. The CRB first allowed a transitional option

for the years 2006 and 2007 to ease the shift in methodology and facilitate the timely payment of royalties, during which webcasters can continue to use ATH as a basis for calculation and payment of royalties. The CRB also set a July 15, 2007 deadline for the payment of retroactive royalties for 2006 and 2007. All parties to the case filed appeals with U.S. Court of Appeals for the Washington DC circuit, along with a motion to stay and suspend the CRB decision until all appeals have been heard. The motion was denied by the Court and the now royalty rates became effective on July 15, despite the pending appeal. On April 26, the Internet Radio Equality Act was introduced in the House of Representatives, in an attempt to void the March 2 , 2007 decision.

C. Internet Radio Equality Act, S. 1353 (IREA)

This bill was introduced on April 26, 2007 by Jay Inslee, in response to the Copyright Royalty Board March 2, 2007 decision relating to webcasting royalty rates. It is still being reviewed in committee. Primarily, the IREA declares the March 2, 2007 decision, the following order denying motions for rehearing and any subsequent modification by the Copyright Royalty Judges published in the Federal Register to be ineffective. In addition, the act proposes to replace standards for determining reasonable rates and terms of royalty payments for public performances of sound recordings by means of eligible nonsubscription transmission services and new subscription services with a requirement that such rates and terms be established in accordance with stated objectives of the Copyright Royalty Judges (currently, rates and terms are required to distinguish among different types of eligible nonsubscription transmission services and include a minimum fee for each type). The IREA would also allow a minimum annual royalty for each provider subject to such rates and terms and revise royalty payment

provisions concerning the use of certain works in noncommercial broadcasting to include sound recordings and performance or display by nonprofit organizations and public broadcasting entities.

D. Status of the IREA and of the negotiations

Sound Exchange agreed to sit down at the negotiating table with the various factions of the streaming community, so progress with the IREA is put on hold. Negotiations are taking place under the supervision of Congress. SoundExchange offered to reinstate the terms of the Small Webcasters Settlement Act of 2002 which expired in 2005 for the 2006-2010 period but it was rejected by a coalition of small webcasters who seeks changes to the CRB's proposed royalty rates and methodology, and supports a scheme that mimics the rates proposed by the Internet Radio Equality Act. SoundExchange had also suggested a settlement to noncommercial webcasters whereby their prior arrangement for royalty rates would be preserved but with some small alterations. The $500 annual minimum fee for 146,000 ATH would be maintained but the royalty rate for additional listeners would be caped at$0.0002176 per performance or $0.00251 per ATH. However, the proposal includes a new requirement that noncommercial webcaster provide records of use of sound recordings on a monthly basis. No final agreement has been reached yet.

Congress has also made strong calls for compromise. On July 12, 2007, Congress organized a meeting of both sides to discuss settling the dispute. SoundExchange offers an annual fee cap of $50,000 if the broadcaster reports everything that is played and adopts technology that limits the ability of listeners to copy broadcasts. This offer was

accepted by the Digital Media Association which represents large webcasters such as Yahoo!, RealNetworks and AOL, who promised to improve reporting and to “research, identify, review and evaluate” the prevalence of stream-ripping and potential technologies to limit it. However, SoundExchange denied making the offer as DiMA understood it while DiMA criticized SoundExchange for reneging on its offer and demanding technology mandates that are unreasonable. The possibility of a solution in the near future looks unlikely. However, National Public Radio, which represents public radio stations, reached a temporary agreement with SoundExchange to delay enforcement of the new fees and to continue good-faith negotiations until at least October 15.