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Attached is an ABA article we wrote which sets forth in detail the history and current status of U.S. Performance, Mechanical and Artist digital royalties. May be of interest in your Decree review. We also had an ABA Entertainment and Sports Lawyer article on Direct Licensing entitled "Performing Rights Licensing in the U.S.: a World of Multiple Choices, Considerations and Results". It may also be of interest. Sincerely Todd Brabec. Governing Committee Member ABA Forum on the Entertainment and Sports Industries.

**Online Music Licensing: From PROs, AOL and MobiTv to SoundExchange,
Pandora and the CRB
(American Bar Association Forum on the Entertainment and Sports
Industries/Entertainment and Sports Lawyer)**

By: Todd Brabec and Jeffrey Brabec

Music licensing in the digital/online space has been, from inception, in a continuing state of evolution as to what is actually licensable, who is entitled to negotiate and collect license fees, how will royalties be distributed once collected and what is the value of music in all of the new configurations and business models. The primary rights involved in these discussions are the mechanical right and the performance right(songwriters, composers and music publishers) and the sound recording performance right(recording artists and record companies). Though there remain some major unresolved issues, particularly in the musical composition performance area, overall ground rules as well as precedents appear to be taking hold creating a more stable environment for creators, music business entities and music users.

Most countries of the world exist in a world of 2 copyrights in music transactions-the copyright governing the underlying musical composition (the song) and the copyright governing the sound recording (the record). The scope of rights involved in each of these separate copyrights are primarily the jurisdiction of national legislatures with the meaning and scope of these rights normally handled by each countries judiciary- whether it be courts, tribunals, copyright boards or other designated bodies. Negotiated voluntary agreements between the users of music (webcasters, broadcast television, cable, radio, satellite, etc.) and large organizations organized to negotiate and collect for multiple copyright owners (performing right organizations, mechanical right organizations, sound recording organizations, etc.) or individual copyright owners themselves play a major role in deciding what the license fees should be as well as what the scope of the license is in any media.

In situations where voluntary license agreements cannot be reached by the parties, federal rate courts (e.g. ASCAP and BMI in the U.S.), Copyright Tribunals (e.g. PRS for Music in the U.K., APRA and AMCOS in Australia and New Zealand) or Copyright Boards (SOCAN, CMRRA and SODRAC in Canada; songwriters, music publishers, record labels, websites, artists, etc. in the U.S.) decide the issues and determine rates.

At the time the Internet was just taking hold by consumers, the music business throughout the world had a long history of established rules and negotiations governing licensing and the establishment of rates. Though many of these license negotiations were restricted in the sense of territory and term, among other items, many were not (i.e. grant of the worldwide distribution right in feature film licenses).

In the area of the song, integrating the internet into licenses by copyright owners (music publishers normally) was significantly easier to accomplish than integrating master

recordings. In the U.S., Copyright Royalty Judges already had a history of dealing with the setting of rates in many areas and the 2008 CRB hearing regarding the "mechanical rate", showed that the setting of rates in the online world was not only doable but also a reality.

In October of 2008, U.S. Copyright Royalty Judges, "In the Matter of Mechanical and Digital Phonorecord Delivery Rate Determination Proceeding," set the physical and download statutory license rate to be paid to songwriters and music publishers for the period 2008-2012 at the larger of 9.1 cents or 1.75 cents per minute of playing time with the ringtone rate at 24 cents. In addition, a late payment fee of 1.5% per month was put into effect. Both the ringtone rate as well as the late payment fee were appealed with a June, 2010 decision by the U.S. Court of Appeals for the D.C. Circuit affirming both. The Royalty Judge proceeding decision was interesting as it incorporated a private settlement between the parties regarding the rates for limited downloads and interactive streaming (on demand streams). This settlement took into account a service's revenue, applicable service type minimums, PRO royalties (ASCAP, BMI, and SESAC) and a per subscriber fee to arrive at a per work royalty allocation.

In 2012, the NMPA, RIAA and DIMA entered into an industry wide agreement for the period through 2017 for new rates regarding the 2008 configurations as well as new configurations which came into existence subsequent to the 2008 agreement. The agreement was submitted to the Copyright Royalty Judges who approved the new deal effective January 1, 2014. The new royalty bearing categories for music publishers, songwriters, composers and lyricists are Paid Locker Services, Purchased Content Lockers, Limited Offerings, Mixed Service Bundles and Music Bundles. The rates for the new categories involve the greater of a percentage of service revenue, total content costs (payments to record companies for sound recording rights) and, in the case of limited offerings, a per subscriber figure. The 2008 category rates and formulas for physical product sales and downloads, limited downloads, interactive streaming and ringtones remained the same under the new agreement.

On the record side, there has not been a long history of collective licensing efforts. A copyright for sound recordings came into effect in 1972 in the U.S. (long after the 1909 Copyright Law and exclusive rights for musical compositions) with the 1st recognition of a performance right in sound recordings coming in 1995 and 1998 via the Digital Performance Right in Sound Recording Act and the Digital Millennium Copyright Act- and then the right was a limited one applying primarily to websites, satellites and cable and not to terrestrial broadcasting. The industry's approach for many years was to sue infringers in the online world- an approach generating among consumers not the best of publicity or results. The labels not only were slow to appreciate the fact that the physical world of sales was quickly disappearing but also did not have the history of different types of licensing negotiations and alternatives that the "song" copyright community had experienced over many years.

In recent years, U.S. Copyright Royalty Board decisions have been of help in determining the online value of sound recordings. The webcaster decisions alone have established industry wide fees and rates for non-interactive websites as well as a compulsory license in the field. Rates are either per song/per listener or a percentage of revenue or a percentage of expenses coupled with minimums. For the period 2011-2015, the Copyright Royalty Board rates for FCC broadcaster simulcasts, commercial webcasters and non-commercial and non-commercial educational webcasters are either a "per performance" rate with minimums per station or channel or a minimum only depending on the number of aggregate tuning hours streamed.

In addition to the CRB rates, SoundExchange, the sole entity designated by the Librarian of Congress and the Copyright Royalty Board to collect and administer the royalties due from non-interactive webcasting, digital cable and satellite transmissions, and satellite audio services, was given the authority by Congress via the Webcaster Settlement Acts of 2008 and 2009 to negotiate agreements separate from those set by the CRB giving many licensees a choice of rate structures to choose from. By choosing the SoundExchange rates, which run through 2015, one is precluded from choosing any of the CRB set rates. Recent SoundExchange agreements include Sirius XM Radio, College Broadcasters, the Corporation for Public Broadcasting, the National Association of Broadcasters and certain "Pureplay" webcasters, among others.

SoundExchange distributes the royalties it receives (650 million dollars in statutory royalties in 2013 plus 6 million from foreign collection societies) 50% to sound recording copyright owners, 45% to featured artists and 2.5% each to non-featured musicians and non-featured vocalists (this latter 5% Digital Performance Royalties Fund is administered by the AF of M and AFTRA.)

On the interactive side (user selects the music they hear), individual negotiations prevail as sites must negotiate with the sound recording copyright owner as to what the fees should be. Some examples of the progress in this area are deals involving a percentage of gross revenue from subscribers and advertisers or a percentage of a net figure (gross minus certain expenses) with the resulting figure shared by the label with artists either on a contract royalty percentage basis or a 50/50 license split. Payments to the labels are based on their pro-rata share of activity on each site or by each licensed entity.

In the world of the musical composition performance right in the United States (ASCAP, BMI and SESAC), negotiated industry agreements have been the norm with federal rate court alternatives (mandated by Consent Decrees entered into in 1941 with the government) coming into play only when ASCAP or BMI could not come to an agreement with a music user as to "what a reasonable license fee should be". The Decree also allows any party to apply to the Court (whether or not there were any prior negotiations) and upon such application to be able to perform music for fees to be determined later.

This rate court option has been in effect since 1950 with ASCAP and 1994 with BMI and represents a primary way to resolve disputes and set collective licensing rates when the parties cannot reach an agreement. SESAC, the smallest of the 3 U.S. performance

right licensing organizations, is not under a Consent Decree with the government nor does it have a rate court alternative; issues which are currently being discussed as part of a Southern District of New York Sherman Act antitrust action brought by a class of local television commercial broadcast stations entitled Meredith Corporation v. SESAC. Another case brought by radio broadcasters involves some of the same issues.

In the online world of music licensing, the ASCAP rate court (Southern District Court in New York) has been instrumental in deciding what the license fees should be in the online world as well as what is actually licensable by U.S. collective licensing organizations. In recent interim and final decisions involving music use by AOL, Yahoo, Real Networks, AT&T, YouTube, Verizon and others, a percentage of revenue formula has been applied taking into account, among other factors, the amount of time music is performed versus the amount of total time spent on the site for all reasons- a business unit's revenue adjusted by a music use adjustment factor multiplied by a court set percentage figure (2.5% in the initial decision).

An important issue in the ASCAP rate court cases was whether a retail wireless communications company required a public performance license for musical compositions because it provides ringtones to its customers (In Re Application of Cellco Partnerships, D/B/A Verizon Wireless) and whether the downloading of a digital file embodying a song constituted a public performance within the meaning of the U.S. Copyright Act (17 USC Section 101) (In The Matter of the Application of AOL, Real Networks and Yahoo for the Determination of Reasonable License Fees).

Though the reasoning for the two separate decisions was somewhat different, both decisions by two separate Southern District Court of New York federal judges ruled against the existence of a performance right in each situation. ASCAP filed a petition for certiorari with the United States Supreme Court on the issue of whether a digital download of a music file constitutes a public performance under the Copyright Act but the Court refused to entertain the case. There was some language in the 2009 AOL/Yahoo/Real Networks decision and final order which left open the possibility of a performance right in certain situations but the current state of affairs in the U.S. basically denies a performance right both in a download and a ringtone.

The court did recognize the fact that a mechanical right is involved in a download of a song and in a ringtone and referred to the Copyright Royalty Board 9.1¢ writer / publisher song download rate and 24¢ ringtone rate as appropriate compensation for these type of uses. These decisions did not deal with the issue of ringbacks as there is not a download involved. Accordingly, ringbacks are licensable by performing right organizations.

The ramifications of the "no performance right in a download" ruling in these rate court licensing cases goes far beyond U.S. borders as practically every other major country of the world recognizes a performance right in a download which puts U.S. court decisions 100% contrary to the laws and practices of other country jurisdictions. In many of these countries, the separate mechanical right and performing right (referred to as the

reproduction and communication right in some countries) are many times combined in a single joint license which provides the user all of the rights it needs without having to argue the distinctions between the separate rights of copyright.

For example, PRS for Music in the U.K. issues gross revenue combined performance and mechanical licenses for music downloads (8%), music on demand services (10.5%), webcasts (6.5%), interactive webcasts (8%), and single artist webcasts (10.5%) among others. These licenses also include minimums. In Canada, pursuant to a Copyright Board decision, the total value of the bundle of rights (communication and reproduction) is 12.2% of the price paid by the consumer and or subscribers. The amounts are allocated between SOCAN (the performance rights society) and CSI, a joint venture of CMRRA and SODRAC (the 2 mechanical right societies) and are divided between the societies depending on whether the activity was a permanent download, a limited download, or on demand streaming. A 2012 Supreme Court of Canada decision (*Entertainment Software Association v. SOCAN/CMRRA/SODRAC*) though overruled the Copyright Royalty Board of Canada and decided that there was no performance right (communication right) in a download. As this decision only involved downloads, streaming situations still involve the licensing of both rights.

An additional important issue and ruling came via the AT&T Wireless f/k/a Cingular Wireless ASCAP rate court litigation to determine reasonable fees for a blanket license for the public performance of copyrighted music via wireless and internet transmissions by a cellular telephone communications provider. AT&T had moved for a summary judgement on the issue of whether ringtones and ringback tones constituted fair use within the meaning of the U.S Copyright Act, 17 U.S.C, 101.

In support of its position against previews as a “fair use”, ASCAP set forth numerous examples of other 3rd parties that make previews of music available on the internet. These included production music libraries, which allow potential users to search their databases via streams, samples or previews. Also, major music publishers often streamed samples of their catalogue to encourage synch licenses and songwriters and composers many times make their works available on their individual websites for promotional purposes. In addition ASCAP also described the demand for the licensing of “short forms of music” where “in many areas of music licensing, the licensee will specifically seek a license for a limited duration excerpt and that in agreements across different areas of the music business, it is often standard industry practice to expressly grant the right to make limited use of samples or previews of longer musical compositions for promotional purposes.”

The Court reviewed the factors to be considered as to the use made of a work and concluded that the use of previews was not transformative, that the use is commercial and that “traditional and reasonable markets existed for the license of preview performances and other short segments of copyrighted music. Therefore, the court ruled that previews do not constitute fair use and denied the motion in its entirety. The resolution of this issue was important as ringback and ringtone previews were taken into account in both the 2010 AT&T Mobility and 2011 Verizon Wireless ASCAP settlements where a rate of 2% of the price for all ringbacks sold was agreed upon. Excluded were

tones directly licensed, or acquired from others who already had a license or where record companies had acquired the performance right.

In May of 2010, a decision was rendered in the ASCAP rate court case involving MobiTv. In May of 2008, ASCAP applied to the Court to set a reasonable rate pursuant to Mobi's license application to ASCAP with a bench trial being held in April of 2009. The issue involved what is a reasonable fee for the delivery of television and audio programming to mobile telephones. The court determined in this case that a reasonable fee for a "through to the audience" license for Mobi for the years 2003 through 2011 was a revenue based fee multiplied by 4 specific percentage numbers based upon the type of content. This fee structure was a combination of the 2007 AOL / RealNetworks / Yahoo rate court formula (January, 2009 final order) of 2.5%, the ASCAP/Music Choice 2.5% of gross revenues agreement and the ASCAP 1990's post Turner litigation settlements regarding the cable industry where the percentage of revenue fees were based on the music intensity of the programming.

Specifically, the court ruled "the revenue base upon which the licensing fee will be calculated is (1) for the content that Mobi licenses from content providers, aggregates, and conveys to wireless carriers, the amounts that Mobi pays to the cable television networks or other providers to license the content, plus any revenue from advertising Mobi inserts into that programming; and (2) for the music video channels and any other channel programmed by Mobi, the payments Mobi receives from the wireless carriers for those channels, plus any revenue from advertising that Mobi inserts into that programming. The rate to be applied to that revenue base is 0.1375% for news and sports content; 0.375% for general entertainment; 0.9% for music intensive programming, to include Mobi's music video channels; and 2.5% for all-audio offerings." In October of 2010, ASCAP filed an appeal of this decision to the 2nd Circuit Court of Appeals. It is important to note that the MobiTv percentage of revenue figures (Turner/Music Choice) were subsequently agreed upon in both the AT&T Mobility (CV Service) and Verizon Wireless (V Cast and ALLtel Licensed Services) ASCAP final settlement agreements.

In September 2010, the Second Circuit Court of Appeals in the ASCAP/Real Networks, Inc./Yahoo! Inc. rate court case (AOL had previously settled with ASCAP) issued the first appellate decision in the string of online music licensing ASCAP rate court cases.

The Court affirmed that a download of a musical work does not constitute a public performance of that work and further, it vacated the District Court's assessment of fees (2.5% music use adjustment factor formula) for the ASCAP blanket license and remanded the issue for further proceedings.

As to the “download issue”, the Court concluded that there was no “contemporaneous perceptibility” necessary, in the Court’s mind, for the existence of a performance right in the transfer of a musical file.

As to the royalty rate formula, the Court of Appeals felt that the District Court “did not adequately support the reasonableness of the 2.5% royalty rate applied to music use”. The Court did not specify a particular method of developing a formula for music use revenue by the District Court in the remand but did suggest a number of considerations and approaches that might be helpful in arriving at an appropriate formula. Among them were valuing each of a services different types of music uses separately and then applying a “blended uniform rate and revisiting it periodically” as well as a variation of the BMI license utilizing multiple revenue categories apportioned into “buckets” and applying different revenue percentages to each. The latter an admittedly complicated and complex way of doing things. The Court also looked at the ASCAP/Turner agreement which involved different revenue rates based on varying music intensity as well as the 2.5% of gross revenue Music Choice/ASCAP negotiated agreement in addition to other past different media agreements by PRO’s and music users. Subsequent to this decision, the parties settled the remaining issues.

Two additional Rate Court cases, DMX and Pandora, involved not only the determination of reasonable license fees but also the role that Direct Licensing plays in the PRO licensing picture. Under the ASCAP and BMI Consent Decrees, the agreements that writers and music publishers sign with ASCAP, BMI and SESAC are non-exclusive- members and affiliates are allowed to directly license their works to a music user and bypass the PRO structures entirely.

DMX is a leading background and foreground music service provider which provides pre-programmed music for business establishments via direct broadcast satellites or on premise delivery mechanisms. DMX hired a company to assist and design a Direct Licensing program with copyright owners which eventually resulted in direct licenses representing over 7,000 catalogues including one major music publisher, Sony. DMX was requesting from ASCAP and BMI a "through to the audience" blanket license which reflected the DMX direct licenses already obtained as well as those to be negotiated in the future.

In July of 2010, the BMI Rate Court entered a final rate for the blanket license subject to adjustment of DMX's BMI performances directly licensed. In a separate decision, the ASCAP Rate Court ruled that ASCAP is required to issue to DMX a blanket license with "carve outs" for the direct licensing program. Both decisions were appealed to the 2nd Circuit Court of Appeals which in June of 2012 affirmed the Rate Court decisions. The resulting rates significantly reduced the license fees that DMX was paying to ASCAP and BMI.

Pandora is the leading Internet customized radio service and is considered a non-interactive service as opposed to an on demand/interactive service where the user chooses what they want to hear. Pandora entered into license agreements with both ASCAP and BMI in 2005 and terminated those licenses at the end of 2010 and 2012 respectively. In the case of ASCAP, Pandora applied to the Court for a through-to-the-audience blanket license for the period 2011 through 2015. In the case of BMI, Pandora filed an application for a 5 year license commencing January 1, 2013.

Based primarily on the small license fees that were awarded by the ASCAP and BMI Rate Court judges commencing with the AOL/Real Networks/Yahoo case in 2007, the 4 major music publishers, starting with EMI(later acquired by Sony), notified ASCAP and BMI that they were withdrawing their catalogues for online licensing purposes. The majors felt strongly that they could negotiate more financially acceptable online value deals than the arrangements that had been set by prior Rate Court decisions and the subsequent settlements emanating from those decisions. These online media withdrawals were accomplished by specific changes in the rules, regulations and practices of ASCAP and BMI. Upon withdrawing their works, a number of the publishers entered into direct licensing deals with Pandora. In effect creating a system whereby Pandora had licenses with ASCAP, BMI and SESAC as well as short term negotiated direct performance licenses with the major publishers. Discussions were also held between ASCAP, BMI and the major publishers with a view toward ASCAP and BMI handling the administration of the online licenses negotiated by the publishers.

In response to a Motion for Summary Judgement in September of 2013, Judge Cote, the ASCAP judge, ruled that a selective withdrawal of new media rights by publisher members could not be implemented without violating the Consent Decree and further that the ASCAP repertory subject to that license is all works in ASCAP at the time Pandora applied for a license(January 1, 2011)-not when the final license is arrived at. In short, an application for a license is treated as a license in effect and in this case no works could be removed during the period 2011 through 2015. And when works are finally removed by any publishers , those works have to removed for ALL licensing purposes, not just for online licensing.

In a similar Motion for Summary Judgement in the BMI case, Judge Stanton allowed the removal of works which occurred prior to January 1, 2013 but ruled that those works could not be licensed by BMI to any others after any existing license agreements expired. If BMI cannot offer those compositions to new media applicants, their availability does not meet the standards of the BMI decree and they cannot be held in the BMI repertory. The actual BMI Rate Court trial is set for December of 2014.

On March 14, 2014, Judge Cote issued her "determination of reasonable license fees" 136 page decision in the ASCAP/Pandora Rate Court case. The judge ruled that the appropriate fee for the years 2011-2015 was 1.85% of revenue less certain deductions. ASCAP had requested a rate of 1.85% for 2011 and 2012, 2.5% for 2013 and 3% for 2014 and 2015. Pandora had requested a rate between 1.7%(the current traditional radio rate) and 1.85%(the ASCAP form rate in effect for Pandora since 2005). Subsequent to the decision, major music publishers and ASCAP separately filed appeals.

Two of the more important issues in the Pandora Rate Court Proceedings involve the concept of the divisibility of copyrights which allow a publisher/copyright owner to make deals with various classes of users for their catalogue and the disparity in payments between artists and record companies and songwriters and music publishers for the same type of performance.

As to the latter issue, the AOL/Yahoo/Real Networks 2007 Rate Court case provided evidence of the in excess of 30 million dollars paid by these services to the major record companies over a 2 year period whereas their fees to the PROs were, in comparison, very small(the YouTube Rate Court interim ASCAP fee of \$60,000. a month is a good example of the relative size of PRO fees in this area). As to Pandora, the company expended in 2013 approximately 315 million dollars of its total revenue of 600 million dollars on Content Acquisition. Of that amount, close to 290 million went to SoundExchange for artists and record companies with all three PROS collecting a total of less than 25 million dollars for songwriters and publishers. As a point of additional reference, total 2013 limited performance right statutory royalties to SoundExchange were 650 million dollars in addition to significant record company interactive streaming payments whereas combined ASCAP, BMI and SESAC revenue for all new media uses was less than 100 million dollars.

In part because of the Pandora decisions, a major development occurred in June of 2014 when the Department of Justice announced that they would review both the ASCAP and BMI Consent Decrees "to account for changes in how music is delivered to and experienced by listeners and if so, what modifications would be appropriate". The Department allowed a 60 day period for comments from any interested party(music publishers, songwriters and composers, PROs, online service companies, music users of any nature, the general public, etc.).

It is important to note that there are numerous ASCAP, BMI, and SESAC voluntary negotiated agreements as well as settlements in the online area, including all of the aforementioned rate court cases with the exception of Pandora. These agreements include percent of music revenues as well as gross revenues, multiple revenue categories with different rates, different revenue percentages for on demand streaming, Internet radio and audio visual programming, gross revenue attributable to the service calculations, aggregate tuning hours calculations, flat fee deals, lump sum payments for past activity, different values assigned to a service's different music uses as well as minimum fees, among others. All three organizations also have standard website agreements which can be accessed via each organization's website. It should be noted that many of the ASCAP, BMI and SESAC agreements and settlements in the online world are confidential.

Where Do We Stand Now

Of the three areas of music licensing under discussion, two of the three (mechanicals and sound recordings) seem clear, with the third (performances) uncertain as to a number of important issues and practices.

In the mechanical licensing area, rates for physical product, digital downloads, ringtones, interactive streaming and limited downloads have been set through 2017 with an additional five new configurations now covered.

In the area of the limited performance right in sound recordings, CRB rates for cable, satellite and webcasters are in effect through 2015 with SoundExchange separate negotiated rates extending also through 2015. For rates commencing 2016 and beyond, a Copyright Royalty Board is currently underway(Web IV). Also, payment formulas are in effect as to distribution of royalties to record labels, featured artists and non-featured musicians and vocalists. Reciprocal agreements with foreign country collection societies are also in effect at least as to coverage afforded by the U.S. limited right(non-interactive webcasting, etc.).

A remaining open question involves whether this limited right sound recording right will be extended by legislation to United States terrestrial(traditional) radio broadcasting- a "neighboring" right in effect in most other major countries of the world. Such an extension would significantly increase artist and record company royalties both in the U.S. and in foreign countries.

The performance area of ASCAP, BMI, and SESAC though, remains in a state of flux with multiple different license fee negotiated and standard form formulas in effect in addition to rate court decisions and settlement agreements with various major players including AOL, YouTube, AT&T Mobility, Verizon Wireless, Ericsson, Spotify, Netflix and many others. Also, the current Pandora ASCAP and BMI Rate Court proceedings are not as yet final in addition to the Department of Justice reviewing the ASCAP and BMI Consent Decrees which could significantly effect licensing rates and strategies as well as significantly increasing or decreasing the complexities of licensing music.

As to Direct Performance licensing, around since at least the 1950 ASCAP Amended Consent Decree, the issue is in the forefront again as a result of the ASCAP and BMI Rate Court cases involving the background music supplier DMX as well as the online music service Pandora.

As you can see, rate courts, royalty boards, litigation, legislation, industry practice, foreign country considerations, the Justice Department and voluntary agreements all have a role in determining what is actually licensable in the online world as well as how much money is being made by writers, artists, music publishers and record companies.

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This is a revised and updated version of an article that first appeared in the American Bar Association ENTERTAINMENT and SPORTS LAWYER(Forum on the Entertainment and Sports Industries).

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