

telephone call or other communication or message or to alert the receiver to the fact that there is a communication or message.

C. Interactive Streams (Including all Known Forms of Incidental Digital Phonorecord Delivery) and Limited Downloads

Royalty rates and terms for interactive streams and limited downloads are subject to a settlement agreement announced to the Court on May 15, 2008 and expected to be provided to the Court on or after September 15, 2008.

II. Calculation of Royalties

A. Definition of Wholesale Revenue

For purposes of Parts I(A) and (B) above, when the licensee is not distributing phonorecords directly to end user consumers (e.g., when a record company is selling a physical product to a retailer, or authorizing a digital music service to resell digital phonorecord deliveries), the licensee's Wholesale Revenue shall mean revenue recognized by the licensee in accordance with Generally Accepted Accounting Principles from the distribution of such phonorecords, and shall be comprised of the following:

(i) in the case of physical products, sales revenue recognized by the licensee directly from distribution of phonorecords, meaning gross sales as reflected on the applicable invoices, less returns and applicable sales discounts; and

(ii) in the case of digital phonorecord deliveries, sales, licensing and other revenues received from digital music services attributable to distribution of such digital phonorecord deliveries, as reflected in sales reports and accountings provided to the licensee by such services.

The licensee's Wholesale Revenue shall include such payments as set forth in paragraphs (i) and (ii) above to which the licensee is entitled but which are paid to a parent, wholly owned subsidiary or division of licensee.

The licensee's Wholesale Revenue shall exclude sales and use taxes, shipping, and handling and insurance charges.

The foregoing assumes that licensees will be permitted to reserve for returns as provided in the Copyright Office's regulations implementing Section 115 of the Copyright Act (37 C.F.R. § 201.19).

B. Digital Music Service as Licensee

In a case in which the licensee is a digital music service that has been authorized by a record company (as defined in the draft regulations provided herewith) to

resell digital phonorecord deliveries but that has itself acquired licenses under Section 115, the applicable royalties under Part I above shall be the percentage set forth in Part I applied to an “all-in” payment that is equivalent to the amount payable for the sound recordings plus the amount payable for mechanical rights to musical works. Thus, the rate under Part I(A) would be 9.9% of the amount paid by the service to the record company for the sound recording only, and the rate under Part I(B) would be 17.6% of the amount paid by the service to the record company for the sound recording only. Consistent with the Copyright Owners’ concept of “total content costs,” this amount is added to the amount paid by the service to the record company for the sound recording to yield an equivalent “all-in” royalty base.

Note:

This is a mathematically equivalent expression of the same approach proposed by the Copyright Owners when they request a mechanical royalty rate based on “total content costs.” A mechanical royalty rate expressed as a percentage of the sound recording payment that is the equivalent of a mechanical royalty expressed as a percentage of the all-in payment (i.e., the combined musical work and sound recording payment) can be determined by the following formula:

$$P_R = \frac{P_A}{100 - P_A}$$

where P_R = the percentage mechanical royalty rate based on the payment for the sound recording only, and
 P_A = the percentage mechanical royalty rate based on the all-in payment

Thus, for example, under RIAA’s rate request in Part I(A), a record company that received \$1 from a service from the resale of a download would pay a mechanical royalty of \$0.09. If instead the record company and service agreed that the service would pay the \$0.09 in mechanical royalties directly, the record company would receive \$0.91 cents for the sound recording only. The \$0.09 in mechanical royalties to be paid directly by the service is 9.9% of the \$0.91 cent payment to the record company for the sound recording alone. Thus, increasing the \$0.91 cent payment to the record company for the sound recording by 9.9% yields a \$1 royalty base equivalent to that which would apply if the record company was responsible for the mechanical licensing. Applying the 9% royalty rate to that \$1 royalty base yields the same \$0.09 payment.

C. Record Company as Direct Retailer

When the licensee is a record company that is distributing phonorecords directly to end user consumers, the licensee’s Wholesale Revenue shall mean the revenue recognized by the licensee in accordance with Generally Accepted Accounting

Principles from the distribution of such phonorecords multiplied by the applicable percentage from the table below:

Configuration	Percentage
Physical and Permanent Download	70%
Other	50%

D. Calculation of Royalty Base for Bundles

If, in a single transaction, a licensee receives payment for sound recordings of musical works distributed pursuant to Section 115 and subject to the rate provided in one of Parts I(A) and (B), as well as other products or services (e.g., where a phonorecord or online bundle contains material other than sound recordings of musical works, or an online bundle contains both permanent downloads and ringtones), the licensee's revenues from the transaction shall be attributed to the sound recordings of musical works and other products or services in proportion to the licensee's published prices thereof when distributed separately, if any, or otherwise in accordance with a reasonable and non-discriminatory allocation methodology consistently applied.

E. Allocation of Revenues among Musical Works

If, in a single transaction, a licensee receives payment for sound recordings of multiple unique musical works distributed pursuant to Section 115 and subject to one of Parts I(A) and (B) (e.g., the tracks on a CD or a digital album), the applicable revenues shall be allocated equally among such musical works.

III. Transition Period

To allow copyright owners and licensees reasonable time to implement the percentage royalty structure described above –

(i) these rates shall be effective on the first day of the first calendar quarter beginning more than six months after the publication of the determination of the Copyright Royalty Judges in the Federal Register; and

(ii) in the case of any product the first phonorecords of which were distributed to the public prior to the date identified in clause (i) above, the licensee shall have the option to pay royalties for any phonorecords distributed during the 12 months following such date at the rates set forth above or at the statutory rate previously in effect.

IV. Alternative Rate Request (Not RIAA’s Preferred Approach)

RIAA believes that a percentage royalty rate structure is most appropriate for all the reasons explained in the testimony it has presented and in its Proposed Findings of Fact and Conclusions of Law, and RIAA does not advocate for a cents-rate royalty for any category of product or service. However, in the event that the Copyright Royalty Judges determine that a percentage royalty structure is not appropriate for any category of product or service, RIAA has set forth below an alternative rate proposal including cents rates designed to approximate its percentage rate proposals for certain configurations.

Rate Category	Rate	Basis for Rate
Premium Price Physical Product or a la Carte Download (Wholesale price \$1/track or more)	9.45¢/track	Wholesale price of \$1.05 x 9%. E.g.: <ul style="list-style-type: none"> • \$1.05 per track wholesale price for physical album with wholesale price of \$10.50 and 10 tracks¹ • \$1.04 wholesale price for single download having a \$1.49 retail price
High Price Physical Product or a la Carte Download (Wholesale price 80¢/track or more but less than \$1/track)	8.1¢/track	Wholesale price of 90¢ x 9%. E.g.: <ul style="list-style-type: none"> • 90¢ per track wholesale price for physical album with wholesale price of \$9 and 10 tracks • 90.3¢ wholesale price for single download having a \$1.29 retail price
Medium Price Physical Product or la Carte Download (Wholesale price 60¢/track or more but less than 80¢/track)	6.3¢/track	Wholesale price of 70¢ x 9%. E.g.: <ul style="list-style-type: none"> • 69¢ per track wholesale price for physical album with wholesale price of \$9 and 13 tracks • 70¢ wholesale price for single download having a 99¢ retail price
Low Price Physical Product or a la Carte Download (Wholesale price 45¢/track or more but less than 60¢/track)	4.7¢/track	Wholesale price of 52.5¢ x 9%. E.g.: <ul style="list-style-type: none"> • 53.8¢ per track wholesale price for physical album or album download with wholesale price of \$7 and 13 tracks • 55.3¢ wholesale price for single download having a 79¢ retail price
Very Low Price Physical Product or a la Carte Download (Wholesale price less than 45¢/track)	3.6¢/track	Wholesale price of 40¢ x 9%. E.g.: <ul style="list-style-type: none"> • 38.5¢ per track wholesale price for physical album with wholesale price of \$5 and 13 tracks • 43¢ per track wholesale price for album download having a wholesale price of \$5.59 (retail \$7.99) and 13 tracks

¹ RIAA understands there to be approximately 13 tracks per album on average, but the range in the number of tracks per album is wide. Ten tracks is used here as an example of a product that would warrant the proposed per-track payment based on existing economic conditions.

Ringtone	18¢	\$1.20 wholesale price x 15%
Other DPDs in General	9% of wholesale	Rate under Part I(A) above

Additional Rate Provisions:

If the Copyright Royalty Judges adopt cents rates such as those set forth above, the adjustments in Parts II(B) and (C) shall apply where applicable, and revenues from bundles shall be allocated as provided in Part II(D), to calculate the per-track wholesale price. The following additional provisions concerning calculation of the royalty also shall apply:

A. Locked Content

In the case of a locked content product, the product is considered distributed, and the royalty becomes payable, when the product is unlocked.

Definitions:

For this purpose –

- A “locked content product” is a phonorecord on which the sound recording has been encrypted or otherwise protected by digital rights management, or degraded (e.g., by means of voiceovers) so as not to materially substitute for the sale of a copy of a non-degraded recording, and is either (i) not otherwise accessible to, or playable in a non-degraded form by, the consumer without additional payment and/or authorization, or (ii) accessible or playable in a non-degraded form by a consumer for no more than a limited time period and/or a limited number of “plays” that is commercially reasonable for the purpose of inducing the consumer to make an additional payment to permanently obtain access to or enable the non-degraded play of the recording.
- A locked content product is “unlocked” when a consumer is given permanent access to non-degraded play of the relevant recording.

B. Multiple Instances

In a case in which multiple fixations of the same sound recording are distributed on a physical product or as a la carte downloads as part of a single transaction (e.g., a multisession disc, or downloads to a computer and cell phone), the price of the transaction shall be used to determine the applicable rate category, but all such fixations together shall be considered the same track.

V. **Terms**

A. **Clarification of Covered Reproductions**

Regulations shall confirm that a compulsory license under Section 115 extends to all reproduction and distribution rights that may be necessary to engage in activities covered by the compulsory license, including –

- (1) the making of reproductions by and for end users;
- (2) reproductions made on servers under the authority of the licensee; and
- (3) incidental reproductions made under the authority of the licensee in the normal course of engaging in such activities, including cached, network, and buffer reproductions.

B. **Accounting for Digital Phonorecord Deliveries²**

Notwithstanding 37 C.F.R. § 201.19(a)(6), when a digital phonorecord delivery is not distributed to the end user consumer directly by the compulsory licensee, the digital phonorecord delivery shall be treated as made, distributed, voluntarily distributed, relinquished from possession and permanently parted with in the accounting period in which it is reported to the compulsory licensee.

C. **Signing Statements of Account**

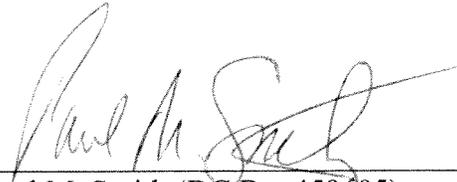
Notwithstanding 37 C.F.R. § 201.19(e)(6) and (f)(6)(i), monthly and annual statements of account shall be valid if signed by any duly authorized agent of the compulsory licensee.

D. **Audit**

Notwithstanding 37 C.F.R. § 201.19(f)(6)(ii), an audit performed in the ordinary course of business according to generally accepted auditing standards by an independent and qualified auditor shall serve as an acceptable verification procedure with respect to the information that is within the scope of the audit.

² RIAA has indicated its view that Section 115 should be interpreted to grant this Court only limited authority to supplant the Copyright Office's payment regulations. As discussed in RIAA's Conclusions of Law, RIAA does not believe that this Court has the authority to adopt the term set forth in Part V(B), and so RIAA does not propose it here. Nonetheless, RIAA sets forth this term in case the Court concludes that, as a matter of law – and contrary to RIAA's view – it does have authority to adopt this term. If this Court concludes that it lacks jurisdiction over this issue, then RIAA withdraws the term set forth in Part V(B).

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