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Scuffling for a Slice of the Ringtone Pie: Evaluating Legal and Business Approaches to Copyright Clearance Issues

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Vanderbilt University Law School

Scuffling for a Slice of the Ringtone Pie: Evaluating Legal and Business Approaches to Copyright Clearance Issues

*Carmen Kate Yuen**

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A cell phone goes off, but instead of “Brring,” you hear the disco swirls of ABBA’s “Money, Money, Money.” The tune is rather revealing about the potential of the U.S. ringtone market. Consumers are enjoying an increased selection of MP3-quality ringtones, but the music industry is grappling with a host of legal complications. The new ringtone format is unprecedented, and copyright law offers little clarification on which royalties are due to whom. As a result, labels, publishers, ringtone companies and performing rights organizations are avoiding litigation, and negotiating innovative deals instead. Are private business solutions enough to resolve the ringtone issues? How can the Copyright Act stay pertinent to new digital media?

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I. THE RISE OF THE MASTER RINGTONE

Mobile ringtones have evolved since the late twentieth century. The first ringtones were MIDI files that played single tones in succession; a monophonic recreation of Blondie's "Call Me" would simply consist of the melody notes. When polyphonic ringtones developed, multiple tones could be played at the same time, creating harmony and counterpoint. The latest rings are known as truetones, puretones, songtones, or master ringtones.¹ These are usually MP3s and consist of actual song clips—now you get thirty seconds of the Blondie hit with Deborah Harry on vocals. Mobile companies are also offering ringbacks, which are song snippets that callers hear, in lieu of a buzzing tone, while they wait for the recipient to pick up the phone. A master ringtone can also be a spoken line or specially-recorded ditty.

In the United States, ringtones are now the third most popular wireless application after talk and text-messaging.² Research group IDC predicts that ringtones will generate \$600 million in the U.S. in 2005, with master ringtones accounting for fifty-one percent of the market.³ By 2008, the total market will grow to \$1.5 billion, with masters making up sixty-five percent.⁴ The slumping music industry is looking to ringtones as a booming source of revenues.⁵ Ringtones sell for almost three times as much as a legally downloaded song,⁶ and can serve as a vehicle for promoting new releases.

II. COPYRIGHT CLEARANCE ISSUES

The advent of master ringtones has initiated a set of rights clearance issues. The confusion chiefly stems from the two distinct copyrights embodied in a sound recording. The musical composition copyright owner (MCCO) has the copyright in the underlying song, which consists of the music and lyrics.⁷ Typically, the MCCO is

1. See Antony Bruno, *Content Aggregators Feel The Squeeze*, BILLBOARD, Mar. 5, 2005. There is presently no standard name for these ringtones, although "master ringtone" is frequently used.

2. Jason Fry, *The Ringtone Riddle*, WALL ST. J., Nov. 21, 2005, available at http://online.wsj.com/public/article/SB113199653761196701-dj6iAi9UQT4i5gEDwwscCoaKX8_20061120.html?mod=blogs.

3. Bruno, *supra* note 1.

4. *Id.*

5. See generally *id.*; Fry, *supra* note 2.

6. See Fry, *supra* note 2.

7. See U.S. COPYRIGHT OFFICE, CIRCULAR 56A: COPYRIGHT REGISTRATION OF MUSICAL COMPOSITIONS AND SOUND RECORDINGS (Dec. 2004), available at <http://www.copyright.gov/circs/circ56a.html>.

represented by a publisher, and the royalties are split 50/50.⁸ In contrast, the sound recording copyright owner (SRCO) has the copyright in the actual recording of the composition, consisting of the “fixation of a series of musical, spoken, or other sounds,”⁹ including the artist’s interpretation and the creative efforts of the producer, sound engineers and background musicians. The SRCO is usually the music label because in most record contracts, performers sign away ownership of the sound recording copyright.

Since monophonic and polyphonic ringtones are digital recreations of a song, ringtone aggregators only require a “mechanical license” from the MCCO.¹⁰ Most aggregators pay the MCCO either a royalty of twelve cents per ringtone, or ten percent of the retail price, whichever is greater.¹¹ The owner of a copyrighted musical work has the exclusive right to perform it publicly,¹² so ringtone companies also pay performing rights organizations (PROs) a small licensing royalty. Master ringtones, however, are a shortened version of the actual sound recording. Thus, in addition to paying the MCCO and PRO, ringtone companies must also license the sound recording.¹³ Record labels are accustomed to receiving forty to fifty percent of gross revenues from digital music sales, and insist on a similar cut for master ringtones.¹⁴

With labels cashing in on ringtones, there is less profit to divide. Ringtone companies are trying to pay the minimum royalties, while labels, publishers, and PROs are fighting for the largest possible percentage.¹⁵ To resolve these competing agendas, the parties may turn to litigation or negotiations. The following two sections examine the effectiveness of these strategies.

8. Joshua Kaufman, *Legal Tones*, LICENSE!, Nov. 1, 2005, available at <http://www.licensemag.com/licensemag/article/articleDetail.jsp?id=193621>.

9. 17 U.S.C. § 101 (2000) (defining the term “sound recordings”).

10. See Kaufman, *supra* note 8.

11. Mario F. Gonzalez, *Are Musical Compositions Subject to Compulsory Licensing for Ringtones?*, 12 UCLA ENT. L. REV. 11, 13 (2004).

12. See 17 U.S.C. § 106; discussion *infra* Parts 3.C., 4.A.

13. See *id.* § 106(6) (sound recording copyright owner has the exclusive rights “to perform the copyrighted work publicly by means of a digital audio transmission”).

14. Eriq Gardner, *Shake Rattle and R-R-Ring*, CORPORATE COUNSEL, July 18, 2005, available at <http://www.law.com/jsp/cc/PubArticleCC.jsp?id=1121418316067>.

15. See *id.*

III. LEGAL ARGUMENTS

A. Ringtone Aggregators and Record Labels

The primary dispute over royalties concerns the amount that the MCCO is owed. Publishers are accustomed to receiving ten percent of the retail price of ringtones, and since a master ringtone retails for \$2.49 to \$2.99, a publisher would be entitled to 24.9 to 29.9 cents per sale.¹⁶ However, record labels and ringtone companies interpret section 115 of the Copyright Act to read that publishers should only receive the “mechanical royalty,” or 8.5 cents per master ringtone.¹⁷ According to section 115(a)(1), once a composition has been recorded and commercially released, anyone who wishes to make digital phonorecord deliveries to the public for private use can obtain a compulsory license.¹⁸ The Digital Performance Rights in Sound Recordings Act of 1995 (DPRA) amended section 115 to clarify that the compulsory license applies to “digital phonorecord deliveries.”¹⁹ Ringtone companies and labels therefore argue that the minimum statutory rate applies to master ringtones because they are “digital phonorecord deliveries.” Copyright law, however, provides little clarification because the provisions are not tailored to the new ringtone format. A “digital phonorecord delivery” is defined as a “digital transmission of a sound recording which results in a specifically identifiable reproduction”²⁰ Master ringtones may meet this definition, as they are digital files that may be downloaded and copied. However, section 101 defines “phonorecords” as “*material objects* in which sounds . . . are fixed . . . and from which the sounds can be perceived, reproduced, or otherwise communicated”²¹ In the wireless context, it is difficult to determine what the “material object” is. The language of section 105 and section 101 is ambiguous

16. Gonzalez, *supra* note 11, at 14-15.

17. See *id.* at 14-17; see also Patents, Trademarks, & Copyrights, 22 C.F.R. § 255.3(l) (2006) (providing that from January 1, 2004 to December 31, 2006, the minimum statutory rate is 8.5 cents per digital phonorecord delivery of a musical recording under five minutes long); *c.f.* Mechanical and Digital Phonorecord Delivery Rate Adjustment Proceeding, 64 Fed. Reg. 6221 (Feb. 9, 1999) (to be codified at 37 C.F.R. pt. 255) (stating that mechanical royalty rates for digital phonorecord deliveries are the same as for physical records).

18. 17 U.S.C. § 115(a)(1); see also *id.* § 115(c)(3) (stating that a compulsory license includes the right to distribute works by means of a digital transmission, which constitutes a digital phonorecord delivery).

19. S. REP. NO. 104-128, at 36-37 (1995).

20. 17 U.S.C. § 115(d).

21. *Id.* § 101 (emphasis added).

when applied to master ringtones, making it difficult to present a strong legal argument for the compulsory rate.

B. Publishers

Music publishers take the position that section 115 does not allow a compulsory mechanical license for ringtones. In reference to section 101, publishers contend that ringtones are not material objects, and therefore may not be classified as “digital phonorecord deliveries.”²² Publishers also appeal to section 115(a), which states that under a compulsory license, a licensee cannot “change the basic melody or fundamental character of the work”²³ If a master ringtone is a new arrangement of the underlying musical composition, then labels and aggregators may not pay the minimum licensing rate. However, it is debatable whether a short clip of a sound recording constitutes a change in the arrangement. Again, it is unclear where ringtones fall under the provisions of the Copyright Act.

C. Performing Rights Organizations (PROs)

PROs such as ASCAP, BMI, and SESAC monitor public performances, and collect and distribute royalties to the composers and publishers they represent. The PROs claim that when a cell phone rings, the reproduction of the composition constitutes a public performance, and they insist that royalties be anted up.²⁴ Pursuant to Section 101 of the Copyright Act, a “public performance” means “to transmit or otherwise communicate a performance . . . to the public, by means of any device or process,” without regard to the spatial or temporal conditions of the reception.²⁵ For example, broadcasting a song in a restaurant is a public performance. Mobile phones, however, may ring in public or in private, and if they are set on “vibrate” or “silent,” they may not sound off at all. If a master ringtone plays for a few seconds in a McDonald’s, is that a public performance of the composition? Once more, the terms of the Copyright Act provide little guidance in resolving the royalty issues associated with master ringtones.

22. See *id.* § 115(d) (defining “digital phonorecord delivery”).

23. *Id.* § 115(a)(2).

24. Eriq Gardner, *Ringtones Breed Tension Within Music Industry*, ENT. L. & FIN. (ALM, New York, N.Y.), Nov. 2005, at 3.

25. 17 U.S.C. § 101.

IV. BUSINESS INNOVATIONS

Since current copyright law is ambiguous in its application to ringtones, the music industry is favoring negotiation over litigation. The parties are relying on three innovative strategies to circumvent the disputes.

A. *Pioneering Contracts and Royalty Rates*

Publishers are stipulating that the minimum statutory rate does not apply to ringtones. The Harry Fox Agency (HFA), which handles mechanical licensing and collects royalties for most publishers, takes the position that “[digital phonorecord delivery] licenses issued under section 115 of the Copyright Act do not extend to the making or distribution of [ringtones].”²⁶ Licensees must request and obtain a separate license from the HFA for each song that they wish to offer as a ringtone.²⁷ The “HFA collects 10 to 12 cents per download, plus an initial ‘fixation’ fee of up to \$50 to include the composition in a ringtone service.”²⁸

The PROs have issued notices stating that ringtones constitute public performances and are subject to licensing fees.²⁹ ASCAP created a specific new media license for authorizing ringtones and ringbacks.³⁰ Licensees pay either “2% of the revenue attributable to ringtones, 1.5 cents per ringtone, or a quarterly minimum fee of \$500, whichever is greatest.”³¹ Other PROs set different rates: “BMI collects 2.5 percent of [the] gross,” and “SESAC fees vary depending on the number of ringtones sold.”³²

Since old recording contracts do not mention ringtones, labels are re-negotiating with artists over mobile content rights.³³ The labels seek to market and bundle a wide range of mobile content.³⁴ To increase their share of the profits, they are categorizing master ringtones as a “sale,” which triggers the ten to twenty percent artist royalty rate, as opposed to a “license,” which would generate a rate of

26. HFA, Ringtones FAQ, <http://www.harryfox.com/public/infoFAQRingtones.jsp> (last visited Apr. 14, 2006).

27. *Id.*

28. Scott Banerjee, *Ringtone Rumble Brewing*, BILLBOARD, May 22, 2004.

29. *See* Gardner, *supra* note 14.

30. ASCAP, ASCAP Experimental License Agreement for Wireless Music Services - Release 3.0., <http://www.ascap.com/weblicense/release3.0.pdf> (last visited Apr. 14, 2006).

31. Gardner, *supra* note 14.

32. Banerjee, *supra* note 28.

33. Gardner, *supra* note 14.

34. *See* Bruno, *supra* note 1.

forty to fifty percent.³⁵ “Some artists[, however,] have argued successfully for the latter.”³⁶

B. Comprehensive, Short-Term Business Agreements

Ringtone companies, publishers, PROs, and labels are setting aside section 115 arguments and making comprehensive licensing agreements. Blue Frog Mobile has acquired ringtone publishing rights from all the major publishers: Universal, BMG, Sony/ATV, EMI, Warner/Chappell, and Zomba.³⁷ Aggregators and PROs are also signing agreements; Zingy may now “distribute ringtone versions of any of the millions of songs [BMI represents.]”³⁸ Furthermore, labels and publishers are setting defined rates for mechanical royalties, which are generally ten to fifteen percent of the gross or a minimum of ten cents per master ringtone. The HFA sealed a licensing deal for master ringtones and ringbacks with EMI Music North America,³⁹ Sony BMG set ringtone clearance guidelines with EMI Publishing and Warner/Chappell,⁴⁰ and “Warner Music Group . . . brokered an . . . agreement between its recorded-music and [publishing divisions,] . . . le[adding] to the release of over 2,000 tracks for ringback distribution.”⁴¹ Finally, labels are making pacts with mobile companies; Ericsson has agreed to distribute ringback tones from EMI Music North America’s catalog.⁴² These business agreements are generally short-term and leave rates for other emerging technologies, such as video, open for later determination.

35. See Susan Butler, *Legal Matters: Lawyers Predict More Opportunities In 2005*, BILLBOARD, Jan. 8, 2005; Antony Bruno, *Video Booms Online—But For Whom?*, BILLBOARD, Oct. 29, 2005.

36. Bruno, *supra* note 35.

37. See Blue Frog Mobile, About Blue Frog Mobile, <http://corp.bluefrogmobile.com/htmlcorp/news.php> (last visited Apr. 14, 2006).

38. Press Release, BMI, Zingy Signs Comprehensive Ringtone Licensing Agreement with BMI (Oct. 30, 2001), available at <http://bmi.com/news/200110/20011030a.asp>.

39. Susan Butler, *The Publishers’ Place: A Happy Reminder: It’s All About A Song*, BILLBOARD, Oct. 22, 2005.

40. Brian Garrity, *New Sony BMG Deal*, BILLBOARD, Apr. 30, 2005.

41. Brian Garrity, *EMI Pub, Sony BMG Forge Digital Licensing Pact*, BILLBOARD, Dec. 25, 2004.

42. Press Release, Ericsson, Ericsson Signs North American Ringback Tone Agreement with EMI Music (Sept. 28, 2005), available at <http://www.ericsson.com/press/20050928-175505.html>.

C. Investing in the Future of Ringtones

Record companies are taking steps to cash in on the burgeoning wireless sector. Research company Strategy Analytics predicts that these conglomerates will buy ringtone providers, although they will “continue to license their music to independent ringtone producers.”⁴³ Labels are likely to set up ringtone studios for recording original ringtones. Sony BMG has set aggressive targets for increasing mobile revenues and using ringtones as a marketing tool.⁴⁴ The company has launched a website to sell downloads, and will be introducing new services such as video downloads.⁴⁵

V. BUSINESS SOLUTIONS ARE PROMISING BUT INSUFFICIENT

Business agreements are taking precedence over litigation because the language of copyright law is unclear with regard to ringtone transmission rights. In the short-term, the music industry is bypassing section 115 arguments in favor of experimentation with new business models. These deals are a promising step, as they simplify the licensing process and provide the flexibility to test this new economy on consumers. These agreements will enable the music industry to capitalize on the demand for master ringtones and ringbacks, and may create a paradigm for digital licensing.

However, the private market alone cannot resolve statutory license scope issues in the long view. First, business deals and industry standards do not pertain to all parties in the musical economy. The HFA, for instance, licenses only about sixty-five percent of available music, meaning that thirty-five percent of publishers are unaffected by the HFA’s stand on section 115.⁴⁶ Second, the terms of these agreements do not set legal precedent. The parties’ interpretation of section 115 “is not binding on the Copyright Office or the courts. It merely represents their mutual understanding of the

43. Frances Gleeson, Labels to Delve Deeper Into Ringtones, *ElectricNews.net*, July 31, 2003, <http://www.enn.ie/print.html?code=9370275>.

44. Press Release, Minick, Minick Signs Agreement with Sony BMG to Power Mobile Multimedia Downloads, (May 18, 2005), *available at* http://www.minick.net/press_sonybmg.html.

45. *Id.*

46. *Section 115 of the Copyright Act: In Need of an Update: Hearing before the Subcommittee on Courts, the Internet, and Intellectual Property of the H. Comm. on the Judiciary*, 108th Cong., 2d Sess. 20 (Mar. 11, 2004) [hereinafter *Section 115 Hearing*] (testimony of Jonathan Potter, Executive Director, Digital Media Association), *available at* <http://judiciary.house.gov/Oversight.aspx?ID=53> (follow “Hearing PDF (Serial No. 75)” hyperlink).

scope of the section 115 license as a term of their privately negotiated license.”⁴⁷ Third, the terms of these business agreements may not be fair for all parties. Those with greater bargaining power can offer more or fewer rights in accordance with their own institutional interests. Record companies, for example, may reserve an artist’s promotional rights as well as recording rights.⁴⁸ As a result, the artist may be barred from creating exclusive spoken content and making lucrative deals with ringtone aggregators.⁴⁹

VI. UPDATED COPYRIGHT LEGISLATION IS URGENTLY NEEDED

Legislative action is necessary to create a workable long-term solution to the problems associated with ringtones. Amending section 115 is a daunting task because emerging mobile and digital technologies will inevitably resist classification under the Copyright Act. However, a strong legal foundation is required to ensure that the rights of artists, writers, and music industry players are not compromised. Congress must immediately streamline and clarify the sound recording provisions of Title 17 to address new licensing issues. In a 2004 congressional hearing on updating section 115, Marybeth Peters, Register of Copyrights at the U.S. Copyright Office, made several legislative recommendations with respect to the scope of the section 115 license.⁵⁰ First, she proposed eliminating the statutory license and leaving rights licensing to the marketplace, most likely by means of collective administration.⁵¹ Second, she suggested amending section 115 to re-define “digital phonorecord deliveries” and clarify which media formats fall within the scope of the compulsory license.⁵² Congress must consider Peter’s section 115 proposals and push to amend the Copyright Act, with particular attention to the definitions of “phonorecords” and “public performances.” Updated legislation will not only help the music industry, but will also benefit consumers and help curb piracy. To attain promising long-term solutions, Congress must work closely with the music industry in evaluating legislative proposals.

47. *Id.*, at 12 (testimony of Marybeth Peters, Register of Copyrights, US Copyright Office).

48. See Susan Butler, *Legal Matters: Who Owns Rights To Artist’s Speaking Voice?*, BILLBOARD, Oct. 16, 2004.

49. *See id.*

50. *See Section 115 Hearing, supra* note 46, at 5-17.

51. *Id.* at 13.

52. *Id.* at 14.

VII. CONCLUSION

Technologies for delivering music to consumers will continue to develop, and Congress and the music industry will face new challenges to the interpretation and application of section 115. Modernizing relevant provisions of the Copyright Act will remain difficult, as wireless content will soon include video ringtones, full song playback, and “call soundtracks,” which allow users to listen to background music while they talk. If the current legal issues are not immediately addressed, the music industry will be unable to benefit from the profitable, dynamic mobile market as it develops.