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Second Circuit Rules that Yahoo Doesn't Have to Pay Fees to Record Labels for Webcasting Songs

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In a decision applauded by webcasters and lamented by the recording industry, the Second Circuit ruled last week that individualized radio stations—such as those offered by LAUNCHcast and Pandora—are not "interactive services" under the DMCA, freeing the webcasters from the potentially massive financial burden of having to pay licensing fees to record labels for the transmission of sound recordings as part of their services. The decision was the first by a federal court of appeals to examine the hotly-debated issue. The suit, originally filed in 2001 by several labels owned by Sony BMG, including Arista, Bad Boy and Zomba, alleged that LAUNCHcast, a webcasting service run by Yahoo's Launch Media unit, which enables users to create "stations" that play songs within a particular genre or similar to a particular artist or song, violated provisions of the DMCA that required payment of licensing fees for the use of sound recordings in an "interactive" service." The DMCA defines an interactive service as one "that enables a member of the public to receive a transmission of a program specially created for the recipient, or on request, a transmission of a particular sound recording . . . which is selected by or on behalf of the recipient." The provision was intended to distinguish individual playbacks from transmissions "whose primary purposes . . . is to provide to the public such audio or other entertainment programming." That distinction was critical. The DMCA requires payment of royalties, based on a negotiated license, to the owner of a sound recording (in most instances, a record label) for use in an interactive service. For non-interactive services, webcasters need only pay a compulsory or statutory licensing fees set by the Copyright Royalty Board, which are considerably lower than individual, negotiated license fees. The rationale behind the differing licensing schemes was to protect the recording industry from lost sales. As the Second Circuit stated "If the user has sufficient control over the interactive service such that she can predict the songs she will hear, much as she would if she owned the music herself and could play each song at will, she would have no need to purchase the music she wishes to hear." In affirming the jury's finding that LAUNCHcast's service is not "interactive" under the DMCA, the Second Circuit analyzed the functions and features of the service itself, focusing on whether a user can receive a transmission of a program "specially created" for him or her. For the Court, the key issue was "predictability"—to fall within the provisions requiring payment of a sound recording license fee, a service must provide "a degree of predictability-based on choices made by the user-that approximates the predictability the music listener seeks

when purchasing music." The appellate panel found that the LAUNCHcast service does not provide sufficient control to users such that the playlists selected are so predictable that users will choose to listen to the service instead of purchasing music. The court reached that conclusion based on three primary factors. First, the rules governing what songs are pooled in a playlist ensure that the user has no ability to control—much less predict—which songs are pooled for selection. The panel noted that at least 60% of the songs are generated by factors entirely beyond the user's control. Second, the service's rules prevent a user's explicitly rated songs—presumably the ones he or she wants to listen to—from being anywhere near a majority of the songs on a playlist. At a minimum, 20% of the songs are unrated. In addition, when a user rates a particular song, the service "implicitly" rates all the other songs by that artist, subjecting the user to many songs the user may never have heard or may not like. Lastly, the court noted that LAUNCHcast randomly orders playlists—taking into account the DMCA's restrictions on the consecutive play of artists or albums—further restricting the user's ability to choose artists or albums they wish to hear. The court concluded that the only thing a user can predict with certainty is that by rating a song at "zero" the user will not hear that song on that station again. The decision is significant for several reasons. It is the first time a federal appeals court has undertaken a careful, detailed and well-reasoned analysis of the DMCA's provisions related to sound recording performance rights. The decision clearly sets forth the rationale for the different licensing schemes for web transmission of music established by the DMCA, removing a considerable amount of uncertainty to webcasters and others who feared that their business models might be in jeopardy if they faced additional licensing fees. And it parsed the features and functions of the LAUNCHcast service. In doing so, the court has provided significant guidance on the legal, business and technical fronts which may enable future growth and innovation in the space.

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