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By hand

European Commission
Directorate General for Competition
Attn.: Dr. Herbert Ungerer and
Mr. Miguel Mendes Pereira
Rue de Genève 1
1140 Brussels

6 September 2002

Subject: Case COMP/C2/38.440 Universal v BIEM

Dear Dr. Ungerer,

Dear Mr. Mendes Pereira,

On behalf of Bureau International des Sociétés Gérant les Droits d'Enregistrements et de Reproduction Mécanique ("BIEM"), we are writing to reply to the complaint lodged by Universal Music International Limited ("the complainant"), dated 31 May 2002. Our power of attorney is enclosed in annex 1.

A courtesy summary of our main arguments in included.

T A B L E O F C O N T E N T S

A. THE COMPLAINANT'S BASIC MISUNDERSTANDINGS

I. Unavailability of the Relief Sought

1. The complainant seeks to use competition law as a tool to lower royalties for musical copyright licenses. However, it is outside the purpose of competition law to set prices. Competition law in fact aims at an environment of undistorted competition where prices are determined by the interplay of market forces. It is concerned with *competition as an environment*, but *not with specific bargaining results.*[1] This does not rule out investigations under Article 82 EC, but the competition-based system that the Treaty establishes must not be changed to one of public price-fixing.

2. Entwined with the complainant's misconception of competition law is a procedural misunderstanding: The Commission, acting as a competition authority, is not a regulator. Rather, the Commission investigates alleged infringements of the competition rules. Where the Commission finds such an infringement, it requests the responsible parties to bring that infringement to an end (*"negative relief")*.[2] By contrast, the Commission, in competition matters, normally does not request enterprises to adopt a specific conduct *("positive relief")*. For example, the Commission normally does not oblige enterprises to offer certain prices.[3]

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1 See the recent statement by a leading author of competition law: „Im Recht der Wettbewerbsbeschränkungen geht es ... darum, Hindernisse für Wettbewerb beiseite zu räumen und im Übrigen Marktprozesse mit unbekanntem Ergebnis spielen zu lassen." *Werner Möschel*, Neue Zürcher Zeitung, 10 July 2002, p. 13.

2 See Article 3 (1) of Regulation N° 17.

3 See Temple Lang *Community Antitrust Law and National Regulatory Procedures* [1998] Fordham Corp. L. Inst. 297 at 299: "A regulator may have powers, if necessary, to approve or determine a precise price, issue licenses, order divestiture, impose contract terms, impose a technical specification or allocate a scarce resource … A competition authority acting as such may not be able to do all these things." See also *id.* at 301: "Community or national competition law … may not fix the precise price that should be paid … If these prices have to be fixed (which of course is not necessarily the case), they can be fixed by a national authority under national law: *there is no Community regulator.*" (emphasis added).

3. In disregard of this legal framework, the complainant requests regulatory intervention by the Community competition authority following a first formal round of negotiations between BIEM and IFPI.[4] This culminates in the "orders sought" where the complainant bluntly requests "A declaration that the Standard Rate is too high; …". We understand that the complainant is dissatisfied with the standard agreement that IFPI negotiated with BIEM which expired on 30 June 2000. To further increase IFPI's bargaining power in the negotiation of a new standard agreement, the complainant suggests that the Commission interfere with the current negotiations, and support IFPI in these negotiations in order to reach a better result. In our view, that is outside the scope of competition law.

II. The Superior Bargaining Power of the Major Record Producers

4. BIEM negotiates with the International Federation of the Phonographic Industry ("IFPI"). IFPI's members include the five most powerful Record Producers, which together dominate the record-producing market: BMG, EMI, Sony, Time Warner, and Universal ("the majors"). These majors are part of media conglomerates whose turnover, financial resources, manpower and information are incommensurately greater than those at the disposal of BIEM. IFPI is also an organization with funding and resources far superior to BIEM.

5. The combined bargaining power of the majors has already been determined in other competition cases. In its provisional statement of objections in *Time Warner / EMI*, the Commission has highlighted this bargaining power and has analyzed the factors at its basis.[5] Moreover, in a decision of 9 October 1997, the Italian competition

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4 See, e.g., § 4.17 of the complaint: "In the absence of regulatory intervention, it is to be expected that the BIEM rate will naturally settle at a monopoly rate …".

5 Case N° Comp/M.1852 – *Time Warner / EMI*, (provisional) Statement pursuant to Article 18 of Council Regulation and Protocol 21 of the EEA Agreement, §§ 42, 50 (fourth point) and 57. This draft statement has been disseminated by the music industry and thus has come to the attention of BIEM.

authority (*Autorità Garante della Concorrenza e del Mercato)* found that the majors were liable for fixing uniform and constant prices.[6] In the United States, authorities are investigating the behaviour of the majors as regards artists' contracts. In the same country, legislators have had to address highly unfair clauses in licensing contracts whereby the majors' systematically diminish creators' income. We will revert to these so-called "controlled composition clauses" at point 189 below.

6. *The complainant cannot seriously pretend that IFPI and the majors are in a stranglehold situation which is characteristic of cases to which Article 82 EC is applied.*[7] *Quite the contrary, the combined bargaining power of the majors and IFPI is incommensurately greater than that of BIEM.*

7. It is also a gross distortion to say that BIEM can insist on any condition because record producers unilaterally depend on BIEM. As the United Kingdom Copyright Tribunal rightly remarked, "Composers need the record companies: without records most composers would not get far these days."[8]

8. Given the bargaining power of the majors, *BIEM is a counterbalancing necessity*: BIEM acts as an association of representatives of composers, lyricists ("creators") and their publishers that negotiates with a counterpart association, IFPI, to ensure fair remunerations for creative persons. For these reasons, the Court of Justice has acknowledged as far back as 1974 that collective copyright management was absolutely necessary to protect the rights and interests of creators.[9]

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6 Decision against BMG Ricordi S.p.a., EMI Music Italy S.p.a., Polygram Italia S.r.l., Sony Music Entertainment S.p.A, and Warner Music Italia S.p.A. See, in particular, §§ 141, 167 and 176 of that decision. The Italian authority imposed high fines. An English translation is available upon request.

7 The complainant's observations to this effect are not pertinent (§ 4.16) or incorrect (§ 5.22: "almost total absence of bargaining power on the part of IFPI members").

8 United Kingdom Copyright Tribunal, 1 November 1991, *British Phonographic Industry Limited v. Mechanical-Copyright Protection Society*, at the end of point C of the opinion.

9 Case 127/73 *BRT v SABAM and Fonior* [1974] ECR 313, § 9.

<u>III. The Complainant's *Leitmotiv* and Flaws</u>

9. The complainant's third basic misunderstanding is the *leitmotiv*, which is wrong and raises fundamental questions about the complaint's position:

10. The complainant suggests that creators' remuneration should follow, like an analogous wave, the downturn fluctuations that result from the Record Producers' commercial policy. In the opinion of the complainant, royalties should follow the discounts that Record Producers grant to retailers in general or on a case-by-case-basis. The complainant feels that Record Producers should not pay royalties to the extent that they have not received "money" from their own customers.[10]

11. This is the language of exploitation: "Give me your creation, leave its commercialization in my hands, and wait and see what earnings remain for you." This language warrants, from the outset, three observations:

    (1) Creators are neither the banks nor the joint-venturers of the Record Producers, and their refusal to assume that role cannot be deemed an "abuse" within the meaning of Article 82 EC. Creators are entitled to fair remuneration for their work, and they cannot be forced to sell that work at any price.

    (2) The correct view, in our opinion, is the opposite: *It would be "abusive" to force creators to be remunerated on the basis of transactions between the majors and third parties which are not only beyond the sphere of influence of creators, but are also not transparent.* In the past, creators have been forced into certain royalty schemes (see points 54 seq. below), which already take account of the majors' commercial decisions or transactions. However, these

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[10] <u>See, e.g.</u>, p. 9, § 1.10, 3rd bullet point: "… it is unfair and abusive to require record companies to pay royalties to BIEM and the relevant BIEM Members on income not received by record companies, …", and § 4.9 of the complaint: "… record companies should not pay royalties on money they do not receive."

forced concessions do not constitute precedents, and creators are by no means obliged to move any further.

(3) The complainant systematically disregards one important fact: To reach agreement, creators have already been forced to accept very significant deductions from their income in order to take account of benefits that Record Producers grant to retailers. These deductions are of a general character (flat percentages of the list price, see points 61 to 67 below). What the creators refuse, however, is: additional deductions from their income, which follow all of the benefits that Record Producers grant to retailers on an unforeseeable and uncontrollable basis, and that are different from transaction to transaction and from retailer to retailer. In the absence of a joint-venturing arrangement, reluctance to accept such an uncontrollable and unforeseeable income basis is the attitude of the reasonable man (or woman), who does not want to work in vain. It is not an “abuse”.

12. The complainant suggests that the majors’ individual dealings with artists (e.g. singers) be the yardstick for royalties that creators receive for copyright licenses.[11] This implies a comparison that is fallacious and unfair. The situations of the artist and of the creator are completely different. In general, artists have to conclude individual deals with the majors, a process in which they are fully exposed to the majors’ superior bargaining power.

B. Facts

13. In our view, a full statement of facts is necessary. The complaint contains numerous misrepresentations, distortions, incomplete statements, and statements out of context.

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[11] See complaint, § 5.13, last sentence and § 5.26.

I. The Purpose and Functioning of Copyright Management Societies

14. Copyright management societies ("societies") were set up by composers, text writers ("lyricists"), and their publishers.[12] Hereinafter, composers and lyricists will be collectively referred to as "creators". However, members may also be publishers, who administer musical works on the basis of rights assigned or licensed to them by creators. It is noteworthy that the majors, in addition to being record producers, also act as publishers. In their capacity as publishers, they are all members of BIEM societies. They dispose of most of the musical copyrights worldwide that are of economical importance.

15. Societies treat repertoires (defined at point 20 below), be it their own or that of the other societies, on a non-discriminatory basis. Members are democratically represented, and in full control of their societies. The main decisions of the societies, and the annual report of the societies, must be approved by the members. The highest decision making bodies (boards and general assembly) consist of copyright owners. Membership is voluntary.

16. Societies are non-profit organizations. Their purpose is to enable copyright owners to receive a fair remuneration for the use of their works by users. The means to obtain such remuneration is collective licensing of copyrights (to be explained below).

17. Although copyright protection may differ according to the applicable national laws, all copyright systems include the right of public performance and the right of reproduction of protected works.[13] Creators may assign to societies their exclusive

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[12] As early as 1860, Richard Wagner was a member of the French Société des Auteurs, Compositeurs et Éditeurs de Musique (SACEM). See Neue Zürcher Zeitung, 27 and 28 July 2002, p. 51. Also, Richard Strauss was instrumental in the establishment of the German Gesellschaft für musikalische Aufführungs- und mechanische Vervielfältigungsrechte ("GEMA").

[13] See Articles 9 and 11 of the Berne Convention for the Protection of Literary and Artistic Works.

right to exercise worldwide the rights of public performance and of mechanical reproduction.[14]

18. Publishers, too, may assign or license copyrights to societies. This possibility has its origin in Anglo-American jurisdictions where creators transfer their right of reproduction to publishers (rather than to societies). Affiliated publishers ("sub publishers") headquartered in the territory of a society may become members in that society and, as such, may assign or license their copyrights to that society.

19. Contrary to the complaint[15], no creator or publisher is required to make copyright assignments to societies.

20. The copyrights which a society administers together are called "the repertoire". Societies exchange their repertoires with other societies, based on bilateral agreements called "reciprocal representation contracts". By way of these contracts, societies give each other the right to grant, within the territory for which they are responsible, licenses in respect of copyrights whose owners are members of the other contracting society. In accordance with the BIEM statutes, reciprocal representation contracts provide for the forwarding of proceeds between societies with only a deduction for administration costs. They do not provide for any exclusivity.

21. In summary, societies have three ways to obtain copyrights: (1) from creators; (2) from original publishers or sub-publishers, and (3) through reciprocal representation contracts with other societies. All societies have almost the entire world repertoire of protected musical works at their disposal for negotiations and licensing.

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14 Contrary to § 1.2 of the complaint, creators in continental Europe do not transfer their copyrights to publishers. The complainant confuses the system in continental Europe with Anglo-American systems.

15 Complaint, § 4.1.

22. Societies negotiate and grant copyright licenses to users. Users are either in the scope of public performance of music (broadcasters, concert promoters etc.), or producers of sound carriers (discs, tapes and cassettes, today in the Union mostly Compact Discs ["CDs"]). Copyright licenses relate either to the performance of music or to the reproduction of works on sound-carriers commonly referred to as mechanical reproduction. In case of on-line exploitation, both the mechanical reproduction right and the performing right are involved.

23. By virtue of their role to protect their members, the tasks of societies further comprise such activities as legislative advocacy, piracy fighting, and auditing of users.[16] In summary, societies protect the material and immaterial interests of their members.

24. Only the system of copyright management societies enables all creators to benefit from the use of their works. If they were left on their own, few would be able to obtain a fair remuneration. Advocate General *Mayras* has described this in memorable language. He said (in French, the language of his opinion):

> « … aucun compositeur, auteur ou éditeur de musique ne peut, en pratique, se soustraire à l'obligation de recourir aux services de SABAM pour exercer ses droits.
>
> En effet, l'exploitation personnelle en est matériellement irréalisable ; elle supposerait des moyens très puissants et exigerait des frais sans nul doute excessifs. …
>
> … l'auteur ou le compositeur, voire même l'éditeur d'œuvres musicales – à moins qu'il ne s'agisse, dans ce dernier cas, d'une entreprise très puissante – n'a pas, en pratique, le pouvoir d'exercer lui-même ses droits. Il ne dispose pas de moyens de contrôler les diverses utilisations qui peuvent être faites de son œuvre. Bien plus, certains utilisateurs de musique : industriels du disque, offices publics ou stations privées de

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16 To describe societies as mere data processors (which the complainant does [see complaint, p. 39, § 5.19: "just a data processing function"]) is similar to describing the majors as passive exploiters of creative talent (which we do not).

> radiodiffusion et de télévision, occupent sur le marché des positions si fortes qu'elles leur permettraient de placer les auteurs et compositeurs dans une situation de dépendance en exigeant la cession de certaines de leurs œuvres, spécialement celles qui, appelées à connaître un grand succès, sont d'une exploitation particulièrement intéressante.
>
> La Commission a elle-même reconnu le danger de cette situation et admis que le fait d'être lié à une société telle que la SABAM assure aux intéressés une protection nécessaire. »[17]

25. On the demand side, relevant users would find it impracticable to deal with individual creators. They prefer societies as "one-stop shops". The majors want collective licensing because this system lowers the cost of obtaining licences. For small Record Producers collective licensing is the only gateway to the market. They may disappear, were it not for the advantages of collective licensing, that is: cost-efficient and easy access to the world repertoire, through only "one shop". Collective Licensing lowers the threshold for newcomers to enter the market. However, to extort impracticably low rates is to jeopardize collective licensing, and to jeopardize collective licensing is a means to put smaller Record Producers out of the market.

26. Through societies, creators can fairly exploit their copyrights: Societies simplify copyright administration, and allow creators to concentrate on their creative work. Societies manage copyrights in the best interest of members (*"en bon père de famille"*). They distribute all income to their members, subject only to a deduction for the cost of administration.

27. In addition to the administrative ease and cost-effectiveness which they procure, societies permit every user to obtain access to the world repertoire of music *free of discrimination or exclusive dealing*.

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[17] Case 127/73 *BRT v SABAM and Fonior* [1974] ECR 313 at 323 to 325.

II. BIEM

28. BIEM was founded in 1929 by music publishers. Today, its members are national societies. The original objective of BIEM was to protect mechanical reproduction rights. BIEM was then entrusted with the administration of mechanical reproduction rights on a European level, which means dealing with the various producers at identical conditions and in the name of the right owners. Since its reform in 1968, BIEM only acts on behalf of its member societies, who manage their respective repertoires. *BIEM's statutes concern only the right of mechanical reproduction.*

29. Like its members, BIEM is a non-profit organization, and is confined to one mission: to ensure fair remuneration for creative persons. The complainant nevertheless states:

> "In the absence of regulatory intervention [sic!], it is to be expected that the BIEM rate will naturally settle at a monopoly rate because this is the rational profit-maximising outcome for the monopoly societies."[18]

30. This is standard language which may befit other cases, but which has no bearing on the case at hand. The complainant misrepresents the specific mission with which BIEM and its members are entrusted and which is not profit-oriented.

31. Since its inception, BIEM has negotiated (and renegotiated) a model contract for the granting of copyright licenses by member societies to users ("the Standard Agreement"; see points 40 seq. below). Contrary to the complaint[19], BIEM does not itself contract in relation to the licensing of mechanical reproduction rights. Nor does BIEM hold any "requisite rights", contrary to the complainant's allegation.[20]

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18 See complaint, § 4.17, bottom of p. 26.

19 P. 5 at § 1.1.

20 See complaint, § 3.1.2.

32. BIEM assists its member societies in their national negotiations. Such assistance is a consequence of Article 7 of the BIEM statutes, which the Commission has approved (see point 34 below).[21]

33. BIEM has always informed the Commission about its essential dealings, also after the expiration of the Standard Agreement (see point 44 below). We refer to the summary of BIEM's contacts with the Commission in annex 2.

34. On 24 February 1998, following a request from the Commission, BIEM notified its statutes to the Commission and applied for negative clearance (and, *"à titre purement conservatoire"*, for an exemption under Article 81 [3] EC). This led to a comfort letter dated 4 December 2000 (COMP/36.941), in which the Commission advised BIEM that its examination of the BIEM statutes:

> "n'a fait apparaître aucun motif pour la Commission d'intervenir en vertu des dispositions de l'article 81 paragraphe 1 à l'égard de l'accord notifié, car cet accord ne restreint pas sensiblement la concurrence au sens de cet article."

35. Article 7 of the BIEM statutes (annex 5 to the complaint) provides, among other things, that member societies must comply with BIEM objectives, statutes and decisions and must follow the Standard Agreement when entering into licensing agreements with users. Article 7 reads, in part:

> "Les Sociétés associées et les Sociétés adhérents s'engagent à mettre tout en œuvre pour atteindre l'objet du BIEM, à s'abstenir de tout ce qui pourrait le compromettre, à respecter toutes les stipulations des présents Statuts et à appliquer toutes les décisions prises par les organes sociaux.
>
> 1) Chaque Société associée s'engage à confier la gérance de son répertoire aux autres Sociétés associées pour leurs territoires d'exploitation.

[21] For the sake of clarity, our plea to reject the complaint (point 239 below) also relates to the fourth point in the orders sought.

…

Les contrats à conclure entre les Sociétés associées seront des contrats de représentation réciproque ou unilatérale, prévus à l'Article 2, 2).

3) La gérance des Sociétés associées comprend toutes les fonctions propres à assurer sur leur territoire d'exploitation le plein exercice et la sauvegarde des droits d'enregistrement et de reproduction mécanique confiés à leur gestion, en particulier:

a) la négociation, la conclusion et l'exécution des contrats avec les usagers, conformément aux contrats types ou, le cas échéant, aux contrats cadres ou aux conditions générales d'utilisation établis par le BIEM; ...“

36. The underlying policy of Article 7 of the BIEM statutes is to provide a homogenous legal environment, which is indispensable to enable societies to exchange their repertoires. Exchange of repertoires, in turn, enables each society to offer users a single licence (*“une licence unique et globale”*), which covers the entirety of the repertoires of all BIEM societies.

37. To this end, all BIEM societies have undertaken to conclude reciprocal representation contracts with all other BIEM societies (see Article 7 [1] 1st paragraph of the BIEM statutes). All reciprocal representation contracts correspond to the same model (see Articles 7 [1] paragraph 3 and Article 2 [2] of the BIEM statutes). All societies follow the Standard Agreement when concluding licencing agreements with users.

38. This has a fundamental consequence without which collective licensing would not be possible: Society A (the assignor or principal) may grant society B (the assignee or agent) a mandate to manage the repertoire of society A. Society A can only do this because it knows in advance the terms and conditions at which society B will carry out this mandate. In particular, the terms and conditions of society B will conform to the Standard Agreement and to the BIEM statutes. Consequently, society A has the certainty that society B will manage the repertoire of society A as

far as possible on the same terms and conditions as society A itself (see Article 7 [3] [a] of the BIEM statutes).[22]

39. This policy (single licence [*"licence unique et globale"]*), and its effects were already set out in the notification of the BIEM statutes to the Commission,[23] which was the basis for the comfort letter (see point 34 above).

III. The Standard Agreement

40. The Standard Agreement stipulates the granting of rights, the obligations of the licensee, and the amounts of royalties for copyright licenses to users. Copyright licenses are granted by the member societies in accordance with the Standard Agreement and the Statutes of BIEM (see point 22 above).

41. Standard Agreements are negotiated between BIEM and IFPI. IFPI today represents about 80 % of the music industry in Europe. The first contract between BIEM and

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22 Exceptions apply in case of mandatory national legislation (Article 7 [4] of the BIEM statutes). Also, a society can apply for a dispensation pursuant to Article 7 (2) of the BIEM statutes.

23 See notification of 24 February 1998 in case COMP/36.941, p. 35:

"Fondamentalement, ces statuts [the BIEM statutes] permettent en effet à chaque société associée de délivrer une licence globale portant sur l'ensemble des répertoires. Il en est ainsi parce que chaque société associée se voit confier le répertoire des autres sociétés. Mais si chaque société associée prend l'engagement de confier son répertoire aux autres, c'est parce qu'elle connaît les conditions dans lesquelles son propre répertoire sera exploité par les autres sociétés associées. En effet, ces conditions sont déterminées par le contrat type portant sur l'ensemble des répertoires, que le BIEM a négocié avec l'industrie.

En d'autres termes, seul l'engagement de chaque société associée de confier son répertoire à toutes les autres garantit la disponibilité de l'ensemble des répertoires auprès de chaque société associée et donc la possibilité pour chacune d'entre elles de délivrer une licence globale et unique. Or un tel engagement n'est évidemment concevable que parce que chaque société est certaine, du fait de la conclusion du contrat type et du respect de ce dernier par les sociétés auxquelles elle confie son répertoire, des conditions dans lesquelles le mandat de gestion de ce dernier sera exercé.

Ainsi, les statuts du BIEM permettent à chaque société d'offrir un produit "nouveau", à savoir une licence globale et unique concernant l'ensemble des répertoires, par rapport à celui que chaque société pourrait seulement offrir en l'absence de statuts du BIEM : son propre répertoire.".

IFPI was signed in 1947. Each new version of the Standard Agreement takes account of changes to market conditions that have occurred. The Standard Agreement is negotiated by BIEM's Management Committee. It must be approved by the General Assembly of BIEM in order to become binding on member societies.[24]

42. The complainant alleges that Standard Agreements are imposed by BIEM no matter what the market conditions (often incorrectly referred to as "commercial usage") may be.[25] This is a gross misrepresentation, as the opposite is true. As we demonstrate below, creators have many times been forced to accept deductions in favour of the Record Producers or to lower minimum royalties.

43. The complainant also contends that the Standard Agreement has limited technical progress and consumer choice.[26] This is another misrepresentation, drawn on the abstract wording of Article 81 (3) EC, but without a substantiated basis in the complainant's statement of facts.[27] [28]

44. The latest Standard Agreement dates back to 1975. It has been renegotiated seven times. The last renegotiated version is reflected by Amendment No 7 which was

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24 Pursuant to Article 7 (4) of the BIEM statutes, the societies may depart from the standard contracts established by BIEM to the extent that they are subject to legal provisions of a compulsory nature. That is the case in the United Kingdom. The rate in Ireland results from negotiation alone. That this rate was fixed by a tribunal (complaint, p. 4, footnote 1) is a misrepresentation.

25 See, e.g. complaint, § 1.9., 1st sentence.

26 See complaint, p. 8, 2nd sentence.

27 At the request of the Commission, we would be pleased to submit details. For example, BIEM has granted royalty breaks to promote *technical progress* (the introduction of the music cassette and later the CD). A decreased royalty regime still applies today to Minidiscs and Digital Compact Cassettes (DCC).

28 The sole cause for limitations of *consumer choice* is the majors' decision to develop sales volume with supermarkets offering little choice, and to decrease business with small retailers offering a wide choice. Neither logic nor the complainant's statements suggest any link between the Standard Agreement and consumer choice. The majors' volume orientation will be discussed at points 95 seq. below.

signed on 30 June 1998. See annex 2 to the complaint. This version expired on 30 June 2000. On 29 June 2000, BIEM sent a circular to its members in which it recommended to continue with the application of the Standard Agreement. This was to avoid a vacuum, and to enable all concerned to stay in business. All Record Producers continued on that basis, as at present.

45. For ease of reading, a consolidated version of the Standard Agreement (a version that incorporates all seven amendments and all seven annexes) is enclosed as annex 3.

46. The Presidents of BIEM and IFPI had several informal discussions in respect of the Standard Agreement. Formal negotiations only began on 19 February 2002 in London. The meeting was held at the request of BIEM. BIEM proposed an anti-piracy fund and a straightforward extension of the Standard Agreement. IFPI rejected this as insufficient.[29] This first round of negotiations did not lead to a satisfactory result for either party. The negotiations have not been formally closed by either party.

IV. The Use of the Standard Agreement by Member Societies

47. After approval by BIEM's General Assembly (see at point 41 above), Standard Agreements become a matter of further negotiations between BIEM's member societies and the corresponding National Group of IFPI. These two parties examine the Standard Agreement under the applicable national legislation. Article 7 (4) of

[29] The internal minutes of the BIEM / IFPI negotiating Committee read as follows: "IFPI considers BIEM's proposed contribution as a 'drop in the ocean' compared to millions of dollars it invests to reduce piracy. Mr. Berman qualifies the proposal as very difficult if not impossible to accept, as it does not outweigh the areas where the industry believes it is overpaying. It was expecting some additional concessions from BIEM. … Mr. Vervoord reiterates the proposal as described above, and IFPI asks BIEM to confirm that it is not prepared to accept changes on the other subjects raised by IFPI. It is then considered that the subject of the standard agreement *for this meeting* is exhausted, and that IFPI needs to reflect on the situation after the meeting it will have with some societies in Europe on the subject of on line exploitation." (emphasis added).

the BIEM Statutes allows deviations from the Standard Agreement to the extent required by mandatory national legislation. In addition, the relevant member society and the corresponding branch of IFPI negotiate complementary agreements to the extent provided by the Standard Agreement. These complementary agreements concern the following:

(1) Article V (7bis): export royalties for exports to non-European countries other than the United States and Canada,

(2) Article V (9bis): deduction for returns in case of exports,

(3) Article V (11): small quantity exports being treated as national sales,

(4) Article V (18 bis): fixed percentage deductions, or any other appropriate system of deduction, for returns of sound carriers,

(5) Article V (24): exempt copies for promotion,

(6) Article V (25): conditions for TV-advertised products,

(7) Article VI (2) : prices serving as basis for the calculation of minimum royalties.

48. On the basis of the Standard Agreement, member societies conclude licensing agreements with Record Producers. These licensing agreements follow the Standard Agreement and the national agreements concluded within the framework of the Standard Agreement. The conditions of licensing by BIEM member societies are therefore substantially[30] the same for all Record Producers. This rules out any discrimination between Record Producers or exclusive licensing.

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[30] The term "substantially" only reflects the complementary agreements set out in point 47 above, which are concluded within the framework of the Standard Agreement.

49. Once a society has concluded a licensing agreement with a Record Producer, this producer provides the society with label information. The society uses this label information to identify the reproduced works, and to grant the necessary licences for these works ("works identification").

50. The Record Producer further provides the society with reports on its sales of records and their list prices ("PPDs", to be discussed at points 56 to 60 below). The society audits the accuracy of these reports.

51. The works identification together with the sales reports and the PPD constitutes the basis on which the society prepares invoices to the Record Producer. The invoices set out the royalties due for the mechanical reproduction of each of the reproduced works. They are sent on a quarterly or on a six-monthly basis.

52. The society distributes royalties, which the Record Producer pays, to those copyright owners whose works are included in the invoice.

53. This procedure, based on extensive documentation, follows the conclusion of the licencing agreement and is called "rights clearing and invoicing".

V. The Determination of Royalties

54. The complaint is directed against the royalty of *9,009 % of the Published Price to Dealers ("PPD")*. That *is* indeed *the standard net royalty*. However, the complainant concedes that it receives 2,5 % of the royalties paid by it from the central licensing society MCPS under a central licensing agreement with MCPS; thus the net amount (if one would take this into account) would be 8,78 %.[31]

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[31] See complaint, p. 28, at the end of § 5.1 (iii).

55. The complainant's description of royalty calculation is partly incorrect or unintelligible.[32] Therefore, we give a full account of the current situation:

1. The Calculation Method: the Published Price to Dealers

56. Under the first Standard Agreement between BIEM and IFPI, concluded in 1947, the mechanical royalty rate was 8 % of the recommended retail price. For a short period of time, in the beginning of the 1980's, the royalties were calculated on the basis of the list price increased by a mark-up for the dealer margin.

57. In 1982 and 1983, the Commission requested BIEM to use another calculation basis for royalties, namely the price list for dealers, called "Published Price to Dealers" ("PPD"). The Commission argued that royalties on the basis of average retail price were widely different depending on the country of sale. The Commission also found that Record Producers had no influence on the average retail price.[33] According to the Commission, if royalty calculation was based on the PPD rather than on the average retail price, then Record Producers could monitor royalties as one of their cost factors.[34]

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32 See complaint, p. 21, § 4.7.

33 See XIIIth Report on Competition Policy (1983), §§ 149 and 150.

34 In a letter to BIEM dated 17 June 1982 (Cases IV/00.0366 – BIEM / IFPI and IV/30.467 – CBS / SIAE), the Commission advised that: "[T]he basis of the royalty is an artificially–calculated and therefore fictitious retail price. This 'reconstructed retail price' could often be inadequately related to the reality of prices actually realized, and tends to prolong and maintain traditional and unrealistic price structures as well as differences between markets." Commitments by the societies followed to take care of this concern, and in a letter to BIEM dated 24 November 1983 (Cases IV/00036 BIEM / IFPI and IV/01255 GEMA/STEMRA), the Commission informed that it had closed its procedure. As far as royalty calculations were concerned, the Commission wrote in this last letter: "Les sociétés ont en outre déclaré qu'en ce qui concerne le calcul des redevances d'auteurs lors des ventes dans la Communauté, ils ne se réfèreront plus au prix de vente au détail du pays de la destination, mais exclusivement au prix de liste pour le commerce au détail publié par le producteur. Cette référence nouvelle garantit que le producteur n'aura plus désormais à payer de redevances sur une base qui échappe à toute influence directe de sa part, comme cela avait été le cas dans le système antérieur (référence aux prix de vente pour le commerce au détail)".

58. Further to this request, BIEM and IFPI agreed as follows: On the one hand, a lower price was introduced as the calculation basis for royalties (the PPD instead of the average retail price). On the other hand, a higher rate was introduced, namely 11 % (instead of 8 %). This change became effective as of 1 November 1985. Contrary to the complainant's allegations, this resulted from negotiations between BIEM and IFPI. *It did not result from mathematical deduction.* By way of example, this is demonstrated by versions changes of parameters (like packaging deductions) at that time.

59. The 1985 agreement is incorporated in the following basic rules of the Standard Agreement (rules on details omitted from the following citation):

> "Article V – calculation of royalty
>
> (3) The Producer shall pay to the Society for each disc, tape and cassette reproducing one or more works of the repertoire of the Society a royalty rate of which and the domain of application of which are fixed in Annex IV of the present contract.
>
> (4) Subject to paragraph (5) below, the royalty shall be calculated on the highest price appropriate to the copy in question as published by the Producer (PPD) with a view to retail sale on the day of outgoing from the depot in the list mentioned in Article VII (4) c). …"
>
> "ANNEX N° IV
> Royalties
>
> The royalty provided for in Article V (3) is as follows:
>
> (1) In Continental Europe, including Turkey, the rate of royalty per copy is 11 % of the price determined in accordance with Article V (4). …".

60. The introduction of the PPD as the calculation basis had the following effects:

(1) Creators' income depends on factors which are transparent and not on factors which are beyond the sphere of influence of creators (such as transactions between producers and retailers).

(2) Royalties are inexorably linked to the market. This is because they are calculated as a percentage of the list price (the PPD), which is a market-driven parameter. Royalty income automatically follows changes of the PPD and of the sales volume.

2. Consecutive Deductions, and their forced Character

61. Rates have continuously decreased, as the complainant has acknowledged.[35] The standard rate is still 11 % of the PPD.[36] However, in its negotiations with IFPI, BIEM was forced to accept several important deductions: a deduction for packaging and a deduction of invoiced discounts.

(1) The *deduction for packaging* amounts to 10 % of the said 11 % of the PPD, and leads to a rate of 9,9 % of the PPD. See Article V (23), 1st sentence of the Standard Agreement.

(2) In November 1985, *an adjustment for invoiced discounts which are usually applied* (by Record Producers to retailers) was introduced. This adjustment was flexible but could amount to up to 4 % of 9,9 % of the PPD. The exact percentage was to be negotiated by the societies at the national level. This brought the standard rate down to 9,504 % of the PPD. Very shortly after the agreement of November 1985, the 4 % rate was set as a flat rate deduction.

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35 See complaint, § 5.15: "Record companies are paying lower standard rates than previously."

36 The complainant insinuates that the standard rate is 9,009 % of the PPD which creates the impression that deductions only begin below 9,009 % of the PPD. See, e.g. § 1.3 of the complaint. That is misleading. The standard rate is 11 % of the PPD, and the net rate of 9,009 % is the result of significant deductions, to be explained in the main text after the present footnote.

(3) On 1 October 1992, the bandwidth of the adjustment for invoiced discounts which are usually applied was enlarged from 4 % to 6 %. This brought the standard rate down to 9,306 % of the PPD.

(4) On 1 July 1997, the adjustment for invoiced discounts which are usually applied was enlarged from 6 % to 9 %, which brought the standard rate down to 9,009 % of the PPD.

62. These deductions are enshrined in Article V (4) 2nd sentence of the Standard Agreement.

63. In 1989 and 1990, BIEM agreed to transitory deductions of 15 % and 10 % respectively for Compact Discs. These were a contribution by the creators to the introduction of new technology. They highlight BIEM's openness for negotiations on the occasion of breakthrough developments, such as new technology. However, by no means do they constitute a precedent or reflect a principle.

64. Since 1985 (when the PPD basis was introduced as the calculation basis), BIEM members have not applied mark-ups. The allegation of mark-ups in the complaint[37] is without basis after 1985. It is a straightforward misrepresentation.

65. For BIEM, 9,009 % of the PPD is a bottom line. The 9,009 % net rate results from a long series of significant concessions that the majors, through IFPI, have forced on the creators. BIEM cannot accept that each round of negotiations with IFPI should constitute an automatic reason for further losses of income.

66. In BIEM's judgment, the 10 % deduction for packaging is highly disproportionate in relation to the cost of the packaging. In the negotiations on amendment No 2 of

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[37] Complaint, p. 9, 2nd bullet point; p. 21 at § 4.7; §§ 5.10 to 5.12; p. 52 ("orders sought"), 2nd bullet point at (i) ("level of mark-up") and annex 8 to the complaint.

the Standard Agreement, IFPI had insisted on an increase of this deduction, claiming that it was common in contracts between the majors and artists.[38] Moreover, the disproportion of the packaging deduction is evidenced by letters from IFPI where they accepted that the packaging cost of the most important formats was below 10 % of PPD.

67. We mention this in order to illustrate two points. Firstly, the continued pricing "diktat" of IFPI disproves the claim of BIEM having a superior bargaining power. Secondly, *BIEM is by no means satisfied with all provisions in the Standard Agreement*: The complainant cannot attempt to eliminate selected provisions, which it dislikes, and maintain all the others. In response to such a cherry-picking attempt, BIEM would have to put all provisions at issue which are unfavourable for BIEM's members. To touch at one part of the equilibrium is to destroy it as a whole. We shall revert to this point in our conclusions.[39]

VI. The Allowance for Discounts: Flat Rate Deduction, Cost-Effectiveness and Ease of Control

68. The foregoing points make clear what the complainant systematically obscures: *There is already an important deduction for discounts*. [40]

69. The deduction for discounts is *general* in that it is expressed as *a flat percentage* of the PPD. It is not affected by individual discounts which Record Producers

[38] The Minutes of the BIEM / IFPI Negotiation Committee (London, 11 May 1983) show the following: "Ensuite, M. GOLDSTEIN a indiqué que le principe des déductions pour pochettes et cassettes devait absolument être maintenu parce que les contrats entre producteurs et artistes comportaient le même système de déduction, à quoi M. WILLEMSEN répond que le BIEM n'a jamais négocié pour le compte des artistes, de sorte que l'IFPI ne peut lui opposer une situation à laquelle il est totalement étranger. "

[39] Below at points 241 and 242.

[40] This adds to the equally important deduction for packaging.

negotiate with specific retailers on a case-by-case basis, and which may vary from transaction to transaction and from retailer to retailer (e.g., special incentives to enlarge the sales volume of a Record Producer, early payment bonuses, or end-of-year bonuses).

70. The general character of the allowance presents two advantages:

(1) The calculation method is simple, transparent, cost-effective and easy to audit. If the calculation of royalties were based on a system taking account of all individual discounts, then societies would have to verify all these discounts in each case. Such verification would increase the administrative burden on societies to an impracticable level. Societies would incur added costs for auditing, and creators would lose income without countervailing benefit. Details are set out in a letter dated 31 March 2000 from BIEM's president, Mr. Cees Vervoord, to IFPI's Chairman and Chief Executive Officer, Mr. Jason Berman (annex 4).

(2) *Creators' income does not depend on factors that are not transparent, secret and hidden, and beyond the sphere of influence of creators.* Among these factors are specific dealings between Record Producers and retailers, some of which involve considerable risk. On the PPD basis, creators' income is foreseeable and controllable because it is not contingent on such specific dealings.

(3) The PPD calculation basis ensures equitable allocation of income to creators. By way of illustration, a record with a work of creator A may be sold to the consumer at a reduced price, but on the condition that the consumer buys a record with a work of creator B at full price. Despite this situation, creator A and creator B would be remunerated according to the same terms.

VII. Minimum Royalties and Maximum Track Numbers

1. Purpose

71. The Standard Agreement provides for minimum royalties and for maximum track numbers per record. Both devises follow the same purpose: to protect the creator's income against dilution. Both ensure that the creator receives *fair remuneration, whatever the commercial or technical conditions may be on which Record Producers mechanically reproduce the creator's work and sell the ensuing records.* Minimum royalties and maximum track numbers reflect the freedom of every economic operator not to sell his (or her) goods, services or intellectual property at any price.[41]

72. In particular, minimum royalties and maximum track numbers protect the creator (1) against extremely low list prices ("PPD"), (2) against extremely low income per track, and (3) against possible mismanagement by Record Producers for which the creator is not responsible.

73. Minimum royalties and maximum track numbers always have been the subject of negotiations between BIEM and IFPI. They have been adapted several times by way of negotiations between these two associations, each time in favour of the Record Producers. BIEM recalls that these adaptations neither constitute precedents nor reflect a principle. BIEM rejects the idea that each new round of negotiations should automatically constitute a reason for further concessions to the Record Producers.

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[41] A comparison may be made with minimum wages for labour.

2. Minimum Royalties

74. The basic rule on minimum royalties is set out in Article VI (1) of the Standard Agreement in connection with the first paragraph of Annex IV to the Standard Agreement: The minimum royalty shall be two thirds of the royalty of 11 %, such 11 % royalty to be calculated on the basis of the PPD most generally practiced by the members of IFPI in each country for each type of sound carrier ("the Reference Price"). Pursuant to Article VI (2) of the Standard Agreement, the Reference Price shall be agreed at the level of BIEM members, that is: between the relevant member society and the corresponding National Group of IFPI. *This is the normal regime*.

75. The two thirds minimum rate is based on a concession by BIEM: It is a reduced minimum rate in comparison with the minimum rate under the original 1975 version of the Standard Agreement, which was fixed at three quarters.

76. *In addition to the normal regime, there is a special regime providing for a still lower minimum royalty.* This lower minimum royalty is called "minimum budget royalty". It is limited to 57 % of the normal minimum royalty. It takes account of cheap re-releases of records.

77. The rule currently applicable is set out in Article VI (1 bis) of the Standard Agreement. It provides, in essence, that in the case of records which have been re-released not less than 1 year after the original release and which are priced at 35 % below the original price or less, the minimum royalty shall be 57 % of the normal minimum royalty, that is: 57 % of two thirds (66,66 %) of the royalty calculated on the basis of the Reference Price. However, no minimum budget royalty shall be less than 9,009 % of the PPD applicable to the relevant re-released records.

78. The special regime was introduced in 1992, by virtue of Amendment No 6 to the Standard Agreement. Under Amendment No 6, the minimum budget royalty was 70 % of the normal minimum royalty. In 1998, by virtue of Amendment No 7, the

minimum budget royalty was reduced from 70 % to 57 % of the normal minimum royalty. The introduction of the minimum budget royalty and the subsequent reduction of this royalty were concessions by BIEM. These occurred in addition to the aforementioned concession which consisted of a reduction of the normal minimum royalty.

79. The complainant conceals the special regime. In vague terms it claims that the normal minimum royalty applies to cheap second releases and that, in respect of such releases, the normal minimum royalty is too high.[42] This is misleading because there is a special regime for cheap re-releases.

3. Maximum Track Numbers

80. The relevant rules are set out in Article VI (5) to (10) of the Standard Agreement. *It is important to note that these rules do not prevent Record Producers from manufacturing any format of records.[43] They only provide a proportional increase of royalties.* To the extent that the contents of a record exceed certain thresholds (e.g., a threshold number of "tracks"), the royalty is increased in the same proportion. In other words, the said rules provide for a form of minimum royalties.

81. The Standard Agreement provides for two thresholds: firstly, the playing time of a record and secondly, the number of complete protected works (or fragments of such works) on one record. Both thresholds are expressed by way of precise technical specifications, which are listed in Article VI (5) to (5 quater) of the Standard Agreement. These specifications correspond to market categories of records. Together, they represent a scale of categories, from which Record Producers can

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42 See complaint, § 5.26.

43 There is one exception: If a reproduction is intended to be fragmentary, this fragmentation requires consent by the relevant society. See Article VI (10) of the Standard Agreement.

choose. This disproves the complainant's allegation that maximum track numbers are not adapted to technical constraints or market conditions.[44]

82. To the extent that a Record Producer exceeds a threshold, the royalty is increased by the same proportion. To this effect, the basic rules provide (rules on details being omitted from the following citation):

> "Article VI
> …
>
> (6) If the Producer wishes to reproduce on the same disc, tape or cassette a *number* of protected works or protected fragments exceeding that mentioned above, the total royalty for the disc, tape or cassette in question shall be increased in the same proportion, …
>
> (7) If the *playing time* of a disc, tape or cassette exceeds the playing time fixed above by more than sixty seconds, the total royalty due for the disc, tape or cassette shall be increased in the same proportion."
>
> (emphasis added)

83. The complainant alleges that the aforementioned rules make it more difficult for it to allocate tracks to certain formats of presentation. The complainant is wrong for three reasons:

84. Firstly, the allegation is incorrect factually. The technical specifications in the Standard Agreement correspond to market categories.[45]

85. Secondly, difficulties may well stem from other factors than maximum track numbers. For example, the complainant claims that maximum track numbers oblige it to create albums with more than one record, which, according to the complainant,

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44 See complaint, beginning of § 5.41.

45 We do not deem it necessary to go into micro-economic considerations, on which the production of special formats (such as albums) are based – even though we would, of course, do so upon the Commission's request.

raises the PPD and hence the royalty.[46] This is a false pretense. A double album leads to an increase of manufacturing and packaging costs. The amount of this increase is greater than the amount of additional royalties due for additional works in the album. This illustrates that commercial decisions of the majors (such as the decision to create a double album) do not mainly depend on maximum track numbers, but depend on different considerations (such as the marketing prospects of an album and the additional costs of manufacturing and packaging). *The final price of records is influenced by many other factors than royalties before they reach the market.*

86. Thirdly, as we shall elaborate in our legal observations, mere commercial difficulties (assuming that they are proven) do not constitute a reason to challenge an agreement (here: the agreement on maximum track numbers) on a theory of "abuse" or "unfairness". The entire concept of agreements, and of freedom of contract, would become futile if agreements had to be adapted to one party's wishes each time that this party finds that compliance with the agreement would not fit to its commercial designs.

VIII. Lack of Correlation between Royalties and Consumer Prices

87. Contrary to the complainant's allegation[47], decreases of royalties have never impacted on consumer prices. This is shown by four points:

88. Firstly, annex 5 ("10 Year Development of CD Album Pricing") shows that there is *no empirical interrelation* (let alone a linear interrelation) between royalties and retail prices. Royalties decreased from 9,504 % in 1991 and are at 9,009 % since 1997. Nevertheless, from 1991 to 2001, retail prices in Austria, Finland, Italy,

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[46] See complaint, § 5.37.

[47] Complaint, p. 9, § 1.10, 3rd bullet point, and last paragraph on p. 11.

Spain, Sweden and the United Kingdom rose, whilst retail prices in Belgium, Denmark, France, and the Netherlands dropped, and retail prices in Germany first dropped and then rose. Annex 6 ("Comparison of Warner and BMG's German PPD of a Full Price CD with BIEM rates") further shows that the PPD of Time Warner and of BMG, respectively, have developed independently from the royalty under the Standard Agreement.

89. Secondly, *royalties* represent *only a small part of consumer prices*. Annex 7 ("Quelle est la composition moyenne du prix d'un disque ?") sets out a breakdown of CD pricing by component costs. The share of creators in consumer price is roughly between 6 % and 7,5 %, as is shown by the position "droits d'auteur" in annex 7.

90. As a result of the small share of royalties in CD pricing, consumer prices are the same for (1) records carrying copyrighted music and whose production, consequently, requires a copyright license and the payment of a royalty, and (2) records carrying music that is not copyrighted and whose production, consequently, does not require such payment. In annex 8, we submit records bought in the Paris FNAC on the same day. Those with copyrighted music bear exactly the same price as those with non-copyrighted music.[48]

91. Thirdly, *royalties are substantially the same in each Member State* because they are calculated in accordance with the same method (that set out in the Standard Agreement). *By contrast, average retail prices vary considerably from Member State to Member State.* We refer to annex 5 ("10 Year Development of CD Album Pricing"), and to annex 9 ("PPD Comparison in Europe")[49]. This evidence makes it

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48 The music of Claude Debussy in annex 8 is not copyrighted any more, whilst the music of Olivier Messiaen, also in annex 8, still is. A CD with music of Claude Debussy costs exactly the same (at the time of purchase € 13,72) as a CD with music of Olivier Messiaen.

49 In annex 9 ("PPD Comparison in Europe"), MCPS is the British, SDRM the French, and STEMRA the Dutch society.

clear that consumer prices are determined by the majors, and do not depend on royalties.[50] [51]

92. Fourthly, the complainant requests lower royalties to grant higher discounts to retailers. However, to BIEM's knowledge, *retailers do not automatically pass* such *discounts on to the consumer* (by way of lower prices of CDs). Retailers alone decide what to do with the benefits derived from discounts.

93. These four points show that there is no "economic rule" whereby further decreases of royalties (which the complainant requests) would cause a decrease of consumer prices. By contrast, our first point is economic experience to the effect that consumer prices develop independently of royalty decreases. As stated (point 85 above), *the final price of records is influenced by many other factors than royalties before they reach the market.* The complainant has not provided any economic evidence to support its thesis of consumer price impact.

IX. No "Cross Price Elasticity"

94. Sound-carriers are luxury products in the sense that few consumers depend on these products for their existence or economic operations. Consequently, if consumers find records too expensive they simply do not buy them. There is no "cross price elasticity": Consumers do not react to price increases by switching to an interchangeable product. It follows that *consumer prices are determined by the*

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50 There may be a case against the majors on whether retail price differences between Member States can be justified under the competition rules. See *Christophe Forax*, spokesman of Commissioner *Reding*, La lettre du disque n° 343 of 25 June 2002: "Si le prix du disque est plus cher en France que dans d'autres pays,…, il faut peut-être d'abord se tourner vers les maisons de disques pour y remédier."

51 The special royalty scheme for the United Kingdom was accepted by BIEM on the basis of Article 7 (4) of the BIEM Statutes (consequently also for Ireland).

majors and by the retailers. These aim at the maximum that, in their expectation, consumers are prepared to pay.

X. The True Cause of the Complainant's Dissatisfaction: The Volume-Policy of the Majors

95. The dissatisfaction, which is at the basis of the complaint, stems from the majors' commercial policy in relation to retailers. It does not stem from the provisions on royalties which govern the relation between Record Producers and societies.

96. The complainant wrongfully claims:

> "… the high level of discounts which record companies are required to pay are a direct result of ever increasing commercial pressure from retail customers. The market reality today is that distribution lies in the hands of very powerful customers, who demand *hefty discounts* from the record companies … In order to meet these competitive forces on the downstream market, Universal has moved towards a more flexible pricing structure, involving higher discounts on PPDs being given to retailers." (complaint, § 5.14, emphasis added).
>
> "… the record producers have, as a result of the increasingly competitive nature of the market for sound carriers, been required to spend more in order to achieve sales." (complaint, § 5.20)
>
> "… the increasing use of lower price categories to extend record sales" (complaint, § 5.30, top of page 44).

The complainant further incorrectly claims that the majors are obliged:

> "to lower and be more flexible with their prices" (complaint, p. 9, 3rd point, 5th line)

97. *The allegation of pressure from retailers is a legend.* As the Commission has determined in *Time Warner / EMI, retailers have low bargaining power vis-à-vis*

the majors.[52] This shows a differential of bargaining power. It rules out that retailers have power to extort "hefty discounts" from a group consisting of the five most powerful media conglomerates in the world.

98. In reality, the majors' dissatisfaction is caused by the majors themselves: *These conglomerates have made it a priority to enlarge their sales volumes by way of give-away pricing*. For example, the majors enable retailers not specialized in music (e.g. supermarkets) to use sound-carriers as a means to generate shop traffic in other fields than records (e.g., consumer hardware). In France, supermarkets (e.g., Auchan, Carrefour, and Champion) offer limited ranges of Compact Discs at hugely reduced prices. In Germany, retailers like Media Markt offer large volumes of record below their purchase price[53] in order to create business with consumer hardware.

99. As the Commission has determined[54], this policy of increased volumes, financed through discounts, stems from a concerted practice: All the majors basically use the same structure of discounts. The Commission has held, in essence, that the fight for market share limits the diversity of offering to the public by the retailers.

100. *To finance their volume-policy, the majors undertake to shift losses to the creators ("beggar-thy-neighbour"). That, rather than stipulations on royalties, is the cause for the present complaint*[55].

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52 *Time Warner / EMI id. (footnote 5 above)* §§ 42 and 57; see also § 50.

53 This practice is not prohibited by German law.

54 Time Warner / EMI *id.*, §§ 38 and 52.

55 As an aside, the majors' volume policy endangers small Record Producers who cannot sustain such a policy. Moreover, the majors are undercutting the small record producers through a volume of discounts which these small producers cannot meet. As stated (above at point 25), for small Record Producers, collective bargaining is the only gateway to their market.

101. In the interests of the creators, BIEM hopes that the present proceedings will provide the majors with a basic insight: that in a market economy the normal reaction to decreasing turnover should be increased efforts to compete. In the sector here concerned, the key to competition is innovation: the search and development of talent, and the concept of better marketing and distribution methods. Strangely, the complainant, which prides itself to be "at the forefront of innovation"[56], in its complaint does not mention competition through innovation. Instead, it asks the Commission to support its "beggar-thy-neighbour"-policy.

102. We conclude, already at this stage, that upon the scarce facts presented by the complainant, no rule or policy of Community law requires creators to share losses resulting from commercial decisions, the Record Producers, over which creators have no control. This is a major point, which we shall develop in our following legal observations.

C. LEGAL OBSERVATIONS

I. The Limited Subject Matter of the Complaint

103. We note that the complainant has not raised any objections against BIEM and its member societies as such[57], or against the Standard Agreement and collective licensing as such.[58] This is understandable because the complainant itself benefits from collective licensing.[59] Also, *the complainant expressly states that it does not*

56 See § 2.1.4 of the complaint.

57 Admitted at the end of § 1.4 of the complaint.

58 Admitted at the beginning of § 1.4 of the complaint.

59 As a Record Producer, the complainant relies on the efficiencies of collective licensing. As a publisher, the complainant relies on societies for the administration of its own copyrights. As licensor of its own neighbouring rights in sound recordings, it relies on its own collective licensing society. The complainant has acknowledged the important role of collecting societies by allowing its

object to the PPD as a calculation basis.[60] Finally, the complainant nowhere questions minimum royalties and maximum track numbers as such.[61]

104. What remains is a *"fishing expedition"*, blurry as to its objectives and contradictory in its argument. We address this situation by focusing on four points: (1) the standard rate; (2) deductions for retail discounts; (3) minimum royalties; and (4) maximum track numbers (hereinafter collectively referred to as "the Four Points").

105. If, in the opinion of the Commission, other points are relevant, we would be pleased to address these. We would be grateful if the Commission made us aware thereof and provided us with an opportunity to comment.[62]

II. Procedural Shortcomings

1. Lack of Legitimate Interest[63]

106. The complainant pursues *no defined interest* – that is: an interest phrased with such precision that the Commission can test whether it is well founded. The complainant avoids any statement as to what precisely, in its opinion, should be brought to an end in terms of Article 3 (1) of Regulation No 17.

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publishing entity to have its rights administered by the various national societies comprised by BIEM.

60 See complaint, top of p. 33, § 5.5, 4th line: Universal "is not advocating the PPD as a basis for calculating the royalty is inherently unfair or anti-competitive and therefore, some alternative basis should be used."

61 This emerges, in particular, from the 4th bullet point in § 1.10 of the complaint.

62 For example, we do not see the relevance of "on-line" marketing to which the complainant alludes (complaint, § 1.15). The complainant has failed to state any verifiable objections against BIEM in this regard.

63 Article 3 (2) (b) of Regulation No 17.

107. Interestingly, IFPI was perfectly aware of the preparation of the complaint. It is strange that Universal rather than IFPI has lodged the complaint. Firstly, Universal has made no effort whatsoever to raise its concerns directly with BIEM before lodging its complaint, thereby sparing the Commission the necessity of action under Regulation No 17. secondly, we interpret the complaint as a means to use the Commission as a negotiation facilitator: Either the complainant wishes to strengthen IFPI's hand, or the majors are divided among themselves.

2. Unavailability of the Relief Sought

108. As stated (points 1 to 3 above), the Commission, acting as a competition authority, does not have a role as a price-determining regulator ("*positive relief*"). Pursuant to Article 3 of Regulation No 17, the Commission only investigates infringements, and requests enterprises to bring infringements to an end ("*negative relief*").[64] It is one of the complainant's self-contradictions, observed in point 104 above, to pay lip service to the principle of negative relief, on the one hand[65], but to ask the Commission for regulatory price determination, on the other hand.[66]

III. Lack of Community Interest

109. In our view, neither competition policy nor the circumstances of the case require an investigation. To show this, we will make two points:

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64 In a letter dated 28 May 1982 to MCPS (Case IV/30.370 – GEMA / MCPS), the Commission advised that: "It is neither within the competence of, nor intended by, the Commission to determine how, on what, or at which rate, sound record producers are to pay royalties for production and distribution of protected works." The principle of *"pouvoirs d'attribution"*, to which the aforementioned letter refers, is enshrined in Article 5 (1) EC.

65 See, e.g., complaint, p. 5, § 1.4, 2nd sentence.

66 The most revealing statement to this effect is the first point of the „orders sought". The complainant requests "A declaration that the Standard Rate is too high; …".

(1) Collective licensing leads to results similar to the licensing of a Europe-wide copyright (which does not presently exist).[67] The key to this result is the single license (*"licence unique et globale"*) which every BIEM society can grant and which covers the entirety of the repertoires of all BIEM societies. In our view, such a Europe-wide solution is in the Community interest. Therefore, we suggest that Commission involvement with the system should be limited to the necessary minimum.[68]

(2) The existing system is self-regulatory. The questions raised in the complaint can be fully dealt with through negotiations or by national courts or authorities.

110. *As to the first point*, copyrights are territorial in scope and regulated exclusively by national laws differing from Member State to Member State. However, the existing system solves much of the ensuing problems:

(1) Users deal with only one contractual partner (a society) in order to obtain access to the whole world repertoire of music.

(2) Societies do not need to set up organizations outside their territories, but can rely on local societies with whom they conclude reciprocal representation contracts. There is no need for multiple negotiations between individual creators and individual users. This leads to simplicity and cost-effectiveness.

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67 An exception applies to the United Kingdom because of the power of the United Kingdom Copyright Tribunal as a regulator.

68 The requirement of "necessity" is anchored in the principle of proportionality set out in Article 5 (3) EC.

(3) Each society provides a Europe-wide bundle of copyright licenses. That comes close to one Europe-wide copyright license (which does not presently exist).[69]

(4) Licenses are subject to uniform terms and royalties throughout the Community.[70] In particular, terms and royalties do not vary according to whether licenses relate to the repertoire of the licensing society or to that of another society (to which the licensing society has access pursuant to a reciprocal representation contract). Owing to this, there are no royalty differences from Member State to Member State, as far as mechanical rights are concerned.

(5) Every user enjoys non-discriminatory access, on a non-exclusive basis, to all licenses within the world repertoire.

111. In *Tournier*, the Court recognized that this Europe-wide system is beneficial – and far from being restrictive of competition within the meaning of Article 85 (1) of the EC Treaty (now Article 81 [1] EC).[71] In *SABAM*, Advocate General *Mayras* concluded that copyright management societies are necessary in order to counterbalance the power of the music industry and to protect creators.[72] Finally,

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69 See footnote 68 above.

70 See the findings in Case 395/87 *Ministère Public v. Tournier* [1989] ECR 2521, § 17.

71 *Tournier, id.,* §§ 19 and 20; *idem* Case 395/87 *Lucazeau and others v SACEM and others* [1989] ECR 2823, §§ 13 and 14. § 19 in *Tournier* and § 13 in *Lucazeau* are phrased as follows: “Dans ces conditions, il apparaît que les contrats de représentation réciproque entre sociétés de gestion visent un double but : d’une part, ils cherchent à soumettre l’ensemble des œuvres musicales protégées, quelle qu’ en soit l’origine, à des conditions identiques pour les usagers établis dans un même Etat, conformément au principe retenu par la réglementation internationale ; d’autre part, ils permettent aux sociétés de gestion de s’appuyer, pour la protection de leur répertoire dans un autre Etat, sur l’organisation mise en place par la société de gestion qui y exerce ses activités, sans être contraintes d’ajouter à cette organisation leurs propres réseaux de contrats avec les utilisateurs et leurs propres contrôles sur place.” The complainant acknowledged this; see complaint, § 1.4 („pan-European licensing and management of mechanical rights“) and § 1.5, 3rd line: “… a pan-European model can produce a positive, competitive outcome.”

72 See the quotation in point 24 above.

the Commission, through Commissioner *Monti*, in 1997 emphasized that the existing system is fully justified by its merits and must be protected:

> "Collective management is one of the methods of rights management. It is generally considered appropriate for literary and artistic works since it enables a satisfactory balance to be struck between the interests of rightholders and the culture industry, on the one hand, and those exploiting the works, on the other. Accordingly, the Commission has always taken the important role played by collective management into account when preparing legislation. … rightholders and users alike can derive maximum benefit."[73]

112. *As to the second point,* the existing system regulates itself:

113. The first level of self-regulation is that of negotiations of Standard Agreements between BIEM and IFPI, two international associations, at arm's length. We submit that the complainant should wait for the outcome of the negotiations of a new Standard Agreement between BIEM and IFPI. None of the two associations has declared that their current negotiations have come to an end.

114. The second level of self-regulation is that of licensing agreements, which societies and users conclude in accordance with the Standard Agreement. Where the user is not satisfied with the conditions offered by the society, it can challenge these conditions before national authorities or courts, both on grounds of Community law and on grounds of national law. National courts can seek guidance by the Court of Justice under Article 234 EC.

115. This system of self-regulation has always worked and been sufficient. Nothing suggests that the questions raised in the complaint cannot be dealt with through negotiations or by national courts and authorities.

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[73] Answer on behalf of the Commission dated 12 November 1996 to written question No 2255/96 by *Klaus-Heiner Lehne*, OJ C 105 / 4 of 3 April 1997.

116. To give a concrete example, the *"Deutsches Patent- und Markenamt"* (German Patent and Trademark Office, formerly *"Bundespatentamt"* [Federal Patent Office]) acts as a regulator, with power to propose "reasonable conditions". The proposals of this office are subject to review by the German civil courts. These courts make findings of the full facts, apply Community and German law and, in addition, have power to determine "reasonableness". Also, they can seek guidance by the Court of Justice under Article 234 EC.[74] Nothing prevents the complainant from pursuing this procedure. One advantage from the Community standpoint would be that the scope of review of the German courts would be much broader than that of the Commission, which is limited to the Community competition rules.

117. Under these circumstances, there is in our view no Community interest to investigate the complaint because (1) the system of collective licensing as such is in line with Community policy and not restrictive of competition, and (2) questions arising *within* this system can be adequately dealt with by way of negotiations or by national courts and authorities.

118. In addition, according to the Commission Notice on Cooperation between National Competition Authorities and the Commission in Handling Cases Falling Within the Scope of Articles 81 or 82 of the EC Treaty[75], national authorities are often in a better position to protect competition (§ 6 of the Notice). Companies should be

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74 The legal basis of the German system is laid down in the *"Urheberrechtswahrnehmungsgesetz"* (Copyright Administration Act – "the Act"). The Act addresses, among other things, cases where a user (e.g., the complainant) believes that a copyright management society refuses to grant it "reasonable conditions" in respect of the use of a right managed by that society. In such case, the user can apply to the *"Schiedsstelle"* (Arbitration Body) of the German Patent and Trademark Office. The Arbitration Body has full jurisdiction to review the reasonableness of the conditions and to make a proposal to the parties setting out what it believes is reasonable. If the user is not satisfied with this proposal, it can file an action with the German civil courts and apply for a determination of reasonable conditions. See Sections 14 (1) N° 1 (a) and 16 (1) and (2) of the Act. The basic provision is laid down in Section 14 (1) of the Act: "Die Verwertungsgesellschaft ist verpflichtet, auf Grund der von ihr wahrgenommenen Rechte jedermann auf Verlangen zu angemessenen Bedingungen Nutzungsrechte einzuräumen oder Einwilligungen zu erteilen".

75 OJ 1997 C 313/3.

induced to approach national authorities more often (§ 8 of the Notice), the more so since these authorities often know the relevant markets better (§ 12 of the Notice).

119. We shall conclude that the complainant should be rejected (below at point 238). However, if the complaint is to be examined, it should first be submitted to national authorities. Copyrights are regulated by national law and are territorial in scope. No exercise of the Commission's power under Article 81 (3) EC and Article 9 (1) of Regulation No 17 is required. National authorities can settle the case under Community *or* under national law. All national authorities are guided by Community law. Some (like the *Deutsches Patent- und Markenamt*) have additional power to act as a regulator. Their jurisdiction is broader than that of the Commission.

120. Furthermore, a comfort letter has already been issued by the Commission on the basis of the full facts. For us, there appears to be no Community interest to start a fresh investigation. The complainant has not stated any relevant facts that occurred since the sending of the comfort letter. This last point will be developed in points 126 to 132 below (concerning Article 81 [1] EC).

IV. Non-Applicability of the Competition Rules to Collective Licensing

121. We respectfully submit that the competition rules should not be applied, or at the very least be applied with great restraint, to:

(1) collective agreements between BIEM and IFPI such as the Standard Agreement ("external collective arrangements"), and

(2) collective arrangements between BIEM, BIEM societies and / or members of BIEM societies to the effect that creators shall not receive remunerations less favourable to creators than those under the Standard

Agreement and under the BIEM statutes (“internal collective arrangements”).

This submission relates to collective arrangements that (1) have been concluded in good faith, (2) deal with the core subject of fair remuneration for creators, and (3) do not directly affect third markets or third parties.

121. Collective action under the auspices of BIEM (and BIEM member societies) is an indispensable means for creators to receive fair remuneration for the use of their works. BIEM and its member societies represent far more than 100.000 creators in Europe. The vast majority of these creators are too weak in economic terms to negotiate fair licencing agreements with the powerful majors on their own.

122. It follows that the “object or effect” of collective arrangements, whether internal or external (point 121 [1] and [2] above), pertains to social protection within the meaning of Articles 3 j and 136 seq. EC. By contrast, the “object or effect” of the said arrangements is not to restrict the possibilities of undertakings to compete, as envisaged by the competition rules.

123. The attainment of fair remuneration and of social protection for hundreds of thousands of creators would be seriously undermined if internal or external collective arrangements were subject to scrutiny under Article 81 (1) EC. The two associations, BIEM and IFPI have to strike delicate balances between the mutual interests of their members. This would be rendered impossible if such a balance, once it is agreed between the associations and applied by their respective members, could be challenged under the pretense of competition restrictions, and could be claimed to be automatically void under Article 81 (2) EC. It would be necessary, in each case, to apply to the Commission for negative clearance or for exemption. However, neither paragraph 1 nor paragraph 3 of Article 81 EC allow social objectives to be taken into account.

124. Collective arrangements, both external and internal, rest on the objective of "fair remuneration" for a vast number of creative persons, and not on considerations of competition between undertakings. In our opinion, *to apply the competition rules to such arrangements would be to use the wrong yardstick.*

125. The Court has already held that collective bargaining agreements, by virtue of their nature and purpose, fall outside the scope of Article 81 (1) EC.[76] There is an obvious similarity of collective bargaining and collective licensing: Both aim at fair remuneration and at minimum conditions. This similarity is so strong that the Court's case law should be extended to the case at hand.

V. No Breach of Article 81 (1) EC

126. The complaint does not disclose a *prima facie* case of an infringement of Article 81 (1) EC.

127. Based on Article 7 of the BIEM statutes, the societies use the Standard Agreement as a model contract (*de facto* since the expiration of the Standard Agreement in June 2000). The Commission has made clear in its comfort letter that this practice does not give raise to concerns under Article 81 (1) EC. This comfort letter has been made known to the public.[77] To BIEM's knowledge, no third party has raised any objections further to this publication.

128. The comfort letter also covers the Four Points and the obligations of the BIEM member societies under Article 7 of the BIEM statutes. In the notification that led to the comfort letter, BIEM had informed the Commission about the Standard

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76 See Case C-67/96 *Albany v Stichting Bedrijfspensioenfonds Textielindustrie* [1999] ECR I-5751, §§ 52 to 59; see also the opinion of Advocate General *Jacobs id*. at §§ 178 and 179: "… collective agreements between management and labour on wages and working conditions should enjoy automatic immunity from antitrust scrutiny.". See further §§ 182 and 194 of that opinion.

77 XXXth Report on Competition Policy (2000), p. 164.

Agreement because this agreement implemented Article 7 of the BIEM statutes. Already at the time of the notification, the Standard Agreement had included the Four Points. Amendment No 7 was brought to the attention of the Commission on 9 July 1998, together with the notification of the correspondence between the Presidents of BIEM and IFPI.

129. In disregard of the comfort letter, the complainant alleges that the application of the Standard Agreement infringes Article 81 (1) EC. This allegation is deprived of any basis. To state a *prima facie* case for Article 81 (1) EC, the complainant would have to show facts of which the Commission had not been aware at the time of the comfort letter.[78] These facts would have to suggest, with a degree justifying an investigation, that the application of the Standard Agreement by member societies restricts competition appreciably and *in excess* of the practices known by the Commission at the time of the comfort letter.

130. The complainant does not even purport to state such facts. It only alleges that the Commission has not investigated all pertinent facts in connection with the comfort letter.[79] We suggest that the complainant first do its own homework (and state verifiable facts) before it blames the Commission for not investigating properly.

131. Enclosed as annex 2 is a summary of the exchanges between BIEM and the Commission, of the facts brought to the attention of the Commission, and of the topics discussed, in connection with the notification that led to the comfort letter. It emerges from this annex that BIEM has brought the full facts to the attention of the Commission, including its statutes, and the Standard Agreement in its 1998 version (Amendment N° 7). We respectfully submit that *the Commission would have raised concerns under the rules on competition if the full facts disclosed to it had given it any reason to do so.* The statutes and the Standard Agreement have not been

78 See Case C-279/95 P *Langnese-Iglo v. Commission* [1998] ECR I-5609, § 30.

79 See complaint, § 1.15: "… whilst the Commission may not have fully recognised these matters arising from the Standard Contract, or at least felt a pressing need to examine them in the past …"

changed since the Commission has sent its comfort letter. The Standard Agreement continues to be applied *de facto*.

132. We conclude that given the comfort letter and the complainant's failure to state relevant facts not known to the Commission, there is no *prima facie* case for Article 81 (1) EC. It is therefore not necessary to discuss issues under Article 81 (3) EC.

VI. No Breach of Article 82 EC

133. We will show that the complainant has not stated a *prima facie* case for an "abuse" within the meaning of Article 82 EC. In particular, by observing the Four Points, neither BIEM nor its member societies impose "unfair trading conditions" within the meaning of Article 82 (a) EC. In the absence of a *prima facie* case, the Commission is not obliged to start an investigation under Article 82 EC.

134. We do not address the further requirements of Article 82 EC at this time. In our opinion, the complaint can be rejected for lack of an "abuse" alone. By no means do we admit that the further requirements of Article 82 EC are met.

1. Burden on Complainant to Prove "Abuse"

135. Having lodged a complaint under Regulation No 17, the complainant must put forward "*documents not devoid of probative value*" for an infringement of Article 82 EC. The Commission in turn must ascertain whether or not this information is substantiated and must check, *where appropriate*, whether the particular circumstances of the case point to a breach of Article 82 EC.[80] Only if these requirements are met, it is justified for the Commission to investigate the truth of

80 See Case T-198/98 *Micro Leader v Commission* [1999] ECR II-3989.

the facts alleged and to check whether it can adduce full evidence capable of demonstrating to the requisite legal standard the existence of the circumstances constituting a breach of Article 82 EC.[81]

136. We will show that the complainant has failed to provide evidence "not devoid of probative value" as to any possible infringement of Article 82 EC.

2. No "Imposition"

137. The notion of an "imposition" within the meaning of Article 82 (a) EC requires that the relevant conditions are not negotiable.[82] Also, the dominant undertaking must "force" the other party to accept these conditions.[83]

138. These requirements are not fulfilled.[84] Firstly, it was IFPI that has flatly rejected BIEM's proposals on 19 February 2002. Secondly, since its inception in 1947, the Standard Agreement has at all times been negotiated. *The fact that the formal negotiation meeting has not led to a result does not mean that the complainant is faced with an "imposition" by BIEM.* Thirdly, the complainant does not even pretend to be in a stranglehold situation which is characteristic of cases to which Article 82 EC is applied. The majors, acting in concert under the auspices of IFPI, by far have superior bargaining power.[85]

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81 Case C-185/95 P *Baustahlgewebe v Commission* [1998] ECR I-8417, §§ 56 und 58; Case T-43/92 *Dunlop Slazenger v Commission* 1994 ECR II-409, § 79.

82 See *Tournier id.*, § 35: "The first question … emphasizes the point that the conditions are not negotiable and are unfair."

83 See the German wording of Article 82 (a) EC: *"Erzwingung"*.

84 The complainant presents the Standard Agreement as if it were some sort of a regulation that BIEM imposes, similar to the conduct of a national legislator. See, e.g, complaint, p. 12 (bottom) and p. 13 at § 1.11. That is a misrepresentation.

85 See points 4 to 8 above.

139. Already because there is no "imposition", the complainant has failed to state a *prima facie* case under Article 82 EC.

3. Acceptance of the Four Points by Way of Contractual Negotiations

140. On behalf of the Commission, Commissioner *Monti* has stated that:

> "… the Commission wishes to stress that management societies' fees are the result of contractual negotiations that reflect market conditions and the interests at stake."[86]

141. In accordance with this basic consideration, IFPI and the majors cannot complain about the Four Points because *IFPI <u>accepted</u> the Four Points by way of an arms' length agreement with BIEM*: the Standard Agreement in its 1998 version (despite certain concerns raised). Moreover, the complainant has always fulfilled its obligations under the Four Points (even during the two years since the expiration of the Standard Agreement).[87]

142. The complainant has not alleged that IFPI, in accepting the Four Points (or itself in fulfilling the Four Points), have been in a stranglehold situation which characterizes cases under Article 82 (a) EC. The complainant has also never attacked any of the Four Points before national courts or authorities.

143. The fact that the Four Points have been agreed and fulfilled at arm's length creates a strong and conclusive presumption for "fairness" within the meaning of Article 82 (a) EC.

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86 *Id.*

87 Those obligations arose from licensing agreements between the complainant and the British society MCPS into which the Four Points had been incorporated.

144. This presumption is corroborated by the fact that creators and their associations, but also IFPI enjoy freedom of contract. It is settled case law that this freedom must not be discarded lightly through the application of competition law.[88]

145. It is for the complainant to rebut the presumption of ”fairness” right within its complaint.[89]

146. In this context we recall that 1998 was the year during which the latest version of the Standard Agreement was concluded. According to the complainant, the increase of discounts for retailers, which is at the basis of the complaint, had begun in 1985, that is always according to the complainant, well before 1998.[90] [91] Under these circumstances, the complainant not only had to state facts that rebutted the presumption of “fairness”. More than that, it had to state facts arisen *after 1998*. It had to explain why, in its opinion, those post-1998 facts had caused the Standard Agreement to become “unfair” as of today even though IFPI and the majors had accepted the Standard Agreement as “fair” in 1998.

147. None of these requirements is satisfied by the complaint. The complaint is limited to unverifiable generalities (e.g., “pressure”, “flexibility”, “market realities”,

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88 See Case T-41/96 *Bayer v. Commission (“Adalat“)* [2000] ECR II-3382, §§ 174, 176 and 180; Case T-41/96 R *Bayer v. Commission* [1996] ECR II-381, §§ 43, 54 and 59; Case T-128/98 *Aéroports de Paris v. Commission* [2000] ECR II-3929, § 82; Case T-24/90 *Automec v. Commission* [1992] ECR II-2223, §§ 51 and 52; Advocate General *Jacobs*, Case C-7/97 *Bronner* 1998 [ECR] I-7791, § 57. See also Article 16 of the Charter of Fundamental Rights.

89 The relevant time period is from 1998 to 2002. The complainant insinuates that “the Standard Rate was settled 50 years previously” (complaint, p. 7, § 1.5). That is misleading. The rated currently applied were settled in 1998.

90 Complaint, § 4.9, before footnote 35 of the complaint.

91 The majors, under the auspices of IFPI, have not exhausted the possibility of negotiations. We suspect that the complainant, in concert with the other majors, has caused IFPI to refuse BIEM’s proposals in order to get its hands free and to complain to the Commission in order to use the Commission as a negotiation facilitator (*détournement de procédure*). One basis for this suspicion is that the complainant plays a leading role in the IFPI negotiating committee.

"current market usage"), topped off by a sentence that is noteworthy for its sheer voidness:

> "Even if, quod non, the rate was set appropriate in 1985, it is clearly not appropriate now."[92]

This is a *petitio principii*, devoid of probative value.

148. The complainant repeatedly refers to the notion of "commercial usage". We know of no "commercial usage" which would give the complainant a right to greater concessions than those agreed in 1998. However, BIEM has to stress that dealings between copyright management societies and Record Producers are governed by two "usages" on which the complainant remains silent:

(1) Market conditions are addressed by negotiated agreements between two associations, BIEM and IFPI, and not under some "objective" standard.

(2) Royalties must be such that creators receive a fair remuneration.

5. No Obligation of Creators to Share Risks

a) Limitation of the Issue

149. *The Standard Agreement already provides for very significant deductions:* The deduction for packaging and the deduction for discounts together bring the royalty rate from 11 % of the PPD down to 9,009 % of the PPD.[93] These deductions are of a general nature: They do not depend on specific transactions between Record Producers and third parties or on other factors which are opaque to creators.

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92 Last sentence of § 5.6 of the complaint.

93 We recall that BIEM had been forced to accept these deductions.

150. This is an important fact which in our view limits the issue which the Commission has to consider: In our view, the only remaining issue, if any, is whether it constitutes an "abuse" for BIEM to refuse additional "specific" deductions that are not provided for in the 1998 agreement – even though the question of deductions is already settled in the 1998 agreement by way of a general deductions.

151. The complainant states nowhere with precision what sort of additional "specific" deductions it claims. We understand, however, that, in any case, a "specific deduction" would be one that follows specific transactions between Record Producers and third parties (like an analogous wave). In the following paragraph we shall develop that it does not constitute an "abuse" for BIEM to refuse such additional "specific" deductions.

<u>b) No Joint-Venture between Creators and Record Producers</u>

152. For the complainant, it is "unfair" within the meaning of Article 82 (a) EC that creators receive royalties that are independent of the specific earnings of Record Producers (as determined, for example, by specific rebates and discounts). In economic terms, the complainant requests the Commission to rule that creators share the financial burden and risks of the majors.[94]

153. *This is an astounding position. Creators and their societies are not the banks of the majors. Nor are they joint-venturers of the majors*. Rather, a major CAVEAT is appropriate: If societies were to finance the majors' risk business (and, in particular, risky deals between Record Producers and retailers) they would subject all the

[94] The language in the complaint is revealing. <u>See, e.g.</u>, complaint, p. 9, § 1.10, 3rd bullet point: "… it is unfair and abusive to require record companies to pay royalties to BIEM and the relevant BIEM Members on income not received by record companies, …"; § 4.9 of the complaint: "… record companies should not pay royalties on money they do not receive."; § 5.13: "… the BIEM rate should only be paid on the price actually paid on the product."

creators whom they represent to uncontrollable and arbitrary risks. This would clash with their mission to ensure that creators receive a fair remuneration.

154. To our knowledge, it has never been deemed "unfair" within the meaning of Article 82 (a) EC that a provider of valuable things (here: musical copyright licenses) is paid simply for the provision of these things, and does not assume risks, which its trading partner incurs in the course of dealings with third parties (such as transactions between the majors and retailers). In other words, the fact that the licensee (the record producer) fails to draw economic benefit (or a certain economic benefit) from the license does not make it "unfair" for the creator to receive his royalty in full accordance with the licensing agreement.[95]

155. If, nevertheless, the complainant's proposition were upheld, then at their whim the majors could determine how much creators earn. *Creators' royalties would be calculated on the basis of factors over which creators have no control.* Among these factors would be dealings between majors and retailers, and ad hoc discounts which stem from the majors' sole decisions.

156. The complainant, in essence, makes two points to justify its position: "illegitimate interference" with its business, and "commercial usage". Neither of these points has any meaning.

157. Concerning *"interference"*, the price of a supplier always impacts on the profitability of the buyer. To call this "an illegitimate interference", as the complainant does[96], is an unworldly statement and beyond business reason.

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[95] In German law, this principle is long established. For an early case <u>see</u> German Supreme Court (*Bundesgerichtshof*), judgment of 18 May 1955 [1955] Gewerblicher Rechtsschutz und Urheberrecht (GRUR) 492 at 497 - "Grundig-Reporter".

[96] <u>See</u> complaint, 2nd bullet point on p. 10, § 1.10; <u>see also</u> § 5.16.

158. The complainant similarly proposes that societies should pay to the majors money which societies save through limitations of their overhead.[97] That proposition is as unworldly as the aforementioned. As the complainant knows, BIEM and its member societies only operate for a fair remuneration of their members. They are not joint-venturers of the record industry. Accordingly, money saved goes to the members.[98] As an aside, we recall that the music publishing entities of the majors are members of BIEM societies.[99] Like all members, the publishing entities of the majors benefit when lowered overhead of societies leads to higher earnings. There is no reason why the majors should benefit from this in their capacity as Record Producers and in the form of lowered rates.[100]

159. Concerning *"commercial usage"*[101] (or "willing licensors" and "willing licensees"[102]), we reiterate that we do not know what the complainant means. We note, however, that the complainant itself follows markedly different "commercial usages" depending on what suits best: In contracts with artists where the complainant acts as a licensee, the complainant considers as "commercial usage" all those concessions that it can extort by exploiting its superior bargaining power. By contrast, in its dealings with smaller companies where it acts as a licensor (licensing out its own copyrights), the complainant considers it a "commercial usage" to limit or reduce discounts, to set minimum prices at which the record may be wholesaled, to reserve the right to approve track numbers, and to forbid deletion sales. For

97 Complaint, § 5.6, § 5.18 and § 5.19.

98 If BIEM and BIEM societies did not do their very best for creators' remuneration, also in respect of saved money, they would cease to be the "best solution" for creators and begin to fall apart.

99 In their capacity as music publishers, the majors have an institutional responsibility for creators.

100 We mention this to illustrate that most of the complainant's positions boil down to one misconception that we have pinpointed at the outset: "Give me your creation, leave its commercialization in my hands, and wait and see what earnings remain for you."

101 Under Article 82 (e) EC the notion of „commercial usage" is relevant in connection with tying arrangements. The complainant does not allege such an arrangement, but omits, on the other hand, to explain what bearing that notion might have in the context of Article 82 (a) EC.

102 Complaint, § 5.5.

example, where specialist record companies seek a copyright license in sound recordings from one of the majors, they have to pay a royalty far in excess of 9,009 % of the PPD, often subject to the requirement that PPD is a fixed amount.[103]

160. This shows that the complainant, depending on its own interests, has multiple standards of what constitutes "commercial usage". For this reason, it should not be heard with this notion.

161. We conclude that there is no "abuse" for creators to refuse to bear or share the risks of transactions between the majors and third parties over which the creators have no control.

162. The context warrants one further observation: There is a Standard Agreement, and there are licensing contracts made in accordance with this Standard Agreement. The majors should negotiate transactions with third parties in such a way that they can fulfill their obligations under the said license contracts. Given their bargaining power over retailers[104], *the majors are in a position to refuse increased discounts, thereby eliminating the grievance which the complainant invokes*. In our view, it is an abuse of the procedure under Regulation No 17 that the majors do not take account of their licensing contracts with societies when making deals with third parties and instead burden the Commission with a "fishing expedition".

c) Alternative Methodologies are no indication of "Abuse"

163. The complainant at one point requests that rates be calculated "by reference to a percentage of actual or average realized price."[105] This is puzzling because the

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[103] Presentations in this paragraph, as elsewhere in the present submission, are based on BIEM's best knowledge.

[104] Found by the Commission in *Time Warner / EMI id.* (footnote 5) §§ 42 and 57; see also *id.* at § 50.

[105] Complaint, § 1.10, p. 11, before footnote 14 of the complaint.

complainant at another point states that it does not object to the list price ("PPD") as the calculation basis.[106]

164. Whatever the complainant may have wished to express, the list price ("PPD") as the calculation basis is the result of an arm's-length negotiation and therefore cannot be deemed "unfair".[107]

165. The fact that imagination leaves room for another calculation basis does not indicate that the PPD is an "unfair" basis. Quite the contrary, as the Commission has determined in *Time Warner / EMI*, PPD is completely transparent and is "a good benchmark for prices charged to retailers, because there is an incentive for record companies to offer as little discount as possible."[108]

d) The LECG Study

166. The LECG study (annex 16 to the complaint) was not enclosed with the non-confidential version of the complaint. Neither BIEM nor its members have access to this study. To be able to comment, BIEM would be grateful for a copy, with business secrets and other confidential information, if any, deleted. If such a non-confidential version cannot be prepared, BIEM would be grateful for a non-confidential table of contents of the study and for a non-confidential summary.[109]

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106 See point 103 above with a quotation from the complaint in a footnote.

107 BIEM has explained to IFPI in detail why it cannot accept either actual or average realized price as a calculation basis. The reasons are set out below at points 210 to 216 of the present submission; also, we refer to the letter dated 31 March 2000 from Cees Vervoord, the President of BIEM, to Jason Berman, the Chief Executive Officer of IFPI (annex 4).

108 *Id.* (footnote 5) at §§ 36 and 46.

109 Concerning access to a non-confidential version, we rely on Article 41 (2), 2nd dash of the Charter of Fundamental Rights and on the Commission Notice on the application of this charter by its services (Agence Europe Nr. 7918 of 8 March 2001, p. 7).

Until such disclosure, BIEM rejects the LECG study and the complainant's conclusions as unverifiable.

167. The complainant further relies on an "IFPI analysis at the time" (1997 or 1998?) concerning the effect of a further change of the calculation basis.[110] Since this analysis was not enclosed with the complaint, it is unverifiable and hence inadmissible.

6. No Disproportion or Excessive Royalty Disparities

168. The only interest that BIEM and its members pursue is to ensure that creators receive a fair remuneration. This interest is perfectly legitimate. In the words of the Court of Justice (French original):

> " … les sociétés de gestion poursuivent un but légitime lorsqu'elles s'efforcent de sauvegarder les droits et intérêts de leurs adhérents à l'égard des utilisateurs de musique enregistrée."[111]

169. The Court has also stressed that, in examining allegations of "abuse" made by Record Producers against societies, account must be taken of the specific mission of societies and of the superior bargaining power of exploiters, including Record Producers, to which societies are exposed in their actions to protect creators:

> "To determine whether, in these circumstances, the practices mentioned in the referring judgment constitute an abuse within the meaning of Article 86 of the Treaty account must however be taken of the fact that an undertaking of the type envisaged [a society] is an association whose object is to protect the rights and interests of its individual members against, in particular, major exploiters and distributors of musical material …"[112]

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110 See complaint, § 4.10.

111 *Tournier id.* at § 31.

112 Case 127/73 *BRT v SABAM and Fonior* [1974] ECR 313, § 9. Dutch original: "… dat bij de beoordeling of onder die omstandigheden de in het verwijzingsvonnis vermelde gedragingen al dan

170. All the provisions here complained of have come about through arm's-length negotiations between two associations. The present case is entirely different from situations where a major association negotiates with a small individual user (e.g., the operator of a discothèque, a café or a shop).

171. It is in these circumstances (*legitimate aim of societies, bargaining power of majors, complaint against a result negotiated by two associations*) that the question arises what criteria might be used to test whether a license royalty is "unfair" and hence "abusive".

172. In any case, the circumstances require the complainant to show very exceptional circumstances, which conflict with the objectives of the Treaty, if it wishes to state a *prima facie* case of "abuse".

173. The Court's decisions in *Tournier* and *Lucazeau*[113] and the opinion of the Advocate General in *Tournier* suggest that in the case of copyright management societies, there may be only two criteria, if any, which might, in extreme cases, indicate "abuse":

(1) either a disproportion between royalties and the value of the license (fair remuneration) or

(2) levels of royalties that are appreciably higher in one Member State than in other Member States, without justifiable grounds.

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niet misbruik in de zin van artikel 86 van het verdrag opleveren nochtans in aanmerking moet worden genomen dat een dergelijke onderneming een vereniging is, die ten doel heeft de rechten en belangen van haar individuele leden te beschermen onder meer tegenover belangrijke muziekgebruikers en –verspreiders, zoals de radio-omroepen en de grammofoonplaten-fabrikanten; ..."

113 Joined Cases 110/88, 241/88 and 242/88 *Lucazeau and others v Sacem and others* [1989] ECR 2811.

174. Whichever criterion may be appropriate, it is clear that the burden is on the complainant to furnish full proof.[114]

a) No Disproportion

175. In our view, the criterion of "disproportion" is inapplicable in the present case.

176. The term "disproportion" may refer to the relationship between the royalty and value of the license. However, nothing in the complaint refers to the value of copyright licences to Record Producers.

177. The term "disproportion" may also refer to the relationship between the royalty and the cost of production of the relevant creation. However, in the case of musical works, there can be no comparison between the cost of production and the royalty. The reason is that it is impossible to determine the cost of a musical creation. As Advocate General *Jacobs* said in *Tournier*:

> "… it is inappropriate in the present context to proceed on the basis of a comparison between the costs of production and the selling price because it is impossible to determine the cost of the creation of a work of the imagination such as a musical work."[115]

178. We conclude that the possible criterion of "disproportion" is inapplicable. We shall therefore confine our observations to whether the complainant has established a *prima facie* case for abuse in the form of excessive royalty disparities.

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[114] See our observations on the burden of proof in points 135 and 136 above.

[115] See Advocate General *Jacobs*, Case 395/87, Ministère Public v Tournier, [1989] ECR 2521 at 2553, §§ 53 and 69, distinguishing the copyright licensing case before him from prior case law dealing with allegedly unfair pricing under Article 86 of the EC Treaty (now Article 82 EC); this case law had dealt with the sale of goods.

b) No Excessive Royalty Disparities

179. It is uncontested that, within the Community, there are no appreciable disparities of royalties.[116] The complainant therefore relies on comparisons of rates in the Community with rates in third countries. These comparisons are irrelevant.

180. In *Tournier*, the Court of Justice has held (cited in French, the language of the *Tournier* case):

> "Il y a lieu d'observer que, lorsqu'une entreprise en position dominante impose des tarifs pour des services qu'elle rend, qui sont *sensiblement plus élevés* que ceux pratiqués *dans les autres États membres*, et lorsque la comparaison des niveaux des tarifs a été effectuée *sur une base homogène*, cette différence doit être considérée comme *l'indice* d'un abus de position dominante."[117] (emphasis added)

Three conclusions follow from this judgment:

181. Firstly, to establish "abuse", regard may only be made to rates within the Common Market (below at aa).

182. Secondly, the mere existence of royalty disparities is not conclusive of an "abuse". Royalty disparities may exist for the most different reasons, and the burden is on the complainant to show that the disparity concerned can only be explained by an "abuse". Such a showing requires that the relevant prices are compared on a *homogenous basis* and that this comparison reveals a disparity that is "*appreciably high*" (*"sensiblement élévé")*. The mere rate figures presented by the complainant do not suggest that these two requirements are met, even if one were to deviate from *Tournier* and take account of figures from third countries (below at bb).

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116 As stated, exceptions apply where there is mandatory national legislation.

117 *Id.* at § 38.

183. Thirdly, even if the aforementioned requirements were met (which is not the case), it follows from § 38 of the *Tournier* judgement (cited at point 181 above) that there would only be an "indication" of an abuse. The term "indication" means that BIEM could present an objective justification for the price disparities. Such justification then would rule out an "abuse".[118]

<u>aa) The Common Market as the Only Proper Basis for Price Comparisons</u>

184. It is striking that the complainant only cites examples from third countries.[119] Under Article 82 EC, such examples are irrelevant. The Community context of Article 82 EC ("trade between Member States") as well as Article 3 g EC ("competition in the *internal* market") require that royalty disparities must be established as between Member States (and not as between the Community and third countries) if a user wishes to challenge royalties on a theory of "abuse".[120]

185. It must also be borne in mind that BIEM has no responsibility for all the levels of royalties worldwide.

186. What the complainant advocates, in fact, is *a worldwide race to the bottom*, that is: the prevalence of the cheapest rate of the day, wherever in the world it is charged, and irrespective of the context in which this rate has come about. If this were the test, then the Commission would be limited to a purely empirical search for the cheapest price worldwide, and Community policies, such as fair remuneration for

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[118] In the present submission, we shall only state our view that the complainant has not proven royalty disparities of a kind that would be relevant under *Tournier*, that is: royalty differences within the Common Market and comparable on a homogenous basis. In case the Commission does not share our view, BIEM would ask to be informed about the Commission's standpoint, and would reserve the right of furnishing an objective justification.

[119] <u>See, e.g.</u>, complaint, § 1.5, 3rd bullet point: "taking full account of current market condition comparables elsewhere in the world; …"; <u>see also</u> complaint § 1.9.

[120] *Tournier, id.,* §§ 35 and 38.

creators, protection of intellectual property, and maintenance of culture, would lose all bearing.

bb) Royalty Disparities, Determined on a "Homogenous Basis", not "Appreciably High" within the Meaning of the *Tournier* Judgment

187. Even if one were to accept comparisons with third country rates (which, in our view, is contrary to the law), the complainant's submission would be insufficient for a *prima facie* case of "abuse" in the form of excessive royalty disparities. In *Tournier* (cited in point 181 above) the Court has taken care to emphasize that price differences as such are not conclusive evidence for an "abuse". They may "indicate" an abuse, but only if (1) a comparison is made on a *homogenous basis*, and (2) this comparison shows that the disparity is *"appreciably high"*. Neither is the case in the complainant's submission.

i) No Proof of a "Homogenous Basis" of Comparison

188. Comparison of rates in different countries is a matter of great delicacy. In the words of Advocate General *Jacobs* (who, at this point, discussed comparisons between Member States):

> "The difficulty with this comparative method is that it is necessary to devise an objective means of comparison between the rates charged in the different Member States. This is no easy task, given the differences in national legislation and in the methods of assessment and collection of royalties used by the different copyright-management systems."[121]

Obviously, this difficulty is still greater in relation to third countries.

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[121] Case 395/87 *Ministère Public v Tournier* [1989] ECR 2521 at 2556, § 60; see also § 62 of the Advocate General's opinion.

189. Against this background, it is astounding how nonchalantly the complainant disposes of comparability and "comparables" as if they were no issue: "These rates", the complainant states in relation to its figures from third countries, "are comparable to the Standard Rate and there are no objective, relevant dissimilarities ..."[122] The complainant does not deem it important to mention all the specific contexts in which the figures on which it relies have come about. Nor does the complainant go into any sort of economic field research.[123] Whilst demonstration of comparability and "comparables" may be cumbersome, there is no reason why the complainant should be relieved of this burden and why the Commission should start an investigation based on mere rumour.

190. In relation to rates in the United States, one special remark is warranted. Although irrelevant, the complainant's reliance to these rates[124] reveals that it has set its mind for a purely symbolic remuneration of creators. Until 1978, United States legislation provided a compulsory mechanical royalty rate, which that same legislation limited to 2 cents per composition, multiplied by the number of copies distributed. When the United States Congress provided modest adjustments of the 2 cents rate in 1978, Record Producers instituted restrictions ("controlled composition clauses") in their contracts with creators that eliminated the greater part of these adjustments. Should this world of "creator looting" serve as a benchmark for the Community, as the complainant suggests?[125] A fuller account of the United States system is set out in a statement by Mr. Edward P. Murphy, the President of the National Music Publishers Association (NMPA) of the United States (annex 10).

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122 See complaint, §1.9.

123 For that requirement see Advocate General *Jacobs id.* at the end of § 62.

124 See complaint, at the end of § 1.9.

125 We also wonder why the complainant claims, in annex 3 to the complaint, that its comparison of United States and European rates is a business secret, thereby preventing BIEM from more ample comment? We note that the complainant itself considers this comparison as "problematic"; see complaint, at the end of § 1.9.

ii) No "Excessive" Character of the Alleged Price Differences

191. As set out above, mere existence of price disparities, even on a homogenous basis, is not conclusive of an "abuse".[126] Price differences have never been found to indicate an "abuse" unless the challenged price was *many times higher* than the price with which it was compared.[127] Thus, in *Tournier*, the Commission had made empirical findings whereby certain royalties were limited to only 6,7 %, 12,24 % or 19,04 % of the royalty challenged.[128] Reading the complaint, disparities between royalties, if any, are not such that one royalty is many times the amount of another, even if one took the figures presented by the complainant at face value (which is impossible due to factual irregularities and lack of proper comparison).[129]

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126 See Advocate General *Jacobs id.* at § 63.

127 Apart from *Tournier*, there seems to be no case law relating to allegedly "excessive royalties" for musical copyright licences. However, there is case law on the treatment under Article 82 EC of allegedly excessive prices in other contexts. It emerges from this case law that, for a verdict of "abuse" (and hence an interference with freedom of contract), the challenged price must be (1) either "many times" higher than comparable prices, or (2) without any reasonable relation to the product or service supplied. See,e.g., Case 27/76 *United Brands v Commission* [1978] ECR 207, § 251, requiring a comparison of the challenged prices with costs of production (which cost, as stated, is not assessable in case of artistic creations); Case 226/84 *British Leyland v Commission* [ECR] 1986 3263, § 27: an undertaking with an administrative monopoly was liable of an "abuse" where it had charged for its services fees which had been disproportionate to the economic value of the service rendered (which value is also not assessable in case of artistic creations); Case T-30/89 *Hilti v Commission* [1991] ECR II-1439, § 99 (six times the amount of the royalty fixed by the president of the patent office), confirmed on other grounds in Case C-53/92 P *Hilti v Commission* [1994] ECR I-667. In old Roman law, such cases were called *laesio enormis.*

128 Referred to by Advocate General *Jacobs* at § 61 of his opinion; see also the Court's judgment at § 37.

129 The complainant's reliance on the Visa case is inappropriate for many reasons. In *Visa*, where consumer A paid to retailer B with his Visa card, A's bank (the bank that had issued the Visa card to A) transferred the amount paid to B's bank. In consideration of this service, B's bank paid a multilateral interchange fee to A's bank, but B's bank would normally pass that fee on to B, the retailer. After adaptations that brought the multilateral interchange fee into a reasonable relation to the relevant costs, the Commission exempted the multilateral interchange fees for cross-border Visa card payments under Article 81 (3) EC. The single most important difference to the present case is that the "fee-earners" (the banks) had fixed conditions in concert and under the auspices of an association (Visa International Service Association), whilst the "fee payers", that is: the retailers, were only persons "from the people" and were not at all organized. By contrast to *Visa*, the Record Producers, who are the "fee payers" in the present case, are organized under the auspices of IFPI, BIEM's counterpart, and together have superior bargaining power over BIEM, BIEM's members

192. The *Commission* in its practice under Article 82 EC *does not normally control or condemn allegedly high prices as such* (as a regulator would do). Rather, as a competition authority, the Commission examines whether the behaviour of the allegedly dominant company affects competitors or new entrants who would normally bring about effective competition and a different price level.[130]

7. No Effect on Consumer Welfare

193. As demonstrated above (points 87 to 93), lower royalties would not result in lower consumer prices. There is no economic interrelation (let alone a linear interrelation) between the two.[131] The final price of records will be influenced by many other factors before they reach the market.

8. No Possibility to Extort Random Prices ("Quiet Life")

194. We understand that, with the term "quiet life", the complainant wishes to refer to a situation where the demand side depends on one supplier for the provision of certain goods or services which are essential for the demand side's existence or operations and where, consequently, the supplier can lean back and extort any amount.

195. The present case does not fall within this category. As we have said in point 7 above, creators need the record companies just like record companies need creators. There is no unilateral dependence, but a set of agreements providing for the

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and the creators that BIEM members represent. See Commission Decision of 9 August 2001, Case No COMP / 29.373 – Visa International, OJ L 293/24 of 10 November 2001.

130 See XXIVth Report on Competition Policy (1994), point 207.

131 We note a recent statement by a Commission official, *Christopher Forax*, cited above in footnote 50.

exchange of mutual benefits. Also, the complainant conceals that royalties have declined significantly over the last years as far as copyright licences for mechanical reproduction are concerned.[132]

196. The complainant's allegation of a "quiet life" reveals how wantonly the complainant disregards the role of societies for creators' income, for the creation of music and text, and for the efficiency of management.[133]

9. No Specific "Unfairness" of the Four Points

197. None of the Four Points is "unfair". After two preliminary remarks we shall address these points in turn.

a) The Necessity to Protect Intellectual Property and Culture

198. We submit that, in its analysis of "unfairness", the Commission should take account of two points: (1) the creators' fundamental right of property and (2) the need to encourage artistic creation, and to promote culture and cultural diversity pursuant to Article 151 EC:

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132 The way in which the complainant relies on a speech of the President and Chief Executive Officer of GEMA (complaint, p. 11, § 1.10) is selective and misleading: In Germany, revenue from the musical copyright licences in sound carriers actually declined from 1999 to 2001 by about 10 %, from € 195 million in 1999 to € 185 million in 2000 and to € 178 million in 2001. The President and Chief Executive Officer of GEMA mentioned this in a part of his speech of 27 June 2001 that the complainant conceals: "with sound carriers … however, one can sense a certain continuing weakness in the market" (point I. 3. d. of the speech). Also, in a speech on 26 June 2002, GEMA's President and Chief Executive Officer had emphasized: "And if you consider further slump in the German audio carrier market in the first six months of 2002, then it is quite obvious that this is a trend clamouring for change." Both speeches are published at http://www.gema.de/engl/communication/speeches. In reality, there can be no question of creators enjoying a "quiet life". Of the composers in Europe, which are far more than 100.000, "only a small portion … are able to earn a full salary from their work as a composer." See Music in Europe, Study by the European Music Office with the support of the European Commission (Directorate General X), September 1996, p. 8, fifth paragraph, 3rd sentence.

133 See also footnote 17 of the present submission.

199. *Copyrights*, which are the subject of the complaint, are a form of property. As property, they are protected by the Community legal order.[134] In light of the fundamental right of property, creators and their societies should not be forced to agree on royalties that do not allow creators to receive a fair remuneration. A "squeeze-out" would deprive property in the form of copyrights of its very purpose.

200. *Article 151 EC* requires that action by the Community shall encourage *artistic and literary creation*. Also, by virtue of paragraph 4 of Article 151 EC, the Community must take cultural aspects into account, *also in its action under the competition rules.* This shall serve, in particular, to promote the diversity of the Community's cultures. The underlying policy of Article 151 EC is that *the Union aims at promoting artistic creation and cultural diversity to a greater extent than can be justified on economic grounds alone. To the extent necessary, a balance must be struck between the rules on competition and the values protected by Article 151 EC.*

201. Moreover, the protection of intellectual property, and of culture and cultural diversity, requires that the risk business of the majors should have no effect on the income of creators (e.g. volume-policy or risky discounts). Rather, in order to protect copyright property and culture, royalties should be such that creators receive a fair remuneration. Were it otherwise, then artistic creation would be stifled, few creators could continue their activity, and cultures in the Union would become uniform, superficial, and dull.

202. One factor must never be overlooked. *Cheaper royalties obtained by a forced reduction of creators' income have a cultural price: The incentive to create is diminished, and fewer songs and other pieces of music will appear.*

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[134] See Article 30, 1st sentence EC (protection of industrial and commercial property) and Article 17 (1) of the Charter of Fundamental Rights.

203. These two points correspond with the Commission's policy. As far as we can see, the Commission has always had the strong intention to ensure, in relation to users, that rights-holders enjoy a fair remuneration for the exploitation of their works. Contrary to the complainant's allegation, protection of creators income (at which Commission policy aims) is never an "anti-competitive result".[135]

b) Lack of Precise and Conclusive Evidence

204. We respectfully submit that in an economy based on the interplay of market forces, a competition authority should be prudent as to whether it should interfere with prices and conditions that have been reached by way of arms-length negotiations. The authority in such cases should insist on particularly precise and conclusive evidence.

205. With that in mind, one would expect that the complainant presents either *(1) concrete empirical evidence* or *(2) verifiable economical models*. Such evidence should show that the royalties complained of, despite their negotiated character, have led to grossly unjust results ("unfair" or "limitative", to use the language of Article 82 EC). It should also clearly result from the complainant's submission that there is a *causal link* between the prices and conditions, on the one hand, and the harm complained, of on the other. If it cannot be ruled out that the harm is caused by the complainant's own commercial decisions, Article 82 EC should not apply.

206. In stark contrast to these requirements, the complaint is devoid of any empirical evidence.[136] Nor is there any economic expertise in the scientific sense.

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135 But see the insinuation to that effect in the complaint, p. 5, § 1.4, before footnote 5 and p. 6, end of § 1.4 (before the sentence in brackets; which is the last one).

136 As the Commission knows, empirical evidence often consists of anecdotal events from business practice. However, the complainant has not cited any project in its business practice that failed precisely on the ground of licensing contracts with societies.

207. We also note that the complainant has not presented any reactions from retailers or consumers, despite its heavy reliance on the alleged effects which the royalties have on retailers and consumers.

208. In summary, *the complainant's submissions generate feelings instead of providing evidence*. The reader is left with isolated figures, generalities and laments on which he cannot make a judgment. What is lacking are clear, verifiable facts that, if proven, may justify an investigation under Article 82 EC.

209. We now turn to the Four Points:

c) The PPD Calculation Basis and the Standard Rate

210. The complainant expressly states that it does not object to the PPD as the calculation basis.[137]

211. Indeed, the PPD is "fair" because it protects creators' income in two essential respects of which no other calculation basis can take account:

(1) Only the PPD is easy for creators and societies to control. By contrast, creators and societies cannot control transactions between Record Producers and retailers.

(2) Transactions between Record Producers and retailers and, in particular, special discounts on a case-by-case basis are beyond the influence of creators. Such transactions derive exclusively from the commercial policy of Record

137 See point 103 above.

Producers. Creators' income should not depend on this commercial policy or on the risks that this policy implies.

212. For these two reasons (ease of control and lack of influence), the Commission on two occasions advocated a PPD calculation basis. The first occasion was in 1985, when BIEM and IFPI, at the insistence of the Commission, changed their calculation basis from average retail prices to PPD.[138] The second occasion was the Commission's statement of objections in the *Time Warner / EMI* merger case where it said:

> "The investigation has shown that the PPDs are completely transparent. The Commission has found that the PPD is a good benchmark for prices charged to retailers because there is an incentive for record companies to offer as little discounts as possible. The reason for this is that the royalties paid to artists are tied to the PPD and not the net realized price (NRP) paid by retailers. …"[139]

We take it from this statement that the Commission considers the PPD as a fair balance between the interests of record producers and creators.

213. In the same vein, United Kingdom Copyright Tribunal took it as an acknowledged starting point that royalties should be expressed as a percentages of the PPD.[140]

214. Finally, the French *Cour de cassation* has decided that, under Article L. 131-4 of the *Code de la propriété intellectuelle*, the creator must not be remunerated on the basis of prices agreed between the user of the relevant work and a third party (e.g. a distributor).[141]

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138 Discussed in point 57 above.

139 *Id.* (footnote 5), §§ 36 and 46.

140 United Kingdom Copyright Tribunal, 1 November 1991, *British Photographic Industry Limited v. Mechanical Copyright Protection Society*, at point T (2) of the opinion.

141 Cass., 1re chambre civile, judgment of 9 October 1984, Société Masson c/ Jacques Ninio, and judgment of 26 January 1994, Éditions GLENAT c/ François BOURGEON et Sté FRANCE-LOISIRS .

215. The complainant's references to materials from Australia and Switzerland are misleading.[142] [143]

216. We conclude that the PPD is not "unfair". Quite the reverse, *it would be abusive to force creators to be remunerated on the basis of negotiations (between Record Producers and third parties) in which they cannot participate.* Also, as stated, only the PPD provides a safe and cost-effective basis for the auditing that societies must carry out to avoid under-payment by Record Producers.

217. If the Commission accepts this viewpoint, then the only question is whether the *percentage* of the PPD by which the amount of the standard royalty is calculated is

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142 The complainant refers to a case before the Australian Copyright Tribunal (complaint, § 5.14). This reference is selective, out of context, and misleading. The complainant's quotation is from a decision on interim relief: Copyright Tribunal of Australia, 14 June 2000, Universal Music Australia and others v. EMI Music Publishing Australia Pty Limited. In a portion of § 15 of that decision that the complainant does not quote, the Tribunal said:

> "For the present purposes [interim relief] it is neither necessary nor appropriate to determine whether a royalty based on the actual selling price is to be preferred over a royalty based on the list price."

Discussion was postponed until the main case; that is the only meaning of the words "not frivolous" on which the complainant relies. The background of the case was that parallel importation legislation had been changed to allow importation into Australia of records from third world countries with artificially low prices or inadequate copyright licensing regimes. This put enormous pressure on the majors to increase their discounts to dealers. Record Producers and publishers finally settled the case by agreeing that the PPD was the proper basis for royalty calculation.

143 Grossly misleading is the complainant's reference to an "opinion" of the "Swiss Competition Authority" (complaint, §§ 5.17 and 5.26). Annex 12 to the complaint is an internal recommendation dated 15 October 1997 by the "Preisüberwachung" (Surveillance des prix / Sorveglianza dei prezzi) to another Swiss authority, the "Eidgenössische Schiedskommission für die Verwertung von Urheberrechten und verwandten Schutzrechten" (Confederate Arbitration Committee for the Exploitation of Copyrights and Similar Protective Rights). The Swiss Competition Authority ("Wettbewerbskommission") was not at all involved. The "Preisüberwachung" in its recommendation tried to come to grips with lack of evidence for the proper price and only expressed a tendency away from the current tariff. However, the Arbitration Committee in a decision dated 4 November 1997 rejected the recommendation of the "Preisüberwachung", and approved an extension of the current tariff for one year, without any changes, that is: 9,009 % of the PPD, coupled with minimum royalties and maximum track numbers. In further decisions dated 27 October 1998, 13 December 1998 and 1 November 2000, the Arbitration Committee again approved this tariff, subject to minor modifications.

"unfair" within the meaning of Article 82 (a) EC. In our view, this question is to be determined by BIEM and IFPI alone, under their respective freedom of contract, since, as demonstrated, there is neither a disproportion nor an excessive disparity of levels of royalties, compared on a "homogenous basis".

d) Deductions for Retail Discounts

218. The complainant systematically overlooks that there is already an important deduction for discounts. This deduction has been enlarged several times by way of negotiations between BIEM and IFPI.

219. All that can be observed is that *this deduction is general*: It is expressed as a flat percentage of the PPD. It does not depend on specific transactions which occur between Record Producers and third parties on a case-by-case basis. We submit that this feature of "generality" does not suggest "unfairness".

e) Minimum Royalties

220. The complainant is not opposed to minimum royalties as such. Indeed, minimum royalties are justified by two needs:

(1) It must be ensured that creators receive a fair remuneration for the use of their copyrighted works.

(2) Minimum royalties are designed to protect creators to some degree against extremely low list prices which Record Producers alone determine and over which creators have no control. [144]

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144 Thus, the Cour d'appel de Chambéry held in a judgment of 12 December 1983, Case N° 1209-81 *Mentreau v. SACEM* that: "… ni la loi ni les principes du droit des contrats n'interdisent à la

German jurisprudence, which has always upheld minimum royalties, has summarized this simply: *Minimum royalties protect the creator against possible mismanagement of the exploiter for which the creator is not responsible*.[145] The complainant's reference to a decision of the United Kingdom Copyright Tribunal on 1 November 1991 is inappropriate. [146]

221. One example where minimum royalties may apply is the practice of "give-aways", which is admitted in § 5.39 of the complaint. There, the complainant states in relation to a "six-track CD sampler" given away at no charge:

> "As a promotional product, the recording artists waive their respective royalties entitlements on sales of the sampler in recognition of its promotional value."

SACEM de stipuler le paiement d'une redevance minimale calculée à partir des éléments d'exploitation de l'établissement, et destinée à prémunir la SACEM contre la baisse ou la dissimulation des recettes."

145 See, e.g., *Bundesgerichtshof* (Federal Supreme Court, judgment of 28 October 1987 – I ZR 164/85 – "Schallplattenimport III" – [1988] Zeitschrift für Medien- und Urheberrecht 410 at 413; *Oberlandesgericht München* (Munich Court of Appeals), decision of 30 April 1987 – 6 AR 19/85, GEMA / Deutsche Landesgruppe der IFPI, not published: Minimum royalties are necessary to protect creators against a possible devaluation of their rights since creators have no influence on the market behaviour and, in particular, on the price strategies of Record Producers. Cf. page 71 and 72 of the Munich Court of Appeals decision: „Eine Mindestvergütung ist erforderlich, um die Urheberberechtigten vor einer möglichen Entwertung ihrer Rechte zu schützen. Die Urheberberechtigten haben wegen des Abschlußzwangs der Antragstellerin gemäß § 11 WahrnG [Urheberrechtswahrnehmungsgesetz] und wegen der Zwangslizenz des § 61 UrhG [Urheberrechtsgesetz] auf das Marktverhalten des Tonträgerherstellers, insbesondere auf seine Preisgestaltung, keinen Einfluß". See also *Bundesgerichtshof*, judgment of 18 May 1955 – I ZR 8/54 – „Grundig-Reporter" –, [1955] GRUR 492 at 497: A creator is entitled to remuneration even where the user, by way of exploitation of the creator's work, does not achieve the economic benefit that the user desires.

146 In particular, the complainant's reliance on that decision (complaint, p. 44, § 5.34) is out of context. As is clear from the complainant's own quotation from that decision, the Tribunal decided only "on the figures before us". An important part of the context was that the Tribunal, acting as a straightforward regulator, had raised the standard rate from about 8,2 % to 8,5 % of the PPD.

We do not see why creators should do the same as artists: to give up income in recognition of “promotional value”.[147]

222. Since the complainant does not object to minimum royalties as such, the complaint boils down to an objection to the amount of the minimum royalties.

223. This amount is the result of arm’s-length negotiations, covered by the freedom of contract and laid down in the 1998 version of the Standard Agreement.

224. The complainant sets out laments and generalities, but has not furnished concrete and verifiable proof as to why the minimum royalties, accepted in 1998, should have become “unfair” since 1998. In addition, the complainant has not proven that even in the case of lower minimum royalties (which it imagines) the interests of the authors, composers and publishers of music could entirely be safeguarded. For the requirement of such proof we refer to § 31 of the Court’s judgment in *Tournier*.[148]

225. Contrary to the complainant’s allegation[149], *minimum rates do not prevent low consumer prices*.[150] Empirical experience shows that royalties do not affect consumer prices.[151]

226. In addition, minimum royalties are tied to the movement of PPDs on the market by the provisions in the Standard Agreement. Nothing prevents Record Producers from setting the PPD at any low level that they desire.

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[147] This is all the more true where the sampler is promoting products containing works written by other creators. Also, we reiterate that the creators already sacrificed portions of their income for “promotion”. See Article V (24) of the Standard Contract.

[148] The complainant’s allegations that minimum royalties may harm BIEM members (complaint, § 5.34, 2nd bullet point) is an unworldly statement which requires no comment.

[149] Complaint, § 5.26 and § 5.34, 1st bullet point.

[150] Minimum royalties only protect creators against decisions and policies of the Record Producers over which creators have no control. They are a guarantee against dilution of their royalties.

[151] See points 87 to 93 above.

227. Finally, there is a “budget minimum royalty”. This royalty applies to cheap re-releases and is limited to 57 % of the normal minimum royalty. It takes account of a special sales method of the majors.

228. We conclude that the complaint does not set out reasons for an investigation as far as minimum royalties are concerned.

f) Maximum Track Numbers

229. Exactly as with minimum royalties, the purpose of “maximum track numbers” is to protect the earnings and the intellectual property of creators against dilution. Were it not for maximum track numbers, the creator would obtain only a smaller royalty if he has to share it with more than a set number of other creators. Therefore, our observations in respect of minimum royalties are equally applicable to maximum track numbers.

230. The complainant argues that certain of its products are not “viable” on account of maximum track numbers.[152] As stated (point 80 above), the rules on maximum tracks do not prohibit any technical format. Also, this argument is misconceived, and the misconception is a reiteration, *ad abundantiam*, of the complainant’s flawed *leitmotiv*: The complainant suggests that creators in their relation to Record Producers should behave like joint-venturers. However, creators do not act in that capacity.

231. Where a product is not viable, it is the logic of a market economy that this product must be dropped or changed. The mere fact of non-viability of a product does not

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152 See complaint, p. 10, 1st paragraph, § 1.10.

indicate that suppliers of raw materials (here: copyright licenses) are liable of an "abuse" within the meaning of Article 82 EC.

g) Closing Remarks

232. Application of the Four Points does not constitute an "abuse" within the meaning of Article 82 EC. We note that the majors themselves often have similar practices whenever they license out their own rights.

10. The Consequences of the Complainant's View

233. What consequences would occur if, on a theory of "abuse", royalties were decreased to such an extent that BIEM and its members could no longer ensure that creators can receive a fair remuneration?

234. Creators would become disinterested in collective licensing. Societies would lose members, and would no longer dispose of the entire world repertoire. Lack of a full repertoire would cause reciprocal representation contracts and the system of collective licensing to crumble.

235. If the system of collective licensing crumbles, then societies can *no longer* provide a *single license ("licence unique et globale")*. National societies might continue to grant copyright licences. However, there could be either a different rate for each repertoire (that of the French, the Belgian, the Dutch society etc.). Alternatively, there could be a different rate for each territory, which would mean price differences from Member State to Member State. Such consequences would clash with the internal market principle set out in Article 14 (2) EC.

236. Few creators (only those powerful enough to act on their own) would survive economically. Creation would be stifled, and cultures would become uniform, dull, and superficial. Users would have to deal with the remaining creators individually.

237. Under the existing system, each user has access to the world repertoire on a non-exclusive and non-discriminatory basis. By contrast, in a system of multiple negotiations (individual creators dealing with individual users), exclusive licensing arrangements would prevail.

238. All this would be detrimental to the music business generally and even to the majors. The complainant therefore wisely affirms that it does not seek the disappearance of BIEM, of BIEM's member societies, and of the system of collective licensing. At the same time, however, the complainant advocates a "squeeze-out" that would inevitably lead to this situation. Once again, the complainant contradicts itself: It cannot have both – the "squeeze-out", on the one hand, and the continued operation of the existing system, on the other.

D. Conclusion

239. In our view, the complaint should be rejected, and the complainant should be advised thereof in accordance with Article 6 of Regulation N° 2842/98.

240. If, contrary to our conclusion, the Commission wishes to investigate the complaint, BIEM would be grateful for an early opportunity of orally expressing its views, in accordance with Article 9 (3) of Regulation N° 2842/98.

241. In this case BIEM would suggest, among other things, that the Four Points should not be examined in isolation. *The Four Points are an integral part of a negotiated equilibrium*, which is set out in the Standard Agreement. If the Four Points are put in question, then the other parts of the equilibrium are also put in question.

Important concessions by BIEM to IFPI would have to be reconsidered, including the deduction for discounts set out in point s 61 to 67 above. If, for example (and contrary to our view), there were a basis for a declaration by the Commission that the standard rate was "too high", BIEM would reserve the right to make a counter-complaint and seek a declaration that the 10 % deduction for packaging was also too high.[153]

242. Also, BIEM would submit that it is naïve for the complainant to believe that it can push creators into a de facto joint-venture arrangement with the Record Producers. The flip side of such a move would be that the basic royalty would have to be higher and then further escalate as the record becomes more successful.

Respectfully submitted,

Dr. Gerrit Schohe

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[153] See points 66 and 67 above.