DRAFT – November 21, 2005

Legal Opinion concerning European Competition Law Issues Arising From the Possible Introduction of a Formal Prior Approval from Each Collecting Society Whose Territory Would Be Included in a Central Licensing Scheme

1. We have been asked to provide a legal opinion dealing with European competition law issues arising from the possible introduction of a formal prior approval from each collecting society whose territory would be included in any central licensing agreement (hereafter, "CLA").

2. Preliminarily, we would like to note that we are only considering the situation where the CLA is concluded with a recording group which has branches in different countries and where these branches are themselves genuine record producers, *i.e.* are the legal persons in charge of exploiting the repertoires in the different territories covered by the agreement[1]. In this case, it is the society in the territory of which the record producer branch is located which has the rights to grant a license covering the use of its repertoire in its territory. The reciprocal representation agreements do not grant to another society the rights to grant a license for the territory of the other society.

3. At this stage, the European Commission has not challenged this limitation in the field of mechanical rights. However, it has to be noted that for Internet, the European Commission is clearly seeking to obtain that each European collecting society be allowed to have the right to grant a license for all the European territories and it seems that it is willing to take action with similar goals for broadcasting in the framework of the so-called Music Choice of Europe / RTL cases.

4. Moreover, one could think that these limitations for mechanical rights have not been challenged since in fact they have not prevented the development of competition between societies for CLAs.

5. Indeed, it must be observed that the European Commission has always favorably considered CLAs, seen as a key element of competition between collecting societies for nearly 20 years now.

6. An illustration of the importance given by the Commission to CLAs and the competition they are deemed to have created between collecting societies can be found in the treatment of the complaint filed in 2003 by Universal International Music against MCPS, GEMA,

[1] The situation would be different if a record producer established in one Member State were the only legal person using the repertoires and exported the records throughout Europe. In this case, it is clear that the society in whose territory the user is located could grant a license for all the records produced whatever their final destination. Once the license is granted, the records would not be subject to any further authorization wherever the physical manufacturing takes place or whatever the final destination (see the so-called 1984 GEMA custom pressing case in the *European Commission Competition Report*, 1985, p. 88). However, this principle does not mean of course that under the current reciprocal representation agreements each and every society could grant a license for the repertoires of other societies to users located outside their territory.

SDRM, NCB, SGAE, SIAE and STEMRA "*in relation to the collective refusal of certain EU collecting societies to grant rebates in central licence agreements for mechanical rights*".

7. In this complaint prompted by the difficulties encountered in renewing its CLA with MCPS, Universal International Music argued in particular that Clause 9(a) of the Cannes Extension Agreement[2], "[I]*n removing the rebate* [granted to users in the terms negotiated in CLAs]*, the one remaining element of price competition which the collecting societies against whom the Complaint is made can offer, and in relation to which they were formerly able to compete, has been eliminated. This in turn removes all competition in the market for the provision of the service for collection of mechanical royalties*" (§ 2.7).

8. The European Commission asked that Clause 9(a) be amended in order for it to close the file and dismiss the complaint[3].

9. BIEM itself has used this argument in various submissions made to the European Commission over the last 10 years.

10. In the notification of the BIEM Statutes, which provide for the BIEM-IFPI Standard Contract, reference was made to the fact that this Standard Contract does not prevent the development of centralization agreements. The BIEM Statutes were cleared by the European Commission in a comfort letter dated 4 December 2000.

11. This reference was repeated in (i) a letter sent to the European Commission on 23 July 1998 concerning Amendment 7 of the Standard Contract, (ii) the answer made to a request for information dated 17 August 1998 and more recently in (iii) a letter sent to the European Commission on 26 May 2005 to share elements of reflection concerning the vertical effect the Commission deems to exist with regard to the Standard Contract.

12. Under these conditions, such a change as the change envisaged, *i.e.* the formalization of a prior approval from each collecting society whose territory is to be covered by a central licensing agreement, is likely to raise substantial concerns with the European Commission.

13. Firstly, the introduction of such a system of prior approval will undoubtedly render the conclusion of CLAs more difficult. CLAs have been in force for twenty years and the European antitrust regulators would surely be upset by a restriction on the key, if not the only, factor of competition between societies.

14. Secondly, such a system subjects to the possible competitors of one of the parties to an agreement the conclusion of such agreement. From a competition law standpoint, such a system can only raise concerns, all the more so as it implies that the elements of discussion and negotiation between a collecting society and a possible licensee will be subject to the

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2 Clause 9(a) of the Cannes Extension Agreement, let it be recalled, provides that « *Given that royalties and other sums collected by the Societies are destined for their members, no Society may under any circumstance give any money to any record company or allow any record company to retain or be paid money in the form of a rebate or reduction of tariff or any other form (by way of a lump sum, provision of services or royalty reduction or any other return of value) unless agreed in writing with the relevant member*".

3 The Commission's favorable view on CLAs can be further illustrated by a recent declaration, made by Herbert Ungerer, then Head of the Media Unit at the Directorate General for competition at the European Union. During a meeting which took place on 11 March 2005 with Torben Toft, deputy head of the same Media Unit, and two case handlers involved in cases concerning the collecting societies *i.e.* the Cannes Agreement and the Music Choice of Europe complaint, Herbert Ungerer said that central licensing agreements are "*a good development*".

approval of another collecting society which could be the competitor of the first collecting society for the conclusion of the CLA.

15. Thirdly, competition authorities will probably claim that there are less restrictive alternatives than the prior approval system. For instance, the antitrust authorities could think that a tacit *a posteriori* approval, or even an express *a posteriori* approval, could be a reasonable system striking a fair balance between the rights of each society and the requirements of competition.

16. In any case, we would like to stress that the current context is characterized by the willingness of the European Commission to enforce a pro competitive agenda as regards the relations between collecting societies. The contemplated modification would seemingly not go unnoticed. It would be highly advisable to go and see the Commission before its adoption.