LIBRARY OF CONGRESS

Copyright Office

[Docket No. 2009–1]

Review of Copyright Royalty Judges Determination

AGENCY: Copyright Office, Library of Congress.

ACTION: Notice; correction.

SUMMARY: The Register of Copyrights issues the following decision identifying and correcting erroneous resolutions of material questions of substantive law under title 17 that underlie or are contained in the Copyright Royalty Judges' final determination regarding adjustment of reasonable rates and terms of royalty payments for the making and distribution of phonorecords of musical works, Docket No. 2006–3 CRB DPRA. The Register concludes that the Copyright Royalty Judges erroneously did not refer two novel questions of law as required under the statute; that they were in error in their conclusions regarding both their and the Register's authority to review regulations submitted to them under an agreement by the participants; and that their conclusion that they could not review the agreement submitted by the participants led to the inclusion of regulations that constitute erroneous resolution by the CRJs of material questions of substantive law under title 17. This decision corrects such errors and shall be made part of the record of the proceeding (Docket No. 2006–3 CRB DPRA).

FOR FURTHER INFORMATION CONTACT: Tanya M. Sandros, Deputy General Counsel, and Stephen Ruwe, Attorney Advisor, Copyright GC/I&R, P.O. Box 70400, Washington, DC 20024. Telephone: (202) 707–8380. Telefax: (202) 707–8366.

SUPPLEMENTARY INFORMATION:

Background

The Copyright Royalty Judges (''CRJs'') are required by 17 U.S.C. 115(c)(3)(C) and Chapter 8 to make and issue determinations and adjustments of reasonable rates and terms of royalty payments for the making and distribution of phonorecords of musical works in accordance with the provisions of 17 U.S.C. 115. Under 17 U.S.C. 802(f)(1)(D), the Register of Copyrights may review for legal error the resolution by the CRJs of a material question of substantive law under title 17 that underlies or is contained in a final determination of the CRJs. If the Register of Copyrights concludes, after taking into consideration the views of the participants in the proceeding, that any resolution reached by the CRJs was in material error, the Register of Copyrights shall publish such decision correcting such legal errors in the **Federal Register**, together with a specific identification of the legal conclusion of the CRJs that is determined to be erroneous, which shall be made part of the record of the proceeding.

On November 24, 2008, the CRJs issued to the participants, posted to their Web site, and transmitted to the Register of Copyrights a copy of their final determination setting such rates and terms. *Final Determination of Rates and Terms in the Matter of Mechanical and Digital Phonorecord Delivery Rate Determination Proceeding*, Docket No. 2006–3 CRB DPRA (November 24, 2008). The Register of Copyrights, pursuant to section 802(f)(1)(D), has reviewed the CRJs' final determination. The Register concludes that the resolution of certain material questions of substantive law under title 17 that underlie or are contained in the final determination were in error and issues this decision correcting such errors.

In the course of their proceeding to set rates and terms of royalty payments for the making and distribution of phonorecords of musical works in accordance with the provisions of 17 U.S.C. 115, the CRJs addressed several material questions of substantive law that were properly referred to the Register of Copyrights under 17 U.S.C. 802(f)(1)(A)(ii) and 802(f)(1)(B). However, the Register determines that they erroneously did not refer two additional novel questions of law as required under the statute. The Register also finds that the CRJs were in error in their conclusions regarding both their and the Register's authority to review regulations submitted to them under an agreement by the participants. The CRJs' conclusion that they could not review these regulations led to the inclusion of regulations that constitute erroneous resolutions of material questions of substantive law under title 17, which as stated, are corrected herein.

The regulations ultimately contained in the CRJs' final determination establishing rates and terms of royalty payments for the activities under section 115, i.e. ''making and distributing phonorecords, including by means of digital phonorecord deliveries,'' are divided into two subparts. The first portion, Subpart A, is the product of the findings and deliberations of the CRJs, and delineates the rates and terms for three distinct categories of phonorecords under the section 115 license. These particular categories identify phonorecords made under specific conditions and are categorized as ''Physical phonorecord deliveries,'' ''Permanent digital downloads'' and ''Ringtones.'' *See* 37 CFR 385.1–385.4.[1] The second portion, Subpart B, is the product of settlement negotiations among the participants, and delineates the rates and terms for two additional distinct categories identifying phonorecords made under the section 115 license. These particular categories identify phonorecords made under specific conditions and are identified as ''Interactive streaming'' and ''Limited downloads.'' Subpart B also indicates specific conditions under which ''promotional royalty rates'' are applicable to ''Interactive streaming'' and ''Limited downloads.'' *See 37* CFR 385.10–385.17. The Register observes that although the participants informed the CRJs that their agreement would address Limited downloads and Interactive streaming, including all known incidental digital phonorecord deliveries, their agreement ultimately only addressed ''Interactive streaming'' and ''Limited downloads,'' thus addressing less activity than might reasonably have been expected.

The Register has also concluded that in setting forth rates and terms for these five distinct categories of phonorecords, the CRJs' final determination does not include rates and terms for certain ongoing activities which may be licensable under the section 115 license, *e.g.*, phonorecords made during the course of a non-interactive stream. Nevertheless, if a licensee makes and distributes phonorecords that do not fall within any of the five distinct categories of phonorecords for which specific rates have been set, the making and distribution of these phonorecords may still be covered by the section 115 license, so long as the licensee operates within the statutory terms of the license, including the provisions addressing Notice of Intention to Use and Statements of Account, but the licensee would incur no obligation to pay royalties for such activity during the relevant time period. However, under certain circumstances, which are dictated by section 803(d)(2)(B), royalty rates may be set retroactively in future proceedings.

Procedural Background of the CRJs' Proceeding

On January 9, 2006, the CRJs issued a Notice announcing commencement of this proceeding with a request for

[1] The Register cites to the regulations in the final determination, 37 CFR 385.1–385.17, by the references adopted by the CRJs. As of the date of this review, they have not been codified in the Code of Federal Regulations.

Petitions to Participate, which was published in the **Federal Register**. 71 FR 1453. In response to the Notice, the following parties submitted petitions to participate: Royalty Logic, Inc. (''RLI''); the Songwriters Guild of America (''SGA''); the National Music Publishers'' Association, Inc. (''NMPA''), the Songwriters Guild of America, and the Nashville Songwriters Association International, jointly (collectively, ''Copyright Owners''); Apple Computer, Inc.; America Online, Inc.; RealNetworks, Inc.; Napster, LLC; Sony Connect, Inc.; Digital Media Association (''DiMA''); Yahoo! Inc.; MusicNet, Inc.; MTV Networks, Inc.; and Recording Industry Association of America (''RIAA'').

On August 1, 2006, prior to the filing of written direct statements, RIAA sought from the CRJs a referral of a novel question of law to the Register of Copyrights (''Register''). *See Motion of [RIAA] Requesting Referral of a Novel Question of Substantive Law* (filed August 1, 2006). RIAA asserted that the CRJs were compelled to refer the novel question of law to the Register under section 802(f)(1)(B). After considering the views of all of the participants, the CRJs granted RIAA's motion in part and referred to the Register two novel questions of law regarding (1) whether ringtones—regardless of whether the ringtone is monophonic, polyphonic or a mastertone—constitute delivery of a digital phonorecord subject to statutory licensing under section 115 and (2) if so, what legal conditions and/or limitations would apply. *See Order Granting in Part the Request for Referral of a Novel Question of Law, Docket No. 2006–3 CRB DPRA (August 18, 2006)*. On October 16, 2006, the Register transmitted a Memorandum Opinion to the CRJs that addressed the novel questions of law. The Register's Memorandum Opinion was published in the **Federal Register** on November 1, 2006. 71 FR 64303.

On January 7, 2008, DiMA requested referral to the Register of what it described as a novel question of law as to whether ''interactive streaming'' constituted a digital phonorecord delivery (''DPD''), asserting that the CRJs were compelled to refer the novel question of law to the Register under section 802(f)(1)(B). *See Motion of [DiMA] Requesting Referral of a Novel Material Question of Substantive Law* (''DiMA Motion'') (January 7, 2008). Copyright Owners opposed DiMA's motion and RIAA took no position on it. The CRJs heard oral arguments on the motion on January 28, 2008. On February 4, 2008, the CRJs denied DiMA's motion, finding that the matter of what is ''interactive streaming'' presented a question of fact and not a question of law as required by section 802(f)(l)(B). *See Order Denying Motion of [DiMA], for a Referral of a Novel Material Question of Substantive Law, Docket No. 2006–3 CRB DPRA* (February 4, 2008).

Subsequent to the presentation of the rebuttal phase of their case, on May 15, 2008, the participants informed the CRJs that they had reached a settlement regarding the rates and terms for ''limited downloads and interactive streaming, including all known incidental digital phonorecord deliveries'' and agreed to submit the agreement to the CRJs at a later date. *See Joint Motion to Adopt Procedures for Submission of Partial Settlement* at 1 (filed May 15, 2008).

On July 2, 2008, after the evidentiary phase addressing the remaining issues in the proceeding, the participants filed their respective Proposed Findings of Fact and Conclusions of Law. The participants filed replies on July 18, 2008. Closing arguments occurred on July 24, 2008, after which time the record was closed.

On July 25, 2008, after closing arguments, the CRJs, on their own motion and under authority established in section 802(f)(1)(A)(ii), referred to the Register a material question of substantive law concerning the division of authority between the CRJs and the Register to establish terms under the section 115 statutory license. *See Order Referring Material Question of Substantive Law, Docket No. 2006–3 CRB DPRA* (July 25, 2008). On August 8, 2008, the Register transmitted a Memorandum Opinion to the CRJs that addressed the material question of substantive law. The Register's Memorandum Opinion was published in the **Federal Register** on August 19, 2008. 73 FR 48396.

On September 22, 2008, the participants filed their partial settlement with the CRJs, and it was published in the **Federal Register** on October 1, 2008. 73 FR 57033. Public comments were due on October 31, 2008. CTIA-The Wireless Association and the National Association of Broadcasters (''CTIA/NAB''), non-participants to the rate setting proceeding, jointly filed the only comment on the agreement. They argued that adoption of the settlement was beyond the CRJs' authority, contrary to law and bad policy. *See Comments of CTIA-The Wireless Association and the National Association of Broadcasters* (filed October 31, 2008).

On October 2, 2008, the CRJs issued their Initial Determination of Rates and Terms subject to review by the participants and the filing of motions for a rehearing. *See* 17 U.S.C. 803(c)(1) and (2)(A) and (b). On October 17, 2008, RIAA filed a motion for rehearing to reconsider the timing of the late payment fee of 1.5% per month. After reviewing the motion, the CRJs denied the motion for rehearing, by Order dated November 12, 2008. On November 24, 2008 the CRJs issued to the participants a copy of their *Final Determination of Rates and Terms in the Matter of Mechanical and Digital Phonorecord Delivery Rate Determination Proceeding, Docket No. 2006–3 CRB DPRA* (''Final Determination''), and transmitted a copy to the Register of Copyrights. *See Final Determination of Rates and Terms in the Matter of Mechanical and Digital Phonorecord Delivery Rate Determination Proceeding, Docket No. 2006–3 CRB DPRA* (November 24, 2008).

On January 8, 2009, the Register requested the participants' views on potential legal errors contained in the CRJs' final determination. In response, the Register received written views from RIAA, Copyright Owners, and DiMA on January 15, 2009.

In accordance with the authority granted to the Register of Copyrights under 17 U.S.C. 802(f)(1)(D), the Register of Copyrights has reviewed the CRJs' determination of rates and terms of royalty payments under section 115 taking into account the views of the participants as reported in the CRJs' final determination and in response to a request from the Register for written comments on specific issues. *Request for Participants' Views Regarding Possible Legal ErrorsCcontained in the Copyright Royalty Judges' Final Determination* (January 8, 2009). The Register concludes that certain resolutions of material questions of substantive law under title 17 which underlie or are contained in the final determination of the CRJs are in error.

Review of Copyright Royalty Judges' Determination

1. Failure To Refer Novel Questions to the Register

Under 17 U.S.C. 802(f)(1)(B), in any case in which a novel material question of substantive law concerning an interpretation of those provisions of title 17 that are the subject of the proceeding is presented, the CRJs are required to request a written decision from the Register of Copyrights to resolve such a novel question. A ''novel question of law'' is a question of law that has not been determined in prior decisions, determinations, and rulings described in section 803(a) of the Copyright Act. *See*

17 U.S.C. 802(f)(1)(B)(ii). During the course of the proceeding, the CRJs referred two novel questions of substantive law to the Register, but they did not refer two additional novel material questions of substantive law concerning an interpretation of provisions of title 17. The CRJs' failure to refer a novel material question of substantive law is itself an erroneous legal resolution of ''a material question of substantive law under [title 17] that underlies or is contained in a final determination of the [CRJs].'' Therefore any failure to refer a novel material question is subject to the Register's review under section 802(f)(1)(D).

One such novel question arose amidst DiMA's motion for referral to the Register of what DiMA described as a novel question of substantive law as to whether ''interactive streaming'' constitutes a DPD under section 115. *See Motion of [DiMA] Requesting Referral of a Novel Material Question of Substantive Law* (filed January 7, 2008). After hearing the participants' arguments on the motion, the CRJs denied DiMA's motion, finding that the matter of what is ''interactive streaming'' presented a question of fact and not a question of law as required by section 802(f)(l)(B); a view shared by Copyright Owners. The CRJs accurately noted that the statute does not define or mention the term ''interactive streaming'' and that there is no agreement among the participants as to the precise meaning of the term. Additionally, the CRJs asserted that resolution of DiMA's question would require a certain amount of inquiry into the factual circumstances, and the types of digital transmissions, that may or may not result in reproductions of musical works that are licensable under section 115. *See Order Denying Motion of [DiMA], for a Referral of a Novel Material Question of Substantive Law, Docket No. 2006–3 CRB DPRA* (February 4, 2008).

The Register notes that when the CRJs are confronted with novel material questions of law they are not restricted to considering the motions and formulations of questions as submitted by the participants. Rather, they are required to refer any novel questions (or issues) of law ''concerning an interpretation of those provisions of [title 17] that are the subject of the proceeding.'' 17 U.S.C. 802(f)(1)(B).

While the issue of what is ''interactive streaming'' does appear to involve some degree of factual inquiry, it also raises at least one purely legal question that does not require resolution of specific factual disputes raised between the participants. For some time, the Office has recognized a general agreement among interested parties that streaming necessarily involves reproductions that are made on the receiving computer in order to better facilitate the actual performance of the work (often referred to as ''buffer'' copies). *See Notice of Inquiry* 66 FR 14099 (Mar. 9, 2001). The view that ''interactive streaming'' necessarily involves the making and delivery of buffer copies does not appear to be disputed among the participants to the proceeding. The purely legal question raised under such an undisputed understanding regarding ''interactive streaming'' is ''What constitutes a DPD?'' This question clearly requires an interpretation of a provision of title 17. Specifically, it requires an interpretation of the definition of ''digital phonorecord delivery'' as found in section 115(d).

Additionally, regardless of the factual issues surrounding DiMA's original motion for referral, the Register observes that when the CRJs considered two novel questions concerning the scope of the section 115 license with regard to ringtones—a term also not defined or even mentioned in title 17—the participants submitted briefs that revealed significant factual disagreement as to whether certain ringtones constituted derivative works. In spite of this disagreement, the questions regarding ringtones were properly referred to the Register. Moreover, the Register was able to provide a responsive and instructive decision on the legal questions which acknowledged that factual distinctions would continue to dictate whether various ringtone activities fell within the scope of the section 115 license without needing to resolve any dispute over specific factual situations. *See Memorandum Opinion on Material Questions of Law, Docket No. RF 2008–1* at 10 (August 8, 2008); *see also,* 73 FR 48396 (Aug. 19, 2008). Finally, the Register notes that section 802(f)(1)(B) does not confine the concept of novel question of substantive law to those involving interpretation of terms defined or mentioned in title 17.

Failure to refer the question of what constitutes a DPD to the Register has led to the adoption of a regulation that, on its face, overstates the scope of the section 115 license with respect to interactive streams. *See* 37 CFR 385.11 (defining an interactive stream as an incidental DPD). As discussed in a subsequent portion of this review, the CRJs may exercise their continuing jurisdiction to redraft the regulation to clarify that an interactive stream that delivers a reproduction of a sound recording that qualifies as a DPD is, for purposes of the license, an incidental DPD.

A second novel question was the subject of DiMA and RIAA's requests for a clarification of the statute. DiMA and RIAA, using slightly different language, requested a determination as to the scope of the license with respect to copies made to facilitate the delivery of digital music. *See DiMA PFF at ¶240* (July 2, 2008); *DiMA Second Amended Proposed Rates and Terms at 4* (July 2, 2008); *RIAA PFF at ¶1674–76, 1678–82* (July 2, 2008); *RIAA Second Amended Proposal at 6* (July 2, 2008). Citing to the Register's August 19, 2008, *Memorandum Opinion Responding to Material Questions of Law*, the CRJs concluded that DiMA and RIAA's requests would require interpretation of the scope, operation and/or obligations of the section 115 license, which is inconsistent with the CRJs' authority. *Final Determination* at 71–72, citing to *Memorandum Opinion on Material Questions of Law, Docket No. RF 2008–1* at 10 (Aug. 8, 2008); *see also*, 73 FR 48396, 48399 (August 19, 2008). The CRJs are correct in this conclusion. Furthermore, the CRJs are correct that such questions of scope are inconsistent with their authority. In making these observations, the CRJs appear to recognize that the participants' requests constituted a material question of substantive law. However, they do not appear to have recognized that the question was a novel one, and therefore required referral to the Register. Indeed, in the same Memorandum Opinion relied upon by the CRJs when they declined to interpret the scope of the license, the Register stated that ''In instances where particular rates are being requested for the creation of particular types of DPDs and there is some question whether these DPDs fall within the scope of the license, those questions must be resolved in the proceeding. When such a question has not been determined before, it is a novel question of law which should be referred to the Register under section 802(f)(1)(B).'' 73 FR at 48399.

Ultimately, the failure to refer this question is a harmless error because the Register has addressed the question and has determined, on an interim basis, that ''server copies and intermediate reproductions may come within the scope of the license. The Register note[d] that a person seeking to operate under the section 115 license must still satisfy the threshold requirements of the license. But, having done so, that licensee's coverage may extend to phonorecords other than those that are actually distributed provided that they

are made for the purpose of making and distributing a DPD.'' *Id.* at 66180.

Despite the fact that the failure to refer this question was ultimately harmless, had the CRJs referred the question, the participants and the CRJs could have adopted regulations that more clearly reflect the Register's clarification of the legal issue. *See* 37 CFR 201.18(a)(3); 201.19(a)(3); and 255.4. (Noting that ''a digital phonorecord delivery includes all phonorecords that are made for the purpose of making the digital phonorecord delivery.)''.

2. Erroneous Conclusion Regarding Authority Under Chapter and Section 115.

a. CRJs' authority to review.

Section 801(b)(7)(A) generally directs the CRJs to adopt as a basis for statutory terms and rates ''an agreement concerning such matters reached among some or all of the participants in a proceeding at any time during the proceeding between participants.'' In interpreting this provision, the CRJs concluded that ''[o]nly if an objection is received by one or more of the parties are we given any discretion over the settlement, and then we are limited to rejecting it if we determine that the settlement 'does not provide a reasonable basis for setting statutory rates and terms.''' *Final Determination* at 18–20, citing section 801(b)(7)(A)(ii) (emphasis added). RIAA, DiMA, and the Copyright Owners support the CRJs' interpretation of section 801(b)(7)(A). *Views of RIAA* at 6; *Views of Copyright Owners* at 9–10; and *Views of DiMA* at 1 (January 15, 2009). This interpretation, however, is in error.

While the provisions of section 801(b)(7)(A) do limit the circumstances under which the CRJs are able to decline to adopt aspects of an agreement, it does not foreclose the CRJs from ascertaining whether specific provisions are contrary to law. The noted limitations only apply to the CRJs' ability to adopt an agreement ''as a basis for statutory rates and terms,'' 17 U.S.C. 801(b)(7)(A), and, in doing so, they promote Congress's policy to encourage parties to negotiate statutory rates and terms. *See Views of RIAA* at 6 and Views of Copyright Owners at 11–12 (January 15, 2009).

The CRJs are not compelled to adopt a privately negotiated agreement to the extent it includes provisions that are inconsistent with the statutory license. Thus, while the CRJs are able to review the reasonableness of permissible terms and rates contained in an agreement only if a participant to the proceeding objects to the agreement, this provision does not preclude the CRJs from declining to adopt other portions of an agreement that would be contrary to the provisions of the applicable license(s) or otherwise contrary to statutory law. Furthermore, nothing in the statute limits the CRJs from considering comments filed by non-participants which argue that proposed provisions are contrary to statutory law.

This conclusion is consistent with the CRJs' decision that it had the authority to decline to adopt language in the participants' agreement that stated that the rates in the agreement have no precedential effect and may not be introduced or relied upon in any governmental or judicial proceeding. 72 FR 61586. Moreover, courts have consistently held that agencies cannot adopt regulations that are contrary to law. *See, e.g., Vasquez-Lopez* v. *Ashcroft*, 343 F.3d 961, 965 (9th Cir. 2003) (''The power of an administrative officer or board to administer a federal statute and to prescribe rules and regulations to that end is not the power to make law * * * but the power to adopt regulations to carry into effect the will of Congress as expressed by the statute. A regulation which does not do this, but operates to create a rule out of harmony with the statute, is a mere nullity.''), cited in *Joint Comment of CTIA–The Wireless Association and the National Association of Broadcasters* at 6, filed with Copyright Royalty Judges in response to their notice for comment on the participants agreement. 73 FR 57033 (Oct. 1, 2008).

Since the purpose of this proceeding is to establish rates and terms of payment for a statutory license, an agreement among the participants may only extend to establishing rates and terms which are permissible under the statute. Neither the participants nor the CRJs may add terms or conditions that alter or expand the statutory license. Hence, it was legal error for the CRJs to conclude that the restrictions on its authority to review the reasonableness of specific valid terms and rates also precluded its review of the legality of the provisions of the agreement as a threshold matter.

b. Register's authority to review.

The CRJs' erroneous conclusion that it had no authority to review broad aspects of the participants' agreement led them to also conclude that the settlement does not represent a resolution by the CRJs and that therefore the Register's review is not part of the procedure applicable to the relevant rates and terms established by the settlement provisions of section 802(f)(1)(D). *Final Determination* at 19–20. The CRJs, however, have no authority to determine whether the Register, in her review of the CRJs' final determination, has the authority to review for errors of law provisions in a settlement that is adopted by the CRJs. In reaching their conclusion, the CRJs argue that the provisions of the settlement do not constitute a finding of fact or resolution of law by the CRJs. However, as previously indicated, and despite their mistaken belief, the CRJs were not obligated to adopt *any* portion of an agreement that would be contrary to the provisions of the applicable license(s) or otherwise contrary to statutory law. By choosing to include provisions that they were able to reject, such provisions were freely adopted as resolutions by the CRJs.

Furthermore, section 801(b)(7)(A) requires the CRJs to ''*adopt* as a basis for statutory terms and rates or as a basis for the distribution of statutory royalty payments, an agreement concerning such matters reached among some or all of the participants in a proceeding,'' (emphasis added). By ''adopting'' an agreement, the CRJs necessarily accept the terms of the agreement and ''resolve'' any material question of substantive law that the adopted agreement purports to resolve.

c. CRJs' authority to determine rates for future activities.

The CRJs indicate that in this proceeding they were unable to adopt rates for future activities without acting arbitrarily and capriciously. *Final Determination* at 60–62 (November 24, 2008). The Register acknowledges that the CRJs decry the empty record in the instant case and finds no error in their decision not to set rates for future activities in this instance. However, to the extent the CRJs believe they lack the authority to set rates for future activities, the Register notes that the statute does not foreclose that possibility. Congress contemplated that the CRJs may set rates for particular activities, even prior to the inception of such activities.[2] Additionally, the Register observes that the CRJs have broad discretion in making their determinations. *See RIAA* v. *Copyright Royalty Tribunal*, 662 F.2d 1, 8 (D.C. Cir. 1981) (stressing that ''[t]he setting of the royalty rate is not a routine exercise in historical cost of service ratemaking for a public utility''). Furthermore, the Register notes that Congress directed the CRJs to set royalty rates based upon broad policy objectives that require judgments of an inescapably uncertain and predictive character. See 17 U.S.C.

[2] ''In cases where rates and terms have not, prior to the inception of an activity, been established for that particular activity under the relevant license, * * *'' 17 U.S.C. 803(d)(2)(B).

801(b)(1). For example, ''some of the statutory factors require the [Judges] to estimate the effect of the royalty rate on the future of the music industry,'' or to consider questions of ''fairness.'' *RIAA*, 662 F.2d at 8.

d. CRJs' authority to limit scope of the license by not setting certain rates.

The Register also observes that the consequence of the CRJs having set rates and terms for distinct categories of phonorecords, does not mean that the license is not available for additional activities under section 115. This observation is in contrast to the participants' views expressed in the closing arguments of the proceeding indicating that rights for categories of phonorecords for which no rate is set may only be cleared through negotiation. *See Closing Argument Transcripts* 7/24/08 at 7843–7844; 7954; 7975; and 7989.

As the Register observed in her response to the CRJs' referral of material questions of substantive law concerning the division of authority between the CRJs and the Register, ''[t]he CRJs do not have the authority to issue rules setting forth the scope of activities covered by the license.'' *Final Order, Division of Authority Between the Copyright Royalty Judges and the Register of Copyrights under the Section 115 Statutory License* 73 FR 48399 (Aug. 19, 2008). Section 115 provides a license for the making and distribution of phonorecords, including DPDs. It does not condition coverage on whether a rate for the making and distribution of the phonorecords has been set. Consequently, failure to set a rate for any particular category of phonorecords cannot diminish or otherwise affect the availability of the license. Rather, when categories of phonorecords created in the course of particular ongoing activities within the scope of the license are not assigned a rate, the result is that there is no obligation to pay royalties for those particular activities during the relevant time period. Therefore, contrary to the conclusion of RIAA, there is no ''gap'' in coverage for DPDs that do not qualify as permanent digital downloads, limited downloads or interactive streams. *See Views of RIAA* at 5 (January 15, 2009). However, future proceedings may retroactively apply rates to a particular activity under section 115 in cases where rates and terms have not, prior to the inception of that activity, been established for the particular activity. Such retroactive rates and terms shall then apply from the inception of the particular activity. *See* Infra section 3(b) regarding the final determination's treatment of ''retroactive rates'' under 17 U.S.C. 803(d)(2)(B).

3. Problematic provisions in the regulations promulgated in the final determination.

In addressing the following regulatory provisions contained in the final determination, the Register acknowledges that both RIAA and Copyright Owners have argued that section 385.10 of the regulations satisfactorily addresses instances in which the rates and terms are, on their face, contrary to the statute. *See Views of RIAA* at 8 (January 15, 2009); Views of Copyright Owners at 15 (January 15, 2009). While section 385.10 states that rates and terms shall be ''in accordance with the provisions of 17 U.S.C. 115'' and requires that a licensee shall ''comply with the requirements of that section,'' such a provision is insufficient to address regulatory language that directly conflicts with the statute. The following regulations either conflict with statutory provisions in title 17 or could be read to alter or expand the statutory license. Prior determinations of the Librarian of Congress have considered and rejected similar terms that would have altered or expanded the statutory licenses as contrary to law. *See* Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings, 63 FR 45269 (July 8, 2002) (The Librarian concluded that neither the CARP nor the Librarian had the authority to adopt a regulation, whether as a condition of the license or not, that would foreclose a legal remedy for a breach of a legal obligation). Therefore, consistent with prior decisions specified in 803(a), and under the authority conferred by 802(f)(1)(D), the Register finds the following terms erroneous to the extent indicated herein.

a. Interactive streams constitute DPDs.

Section 385.11 of the regulations set forth in the final determination, which states that ''[an] interactive stream is an incidental digital phonorecord delivery under 17 U.S.C. 115(c)(3)(C) and (D)'' is erroneous. This articulation of what constitutes a DPD equates a means of transmission to the reproduction and delivery of a phonorecord. However, regulations cannot alter statutory terms of the section 115 license regarding what constitutes a DPD.

The statutory criteria as to what constitutes a DPD are set forth in the notice announcing an Interim Rule in which the Office explains that a DPD requires a reproduction of a sound recording that must meet all three criteria specified in the statutory definition: (1) It must be delivered, (2) it must be a phonorecord, and (3) it must be specifically identifiable. 73 FR 66173, 66176 (Nov. 7, 2008). Moreover, this Copyright Office rulemaking proceeding also addressed the question of interactive and non-interactive streams, noting that the determination of what constitutes a DPD is not dictated by the characterization of the transmission that delivers the phonorecord as interactive or non-interactive. Nevertheless, the Office did acknowledge that ''it may be more common for interactive streams to result in DPDs and that it may be relatively uncommon for non-interactive streams to do so. However, if phonorecords are delivered by a transmission service, then under the last sentence of 115(d) it is irrelevant whether the transmission that created the phonorecords is interactive or non-interactive.'' *Id.* at 66180. In other words, a stream—whether interactive or non-interactive—may or may not result in a DPD depending on whether all the aforementioned criteria are met. A regulation that provides categorically that ''[a]n interactive stream is an incidental digital phonorecord delivery under 17 U.S.C. 115 (c)(3)(C) and (D)'', without regard to whether any of those required criteria have been met, articulates an erroneous conclusion of law.

Hence, in light of the Office's analysis accompanying its adoption of a more particularized definition of a DPD, the proposed regulation which states that all interactive streams, as defined by the agreement, are DPDs, is overbroad because it would include interactive streams that do not result in the delivery of a DPD. The Office recognizes, however, that the regulation may not have been intended to set a rate for interactive streams that do not result in the delivery of a phonorecord and that the problem may be the result of inartful drafting of the regulation rather than an erroneous conclusion over what constitutes a DPD, an observation confirmed by RIAA. *Views of RIAA* at 4 (January 15, 2009). Nevertheless, because the regulatory text can easily be misinterpreted as stating that all interactive streams are incidental DPDs, and therefore subject to the license, the ambiguity in the regulatory text should be clarified. In either case, the problem is corrected by construing the regulation as referring only to those DPDs made and delivered during the course of an interactive stream. Under the CRJs' continuing jurisdiction, the regulation may be redrafted to clarify that an interactive stream that delivers a reproduction of a sound recording that

qualifies as a DPD is for purposes of the license, an incidental DPD.

b. Limited retroactive effect of rates.

Section 385.14(e) of the regulations set forth in the final determination provides, in pertinent part, that ''in the case of licensed activity prior to the publication date, the promotional royalty rate shall apply to promotional interactive streams, and to limited downloads offered in the context of a free trial period for a digital music subscription service.'' Such retroactive application of promotional royalty rates is erroneous to the extent that it is overbroad in reaching—and retroactively setting rates for—promotional activity where rates applicable to the activity were set for the previous rate period. Neither the CRJs nor the participants have the power to engage in retroactive rate setting other than that which is expressly authorized by the statute. As indicated in the Register's August 19, 2008 Memorandum Opinion responding to a material question of law, ''retroactive rulemaking is in most cases beyond the power of an agency'' *Memorandum Opinion on Material Questions of Law, Docket No.* RF 2008–1 at 10 (August 8, 2008), Citing to *Bowen* v. *Georgetown University Hospital*, 488 U.S. 204 (1988). The *Bowen* court elaborated on retroactive rulemaking indicating that ''[r]etroactivity is not favored by the law'' and that where rules may have retroactive effect, the ''power is conveyed by Congress in express terms.'' *Bowen*, 488 U.S. at 208 (1988).

In the case of rates and terms set by the CRJs, title 17 establishes circumstances under which rates may be retroactively applied to activities under the section 115 license. Section 803(d)(2)(B) states that ''[i]n cases where rates and terms have not, prior to the inception of an activity, been established for that particular activity under the relevant license, such rates and terms shall be retroactive to the inception of activity under the relevant license covered by such rates and terms.''

With respect to limited downloads, the previous rate-setting proceeding established royalty fees that clearly applied to limited downloads, whether such downloads were promotional or not. See 37 CFR 255.5 (1999) (setting rates for DPDs ''except for digital phonorecord deliveries where the reproduction or distribution of a phonorecord is incidental to the transmission which constitutes the digital phonorecord delivery, as specified in 17 U.S.C. 115(c)(3)(c) and (D)''). As the regulations adopted by the CRJs recite, ''A limited download is a general digital phonorecord delivery under 17 U.S.C. 115(c)(3)(C) and (D)'' Section 385.11 (definition of ''Limited download,'' para. 3). Thus limited downloads—whether or not for promotional purposes—that took place between the effective date of the rates established in 1999 and the effective date of the rates under review here are governed by the rates set in 1999.[3] This error is corrected by clarifying that such promotional royalty rates do not apply retroactively to limited downloads offered in the context of a free trial period for a digital music subscription service. Under the CRJs' continuing jurisdiction, the regulations may be redrafted to conform with this clarification.

With respect to interactive streams, the regulations adopted by the CRJs characterize interactive streams as incidental DPDs (see section 385.11 (definition of ''Interactive stream'')), and the Register accepts that characterization. The 1999 rate-setting proceeding did not set rates for incidental DPDs. Instead, the setting of rates for incidental DPDs was ''deferred'' for consideration until the next adjustment proceeding. See 37 CFR 255.6 (1999). The question thus arises whether, in light of the deferral of setting of rates for incidental DPDs, the retroactive application of the promotional royalty rate to promotional interactive streams would constitute a material error of law. The Register observes that both the meaning of the previous ''deferral'' of setting rates for incidental DPDs, (an activity whose inception appears to have occurred prior to the previous rate setting), as well as the statutory language, which was enacted after the previous proceeding, present complex issues which have not been fully briefed by the parties in any context. Section 803(d)(2)(B) could be read to authorize the retroactive setting of rates for incidental DPDs when no such rates had been previously set, even in cases where the issue could and perhaps should have been addressed in the previous rate-setting proceeding. On the other hand, the Register questions whether permitting the retroactive setting of rates under such circumstances is wise or consistent with the intent of Congress when it enacted the Copyright Royalty and Distribution Reform Act of 2003 (which among other things, amended Chapter 8 to include section 803(d)(2)(B). *See* H.R. Rep. 108–408 (2004), at 101 (remarks of co-sponsor and subcommittee ranking member Rep. Howard Berman: ''The series of interrelated changes ensures that all rates and terms for statutory licenses will be set prospectively, not retroactively, and eliminate, therefore, the possibility that a time period covered by a statutory license will commence before the establishment of rates and terms.''). However, given the lack of any evidence or in-depth argument on these questions and the compressed period of time allotted by section 802(f)(1)(D) for review by the Register of the CRJs' determination, the Register declines to come to a conclusion regarding application of the promotional royalty rate to promotional interactive streams.

c. Timing of payment.

Section 385.15 of the regulations states that ''[p]ayment for any accounting period for which payment otherwise would be due more than 180 days after the publication date shall be due as otherwise provided under 17 U.S.C. 115 and its implementing regulations. Payment for any prior accounting period shall be due 180 days after the publication date.'' This provision erroneously alters the timing of payment already established in section 115. Specifically, section 115(c)(5) states that ''[r]oyalty payments shall be made on or before the twentieth day of each month and shall include all royalties for the month next preceding;'' and it is this provision in the law that governs the payment schedule for use of the statutory license. While the Register understands the participants' reasons for adopting a term that would delay the first payment under the new rate schedule, there is no precedent for this practice, contrary to the RIAA's interpretation of a term adopted in a past rate setting proceeding. *See Views of RIAA* at 11 (January 15, 2009).

Prior determinations of the Librarian of Congress have considered and rejected as contrary to law similar terms on the basis that such terms would have altered or nullified provisions in the statutory licenses. For example, in 1998, the Librarian, upon the recommendation of the Register, rejected a term of payment which would have altered a payment schedule already established by law and delayed the first payment for six months. *Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings,* 63 FR at 25410, citing section 114(f)(5)(B). In that proceeding, the relevant statutory provision required ''any royalty payments in arrears [to] be made on or before the twentieth day of

[3] The Register finds so support for Copyright Owners' assertion that the previous rate for DPDs aplied only to permanent downloads. *See Views of Copyright Owners* at 17 (January 15, 2009).

the month next succeeding the month in which the royalty fees are set.'' Because the proposed term would not have required payment to be made in accordance with this provision, the Librarian rejected the term as contrary to law. Similarly, in a 2002 proceeding to set rates and terms for the digital performance of sound recordings and the making of ephemeral reproductions, the Librarian accepted the Register's recommendation to adopt September 1, 2002, as the effective date of the rates and terms for the statutory license rather than use the publication date of the Librarian's order. The purpose in setting a later effective date was to delay the adoption of the new rates and terms for a period of time as a way to reduce the financial burden on licensees who had to pay royalties that had accrued since 1998, and to ensure that the date that had been adopted for the first payment, October 20, 2002, complied with the statutory provision that required payments in arrears to be paid ''on a date certain in the month following the month in which the rate is set.'' 67 FR at 45271 (July 8, 2002). Had the rates and terms become effective on the publication date, this provision would have been contrary to law. Consequently, in both cases, the Register recommended that the Librarian adjust the effective date for the adopted rates and terms under his authority in 17 U.S.C. 802(g)(2002) to align the date for the first payment adopted through the rate setting proceeding with the date for making the first payment as specified in the statutory license.

The CRJs have the same authority to determine the date the adopted rates and terms take effect. 17 U.S.C. 803(d)(2)(B). This provision first establishes that ''[i]n [other] cases where rates and terms do not expire on a specified date, successor rates and terms shall take effect on the first day of the second month that begins after the publication of the determination of the Copyright Royalty Judges in the **Federal Register**.'' It then continues, ''except as otherwise provided in this title, or by the Copyright Royalty Judges, or as agreed by the participants in the proceeding that would be bound by the rates and terms.'' If the purpose of the regulation on timing of payments was to provide relief to licensees from an onerous first payment, altering the effective date of the license period would be one way to provide the licensees some relief in meeting its royalty obligation when payment becomes due. *See, e.g., Determination of Reasonable Rates and Terms for the Digital Public Performance of Sound Recordings,* 63 FR at 25412 (May 8, 1998) (adjusting the effective date of the rate setting determination to provide licensees with time to adjust their business operations to meet obligation to make timely payment of arrears). The Register takes no position, however, on whether the effective date should be adjusted, noting that such a decision is within the discretion of the CRJs and the participants themselves.

d. Statements of account.

Section 385.14(a)(4) of the regulations set forth in the final determination, which provides, in pertinent part, that ''[f]or the avoidance of doubt, however, except as provided in paragraph (a) of this section, statements of account under 17 U.S.C. 115 need not reflect interactive streams or limited downloads subject to the promotional royalty rate'' is erroneous. Regulations cannot alter statutory terms of the section 115 license regarding Statements of Account. Title 17 authorizes the Register to ''prescribe regulations under which detailed cumulative annual statements of account, certified by a certified public accountant, shall be filed for every compulsory license under this section.'' 17 U.S.C. 115(c)(5). The CRJs cannot alter requirements issued by the Register regarding statements of account. As indicated in the Register's response to the CRJs' referral of material questions of substantive law concerning the division of authority between the CRJs and the Register, ''[a]uthority to issue regulations regarding these statements of account is the exclusive domain of the Register.'' *Final Order, Division of Authority Between the Copyright Royalty Judges and the Register of Copyrights under the Section 115 Statutory License* 73 FR 48398, (August 19, 2008).

Additionally, section 115(c)(5) indicates that ''[t]he regulations [of the Register] covering both the monthly and the annual statements of account shall prescribe the form, content, and manner of certification with respect to the number of records made and the number of records distributed.'' 17 U.S.C. 115(c)(5). There is no statutory authority for an exception to this requirement for certain types of ''phonorecords'' or for the participants to alter this provision by agreement. As previously referenced, prior determinations of the Librarian of Congress have considered and rejected similar terms that altered or expanded the statutory licenses. *See* supra at section 3(c) citing 63 FR 25394, and 63 FR at 45269.

The problem is corrected by clarifying that licensees are required to operate within the Register's Statements of Account and Notice of Intention to Use regulations, even if such regulations foreclose the application of certain provisions included in the CRJs' final determination. Any agreement among a licensee and a copyright owner to adopt terms that alter the statutory conditions and terms necessarily means that the licensee is operating under a private license rather than the statutory license. *Harry Fox Agency, Inc.* v. *Mills Music, Inc.,* 543 F. Supp. 844, 851–852 (S.D.N.Y. 1982). Under the CRJs' continuing jurisdiction, the regulations may be redrafted to clarify that licensees must comply with the Register's regulations addressing Statements of Account.

CRJs' Continuing Jurisdiction

The Register notes that the CRJs enjoy continuing jurisdiction to amend their final determination. Under section 803(c)(4), ''[t]he Copyright Royalty Judges may issue an amendment to a written determination to correct any technical or clerical errors in the determination or to modify the terms, but not the rates, of royalty payments in response to unforeseen circumstances that would frustrate the proper implementation of such determination. Such amendment shall be set forth in a written addendum to the determination that shall be distributed to the participants of the proceeding and shall be published in the **Federal Register**.'' This authority may be exercised to codify the corrections identified and made herein by the Register through her authority under section 802(f)(1)(D).

Conclusion

Having reviewed the CRJs' resolution for legal error, pursuant to the requirements established in section 802(f)(1)(D), the Register issues this written decision correcting the above referenced legal errors not later than 60 days after the date on which the final determination by the CRJs was issued. This decision shall be made part of the record of the proceeding (Docket No. 2006–3 CRB DPRA), and the conclusions of substantive law involving and interpretation of title 17 contained herein shall be binding as precedent upon the CRJs in subsequent proceedings.

Dated: January 16, 2009.

Marybeth Peters,

Register of Copyrights.

[FR Doc. E9–1444 Filed 1–23–09; 8:45 am]

BILLING CODE 1410–30–P