

2023

Revisiting the Convergence of Technology, Legislation, and Industry: The Effect of 17 U.S.C. § 115(c)(3)(E) of the Copyright Act on Mechanical Royalties and the Controlled Composition Clause

Follow this and additional works at: https://digitalcommons.onu.edu/onu_law_review



Part of the [Law Commons](#)

Recommended Citation

(2023) "Revisiting the Convergence of Technology, Legislation, and Industry: The Effect of 17 U.S.C. § 115(c)(3)(E) of the Copyright Act on Mechanical Royalties and the Controlled Composition Clause," *Ohio Northern University Law Review*: Vol. 39: Iss. 3, Article 3.

Available at: https://digitalcommons.onu.edu/onu_law_review/vol39/iss3/3

This Article is brought to you for free and open access by the ONU Journals and Publications at DigitalCommons@ONU. It has been accepted for inclusion in Ohio Northern University Law Review by an authorized editor of DigitalCommons@ONU. For more information, please contact digitalcommons@onu.edu.

Revisiting the Convergence of Technology, Legislation, and Industry: The Effect of 17 U.S.C. § 115(c)(3)(E) of the Copyright Act on Mechanical Royalties and the Controlled Composition Clause

BY BRIAN S. MENCHER* & VIDAL C. MAURRASSE**

ABSTRACT

Despite the passage of the Digital Performance Right in Sound Recordings Act of 1995 (“DPRA”), the compulsory mechanical license found in Section 115(c) of the Copyright Act continues to subjugate Congressional efforts to fully compensate the owners of copyrights in musical compositions—and mainly by its own devices. With the ever-increasing dominance of digital music distribution platforms, the need to revisit the way mechanical royalties apply to digital phonorecords grows more pressing. While the music industry often refers to the compulsory mechanical rates as “minimums,” it has become standard for recording contracts to chop this figure down, awarding copyright owners less than what the Copyright Act seems to indicate they deserve for mechanical reproductions of their works. Although the DPRA created a mandatory mechanical royalty rate in Section 115(c)(3)(E) of the Copyright Act for music purchased by digital phonorecord delivery, there still exist various means by which copyright exploiters can avoid this rate through the section’s own language, as well as through common industry practice. This Article will explain the effect of 17 U.S.C. § 115(c)(3) on the music industry, with a focus on digital phonorecord deliveries in light of the quickly changing distribution landscape, and offer feasible explanations and solutions to the potentially problematic language of 17 U.S.C. § 115 that could still allow record companies to override the statutorily-mandated mechanical royalty rate for digital phonorecord deliveries.

I. INTRODUCTION

Part II of this Article begins by explaining the origin of the mechanical reproduction and its associated rights, and introduces the compulsory

* Brian Mencher is an entertainment attorney based in New York City and is managing partner of Beame & Mencher LLP.

**Vidal Maurrasse is an Associate at Beame & Mencher LLP practicing in the areas of entertainment and intellectual property.

mechanical licensing system enacted by Congress in 1909.¹ Part III discusses the emergence of the Controlled Composition Clause as a response to the increased mechanical royalty rate in 1978.² Part III then goes on to illustrate how the Controlled Composition Clause could drastically reduce the mechanical royalties paid out to song owners by changing the terms and rates of royalty payments.³ Part IV focuses more directly on the issue of digital phonorecord deliveries, and discusses the Contract Override’s ability to trump conflicting mechanical royalty rates in contracts in the case of DPDs.⁴ Part IV introduces the idea of loopholes existing within the Contract Override itself which potentially could allow record labels to circumvent the protections afforded by that provision.⁵ Part V also explains how those loopholes could be exploited through the Controlled Composition Clause to affect royalties for DPDs in much the same way the Controlled Composition Clause reduced mechanical royalties for physical phonorecords.⁶ Finally, Part VI briefly touches on some practical considerations surrounding the Contract Override, and notes the importance of educating industry professionals on its provisions.⁷

II. THE COMPULSORY MECHANICAL LICENSE AND THE EVOLUTION OF THE MECHANICAL ROYALTY

A. *The Right of Reproduction*

When an artistic work is “fixed,” it automatically qualifies for copyright protection.⁸ Even song lyrics written on a napkin are protectable by copyright. Decades (and even centuries) ago, a song was fixed, i.e. written, on sheet music with musical notation and accompanying lyrics. Now, it is more commonplace for a song to be created at the same time that it is recorded, through digital recording capabilities, without the Mozart-style transcription that is often imagined. But regardless of how the song is created, as long as it is fixed, it becomes a protected work.⁹ Under United

1. *See infra* Part II.

2. *See infra* Part III. For a definition of the “Controlled Composition Clause,” *see infra* Part III.B.

3. *See infra* Part III.

4. *See infra* Part IV. For a definition of the “Contract Override” provision, *see infra* Part IV.B. For a definition of “digital phonorecord delivery” (DPDs), *see infra* text accompanying note 52.

5. *See infra* Part IV.

6. *See infra* Part V.

7. *See infra* Part VI.

8. *See* 17 U.S.C. § 102(a) (2006) (“Copyright protection subsists, in accordance with this title, in original works of authorship fixed in any tangible medium of expression, now known or later developed, from which they can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device.”).

9. *See id.*

States copyright law, songs are referred to as “musical works,”¹⁰ and under the Copyright Acts of 1909 and 1976, the author of a musical work had, and still has, rights over the reproduction and subsequent distribution of that work.¹¹

In the music industry, musical works are generally administered by music publishers, who have the works assigned to them by the songwriters who created them, and whose role it is not only to place musical works in movies and television shows, for example, but also to secure the recording and distribution of the songs by record labels. The record labels pay the publisher for use of the underlying musical works. Record labels also control a separate copyright in sound recordings, i.e., the actual recorded musical work in audio form (also called a “master”). For example, a publisher finds a record label that wants to use one of the musical works in its catalog, and the record label records the work. The publisher still holds the rights to the musical work, but the record label holds the rights to the corresponding recording, each party owning separate copyrights that grant them a “bundle of rights,” as provided for in the Copyright Act, and, accordingly, requiring two separate permissions to use the musical work and sound recording.¹² Artists and songwriters obtain their shares of revenues from the sound recording and the musical work, respectively. Additionally, if the songwriter also records the song, the songwriter derives revenue from both the sound recording and the musical work.

Prior to the enactment of the Copyright Act of 1909, protection of a musical work generally extended only to the right of performance and a narrowly-defined reproduction right (i.e., making copies of sheet music).¹³ The scope of the reproduction right was tested in 1908 when the Supreme Court of the United States ruled that a piano roll¹⁴ did not constitute a reproduction of a musical work, since it could not be “read” similarly to that of traditional notation.¹⁵ Instead, the piano roll is simply a part of a device, namely a piano, enabling the mechanical performance of a musical work.¹⁶ The 1909 Act closed this loophole by granting authors of musical

10. *See id.* (including as works of authorship “musical works, including any accompanying words”).

11. *See* Copyright Act of 1909 § 1(d), Pub. L. No. 60-349, § 25, 35 Stat. 1075, 1081 (1909), *superseded by* 17 U.S.C. §§ 101-914 (2006); *see also* Copyright Act of 1976, Pub. L. No. 94-553, 90 Stat. 2541 (2006).

12. *See* 17 U.S.C. § 102(a).

13. *See* Copyright Act of 1790 § 2, 1 Stat. 124 (1790) (discussing only the paper reproduction of copyrighted works as protected).

14. A piano roll is a roll of paper representing a musical work through perforations that correlate to the work’s musical notes. The roll is then fed into a player piano, which reads the piano roll and plays the song that has been converted onto the piano roll.

15. *See* *White-Smith Music Publ’g Co. v. Apollo Co.*, 209 U.S. 1, 18 (1908).

16. *Id.*

works the right of reproduction, including the right to make “mechanical” reproductions, such as the piano roll.¹⁷ Thereafter, the placement of a song onto media through which the sound could be reproduced, such as vinyl, cassette tapes, and compact discs (i.e., “phonorecords”),¹⁸ was also considered a “mechanical” reproduction of a musical work similar to the piano roll.¹⁹ In the age of digital music transmission, a song downloaded from the internet is treated much like a physical “phonorecord.”²⁰

However, the right of reproduction was not absolute. An absolute right would have required piano roll manufacturers and recording companies to obtain consent from songwriters before reproducing songs on phonorecords.²¹ Congress feared that making this right absolute would grant songwriters (and the publishing companies that typically owned songwriter catalogs) monopolistic control over the mechanical reproduction to their musical works.²² Thus, the compulsory license was born.

B. Mechanical Reproductions and the Compulsory Mechanical License

The 1909 Act carved out a major limitation to the reproduction right in 17 U.S.C. § 115. Once the owner of a musical work “made or authorized the recording” of a song—also defined as a “first use”—the owner no longer controlled the right of mechanical reproduction to that work.²³ Third parties could, instead of getting the songwriter’s consent, obtain a “compulsory mechanical license,” which allowed the reproduction of a song (after the “first use”) without the copyright owner’s permission, provided that the third party obtained a license through the Copyright Office’s statutory process and paid the statutory fee of two cents per phonorecord “made and distributed.”²⁴ This rate endured for sixty-eight years. Enter the

17. Copyright Act of 1909 § 1(e).

18. 17 U.S.C. §101. Phonorecords are defined as:

material objects in which sounds, other than those accompanying a motion picture or other audiovisual work, are fixed by any method now known or later developed, and from which the sounds can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device. The term ‘phonorecords’ includes the material object in which the sounds are first fixed . . .

and are generally understood to include vinyl, cassette tapes, compact discs, and even hard drives. *Id.*

19. Copyright Act of 1909 § 1(e).

20. *See infra* Part III.A.

21. For example, this would require a record label to get songwriter consent before releasing a cover of a song.

22. *See* Copyright Act of 1909 § 1(e).

23. *Id.*, superseded by 17 U.S.C. §§ 101-914; *see also* 17 U.S.C. § 115(c)(2).

24. *See* Copyright Act of 1909 § 1(e).

Copyright Act of 1976.²⁵ For the first time in what many considered to be too long, Congress increased the statutory rate for mechanical reproductions; starting in 1978, the new rate per mechanical reproduction was 2.75¢.²⁶

The 1976 Act kept the compulsory licensing system intact. It also limited the meaning of “first use” to any distribution of the song *to the public* embodied on a phonorecord.²⁷ This was included primarily to prevent the distribution of demo recordings, which are not distributed to the public, from qualifying as a “first use”—a use that would have qualified as a first use under the 1909 Act.²⁸ Thus, while song owners still controlled the first use for mechanical reproduction of a particular song, once an authorized and qualifying first use was made, any third party could obtain a compulsory license to reproduce that song and distribute it via a phonorecord, i.e., make a mechanical reproduction.

When the compulsory license was first enacted, Congress included a mechanism by which third parties were required to provide song owners with notice of an intended mechanical reproduction, as well as a way to remit royalty payments.²⁹ While the mechanism bypassed the need to license directly with the song owner, it was, and still is, a fairly complex and inefficient bureaucratic process.³⁰ Most parties interested in obtaining a compulsory license would likely be better off seeking it directly from the song owner, or the song owner’s representative,³¹ such as the Harry Fox Agency, a private organization which was established in 1927 by the National Music Publisher’s Association (“NMPA”) for the purpose of granting mechanical licenses on behalf of song owners.³²

The next part will delve further into the specific provision of 17 U.S.C. § 115, which created the mechanical royalty rate, as well as introduced the

25. For those good with numbers, you will catch that there are only sixty-seven years between copyright laws. While the current Act is referenced by the year 1976, it did not take effect until January 1st, 1978. See Copyright Act of 1976 § 102.

26. See 17 U.S.C. § 115(c)(2) (amending the compulsory royalty to 2.75¢).

27. See Copyright Act of 1976 § 107.

28. See Copyright Act of 1909 § 1(e).

29. See *id.*

30. See *Section 115 of the Copyright Act: In Need of an Update?: Hearing Before the Subcomm. on Courts, the Internet, and Intellectual Property of the H. Comm. on the Judiciary* 108th Cong. 2 (2004) (statement of Jonathan Potter, Executive Director, Digital Media Association).

31. See Timothy A. Cohan, *Ghost in the Attic: The Notice of Intention to Use and the Compulsory License in the Digital Era*, 33 COLUM. J.L. & ARTS 499, 500 (2010) (“Despite the theoretical permission of the Copyright Act to do otherwise, our cover artist may be better off trying to locate and obtain permission from the copyright owner or its agent”).

32. However, even licensing through the Harry Fox Agency has its pitfalls, because it still lacks authority to license a large portion of available music. See *id.* at 508.

music industry's contractual retort to the compulsory mechanical rate, namely, the Controlled Composition Clause.³³

III. SECTION 115 AND THE CONTROLLED COMPOSITION CLAUSE

A. *Section 115 of the Copyright Act*

Despite establishing a compulsory mechanical royalty rate, Section 115 of the Copyright Act provided for an exception to the statutory rate.³⁴ A direct license from the song owner or its authorized agent could vary from the royalty rates established by the Copyright Royalty Tribunal (“CRT”),³⁵ later succeeded by Copyright Arbitration Royalty Panel (“CARP”).³⁶ The song owner could agree to a lesser rate, or could even ask for a greater rate. In that case, however, the requesting party could bypass a direct license by obtaining it at the then-current rate through the compulsory license process. Of course, a song owner would likely never voluntarily agree to a lesser rate, unless the requesting party had the upper hand in the negotiations.

The language of 17 U.S.C. § 115(c)(3)(B), which contains the general exception to the statutory rate, allows “any persons entitled to obtain a compulsory license under subsection (a)(1) [to] negotiate and agree upon the terms and rates of royalty payments under this section.”³⁷ The statute allows for quite a bit of leeway in negotiating the mechanical royalty rate. “Terms and rates of royalty payments” are all fair game for negotiation and, consequently, reduction.³⁸ This provision, however, did not have a substantial effect until the tide shifted in 1976, when the statutory mechanical rate increased by 37.5%, from 2.0¢ to 2.75¢.³⁹ Since then, through a series of administrative proceedings, first by the CRT, then CARP, the mechanical royalty rate has increased periodically.⁴⁰ The current rate is 9.1¢ per song per phonorecord.⁴¹

33. *See infra* Part III.

34. *See* 17 U.S.C. § 115(c)(3)(B).

35. Copyright Act of 1976, ch. 8, § 801, 90 Stat. 2541 (1976) (current version at 17 U.S.C. § 801 (2006)).

36. Copyright Royalty Tribunal Reform Act of 1993, sec. 2, § 801, 107 Stat. 2304 (1993) (current version at 17 U.S.C. § 801 (2006)).

37. 17 U.S.C. § 115(c)(3)(B).

38. *See generally id.* § 115(c)(3)(B)-(D).

39. Copyright Act of 1976 § 115, (current version at 17 U.S.C. § 115 (2006)).

40. *See* 37 C.F.R. § 385.3 (2013).

41. *Id.* § 385.3(a).

B. *The Controlled Composition Clause*

After sixty-eight years of paying two cents for mechanical reproductions, the record companies did not want to have to pay out more money to songwriters, and thus sought ways to limit the amount of mechanical royalties payable. It was shortly after the rate changed, effective in 1978, when the light bulb went off. Record labels figured that if they only paid seventy-five percent of the then-current mechanical rate, they would be able to keep costs on mechanical royalties to near pre-1978 levels. The provision in the recording contract that ultimately allowed this reduction was called the “Controlled Composition Clause.”⁴²

A recording contract is between a record label and a performing artist or band. The record label’s job is to distribute sound recordings, thus the label can either acquire rights from a publisher to reproduce songs, or require artists to record songs directly. In return for recording a song, the artist is normally paid a record royalty. Simultaneously, the record label pays the owner of the underlying song—which may or may not be a different person from the song performer—a mechanical royalty. While the record label will not often be able to successfully negotiate a lower mechanical royalty rate from a third-party song owner, it can insist on a lower rate from a performing artist signing a recording contract who is also the song’s writer. If the artist/songwriter wants a recording contract, they will have to agree to a decreased mechanical royalty rate for the songs controlled by the artist/songwriter, a “Controlled Composition.” The “controlled” element does not merely cover songs written solely by the artist; it often includes songs written or controlled by producers, co-writers, and any other parties whereby the performing artist has a direct or indirect ownership interest, even if those outside parties do not agree to the reduced rate.⁴³

42. The Controlled Composition Clause existed prior to the 1976 amendment to the Copyright Act, but normally acted on maximum amounts payable limited by number of songs per album or single, and not as a reduction of the actual statutory rate per song. See Mario F. Gonzalez, *The Statutory Overriding of Controlled Composition Clauses*, 9 UCLA ENT. L. REV. 29, 32 (2001) (“Prior to the 1976 Copyright Act, many recording contracts merely stated that controlled compositions would be available for mechanical licensing at the statutory rate and that the maximum rates would not be more than ten times the statutory rate for albums, two times the statutory rate for singles, etc.”).

43. As defined in a standard recording contract, Controlled Compositions are “any Compositions or material recorded pursuant to this agreement which, in whole or in part, is written or composed, and/or owned or controlled, directly or indirectly, by you and/or any individual member of Artist and/or any producer of a Master and/or anyone affiliated with you or any such producer.” See Jay Rosenthal, *The Recording Artist/Songwriter Dilemma: The Controlled Composition Clause—Enough Already!*, 3 No. 4 LANDSLIDE 46, 48 (Mar./Apr. 2011) (defining a Controlled Composition).

C. The Controlled Composition Clause Applied to Physical Phonorecords

Songwriters, and their publishing designees, have had mechanical royalties reduced for physical phonorecords by the Controlled Composition Clause since the statutory rate increased in 1976.⁴⁴ The reduced royalties have been effectuated in many ways, and not simply by reducing the actual statutory rate by a certain amount. Below are a few common examples of how record labels have limited the royalties payable to artist/songwriters for physical phonorecords through the Controlled Composition Clause.

1. Base Rate Reduction

The most direct way for a record label to reduce mechanical royalties payable to song owners is to simply reduce the statutory rate by a certain amount—usually by twenty-five percent of the statutory rate.⁴⁵ Thus the Controlled Composition Clause will provide that for each song owned by the recording artist, the maximum amount payable for that musical work will be seventy-five percent of the statutory minimum. For example, a recording artist has three Controlled Compositions with a reduction to seventy-five percent of the statutory rate ($9.1\text{¢} \times 75\% = 6.825\text{¢}$). Assume the album sells 100,000 copies, without the Controlled Composition Clause, the calculation for the recording artist's royalty is straightforward. The royalty comes out to \$27,500 (3 songs per album \times 9.1¢ per song \times 100,000 albums sold).

However, in our example the Controlled Composition Clause changes the equation and reduces the per song rate by 75%, for a total of \$20,475 (3 songs per album \times 9.1¢ per song \times 75% rate per song \times 100,000 albums sold). Here, the Controlled Composition Clause reduces the per song royalty rate, decreasing the amount payable to the artist/songwriter to the tune of \$6,825, an amount that would otherwise go to the recording artist.

2. Per Album Cap

Another common way to reduce the amount of mechanical royalties payable to song owners is to place a ceiling on the number of songs per album that will earn a mechanical royalty. Using this method, a record label will include in its Controlled Composition Clause that it will only pay mechanical royalties on, for example, a maximum of ten songs per album. If there are any additional songs on the album, the artist/songwriter will not be entitled to more mechanical royalties.

44. See *infra* Part III.C.

45. See 17 U.S.C. § 115(c)(3)(B)-(D).

Assume for this example that the recording artist releases a fourteen-song album and is subject to a Controlled Composition Clause with a ten song cap. This album goes platinum and sells 1,000,000 copies. Without the Controlled Composition Clause, the royalties owed to the artist would be \$1,274,000 (fourteen songs per album x 9.1¢ per song x 1,000,000 albums). Thus, if the artist had written all the songs without any other writers, the artist would be entitled to well over one million dollars in mechanical royalties.

But our artist/songwriter is subject to an album cap, and thus the royalty earned actually equals \$910,000 (ten songs [cap per album] x 9.1¢ per song x 1,000,000 albums sold). This is a difference of \$364,000 that otherwise would be paid to the song owner, but because four out of fourteen songs are not earning royalties by virtue of the Controlled Composition Clause, the record label retains that extra profit. After accounting for the twenty-five percent per song reduction that is normally combined with the album cap, the payout is diminished even further.

3. Song Length Cap

Yet another way for record labels to limit the mechanical royalties payable to artist/songwriters is to designate a maximum song length for the purpose of calculating mechanical royalties. Under the Copyright Act, mechanical royalties are: 9.1¢ per song, 1.75¢ per minute of playing time, or some fraction thereof, whichever is larger.⁴⁶ Thus, if a song is longer than 5.2 minutes (9.1¢ ÷ 1.75¢/min.), it should command a mechanical royalty rate greater than the 9.1¢ rate. However, the Controlled Composition Clause can limit royalties to the 9.1¢ rate, creating an effective cap for payable song length of 5.2 minutes, regardless of the actual length of the song on the phonorecord.

For example, the Controlled Composition Clause in a recording contract limits the mechanical royalty payable to the statutory minimum of 9.1¢ per song per phonorecord, regardless of its length. An artist/songwriter writes a nine-minute masterpiece, and it is subsequently released on an album which sells 500,000 copies. Without the Controlled Composition Clause, the mechanical royalty rate should be \$78,750 (one song per album x nine minutes of playing time x 1.75¢ per minute x 500,000 albums sold). However, because of the song length maximum, the royalties payable are actually \$45,500 (one song per album x 9.1¢ per song x 500,000 albums sold). This difference of \$33,250 would have gone to the artist/songwriter

46. See *Mechanical License Royalty Rates*, U.S. COPYRIGHT OFFICE (Jan. 2010), <http://www.copyright.gov/carp/m200a.pdf>.

had the recording agreement not been subject to the song length cap in the Controlled Composition Clause.

4. *Effect of Third Party Songwriters*

The effects of the Controlled Composition Clause are magnified when there are third party writers also contributing to songs on an album. As discussed above, under standard industry practice, labels will limit the amount of songs per album for which they will agree to pay mechanical royalties.⁴⁷ This is detrimental to the recording artist when there are songs that are *not* controlled compositions (i.e., from outside writers) included on the album, which may result in a total amount payable for mechanical royalties that is higher than the amount agreed to between the recording artist and record label.

By way of example, a record label releases a twelve-song album, with eight songs written by the artist (“inside” songs) and four written by a third-party songwriter (“outside” songs). The recording contract establishes a limit on the number of songs per album for which the label is willing to pay mechanical royalties. In this example that limit is ten songs. The maximum amount of mechanical royalties allowed would then be 68.75¢ (ten songs x 75% of 9.1¢). Unless they agree to a reduced rate, third-party songwriters, because they are not subject to the recording artist’s Controlled Composition Clause, will insist on being paid the full statutory rate. Here this amounts to 36.4¢ (four songs x 9.1¢). That leaves the artist/songwriter with the remaining 32.35¢. Thus, the artist/songwriter is subject to an additional reduction in total mechanical royalties. Here, he artist/songwriter received 4.04¢ per song (32.35¢ ÷ 8 songs) or 44.4% of the statutory amount.

These numbers start to hint at the possibility that, in the wrong circumstances, an artist/songwriter’s mechanical royalty may vanish completely. In fact, that is exactly what happens when outside compositions outnumber inside compositions.

Borrowing from the previous example, we still have a twelve-song album subject to the Controlled Composition Clause and a ten-song limit per album. But this time the artist only wrote four of the twelve songs and a third-party songwriter wrote eight. This breakdown would provide for 27.3¢ of mechanical royalties payable to the artist/songwriter (four songs x 75% of 9.1¢) and 72.8¢ payable to the third-party songwriter (eight songs x 9.1¢), for a total of \$1.01. Due to the reduced mechanical royalty and ten-song cap, the artist/songwriter may owe more mechanical royalties for

47. See David Moser, *The Controlled Composition Clause: Is It Out of Control?*, 14 WTR ENT. & SPORTS L. 3, 5 (1997) (discussing the effect of per-album limits in Controlled Composition Clauses).

outside songs than is allowed under the Controlled Composition Clause. The maximum amount of mechanical royalties allowed is 68.7¢ per album (ten songs x 75% of 9.1¢). When the label pays the third-party songwriter, it will quickly realize that it paid more than the agreed total of mechanical royalties, pursuant to the Controlled Composition Clause, in the recording artist/songwriter's contract. In this situation, the label passes the burden of paying the outstanding balance to the recording artist/songwriter. As a result, not only does the artist not receive a mechanical royalty payment (because it all goes to the third-party songwriter's mechanical royalty payment), but the artist also incurs a debt to be recouped by the label! In this example, the artist/songwriter would be responsible for covering 4.1¢ per album (68.7¢ – 72.8¢), a sum that will be recouped directly from the artist's record royalties.

This type of situation may arise with any Controlled Composition Clause royalty reduction, provided that there are outside writers unwilling to agree to less than the statutory royalty rate—as long as a third-party writer is guaranteed his full statutory rate, the artist/songwriter will always take the hit and see his royalties decreased so that the record label does not pay more than the recording contract's Controlled Composition Clause provides. It should also be noted that the reduction methods mentioned above are not mutually exclusive and, in fact, are oftentimes compounded to further guarantee a reduction in the artist/songwriter's mechanical royalties.

The Controlled Composition Clause was not welcomed with open arms by recording artists who also happened to be writers of their songs.⁴⁸ But what if Congress, through the Copyright Act, precluded the practice of reducing royalty rates for certain types of phonorecords?

IV. SECTION 115 AND DIGITAL PHONORECORD DELIVERIES

A. *Inclusion of Digital Phonorecord Deliveries*

In 1995, the Digital Performance Right in Sound Recordings Act of 1995⁴⁹ was passed to accommodate for the quickly-changing technological landscape, namely, the growing availability of digital music files, and the new threat they represented to the vitality of the music industry by substantially decreasing physical record sales.⁵⁰ The DPRA took on the task

48. See Rosenthal, *supra* note 43, at 48.

49. Digital Performance Right in Sound Recordings Act of 1995, Pub. L. No. 104-39, 109 Stat. 336 (1995) (prior to 1997 amendment).

50. See S. REP. NO. 104-128, at 15 (1995).

This legislation is a narrowly crafted response to one of the concerns expressed by representatives of the music community, namely that certain types of subscription and

of defining terms to reflect the industry's new digital realities. Most important was the addition of the "digital phonorecord delivery" ("DPD") to the Copyright Act and the simultaneous expansion of compulsory mechanical licenses to cover DPDs through 17 U.S.C. § 115(c)(3)(E).⁵¹ DPDs are defined as follows:

A "digital phonorecord delivery" is each individual delivery of a phonorecord by digital transmission of a sound recording which results in a specifically identifiable reproduction by or for any transmission recipient of a phonorecord of that sound recording, regardless of whether the digital transmission is also a public performance of the sound recording or any nondramatic musical work embodied therein. A digital phonorecord delivery does not result from a real-time, non-interactive subscription transmission of a sound recording where no reproduction of the sound recording or the musical work embodied therein is made from the inception of the transmission through to its receipt by the transmission recipient in order to make the sound recording audible.⁵²

With this addition, the legislature sought to ensure that copyright owners would receive remuneration for the digital phonorecord deliveries of their compositions in the face of new and rapidly changing technology.⁵³ But the legislature went further than simply ensuring that DPDs would qualify for mechanical royalties.⁵⁴ By including the second sentence of 17 U.S.C. § 115(c)(3)(E)(i), Congress distinguished mechanical royalties for DPDs from physical phonorecords.

interactive audio services might adversely affect sales of sound recordings and erode copyright owners' ability to control and be paid for use of their work.

Id.

51. See Brian Sanchez, *The Section 115 Mechanical License and the Copyright Modernization Act: The Hardships of Legislating Music Industry Negotiations*, 17 DEPAUL-LCA J. ART & ENT. L. & POL'Y 37, 42-3 (2006); see also 17 U.S.C. § 115(c)(3)(E).

52. See 17 U.S.C. § 115(d).

53. See S. REP. NO. 104-128, at 37.

The intention in extending the mechanical compulsory license to digital phonorecord deliveries is to maintain and reaffirm the mechanical rights of songwriters and music publishers as new technologies permit phonorecords to be delivered by wire or over the airwaves rather than by the traditional making and distribution of records, cassettes and CD's.

Id.

54. For the purposes of qualifying for mechanical royalties, "digital phonorecord deliveries" are the same as phonorecords.

B. Section 115(c)(3)(E)(i) – The Contract Override

17 U.S.C. § 115(c)(3)(E)(i) introduced a new type of provision to the Copyright Act, creating a dynamic that had not previously existed for physical phonorecords. The first sentence of this section allows copyright owners to freely negotiate the “terms and rates” for mechanical licenses applied to phonorecords.⁵⁵ However, and most important to this discussion, the second sentence carves out an exception exclusively for DPDs.⁵⁶ Specifically, it states that, subject to the two exceptions discussed below,⁵⁷ the statutory mechanical rates in 17 U.S.C. § 115 (the “Contract Override”):

[S]hall be given effect as to digital phonorecord deliveries in lieu of any contrary royalty rates specified in a contract pursuant to which a recording artist who is the author of a nondramatic musical work grants a license under that person’s exclusive rights in the musical work under paragraphs (1) and (3) of section 106 or commits another person to grant a license in that musical work under paragraphs (1) and (3) of section 106, to a person desiring to fix in a tangible medium of expression a sound recording embodying the musical work.⁵⁸

The language of this provision appears to be tailored specifically to the circumstances surrounding use of the Controlled Compositions Clause, wherein a “recording artist who is the author of a nondramatic musical work”⁵⁹ grants a license to a third party for exploitation of the recording artist’s exclusive right to mechanically reproduce a work⁶⁰—exactly the types of individuals covered by the standard Controlled Composition Clause. Indeed, this is no mere coincidence. Congress’s desire to increase the level of protection afforded compositions in digital formats is quite evident in the legislative record: “Subject to the exceptions set forth in subparagraph (E)(ii), the second sentence of subparagraph (E)(i) is intended to make these controlled composition clauses inapplicable to digital phonorecord deliveries.”⁶¹ This legislation made clear that, except for the

55. 17 U.S.C. § 115(c)(3)(E)(i).

56. *Id.*

57. *See infra* Part IV.C.

58. 17 U.S.C. § 115(c)(3)(E)(i).

59. *Id.*

60. *Id.*

61. *See* S. REP. NO. 104-128, at 41; *see also* Section 115 Compulsory License: Hearing Before the Subcomm. on Courts, the Internet, and Intellectual Property of the H. Comm. on the Judiciary, 109th Cong. 2 (2004) (statement of Marybeth Peters, Register of Copyrights). Apart from the extension of the compulsory license to cover the making of DPDs, Congress also addressed the common industry practice of incorporating controlled composition clauses into a songwriter/performer’s recording

two limited exceptions in 17 U.S.C. § 115(c)(3)(E)(ii) discussed below, the Contract Override should apply to all DPDs.⁶² These DPDs would then command the statutory mechanical rate, and artist/songwriters would receive the entire amount of mechanical royalties as opposed to the typical 75% that applies to physical phonorecords.

As is clear from the legislative history of the DPRA, Congress intended for the Contract Override to mitigate the detrimental effects that the Controlled Composition Clause had on copyright owners.⁶³ However, rather than make it an absolute rule, two exceptions were carved out to allow parties to avoid the mandatory statutory rate for the mechanical reproduction of musical works on DPDs.⁶⁴

C. 17 U.S.C. § 115(c)(3)(E)(ii) – Contract Override Exceptions

1. Subsection I

The first exception addresses contracts entered into on or prior to June 22, 1995.⁶⁵ It protects copyright owners from the alteration of contracts to create less favorable calculations than the original mechanical royalty terms (“Subsection I”).⁶⁶ For present purposes, this exception does not warrant much discussion, because the potential for circumventing the intent of Congress is relatively low. Indeed, any expansion of coverage for reduced rates in the relevant contracts will be overridden by the statutory rate. Most real-world issues that arise from DPDs and mechanical royalty rates will not come from Subsection I, but from the exception found in Subsection II.

2. Subsection II

The second exception is more complex and poses many more issues with regard to protecting copyright owners. Paragraph (c)(3)(E)(ii)(II) of 17 U.S.C. § 115 (“Subsection II”) creates an exception for compositions intended for commercial release, which are already recorded, and for which a contract has not been entered into, wherein the recording artist retains the right to issue mechanical licenses.⁶⁷ The language of the statute states that the statutory rate on DPDs shall not be mandatory for:

contract, whereby a recording artist agrees to reduce the mechanical royalty rate payable when the record company makes and distributes phonorecords including songs written by the performer. *Id.*

62. See S. REP. NO. 104-128, at 41. (“Subject to the exceptions set forth in subparagraph (E)(ii), the second sentence of subparagraph (E)(i) is intended to make these controlled composition clauses inapplicable to digital phonorecord deliveries”).

63. See *id.*

64. See 17 U.S.C. § 115(c)(3)(E)(i).

65. See *id.* § 115(c)(3)(E)(ii)(I).

66. See *id.*

67. *Id.* § 115(c)(3)(E)(ii)(II). Creating an exception for:

[A] contract entered into after the date that the sound recording is fixed in a tangible medium of expression substantially in a form intended for commercial release, if at the time the contract is entered into, the recording artist retains the right to grant licenses as to the musical work under paragraphs (1)[(the right to distribute in copies and phonorecords)] and (3) [(the right to distribute copies on phonorecords)] of section 106.⁶⁸

Despite the many possible interpretations that exist for the Subsection II exception,⁶⁹ the legislative history for the provision makes clear in which situation this exception should apply, namely, when an artist/songwriter is self-publishing and enters into a recording contract only after recording the song.⁷⁰

A hypothetical situation may better illustrate this scenario. Recording artist Angela produces an EP of four songs, which she plans to release for sale, and which she wrote herself. Angela self-publishes her songs on an EP, and signs a contract with Crazy 8 Records to release the EP. Under these facts, Angela meets all the requirements necessary to fall within the Subsection II exception, as explained by Congress. Angela is self-publishing and enters into a deal with a record label after producing her songs. Thus, if Crazy 8 Records wants to pay Angela a decreased mechanical royalty rate, they are free to do so and Angela is free to accept that.⁷¹

What happens if the facts change slightly? Assume the same situation as above, but instead of self-publishing, Angela decides to also look for a third-party publisher and ultimately strikes up a deal with Big Publisher. As with most publishing agreements, Big Publisher has exclusive administration rights in the compositions. Big Publisher then gets Crazy 8 Records to release Angela's EP, subject to a reduced mechanical royalty of 75% for all mechanical reproductions.

a contract entered into after the date that the sound recording is fixed in a tangible medium of expression substantially in a form intended for commercial release, if at the time the contract is entered into, the recording artist retains the right to grant licenses as to the musical work under paragraphs (1) and (3) of section 106.

Id.

68. *Id.*

69. See Gonzalez, *supra* note 42, at 38–39.

70. See S. REP. NO. 104-128, at 42. The second of the exceptions provided in subparagraph (E)(ii) is intended to allow a recording artist-author who chooses to act as his or her own music publisher to agree to accept mechanical royalties at less than the statutory rates, provided that the contract containing such lower rates is entered into after the sound recording has been fixed in a tangible medium of expression substantially in a form intended for commercial release. *Id.*

71. See 17 U.S.C. § 115 (c)(3)(E)(ii)(II).

Under the Subsection II exception, should Big Publisher be precluded from decreasing the rate for mechanical royalties to be paid to Angela for the songs on her EP? Applying Subsection II part-by-part should yield the answer: first, the contract was entered into after Angela fixed the sound recording in a tangible medium of expression ,i.e., she has already recorded the songs; second, Angela intended to sell the songs, so they should be considered intended for commercial release; the third element of the Subsection II exception, arguably, is not met, however, because Angela assigned Big Publisher *exclusive* administration rights. If Angela does not retain “the right to grant licenses as to the musical work,” she may not fall within the exception.⁷² Unless another provision of the agreement allows Angela to issue licenses, notwithstanding Big Publisher’s exclusive administration rights, then the Subsection II exception would not apply and Angela cannot negotiate Controlled Composition Clause treatment for any digital phonorecords distributed by Crazy 8 Records under its license from Big Publisher.

The reality is that most artists will not have carve-outs from the publisher’s exclusive administration rights to license their compositions themselves. Thus, an artist will not retain the right to license their compositions after signing a publishing deal, and the Subsection II exception should not apply, thereby theoretically entitling most artists/songwriters to the full statutory rate for mechanical reproductions on DPDs.

Certain aspects of Subsection II may also be exploited to force contracts to fall within the exception. For instance, record labels could have artists sign a recording contract, record an album, and then sign a separate mechanical licensing agreement for the newly-recorded music. Arguably, this may fall within the exception, because the contract is signed after recording of the songs. In which case, a record label could sign an artist to one album—the initial album—followed by a right of first refusal on subsequent albums. Technically, the artist who retains his publishing to said subsequent albums would not be under contract with the record label at the time of the album’s creation. Thus, Subsection II would appear to be applicable. Additionally, as mentioned above, labels could grant artists a limited right to license the music. Again, this might allow negotiated mechanical rates for DPDs, because it addresses the language in Subsection II regarding the artist’s “right to grant licenses.”⁷³ Nevertheless, the language in the Contract Override may provide room for interpretation wherein the mechanical royalty rate for DPDs is reduced.

72. *Id.*

73. *See id.* § 115(c)(3)(E)(ii).

D. *The Statutory Loophole*

Congress intended to allow license agreements for DPDs to reduce statutory rates in the two limited circumstances described above.⁷⁴ However, there still remains a possibility that mechanical rates for DPDs may effectively be reduced without appeal to Subsection I or Subsection II. The Contract Override states that “the royalty rates” determined by statute shall be applied in lieu of conflicting contract rates,⁷⁵ but does not use the same language from 17 U.S.C. § 115(c)(3)(B) describing flexibility in “terms and rates.”⁷⁶ Thus, a plain reading of the statute dictates that the rates for DPDs not be changed, but does not explicitly prohibit the alteration of mechanical royalty terms.⁷⁷

The following part will analyze the text of the Contract Override, and discuss possible ways in which, even without the application of Subsections I or II, record companies may still pay out less in mechanical royalties for DPDs to song owners than the Contract Override mandates while still technically adhering to its terms.⁷⁸

V. POTENTIAL CIRCUMVENTIONS OF THE CONTRACT OVERRIDE

In practice, the Contract Override may do little to stem the widespread use of the Controlled Composition Clause for DPDs. The potential negative effects will only become more pronounced as the digital distribution of music continues to claim a larger portion of the market.⁷⁹ The above examples of how record companies have applied the Controlled Composition Clause to physical phonorecords begin to show how the Contract Override may fail at achieving its intended purpose of protecting the rights of copyright owners by mandating the application of the statutory mechanical royalty rate. This part of the Article will walk through the language of the Contract Override, and go through some of the practical effects of the Contract Override on common industry practice, with an emphasis on ways in which record companies can potentially subvert its

74. *See supra* Part IV.C.

75. *See* 17 U.S.C. § 115(c)(3)(E)(i).

76. *See id.* § 115(c)(3)(B).

77. *Id.* § 115(c)(3)(E)(i).

78. *See supra* Part V.

79. *See* Lisa Respers France, *Is the Death of the CD Looming?*, CNN (July 20, 2010), <http://www.cnn.com/2010/SHOWBIZ/Music/07/19/cd.digital.sales/index.html>. (“[I]n 2007 CDs accounted for 90 percent of album sales in the United States, with digital accounting for the other 10 percent. Just two years later, that number had shifted to 79 percent CDs and 20 percent digital”); *see also* Joel Rose, *The Legacy of the CD: Innovation that Ate Itself*, NPR (Mar. 9, 2011, 2:00 PM), <http://www.npr.org/blogs/therecord/2011/03/09/134391895/the-legacy-of-the-cd-innovation-that-ate-itself>. (“Sales of compact discs have fallen 50 percent over the past decade.”).

protections and continue to pay copyright owners reduced mechanical rates for DPDs.⁸⁰

A. *The Flexible Language of the Override Exception*

As indicated above, the language of the Override Exception focuses on overriding conflicting “royalty rates” for DPDs.⁸¹ Unlike 17 U.S.C. § 115(c)(3)(B), the Contract Override exerts its power only over “rates” and not “terms and rates,” as mentioned in the case of non-digital phonorecords.⁸² In the case of 17 U.S.C. § 115(c)(3)(B), the flexibility afforded copyright owners allows true freedom to negotiate all aspects of mechanical license agreements and opens the door to various—and creative—royalty payment arrangements, especially because the language of 17 U.S.C. § 115(c)(3)(B) broadly states that “terms and rates of royalty payments” are subject to change.⁸³ The Contract Override, however, refers only to trumping of “royalty rates” when it comes to DPDs.⁸⁴

This difference in language cannot be ignored, given that Congress, only three subparts prior to the Contract Override, evidenced a desire to grant substantial freedom in mechanical license agreements through its choice of broad language. Taken in context, the Contract Override could be interpreted as excluding “terms” from its control. Because of the omission of “terms,” there exist various possibilities for record companies to exploit the omission and decrease the amounts paid to copyright owners—not through alteration of the mechanical royalty “rates,” but through alterations in the terms and accounting practices for said mechanical royalties. Why Congress did not use the same language as in 17 U.S.C. § 115(c)(3)(B) is not clear, but the potential impact it could have on song owners is apparent by looking at industry practice for physical phonorecords.

B. *Album Cap in Royalty Calculation*

As indicated above, the Contract Override is intended to trump conflicting contractual “rates” with regard to mechanical royalties for DPDs. As such, it is unclear whether, even if compensating a recording artist with the full statutory rate for songs reproduced on DPDs, a record label may permissibly put a cap on the number of songs that will earn mechanical royalties. The example above in Part IV.C.2 illustrates the common industry practice of placing a maximum on the number of songs

80. *See infra* Part V.

81. 17 U.S.C. § 115(c)(3)(E)(i).

82. *Id.*

83. *See id.* § 115(c)(3)(B).

84. *Id.* § 115(c)(3)(E)(i).

per album that will earn mechanical royalties. In much the same way, it may be possible for record labels to pay song owners less than the full statutory rate for DPDs while not reducing the “rate.”

An album cap is technically not a rate reduction; songs still earn a full statutory rate, but the number of songs earning the full rate is predetermined. Thus, if a record company places an album cap of ten for mechanical reproductions earning royalties, and then releases the album with fourteen Controlled Compositions, the artist/songwriter will not receive the royalties for the four extra songs, but cannot say that the actual royalty “rate” was reduced. Because the Contract Override only applies to “rates,” this reduction in royalty payments may still adhere to the mandate in Section 115 as it relates to DPDs.

If Section 115’s override exceptions are interpreted to cover only “rate” reductions, this sort of practice, technically, does not reduce the per-song royalty rate. A record label could argue that as long as the “per-song rate” is not being reduced by contract, it does not run afoul of the Contract Override. In practice, the effect is quite obviously to decrease the overall amount of royalties for the same amount of songs, which, effectively, is really a per-song “rate” reduction.

C. *Song Length Caps Potentially Not Rate Reductions*

Part III.C.3 above also explains how record labels may place a cap on the length of the song that will earn mechanical royalties. In order to work around the per-minute rate,⁸⁵ which surpasses the base rate of 9.1¢ once the song length exceeds 5.2 minutes, record labels can negotiate to cap royalty-earning song lengths to equal 9.1¢. Arguably, limiting the royalty-earning length of the song is not a rate reduction—it neither reduces the 9.1¢ base rate, nor decreases the 1.75¢ per minute rate for songs that surpass 5.2 minutes in length.

While this type of Controlled Composition Clause is closer to an actual “rate” reduction than the album cap mechanism, it does not take much imagination to envision record companies attempting to justify it as permissible under the Contract Override. Because most songs, especially those seeking to be “radio-friendly,” are typically less than five minutes long, it is unlikely that this type of structuring will make a meaningful impact on the Contract Override.

85. See *supra* Part III.C.3.

VI. PRACTICAL CONSIDERATIONS

A. *Practical Effects of The Contract Override*

The foregoing discussion shows that the Contract Override may still leave room, if only a little, for record companies to effectively reduce mechanical royalty rates for Controlled Compositions. By taking advantage of the legislature's omission of the word "terms" in the Contract Override, copyright exploiters can use pre-existing, industry-standard contract drafting techniques to impose non-rate changes on DPD mechanical royalties, thereby circumventing the statutory mandate and retaining royalty monies that otherwise would go to the copyright owner. Just as with physical phonorecords, when rates or terms are changed in an effort to lower mechanical royalty payments, the inclusion of songs written by third-party songwriters exacerbates the negative effect on royalties earned for Controlled Compositions. Even the little room that may exist for record companies to decrease payments to song owners could have significant effects on their ability to be fully compensated for exploitation of their copyrights, as is shown in Part IV.C of this Article.⁸⁶

While the DPRA was intended to protect copyright owners from the detrimental effects of the Controlled Composition Clause, the limited language of the Contract Override itself may make it harder for copyright owners to actually reap the benefits of Congress's legislative intent. After nearly twenty years, perhaps it is time for Congress to revisit the Copyright Act and ensure that loopholes like the ones mentioned above are addressed. Especially now, given the increasing availability and widespread adoption of purchasing music by way of digital phonorecord delivery, the question of how DPDs should be treated is as important as ever, and the stakes are increasingly higher.

B. *Potential Solution?*

While the authors do not necessarily believe that making changes to the Copyright Act or copyright regulation is the answer, there may be ways in which the legislature could attempt to eliminate the potential issues that could arise from the Override exception's interaction with the industry-standard Controlled Composition Clause, which may still affect DPDs as if the DPRA had never been passed.⁸⁷

86. See generally *supra* Part III.C.2-3 (regarding differences in royalty payments as a result of the Controlled Composition Clause).

87. See Gonzalez, *supra* note 42, at 44. ("[I]t is surprising that the record companies are not modifying their controlled composition provisions in some manner to address the amendments to Section 115 under the DPRA.").

The language in 17 U.S.C. § 115(c)(3)(B) refers to a copyright owner's ability to freely negotiate the "terms and rates of royalty payments" for mechanical reproductions.⁸⁸ One potential solution is to simply amend the Contract Override provision to include "terms and rates" as opposed to merely overriding conflicting contract "rates." By expanding the coverage of the Contract Override to encompass "terms," it would be much harder for record companies to justify album or song length caps on mechanical royalties. In much the same way the Controlled Composition Clause has taken advantage of the liberty made possible by 17 U.S.C. § 115(c)(3)(B) in changing royalty payments, overriding "terms and rates" for DPDs would have a much more meaningful effect on copyright owners by giving them just as much protection for mechanical rates for DPDs as the Copyright Act grants flexibility for mechanical rates for physical phonorecords.⁸⁹

C. Industry Awareness

It is unclear whether record labels are cognizant of these potential loopholes in the Contract Override. Regardless of their awareness, the issue is important enough to warrant an active effort on the part of labels to understand the Contract Override in detail, and to act accordingly. Perhaps even more important than record labels being aware of these issues, artists and songwriters stand to lose much more. These copyright owners and their attorneys should be fully aware of the outcomes that could result when record labels exploit these loopholes and are willing to risk potential lawsuits to achieve significant savings in mechanical royalty payments. As such, steps should be taken in the industry to educate parties on both sides of recording transactions on these issues.

VII. CONCLUSION

This Article explained mechanical reproductions and the rights that follow them, explained how the compulsory mechanical licensing system was enacted by Congress in 1909, and how the royalty increase in 1978 elicited a response by the music industry in the form of the Controlled Composition Clause as we now know it. The Controlled Composition Clause can reduce the royalty rates for mechanical royalties on physical phonorecords, but the DPRA, enacted in 1995, introduced the Contract Override, which trumps conflicting mechanical royalty rates in contracts in the case of DPDs. However, certain loopholes that exist within the Contract

88. 17 U.S.C. 115(c)(3)(B).

89. *See id.*

Override itself could allow record labels to circumvent the protections afforded by that provision. Upon closer inspection, it is possible that those loopholes could be exploited to reduce mechanical royalty rates for DPDs—something that, according to Congress, should only occur in very limited circumstances. The practical considerations surrounding the Contract Override illustrate the importance of educating industry professionals on the potential impacts of its provisions, and hopefully this Article will assist in raising awareness of the surrounding issues.

The Contract Override obviously has great potential to impact the music industry. And now, with digital delivery of phonorecords becoming the preferred delivery method, the stakes for interpreting and applying the Contract Override are much higher. While Congress intended to protect copyright owners through passage of the DPRA, it seems that there still exist certain unintended statutory loopholes that enable copyright exploiters to skimp on mechanical royalty payments for DPDs. When Congress passed the DPRA nearly twenty years ago, it is unlikely that it realized how important the Contract Override would become, mainly due to its inability to predict how dominant digital music platforms would become in so short a time.

With digital music becoming such an important part of the music industry, it may be time to bring 17 U.S.C. § 115(c)(3) back into focus. That process may have to begin with a strong push to educate artists and songwriters about the rights that they do have when it comes to DPDs. If the legislature truly wishes to protect the rights of songwriters and recording artists, it might be time to revisit Section 115 of the Copyright Act and to take steps to better realize Congress's original intent when it passed the DPRA almost two decades ago.