



Written submission on the opportunities and barriers in the provision of copyrighted and non-copyrighted goods and services online

EMI Group Limited (*EMI*) is grateful to Commissioner Neelie Kroes for the invitation to participate in the meeting of the group of advisers on online issues on 17 September 2008, at which it was represented by Roger Faxon, Chairman and CEO of EMI Music Publishing.

The issues that were discussed at the roundtable are of great importance to EMI and to the music industry generally. Accordingly, EMI would like to take up the opportunity it has been offered to supplement the comments it made at the meeting with this additional written submission.

About EMI

Owned by private equity firm Terra Firm since 2007, EMI is one of Europe's pre-eminent music companies. EMI is present in almost every EU Member State, and it seeks to represent and nurture a culturally diverse group of artists and songwriters, both locally and on a worldwide scale.¹

EMI consists of two creative businesses that are operated largely independently of each other: EMI Recorded Music (*EMI Music*) and EMI Music Publishing (*EMI MP*). EMI Music's record labels sign and develop artists, market and promote them and distribute their music to physical and digital retailers. Its approach to the development of its roster focuses on investing in artists with long-term career potential and is designed to maximise both local and global sales. The EMI MP business involves the acquisition of music rights to, and the exploitation of, musical compositions. More particularly, its business involves the discovery and signing of, and the provision of creative and financial support to, authors/composers; promoting the use of their music; and, principally through the intermediary of collecting societies, licensing the authors/composers' works to those who wish to use the works, and collecting revenues from those users.

While copyright is central to EMI's activities, its experience in both physical sales and the online world, in the EU and elsewhere, may also be relevant to the opportunities and challenges facing online sales of non-copyrighted goods and services, as explained below.

¹ For more information, see: www.emigroup.com.

Opportunities of digital distribution

Like many businesses, EMI does not own the physical or online retail outlets for its products. EMI exited the physical retail business a long time ago. Instead, EMI relies on distributors and other intermediaries to disseminate its music. In the physical world, EMI's recorded music business competes with other entertainment products for shelf space at retailers, which are becoming increasingly concentrated and powerful. In the online world, Apple's iTunes is the only truly global outlet.

The music industry is going through a period of profound change – in large part as a result of digital (i.e., online and mobile) technology, which has become an integral part of the music business at all levels. Music is available nowadays in an increasing number of new formats and through an increasing number of channels, platforms and devices. This, in turn, has attracted new participants in the value chain, with different strategies and business models; and it has also encouraged a number of artists to cut out the music companies altogether and make their music available directly to their fans.

EMI's strategy is to make its content – both recorded music and music publishing rights – available as widely as possible, in any form. Other products may require different distribution strategies (e.g. selective distribution). But, for EMI, the more consumers that can be reached, the more likely its businesses will be able to find an audience for their products. In that context, the internet provides music businesses with the potential to reach huge numbers of consumers.

Accordingly, EMI wants to ensure that the intermediaries through which it reaches consumers make its content available without undue restrictions. For example:

- In recorded music, EMI has been a frontrunner in making available DRM-free downloads – an initiative which it first launched in partnership with iTunes.²
- In music publishing, EMI has taken an initiative to license its rights on a pan-European basis, as widely, efficiently and cost-effectively as possible (see below).³

² See: press release of 2 April 2007, "EMI Music launches DRM-free superior sound quality downloads across its entire digital repertoire", at <http://www.emigroup.com/Press/2007/press18.htm>.

³ See: press release of 23 January 2006, "EMI Music Publishing reaches agreement with MCPS-PRS and GEMA to establish 'one-stop' pan-European licensing of mobile and online digital rights in EMI MP's Anglo-American songs", at <http://www.emigroup.com/Press/2006/press6.htm>.

- Digital distribution also means consumers have more options – in the case of music, they can decide to buy a single track, a number of tracks, or an entire album. They can subscribe to services that let them listen to music without ever buying a disc or a download, and they can view virtually every music video made, at their will.

Challenges of digital distribution

The digital revolution has permitted great innovation, creating new opportunities for consumers and the businesses that serve them. But, in many ways, the digital marketplace in the EU has not developed into the engine of growth that was expected and is needed. To make that happen, there are significant challenges that need to be addressed.

One of the key challenges raised by digital technologies, is piracy. It has to be acknowledged that the pirates have been quicker, more effective and perhaps even more innovative at harnessing the power of the new technology than any legitimate business. In fact, in music, the pirate economy now dwarfs the legitimate market.⁴ However, the issue of piracy is not limited to intangible goods – in cities around the world, vendors are selling copies of products of almost every kind on the street. Pirates are even more pervasive online. They can sell their wares anonymously, and when they are pursued, they disappear only to begin again elsewhere. Piracy is pernicious: it attacks the commercial foundations of legitimate businesses. Without strong laws and the cooperation of the ISPs and the telecommunications industry, it will be impossible to build a stable marketplace for legitimate commerce on the internet.

The internet is a disruptive technology.⁵ It disrupts the historic commercial relationships that were grounded in the physical world. Those relationships must be reformulated and new ones must be developed to meet the different environment found in the digital world. Laws, regulations and institutions which were constructed to meet the needs of the terrestrial world need to be applied flexibly to the digital world. It is essential that this emerging area, and these new relationships and means of doing business, be allowed to develop freely so that the most effective new distribution and licensing models can develop through agreements between market players.⁶

But, as always, there is resistance to change, and in particular to fundamental change. So, it should not be surprising that there are those who are trying to use antitrust and regulation to preserve the status quo. This creates

⁴ See, for example: IFPI Digital Music Report 2008, which quotes independent estimates stating that up to 80 per cent of ISP traffic comprises distribution of copyright-infringing files.

⁵ Bower, Joseph L. & Christensen, Clayton M., "Disruptive Technologies: Catching the Wave", *Harvard Business Review*, January-February 1995.

⁶ See: European Parliament debate on the Report on Commission Recommendation - European Parliament plenary sitting, 14 November 2007 (Procedure INI/2006/2008, Lévai report A6-0053/2007 - Debate CRE 14/11/2007 -16.

confusion and paralysis, instead of the legal certainty that is needed to encourage the development of the digital marketplace.

Specific opportunities and barriers in the digital distribution of music

The fragmentation of the market for copyrighted goods is a significant impediment to the development of the online market. Perhaps more so than other copyrighted products, music in all of its forms – physical, digital, analogue – has been, and will continue to be, fragmented not only geographically but also by underlying rights as long as the institutions and processes for the provision of those underlying rights are nationally based.⁷

This geographic fragmentation is the natural consequence of the historical development of the music industry. The distribution of physical goods embodying music remains to this day largely nationally based because retail is largely organised on a national basis. The broadcast of music through radio, television, cable and satellite is, with rare exception, nationally focused. Also, the public performance of music is necessarily site-specific. So, it is not surprising that the supply of the rights necessary for these uses of music has been granted, and the terms have been set, on a national basis. However, national structures do not work in the online world, as the internet is not innately geographically based and is capable of serving consumers across geographic boundaries. Moreover, online users typically require an array of rights, and the current system is not structured to deliver these efficiently.⁸

Current administrative burden on users

The administrative burden on users of musical rights in the borderless world of the internet is very significant. In order to bring together the rights necessary simply to stream music across the EU, a user must obtain a licence from national performing rights societies (representing the compositions) as well as neighbouring rights societies (representing the master recordings) in every Member State. If a user, in addition, wants to sell the music as a download, it must gain further licences from a similarly long list of national collecting societies (responsible for the mechanical rights in the compositions) as well as licences from various record companies (which control the recordings). The complexity becomes even more striking when a user wants to broaden its offering to include video representations, lyrics, and other rights that are not controlled by the collecting societies. These rights must be obtained by going directly to each publisher(s) of the underlying composition.

⁷ See, for example: Commission Recommendation of 18 October 2005 on collective cross-border management of copyright, OJ 2005 L 276/54 (**Commission Recommendation**); and Commission Study on a Community Initiative on the Cross-Border Collective Management of Copyright dated July 2005 (**Commission Study**).

⁸ See, for example: Commission Recommendation , at recital 8: “*In the era of online exploitation of musical works ... commercial users need a licensing policy that corresponds to the ubiquity of the online environment and which is multi-territorial.*”

Thus, the supply of rights in the music sector is a minefield of complexity. This discourages innovation and locks out all but those with the resources to navigate the current maze and the willingness to adhere to the structure and approaches of the old terrestrial world. It is therefore no surprise that there are very few music-focused services that even approach a pan-European footprint.

The way forward: pan-European digital licensing

Some have suggested solutions ranging from the creation of a single EU-wide monopoly responsible for licensing all rights in the compositions, to streamlining the current inter-society system. The European Commission's Recommendation for Cross Border Online Music Services has suggested a better way forward. It adopts the principle of competition for the provision of licensing services without territorial limit.⁹ The desire of owners of music, whether they be owners of the underlying composition or of the master recording, is to gain the greatest access to the market for their works. It is, similarly, the desire of the developers of online services to have access to those works. However, several collecting societies have been more motivated by the defence of their respective national monopolies than meeting the needs of rights holders, on the one hand, and users of music, on the other. Competition among collecting societies will lead to more effective representation of rights holders and more flexible licensing for users.¹⁰

EMI has experience in this respect as it was the first music publisher to license its songs on a pan-European basis. Working with GEMA (the German collecting society) and MCPS-PRS (the UK collecting societies), EMI Music Publishing created CELAS to bring together in one place all of its digital rights and license them on a pan-European basis.¹¹ CELAS' mission is to create a flexible way of licensing and responding to the shifting requirements of online services. The business models online are not the same as they are in the terrestrial world, and online licensing needs to reflect that. In other words, the competitive marketplace should set the terms for licensing in the online world, not the precedents of the past.

While the CELAS initiative has encountered resistance from a number of national collecting societies, it is a functioning example of how the existing legal framework can be applied with a view to overcoming the problems inherent in the traditional system of licensing in the EU. It shows how market players, given the opportunity to do so freely, are seeking to develop solutions that can effectively overcome the existing problems. Other music publishers and rights managers are following suit.¹² CELAS is just one way of doing

⁹ See Commission Recommendation, at para. 3.

¹⁰ See Commission Study, at section 7.1.

¹¹ See : www.celas.eu.

¹² For example: Universal Music Publishing Group and the French collecting society SACEM have entered into an agreement for a joint framework for the licensing of their digital rights in Europe (see: press release dated 28 January 2008, at www.sacem.fr);

things – there are other business models to achieve the same objective of promoting more efficient licensing of online rights. It is too early to predict which of these business models will be the most successful. What is most important in this emerging market, however, is that these initiatives are given a genuine opportunity to be tested in a competitive environment.

Towards a blueprint for a truly pan-European market in digital rights

There are great advantages in breaking the national collecting societies' monopolies and building a more flexible structure. It is true that collecting societies have played – and continue to play – an important role in a number of areas, where proximity is important. But this should not lead to sticking with the status quo. Under the traditional system of collective rights management in the EU, the rights of composers have not been effectively licensed for digital applications. This has resulted in a very significant loss of revenues and contributed to a proliferation of digital piracy.

What system would be best suited to maximise the opportunities offered by the borderless online world and create a truly pan-European market? EMI considers that the following elements should be taken into account when designing a blueprint for such a system:

- The single most important issue for users is being sure that they can bring together efficiently all the rights they need. Rights in songs can be spread among a number of writers and their publishers, so this is not a trivial issue. Rights holders and users need an efficient and transparent meeting place or exchange. Based upon the existing data held by the societies and publishers, the predicate of such an exchange already exists. Technology can offer an efficient and practical solution to what has historically been an opaque barrier protecting the collecting societies' national monopolies.
- Further, any system must continue to create incentives for rights holders to promote cultural diversity, which is the creative engine of the music business.
- While the current US model has its flaws, and should therefore not be imported into the EU as a blueprint for the future, there are some lessons that can be learned from it. Indeed, US online revenues remain significantly higher than those achieved in the EU, where the potential of online is not fully reached.¹³ What has made this possible is the interaction between the rights holders and potential licensees to construct licensing

Warner Chappell has appointed several collecting societies to grant pan-European online licenses (see: press releases of 30 January and 25 June 2008, at www.wmg.com); and Sony/ATV Music Publishing has entered into a pan-European licensing agreement with GEMA (see: press release of 16 June 2008, at www.sonyatv.com).

¹³ In 2004, US online revenues were almost eight times higher than those achieved in Western Europe. See; Commission Study, at section 1.1.

regimes that are more reflective of the commercial requirements of the new services.

- In a true single market, the representation of pan-European rights would involve consolidation into a smaller number of competitive and efficient rights managers, such as collecting societies. This should be encouraged. However, new barriers to those who wish to represent pan-European rights whether they be societies or other organizations should not be erected. Consolidation should take place to create a more efficient market place, not to create new monopolies.
- Importantly and fundamentally, measures should be adopted to make the protection of copyright in the EU more effective. All illegitimate services should be eradicated. A proper and robust market cannot be populated by pirates, and it is the responsibility of everyone who benefits from this market to close off the access of pirates.

In sum, the experience of the music industry has shown that the digital world must be embraced and not shunned. While existing business models will continue to be undermined by technological developments, fighting change is far too dangerous. Resistance to building new models and approaches only speeds the demise of the old models, and relying on the old assumptions and metrics only leads the industry in the wrong direction. Regulators too should support new approaches and ensure that, like the industry, the regulatory regimes and institutions also adapt. Finally, and perhaps most importantly, it is the responsibility of both the industry and the regulators to deliver to consumers what they want, in a way that protects them from abuse and encourages investment and innovation.

7 October 2008

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