

Thomas Vinje

Clifford Chance – Brussels, Belgium



*The Application of Competition Law
to Collecting Societies
in a Borderless Digital Environment*

written with Ossi Niiranen

European University Institute
Robert Schuman Centre for Advanced Studies
2005 EU Competition Law and Policy Workshop/Proceedings



To be published in the following volume:
Claus-Dieter Ehlermann and Isabela Atanasiu (eds.),
*European Competition Law Annual 2005:
The Interaction between Competition Law and Intellectual Property Law*,
Hart Publishing, Oxford/Portland, Oregon (in preparation).

**Please do not quote or circulate without permission
© Thomas Vinje & Ossi Niiranen. All rights reserved.**

The Application of Competition Law to Collecting Societies in a Borderless Digital Environment

by *Thomas Vinje* and *Ossi Niiranen**

A. Introduction

The rapid growth of the Internet has resulted in dramatic changes in the way copyright works are disseminated and consumed, as well as in demands for changes in the ways in which collecting societies deal with each other, with their members, and with licensees. The application of European competition law to the behaviour of collecting societies, which was developed some years ago in the context of an analogue, non-networked environment, has yet to be adapted to the realities of the new digital, networked environment.

Collecting societies have presented themselves as providing part of the solution to the challenges presented by the new digital, networked environment, and clearly they can and should play an important role in the development of the new digital ecosystem. But this means that they must change, and that they should adjust their behaviour to conform to an application of competition law that reflects the new realities.

In the past, both the European Court of Justice and the Commission have accepted that the peculiar circumstances then applicable to the operation of collecting societies, and the implications of these circumstances for the ability of the collecting societies to play the important role they have played in society, required a rather special and lenient application of competition law to the conduct of collecting societies. While the light-handed application of competition law to collecting societies might remain appropriate in the context of the traditional off-line environment, the revolutionary changes in technology seen in recent years require the Commission and the Courts to rethink the appropriateness of the special rules to collecting societies and in particular to consider whether the old, rather lenient approach in applying competition law to collecting societies remains justified in the new digital, networked environment.

While change can appear frightening to those accustomed to a comfortable status quo, legislative measures aimed at facilitating competition, coupled with more rigorous application of competition law to collecting societies in the digital environment, can benefit not only collecting societies' members (among whom are the actual authors and performers so especially vital to cultural development), but also those who facilitate the dissemination of creative works and performances and indeed also collecting societies themselves.¹

This paper will outline some of the main concerns in relation to the collecting societies and their behaviour with respect to their own members, and to potential licensees - with a particular focus on the latter.

* Clifford Chance, Brussels.

¹ The discussion below focuses on music rights, as these are the rights that have been at the forefront of the issues regarding the application of competition law to collecting societies in the digital networked environment. However, the same basic issues arise in the context of audiovisual works.

B. Overview of collecting societies and their operation

Collecting societies play a vital role in society by, *inter alia*, bringing owners of copyright and neighbouring rights in music (including authors, performers, producers and their potential assignees or exclusive licensees such as record companies) together with those who disseminate music, such as for example analogue radio stations, restaurants and discothèques in the traditional off-line environment and, for example, those who disseminate music via Internet streaming and downloading in the new digital networked environment.

1. The regulatory framework

Collecting societies draw their competence from different sources, depending on the type of collecting society and the Member State in which it operates. In some countries competence is based on a statute, whereas in others such as Germany, France, Spain and the UK, the competence of the collecting societies is to a large extent based on private law, mostly on the licences and assignments the collecting societies enter into with their members.

Collecting societies' operations are based on their internal statutes and bylaws, which in most cases determine both the competence of the collecting society and the relationship between the society and its members. The internal rules vary from one collecting society to another, and it is thus not possible to provide a comprehensive detailed description of the applicable rules.

2. The rights administered by the collecting societies

In order better to understand the role of the collecting societies, and the competition law concerns arising from their practices, it is important to see which rights are involved and which licences are required in most cross-border use licences, as many of the concerns discussed below arise in that context. As noted above, we will focus on the rights involved in dissemination of music.

In deciding on the licences needed, one must distinguish between two types of protected subject matter: (a) the underlying *musical work* and (b) the *sound recording*, and two categories of right holders: (a) the *author* (composer, songwriter, arranger and the like), and (b) the *performer* and *producer*.

The copyrights of authors include the *right of reproduction*, or right to control reproductions of performances embodying protected musical works by mechanical, electro-acoustic or electronic means (“mechanical rights”), and the *right of communication to the public/making available*, which in many Member States is part of a broader *performance* right and includes the right to authorize transmissions or other on-line deliveries of the work (hereinafter cumulatively referred to as “performance rights”).

The performing musician and producer hold neighbouring economic rights in the sound recording that are analogous to the rights of the author in the musical work. Thus, the performer and producer hold analogous rights of reproduction and communication/making available.

The most common ways of distributing music over the Internet (apart from the on-line sale of CDs) are downloading and streaming. Downloads of digital music imply (1) that the

musical work as composed by the author and the sound recording as performed by the performer(s) and recorded by the producer, is *made available* to users over the Internet, and (2) that a copy of that musical work and sound recording is stored (*i.e., reproduced*) both on the music provider's server *and* on the end-user's storage device. Collecting societies (and perhaps others) argue that music downloads require a clearance of: (a) the mechanical *and* performance rights of the author in the musical work, and (b) the mechanical *and* performance rights of the performer and producer in the sound recording. However, the scope of these rights and their relevance to the different forms of on-line music provision vary somewhat from Member State to Member State and may still be subject to unsettled law in many Member States.

Streaming involves the making available (interactively/on demand or non-interactively/by broadcasting) of music, and requires at least a *performance* licence from the author's performing society and from the performer(s)' and producer(s) societies or (more likely) the record company.

Actual authors and performers seldom retain their rights in any musical work or sound recording. Professional composers and songwriters generally transfer their economic rights to a *music publisher*, who in turn usually entrusts the management of these rights to a collecting society managing publishing rights.

Usually, one single collecting society does not manage rights relating to all kinds of copyright protected works. Instead, different societies manage different categories of rights, and thus, unless the collecting societies responsible for the different types of rights offer joint licences, the potential licensee might have to deal with different societies.

3. The roles of collecting societies

The main role of collecting societies is to administer and enforce the rights of their members on their behalf. Thus, among the main activities of collecting societies are the following:

- a. authorising the use of works by providing non-exclusive licences to interested parties;
- b. collecting royalties from licensees;
- c. distributing the royalties to members;
- d. enforcing members' rights.

The collective rights management system is potentially advantageous as it enables right holders to exploit their rights among a great number of users without the burden of individually administering such exploitation. Such a system can also be beneficial to potential licensees/users, as they can obtain licences for all the uses they need from a single source, without having to individually contract with all the relevant right holders (of which there can be many, even with respect to an individual piece of music), thus lowering the transaction costs involved in a typical music licensing deal.

C. Competition law concerns arising from the activities of collecting societies

Collecting societies administer the rights of their members by authorising use, collecting royalty (and levy) revenues, distributing the royalties/levies and enforcing the rights in courts if royalties/levies are not paid. Because of the special circumstances surrounding their

operation, including the fact that enforcing their members' rights traditionally has required territorially-focused monitoring and enforcement and that it would arguably be economically inefficient for more than one collecting society to administer the relevant rights per territory,² as well as the fact that their main functions are all concerned with dealing with copyright and related rights, the collecting societies have claimed that their activities are not subject to competition law in the same way the activities of normal companies are.

Community law has, however, consistently considered collecting societies as being undertakings subject to competition laws.³ While the European Courts have recognized the importance of upholding intellectual property rights because of their role in facilitating innovation and creativity, they have not deemed the behaviour of collecting societies to fall outside the ambit of competition law. They have, however, accepted some of the collecting societies' arguments about the circumstances in which they operate requiring a lenient application of the competition law to behaviour that otherwise would be deemed infringing. The big question today is whether the circumstances justifying a soft application of competition law to collecting societies in the traditional off-line context continue to exist in the new digital networked world.

In the Commission's view, competition law has concerned itself with three distinct categories of anticompetitive behaviour in which collecting societies have engaged, namely (1) restrictive agreements amongst themselves, (2) behaviour as regards their members (the right holders) and (3) behaviour as regards licensees.⁴ Even though the categories of behaviour are in principle separate, it is important to realize that they are in practice to a large extent interconnected and affect each other. In particular, horizontal co-operation can allow collecting societies to restrict competition both *vis-à-vis* right holders and *vis-à-vis* licensees.

A preliminary point that needs to be addressed is the market power of the collecting societies in the relevant markets.

1. Monopolistic position of the collecting societies

In principle, only one collecting society manages any particular type of right on behalf of a certain kind of right holder in a particular territory. Moreover, there is usually only one collecting society to which potential licensees can turn for the licence necessary for the particular type of exploitation they envisage for a particular territory. Thus, each collecting society typically occupies a near monopoly position *vis-à-vis* its potential members and licensees in the market for rights management in its territory.

The Commission and the European Court of Justice have consistently held that collecting societies each possess a dominant, if not monopolistic, position in the rights licensing market in their national territory. The rationale behind the holding is clear. The *de facto* monopoly is a result of the structure of the licensing markets outlined above. The structure itself was created by the collecting societies, which have divided the market for rights management services territorially amongst themselves by concluding with other collecting societies bilateral reciprocal agreements, giving each other the right to grant in their territories licences to the repertoire of the other. As discussed in more detail below, in order to preserve their own national monopolies, collecting societies have ensured that these

² Note, however, that in the United States different collecting societies (and in particular ASCAP and BMI) compete in the same territory both for members and for licensees.

³ See, for example, Case 127-73 *Belgische Radio en Televisie v. SV SABAM and NV Fonior* [1974] ECR-313.

⁴ Case Comp/C2/38.104 *IFPI "Simulcasting"* of 8 October 2002 (2003/300/EC), at recital 13.

agreements include several anti-competitive provisions aimed at preventing competition between the societies party to the agreement from emerging.

Thus, as discussed above, the European collecting societies together have a firm grip on the music market. Through their membership conditions, their practices and bilateral agreements, they have basically eliminated competition between each other. This has benefited only the collecting societies themselves, to the detriment of the on-line music market, including on-line providers of music as well as the creators and performers themselves.

2 Relationship between collecting societies and their members

Among the most harmful of collecting societies practices in the digital environment is the imposition by the societies of strict exclusivity requirements on their members. Currently, a member of a collecting society is effectively prevented from managing on-line usage of his repertoire through several collecting societies, from self-managing his on-line rights,⁵ and from delegating on-line rights management to any entity other than a collecting society. This also means that on-line music providers have no source for on-line music rights other than collecting societies, which reduces significantly the opportunity for on-line music providers to obtain competitive and innovative licence terms.

In the 1970s, the European Commission handed down several decisions requiring certain collecting societies to modify the rules governing their relationships with their members.⁶ These decisions established the basic principle that collecting societies enjoy a dominant position *vis-à-vis* their members. Article 82 EC prohibits as incompatible with the common market any abuse by one or more undertakings of a dominant position within the common market or a substantial part thereof in so far as it may affect trade between Member States.

Such an abuse was found in the Commission's 1971 decision relating to the statutes of the German collecting society GEMA.⁷ At the time, GEMA required as a condition of membership, *inter alia*, that its members grant to GEMA a blanket exclusive licence covering all the members' rights for all categories of their works throughout the entire world.

The Commission condemned this practice as an unjustified abuse of GEMA's dominant position. The *GEMA II* decision established that GEMA must allow a prospective or existing member either a) to assign to GEMA all works for all countries, and to withdraw his rights at any time, and for all *works* and all countries, but only with respect to seven categories of *use* defined in the decision and/or with respect to specific countries, or (b) to assign works to GEMA in whole or in part for *any* type of use (not necessarily those specified in the decision) or for specific countries, but allowing withdrawal of rights with respect to those works *only* at the close of every three-year term and with six months' prior notice. GEMA opted for the latter approach, and thus its members are allowed to withdraw their rights with respect to any type of use - but only at the end of every three-year term, only subject to six months' prior notice (*i.e.*, notice at the latest in June if the three year term ends

⁵ But see Commission Decision of 12 August 2002, *Case C2/37.219 Banghalter & Honem Christo / SACEM ("Daft Punk")*, which indicates that in some circumstances individual management might be possible.

⁶ Commission Decision 82/204/EEC of 4 December 1981 (*GEMA III*) OJ L 94 [1982]; Commission Decision 72/268/EEC of 6 July 1972 (*GEMA II*) OJ L 166 [1972]; Commission Decision 71/375/EEC of 9 November 1971 [1971] OJ L254/15; Commission Decision 71/224/EEC of 2 June 1971 (*GEMA I*) OJ L 134 [1971]. See also Case 127/73, *BRT II*, judgment of 27 March 1974 [1974] ECR 316.

⁷ Commission Decision 71/224/EEC of 2 June 1971 (*GEMA I*) OJ L 134 [1971].

on December 31). Most other European collecting societies have opted for the same option, if they allow the withdrawal of certain rights at all.

The *GEMA II* decision does not allow a member of a collecting society to withdraw his rights for any type of use at any time. Moreover, the Commission's decision did not prevent the collecting societies' practice of requiring *exclusivity* for those categories of rights that they continued to manage.

At the time, the *GEMA II* decision may have represented an appropriate balance between the enforcement of EC competition law and the effective exploitation of IP rights. However, the world has moved on since 1972, and the lawfulness of the conditions imposed on their members by collecting societies should be re-evaluated in light of the dramatic and fundamental changes wrought by on-line technology. The Commission should consider whether the membership conditions permitted in *GEMA II* should be allowed with respect to on-line rights. In particular:

- the three year withdrawal term is extremely long in the on-line context; allowing withdrawal of on-line rights only every three years and only with such long notice periods effectively prevents authors from withdrawing their rights at all;
- the collecting societies' practice of requiring exclusivity from its members is no longer justified with regard to on-line exploitation of rights.

According to the ECJ and the Commission, in assessing the lawfulness of collecting societies' practices, "*account must ... be taken of the fact that [a collecting society] is an association whose object is to protect the rights and interests of its individual members*". In light of this, it is then necessary to "*examine whether the practices in dispute exceed the limit absolutely necessary for the attainment of this object, with due regard also to the interest which the individual author may have that his freedom to dispose of his work is not limited more than need be*" (emphasis added).⁸

Because many of the on-line music providers are at least as well if not better able to distribute royalties to authors and performers quickly and accurately, as well as being better placed to police rights on-line, and because in many respects collective management may be less efficient and less beneficial to right holders than direct management by artists (alone, in parallel with a collecting society or through an on-line music provider it has licensed), it cannot be argued that it is *absolutely necessary* for collecting societies to manage on-line rights *exclusively*. Among other things, the notion that rights can only be effectively administered, monitored and enforced on a national territorial basis is without any foundation in the on-line context. For example, owners of rights in computer software and in sound recordings police their rights across large geographic regions from single locations, and see no need for national on-line policing entities.⁹

The *Daft Punk* case seems to indicate that the Commission is taking steps in the right direction in this respect, although the Commission eventually rejected the complaint. The case dealt with a complaint lodged by the techno-music group Daft Punk, which claimed that the French Collecting Society SACEM was in breach of Article 82 EC by refusing to allow Daft Punk to retain some of their rights for individual management. Briefly put, the Commission was of the opinion that, due to technological advances, prohibitions on individual

⁸ Case 127/73, *BRT II*, judgment of 27 March 1974, *supra* note 3, at paragraphs 9 and 11. See also Commission Decision 82/204/EEC of 21 December 1981, at 36.

⁹ In certain cases collecting societies have also abused their dominance by discriminating between potential members, usually by treating national right holders differently from non-nationals. In *GEMA I*, complaints had been made of the internal rules of GEMA, which provided that "foreign nationals may become ordinary or extraordinary members only if they have their fiscal domicile in Germany", but German nationals were not subjected to the same requirement. The Commission investigated the matter and found that the rule was discriminatory and infringed Article 82 EC.

management of rights were not "absolutely necessary",¹⁰ and hence infringed competition laws. However, the Commission did not pursue the matter further because SACEM modified its membership rules, making individual management of specific rights possible as a derogation from the general rule of collective management of all rights. Therefore, it is difficult to say what the precedential value of *Daft Punk* is – further clarification is still needed.

3. Relationship between collecting societies and licensees

Apart from the damage to licensees caused by anticompetitive agreements between collecting societies (discussed below), competition law concerns can also arise from more direct abusive behaviour *vis-à-vis* the licensees. Because of their *de facto* monopoly, collecting societies are in a position to abuse their dominant position to the disadvantage of licensees of rights, and the Commission has also noted this. As is well known, there is no exhaustive list of abuses that a dominant undertaking can commit, and thus it is not possible to enumerate all types of abusive behaviour in which collecting societies can potentially engage.

However, it is possible to highlight the most prominent types of abuses. In *Lucazeau*,¹¹ a case concerning royalties to be paid by discotheque owners to the collecting society for performance rights, the ECJ condemned excessive tariffs by collecting societies. It held that when a collecting society

*“imposes scales of fees for its services which are appreciably higher than those charged in other Member States and where a comparison of fee levels has been done on a consistent basis, that difference must be regarded as indicative of an abuse of a dominant position. In such a case it is for the undertaking in question to justify the difference by reference to objective dissimilarities between the situation in the Member State concerned and the situation prevailing in all the other member states.”*¹²

The decision thus addresses a major behavioural issue dealing with the relationship of collecting societies and users. Collecting societies, when dealing with their users, cannot exercise their exclusive intellectual property rights to extort excessive royalties from their users. If there is evidence of such behaviour, it is for the collecting society to justify that its tariffs are based on objective and sound criteria.

3.1. *The impact of co-operation between collecting societies*

A major concern from the perspective of both competition law and society has been the refusal of collecting societies to deal adequately with the needs of those who wish to obtain cross-border licences for the purposes of their Internet business. This is unfortunate, as the benefits of on-line music dissemination are clear. Authors and other music right holders can employ the Internet to reach broader audiences more easily, directly and cost-effectively than they can through traditional ‘off-line’ methods of distribution. They can also use the Internet to build new and closer relationships with their listeners. The Internet allows both established

¹⁰ *Supra*, note 8.

¹¹ Joined cases 110/88, 241/88 and 242/88 *Francois Lucazeau and Others v. SACEM and Others* [1989] ECR 2811.

¹² *Lucazeau*, paragraph 25.

providers of on-line music and new market entrants to deliver novel competitive music offerings that are better tailored to the users' individual music desires than those available through traditional music distribution channels. On-line music delivery also brings significant cost reductions and other economic efficiencies, and significantly decreases geographical barriers to music distribution. The availability of more music at lower cost than would ever be possible within the constraints of traditional music dissemination channels also benefits consumers.

A legitimate and dynamic on-line music market can of course develop only if right holders are adequately compensated for the on-line exploitation of their works; otherwise, many will have no incentive to create new musical works and distribute them on-line.¹³ The provision of musical works, whether by webcasting or by streaming or downloading on demand, free of charge or against payment, should take place only if the music provider is authorized by the right holder(s) to do so and appropriately compensates the right holder for this use.

However, the current situation where on-line providers arguably need to obtain rights clearance for making music available on the Internet in all countries where the music is accessible (the country of destination principle), and where the national collecting societies operate on a national basis offering rights licensing only for their national territory -- which effectively creates national monopolies for licensing of rights -- hinders various forms of music distribution on-line. The failure of collecting societies to adapt to new technology and new opportunities for providing music on the Internet also results in constantly growing but unfulfilled consumer demand. To a large extent, this failure results from the fact that current practices rule out any possibility of competition between the different national collecting societies.

The collecting societies have attempted to address the demand for cross-border licences by a web of reciprocal agreements between themselves. Such agreements are considered necessary because the collecting societies are generally only competent to act within their national boundaries, and thus co-operation between collecting societies is needed to ensure that it is possible to obtain cross-border licences. However, co-operative agreements are prone to misuse, and as explained below, active and rigorous competition law enforcement is needed to ensure that competition is not restricted.

3.2. Controlling co-operation through competition law

The conclusion of agreements between collecting societies such as those modelled on the basis of the Santiago Agreement could provide a significant step forward towards resolving the need for a single source for Europe-wide licences necessary for on-line music distribution.¹⁴ However, as noted above, the reciprocal agreements advocated so far by the collecting societies have proved to be problematic from a competition law point of view due to the anticompetitive provisions they contain. Three specific examples of such agreements are analyzed below, namely: (a) the IFPI simulcasting agreement, (b) the Barcelona

¹³ One cannot deny, of course, that many music-makers make music purely for the joy of doing so, and that many music-makers are happier to see wide dissemination of their music than they are to obtain remuneration for it. But one also cannot deny that many music-makers are dependent on their music for their livelihood and that remuneration for their musical creations and performances is vital to them.

¹⁴ Simulcasting was defined in the notification as "the simultaneous transmission by radio and TV stations via the Internet of sound recordings included in their broadcasts of radio and/or TV signals" [see recital 2 of the *IFPI Simulcasting Decision*].

agreement, and (c) the Santiago agreement. The focus of the analysis will be on the Santiago agreement.

a. The *IFPI* simulcasting agreement

In November 2001, the International Federation of the Phonographic Industry ('IFPI') notified to the Commission a model reciprocal agreement between collecting societies dealing with *simulcasting* rights. The purpose behind the agreement was to provide for a one-stop shop for licensees wanting a multi-territorial licence for simulcasting.

The Commission refused to grant clearance to the agreement as originally notified, due to the fact that it contained, *inter alia*, a customer allocation clause which confined potential licensees to only one collecting society which they could negotiate with for a multi-territorial licence. Such a provision is clearly anticompetitive and constitutes a horizontal market sharing agreement prohibited by Article 81 EC Treaty. In the face of Commission opposition, IFPI revised the model agreement and made it possible for licensees to go to any collecting society in the EEA in order to obtain a licence covering multiple territories. The Commission considered the removal of the customer allocation clause to be sufficient and granted an exemption under Article 81(3) EC.

b. The Barcelona agreement

The *Bureau international des sociétés gérant les droits d'enregistrement et de reproduction mécanique* ('BIEM') notified the Barcelona agreement to the Commission in 2001. The agreement is designed to set out the conditions under which collecting societies can provide multi-territorial licences for on-line mechanical rights for *webcasting* and on-demand streaming and downloading. Similarly to the Santiago agreement (see below), the agreement contains a customer allocation provision to the effect that a licensee can only obtain a licence from the collecting society located in the same country as the licensee. As noted above, such a provision is clearly anticompetitive, and the Commission considers that it infringes Article 81.¹⁵

c. The Santiago agreement

In April 2001, a group of collecting societies notified to the Commission the so-called Santiago agreement, which was designed for the purpose of allowing collecting societies to grant to parties interested in on-line music distribution licences to the music repertoires of all societies participating in the agreement. Through such agreements, a single collecting society may be able to offer licences for the on-line exploitation of the repertoire of multiple collecting societies. This form of 'one-stop shopping' could considerably simplify on-line music providers' licence acquisition and administration process and thus help pave the way

¹⁵ Commission Staff Working Document, *Study on a Community Initiative on the Cross-Border Collecting Management of Copyright*, 7 July 2005, at p. 11, available at http://www.europa.eu.int/comm/internal_market/copyright/docs/management/study-collectivemgmt_en.pdf.

for the development of a legitimate and efficient on-line music market and resulting choice and cost benefits for consumers of on-line music (and diminution of piracy).

The Santiago Agreement is a template bilateral agreement, to be concluded between performing rights societies, which will amend the existing bilateral agreements between these societies. With respect to the authors' rights to permit or prohibit public performances of their works, the Santiago Agreement applies to licensing of authors' *performance* rights and the distribution of resulting royalties for *on-line* music provision through downloading and streaming of music over the Internet with the exception of simulcasting.¹⁶

The Santiago Agreement seeks to address a dilemma posed by the current practices of collecting societies in the on-line context. On-line music providers are required, for each country in which their service is available, to obtain a performance right licence for the music they wish to distribute legally. Until arrangements like Santiago were put in place, it was not possible to obtain world-wide (or even Europe-wide) rights from a single source. This left on-line music providers in an untenable situation.

The Santiago Agreement therefore establishes one-stop shopping with respect to licences for public *performance rights* (right to publicly perform, make publicly available and communicate to the public) of the *authors* of music (such as composers and songwriters), which is one of the key elements necessary for on-line music provision. In other words, the model Santiago Agreement has the potential of expanding the territorial reach of performance licences granted by collecting societies for on-line music to the entire world, such that only one licence is required from a single collecting society.

However, the way in which the Santiago Agreement has been formulated raises very serious concerns. It contains customer allocation and other provisions that infringe Article 81 and that cannot be subject to any exemption.

While the Santiago Agreement does allow an on-line music provider to obtain one world-wide licence from one collecting society for the repertoire of all the collecting societies with which the licensing society has concluded a Santiago Agreement, it prevents the provider from obtaining this licence from any collecting society other than the collecting society of the country where it is deemed to be established under the terms of the Santiago Agreement. For example, if the provider is established in Sweden, it can only obtain a Europe-wide license for a particular work from the Swedish collecting society and not from any other collecting society in Europe. The planned system would thus exclude competition between collecting societies for Europe-wide licences of the same repertoire.

In other words, the Santiago Agreement will eliminate any competition among collecting societies with respect to the terms and conditions of on-line music licensing. As a result of the Santiago Agreement, each national collecting society will have a *de facto* monopoly over on-line multi-national music licensees in its own country, and it need not fear competition with respect to the licence terms or administration fees applying to these customers from collecting societies in other countries. This lack of competition will not only delay the development of the on-line music market and of related technology, it will also have adverse consequences for authors (the collecting societies' members). The structure established by the Santiago Agreement clearly constitutes an unlawful market sharing

¹⁶ The 'mechanical rights' collecting societies, which administer the authors' *reproduction* rights, and which usually are either closely linked with (or indeed one and the same organization as) the performance rights societies, are not involved in the Santiago Agreement in their capacity as managers of 'mechanical rights'. However, for the purposes of licensing such rights, a similar arrangement, the so-called Barcelona Agreement (discussed above), has been devised.

arrangement between collecting societies in the form of customer allocation on the basis of a ‘licensee country of establishment’ criterion.¹⁷

For on-line music companies with subsidiaries established in different Member States, the customer allocation of the Santiago Agreement is particularly harmful: the Santiago Agreement provides that, for purposes of determining which collecting society has the authority to license, each company of a multinational group of companies is to be considered (and licensed) separately, regardless of the location from which the website’s content is hosted or distributed. Therefore, each subsidiary will be required to obtain a separate licence from a different country’s collecting society. Such a provision strengthens the division between customer groups among collecting societies.

Furthermore, there is no justification for the anticompetitive provisions in the Santiago Agreement, and these provisions surely cannot qualify for an Article 81(3) EC exemption. The benefits of the ‘one-stop shopping’ approach embodied in the Santiago Agreement can be achieved without any customer allocation or other restrictive provisions. Indeed, these restrictive provisions meet none of the prongs of Article 81(3) EC. On the one hand, they neither (a) contribute to improving the production or distribution of goods or promote technical progress nor (b) provide any benefits to consumers. On the other hand, they (c) impose restrictions that are not indispensable to attaining the benefits of the Santiago Agreement and (d) allow collecting societies to eliminate virtually all competition amongst themselves for on-line music licences.

D. Addressing the concerns through legislation

Apart from enforcing the competition laws, an important means of addressing the need to achieve competition in collective rights management is through legislation.

At least two potential solutions can be identified. First, the implementation of a country of origin principle into on-line licensing could correct the competition distortions in the relationship between the collecting societies and the licensees. The second solution, eliminating the current web of reciprocal agreements between the collecting societies and giving right holders the right to authorize the collecting society of their choice to manage their rights Europe-wide, has its emphasis on the relationship between the collecting societies and their members, *i.e.*, the right holders. However, as explained below, both solutions would also indirectly encourage competition between collecting societies overall.

1. Implementing a ‘country of origin’ principle

Even though national legislation on copyright protection was partly harmonized under Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonization of certain aspects of copyright and related rights in the information society, no harmonized rules exist within the European Union governing clearance of copyrights and remuneration in the field of on-line services.

¹⁷ We note in this context that the Directive on the harmonization of certain aspects of copyright and related rights in the information society of 9 April 2001 provides in Recital 17 that “[i]t is necessary, especially in the light of the requirements arising out of the digital environment, to ensure that collecting societies achieve a higher level of rationalization and transparency with regard to compliance with competition rules.”

Today, the act of communication to the public of the copyright protected work in the field of on-line services, such as webcasting, is considered to take place in every reception state. Therefore, as discussed above, providers of such services need to obtain a licence covering the copyrights involved in each country where the services are accessible via the Internet. Moreover, remuneration is due in all these countries in accordance with the tariffs laid down by the collecting society in each country.

This so-called 'country of destination' principle is inconsistent with the fundamental principles of the Internal Market, and indeed it prevents the development of an internal market in the rights required for on-line music services.

The development of cross-border transmission of on-line services within the EU in accordance with the principle of free movement of services, and thereby the creation of an internal market with undistorted competition, would be facilitated if the country of origin principle were applicable to these services. An amendment of the current practices would to a large extent eliminate the existing obstacles to such development. In order to apply the country of origin principle to interactive services, the current definition of where the act of communication to the public takes place should be redefined so that the act of communication should be considered to take place only in the country of emission.

If this approach were adopted, it would create competition between the different collecting societies, as they would have to compete for licensees. This would lead them to be more efficient in their activities, would reduce their high level of administrative costs, and would encourage them to engage in innovative forms of licensing that facilitate the development of new forms of on-line music dissemination. Not only consumers but also, and most importantly, right holders would benefit from the development of such new business models, as more music is made available and consumed by more people in Europe, and as legitimate on-line music distribution replaces unremunerated file sharing.

2. The Commission's on-line copyright licensing initiative

The Commission has also recognized the inadequacy of competition law in dealing with all the competition concerns arising from the operation of collecting societies. Recently, in July 2005, it published a working document detailing its views on a legislative approach towards solving some of the problems.¹⁸ Although more of an idea paper than a detailed description of a legislative solution to a pressing problem, the paper offers an interesting analysis of three approaches the EU could adopt in order to attempt to improve competition in the market for rights management services.

The first approach considered by the Commission is to do nothing and let market forces develop a solution to the current competition concerns described above. However, as demonstrated by the current market situation, it cannot be expected that market forces will solve the problems. The current requirement for a licensee to negotiate a separate licence agreement for each territory is costly both in terms of time and resources. Collecting societies have not been able to come up with an acceptable solution that would offer one-stop shopping on competitive terms, as well illustrated by the examples of the Santiago and Barcelona agreements.

The second option envisages the elimination of anticompetitive provisions in the reciprocal agreements between the collecting societies. Such an approach would clearly be

¹⁸ Commission Staff Working Document, *Study on a Community Initiative on the Cross-Border Collective Management of Copyright*, 7 July 2005, text available at http://www.europa.eu.int/comm/internal_market/copyright/docs/management/study-collectivemgmt_en.pdf.

more advisable than the first option, as it attempts to address some of the reasons why the current system does not work. It is 'a licensee's option' in the sense that it would have a direct and immediate pro-competitive impact on the relationship between the licensees and the collecting societies. A licensee could choose whichever collecting society offered the most attractive deal, and the collecting societies' revenue would thus be dependent on offering competitive arrangements. The Commission unfortunately and unwisely rejects this approach because it does not address what the Commission considers to be the main issue, namely the lack of competition between collecting societies for right holders. However, it is not clear whether this discarded approach would solve the real problem (the lack of competition on licence terms, including rates).

The third solution, preferred by the Commission, seems to be aimed at abolishing the web of reciprocal agreements between collecting societies that currently form the framework for multi-territorial licences by implementing a cross-border rights management system -- initially only for music. The system would allow *right holders* (as opposed to licensees) to choose a collecting society outside their national territory for the EU-wide licensing of their rights. Thus, instead of relying on reciprocal agreements between collecting societies, the society chosen by the right holder would have a contractual mandate whereby the collecting society would represent the right holder across Europe. This, according to the study, would create a competitive environment in which collecting societies compete for right holders in cross-border management of copyright. Unlike a scheme that would allow licensees to go to any collecting society they wish to obtain a licence for the rights they require, the Commission prefers this 'right-holders option',¹⁹ as it enables competition on the basis of not only price, but also on work repertoire. Currently, collecting societies offer, through their reciprocal agreements with the other collecting societies, an identical repertoire. However, the approach proposed by the Commission would leave it to the collecting societies to build up their own repertoire by competing for right holders. Moreover, increased competition would increase the royalties distributed to right holders, as collecting societies would compete against each other on the basis of, *inter alia*, the amount of royalties they distribute to their members. The system would thus significantly increase the revenue potential of right holders.

An important element of this system would be the option of right holders to withdraw their rights from the sphere of a collective management system they had previously used. Absent such an option there would be a danger that right holders would be locked in to a specific society, unable to realize the benefits of competition between the societies. However, the study also recognizes that right holders should not be able to withdraw their rights at will, as this would make it very difficult for collecting societies to plan their business operations on a viable basis. Therefore the paper proposes that right holders should be given the option to withdraw their rights, but only after the expiry of a reasonable notice period.

The Commission sees its proposed solution as a tool that is mainly aimed at addressing the competition law concerns arising from the relationship between the collecting societies and their members. However, it also believes that opening up competition would lead to efficiencies benefiting licensees as well.²⁰

As the details of the Commission's plans are still sketchy, it is difficult to analyze the potential impact they might have. However, we would like to highlight the main concern we have with the proposal. According to the Commission, it expects only a few, albeit large, collecting societies to remain after the proposal is implemented. However, the remaining societies would not be subject to any real competition amongst themselves on licence terms.

Because it is still not clear how the Commission is planning to implement its proposal, it is too early to dismiss the initiative. However, in our view it would be advisable for the

¹⁹ *Ibid.*, at page 40.

²⁰ *Ibid.*, at page 36.

Commission to note the significant risks inherent in its current proposal and attempt to devise a solution that would take into account the need to ensure that collecting societies are obliged to compete not only for right holders but also for licensees.

E. Conclusion

Collecting societies have an important role to play in rights management, both in the traditional off-line and the new digital networked environments. However, the lack of competition between collecting societies has created a situation where the ideal view of collecting societies does not often equate to reality. Collecting societies have often abused their market power to the detriment of both their own members and licensees and have thus hampered the development of new markets.

Collective management should embrace new technologies and adapt to the new opportunities of music on the Internet. If collecting societies were to do so, and to accept the legitimacy of competition with respect to the collective management of on-line music rights, they would no longer hinder the development of the on-line music market and would ultimately enable more people to obtain legal music more cheaply and easily on-line. Competition would encourage collecting societies to be more efficient as organizations and to lower their administrative costs, and to explore innovative ways of licensing music rights and disseminating music. Moreover, the overall effect would be a net increase in creators' and performers' incomes, as more licences would be granted to more on-line music providers and new and innovative music markets would be developed (instead of free, peer-to-peer file sharing systems that provide no remuneration whatsoever to creators and performers).

In addition to making collecting societies subject to competition through a system of Europe-wide licences obtainable from any collecting society, and not just the collecting society where the potential licensee is established, as required by the template Santiago Agreement, membership conditions of collecting societies should be made more flexible for collecting societies' members so that they can more easily withdraw from the management of the collecting society certain types of rights, certain forms of exploitation or certain works. This would allow artists to self-manage some forms of exploitation where collective management is not appropriate for their needs – as may often be the case in the on-line context, where digital rights management systems facilitate direct management of rights or where digital music companies can better serve the artists' interests. It would also give authors an effective bargaining tool to ensure that collecting societies properly manage their rights.

Finally, one reason for the reluctance of collecting societies to change current practices might be that many of them are intransparent, bureaucratic organizations influenced by their status as quasi-governmental entities. Transparency would be enhanced if collecting societies were subject to comprehensive, intelligible and detailed disclosure and reporting requirements. For example, the collecting societies could be made subject to the accounting principles applicable to public undertakings. One key principle is that the accounts “should show the distinction between different activities, the cost and revenues associated with each activity and the methods of cost and revenue assignment and allocation”.²¹ While supervision by a governmental body of collecting societies is vital to safeguard the interests of artists, such supervision should, unlike the situation today, be truly independent.

²¹ *Commission Directive 2000/52/EC of 26 July 2000 amending Directive 80/723/EEC on the transparency of financial relations between Member States and public undertakings*, OJ L 193 [2000].