STATEMENT OF RICK CARNES, PRESIDENT
THE SONGWRITERS GUILD OF AMERICA
BEFORE THE SUBCOMMITTEE ON COURTS,
THE INTERNET AND INTELLECTUAL PROPERTY
OF THE HOUSE COMMITTEE ON THE JUDICIARY

"The Section 115 Reform Act of 2006"
May 16, 2005

Chairman Smith, Ranking Member Berman, and Members of the Subcommittee, thank you for this opportunity to provide comments on behalf of The Songwriters Guild of America on draft legislation entitled "The Section 115 Reform Act of 2006". We greatly appreciate your invitation.

Founded in 1931, the Songwriters Guild of America (SGA) is the United States' oldest and largest organization run exclusively by and for songwriters. SGA is an unincorporated voluntary association representing approximately 5,000 songwriter members and the estates of deceased SGA members. SGA provides royalty collection and audit functions for its members, as well as music licensing.

My name is Rick Carnes and I am President of SGA. I am a working songwriter and have lived in Nashville since 1978. I have been fortunate to have had a modicum of success in my career-- including co-writing number one songs for Reba McEntire ("I Can't Even Get the Blues") and Garth Brooks ("Longneck Bottle") along with songs for Steve Wariner, Alabama, Pam Tillis, Conway Twitty, and Dean Martin among others.

Economic State of Songwriters

Let me begin by putting this legislation in perspective. Songwriters today are struggling to make ends meet. Revenues are diminishing throughout the industry. The small percentage of royalties that previously trickled down to the creators of the music – on whose creative output the entire music industry rests -- has been on the decline over the past several years. A substantial number of songwriters have left the profession entirely despite artistic success, because they simply can no longer support themselves or their families on dwindling royalty income. We therefore approach any proposed legislation with the following questions: (1) will the legislation do any harm to those songwriters who still make this artistic calling their profession; and (2) will the legislation improve the economic opportunities for those who wish to pursue the craft of songwriting full time?

I am reminded constantly of the perilous existence that all of us who have chosen songwriting as a profession labor under daily. Let me give you the painful facts. When I was a young songwriter, like every aspiring music creator I dreamed of having one of my songs on a million selling album. That, I imagined, would be the very pinnacle of success, assuring my financial security. A closer look at the real numbers illustrates just

how naïve I was to place my faith in the current system.

Under the present compulsory licensing provisions, a songwriter is to receive 9.1 cents per song on any CD ("phonorecord") manufactured and distributed, or legally downloaded, in the United States. So, if one of my songs appears on a million selling album, I am theoretically due $91,000 by statute. However, I split that money half and half with my music publisher by contract. That leaves me $45,500. Then I must split that in half again with the recording artist who co-wrote the song with me, leaving me with $22,750. Practically every artist now co-writes every song on his or her album with the primary songwriter, because the record labels have included a controlled composition clause in every new artist's contract that makes it financially ruinous for the artist to record more than one or two tracks that he or she did not co-write. The reason the record companies do this is so they can pay the artist, and his or her co-writer, 75% of the statutory mechanical royalty rate. Because of the controlled composition clause, and with transaction costs deducted, my royalty income is reduced by thousands more dollars.

Thus, after all is said and done, I end up making less than $17,000 for having a song on a million selling CD. Of course, given that the retail charge to consumers for a CD may be as high as $18, a million sales will generate up to $18 million for someone.

As Register of Copyrights Marybeth Peters observed last year, the current system of compensating authors under Section 115 is "antiquated". No songwriter could possibly argue with such a conclusion other than to insist it was an understatement.

How did American songwriters reach this economic nadir? The most obvious reason is the astonishing fact that the U.S. statutory mechanical royalty rate was not raised from the 2 cent level for 69 years from 1909 to 1978. And for the last 27 years, modest increases to 9.1 cents have not addressed that longstanding, bedrock inequity. The reason I am making less than $17,000 on a million sales is that I am getting 1936 wages in 2006! That truly is "antiquated" compensation. More and more songwriters simply can no longer afford to continue to expend the time and energy required to practice their craft, while attempting to support their families. And as we suffer personally, American musical culture --long a source of enormous national pride, international prestige, and positive trade balance-- is endangered along with us.

General Policy Issues Raised by Legislation

The SGA supports the general objective of simplifying the rules and procedures of section 115 to facilitate the licensing of all digital deliveries of musical works. We are pleased that the draft legislation confirms that "interactive streams" of music are digital phonorecord deliveries, as this clarification is essential to any legislative effort on this topic. We also strongly support the draft's apparent resolution of the record company "gatekeeper" problem, provided that certain bracketed language is included.

We do not object to the principle of establishing a general designated agent with the authority to bind all copyright owners of nondramatic musical works to digital music

licenses, ***provided,*** that songwriters are treated fairly through meaningful participation in the governance of these entities, that on balance the legislation will provide greater economic benefit than economic harm, and that songwriters will have full access to all financial records related to this arrangement.

It is a commonly held legislative principle that Congress cannot guarantee the economic consequences that a party will experience from a piece of legislation. When dealing with large companies or their representatives, this perspective is understandable. But the position of songwriters is unique. Many are at the end of their economic tether. Most are sole proprietors or small businesses. ***And without songwriters, there are no songs, no music, and nothing to digitally deliver.***

The possibility of economic damage to songwriters exists because music copyright owners would be bound by the licensing decisions of a designated agent in which they have no voice, and because limitations are placed on the exclusive rights that music copyright owners currently possess to exploit their artistic creations – in this particular instance, the server copies of streamed musical works. The question we ask ourselves is, "what economic benefits are included in the legislation that would be balanced against the potential for economic damage?" The clarification that interactive streams are within the "digital phonorecord delivery definition" is clearly an economic benefit. So is the resolution of the record-company "gatekeeper" problem, which appears to be resolved in the draft bill but is not certain. What other benefits does the legislation provide?

We look forward to working with the Subcommittee to ensure that, on balance, this legislation is good for songwriters and music copyright owners.

<u>Specific Comments on Draft Legislation</u>

The draft legislation is a sincere attempt to address many of the challenges to easier licensing of the digital delivery of music. We appreciate the spirit in which it is drafted. We nonetheless believe that certain changes are important to making this legislation worthy of approval by the subcommittee. These changes include the following:

1. Songwriter Participation in Designated Agent.

It is imperative that songwriters have a meaningful role in the governance process of any designated agent with the power to bind unwilling copyright owners of nondramatic musical works The inclusion of songwriters in the designated agency dispute resolution process (found at page 34 of the draft bill) is a good start, but it alone is not sufficient. First, the disputes that may be resolved under the bill do not include the initial setting of license rates and terms (particularly for new services where an interim rate might be sought), nor presumably do they include the ability to influence Designated Agent administration fees. Second, if royalties due to songwriters are improperly withheld, the songwriter or its music publisher may not have sufficient resources to contest the issue after the fact. It has been the sad history of the music industry that the most powerful actors can use their economic advantages to win wars of attrition against songwriters and

other less affluent copyright owners. It is imprudent to defer the question of licensing rates and terms and administration fees to a dispute resolution process. Instead, these issues should be considered upfront with at least one representative of songwriters present.

In order to cure this problem and ensure upfront that songwriters interests are not compromised, we suggest for example that page 14, lines 13-16 of the draft bill be amended to read as follows:

> "(III) The General Designated Agent shall be governed by a board of directors consisting of representatives of at least 4 music publishing entities, and of at least one representative with a fiduciary duty to the songwriting community and with no such duty to any other interested party under this section."

This change will help ensure that the rates and terms of digital licenses do not inadvertently worsen the current economic condition of songwriters, and that all major policy discussions regarding the licensing of new modes of digital music delivery and the setting of the agent's administration fees include the perspective of the songwriting community.

The issue of the fairness of license rates and terms to songwriters cannot be underestimated. There is no issue about which songwriters feel more passionately. For example, will the designated agent deviate substantially from the statutory rate when granting a license to a new digital music service? Is there a floor rate below which it will not sink? How will it address any residual record company "gatekeeper" issues that plague the attempts by music copyright owners to obtain a fair share of the revenues from popular music download services such as iTunes? Will it confirm that the actual rates provided for works created after June 1995 are in fact free of limitations imposed by controlled composition clauses, as required by the 1995 legislation? Without a songwriter member on the board of the general designated agent, we fear these issues will not receive full consideration. And if these issues are not properly considered, then the goals of this legislation are likely to be compromised, to the ultimate frustration of all parties to this proposal.

2. Elimination of Gatekeeper Problem.

A critical part of the industry compromise to make this legislation possible is elimination of the current ability of record companies to authorize the digital distribution of nondramatic musical works embodied in a sound recording. This current practice allows record companies to be the "gatekeepers" of the copyrighted works held by another party – music publishers and songwriters. We believe that this reform is a long time in coming and will substantially improve the transparency and fairness of royalty distribution to music copyright owners.

We are support the "blanket license" language starting on page 3 of the draft bill, but were surprised that the language to conform this change to the current law on page 42, lines 6-7, is found in brackets. From SGA's perspective, elimination of the brackets around this reform is essential. Creation of a designated agent with authority to bind all copyright owners under section 115 will be meaningless if the record companies can bypass the process and license the musical works on their own. Absent inclusion of this language, the necessary practical reforms and industry compromises are not clear.

We further wish to clarify that the effect of the bill's "gatekeeper" reform should be to render previously issued licenses pursuant to the record companies' pass-through licensing power null and void as of the effective date of this legislation. The musical composition rights in a substantial number of today's most desired nondramatic musical works have already been licensed by record companies to a number of popular music services. Failure to bring this regime to an end immediately, or at least by a date certain, will render this provision meaningless as well. Given the "blanket license" nature of the designated agent proposal, however, such an approach should not be a significant inconvenience for digital music companies that had previously obtained a musical composition license from a record company. We pledge to be sensitive to the administrative requirements for phasing out all vestiges of the gatekeeper function, but this is a provision whose prior effect and future practice must be ended.

3. Server Copy Licenses.

We understand that, in order to obtain agreement that interactive streaming is a digital phonorecord delivery, certain changes were necessary to clarify liability for server copies that facilitate streaming. We are concerned, however, about the proposal to provide royalty-free licenses for server copies of musical works for the purpose of facilitating noninteractive streaming. We also wish to note an ambiguity in the draft bill's language that could be read to provide for a mechanical license, only, for server copies used to facilitate interactive streaming.

First, the elimination of exclusive rights for all server copies clearly reduces the rights of music copyright owners under current law. The U.S. District Court for the Southern District of New York determined in *Rodgers and Hammerstein Org. v. UMG Recordings Inc.*, No. 00 Civ. 9322 (JSM), 2001 U.S. Dist. LEXIS 16111 (S.D.N.Y. 2001), that server copies for streaming services are outside of the statutory mechanical license and are among the exclusive rights held by music copyright owners. The provision granting a royalty-free license for server copies of noninteractive services would reduce the economic returns to songwriters and music copyright owners and provide a corresponding benefit to digital music companies. The "license facilitation" purpose served by this provision is minimal -- it serves more as a transfer of revenue from songwriters and music copyright owners to large corporations. We do not object to ensuring that server copies may be licensed, provided that interactive streaming is clarified as being a DPD. But at the very least, if license facilitation is the objective, then server copies for noninteractive streams should be included in the rate-setting process for

the similar copies that facilitate interactive streams, rather than found to be without economic value, because that is not the case.

Second, the bill's language can be read to include server copies within the mechanical rate for interactive streams, thus creating the possibility of economic loss. When clarifying that interactive streams constitute a "DPD," we believe that a corresponding limitation of exclusive rights to the server copies for such streams can be justified. But the current language creates the possibility that a server copy will receive a mechanical royalty only. There is no question that the actual economic value of such copies is well in excess of 9 cents per song. And we are troubled by the linkage of server copies to "other incidental reproductions" necessary to facilitate the streaming of the musical work, as this implies that Congress gives the two comparable value, which is certainly not the case in the market place. We therefore recommend that the legislation give clear directions to the Copyright Royalty Board that previous rates negotiated for server copies under current law have significant precedential weight in determining the statutory rate for such server copies, or that the rate-setting process for the entire interactive streaming process consider this as a factor when establishing the proper rate.

The position we take here is consistent with positions taken by the Copyright Office. In its Section 104 Report, the Copyright Office argued that copies without intrinsic economic value, such as incidental reproductions made to facilitate streamed music, should not be subject to mechanical royalty obligations. In this case, there is clear evidence that server copies ***DO*** have intrinsic economic value. As such, the draft bill should not impose a "royalty-free license" requirement on noninteractive-stream server copies, nor should it fail to recognize the value of interactive-stream server copies. We respectfully request that these provisions be amended.

We should emphasize that giving up exclusive rights to server copies for interactive streams is not insignificant. It is not simply a question of money – it is also an issue of control over the works before they leave our hands. Music copyright owners need to identify and track the usage of the songs that are digitally delivered, in order to collect and distribute the royalties in a fair and accurate manner. When we give up the exclusive right to the server copy, we give up the ability to insist on collection of appropriate data on usage of these works by licensees. As you are probably aware, the scope of "metadata" included in each song is an important but unresolved topic among owners and users of digitally distributed music.

In summary, in exchange for confirmation that an interactive stream is a DPD, the exclusive rights currently held in server copies may be incorporated into the statutory license, but the legislation should ensure that a fair rate is set for such server copies – as they currently have economic value that should not be disregarded or eliminated.

4. Audit Procedures.

The establishment of sound and reasonable audit procedures are critical to ensuring that the new section 115 licensing process is transparent to all parties. Mr. Chairman, to

paraphrase a real estate broker, the three essential features of an effective designated agent bill are "transparency, transparency, transparency."

We are initially troubled by the sparse language describing the information that digital music provider licensees are required to provide to designated agents. Page 22, line 22 of the draft bill states that "each licensee under this subsection shall, on a monthly basis and in electronic format, report its usage of musical works under the license, and make royalty payments by reason of such usage . . ." There is no other language of substantive effect, and we find this standard to be insufficient. We believe that the concepts from the section 115(c) requirements should be imported here, including detailed cumulative annual statements of account from all licensees. These statements should be certified by a public accountant and then attested to by the digital music provider as complete and accurate. And the usage data transmitted by the licensee should include the name of the composition and the principal authors of the work, to minimize administrative costs to music copyright owners and to ensure proper accounting.

We are also concerned by the language on page 23, line 5, that places "Limitations on Disclosure" of audit information from a designated agent to a recipient of royalty payments from a digital music company licensee. We believe there is no reason to limit disclosure of royalty and audit information "to musical works owned or controlled by the recipient" (page 23, lines 10-12). This would appear to limit distribution of audit data in many cases solely to music publishers, even though publishers collect such payments on behalf of songwriters and split the proceeds with them under various contractual arrangements and in varying ratios. Newer music publishing contracts often provide songwriters up to 75% of the royalty payments. In this instance, there is no doubt that the songwriter is an interested party entitled to information from the designated agent on the extent and amount of payments received from digital music providers. We therefore suggest that the sentence on page 23, line 6 be amended to read as follows:

> "A designated agent may disclose information received under clause (i) to a recipient of royalty payments made by a licensee only with respect to musical works owned or controlled by the recipient, and shall ensure that any such disclosure be made available as well to the party in privity with such recipient with respect to such musical works."

The audit procedures in the draft bill are complicated, and the current audit practices in the music industry are fraught with controversy. We therefore request additional time to review the bill's provisions to determine whether we have additional comments on this critical topic.

<u>Additional Legislation Is Relevant to Songwriter Interests</u>

Finally, we wish to point out that we are not looking at this draft legislation in a vacuum. There is other legislation pending that would have an economic effect on songwriters, and we would weigh this legislation in conjunction with the other bills.

One such bill is the draft Senate legislation to amend section 114 to address new technologies and copying capabilities to be offered by satellite radio services. We support the principles of the Feinstein legislation, because it addresses an important question in the digital delivery of music. But the theory behind the section 114 legislation is relevant to section 115 parties as well. The new satellite radio services are likely to displace the retail sale of phonorecords. To the extent this occurs, then the rights of music copyright owners in section 115 are clearly implicated. In fact, the legislative history behind the 1995 amendments that created the "digital phonorecord delivery" definition makes this precise point. When digitally delivered music results in diminished sale of phonorecords, compensation to owners of nondramatic musical works is required. Without consideration of this problem, songwriters will once again face a reduction in their royalty income.

Conclusion.

As we stated at the beginning, SGA supports the objective of the legislation and desires to take a constructive role going forward. We are currently reviewing the positive aspects of the legislation to ensure they outweigh the negative aspects. There are clearly positive aspects, particularly the clarification that interactive streams of music are within the digital phonorecord delivery mechanism. And there are benefits that we hope will be confirmed shortly, such as the elimination of the "gatekeeper" problem, which is essential to the compromise that this legislation seeks to obtain.

We seek to understand the benefits better, so that we can balance them against the negative aspects of the bill to our members, which include the ability of a designated agent which currently has no meaningful songwriter input to bind all of our members to digital music licenses to which they may object. Mr. Chairman and Members of the Subcommittee, we seek to work with you to ensure that this legislation strikes the proper balance and will be beneficial to the individuals on which the music industry relies – the songwriters.

Thank you for your attention and consideration of these views.