

INTERNET MUSIC MADNESS: MONEY DUE OR MONEY DIE?

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Introduction

Much has been written about the death of the music industry -- or at least the death of its existing business model where profits largely came from the sale of physical product. Although there may be some disagreement over who actually benefitted from that model, there is no disagreement that digital technology and the Internet have changed the way talent (recording artists, performers, composers) and the rest of the industry now do business and how the value of that business is monetized.

Given the charge of the author, this paper primarily focuses on how talent is making the most of the madness that is now the Internet. Statutory references will be made to the United States Copyright Act, 17 U.S.C. §§ 101 et seq. ("the Act"), which is still the primary source of the right to income from creative efforts. Section I briefly reviews how talent continues to make money from traditional income streams even though product is in a digital format. Section II discusses some of the innovative ways talent has found to use the Internet both to finance creative efforts and to enhance the bottom line. Section III describes some of the ways in which Internet revenue is licensed, collected, and distributed on behalf of talent and ways that talent may track growing popularity. Lastly, Section IV suggests that "Internet Madness" is not without its conundrums, reminding counsel of his or her role in advising clients accordingly.

I. Internet Madness and Traditional Income Streams Based On Use

A. Mechanical Royalties: In the United States, composers (and publishers) are entitled to compulsory mechanical royaltiesⁱ derived from the permanent copying (or copying for a set period of time) of their compositions on the Internet. As a result of amendments to the Act, these royalties are also due from permanent digital downloading, ringtones, interactive streaming, and limited downloadingⁱⁱ. In the United States, the rate of mechanical royalties for permanent digital downloading is currently (and through December 2012) the same as that for the permanent sale of physical product -- 9.1 cents or 1.75 cents per minute, whichever is greater, per song, per album distributed. Also effective through 2012, the rate for ringtones is 24 cents per snippet of a full recording. For interactive streaming and limited downloading by on-line music services, the

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royalty rate is based on a number of factors including service offering type, licensee type, service revenue, recorded content expense, and applicable performance royalty expenses, but is roughly 10.5 cents per song less any public performance royalties paid.ⁱⁱⁱ Examples of online music subscription services which are subject to the higher rates are Rhapsody and Spotify.

Most other countries of the world, through their respective organizations, set the mechanical royalty rate as a percentage of the wholesale price of the album/song.

B. Small Public Performance Royalties: Composers (and publishers) are entitled to royalties whenever a song is transmitted over the Internet in an audio only, non-permanent format, namely, streaming and webcasting. Also known as small public performance royalties, rates may be negotiated directly with the owner of the composition but more commonly are set by public performance rights organizations (PROs), e.g., in the United States, BMI, ASCAP and SESAC). These licenses -- which are non-compulsory -- are administered by the PROs on behalf of the composers and publishers who have registered their titles with them and often take the form of blanket licenses allowing the performance of all compositions in their respective repertoires.^{iv}

As a result of the Digital Performance in Sound Recording Act of 1995, and the Digital Millennium Copyright Act of 1998, whenever a master recording of a song is streamed or webcasted, the featured artist(s), any non-featured vocalists and any musicians (and labels) also are entitled to small public performance royalties for their performances, subject to certain statutory exemptions.^v If certain specific criteria are met, usually involving limitations on the number of times a particular artist may be streamed or webcasted, the right to publicly perform a master on the Internet is compulsory and a statutory license may be obtained subject to payment of a statutory fee.^{vi} Most Internet radio webcasters qualify for a compulsory license as do certain online certain subscription services, e.g., Pandora.

If the webcaster or online subscription service cannot qualify for a compulsory license, then it must negotiate directly with the owner of the master. In that case, the right of the performers to obtain a share of that royalty will depend on their respective agreements with the owner of the master.

In most foreign markets, small public performance royalties are voluntarily negotiated.

C. Synchronization Royalties: Composers (and publishers) may be entitled to royalties from the licensing of their songs in timed relation with visual action on the Internet, e.g., in a website or in a videogame. These licenses are completely voluntary and talent's right to receive royalties is dependent on the composer's agreement with their publisher (if any). Performers (and labels) also may be entitled to synchronization royalties if the master of a song is actually used and if their agreement with the label provides for them.

D. Royalties from Digital Phonographic Deliveries: Performing artists (and non-featured talent) also may receive royalties from an actual Internet sale of a master on which they perform, e.g., a permanent download for a fee from an on-line music store. As in the case of

synchronization royalties, the amount of this royalty is based on the agreement between the artist and the owner of the master.

E. Other Sources of Income. Composers also are entitled to any income derived from the licensing of the right to publicly display lyrics on the Internet. Additionally, there is a statutory surcharge placed on the sale of digital audio recording equipment generally used to record music (does not include computers), a portion of which is distributed by the government to songwriters/publishers and to labels/artists, a/k/a DART royalties.^{vii}

II. Internet Madness and Non-Traditional Financial/Income Streams Based on Provision of Own Content and Web Presence.

A. Web Presence. Talent, especially solo artists and bands, need to have a web presence to attract fans. The plethora of ways to build a website, to find a host, and to be cost-efficient is beyond the scope of general discussion. That said, any webpage worth its salt is either directly on or is linked to a social network – Facebook, Twitter and YouTube (worldwide), Linked-In and MySpace (North America), Friendster, Mixi, Multiply, Orkut and Cyworld (Asia and the Pacific Islands), Badoo and Skyrock (parts of Europe) and MyFrenz.net (India). Facebook alone has over twenty different music related applications, several of which allow talent to create web pages for free on their respective platforms. These applications often allow talent links to stream their music, look at photos in concert, find events, read notes and visit online stores. One example is BandPage, a free (and ad-free) Facebook application that streamlines the online presence of artists within the social network.^{viii} Talent may even create his or her own webpage by going directly to Facebook’s homepage.

B. E-commerce. Evolving from prior practices, talent no longer has to rely on labels and distributors to sell music. They can create their own online store on their website or seek “distribution” from an online music store such as iTunes or CD Baby (the latter of which both sells content directly or acts as a distributor to other on-line music stores.) Other popular online music stores include Vodafone (Europe); Sky Songs, Rhapsody, iMesh, and Emusic.

C. Merchandising: In addition to selling music, talent needs to engage in the sale of subsidiary products -- tee-shirts, hats, etc. It has been reported that some artists will give away music – and then charge heftily for merchandising.^{ix}

D. Brand Sponsorship: When a brand (think Nike or Coke) actually sponsors a group, thereby allowing for free music or discounted tickets, fans come to appreciate that sponsor on another whole level. (Ad-backed streaming services focus on monetizing traffic on sites. Many listeners, however, do not want to be interrupted by ads and either skip over them or pay the fee to avoid them altogether (so-called Plus services). There are websites which attempt to match bands with potential sponsors.^x In addition, one of the criteria for matching is a requirement that a portion of earnings be contributed to charity. This requirement might serve not only as a tax benefit to the sponsor but further enhance fan appreciation.

E. Tie-In with Products: Artists with interests other than music have considered creating events related to those interests and inviting fans to participate. For example, Polydor Records

singer-songwriter, Ellie Goulding, is a runner. Through her Facebook page, she invited a small number of selected fans to run with her in seven different cities on her UK tour and was able to tie-in a Nike sponsorship. Her label then released a remixed version of hit song “Lights”, aimed at providing a running soundtrack for the national running subculture.^{xi}

F. Investment: Both talent and labels have used web-based, social network style “crowd funding” to finance their personal efforts or the efforts of their artists. For example, My Major Company (MMC), an online record label, with a successful record of on-line distribution and marketing artists, uses web-based, social network style “crowd funding” to finance acts.* Currently used in the UK and France, MMC may posts demos and videos of ten artists at a time; users are invited to invest anywhere from £10 pounds to £10,000 pounds; once the act reaches £100,000 pounds financing is locked in and money is used to pay for recording and possibly a tour. Instead of goodies, net revenue resulting from sales, concerts, and merchandise will be split three ways: investors get 40%, MMC gets 40%, and artist pockets 20%.^{xii} As more fully explained in Section IV below, such funding may violate federal and state securities regulations and should not be utilized until legal advice is obtained.

G. Opportunities for Fans to be Part of Your Promotion: One artist enabled fans to tag themselves in a picture taken at a concert posted on his website. By doing so, the fan became attached. It was later suggested that the artist also figure out how to blow up the picture and then sell it as a form of merchandising.^{xiii}

H. Other Internet Guerilla Marketing Techniques: An article appearing on the website [www.Music Biz.Academy.com](http://www.MusicBizAcademy.com) provides the following additional suggestions on how talent may use the Internet to his or her benefit^{xiv}:

- If a fan database includes birthdates, make fans a birthday card embedded with a sound file of a birthday song written directly for them and e-mail it.
- Suggest other music on your website – this will show that talent is not just another selfish musician and will build camaraderie among musicians, leading to job opportunities
- Link to other music related websites and ask fans to recommend favorite websites
- Create contests on the website where the prize is a copy of talent’s latest CD or tickets to a show.

III. Collection of Income

To engage in guerilla marketing, to allow the creative juices to flow, to measure the success of the business and to handle the business end generally, talent (and labels and publishers) often have to turn to third parties to engage in the requisite licensing and collection of royalties which may be due. Here are some of the more popular service providers:

A. Mechanical Royalties: The Harry Fox Agency (HFA) is authorized by numerous composers and publishers to enter into mechanical licenses with third parties on their behalf, including licenses for digital permanent downloads, ringtones, limited downloads, and interactive streaming. Harry Fox also will collect and distribute the royalties derived from these licenses^{xv}.

B. Public Performance Royalties:

- Digital Sound Recordings: SoundExchange, a non-profit organization designated by the Librarian of Congress, has the exclusive right to collect and distribute statutory public performance royalties on behalf of sound recording copyright owners and featured artists, as well as for AFTRA and AFM for further distribution to their constituents, from noninteractive digital transmissions, including satellite and Internet radio and noninteractive music subscription services.
- Musical Compositions: As stated above, for songs transmitted over the Internet and mobile entertainment, the PROs enter into public performance licenses on behalf of the composers (and publishers) with whom titles are registered. The PROs then collect the licensing fees and distribute them to talent based on various formulas distinct to each organization. The PROs also collect other royalties on behalf of their members, e.g., DART royalties. For a complete listing of their services, see the individual website identified above.
- Other Tracking Services: For talent which does not utilize the services of a third party to license or to collect income, or who otherwise wants to track their own music (for both monetary and promotional purposes), there are tracking services available. RootMusic, Inc., recently launched a YouTube tracks feature that enables musicians (and labels) to collect royalties with each play of a song through their BandPage media player on Facebook.^{xvi} Labels also are using VIVO (Video In, Video Out) to track music and visitor hits, which also may inure to the benefit of talent depending on contractual terms.

IV. Internet Madness and Its Dangers

While the Internet has created a new promotional landscape, it is not one without weeds. The potential is great for direct and indirect liability, the waiver of important rights, and becoming the target of cybercriminals -- both as the provider of content and as a user of same. Some of the issues are as follows:

- Viral Nature of Copyright and Trademark Infringement: Music, videos and photos may be used without permission on a website or transmitted through a social network. Even if infringing content is removed from that website or network, it still may appear on other postings to which the content previously was sent or uploaded.^{xvii}
- Breach of EULA (End User License Agreement): Most social networks and other licensing agreements prohibit the uploading or posting of content that infringes a third

party's rights, including intellectual property, privacy and publicity rights. Artist may upload music they recorded, but have no right to the underlying song – or have entered into publishing agreements transferring the copyright. Artist may unwittingly also upload infringing content only to find that it has been removed without notice having an impact on the site. Most agreements allow the service provider to remove such content in its absolute discretion.^{xviii}

- Privacy Concerns: For those sites that are advertising based, data is collected on visitors and used for marketing and other purposes. Fans may be deterred from going to certain sites for fear that this data will be collected. Worse yet, such data falls into the hands of unscrupulous parties and the next thing the user knows is that he or she is a target of cybercriminals. Both talent and users need to become more familiar with the terms and conditions of the sites they use and the individual privacy settings available to the user.
- Securities Regulation: Generally speaking, a product or service which depends entirely on the skill of others is considered a security and requires some degree of registration with the appropriate federal and state agencies before it may be made available to the public as an investment opportunity. Accordingly, marketing for investment dollars should be discussed with a legal professional to determine what can and cannot be done.
- Right of Publicity: In the course of talent's marketing effort, someone's name and likeness may be used in trade or advertising without that person's permission. Rather than just receiving a cease and desist letter, talent may end up being served with a complaint alleging a violation of plaintiff's right of publicity and seeking monetary damages.
- Piracy: Illegal downloading still remains the biggest concern for talent notwithstanding all efforts (pleas) to educate the public and the substantial verdicts against individuals for engaging in such conduct.^{xix}

V. Conclusion

The Internet has changed the conventional way of engaging in the music business – some even say it has become the great equalizer. After all, talent no longer needs a distributor to sell its music, has the ability to build its own fan base, and may deal directly with that base through the use of social networks, no longer having to rely solely on live performances. The madness, however, is not without its problems. Each new marketing technique brings a host of concerns – violations of intellectual property, privacy, and publicity rights, piracy, securities fraud, and inadvertent and not so inadvertent breaches of contracts and license agreements. For these reasons, counsel needs to remain ever vigilant by staying abreast of changes and by advising clients what action is appropriate under the circumstances.

ⁱ Pursuant to Section 115 et seq. of the Act, once the composer has released a recorded song, any other performer is entitled to re-record the song upon payment of no more than the existing statutory mechanical royalty rate.

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- ⁱⁱ See, Section 115(3) (A)-(E) of the Act. Note that the PROs, *infra*, are not entitled to collect any public performance royalties for the downloading of the musical compositions. See *U.S. v. Am. Soc’y of Composers, Authors & Publishers In Re real Networks*, 485 F. Supp. 2d 438 (S.D.N.Y.), *affirmed in part, vacated in part on other grounds*, 2010 U.S. App. Lexis 19983 (2d Cir. 2010)
- ⁱⁱⁱ For a complete listing and explanation of mechanical royalty rates in the United States see the Harry Fox Agency website, www.hfa.com, also discussed *infra*.
- ^{iv} For more information about the individual PROs see, e.g., www.bmi.com, www.ascap.com and www.sesac.com, also discussed *infra*
- ^v Both Amendments may be found codified in Section 114 et seq. of the Act. Artist receive 45%, the AFM receives 2.5% on behalf of musicians; AFTRA receives 2.5% on behalf of non-featured artist. The label receives the other 50%.
- ^{vi} See Section 114(d)(2) of the Act
- ^{vii} See Section 1001 et seq. of the Act
- ^{viii} See www.pitchengine.com/rootmusic/-bandpage-on-facebook-now
- ^{ix} See www.guardian.co.uk/music/op-music-business-digital-revolution/print
- ^x See, e.g. www.hypebot.com/2011/03/ian-kwon-on-famaticfms-platform-to-monetize.
- ^{xi} See www.guardian.co.uk/music/pop-music-business-digital-revolution/print
- ^{xii} See, *Time Magazine*, February 28, 2011 “I’m With the Band” by Thomas Grose
- ^{xiii} See www.hypebot.com/hypebot/2011/03/11-simple-yet-effective-facebook-marketing-tactic
- ^{xiv} Music Biz Academy.com at http://www.musicbizacademy.com/knab/articles/gmm_suggest.htm
- ^{xv} See Footnote 1
- ^{xvi} See www.hypebot.com/2010/09/bandpage--provides-performance-royalties-to-artists
- ^{xvii} See *Jones Day v. Blockshopper LLC*, 2008 U.S. Dist. LEXIS 94442 (N.D. Ill 2008)
- ^{xviii} See, *Williams v. Life’s Rad*, 2010 U.S. Dist. LEXIS 46763 (N.D. Cal. 2010)
- ^{xix} See, *Sony BMG Music Entertainment v. Tenenbaum*, 2010 U.S. Dist. LEXIS 68642 (D. Mass 2010); *Maverick Recording v. Harper*, 598 F. 3d 193 (5th Cir. 2010)