Harvard Journal of Law & Technology
Volume 27, Number 1 Fall 2013

STRONGER THAN KRYPTONITE? INALIENABLE PROFIT-SHARING SCHEMES IN COPYRIGHT LAW

*Guy A. Rub**

TABLE OF CONTENTS

---

* Assistant Professor of Law, The Ohio State University Michael M. Moritz College of Law. I would like to thank Stefan Bechtold, Omri Ben-Shahar, Chris Buccafusco, Rebecca Eisenberg, Larry Garvin, James Gibson, Fernando Gomez, Stephanie Hoffer, Ariel Katz, Edward Lee, Mark Lemley, Glynn Lunney, Mark McKenna, Sean Pager, Margaret Radin, Aaron Romanello, Andres Sawicki, Kathryn Spier, Peter Swire, Greg Vetter, Joel Waldfogel, Chris Walker, Tal Zarsky, and the participants of the Junior Scholars in Intellectual Property Workshop, Workshop for Junior Researchers on the Law and Economics of Intellectual Property and Competition Law, the American Law and Economic Association Annual Meeting, the Faculty Workshop at the Moritz College of Law, the Technology and the Law Workshop at the University of Haifa, and the Ohio Junior Scholars' Workshop for their valuable comments, Christopher Matgouranis and Matthew Gherlein for outstanding research assistance, and the editors of Harvard Journal of Law & Technology for their suggestions and hard work. All remaining errors are, of course, my own.

I. INTRODUCTION

Superman might be dying. It is not Kryptonite that threatens the Man of Steel's life; it is copyright. In fact, it is a little known and unusual mechanism in the Copyright Act that allows authors to terminate every sale and every license they execute after a few decades. The successors of Jerry Siegel and Joe Shuster, the creators of Superman, are attempting to use this mechanism to terminate the agreement that assigned the copyright in Superman to DC Comics and Warner Brothers.[1] If they succeed, and if the parties fail to reach another deal, the Superman franchise as we know it will cease to exist.

The successors of the creators of Superman are not alone. In the upcoming years, several superstar recording artists might also terminate their old recording agreements with their record companies. In doing so they will take advantage of section 203 of the Copyright Act, which provides that every author can terminate any sale of copyright and any license thirty-five years after its execution.[2] This termination right — which some have called "a time bomb"[3] — is

1. *See* Siegel v. Warner Bros. Entm't Inc., 542 F. Supp. 2d 1098, 1102 (C.D. Cal. 2008); DC Comics v. Pac. Pictures Corp., No. CV 10-3633 ODW (RZX), 2012 WL 4936588, at *1 (C.D. Cal. Oct. 17, 2012).

2. 17 U.S.C. § 203 (2012); *see also infra* Section II.B. Section 203 applies to grants executed after January 1, 1978 (the effective date of the Copyright Act of 1976) and therefore, termination under this provision is possible only starting in 2013.

3. David Nimmer & Peter S. Menell, *Sound Recordings, Works for Hire, and the Termination-of-Transfers Time Bomb*, 49 J. COPYRIGHT SOC'Y U.S.A. 387, 387 (2001).

non-transferable[4] and non-waivable, and it can be exercised "notwithstanding any agreement to the contrary."[5]

In enacting this mechanism Congress seems to have accepted a common supposition that protecting authors by giving them "a second bite at the apple" requires making termination rights inalienable. This Article provides an in-depth economic analysis of this mechanism, and it inquires into whether, when, and how these rights might promote the goals of our copyright system and the welfare of authors. It concludes by finding that termination of transfers, as an inalienable right, likely causes more harm than good, and, contrary to Congress's intent, is probably detrimental to the interests of authors.

Termination rights stand out in our copyright system. Part II of this Article describes this mechanism and suggests that it is difficult to find similar mechanisms in U.S. copyright law, which is typically hostile to inalienable rights. While a similar mechanism does not exist in the laws of other countries, most foreign jurisdictions grant some creators of intellectual property inalienable rights to receive a share of the future revenue stream from their work. For example, the droit de suite doctrine, which is part of the copyright law system in the European Union and most other foreign jurisdictions,[6] gives the creators of fine art an inalienable right to receive a share from future resale of their work. Enacting a similar mechanism in the United States has been considered from time to time and is currently being evaluated by a U.S. Copyright Office study.[7] Patent law, in some foreign jurisdictions, also provides an inalienable right to compensation for employees who develop commercially successful inventions in the scope of their employment.[8] The common theme among these legal mechanisms, as well as other mechanisms that exist in some jurisdictions,[9] is that they force the creator and her assignees and licensees to share some of the future profits from the work or invention.

Part III addresses the efficiency of non-mandatory profit-sharing arrangements. The analysis shows that these arrangements align the incentives of creators and their assignees and licensees, especially if the parties are entering a long-term relationship. It is therefore not

4. The terms "non-transferable" and "inalienable" have more than one meaning. *See* Margaret Jane Radin, *Market-Inalienability*, 100 HARV. L. REV. 1849, 1852–55 (1987). In this Article, non-transferable rights are rights that cannot be voluntarily transferred in any way (including by a sale, a gift, or a will). Inalienable rights are rights that are non-transferable, non-waivable, and non-licensable.

5. 17 U.S.C. § 203(a)(5).

6. *See infra* Subsection II.E.1.

7. *See infra* note 70.

8. *See infra* Subsection II.E.2.

9. *See infra* Subsection II.E.3.

surprising that various profit-sharing arrangements are common in copyright industries.

If society wishes to encourage profit-sharing arrangements, it can do so with three different legal mechanisms. First, the lawmakers can take into account the desirability of profit-sharing arrangements when designing contractual default rules in copyright. Specifically, this Article suggests that it might be desirable to use some profit-sharing arrangements as penalty default rules, which reveal information to the less-informed creator. In fact, the legal regime that existed prior to the enactment of the Copyright Act of 1976 might have served such a function by granting authors a transferable right to receive additional future profits from their work. The advantages of this mechanism as a penalty default rule have not been appreciated in the literature to date.[10]

Property law can provide stronger legal protection of profit-sharing arrangements. Indeed, contractual profit-sharing arrangements might become ineffective in the long run because they do not bind downstream buyers. The advantages and disadvantages of allowing authors to create servitudes to secure their rights under voluntary profit-sharing arrangements are explored in Part III.

Inalienability provides the strongest legal protection of profit-sharing arrangements, and this is, of course, the choice that was made by Congress when it enacted the Copyright Act of 1976. Part IV considers the traditional justifications for the inalienability of termination rights and finds them unconvincing. Traditionally, two main justifications were raised: first, artists are presumably exceptionally weak and in a poor bargaining position, and, second, the future value of their work is unknown prior to commercialization. The problem with these arguments, as well as other arguments that are explored in Part IV, is that it is unclear how they can justify inalienability. Indeed, it is doubtful that uncertainty, which is shared by the sellers and the buyers in this market, should lead to inalienability.[11] Moreover, this Article shows that relying on the extreme weakness of artists, which some have called the "starving artist myth," is problematic.[12] This common narrative seems to incorporate several factual assertions, namely that artists are poor individuals who are taken advantage of by shrewd buyers and that they lack sophistication. Those assertions are factually questionable, and, even if true, provide weak justifications for inalienable rights. Instead, this Article suggests that it would be better to focus on the

10. *See infra* text accompanying notes 101–103103.
11. *See infra* Section IV.B.
12. *See infra* Section IV.A.

structure of the market in which creative works are being bought and sold and try to rectify its inefficiencies.

Indeed, the myth of the starving artist, while questionable in itself, might be a straw man for the real economic factors that are at play with respect to termination rights. Parts V and VI of this Article explore those factors in depth. Part V focuses on the effects of termination rights on the initial negotiation between the creator and buyer. It provides a detailed and novel model for analyzing the effects of termination rights on the creators' compensation and their incentives to create. It shows that given a certain market failure — when competition among buyers of copyrighted works (e.g., book publishers and record companies) is limited — inalienability can improve the creators' total compensation. In that case, mandatory termination rights allow creators to sell their work in two steps. First, the creator sells her pre-termination rights for a price that reflects the buyer's superior market power. Then, decades later, the shoe is on the other foot. Now, the value of the work is known and the creator has the market power when she sells her post-termination rights. Overall, the combined expected price for the work, before and after termination, is expected to increase, which is socially desirable because it improves the incentives to create and increases the quantity and quality of works produced.

On the other hand, Part V also shows that inalienable profit-sharing arrangements, by delaying some of the creator's compensation, reallocate both wealth, from young authors to older and probably wealthier authors, and risk, from the risk-neutral buyer (e.g., a record company) to the author, who is probably risk averse. The reallocation of wealth and risk is likely inefficient and can, by itself, make the costs of termination rights higher than the benefits.

While it is difficult to evaluate whether termination rights, as a whole, improve creators' compensation when transactions between them and their buyers are reached, they create real undesirable effects when termination approaches. Part VI thus analyzes two additional drawbacks of the termination-of-transfer mechanism: one that emerges on the eve of termination and the other shortly thereafter. When termination is approaching, the incentives of the author and the publisher are inefficiently misaligned, often creating an "end-game problem." For example, shortly before termination the publisher might invest inefficiently too little in promoting the work. This Article suggests that even without a change in the statute, this problem could be substantially mitigated by allowing the parties to reach contractual solutions before termination vests notwithstanding the inalienability of termination rights. The highly controversial practice of rescinding old transfers and re-granting them to avoid termination[13] is thus consistent with the goals of the Copyright Act and significantly mitigates the end-game problem and should therefore be enforceable.

Another significant drawback of the termination-rights mechanism relates to the way Congress chose to give the author a second bite at the apple. Unlike droit de suite and similar mechanisms in foreign jurisdictions, which grant creators rights to compensation, termination of transfer gives the author the full property rights in her work. Unfortunately, in many cases commercial exploitation of modern copyrighted works after termination will require the consent of many individuals. Those individuals include, inter alia, the joint authors of the work, the statutory successors of deceased authors, and the current owners of any underlying copyrighted works that were used in making the work. Indeed, many intermediaries in the copyright industries (e.g., record companies) labor to bundle together, prior to production, all the rights required to commercially exploit a work, primarily by entering into a series of complex contractual arrangements. The Copyright Act, by allowing the various authors to terminate these contracts, undoes the publishers' bundling. Securing the consent of all authors after termination requires a complex multi-party negotiation. Such negotiation is typically expensive and can sometimes fail, resulting in underuse of the copyrighted work — a phenomenon known as the "tragedy of the anticommons."[14]

This Article suggests several ways to address this problem. The scope of several doctrines in copyright law, such as the work-made-for-hire doctrine, can affect the magnitude of the problem, and if courts take those effects into account when interpreting those doctrines, the harm from the tragedy of the anticommons can be mitigated.[15] A more comprehensive solution requires legislative reform that grants authors a right to additional compensation (for example, by forcing compulsory licenses) instead of granting them property rights.[16] This switch from property rules protection to liability rules protection,[17] similar to the form of protection common in civil law countries, is expected to promote efficiency.

After exploring in Parts V and VI the costs and benefits of termination rights, Part VII considers whether those rights are currently desirable. It shows that mandatory profit-sharing schemes

13. *See infra* Subsection VI.A.2.

14. *See generally* Michael A. Heller, *The Tragedy of the Anticommons: Property in the Transition from Marx to Markets*, 111 HARV. L. REV. 621 (1998).

15. *See infra* Subsection VI.B.3.

16. *See infra* Section VI.C.

17. *See generally* Guido Calabresi & Douglas A. Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972) (contrasting entitlements protected by property rules and liability rules).

might have been more desirable in the past than they are today. In the past, when the book publishing industry, which used to be the most important copyright industry, was highly concentrated, mandatory termination rights might have been justified. Today, the book publishing industry is more competitive and thus inalienable termination rights are not warranted. The analysis suggests that, in its current form, the disadvantages of the termination-of-transfer mechanism probably outweigh the advantages and harm to authors in other major copyright industries, including the film industry, the software industry, and probably the music industry. The continuous decrease in barriers to entry into many copyright industries is expected to make termination rights even less desirable going forward. Similarly, the model developed in this Article makes clear that the Copyright Act should not grant the creators of fine art inalienable resale royalty rights similar to droit de suite. Such a mechanism cannot be justified in a well-functioning competitive industry, such as the fine art industry.

II. TERMINATION OF TRANSFER AND OTHER INALIENABLE PROFIT-SHARING MECHANISMS

A. Termination of Transfer as an Inalienable Right

Copyright law creates property rights in intangible information goods and initially grants those rights to the author of the work.[18] The author, as the initial owner, can transact in these rights, including by entering into agreements to transfer the rights or any part of them, and by licensing others to use them.[19] In the United States, this power to transfer rights in a work is not just an incidental side effect of the copyright regime, but in many respects is the main reason for its existence. Indeed, because copyright law is perceived as a tool to incentivize authors to invest the resources needed to generate creative works,[20] they must have the power to transfer and license their rights in order to realize monetary gains.[21]

---

18. 17 U.S.C. § 201 (2012).

19. *Id.* § 204.

20. This principle is also expressed in the United States Constitution. U.S. CONST. art. I, § 8, cl. 8 (empowering Congress to secure "to Authors . . . the exclusive Right to their respective Writings" in order "[t]o promote the Progress of Science and useful Arts"). *See also* Mazer v. Stein, 347 U.S. 201, 219 (1954) ("The economic philosophy behind the clause empowering Congress to grant patents and copyrights is the conviction that encouragement of individual effort by personal gain is the best way to advance public welfare through the talents of authors and inventors in 'Science and useful Arts.'"). Other legal systems, in particular civil law jurisdictions, justify copyright law on other grounds and in particular on the author's natural rights. *See generally* Jane C. Ginsburg, *A Tale of Two Copyrights: Literary Property in Revolutionary France and America*, 64 TUL. L. REV. 991 (1990)

Therefore the rights created by copyright law are usually transferable, waivable, and licensable. The United States Congress has expressed hostility to inalienable rights under copyright law through the years[22] and thus has created very few narrowly tailored exceptions to this rule.

Considering Congress's hostility to inalienability, the existence of the inalienable right to terminate all transfers is surprising. Nevertheless, sections 203 and 304(c)–(d) of the Copyright Act provide that at certain times the author of copyrighted work can unilaterally terminate any "transfer" of the copyright. "Transfer" is broadly defined and includes, inter alia, any assignment of copyright and any licensing arrangement.[23] Thus, for example, the author of a song may unilaterally terminate a license allowing a record company to record the song; a performer may terminate an assignment of her rights to a record company that allows it to make copies of an album; and the author of a book may terminate a license to create derivative works based on the book, and thus prevent a movie studio from producing a film.

The Copyright Act explicitly provides that all termination mechanisms "may be effected notwithstanding any agreement to the contrary . . . ."[24] In addition, termination rights cannot pass testate (by

---

(exploring the different justifications for copyright law under French and US law). A full analysis of the inalienable legal mechanisms explored in this Article under such natural rights theories is beyond the scope of this work.

21. *See, e.g.*, Richard Watt, *Copyright and Contract Law: Economic Theory of Copyright Contracts*, 18 J. INTELL. PROP. L. 173, 175 (2010) ("[C]opyright itself is not an incentive mechanism, but . . . it does allow an incentive mechanism, namely contracts, to operate.").

22. The scope of moral rights under the Copyright Act is a good example of Congress's hostility to inalienable rights. Moral rights, which are common in civil law jurisdictions, give the author certain rights in her work — e.g., the rights of attribution and integrity — that in foreign jurisdictions are never transferable and rarely waivable. *See* Neil Netanel, *Alienability Restrictions and the Enhancement of Author Autonomy in United States and Continental Copyright Law*, 12 CARDOZO ARTS & ENT. L.J. 1, 23–26 (1994). For many decades, the United States was one of the few western countries that refused to join the Berne Convention for the Protection of Literary and Artistic Works, partly because it requires ratifying countries to protect such rights. Berne Convention for the Protection of Literary and Artistic Works, art. 6bis, Sept. 9, 1886, 828 U.N.T.S. 221 (adopted by the United States Mar. 1, 1989) [hereinafter Berne Convention]. When, eventually, the United States ratified the Berne Convention in 1989, it adopted an extremely narrow version of moral rights by passing the Visual Artists Rights Act of 1990, 17 U.S.C § 106A (2012). Those rights are not just narrow in scope, applying only to relatively few "work[s] of visual art," but they are also waivable. 17 U.S.C. § 106A(e).

23. 17 U.S.C. § 101.

24. *Id.* §§ 203(a)(5), 304(c)(5). This is a very unusual provision in the Copyright Act. Indeed, while some commentators argue that core principles of copyright law cannot be contracted around, the termination-of-transfer provisions are two of the very few provisions in the Copyright Act that explicitly prohibit it. *See* Guy A. Rub, *Contracting Around Copyright: The Uneasy Case of Unbundling of Rights in Creative Works*, 78 U. CHI. L. REV. 257, 258–59 (2011). In several instances in recent years courts have held that terms that contracted around some core copyright doctrines are enforceable. *See, e.g.*, Montz v.

a will), but instead they must pass intestate, to successors designated by the Copyright Act.[25]

B. Termination of Transfer Under Section 203

Authors are granted the right to terminate transfers by two sections in the Copyright Act: section 203 and section 304(c)–(d). While these two sections share much in common, they differ in their rationales and the historical circumstances that led to their enactment.

Termination rights were introduced into federal copyright law as part of a large revision in 1976. For almost two centuries, beginning with the first federal copyright statute — the Copyright Act of 1790 — copyright protection was granted for a certain period, with the possibility of an extension. Before the Copyright Act of 1976 became effective, copyright lasted for a period of twenty-eight years from the date of publication, which could be extended by another twenty-eight years.[26] The 1976 Act provided for one term of protection, originally lasting the life of the author plus fifty years.[27]

Switching from a dual term of protection to a unitary term denied authors the right to a "second bite" of the revenue stream of their creation. Prior to the Copyright Act of 1976, a grant of copyright extended by default to the first period of copyright protection, while the author reserved the rights in the second period (the renewal period). A transfer of the rights in the renewal period was legally binding only if executed by the party who held the power of renewal when it vested. An assignment by the author was therefore enforceable if she were alive twenty-eight years after publication,

---

Pilgrim Films & Television, Inc., 649 F.3d 975, 979–81 (9th Cir. 2011) (en banc); Forest Park Pictures v. Universal Television Network, Inc., 683 F.3d 424, 429–33 (2d Cir. 2012).

25. 17 U.S.C. §§ 203(a)(2), 304(c)(2). A famous example of this limitation on the author's free will had to do with the rights of John Steinbeck, the renowned Nobel laureate writer. Steinbeck bequeathed the rights to his work to his third wife, Elaine, to whom he was married for eighteen years until his death. However, when the termination rights in the work vested, after Steinbeck's death, his two children from a previous marriage shared those rights with Elaine. Upon Elaine's death, and although her will explicitly excluded those two children, all the termination rights in Steinbeck's work were held by those children and their descendants. Penguin Grp. (USA) Inc. v. Steinbeck, 537 F.3d 193, 196 (2d Cir. 2008); *see also* Larry Spier, Inc. v. Bourne Co., 953 F.2d 774 (2d Cir. 1992) (allowing termination even when it frustrated the deceased author's intent to support his mistress); Ray Charles Found. v. Robinson, 919 F. Supp. 2d 1054, 1065–66 (C.D. Cal. 2013) (allowing seven of Ray Charles' children to terminate certain assignments made by Charles and thus frustrating his clear intent to leave all his rights to the Ray Charles Foundation, a charitable organization supporting the hearing impaired).

26. Copyright Act of 1909, Pub. L. No. 60-349, § 23, 35 Stat. 1075, 1080 (repealed 1976).

27. Copyright Act of 1976, Pub. L. No. 94-553, § 302, 90 Stat. 2541, 2572 (amended 1998).

when renewal became available.[28] If the author died prior to renewal, an assignment was valid only if the statutory successors of the right to renew assigned that right.[29] Consequently, it became standard practice for an author's spouse to sign the agreements in which an author assigned her rights in the first and in the renewal period.[30]

Having one protection period instead of two thus denies the author the ability to reclaim the copyright in the work. Some interest groups therefore lobbied Congress to enact a termination-of-rights provision that would allow authors to do just that.[31] Section 203 is the result of these efforts.

Section 203(a)(3) provides that the author can terminate all transfers thirty-five to forty years after the date of the execution of the grant (typically the date of the agreement).[32] A notice of such intent to terminate must be served not less than two or more than ten years before the date of termination.[33] Section 203 applies to grants executed after January 1, 1978 (the effective date of the Copyright Act of 1976) and therefore, termination under this provision is possible only starting in 2013.[34] Consequently, this provision has not yet been subject to extensive litigation, but it is expected to generate many legal disputes in the years to come.

---

28. Fred Fisher Music Co., Inc. v. M. Witmark & Sons, 318 U.S. 643 (1943).

29. Stewart v. Abend, 495 U.S. 207 (1990).

30. *See* Lydia Loren, *Renegotiating the Copyright Deal in the Shadow of the 'Inalienable' Right To Terminate*, 62 FLA. L. REV. 1329, 1336–37 (2010). This practice could not guarantee that the rights in the renewal period would be successfully assigned because if the author died prior to renewal, those rights, when vested, might be held by someone other than the signing spouse (e.g., another spouse or the children of the author if she is not survived by a spouse). *See, e.g.*, Music Sales Corp. v. Morris, 73 F. Supp. 2d 364 (S.D.N.Y. 1999) (enforcing termination that was exercised by the nephew of the author and the executor of his will while the original assignment was signed by the unmarried author, his parents, and siblings).

31. *Copyright Law Revision: Hearing Before Subcomm. No. 3 of the H. Comm. on the Judiciary*, 89th Cong. 92–94 (1965) (statement of Rex Stout, president, Authors League of America) [hereinafter *1965 House Hearings*]; Jessica D. Litman, *Copyright, Compromise, and Legislative History*, 72 CORNELL L. REV. 857, 891–92 (1987).

32. However, if the grant covers the right of publication, termination is available thirty-five to forty years from the date of publication or forty to forty-five years from the date of execution of the grant, whichever is sooner. 17 U.S.C. § 203(a)(3) (2012).

33. 17 U.S.C. § 203(a)(4). Courts have strictly enforced these formalities, as well as additional formal requirements specified in sections 203 and 304. *See, e.g.*, Burroughs v. Metro-Goldwyn-Mayer, Inc., 491 F. Supp. 1320, 1325–26 (S.D.N.Y. 1980); Nance v. Equinox Music, No. 09-cv-7808, 2010 WL 4340469, at *3 (N.D. Ill. Oct. 22, 2010).

34. As of the time of this writing, very few prominent artists have publically announced their intention to use section 203 to terminate transfers they executed in the late 1970s. It is possible that such threats are made in confidential discussions between artists and their publishers. One noticeable exception is Victor Willis, the former lead singer of the Village People, who is currently fighting to terminate several transfers of rights in songs that he co-wrote in the 1970s. *See* Scorpio Music S.A. v. Willis, No. 11CV1557 BTM (RBB), 2012 WL 1598043 (S.D. Cal. May 7, 2012); Larry Rohter, *A Copyright Victory, 35 Years Later*, N.Y. TIMES, Sept. 11, 2013, at C1; *see also supra* note 311 and accompanying text.

C. Termination of Transfer Under Section 304(c)–(d)

Unlike section 203, which provides termination rights after thirty-five years for works created after 1978, older works have different windows for termination, as specified in section 304(c)–(d). The first of these windows can be exercised fifty-six to sixty-one years after the date in which copyright in the work was secured,[35] and the second can be exercised seventy-five to eighty years after the date in which copyright in the work was secured.[36] Here, too, a notice of intent to terminate must be served not less than two or more than ten years before the date of termination.[37]

The rationale for termination rights under section 304 is different from the rationale under section 203. Until the enactment of the Copyright Act of 1976, copyrighted works were protected for up to fifty-six years. When Congress extended the term of protection, it thought that it would be wrong to grant an additional protection period as a windfall to the current copyright owners and instead chose to give it to the authors.[38] Similarly, when Congress enacted the Sonny Bono Copyright Term Extension Act of 1997, extending the duration period by an additional twenty years, it granted the authors a chance to terminate transfers and to exploit the copyright in this period.[39]

Because termination pursuant to section 304 can be exercised many years after publication of the work and because most works are practically worthless after so many years, not many authors have used

---

35. 17 U.S.C. § 304(c)(3).

36. *Id.* § 304(d)(2).

37. *Id.* § 304(c)(4)(A).

38. From an economic perspective this justification seems weak. If extension of copyright duration is a windfall, there is no economic justification to grant it at all as it does not incentivize creation. In fact, one may even doubt whether such an extension promotes "the progress of Science" and is thus authorized by the Constitution. U.S. CONST. art. I, § 8, cl. 8, *see supra* note 20. The Supreme Court rejected this argument in part because the Court did not view the extension of copyright duration as a windfall at all. Eldred v. Ashcroft, 537 U.S. 186, 214–15 (2003) ("Given [Congress'] consistent placement of existing copyright holders in parity with future holders, the author of a work created in the last 170 years would reasonably comprehend . . . a copyright not only for the time . . . when protection is gained, but also for any renewal or extension legislated during that time."). If, as the Court suggests, authors expected to gain from future extension, their assignees and licensees obviously had the same expectations. Moreover, by allowing the authors to terminate their transfers, Congress did not just deny the assignees and licensees a windfall, but actually caused them harm. Prior to the extension of copyright duration, the assignee/licensee (typically an intermediary, e.g., a publisher) was entitled to a monopoly for a certain period (i.e., 56 years under the Copyright Act of 1909) followed by unlimited competition. In that later period, when the work is in the public domain, the assignee/licensee, unable to stop entrance into the market, still enjoyed a first-mover advantage. When Congress extended the copyright duration but allowed the author to terminate the transfer, the assignee/licensee was denied its potential revenues in this later period.

39. Pub. L. No. 105-298, 112 Stat. 2827, 2827–28 (1998).

this provision to terminate their transfers.[40] The comics industry is a significant exception to this rule. This industry still produces massive revenues from characters and storylines that were created in the 1930s, 1940s, and 1960s.[41] Unsurprisingly, several cases regarding section 304 arose in the comics industry, and more are expected in the next few years.[42] The most significant of these, a dispute that arose in 1997 and has been litigated since 2004, deals with the copyright to Superman. Jerry Siegel and Joe Shuster created Superman in the 1930s and were paid the market rate for their work at the time: $130.[43] Siegel's statutory heirs used the termination window provided by section 304(c) and filed notices of termination in 1997, fifty-nine years after the work was first published and copyright secured. The validity of this notice has been the subject of a long and spiteful legal

40. *See* R. Anthony Reese, *Who's Terminating What? The Termination of Transfers Empirical Study, and Preliminary Data*, *available at* https://www.law.upenn.edu/institutes/ctic/papers/201011/Reese.pdf, at 19–23 (2011) (suggesting that preliminary results of an empirical study of termination notices pursuant section 304 indicate that about 230–260 such notices are filed each year).

41. For example, Superman, who was created in 1932 and first published in 1938, was the main character in two blockbuster movies (*Superman Returns* in 2006 and *Man of Steel* in 2013) and a successful TV series (*Smallville*) in the last ten years, and will be the main character in two upcoming high-budget movies; Batman, who first appeared in 1939, was the main character of the *Dark Knight* trilogy — three critically acclaimed mega-hits released between 2005 and 2012 (two of them earned more than $1 billion each) — as well as several animated TV series and computer games; Spiderman, who first appeared in 1962, was the main character in four mega-hit films released since 2002, which earned more than $3 billion worldwide (the fifth is expected to be released in 2014), as well the subject of a Broadway show. Many other comic book superheroes starred in mega-hit movies in recent years, including the Green Lantern (first published in 1940), Captain America (1941), Fantastic Four (1961), Thor (1962), X-Men (1963), and Iron Man (1963).

42. *See, e.g.*, Michael Cieply & Brooks Barnes, *Disney Faces Rights Issues over Marvel*, N.Y. TIMES, Sept. 21, 2009, at B1 (explaining how Walt Disney's $4 billion acquisition of Marvel Entertainment may be affected adversely by forty-five notices of termination, to become effective in 2014, filed by the successors of Jack Kirby, the creator of some of Marvel's best- known storylines, including X-Men and Fantastic Four). This transaction was later completed, and in 2011, a court invalidated those termination notices because Kirby's work was made for hire. Marvel Worldwide, Inc. v. Kirby, 777 F. Supp. 2d 720, 750 (S.D.N.Y. 2011), *aff'd*, 726 F.3d 119 (2d Cir. 2013); *see also* Marvel Characters, Inc. v. Simon, 310 F.3d 280, 282 (2d Cir. 2002) (concerning the termination rights of Joseph Simon, one of the co-creators of Captain America).

43. Barbara Goldberg, *Check That Bought Superman Rights for $130 Sells for $160,000*, REUTERS, (Apr. 16, 2012, 10:08 PM), http://www.reuters.com/article/2012/04/17/entertainment-us-usa-superman-idUSBRE83G02F20120417. While Siegel and Shuster were not legally entitled to any additional compensation after this initial sale, DC Comics had voluntarily paid them and their families millions of dollars over the years. DC Comics v. Pac. Pictures Corp., No. CV 10-3633 ODW (RZX), 2012 WL 4936588, at *2 (C.D. Cal. Oct. 17, 2012) ("[T]he Siegels and Shusters have been paid over $4 million under the 1975 agreement, not including medical benefits or bonuses."). In addition, after selling their rights in Superman, Siegel and Shuster were hired by DC Comics and paid very generously to continue to develop the story on this emerging successful superhero. *Id.* at *1 ("By 1941, the Saturday Evening Post reported that Siegel and Shuster stood to make over $2 million (in today's dollars) in the next year alone.").

battle between the Siegel family and DC Comics and Warner Brothers, the assignee of some of the copyrights in Superman.[44] The statutory successors of Siegel's co-creator, Joe Shuster, have notified DC Comics and Warner Brothers of their intent to exercise their right under section 304(d) to terminate Shuster's transfer in 2013, seventy-five years after the copyrights in Superman were secured. This notice resulted in another ongoing litigation battle, this one between DC Comics and the Shuster family.[45]

D. Exceptions to the Termination-of-Transfer Power

Sections 203 and 304 provide several exceptions to the right of authors of copyrighted work to terminate transfer. This Section reviews the main exceptions.

The most important exception to the right to termination transfers concerns the definition of authorship itself, and in particular, the work-made-for-hire doctrine. This doctrine provides that in some cases the creator of the work is not the author and initial owner. Instead, in these cases the author and initial owner is the employer of the creator or the person who commissioned the work.[46] In these instances termination of transfer is unavailable.[47] Therefore, the scope of the work-made-for-hire doctrine has a decisive effect on the scope of the termination-of-transfer power.

The definition of "work made for hire," however, makes the scope of this doctrine vague. The definition provides two circumstances in which a work might be considered made for hire. First, a work made for hire includes "a work prepared by an employee within the scope of his or her employment . . . ."[48] Courts apply a multi-factor test to determine whether a work is prepared by an "employee" under this section and look at such factors as the benefits provided to the alleged employee, the level of supervision, the tax treatment of the alleged employee, and so on.[49] In practice, this definition typically applies to salaried employees.[50]

---

44. Siegel v. Warner Bros. Entm't Inc., 542 F. Supp. 2d 1098, 1114–16 (C.D. Cal. 2008).
45. DC Comics, 2012 WL 4936588.
46. 17 U.S.C. § 201(b) (2012).
47. *Id.* §§ 203(a), 304(c).
48. *Id.* § 101.
49. *See* Cmty. for Creative Non-Violence v. Reid, 490 U.S. 730, 751–52 (1989).
50. This test can sometimes create difficulties in distinguishing salaried employees from independent contractors. Thus, for example, one of the difficult questions in the litigation between the successors of Jerry Siegel and Warner Brothers was which parts of the Superman storyline were created as a work made for hire (as the term was defined under the Copyright Act of 1909) while Siegel was an employee of DC Comics and which parts were not. Siegel v. Warner Bros. Entm't Inc., 658 F. Supp. 2d 1036 (C.D. Cal. 2009).

The second circumstance in which a work might be considered made for hire is if it was specially ordered or commissioned as such. However, while this circumstance allows the creator and the party ordering the work to contractually create work-made-for-hire status, the power to do so is limited to nine enumerated categories of work.[51] Some of those categories have broad scope, and include, inter alia, all motion pictures. The scope of other categories, in particular "collective work" and "compilation," is unclear and leaves many questions unanswered. For example, can a record company argue that a record is a collective work or a compilation? Does a "greatest hits" record fit this definition?[52] If the answer is yes, the transfer of rights in these works cannot be terminated. These questions and similar ones will likely be litigated in the years to come.

Another important source of uncertainty is the "derivative work exception." The Copyright Act provides that a "derivative work prepared under authority of the grant before its termination may continue to be utilized under the terms of the grant after its termination, but this privilege does not extend to the preparation . . . of other derivative works . . . ."[53] While this provision clearly protects some derivative creators,[54] the statutory language creates a host of difficulties. First and foremost, the definition of "derivative work" is itself open to interpretation. For example, part of the definition states that "[a] derivative work is a work based upon one or more preexisting works . . . in which a work may be recast, transformed, or adapted."[55] Can a record company argue that a sound recording is a derivative work of the lyrics, and therefore it can utilize the record

51. 17 U.S.C. § 101.

52. *See* David Nimmer, Peter Menell & Diane McGimset, *Preexisting Confusion in Copyright's Work-For-Hire Doctrine*, 50 J. COPYRIGHT SOC'Y U.S.A. 399, 402 (2003).

53. 17 U.S.C. §§ 203(b)(1), 304(c)(6)(A).

54. See infra Subsection VI.B.2.d. The most famous example of the need for this exception was presented after the enactment of the Copyright Act of 1976 when the case of *Stewart v. Abend* made its way to the Supreme Court. 495 U.S. 207 (1990). In that case, governed by the Copyright Act of 1909, which did not include a derivative work exception, the Court held that a production company formed by James Stewart and Alfred Hitchcock is liable for copyright infringement for reproducing and publicly displaying of the classic movie "Rear Window." This case was brought by Sheldon Abend, a literary agent, and the owner of copyright for a short story "It Had to Be Murder," on which the movie was based. Abend purchased the copyright in the renewal period, for a small amount, from Chase Manhattan Bank, the executor of the estate of Cornell Woolrich, the author of the short story who died, prior to renewal, without ever getting married or having children.

A recent case raises a somewhat similar fact pattern with respect to another classic movie: "Raging Bull." See Petrella v. Metro-Goldwyn-Mayer, Inc., 695 F.3d 946 (9th Cir. 2012), *cert. granted* 2013 WL 5430494, (denying, because of laches, an argument that continued commercialization of the movie constitutes copyright infringement because the author of the underlying script passed away before renewal of the copyright in the script, at the time of this writing an appeal on this decision in pending before the Supreme Court).

55. 17 U.S.C. § 101.

even if the writers have terminated their transfers? The term "utilize," which is not defined in the Copyright Act, is no clearer. Can a record company release new copies of a derivative work? Can it create a digital version of the work? Can it license a song from an existing album to be used in a new movie?[56]

Finally, another source of vagueness is found in the provisions stating that the termination power "may be effected notwithstanding any agreement to the contrary . . . ."[57] It is clear that a promise by the author not to exercise her termination power is unenforceable, but what about a provision that states that if the author decides to exercise that right she will compensate the licensee?[58] What if part of the royalties will be contingent on not exercising the right of termination? And can a later agreement between the author, her heirs and/or her statutory successors and the licensee eliminate or reset the clock for the termination power?[59]

These are some of the difficult questions that will likely be litigated in the years to come. This Article does not offer a full doctrinal answer to all of them, but the analysis it provides sheds light on the economic effects of the decisions courts will face.[60]

E. Inalienable Profit-Sharing Mechanisms in Other Jurisdictions

The termination-of-transfer mechanism, which grants authors an inalienable right to have a second bite at the apple, is unique to U.S. federal law.[61] However, in other jurisdictions creators of intangible goods are sometimes granted an inalienable right to receive additional compensation once their creation is proven to be commercially successful.[62] This Section briefly mentions several such mechanisms

---

56. *See* Nimmer et al., *supra* note 52.

57. 17 U.S.C. §§ 203(a)(5), 304(c)(5).

58. *See* Peter S. Menell & David Nimmer, *Pooh-Poohing Copyright Law's "Inalienable" Termination Rights*, 57 J. COPYRIGHT SOC'Y U.S.A. 799, 827 (2010).

59. *See infra* Subsection VI.A.2; *see also* Loren, *supra* note 30, at 1344; Menell & Nimmer, *supra* note 58, at 828–29.

60. *See infra* Subsection VI.B.3.

61. Copyright law in Britain provided the author a second bite at the apple until 1814. *See* Lionel Bently & Jane C. Ginsburg, *"The Sole Right . . . Shall Return to the Authors": Anglo-American Authors' Reversion Rights from the Statute of Anne to Contemporary U.S. Copyright*, 25 BERKELEY TECH. L.J. 1475, 1547 (2010). In Germany, in 2001, a "right to terminate any copyright contract after 30 years if continuation on the existing basis was unreasonable" was included in a draft of a larger revision to the country's copyright law. Reto M. Hilty & Alexander Peukert, *"Equitable Remuneration" in Copyright Law: The Amended German Copyright Act as a Trap for the Entertainment Industry in the U.S.?*, 22 CARDOZO ARTS & ENT. L.J. 401, 414, n. 76 (2004). However, this right was not included in the final version of the bill that was enacted in 2002. id., at 416. Currently there is no similar right to terminate in civil law countries.

62. Interestingly, I am not familiar with any legal system that forces the creator to pay the buyer if her work turns out to be worth less than expected. *See* John Henry Merryman, *The*

and focuses on two of them: the droit de suite doctrine, which is part of copyright law in most civil law countries, and the inalienable right of employees to receive additional compensation for their inventions — a right that has been expanded in many countries in recent decades. The common theme among termination rights, droit de suite, and employees' right to compensation — allowing creators to receive additional compensation for successful creations — will be further explored in other Parts of this Article.

1. Droit de Suite

Droit de suite (French for "right to follow") is a right of creators of fine art, and typically their heirs, to receive a portion of the gross price or the capital gain obtained from subsequent resale of such art.[63] In most jurisdictions this right cannot be transferred or waived.[64]

While many jurisdictions recognize this right, including through a recently adopted European Union directive,[65] the scope of the right and the exceptions to it vary from one country to another.[66] For example, while in France and Germany future royalties used to be based on the gross resale price, in Italy future royalties were based on the capital gains.[67] In the United Kingdom the right is limited to resale through dealers and public auctions.[68]

Federal law in the United States does not recognize such a right, and there is no international obligation to enact it.[69] However, Congress has, from time to time, considered adding it to the Copyright Act, and at Congress's request the U.S. Copyright Office has

---

Wrath of Robert Rauschenberg, 41 AM. J. COMP. L. 103, 111–12 (1993) (suggesting that the logic underlying droit de suite justifies compensation of the buyer if the value of the work decreases over time).

63. John L. Solow, *An Economic Analysis of the* Droit de Suite, 22 J. CULTURAL ECON. 209, 209 (1998); *see also* Netanel, *supra* note 22, at 23–26.

64. *See* U.S. COPYRIGHT OFFICE, DROIT DE SUITE: THE ARTIST'S RESALE ROYALTY, iv (1992) [hereinafter DROIT DE SUITE STUDY]; Michael Rushton, *The Law and Economics of Artists' Inalienable Rights*, 25 J. CULTURAL ECON. 243, 250 (2001).

65. Council Directive 2001/84, 2001 O.J. (L 272) 32, 32 (EC) [hereinafter The EU Directive].

66. *See* Merryman, *supra* note 62, at 104.

67. *See* DROIT DE SUITE STUDY, *supra* note 64, at iii; Monroe E. Price, *Government Policy and Economic Security for Artists: The Case of the Droit de Suite*, 77 YALE L.J. 1333, 1333 (1968). In the European Union the law has recently changed so as to direct member countries to base the calculation of resale royalties on the gross resale price. The EU Directive, *supra* note 65, art. 4.

68. Chanont Banternghansa & Kathryn Graddy, *The Impact of the* Droit de Suite *in the UK: An Empirical Analysis*, 35 J. CULTURAL ECON. 81, 82–83 (2011).

69. *See* Berne Convention, *supra* note 22, art. 14ter(2); Peter Burger, *The Berne Convention: Its History and Its Key Role in the Future*, 3 J.L. & TECH. 1, 36 (1988).

researched the desirability of such an initiative. At the time of this writing, the U.S. Copyright Office is conducting such research.[70]

California is the only state that created a similar statutory right to resale royalties. This legislation was passed in 1976[71] but in May 2012 a federal court struck it down as violating the Commerce Clause of the U.S. Constitution by purporting to regulate transactions that take place wholly outside of California.[72]

2. Employees' Compensation Rights

Federal law in the United States allows employees to freely assign their inventions to their employers, and it does not regulate the terms of these assignments.[73] Therefore, an employee might assign her rights to future inventions for no compensation at all beyond her salary, even if the invention turns out to be extremely valuable to the employer.

In many other countries the law is different. In recent decades, foreign jurisdictions have enacted laws that regulate the compensation that an employee is to receive for inventions. The employer and employee cannot contract around those arrangements. In Austria — the first country to recognize such inalienable employee compensation rights — the employee is given an inalienable right to receive

70. DROIT DE SUITE STUDY, *supra* note 64, at iv-vi; *Copyright Resale Royalty Right*, U.S. COPYRIGHT OFFICE, http://www.copyright.gov/docs/resaleroyalty/ (last visited Dec. 20, 2013) ("The Copyright Office has been asked by Congress to review how . . . a federal resale royalty right for visual artists would affect current and future practices of groups or individuals involved in the creation, licensing, sale, exhibition, dissemination, and preservation of works of visual art.").

71. CAL. CIV. CODE § 986 (West 2000).

72. Estate of Graham v. Sotheby's Inc., 860 F. Supp. 2d 1117, 1126 (C.D. Cal. 2012). At the time of this writing, an appeal of this decision is pending before the Ninth Circuit. It should be noted that the defendant in this case argued that the California statute is also preempted by the Copyright Act and constitutes taking without compensation in violation of the Fifth and Fourteenth Amendments. However, the court did not address these issues as it accepted the defendant's position regarding the violation of the Commerce Clause. *Id.* at 1119; *cf.* Morseburg v. Balyon, 621 F.2d 972 (9th Cir.1980) (holding that California's resale royalties right is not preempted by the Copyright Act of 1909, the Due Process Clause, or the Contracts Clause of the Constitution).

73. *See* 35 U.S.C. § 261 (2006 & Supp. V. 2011); Teets v. Chromalloy Gas Turbine Corp., 83 F.3d 403, 407 (Fed. Cir. 1996) ("[C]ontract law allows individuals to freely structure their transactions and employee relationships. An employee may thus freely consent by contract to assign all rights in inventive ideas to the employer."). Some states limit the types of inventions that can be assigned to those that were created in the scope of employment. *See* Donald J. Ying, *A Comparative Study of the Treatment of Employee Inventions, Pre-Invention Assignment Agreements, and Software Rights*, 10 U. PA. J. BUS. & EMP. L. 763, 766–67 (2008). No state, however, regulates the terms of the assignment, and specifically the employee's compensation (if the invention was created in the scope of employment).

"adequate" royalties in addition to a salary.[74] The law in Japan provides that employees shall receive reasonable compensation for their intellectual labor.[75] British law is more limited and provides that in exceptional circumstances, such as when the employee's invention results in a patent that provides outstanding benefits to the employer, the employee is entitled to an additional compensation, determined by a court.[76]

3. Other Inalienable Rights in Commercially Successful Works

While the droit de suite doctrine and the rights of employees with respect to their invention are recognized in many countries, various foreign jurisdictions enacted additional specific rules that give authors an inalienable right to receive a share of the revenue stream from commercially successful work.

German law, for example, includes a "surprise best-seller clause" which gives the author an inalienable right to receive additional remuneration if the author's compensation is disproportionate with regard to the proceeds from the work.[77] Croatian copyright law includes a similar provision.[78] French law provides that an author is entitled to proportional remuneration for the commercial exploitation of the work, and such right cannot be waived contractually.[79] A recent amendment to the copyright law of India provides, inter alia, that authors whose work is used in films have an inalienable right to receive royalties "on an equal basis" with those to whom they transfer their copyright.[80]

---

74. Ying, *supra* note 73, at 765, 768. Under Austrian law, the employee does not receive additional compensation if she is hired specifically to produce inventions, but this exception requires the showing that the employee's salary is correspondingly higher than comparable employees. *Id.* at 768.

75. *Id.* at 774.

76. MORAG PEBERDY & ALAIN STROWEL, COVINGTON & BURLING LLP, EMPLOYEE'S RIGHTS TO COMPENSATION FOR INVENTIONS — A EUROPEAN PERSPECTIVE 63–65 (2009–2010).

77. William Cornish, *The Author as Risk-Sharer*, 26 COLUM. J.L. & ARTS 1, 8–10 (2002); Hilty & Peukert, *supra* note 61, at 416–18.

78. 1 SILKE VON LEWINKSKI, 1 COPYRIGHT THROUGHOUT THE WORLD § 11:32 (2012).

79. Cornish, *supra* note 77, at 7.

80. Because this amendment was recently enacted, it is unclear how the provision regarding the sharing of royalties will be implemented. *See* Vaishali Mittal & Gurpreet Singh Kahlon, *Welcoming in the New Royalty Regime*, INTELLECTUAL ASSET MANAGEMENT MAGAZINE, Jan. 2013, at 151, 152–55.

III. NON-MANDATORY PROFIT-SHARING SCHEMES

The legal rules that are explored in Part II — termination of copyright transfer, droit de suite, and employee compensation rights — give the creator a right to share in the future profits of successful creations. These arrangements can be analyzed by exploring four questions: First, do voluntary profit-sharing arrangements between the creator and the buyer[81] make sense and what is their economic function? Second, how should the desirability of those arrangements, if they are indeed desirable, affect the design of contractual default rules? Third, is contract law sufficient in providing the legal framework needed for such arrangements, or should property rights secure them too? Fourth, should those arrangements, assuming they are desirable, be mandatory? This Article focuses on the last of these questions — the rationale and the effects of inalienability. However, to put that question in context, this Part briefly discusses the first three questions.

A. The Desirability of Profit-Sharing Arrangements

This Subsection demonstrates that profit-sharing arrangements are common in many copyright industries. These arrangements are established by the parties even when the law does not mandate them, as they serve important economic functions.[82]

In general, profit-sharing arrangements are common in the context of agency relationships, as they partly align the interests of the agent and the principal[83] and are sometimes encouraged by law.[84] They are extremely valuable in long-term relationships because they incentivize the parties to invest in promoting the welfare of the joint endeavor. Thus, sharing profits between economic actors that work together for a long period of time, especially when the future activity

81. I use the term buyer to refer to an assignee or a licensee of the copyright. In most cases the distinction between the two is immaterial as the author can terminate sales and licenses alike.

82. Obviously, the efficiency of those arrangements, as explored in this Section, might explain why they are common but not why the law should sometimes make them mandatory. This point is simple, but it is not made explicit in some of the literature on the topic. *See, e.g.*, Solow, *supra* note 63, at 211; Matthew Vincent H. Noller, Note, *Darkness on the Edge of Town: How Entitlements Theory Can Shine a Light on Termination of Transfers in Sound Recordings*, 46 GA. L. REV. 763, 785–92 (2012).

83. *See, e.g.*, Robert Cooter & Bradley J. Freedman, *The Fiduciary Relationship: Its Economic Character and Legal Consequences*, 66 N.Y.U. L. REV. 1045, 1064–68 (1991).

84. *See, e.g.*, David Gregory, *The Scope of ERISA Preemption of State Law: A Study in Effective Federalism*, 48 U. PITT. L. REV. 427, 439 n.32 (1987) ("ERISA encourages profit sharing and stock bonus trusts . . . .").

of each of them may create externalities that affect the utility of the other, might be efficient.

Copyright industries provide strong support for this argument.[85] In many copyright industries (but certainly not all of them) profit sharing is the industry norm. For example, the standard compensation structure in the recording industry uses a fixed amount called an advance. However, once the revenues from a record reach a certain threshold (which is typically quite high), the artist and the record company share any additional profits.[86]

The typical compensation structure in the book publishing industry is quite similar.[87] In other industries that produce literary works, the typical arrangements are different. For example, most people who write for a newspaper, either as employees or as freelancers, are paid a predetermined fixed amount.[88]

The typical compensation scheme in the software industry is based on a fixed salary.[89] However, bonuses, which in many cases are loosely tied to the company's profits, are common, and options to buy the company's stock are an industry standard.[90] In this way the

---

85. Similar arrangements exist in patent industries as well, in particular with respect to the employee's rights over her valuable inventions or discoveries. *See* Robert P. Merges, *The Law and Economics of Employee Inventions*, 13 HARV. J.L. & TECH. 1, 38–45 (1999) (discussing various profit-sharing arrangements between employees and employers); Richard A. Kamprath, *Patent Reversion: An Employee-Inventor's Second Bite at the Apple*, 11 CHI.-KENT J. INTELL. PROP. 186, 196 (2012) (discussing profit-sharing arrangements between universities and their employees); UNIV. OF CAL., PATENT POLICY (Sept. 4, 1997), http://www.ucop.edu/ott/genresources/policy_pdf/patentpolicy08.pdf (declaring that the University of California system requires pre-assignment of all patent rights of its employees, but also providing a royalty-sharing plan).

86. DONALD S. PASSMAN, ALL YOU NEED TO KNOW ABOUT THE MUSIC BUSINESS 83–103 (8th ed. 2012). Technically, the typical recording agreement includes a profit-sharing scheme for all levels of sales, and the advance is, as the name suggests, just an advance of future royalties. However, in practice, with rare exceptions, advances are non-returnable and thus, economically, they serve as a fixed payment that does not vary with sales.

87. Henry Hansmann & Marina Santilli, *Royalties for Artists Versus Royalties for Authors and Composers*, 25 J. CULTURAL ECON. 259, 269 (2001).

88. *See* Tony Rogers, *Journalism Salaries: What You Can Expect to Earn in the News Business*, ABOUT.COM, http://journalism.about.com/od/careersinjournalism/a/salaries.htm (last visited Dec. 20, 2013).

89. Curt Nickisch, *For Software Developers, A Bounty of Opportunity*, NPR (Sept. 5, 2011, 2:01 PM), http://www.npr.org/2011/09/05/140194803/for-software-developers-a-bounty-of-opportunity. There are, of course, exceptions to this rule, especially in the open source software movement in which programs are produced by dozens or hundreds of contributors who are not subject to any contractual limitations. *See generally* Timothy K. Armstrong, *Shrinking the Commons: Termination of Copyright Licenses and Transfers for the Benefit of the Public*, 47 HARV. J. ON LEGIS. 359 (2010) (discussing termination rights as applied to open source programs).

90. *See, e.g.*, Paul Oyer, *Why Do Firms Use Incentives That Have No Incentive Effects?*, 59 J. FIN. 1619, 1641 (2004); Gavin Clarke, *Microsoft Chucks Bigger Salaries and Cash Bonuses at Staff*, THE REGISTER (Apr. 21, 2011, 11:55 PM), http://www.theregister.co.uk/2011/04/21/microsoft_salary_bonus_increases; *Google Software Engineer Salary*,

employee does not typically receive a bonus that depends on the commercial success of the product she is developing, but of the company as a whole.

The compensation structure in the movie industry is complex. Many creators in this industry are compensated by a fixed amount that does not depend on the movie's future commercial success. Others are paid a fixed amount plus a share of the net profits of a movie, while others, typically the biggest stars in the industry, are paid a fixed amount plus a share of the movie's gross revenues.[91]

Finally, in the fine art industry,[92] artists typically share the profits from their initial sale of each item with an agent or a gallery, but they do not receive a share from future sales of their work.[93]

This short review suggests that profit-sharing schemes, although not mandatory by law, are common in copyright industries and take many forms. This is not surprising. A profit-sharing scheme involves transaction costs that are typically economically justified only when the actions of one actor affect the utility of another, especially in the long run. Thus, for example, when a record company decides to sign a recording artist, it does not make economic sense for the deal to cover only one album. The promotional efforts of the company create a positive externality on the artist's reputation and potential commercial success that typically goes beyond a single album.[94] Therefore, the record company will demand a long-term commitment by the artist. However, having a long-term arrangement for fixed compensation might create a principal-agent problem because the artist might have too little incentive to produce additional commercially successful work and to promote her existing work. Profit-sharing arrangements address those concerns.[95]

GLASSDOOR, http://www.glassdoor.com/Salary/Google-Software-Engineer-Salaries-E9079_D_KO7,24.htm (last visited Dec. 19, 2013).

91. Hollywood studios are notorious for using creative accounting arrangements that lead to movies allegedly not making any profits. Thus, in practice, those in the industry whose compensation is based on a fixed amount plus a share of the profits of a movie are typically paid only the fixed amount. *See* Mark Weinstein, *Profit-Sharing Contracts in Hollywood: Evolution and Analysis,* 27 J. LEGAL STUD. 67, 68 (1998); Gabriel Snyder, *How Movie Stars Get Paid*, GAWKER (Apr. 2, 2009, 8:00 PM), http://gawker.com/5196154/how-movie-stars-get-paid.

92. I include in the fine art industry creators who produce and typically sell very few physical objects — perhaps only one — of each of their works, e.g., a painting or a statue.

93. Merryman, *supra* note 62, at 105–07.

94. Larry S. Karp & Jeffrey M. Perloff, *Legal Requirements That Artists Receive Resale Royalties*, 13 INT'L REV. L. & ECON. 163, 169 (1993).

95. This problem is mitigated if the artist is concerned that commercial failure will negatively affect her other sources of income (e.g., touring revenues) or her future income once the agreement with the buyer (e.g., the record company) expires. *Cf. infra* Section IV.C (discussion the limitation of profit-sharing arrangements in solving the principal-agent problem).

Therefore, those profit-sharing arrangements have several advantages and disadvantages that vary among industries and sometimes among creators. Those arrangements are not created by law, and therefore, neither the legislature nor a governmental agency needs to decide whether profit sharing is desirable in a given situation and what form it should take. Market participants, who are often better informed than government actors (who face a principal-agent problem of their own), make those decisions routinely.[96] The correct conclusion is not that a certain type of profit sharing is desirable or not. The conclusion is that in some cases, some types of profit-sharing schemes are desirable and in other cases, other arrangements, or no future sharing in profits at all, are preferred. Generally, without any legal intervention, the market provides such a menu of possibilities.

B. Profit Sharing and Contractual Default Rules

What is the role of the legal system when the market provides a wide menu of profit-sharing schemes? As mentioned, there are three non-mutually exclusive legal tools to be considered. First, the role of contractual default rules must be analyzed. Second, the ways in which property rights might reflect the general desirability of profit-sharing arrangements should be explored. And third, the need for mandatory profit-sharing arrangements should be considered. This Section discusses the first of those questions — the role of default rules.

The first social goal that can be achieved by smartly designing default rules is a reduction in transaction costs by saving the parties the need to draft their own arrangements.[97] Thus, if most authors and publishers prefer a certain profit-sharing arrangement, making such an arrangement the default rule could save them transaction costs in negotiating and drafting such an arrangement. This argument is however not convincing in the context of copyright law. First, as shown above, while profit-sharing arrangements are common, they differ from one another, even within the same type of creation (e.g., literary work) and the same industry (e.g., the film industry). There is therefore no reason to assume that any profit-sharing arrangement will

---

96. *See generally* FRIEDRICH VON HAYEK, THE ROAD TO SERFDOM (1944) (discussing the superior information of market participants in comparison to central planning entities). See also the famous story *I, Pencil* by Leonard Read which discusses how the production process occurs in "the absence of a master mind, of anyone dictating or forcibly directing these countless actions which bring [the product] into being. No trace of such a person can be found. Instead, we find the Invisible Hand at work." LEONARD E. READ, I, PENCIL: MY FAMILY TREE AS TOLD TO LEONARD E. READ (1958), *available at* http://www.econlib.org/library/Essays/rdPncl1.html.

97. Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87, 93 (1989) ("Lawmakers can minimize the costs of contracting by choosing the default that most parties would have wanted").

be desirable by a majority or even a significant minority of authors and publishers.[98] Moreover, the industries in question are large and are therefore expected to use standard industry agreements and take advantage of economies of scale in drafting and even negotiating those agreements.[99] In other words, the transaction costs in reaching desirable arrangements are probably not high.

A different function of well-designed default rules is to encourage the exchange of information. Thus, when a default rule — commonly referred to as a "penalty default"[100] — is drafted in a way that is undesirable to the better-informed party, that party will typically prefer to contract around it. A suggestion to contract around the default rule conveys information from the more-informed party to the less-informed one. In this context, it is reasonable to assume that the typical buyer (e.g., a publisher, a record company, or another intermediary) is well-informed. Therefore, a default rule that is detrimental to the buyer — for example, one that gives powerful rights to the creator —might encourage the parties to explicitly negotiate a contractual arrangement that differs from the default rule. Doing so will inform the less-informed seller — the artist — of her legal rights.

Interestingly, the copyright regime that existed before the enactment of the Copyright Act of 1976 seems to generally fit this mold. As further explored in Section II.B of this Article, this regime granted the author a right to keep all the copyrights in the work in the renewal period but allowed the parties to contract around that right.[101] As this default rule was detrimental to the buyer, it incentivized the buyer to suggest to the author to contract around it. That suggestion, by itself, conveyed valuable information to the less-informed author.[102] The author was informed that she had a waivable right to reacquire the copyright upon renewal and that the other side (e.g., the publisher) found it worthwhile to buy this right from her. With this information, the author could rationally negotiate over her rights in the renewal period. Indeed, several commentators who have harshly

98. Default rules that are inefficient for many contracting parties might result in real social harm because they tend to cause some parties to be stuck with arrangements that would not have been chosen in the absence of those default rules. *See* Omri Ben-Shahar & John A. E. Pottow, *On the Stickiness of Default Rules*, 33 FLA. ST. U. L. REV. 651 (2006).

99. In fact, even the smaller actors in this industry, e.g., individual authors, are, in many cases, represented by attorneys and/or agents and are member of strong associations. *See infra* note 105.

100. Ayres & Gertner, *supra* note 97.

101. As explained in Section II.B of this Article, that regime did not allow the author to freely transfer the rights in the renewal period if she passed away prior to renewal.

102. It should be noted that authors are not always poorly informed. *See infra* note 105. However, it is reasonable to assume that the vast majority of buyers (including publishers, record companies, and most other intermediaries) are, as repeat players, very well informed.

criticized this regime as ineffective and even illusory might have failed to fully appreciate the value of default rules in conveying information to authors.[103]

A similar regime can deal with the problems addressed by droit de suite or the employee compensation right regime. The law can set a default rule giving the creator of fine art a waivable right to resale royalties and giving an employee a waivable right to special compensation for successful inventions.

The law can also regulate the ritual that the parties need to follow to contract around those arrangements to make sure that this process will be salient.[104] For example, the law can provide that the employee can waive his right for compensation only in a separate document and not if such a waiver is buried in the boilerplate of a long employment agreement.[105] This arrangement and similar ones can guarantee the flow of information and warn the less-informed party — the author or employee — that she is waiving her legal rights.

---

103. *See, e.g.*, Loren, *supra* note 30, at 1344 ("If the renewal term was meant to give authors the opportunity to renegotiate their compensation, permitting assignments of contingent interests made that benefit largely illusory."); Menell & Nimmer, *supra* note 58, at 802 (noting that the "judicial interpretation of the 1909 Act frustrated [Congress's] intent by upholding advance assignments of renewal terms"); Litman, *supra* note 31, at 866 n.56 (arguing that by allowing assignment the Supreme Court was "effectively gutting the reversionary feature of renewal"); *cf.* Molly Shaffer Van Houweling, *Author Autonomy and Atomism in Copyright Law*, 96 VA. L. REV. 549, 602–03 (2010) (arguing that the Supreme Court's decision reduces fragmentation in copyright).

104. *See generally* Ian Ayres, *Regulating Opt-Out: An Economic Theory of Altering Rules*, 121 YALE L.J. 2032 (2012) (explaining how different rituals for contracting around default rules can provide effective notices to the parties).

105. Boilerplate agreements might cause a market failure if creators are not aware of their terms and cannot take them into account when assessing the value of a proposed transaction with their buyers or employers. Under these conditions, the buyers or employers will not compete on the terms of the agreement and inefficiently harsh unilateral terms will be included in it. *See* Guy A. Rub, *Market Solutions to the Boilerplate Problem*, 54 CAN. BUS. L.J. 258, 263 (2013). While many artists might not read or understand the terms of their agreements, it is not clear that such a market failure is common in the copyright industries. Other mechanisms can limit the inclusion of inefficient harsh terms. For example, using entertainment attorneys is common in many transactions between a recording artist and major recording labels, while, in many other cases, authors are represented by managers or agents (whose experience and skills vary). It is enough if any of those parties is aware of the terms of the contract and assists the author in its evaluation. In addition, many creators are members of a powerful professional association that also protects their interests. *See generally* Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure*, 159 U. PA. L. REV. 647, 671–72, 725–27 (2011) (arguing that while disclosure, including of boilerplate provisions, rarely substantially improves laymen's decision-making process, using experts might yield better results). This problem is not entirely separate from the oligopsony problem, which is the focus of Part V of this Article. Indeed, in a highly competitive market it is likely that some buyers will make sure that authors know of desirable efficient terms they are offering. In less competitive markets, the law might need to regulate the disclosure of these terms or other aspects of the bargaining process. *See also* MARGARET JANE RADIN, BOILERPLATE: THE FINE PRINT, VANISHING RIGHTS, AND THE RULE OF LAW 82-109 (2013).

C. Rights Against Downstream Buyers: Profit Sharing and Property Law

Are contractual default rules sufficient to allow the creator and her buyer to establish a profit-sharing arrangement? Contractual rights are *in personam* and thus require contractual privity.[106] Therefore, they cannot bind downstream buyers. In other words, any contractual rights that the author has with respect to a work might sever by a sale to a downstream buyer. Some have suggested that this is one of the main justifications for the existence of moral rights.[107] The argument is that if it is efficient for the artist to exercise moral rights (e.g., the right to integrity of the work) after the work is sold, contracts cannot typically achieve the desired level of control. Instead, a stronger legal mechanism, such as property rights or inalienable rights, is required. This Section explores whether a similar argument can justify either the creation of property rights that will protect the profit-sharing arrangements or inalienability.

Property rights might be able to facilitate some profit-sharing arrangements between the author and her buyer by guaranteeing that such arrangements will not be circumvented by a sale of the buyer's rights. For example, the author of a book would like to guarantee that her rights to receive a share of the profits will not be frustrated when the publisher transfers the rights to a third party and disappears. Similarly, a painter would like to make sure that her right to have a share of every future resale will not be extinguished by the first resale.

The legal system can solve the downstream-buyers problem by granting the authors a servitude in the copyright or, in the case of fine art, in the items in which it is embodied (e.g., a painting). It can alternatively solve this problem by making a profit-sharing mandatory. And finally, it can decide that this problem does not justify legal intervention beyond the scope of contractual rights. The last option — relying on contractual rights — might suffice, because under a profit-sharing arrangement the author's remedies are solely monetary, and therefore, as long as the initial buyer is solvent, contractual rights can protect the author's interests.[108] In other words,

106. *See generally* Robert P. Merges, *The End of Friction? Property Rights and Contract in the "Newtonian" World of On-Line Commerce*, 12 BERKELEY TECH. L.J. 115 (1997) (exploring the need for guarantying contractual privity in the distribution of information goods).

107. Henry Hansmann & Marina Santilli, *Authors' and Artists' Moral Rights: A Comparative Legal and Economic Analysis*, 26 J. LEGAL STUD. 95, 100–02 (1997).

108. The monetary nature of the right also means that if the creation of a property interest is allowed, it will serve as a lien and not an affirmative equitable servitude. *See Recent Cases: Equitable Servitudes — Creation and Kinds — Obligation to Work Copyrights and Pay Royalties*, 45 HARV. L. REV. 577, 586–87 (1932); Zechariah Chafee, Jr., *The Music Goes Round and Round: Equitable Servitudes and Chattels*, 69 HARV. L. REV. 1250 (1956).

profit-sharing arrangements, unlike moral rights, do not require the author to control the use of the work. In many cases, the small likelihood of insolvency of the buyer (typically, a record company or a book publisher) might not justify strong legal protection that, as explained below, is socially costly.

Many legal systems are hostile to the creation of servitudes, especially outside of the realm of real property.[109] Servitudes typically create two related problems: First, they increase transaction costs by requiring buyers to spend resources on evaluating the actual rights they are buying and the legal limitations on these rights. This is sometimes called a notice problem or information-cost problem.[110] Second, by fragmenting the ownership of the item, servitudes discourage future changes in it. This can lead to a tragedy-of-the-anticommons problem[111] because future changes would require the consent of several right holders and not just one.[112] This phenomenon is sometimes called "the problem of the future."[113]

Notice might not be a major problem in intellectual property law. Intellectual property rights are typically registered. While registration of copyright, unlike patents, is not mandatory, it provides considerable benefits[114] and thus the copyright in most commercially successful works is registered. Therefore, requiring servitudes in intellectual property to be registered should not be burdensome and would substantially reduce the transaction costs of verifying the legal rights.[115] In addition, transactions in the copyright of a work are not common and thus the social costs of the servitudes are limited.[116]

---

109. Hansmann & Santilli, *supra* note 107, at 101 ("Under both European and American contract law, a seller of a chattel generally cannot reserve rights in the chattel, of either an affirmative or a negative character, that are enforceable against subsequent purchasers even if those purchasers have notice of the initial seller's intention to reserve such rights."); Molly Shaffer Van Houweling, *The New Servitudes*, 96 GEO. L.J. 885, 908–09 (2008) (discussing skepticism toward servitudes in personal property); *but see supra* note 108.

110. Van Houweling, *supra* note 109, at 893.

111. This phenomenon occurs once an economic activity requires the consent of many property right holders. Transaction costs then rise, holdouts occur, and underuse of the resource can be expected. Heller, *supra* note 14. The tragedy of the anticommons in the context of termination of transfers is explored in detail in Section VI.B. of this Article.

112. *See* Ben W.F. Depoorter & Francesco Parisi, *Fragmentation of Property Rights: A Functional Interpretation of the Law of Servitudes*, 3 GLOBAL JURIST FRONTIERS art. 2 (2003), *available at* http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=1012&context=lepp_papers; Van Houweling, *supra* note 109, at 902–03.

113. *See*, Julia D. Mahoney, *Perpetual Restrictions on Land and the Problem of the Future*, 88 Va. L. Rev. 739 (2002) (exploring this problem in the context of real property); Van Houweling, *supra* note 109, at 900 (exploring the problem in the context of information goods).

114. *See, e.g.*, 17 U.S.C. §§ 205, 411, 412 (2012); William M. Landes & Richard A. Posner, *Indefinitely Renewable Copyright*, 70 U. CHI. L. REV. 471, 496–97 (2003). Termination of transfers also requires registration. 17 U.S.C. §§ 203(a)(4)(A), 304(c)(4)(A).

115. It should be noted that such a mechanism will not violate the United States' international obligations. Indeed, the Berne Convention provides that the enjoyment of the

Notice might be a more significant issue if servitudes are granted with respect to the tangible medium in which a copyrighted work is embodied (e.g., in a painting or a statue) because the rights in those items are not currently registered. Nevertheless, servitudes in physical items might be important in the fine art industry. Fortunately, creators in this industry usually create very few copies, typically only one, of each work. Thus, establishing an effective notice system for those unique pieces of art might not be very expensive.[117] Modern digital technology can further reduce those costs.

There are two reasons why inalienability might marginally mitigate the notice problem with respect to servitudes. First, if the law makes profit sharing mandatory and inalienable, the buyer does not need to spend any resources exploring whether such an arrangement is in place. The buyer knows that profit sharing is required by law and can evaluate the item she purchases accordingly. Nevertheless, some resources must still be spent in exploring the legal rights with respect to the item purchased (e.g., finding out who is the author with whom the profits are to be shared), which might encourage registration. Second, inalienable profit-sharing regimes can also reduce information costs by standardizing the profit sharing arrangement. Under such arrangements the buyer does not need to explore the exact nature of an idiosyncratic arrangement used by the parties that created the servitude.[118] However, inalienability is not a required condition for standardization as property law can dictate standard profit-sharing arrangements to be chosen by the parties. In other words, the law can dictate the exact types of servitudes that are allowed to run with the item and thus reduce the information cost. Finally, the law can also limit servitudes to only valuable works and thus eliminate the information cost of the servitudes in common low-value transactions.[119]

---

rights granted by the Convention "shall not be subject to any formality . . . ." Berne Convention, *supra* note 22, art. 5(2). However, rights that are not granted by the Convention can be subject to formalities. This is why some rights, such as the right to statutory damages, require prior registration. 17 U.S.C. § 412. Termination rights are not granted by the Berne Convention and thus can be subject to formalities, including registration.

116. Van Houweling, supra note 109.

117. *See* Hansmann & Santilli, *supra* note 87, at 276 (discussing the need to have a recording system for fine art).

118. *See generally* Thomas W. Merrill & Henry E. Smith, *The Property/Contract Interface*, 101 COLUM. L. REV. 773 (2001) (discussing how property law and idiosyncratic contractual arrangements affect information costs).

119. This limitation can be implemented in many ways. For example, the law could state that a profit-sharing servitude is enforceable only if future sales exceed a certain amount (similarly, as mentioned, in civil law countries, droit de suite typically applies only above a certain threshold, *see* The EU Directive, *supra* note 65, art. 3) or, alternatively, the fees for the registration of such servitude can be non-trivial and thus guarantee that it will be registered only for valuable items. *See* Van Houweling, *supra* note 109, at 914–16

The "problem of the future" exists when there are many property right-holders with respect to one asset. In those cases, if in the future the asset needs to be put to a new use, the change will typically need to be approved by every right holder. Each right holder would have a veto power and therefore holdout could be expected. Thus, putting the asset to new use might be expensive or impossible.[120] For example, if a negative servitude on a parcel of land prohibits the building of high rise buildings on it, and the servitude is in favor of ten neighboring lots, building the high rise will require the consent of all ten neighbors. In that case negotiation can be expensive and it might fail.

The problem of the future exists in the context of profit-sharing arrangements as well. For example, it is possible that several parties (e.g., the publisher and the author) share the profits from a book, but a movie studio will demand to buy all the rights in that book as a condition of producing a film based on it. In that case, it is possible that the consent of all right holders in the book will need to be secured, which will lead to a difficult multi-party negotiation. Nevertheless, several factors might partly mitigate the problem in this context. First, because the ownership of the copyrights (or, in case of fine art, the article in which the work is embodied) is typically initially divided just between two right holders — the current owner and the author[121] — future negotiation might be easier. Moreover, the parties may address those problems contractually ex ante. For example, they may agree that one of the parties (or a majority of the right holders) be entitled to sell the asset on behalf of all of them. Finally, it is important to note that the problem of the future is worse under an inalienable profit sharing regime than under a regime of voluntary servitudes. Indeed, the core of the problem-of-the-future is the high transaction cost of renegotiation, and therefore it is clear that a solution to the difficulty of contracting is not to legally prohibit contracting at all.[122]

(discussing the significance of keeping transaction costs low compared to the total cost of an item); Guy A. Rub, *The Economics of* Kirtsaeng v. John Wiley & Sons, Inc.*: The Efficiency of a Balanced Approach to the First Sale Doctrine*, 81 FORDHAM L. REV. RES GESTAE, 41, 52 (2013), *available at* http://ir.lawnet.fordham.edu/cgi/viewcontent.cgi?article=1016&context=res_gestae (distinguishing the effects of information costs on cheap and expensive products).

120. This is another application of the general problem called the "tragedy of the anticommons." See *supra* note 111 and *infra* Section V.B for a discussion of this problem.

121. Later in the life of the work the servitude might be held by more parties. For example, the author might die and bequeath all his assets to several heirs. In addition, in some cases there is more than one author to a work. Those issues are discussed in detailed in Section VI.B of this Article.

122. In other situations inalienability can help overcome difficulties in future negotiation. *See generally* Lee Anne Fennell, *Adjusting Alienability*, 122 HARV. L. REV. 1403 (2009) (exploring cases in which inalienability promotes efficiency). However, as further explained in Section VI.B, inalienable termination rights themselves create fragmentation in the

The conclusion is that it is unclear whether property law should allow the creation of servitudes that guarantee that the author's right to a share of the profits will run with the copyright or the tangible item in which it is embodied. Such a right might be efficient if it is registered. However, the problem with downstream buyers probably cannot, by itself, justify inalienability. If the problem requires special legal treatment, servitudes can solve it more efficiently.

IV. THE UNCONVINCING TRADITIONAL JUSTIFICATIONS FOR INALIENABLE TERMINATION RIGHTS

Part III shows that profit-sharing arrangements are common, and in many cases desirable, in copyright industries. It suggests that default rules that provide broad rights to a share of future profits to creators, and possibly a property regime that makes profit sharing a right in rem (against the world), might be justified. However, the Copyright Act of 1976 chose a different path and made termination of transfer, like droit de suite and employees' compensation rights, inalienable.

What are the justifications for denying the author the right to transfer or waive her termination rights? What are the economic justifications for making the droit de suite and employees' compensation rights inalienable?

Traditionally, two arguments have been raised to justify these mechanisms. The first and main argument is that authors are so weak that they are entitled to protection in their interactions with buyers of their work. Some have called this line of reasoning the "starving artist myth."[123] The second argument relies on the fact that the future value of a specific copyrighted work is uncertain. The Supreme Court, for example, used both justifications when it stated that "the termination right was expressly intended to relieve authors of the consequences of ill-advised and unremunerative grants that had been made before the author had a fair opportunity to appreciate the true value of his work product."[124] Similarly, Barbara Ringer, who was later appointed Register of Copyrights, noted that "[t]here is more evidence of a Congressional recognition that author-publisher contracts must frequently be made at a time when the value of the work is unknown

---

copyright in the work. In comparison, a system of voluntary servitudes allows the parties to contractually overcome such problems.

123. *See, e.g.*, Randall K. Filer, *The "Starving Artist" — Myth or Reality? Earnings of Artists in the United States*, 94 J. POL. ECON. 56 (1986); *see also* Merryman, *supra* note 62, at 107 (discussing the "folklore of droit de suite" as a myth).

124. Mills Music, Inc. v. Snyder, 469 U.S. 153, 172–73 (1985).

or conjectural and the author (regardless of his business ability) is necessarily in a poor bargaining position."[125]

However, as explained below, those assertions are not only factually questionable, but they seem to provide a weak justification for inalienability. As such, they have been heavily criticized by some commentators. This Part explores those rationales and explains why they fail to justify inalienability.

This Part also finds several other justifications unsatisfactory: the need of one buyer to control the interactions between other buyers and the creator, the need to provide expressive incentives to authors, and the desire to allow them to exploit works that are currently unexploited. It will be explained that while those motivations might be compelling, it is unclear why inalienability is required in order to satisfy them.

A. The Weakness of Authors: The Starving Artist Myth

The main historical justification for inalienable profit-sharing arrangements is heavily rooted in a romantic notion of the starving artist. The argument is that artists are so poor, weak, unsophisticated, and stressed, and thus in such a "poor bargaining position," that their decisions to sell or license their works should not be binding but instead should be subject to inalienable protection of their interests.[126]

This common narrative of the artist who is too weak to properly handle her economic affairs was further fueled by anecdotal stories about the miserable fate of famous and loveable artists and about the disparity between their gloomy state and the prosperity that speculative dealers gained by transacting in their art. When droit de suite was enacted in France, the story of Jean François Millet's granddaughter wandering hungry while her grandfather's painting sold for a million francs, more than 1,000 times the amount he was originally paid, received much media attention.[127] In the United

---

125. STUDIES PREPARED FOR THE SUBCOMM. ON PATENTS, TRADEMARKS, AND COPYRIGHTS OF THE S. COMM. ON THE JUDICIARY, 86TH CONG., STUDY NO. 31 RENEWAL OF COPYRIGHT 125 (Comm. Print 1961) [hereinafter STUDY ON RENEWAL]; *see also* Loren, *supra* note 30, at 1342–46.

126. *See, e.g.*, STUDY ON RENEWAL, *supra* note 125, at 125 (discussing the author's "poor bargaining position"); *id.* at 235 ("The author today, particularly the young author, often lacks the bargaining power to secure a contract which is fully adequate."); *1965 House Hearings*, *supra* note 31 at 548 (statement by Congressman Miller) (discussing how Congress "weep[s] bitter tears for the poor, impoverished artist who had no business acumen, and who lost his music").

127. Price, *supra* note 67, at 1334–35; *see also* Michael B. Reddy, *The Droit De Suite: Why American Fine Artists Should Have the Right to a Resale Royalty*, 15 LOY. L.A. ENT. L.J. 509, 515 (1995) (giving additional examples of prominent artists whose stories shocked the French press in a period that led to the enactment of droit de suite, including "a widely published drawing which showed an auctioneer pounding his hammer down saying,

States, the torchbearer for the rights of the author to regain his copyright was Mark Twain. In a much-cited statement, Congressman Frank Currier, the chairperson of the House committee that drafted the 1909 Act said:

> Mr. Clemens [Mark Twain] told me that he sold the copyright for [The] Innocents Abroad for a very small sum, and he got very little out of [T]he Innocents Abroad until the twenty-eight year period expired, and then his contract did not cover the renewal period, and in the fourteen years of the renewal period he was able to get out of it all of the profits.[128]

These stories led many to believe that artists are routinely abused and that they need to be paternalistically protected by the legislature. Professor Monroe Price, for example, cites a French writer who summarized the general sentiment that "[i]t is a matter of fact that often artists sell their works for little money and that some years afterward, sometimes after their death, these works are resold for a very high price. To give a participation to the artists or their heirs on this high price is equitable."[129]

There are numerous problems with this justification. First and foremost, legislation based on anecdotes is problematic in itself. As Professors Omri Ben-Shahar and Karl Schneider state: "[t]rouble stories . . . are dubious bases for regulation. They are anecdotes and may not represent a problem at all, much less one extensive and serious enough to necessitate regulation."[130] Indeed, anecdotes, especially salient stories about famous and beloved artists, tend to make a phenomenon seem significantly more common than it actually

---

'100,000 francs, gone!', while two children in rags sitting in the front row shouted, 'Look, one of Papa's paintings!'").

128. *Hearings Before the Comms. on Patents of the S. and H.R. on Pending Bills to Amend and Consolidate the Acts Respecting Copyright*, 60th Cong. 20 (1908). This statement was cited by many later, including by the Supreme Court. Fred Fisher Music Co., Inc. v. M. Witmark & Sons, 318 U.S. 643, 653 (1943).; *see also* Bently & Ginsburg, *supra* note 61, at 1559 (discussing how this example was repeatedly used in the discussions that led to the enactment of the Copyright Act of 1909).

129. Price, *supra* note 67, at 1334–35. A similar argument, inferring from few and questionable examples that there is a widespread problem in the interactions between authors and buyers, can also be found in the legislative history of termination rights. *See, e.g.*, Armstrong, *supra* note 89, at 360 ("[E]xamples of such overreaching [by licensees] are not difficult to locate in the cases construing the termination provisions."); *id.* at 399 ("Siegel and Shuster's situation exemplified a pattern that, the legislative history suggests, occurred all too frequently . . . .").

130. Ben-Shahar & Schneider, *supra* note 105, at 480.

is.[131] In fact, in those cases even the anecdotes themselves are factually questionable, as neither the French Impressionist painters[132] nor Mark Twain[133] were starving because of exploitation by greedy, shrewd buyers.

More importantly, the argument about the artists' poor bargaining position and weakness, i.e., the starving artist myth, is not well defined. It relies on several factual claims that are used interchangeably to construct a compound argument. By lumping different assertions together, it masks the true nature of the problems artists face and offers an easy way to criticize inalienable profit-sharing arrangements. The most common ways in which artists are portrayed in this narrative are as poor, immature, unsophisticated, and inexperienced individuals who are being taken advantage of by dealers who are wealthy, well-educated repeat buyers. This portrayal is not only factually questionable, but it also provides a weak justification for termination rights.

This Article instead suggests that inalienability might be better justified when the artists' position is examined by exploring the level of competition, i.e., the market power, among buyers.

1. Are Artists Poor, and, if so, Are Termination Rights the Solution?

The first, and possibly most salient part of the starving artist myth, characterizes the artist as extremely poor. A related narrative paints buyers as rich and the transaction between the artist and the buyer as one that makes the first even poorer and the latter even

---

131. Behavioral economists call this phenomenon the availability bias. For a discussion of this bias and its effect on lawmakers, *see* Christine Jolls, Cass R. Sunstein & Richard Thaler, *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1518–19 (1998).

132. Merryman, *supra* note 62, at 108 (explaining that most buyers of the Impressionist paintings were not wealthy, but dealers on the fringes of the French art scene. Those paintings had little market value and most of them failed commercially.).

133. While the story of Mark Twain is commonly referred to in discussions of termination rights, it is historically incomplete and misleading. Mark Twain was anything but a starving, unappreciated artist who was taken advantage of by a speculator buyer. Mark Twain was tremendously popular during his lifetime and made considerable sums in royalties on his books. His wife was a member of one of the wealthiest families in the country at the time. Twain did lose considerable amounts of money, but not by selling his works for pennies to a greedy publisher. Twain lost his money by making a series of very poor investments. In fact, the worst investment Twain made, which cost him millions of dollars in today's values, was trying to get into the publishing business. *See* GEOFFREY C. WARD & DAYTON DUNCAN, MARC TWAIN: AN ILLUSTRATED BIOGRAPHY 124, 140–41, 156–57 (2001). Similarly, the story of the co-creators of Superman, who received only $130 for their story, which later generated millions, fuels analogous sentiments. *See, e.g.*, Armstrong, *supra* note 89, at 399–400. It is, however, rarely mentioned that the creators of Superman had difficulties convincing publishers to publish their story, that they received the market price for their work, and that later they received considerable amounts both for their original story and for continuing to develop it. *See supra* note 43.

richer.[134] Many anecdotal stories support this narrative, including the one regarding the hunger of Jean-François Millet's family,[135] or the one about the extreme poverty in which Vincent van Gogh lived.

This is also the characterization that attracted much of the criticism of the starving artist myth. Professor John Henry Merryman called it "the Folklore of the droit de suite," and, by exploring various historic and current examples, suggested that "it has little connection with reality" and is "demonstrably false."[136] Monroe Price called it "the theology of droit de suite," and he described it cynically:

> The droit de suite springs from a nostalgic recollection of the late nineteenth century. It is a case, not unusual, of legislation passed or posed to correct a situation that no longer exists with the intensity that provoked reform. . . .
>
> At its core is a vision of the starving artist, with his genius unappreciated, using his last pennies to purchase canvas and pigments which he turns into a misunderstood masterpiece. The painting is sold for a pittance, probably to buy medicine for a tubercular wife. The purchaser is a canny investor who travels about artists' hovels trying to pick up bargains which he will later turn into large amounts of cash. Thirty years later the artist is still without funds and his children are in rags; meanwhile his paintings, now the subject of a Museum of Modern Art retrospective and a Harry Abrams parlor-table book, fetch small fortunes at Park-Bernet and Christie's…. The *droit de suite* is *La boheme* and *Lust for Life* reduced to statutory form.[137]

Several other scholars that commented on the poverty of artists, especially in the context of justifying inalienable profit-sharing arrangements, have also questioned the accuracy of this assertion.[138]

---

134. *See supra* note 129 and accompanying text.

135. *See supra* note 127 and accompanying text.

136. Merryman, *supra* note 62, at 107–08.

137. Price, *supra* note 67, at 1334–35 (internal citation omitted).

138. *See, e.g.*, Elliot C. Alderman, *Resale Royalties in the United States for Fine Visual Artists: An Alien Concept*, 40 J. COPYRIGHT SOC'Y U.S.A. 265, 280–81 (1992) ("The notion of starving artists being exploited by wealthy, savvy investors may not do justice to reality."); William A. Carleton, III, *Copyright Royalties for Visual Artists: A Display-Based Alternative to the Droit De Suite*, 76 CORNELL L. REV. 510, 537–38 (1991) (suggesting that more empirical evidence is needed).

While comprehensive empirical research on the wealth of creators is lacking, the empirical evidence that does exist seems to contradict the myth of the starving artist. One important study, conducted by economist Randall Filer, concluded that artists' lifetime earnings "very closely approximate what they could achieve in non-artistic pursuits."[139] This is a comprehensive study, although its main shortcoming, other than its age, is that it did not accurately isolate only those artists who are creators.[140]

Other empirical studies that focus on a group of creative artists reveal that many of them rely on earnings from non-creative (e.g., teaching), and sometimes non-artistic (e.g., waiting tables) labor, and sometimes even the earnings of their spouses, but that, overall, their earnings are typically quite similar to those of the general population.[141]

More importantly, even those who believe that the starving artist myth is factually correct (or those who are concerned that while the myth might not be generally true a significant number of artists still starve) should be hesitant to support inalienable profit-sharing arrangements.

First, both termination rights and droit de suite do not seem to effectively address the poverty of artists. Both mechanisms provide artists additional compensation years after creation when they are less

---

139. Filer, *supra* note 123, at 59. The study relied on 1980 census data, and it also concluded, inter alia, that artists are younger than the general working force and, perhaps contrary to popular belief, that their work is more stable, i.e., relatively few of them leave the profession. Relying on census data allowed Filer to eliminate much of the selection bias that might exist in other studies, but it may have created a reporting bias that made artists' earnings appear lower than they were, mainly because the self-employment of many artists allows them to underreport their earnings, primarily for tax purposes. *Id.* at 60–61.

140. Ideally an empirical study should explore the earning and wealth of those artists who create and sell (or aspire to create and sell) their work. Unfortunately, the classifications employed in the census data that were later used by Filer were sometimes over-inclusive as they included non-creators, such as postsecondary teachers of art. At the same time, in other respects they were under-inclusive because they only included those whose *primary* source of income was from one of the census categories for artists. Thus, an aspiring artist with most of her income coming (in the year of the census) from waiting tables was not included in the data, which is, as Filer concedes, unfortunate. Filer, *supra* note 123, at 59-60.

141. For example, economists Gregory Wassal and Neil Alper surveyed New England artists and found that the median personal income of artists surveyed was only 1.6 percent lower than that of the general labor force (while their family income was 11.3 percent higher). Economist Richard Caves explored similar surveys regarding Canadian writers, U.S. visual artists, Australian artists, and 19th and 20th century etching artists and concluded that "[o]ther surveys of practicing artists confirm these conclusions [of the Wassal and Alper study]." RICHARD E. CAVES, CREATIVE INDUSTRIES: CONTRACTS BETWEEN ART AND COMMERCE 78–81 (2000). At the same time, those studies suggest that the variance among artists is more significant than that of the general labor force and therefore focusing on the median income of the artist might not reveal the full picture of the state of the poorest artists.

likely to be poor.[142] Second, there are other legal mechanisms that better address the unfairness of transactions that are made under conditions of extreme poverty. In particular, the doctrine of economic duress in contract law[143] might provide a better solution to this predicament. The doctrine is properly applicable only in extreme situations in which a buyer takes illegitimate advantage of an artist's poverty which results in unfair terms.[144] Moreover, once duress is proven, it provides the artist with a powerful and immediate remedy — a right to void the contract.[145] The Supreme Court also suggested that even if the artist's rights to a share of the profit is alienable, assignment of this right might not be enforced if made "under oppressive circumstances" and "where the author was under such coercion of circumstances that enforcement would be unconscionable."[146]

2. Are Artists Unsophisticated, and, if so, Are Termination Rights the Solution?

Another component of the argument regarding the weakness of artists is the supposition that even if artists are not poor, they are unsophisticated, immature, uninformed, or inexperienced while their buyers, to the contrary, are well-educated repeat transactors.[147]

This paternalistic approach also drew criticism. Several scholars have criticized it as factually and normatively questionable.[148] Similarly, the Supreme Court, when considering whether the right of

---

142. Merryman, *supra* note 62, at 117 ("'The droit de suite is not designed . . . to come to the aid of needy artists . . . . [I]f success strikes, the income from resale proceeds will be trivial in comparison with that from first sales . . . ."). *See also infra* Section V.B (exploring how inalienable profit-sharing arrangements transfer wealth from young artists to older, and probably wealthier, artists).

143. *See generally* ROBERT A. HILLMAN, PRINCIPLES OF CONTRACT LAW 198–203 (2d ed. 2009) (discussing the principles of duress); Melvin Aaron Eisenberg, *The Bargain Principle and Its Limits*, 95 HARV. L. REV. 741 (1982) (discussing circumstances in which bargained-for contracts should not be enforced).

144. *See* RESTATEMENT (SECOND) OF CONTRACTS § 176(2)(c) (1981).

145. *See id.* § 175(1).

146. Fred Fisher Music Co., Inc. v. M. Witmark & Sons, 318 U.S. 643, 656–57 (1943).

147. *See, e.g.*, M. Witmark & Sons v. Fred Fisher Music Co., Inc., 125 F.2d 949, 955 (2d Cir. 1942) (Frank, J., dissenting) (taking judicial notice that "authors are hopelessly inept in business transactions"), *aff'd*, 318 U.S. 643 (1943); Thomas F. Cotter, *Pragmatism, Economics, and the Droit Moral*, 76 N.C. L. REV. 1, 68 (1997) (discussing the argument that "artists, like children, need to be protected from their own poor judgment"); *cf.* STUDY ON RENEWAL, *supra* note 125, at 125 (noting that "it has often been said that the renewal provision was based on the familiar imprudence of authors in commercial matters," although suggesting that "[w]hile superficially logical, there is nothing in the legislative history to support this supposition").

148. *See, e.g.*, Neil Netanel, *Copyright Alienability Restrictions and the Enhancement of Author Autonomy: A Normative Evaluation*, 24 RUTGERS L.J. 347, 418–19 (1993); Cotter, *supra* note 147, at 67; Hansmann & Santilli, *supra* note 107, at 126–27.

an author in the renewal period should be assignable, has sarcastically stated:

> The policy of the copyright law, we are told, is to protect the author — if need be, from himself — and a construction under which the author is powerless to assign his renewal interest furthers this policy. We are asked to recognize that authors are congenitally irresponsible, that frequently they are so sorely pressed for funds that they are willing to sell their work for a mere pittance, and therefore assignments made by them should not be upheld.[149]

The Court also mentioned the story of Mark Twain[150] and noted that even under the default rules regime, pursuant to the Copyright Act of 1909, he was able to protect his interests and enter into a deal with his publisher without assigning his rights in the renewal period.

Nevertheless, there is probably a disparity between the experience level of sellers and buyers of creative works. While most of the buyers in this market are experienced repeat transactors (such as record companies and publishers), the experience level of artists is probably limited. This inequality is mitigated by using lawyers and agents, who are repeat players.[151] In addition, many creators are members of powerful professional associations (e.g., the Authors Guild, the Writers Guild of America, or the Songwriters Guild of America) that also protect their interests.

However, even if one believes that the artists' lack of experience and sophistication requires legal intervention,[152] existing inalienable profit-sharing schemes, such as termination rights as well as droit de suite, seem like a weak and inappropriate solution to the problem. Those mechanisms neither improve the bargaining process nor limit the enforceability of the contracts reached (except with respect to promises to circumvent the profit-sharing arrangements, promises whose lack of enforceability becomes relevant many years in the future). Merryman criticizes this rationale for similar reasons: he questions why the law does not trust the artist to effectively negotiate

149. *Fred Fisher Music*, 318 U.S. at 656.

150. *Id*. at 653–54.

151. *See supra* note 105.

152. This is not a trivial position to take. In many cases the law does not prevent a seller from selling her property, even very valuable property, to a more sophisticated buyer. See, for example, the official comment to section 2-302 of the Uniformed Commercial Code, which deals with unconscionable contracts. This comment makes it clear that: "The principle [of unconscionability] is one of the prevention of oppression and unfair surprise … and not of disturbance of allocation of risks because of superior bargaining power." U.C.C. § 2-302 cmt. 1 (2011–2012).

her resale rights when it trusts her to set the initial sale price of the work, which is significantly more crucial to her financial wellbeing.[153]

Indeed, even if the concern of unequal sophistication and experience level requires legal intervention, solutions should focus on the time of negotiation. They could include procedures that would encourage the parties to seek professional counseling,[154] improve the disclosures made prior to such transactions,[155] or slow down the negotiation process,[156] by, for example, providing a short cooling-off period.[157]

3. The Buyers' Market Structure

The analysis in the previous pages suggests that even if artists are poor, which is factually doubtful, and even if they lack sophistication, these conditions cannot properly justify inalienable termination rights or the doctrine of droit de suite. This Article instead suggests that it is better to focus on the artists' vulnerability in the context of the buyers' market. When the buyers' market is uncompetitive, artists, even if they are wealthy and sophisticated, might need to deal with buyers (e.g., record companies) who have market power that they lack. This weakness is not attributed to or controlled by the artists.[158]

---

153. Merryman, *supra* note 62, at 123.

154. There are various ways to encourage professional counseling. In other areas, the law encourages representation by, for example, placing additional duties on lawyers or brokers when they are dealing with unrepresented parties, or by giving the unrepresented party a stronger claim to avoid the result of full enforcement of their obligations. *See, e.g.*, Am. Software, Inc. v. Ali, 54 Cal. Rptr. 2d 477, 480 n. 3 (Cal. Ct. App. 1996) (representation by counsel is a strong indication of the lack of procedural unconscionability); Monetary Funding Grp., Inc. v. Pluchino, 867 A.2d 841 (Conn. App. Ct. 2005) (the clean hands doctrine prevents a lender from collecting on certain defaulted loans that were reached with an unrepresented party).

155. *See generally* Hansmann & Santilli, *supra* note 107, at 126 ("[I]f individuals are well informed, one cannot make them better off by refusing to enforce contracts they might choose to enter into."). *But see* Ben-Shahar & Schneider, *supra* note 105 (arguing that in many cases providing better information to an unsophisticated party is complex and it typically fails to improve that party's decision making process).

156. One mechanism that is already in force to slow down the negotiation process and inform the parties of the significance of the transaction is the writing requirement. 17 U.S.C. § 204(a) (2012).

157. A "cooling-off" right, which is usually inalienable, allows a transactor, who is typically subject to aggressive sales tactics, to cancel the deal during a certain, typically short, period of time after it is reached. *See* Omri Ben-Shahar & Eric Posner, *The Right to Withdraw in Contract Law,* 40 J. LEGAL STUD. 115, 119–20 (2011); Shmuel I. Becher & Tal Z. Zarsky, *Open Doors, Trap Doors and the Law*, 74(2) LAW & CONTEMP. PROBS. 63, 66 (2011). It is doubtful that in a typical deal between an author and a buyer such aggressive tactics are common.

158. See M. J. Trebilcock, *The Doctrine of Inequality of Bargaining Power: Post-Benthamite Economics in the House of Lords*, 26 U. TORONTO L.J. 359, 364–65 (1976) (suggesting that in determining the enforceability of standard form agreements courts should focus on the level of competition among the providers of such agreements).

Part VII of this Article explores whether these conditions exist in modern copyright industries, and finds that they typically do not, though the music recording industry might be an important exception.

If the buyers' market is uncompetitive, and if such conditions cause inefficiencies, can inalienable profit-sharing arrangements help mitigate them? Some commentators are skeptical. Professors Henry Hansmann and Marina Santilli, for example, stated their position quite bluntly in their analysis of moral rights: "It is now a familiar point, however, that if individuals are well informed, one cannot make them better off by refusing to enforce contracts they might choose to enter into."[159] Part V of this Article challenges this assertion and shows that under certain conditions, primarily the lack of competition among buyers, fully informed sellers can be made better off by granting them certain inalienable rights to a share of the profits from their work.

In conclusion, the starving artist myth is a powerful narrative and it convinced legislators to enact inalienable profit-sharing arrangements. The myth is comprised of several assertions, the most common of which is that artists are poor and unsophisticated. These assertions provide a weak justification for inalienability. Instead, this Article suggests that the question should not be whether the artists are poor, but whether the market in which they operate is competitive.

B. The Uncertain Future Value of Copyrighted Works

The other traditional justification for the termination mechanism is the difficulty of appraising the value of art before its commercialization. Professor Lydia Loren, for example, has suggested that:

> Many believe that Congress based the [termination mechanism] on a paternalistic desire to protect creative individuals lacking business acumen. This Article demonstrates that Congress was much more concerned with the valuation problem inherent in creative works, a valuation problem that is particularly acute prior to the commercial exploitation of a work.[160]

As a factual matter it is probably true that Congress and the Copyright Office did place significant weight on the uncertain value

159. Hansmann & Santilli, *supra* note 107, at 126.
160. Loren, *supra* note 30, at 1329.

of creative works.[161] In particular, they were concerned that this uncertainty causes works that turn out to be very successful to be sold for modest amounts.

This justification, in itself, is weak. While it is true that prior to commercial exploitation the value of the work is difficult to evaluate,[162] it is unclear why this should justify a termination mechanism, especially an inalienable one. From an economic perspective, prior to commercialization the work might be a risky investment. It is risky for the seller, but it is similarly risky for the buyer.[163] The risk can be placed, in whole or in part, on the author or the buyer, who is typically an intermediary (such as a publisher or a record company). As further analyzed in Section V.B, the termination mechanisms place some of the risk — the risk of whether the work will be commercially profitable in thirty-five years — on the author and prevent her from transferring this risk to the buyer.[164]

Typically, it is socially efficient to transfer risk to parties that can better handle that risk.[165] The parties themselves typically know which of them can better handle risk, and thus mandatory rules that prevent risk assignment are not common.[166] Moreover, in most cases, the buyer-intermediary can handle the risk much better than the seller-author. The intermediary's portfolio typically includes many artists, and thus the aggregate risk it faces is considerably smaller than the risk associated with any single work. For that reason, some commentators have suggested that droit de suite rights are inefficient because they prevent the transfer of risk (in that case, some of the risk of future profitable resale) to the party that can best handle it.[167] Part V below further analyzes the effects of uncertainty on the desirability of inalienable profit-sharing rights.

---

161. *See, e.g.*, *Study on Renewal*, *supra* note 125, at 188 (suggesting that one motivation for the renewal provision is "the recognition that when most copyright bargains are made there is no way to judge the ultimate value or life of the work"); *supra* text accompanying note 125.

162. *See* CAVES, *supra* note 141, at 2–3.

163. *See infra* note 197 and accompanying text.

164. The author cannot transfer this risk to the publisher because the author is prevented from selling her post-termination rights. 17 U.S.C. §§ 203(b)(4), 304(c)(6)(D) (2012). This also means that the author cannot buy insurance to deal with this risk.

165. *See* Richard A. Posner & Andrew M. Rosenfield, *Impossibility and Related Doctrines in Contract Law: An Economic Analysis*, 6 J. LEGAL STUD. 83, 90–92 (1977).

166. Assigning risk is typically prohibited if the resulting moral hazard might be socially destructive. Thus, for example, insuring for liability for intentional criminal activity is prohibited in many jurisdictions. *See, e.g.*, Cal. Civ. Code § 1668 (West 2000). This justification is not applicable to termination rights.

167. *See, e.g.*, Hansmann & Santilli, *supra* note 87, at 262; William M. Landes & Richard A. Posner, *An Economic Analysis of Copyright Law*, 17 J. LEGAL STUD. 325, 327 (1989) (suggesting that "such principles reduce the incentive to create by preventing the author or artist from shifting risk to the publisher or dealer").

C. Agency Costs and Collective Action Problems Among Buyers

While termination rights are typically justified by the artists' weakness or by the uncertainty regarding the value of the work, the literature on droit de suite provides an additional justification based on the long-term relationship between artists and buyers of art[168] that might be applicable to termination rights as well. This Section explains this argument and shows why it is a valid, yet weak, justification for inalienability.

The demand for many types of copyrighted works, including many records, books, and movies, is affected by the reputation of the author. When a work becomes successful it creates a positive externality for other works (past and future) of the same author.[169]

This phenomenon creates an evaluation problem and an interesting link between different buyers. When the buyer determines the value of the item she is buying (whether the physical object in which the creative work is embodied or the copyright in that work), she can take into account the artist's current reputation, but she does not know what actions the artist will take in the future that will affect the value of that item. Will the artist continue to produce valuable work that will increase the value of her portfolio? Will she instead be associated with scandalous actions that will decrease the value of her works? In that respect, because the creator is able to take actions that will affect the value of the work, she is an agent of the buyer, and the well-known problem of the principal-agent relationship emerges.[170] The principal (buyer) is concerned that the agent (artist) will take actions that will promote the agent's interests even if those actions will damage the principal. These concerns might cause the principal-buyer to be willing to pay less for the work or to refrain from buying it at all.

How can the parties address the principal-agent problem? As discussed in Section III.A, one way to minimize agency costs is to enter into a profit-sharing arrangement between the current owner and the author. In that way, the agent will internalize some of the outcomes of her actions and will care about the future value of the work. One significant drawback of this solution, however, is that the internalization cannot be perfect, and in some cases, it will not provide a strong enough incentive for the author to maximize the

168. *See, e.g.*, Hansmann & Santilli, *supra* note 87, at 264–65.

169. In technical terms, this means that the cross elasticity of demand between the two works is positive, or that the works are complementary goods.

170. *See* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976); *see also infra* Section VI.A.

value of her old work.[171] For example, imagine a situation in which the author is entitled to 10% of the future resale value of a certain work, which is currently valued at $1,000. The author now considers whether to take an action that will increase the value of the work by 20% and will cost her $100. While it is socially efficient to take this action (it is an action that costs $100 and produces a total social revenue of $200), it is undesirable for the creator (it costs $100 and will generate only $20 for her) and will not be taken.[172]

If, however, the author enters profit-sharing arrangements with many buyers, she will have more "skin in the game" and will be better incentivized to take profit-enhancing actions. For example, if the author from the previous example entered profit-sharing arrangements that allow her to receive 10% of the future resale price of ten of her works, each valued at $1,000, then she will take an action (e.g., donate works to charity or create another popular work) that costs $100 and increases the value of each work by 20%. Her benefit from this action is now $200,[173] which is greater than the cost. It is therefore in each buyer's interest that the author enters profit-sharing arrangements with other buyers.[174] Buyers, however, typically do not act together and thus cannot be sure that the seller will enter into profit-sharing arrangements with other buyers. Legally mandated inalienable profit-sharing arrangements provide a solution by guaranteeing to all buyers that those arrangements are in place with every other buyer.[175]

While this is a reasonable argument, I do not believe that it is persuasive, for several reasons.[176] First, in most cases, the author will have a strong incentive to improve her reputation, as she receives significant benefits from it. The most obvious benefit is a higher

---

171. This is a general problem in any agency relationship. Profit sharing between the agent and the principal can only mitigate, but not eliminate, the agency problem. *See* Jensen & Meckling, *supra* note 170, at 312–13 (explaining that the agent will only take actions as long as the agent's marginal benefits exceed the costs, and therefore even giving the agent ninety-five percent of the profits will not eliminate the agency problem).

172. This is, of course, a simplified example. A fuller model should, at the minimum, take into account the lessons from the Coase Theorem and consider the possibility of renegotiation between the parties. *See infra* Section VI.A.

173. The value of each work increases by $200 (20% of $1,000), of which the author receives 10%. Therefore the author benefit is $20 per work and $200 in total.

174. As explained previously, *supra* note 171, this cannot, and does not, provide a perfect solution, but just mitigates the agency problem. If, for example, the creator can take an action that will cost her $100 and will improve the value of her ten works, each valued at $1,000 by 2 percent, of which she is to be paid 10 percent under profit-sharing agreements, she will not take that action although it is socially desirable.

175. *See,* Hansmann & Santilli, *supra* note 87, at 264–65.

176. Hansmann and Santilli, who have suggested that the collective action problem might support inalienability, eventually also concluded that a resale royalty right should be voluntary. *See* Hansmann & Santilli, *supra* note 87, at 278–79.

demand for works she will sell in the future.[177] Other possible benefits, such as respect in her community, are non-transferable by nature and positively correlate with good reputation. Therefore, even without profit-sharing arrangements, most creators most of the time will gladly undertake actions that improve their reputation.

Second, voluntary profit-sharing arrangements, like those explored in Section III.A, typically provide an adequate solution to this problem. Indeed, as explained, with only voluntary agreements, a buyer cannot be certain that the author will reach profit-sharing arrangements with other buyers. However, the buyer knows that such arrangements are very likely. The buyer knows that if profit-sharing arrangements were desirable for her, they are likely to be desirable for other buyers. Indeed, as shown in Section III.A, profit-sharing arrangements with respect to most creative works are determined by industry standards. Thus, as it is a standard arrangement in the book industry to share the profit for a novel between the publisher and the author, each publisher can assume that future publishers of the same author will also be inclined to enter profit-sharing arrangements. Moreover, buyers know that once the author has entered into a profit-sharing agreement in the past she will be incentivized to internalize the effect of her future actions on her old work and therefore she will likely require similar arrangements from future buyers. Indeed, the author's good reputation is a public good:[178] providing it to one buyer does not limit the author's ability to provide it to another buyer, and, at the same time, the author cannot deny a buyer the ability to take advantage of her good reputation. As such, once the author agrees to provide it, by entering a voluntary profit-sharing arrangement, she is likely to demand similar arrangements from other buyers.

Overall, it seems that inalienable profit-sharing arrangements are not required to incentivize the creator to take actions that will promote her reputation and to refrain from taking action that will hurt it.

---

177. Merryman gives a wonderful example of how a sale of one of Robert Rauschenberg's early works for a considerable amount (for which Rauschenberg, much to his frustration, was not directly compensated) caused a sharp increase in the price of Rauschenberg's other early works, many of which were still in his possession, as well as his new works, making Rauschenberg a millionaire. *See* Merryman, *supra* note 62, at 111. Similarly, the creators of Superman earned considerable amounts as employees of DC Comics after their early creation became commercially successful. *See supra* note 43.

178. Public goods are items for which there is no rivalry in consumption among consumers while it is difficult, expensive, or impossible to exclude non-payers. The market typically under-produces public goods, and therefore some intervention, typically (but, as this example shows, not always) a governmental intervention, is required to supply them.

D. Profit-Sharing Arrangements as Providing Expressive Incentives

This Article explicitly explores the desirability of inalienable profit-sharing arrangements from a utilitarian perspective, which dominates the copyright discourse in the United States and perceives copyright law primarily as a tool to incentivize creation.[179] As such, it does not explore whether such arrangements can be justified by natural rights theories that dominate the copyright discourse in civil law countries.

However, in a recent article, Professor Jeanne Fromer pointed out that the two rationales can actually complete, rather than compete with, one another. More specifically, Fromer argues that true commitment to a utilitarian approach requires the law to take a broad approach that respects the artist's personhood:

> Creators of copyrightable and patentable work typically attach great significance to both their personhood and labor interests in their work. As such, the incentive to create ought to be all that much stronger when intellectual property laws are structured both to protect and to communicate solicitude for authors' personhood and labor interests.[180]

Fromer called those principles that use artists' personhood and labor interests to encourage creation "expressive incentives."

Can expressive incentives explain the existence of termination rights or other inalienable profit-sharing arrangements? Professor Fromer explained the connection between termination rights and expressive incentives:

> First, even if it is not exercised very much, [the right to terminate transfers] sends a powerful signal to authors that copyright law cares about the personhood, labor, and possessory interests they have in their work by allowing them to regain control of the rights in their work at a certain point in time. Second . . . the right . . . can be seen as

179. *See supra* note 20 and the accompanying text.

180. Jeanne C. Fromer, *Expressive Incentives in Intellectual Property*, 98 VA. L. REV. 1745, 1746 (2012). It is important to note that Fromer's argument explores the authors' personhood and labor interests from the perspective of the utilitarian incentive theory. As such, like this Article, it does not consider whether certain copyright doctrines (e.g., termination rights) can be justified without relying on incentive theory at all but instead only on the authors' natural rights as such.

> restoring to the author control over the work on which he or she labored and infused with personhood. Rights in works that, to the author, are intimately linked with the author's being can be reunited, so to speak, with the author. With this right, then, copyright law might be understood as offering the expressive incentive of control . . . .[181]

While this might explain why profit-sharing arrangements, and specifically a right to terminate transfers, are desirable, this does not account for the inalienability of this mechanism.[182]

Both the creator and her buyer (or licensee) place a certain value on the ability to control the work thirty-five years after its creation. If the creator places a higher value than the buyer, whether or not this value is partly attributed to the creator's personhood or labor interests, as reflected in the work, it will be in both parties' best interests to allow the creator to gain control over the work after thirty-five years. In this case, a transaction that will revert the rights back to the creator will be Pareto superior to a transaction that will give this asset (control after thirty-five years) to the party who values it less (the buyer), and it is therefore expected that the parties will voluntarily reach it.[183]

In other words, even if one believes that authors have a strong desire and interest in controlling their work several decades after its creation, it seems that default rules that provide termination right should suffice to protect such interests.

E. Termination of Rights in Works That Are Not Exploited

It is commonly assumed that termination rights are mainly a way for authors to regain control over the very few works that are commercially valuable decades after publication.[184] In other words, it is a right that protects the interest of authors of exceptionally successful works. However, termination rights can serve a different

---

181. Fromer, *supra* note 180, at 1806–07.

182. Fromer acknowledges that the decision regarding the alienability of rights require separate and somewhat different considerations. *See id.* at 1821.

183. In other words, if we denote the author's value of the right to control the work after 35 years, considering, inter alia, the author's interests in his personhood and labor, as x, and the buyer's value of that right as y, then if $y>x$, termination rights are clearly harmful. However, if $x>y$, both parties will prefer to allow the author to terminate the transfer after 35 years. Otherwise, the buyer will need to pay at least x to be allowed to control the work after 35 years, which is more than the buyer's willingness to pay, y.

184. See, e.g., Loren, *supra* note 30, at 1352; William Patry, *The Failure of the American Copyright System: Protecting the Idle Rich*, 72 NOTRE DAME L. REV. 907, 932–33 (1997). This assumption is also at the core of Part V of this Article.

group of creators: those whose work is no longer commercially exploited, such as authors whose books have gone out of print. Some of these creators can sometimes[185] exercise their termination rights, get back the rights to their work, and then try to commercially exploit the work, use it in some new way, distribute it (for free or not), or dedicate it to the public domain.[186]

In that respect, termination rights, to a degree, mimic a doctrine that exists in some foreign jurisdictions, such as France and Germany. In those countries, an assignee has an obligation, which the author cannot transfer or waive, to exploit the work. A breach of this obligation allows the author to terminate the transfer of rights to the assignee.[187]

Nevertheless, it does not seem that this potential use of termination rights justifies inalienability.[188] First and foremost, one should note that the argument regarding termination rights in unexploited work is part of a significantly broader discussion in copyright literature. Copyright lasts for a very long period, about 100 years, although the vast majority of works lose any commercial value after just a few years. Keeping those works protected under copyright is clearly inefficient and creates numerous problems, such as the famous orphan works problem.[189] Termination rights seem, at best, to marginally mitigate this problem, because they vest after many decades, require action by the author or her statutory heirs (which

---

185. As further explained in Section VI.B, the termination mechanism sometimes does not give the terminating author full rights to effectively exploit the work post-termination. For example, if a music record is no longer distributed, termination might not practically allow the terminating recording artist to fully exploit the work because it does not give her rights over the physical master recordings kept by the record company.

186. Most jurisdictions, including the United States, do not provide a procedure for dedicating work to the public domain, and therefore is it questionable whether such private dedication is effective. *See* Armstrong, *supra* note 89, at 391–93; CREATIVE COMMONS: OUR PUBLIC DOMAIN TOOLS, http://creativecommons.org/publicdomain/ (last visited Dec. 20, 2013).

187. Netanel, *supra* note 148, at 389.

188. It is unclear how common such a use is or will become. Exercising termination requires the author to precisely follow a procedure prescribed by the Copyright Act, which might be non-trivial for laypersons. *See supra* note 33. Therefore, some authors whose work has very low commercial value might be disincentivized to use this mechanism. A preliminary study of the use of termination rights in the year 2000 found that those are dominated by known authors. Reese, *supra* note 40, at *28 ("Many of the names [of the authors who terminate their transfer in 2000] will be familiar to many readers. . . . Clearly, terminations under section 304 often involve works by well-known authors. This is perhaps not surprising. Exercising termination rights under section 304 is not costless, so a termination should in many cases represent a decision that the value of the remaining copyright term is likely sufficient to justify the expense of the termination.") It is possible that termination of transfer in unsuccessful works will be more common pursuant to section 203.

189. Orphan works are works, protected by copyright, whose right holder cannot be identified or located, and thus a license to use those work cannot be granted. *See* U.S. COPYRIGHT OFFICE REGISTER OF COPYRIGHTS, REPORT ON ORPHAN WORKS (2006).

means that they cannot address the orphan works problem), and are administratively expensive. Other possible solutions to this problem, such as relying on the fair use defense, might provide a better remedy.[190]

Second, if the concern over unexploited works is significant, then it is unclear why the parties cannot address it themselves. The parties can address it ex post, as the author can approach the buyer (or licensee) and offer to buy back the rights for her work. As the buyer is not using the work in this scenario, the price is expected to be modest, although the transaction costs might be significant. A more efficient way to achieve a similar goal is to agree to such a "use it or lose it" arrangement ex ante. In other words, the parties are free to agree that if the buyer refrains from exploiting the work the rights will revert to the author.[191] Such an arrangement should be desirable to all the parties to such a transaction.[192]

Overall, the fear of non-exploitation of creative works does not seem to justify inalienable termination rights.

V. THE EX ANTE EFFECT OF INALIENABLE PROFIT-SHARING SCHEMES: TERMINATION OF TRANSFERS AND INCENTIVES TO CREATE

Part IV shows that the myth of the starving artist, which publicly justified the enactment of the termination-of-transfer rules (and similar mechanisms in foreign jurisdictions), at least as it applies to the artists' wealth or level of sophistication, cannot justify inalienability. However, it is possible that this myth was just a straw

190. *See* Authors Guild, Inc. v. Google Inc., 05 CIV. 8136 DC, 2013 WL 6017130, *7-*11 (S.D.N.Y. Nov. 14, 2013) (mass digitalization of copyrighted works, including orphan works, is fair use); Authors Guild, Inc. v. HathiTrust, 902 F. Supp. 2d 445, 458-64 (S.D.N.Y. 2012) (same). Other possible solutions, such as requiring renewed registration every few years, can tackle this problem more effectively but they involve legislative reform that might not be consistent with the international obligations of the United States. *See, e.g.*, Jerry Brito & Bridget Dooling, *An Orphan Works Affirmative Defense to Copyright Infringement Actions*, 12 MICH. TELECOMM. & TECH. L. REV. 75, 86–107 (2005).

191. There are many ways to implement such a solution. For example, the initial agreement between the parties can only cover an initial short period plus an option for long exploitation for an addition payment. The buyer will exercise the option only if the work has commercial value at that stage. Such arrangements are quite common in many commercial transactions. Other areas of the law, such as trademark law and water rights, also grant rights that are lost if not used. *See generally* Dean Lueck*, The Rule of First Possession and the Design of the Law*, 38 J.L. & ECON. 393, 431 (1995).

192. The analysis here is similar to the analysis in Section IV.D. If the author values the ability to get back the copyright to her failed work she should be willing to accept less for the work in the first place. As the buyer is giving away a right that is worthless to it, it should agree to such an arrangement for any decrease in the initial purchase price.

man for more complex economic forces that are at play in the relationship between the creator and the buyer of her work.

The remaining Parts of this Article provide an in-depth analysis of the economic effects of termination of transfer and similar inalienable profit-sharing arrangements. This Part explores the ex ante effects of the inalienable right to terminate a transfer. This analysis focuses on the ways in which this legal mechanism can affect the income of authors and their incentives to create.[193] While the focus of this Part is on the U.S. Copyright Act's termination-of-transfer mechanism, the analysis also applies to droit de suite and employee compensation rights, which are common in civil law countries.

A. Competitive Markets with Risk-Neutral Participants

In analyzing the effects of termination rights on the negotiation between the creator and a buyer, it is worthwhile to start with a simple model that assumes that the creator and the buyer are rational and risk neutral and that the buyer operates in a perfectly competitive market. As the buyer is typically an intermediary (e.g., a publisher or a record company), the meaning of this assumption is that the publishing market or the recording market is competitive. Those assumptions will later be relaxed.

The structure of many transactions in the copyright industries, including the book publishing industry and the recording industry, is quite simple. The publisher considers many authors and eventually chooses whom it would like to sign.[194] The resulting agreement is typically for a long term and covers several works, although, at least in the recording industry, the label is usually given an option to terminate it at certain times during that term.[195] The agreement will typically include an assignment of the author's copyright to the publisher (or a permanent license, typically an exclusive one).[196] Uncertainty is high. Although the buyer spends resources trying to choose successful authors to sign, most chosen authors will fail

193. This Article is of course not the first to explore how ex post allocation of rights affects the ex ante investment incentives of various parties. *See, e.g.*, Lucian Arye Bebchuk, *Property Rights and Liability Rules: The Ex Ante View of the Cathedral*, 100 MICH. L. REV. 601 (2001) (explaining how the ways in which a legal system handles externalities after their creations (ex post) affect investment decisions ex ante). In fact, one of the main justifications for property rights in general, and the primary justification for intellectual property rights in particular, is that granting property rights ex post is required to efficiently incentivizes ex ante investment. *See* WILLIAM LANDES & RICHARD POSNER, THE ECONOMIC STRUCTURE OF INTELLECTUAL PROPERTY LAW 13–14 (2003).

194. *See* CAVES, *supra* note 141, at 52–72 (discussing the publisher's role as a gatekeeper).

195. PASSMAN, *supra* note 86, at 104–07.

196. *See, e.g.*, Menell & Nimmer, *supra* note 58, at 802.

commercially.[197] When the initial agreement is signed, it is very difficult for the author or the buyer to know whether the author will turn out to be an unusual commercial success.[198] For simplicity I will assume that the parties do know the likelihood of major commercial success. Major commercial success in this context — superstardom — will be defined as having considerable income from old works at the time of termination.[199] Let's mark this probability of superstardom as p.

In competitive markets among buyers, each buyer's willingness to pay is equal to the benefits that such a buyer expects to receive from the product. Thus, a publisher will be willing to pay each author a payment equal to the average (expected) income stream from such an artist, minus the costs of production.[200] The sellers in this market, the authors, vary in their willingness to accept this amount. Those who face particularly high costs, especially opportunity costs, will be hesitant to accept.

Mandatory termination-rights mechanisms will affect authors' compensation.[201] The buyer must assume that the stream of revenues it will get from each signed author will be shorter in time and therefore smaller in size. While for most performers the work will be worthless shortly after publication, for some the stream of revenues is expected to last decades. Thus, terminating the transfer denies the buyer a part of that stream of revenues from superstars. This denial

---

197. *See, e.g.*, CAVES, *supra* note 141, at 61 (noting that "roughly 80 percent of albums and 85 percent of single records released fail to cover their costs").

198. *See, e.g.*, CAVES, *supra* note 141, at 2–3.

199. As explained in Section V.E, because section 203 of the Copyright Act allows termination only after 35 years, only few artists will be considered successful under this definition.

200. As suggested in Part III of this Article, most publishers and record companies prefer profit-sharing arrangements. However, for simplicity, in this model I assume that the author receives a lump sum payment. While the calculations required for lump sum and for voluntary profit-sharing schemes are not identical, the principles are the same. In both instances, the publisher will need to base every payment the author receives before the value of the work is known on the expected income from an average similar author.

201. Most commentators assume that denying the buyer a share of future profits will cause a price decrease in the initial sale. *See, e.g.*, Landes & Posner, *supra* note 167, at 327; J. D. Stanford, *Economic Analysis of the* Droit de Suite *— The Artist's Resale Royalty*, 42 AUSTL. ECON. PAPERS 386 (2003).. However, the empirical research on the topic (in the related context of resale royalties and similar rights) is currently inconclusive and unsatisfying. *Compare* Carson W. Bays, *Does a Resale Royalty Benefit Artists?* (Nov. 2009) (unpublished manuscript) (on file with the author) (suggesting that resale royalties reduced the price of fine art in California), *and* Christoph Engel & Michael Kurschilgen, *Fairness Ex Ante and Ex Post: Experimentally Testing Ex Post Judicial Intervention into Blockbuster Deals*, 8 J. EMPIRICAL LEGAL STUD. 682, 693-94 (2011) (testing the effect of the best-seller provision in German law and finding that it causes a price decrease ex ante), *with* Banternghansa & Graddy, *supra* note 68 (suggesting that resale royalties did not reduce the price of fine art in the UK). I am not aware of an empirical study that examines the effects of termination rights on the authors' compensation.

lowers the buyer's average income per signed author, and, because the contract price is equal to the expected (i.e., average) income, the contract price will be lowered as well. Let's mark the expected post-termination revenue stream of superstars (in present day value at the time of negotiation) as T.[202] The average decrease in the revenues of the buyer is therefore pT per artist, which, in a competitive market, will also be the decrease in each artist's compensation upon signing.

Years in the future, at the time of termination, the value of the work is certain. For most authors it is practically zero. For very few superstars it is not. These superstars will therefore terminate their transfers. After termination they can either exploit the work themselves, or, if needed, they can sign a new deal with an intermediary. In this transaction the author has significant market power as she sells one unique item — her post-termination revenue stream — valued T. The author can therefore reach a deal that will allow her to keep almost all of T.

As a whole, the termination-of-transfer mechanism does not change the author's expected income. It initially reduces her income by pT, but it also gives the author a chance — equal to p — to get an additional T of income in the future (all in present day values).

B. Competitive Markets with Marginally Diminishing Utility of Wealth and Risk Aversion

One important factor that is not considered in the previous Section is the decreasing marginal utility of wealth. This factor, which is considered in this Section, is important as it has a significant effect on the desirability of termination rights.

The decreasing marginal utility of wealth means that the same wealth has a different impact on different individuals' utility at different times: $5 does not typically increase the utility of a rich individual as much as it increases the utility of a poor one, and a ten percent chance of receiving $50 typically does not have the same utility effect of receiving $5. "[A] dollar is not a dollar is not a dollar."[203] This Subsection demonstrates that once this effect is taken into account, termination of transfer is probably ex ante inefficient in competitive markets because it decreases total social utility by misallocating both risk and wealth.

202. While only superstars can expect to have significant commercial success after decades, the magnitude of that success will vary. However, to keep the model simple, I assume that superstars have similar revenue streams after termination (which is equal to T, when brought to present day value at the time of negotiation).

203. DAVID FRIEDMAN, LAW'S ORDER: WHAT ECONOMICS HAS TO DO WITH LAW AND WHY IT MATTERS 63 (2000) (explaining why the value of money depends on the ways that it is expected to be used, and why this makes the purchase of insurance rational).

1. Termination Rights and Reallocation of Risk

Individuals do not make risky decisions — in this case the decision of whether to create — based on the expected value. Instead, they consider the certainty equivalent of the possible outcomes.[204] If individuals are risk averse their certainty equivalent will be lower than the expected outcome of a risky situation.

Termination of transfer reallocates risk to the author. Instead of getting a fixed amount as compensation, the fixed payment is reduced by pT in return for participation in a risky bet — a bet that by probability p will result in T and by a probability of $(1-p)$ will result in nothing. For a risk-averse individual, the certainty equivalent of this bet is lower than the expected outcome pT. Therefore, if the creators are risk averse, termination of transfer will reduce the subjective value (i.e., the utility) of their compensation.

Unfortunately, because of the decreasing marginal utility of wealth, a young artist is likely to be risk averse with respect to her work, which is a significant asset to her.[205]

The buyers, who are typically intermediaries, can handle risk better and can usually be assumed to be risk neutral. Those companies have a large portfolio of signed artists and therefore, their total income will be very close to the expected income from the artists they signed.

Indeed, termination rights create economic inefficiency by placing a certain risk — the risk with respect to the post-termination revenue stream — on a risk-averse party: the author.

---

204. A certainty equivalent is the guaranteed return that one would accept rather than take a chance on an uncertain return.

205. *See* Hansmann & Santilli, *supra* note 87, at 262. When the risk that an individual faces involves a significant asset, risk aversion is very common because the individual compares her state in case of winning (being rich) and losing (being extremely poor). Because of the decreasing marginal utility of wealth, the disutility of extreme poverty is almost always more significant than the utility of being rich. *See also,* FRIEDMAN, *supra* note 203, at 63–65 (explaining how the different valuations of money cause risk aversion).

Psychological research in recent decades shed light on the complex preferences of authors. For example, Marvin Zuckerman explored how important it is for artists (and others) to satisfy their sensation-seeking preferences. MARVIN ZUCKERMAN, SENSATION SEEKING: BEYOND THE OPTIMAL LEVEL OF AROUSAL (1979); s*ee also infra* Section V.G (suggesting that creators might fail to correctly value the exact risk they are taking). Notwithstanding the research on the psychology of artists, I do not believe that these studies suggest that when it comes to major financial decisions the typical artist, unlike most other individuals, prefers a risky financial bet over a certain one. *See also* Colin Camerer, et al., *Regulation for Conservatives: Behavioral Economics and the Case for "Asymmetric Paternalism"*, 151 U. PA. L. REV. 1211, 1230–31 (2003) (exploring the irrationality of lotteries). *But see* Lloyd R. Cohen, *The Lure of the Lottery*, 36 WAKE FOREST L. REV. 705 (2001) (suggesting that the playing the lottery is rational).

2. Termination Rights and Reallocation of Wealth

A related downside of termination rights has to do with the reallocation of wealth over time and among creators.[206] While, as explored in Section V.A, the expected income of an author in a competitive market is not affected by the termination mechanisms, this legal rule changes the distribution of income over time and between creators. Under this model, without termination rights all artists will receive the same compensation, and with termination rights everybody will initially receive less, but the creators of very successful works will eventually, after termination, receive more. Therefore, this rule transfers wealth from all young artists to an older few.

It is reasonable to assume that the wealth that is being redistributed by the termination mechanism (the value of the post-termination revenue stream, denoted T in Section V.A) could increase the utility of young artists, who are typically poor, more than the utility of older superstars, who are typically wealthier.[207] Therefore, artists would probably prefer not to transfer income from their young poor selves to their old wealthy selves.[208] Indeed, this reallocation of wealth from the poor to the rich is probably not just unfair, but also inefficient.

Some have suggested that a legal rule that forces the buyer to compensate the creator for work that turns out to be successful is efficient because the transfer of income from less successful artists to successful artists incentivizes commercially successful creations.[209]

---

206. The problems of reallocation of risk and reallocation of wealth are related (and, in some respects, they are effects of the same phenomenon) because they both result from the decreasing marginal utility of wealth. The decreasing marginal utility of wealth causes most individuals to be risk averse with respect to major assets and to prefer to earn an extra dollar when they are poor rather than when are wealthy. *See* FRIEDMAN, *supra* note 203, at 63–65 (discussing the effect of marginal utility of wealth on risk preferences).

207. Not all authors of works that possess commercial value at the time of termination are wealthy. Many of them are wealthy because commercial success of old works is commonly correlated with a successful career of an artist. *See also infra* text accompanying note 318. However, in some cases the author might be less successful or even a "one-hit wonder." Nevertheless, on average, creators who terminate their work are considerably wealthier than the average author at the time of creation. *See also* Reese, *supra* note 40, at *28 (suggesting that in the year 2000 many of the works that had their transfers terminated were created by successful authors).

208. *See* Hansmann & Santilli, *supra* note 87, at 262. It should be noted that many legal rules are designed to incentivize individuals to save money when they are young to be used when they are older. These rules help those individuals overcome their bounded willpower problem. *See, e.g.*, RICHARD H. THALER & CASS R. SUNSTEIN, NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH AND HAPPINESS 103–17 (2009). However, this seems like a weak justification for the termination mechanism, partly because the beneficiaries of this mechanism are usually very few, and typically successful, rich superstars.

209. *See, e.g.*, Hansmann & Santilli, *supra* note 87, at 265.

This argument is misguided because artists do not typically possess superior information (compared to buyers) regarding the chances of their future success. Therefore, at the crucial time when an artist needs to decide whether to create or to pursue other interests, she does not know if her work will be commercially successful. In other words, artists do not know if they are going to be on the winning side or the losing side of this transfer from less successful to superstar artists. All they know is that they have some chance to receive a considerable amount in a few decades if they become very successful.[210] This simply cannot, in itself, increase their expected revenues or their incentive to create.

Therefore, by reallocating wealth from younger authors to older superstars and by reallocating risk from buyers to sellers, the termination-rights mechanisms, while keeping the wealth of authors, as a group, constant, decrease the total utility of the authors and society as a whole. This causes a decrease in the incentives to create and a reduction in the quantity and quality of works created.[211]

C. Non-Competitive Markets with Risk-Neutral Participants

Let's now assume that there is very limited competition among buyers. In other words, the assumption is that the market is an oligopsony: a market with a few big buyers. In this scenario, the buyer knows that paying a lower price per work will decrease its supply because the reduction in the authors' compensation will cause some of them to create less. Knowing this, the buyer will set a price that will maximize her revenues.[212] This price will be lower than the average

---

210. Artists however might misperceive their chances of success. *See infra* Section V.G.

211. It is well known that during the legislative process of the Copyright Act of 1976, various artists' groups (such as the Authors Guild) strongly supported the enactment of termination rights. Can one infer from this support that, notwithstanding the analysis in this Part, termination rights are valuable to artists? I believe that the answer is no. The difficult question this Part tackles is how to compare the various effects of termination rights, particularly the expected decrease in the initial compensation of artists and the later post-termination revenue stream that some of them will enjoy. However, because the Copyright Act of 1976 was applied to old and new works, established artists did not suffer the decrease in their initial compensation, and thus, as a result of the enactment of termination rights, received a pure windfall. Consequently, it is not surprising that artists' groups, in which established artists were heavily represented, supported the enactment of termination rights.

212. In a monopsonistic market the buyer will set the price. In an oligopsony the few buyers will set the price, taking into account the actions of the others, as suggested by economic models such as Cournot competition. For the purposes of this Article, the exact ways in which the prices in oligopsony are determined are immaterial, although it is assumed that such prices are based on and lower than the expected benefits from the product purchased. It should be noted that the publisher has two main decisions to make. First, in its oligopsonistic interaction with the artist, it needs to decide what price to pay. Second, in the monopolistic interactions with the buyers of the work, it needs to decide what price to

revenue per author and therefore a deadweight loss will be created. Deadweight loss is a form of economic waste that results from prices in non-competitive markets that do not match the marginal costs and benefits.

In an oligopsony, some sellers (i.e., authors) who would have been willing to accept a price lower than the marginal benefits to a buyer but higher than the oligopsony price will be priced out of the market. In other words, the market power of the buyers will cause some authors to stop creating even if they are willing to accept an amount that is lower than the average revenue per signed author. Pricing them out of the market denies society the benefits of this interaction. In addition, it denies society the benefits that would have arisen from transactions between the buyer (e.g., a publisher) and consumers of the work if it had been created, as well as the positive externality (spillover) that copyrighted work typically creates.[213]

The following graph illustrates this argument:

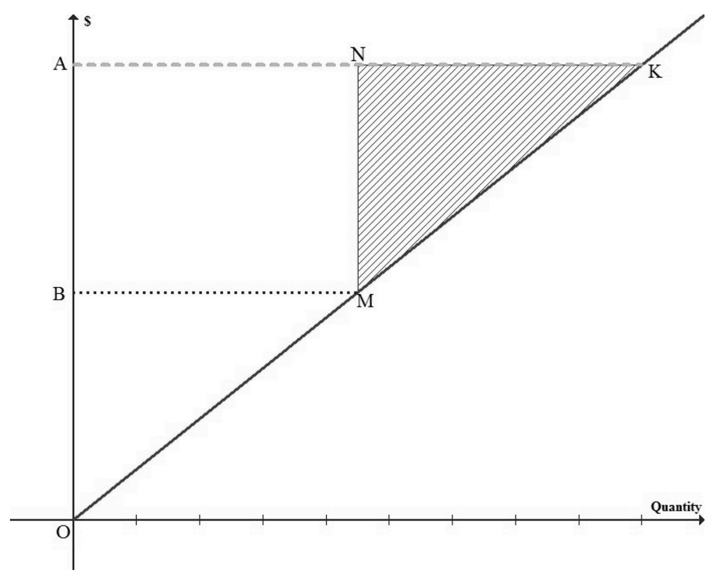

Figure 1

In Figure 1, presenting the supply curve a buyer faces, A is the expected net revenue of the buyer for an average author. This would have been the price in a competitive market. However, B is the price

charge. Because I assume that the price in the first market is fixed, it does not affect the price in the second market.

213. *See* Mark A. Lemley & Brett M. Frischmann, *Spillovers,* 107 COLUM. L. REV. 257 (2007).

that a buyer will pay in this non-competitive market.[214] The buyer is trying to maximize rectangle ABMN but by doing so it creates a deadweight loss in triangle NMK.

With termination of transfer this graph becomes different:

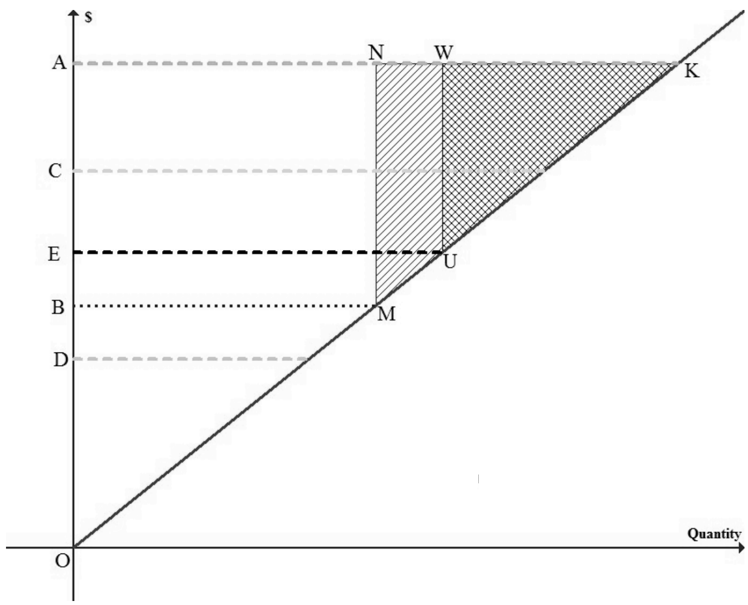

Figure 2

Mandatory termination rights reduce the expected (average) net revenue per author by pT.[215] In Figure 2, A represents the expected net revenue of the buyer from an average author without termination of transfer and C the reduced (by pT) expected benefits with mandatory termination rights. This reduction in expected revenues causes a reduction in the compensation offered to the author from B to D. This reduction is smaller than pT.[216]

However, when termination is exercised, the shoe is on the other foot. Now the artist has market power over her work. The few buyers will compete with one another, and the artist is likely to be able to

214. B is typically assumed to be a fraction of A such that $\mathrm{B} = \alpha\mathrm{A}$ ($0 < \alpha < 1$). Figure 1 presents a case of a linear supply curve, in which $\alpha = 0.5$.

215. *Infra* Subsection V.B.1.

216. In other words, $\mathrm{B} - \mathrm{D} < pT$. The reason for this is that the author's compensation is proportional to the expected revenues of the buyer. $\mathrm{B} = \alpha\mathrm{A}$ and $\mathrm{D} = \alpha\mathrm{C}$ ($0 < \alpha < 1$). Therefore, $\mathrm{B} - \mathrm{D} = \alpha\mathrm{A} - \alpha\mathrm{C} = \alpha\mathrm{A} - \alpha(\mathrm{A} - pT) = \alpha pT < pT$. For example, if the supply curve is linear, as presented in Figure 2, a monopsonistic buyer will pay a price that is half her expected revenues. Because the expected revenues are decreased by pT, the author's compensation will decrease by $pT/2$.

keep most of the post-termination revenue stream (practically all of *T*).[217] In that case, the total expected revenue of the artist will be D (the original compensation), plus an amount close to pT, an expectation with likelihood p (the chances of superstardom) to receive an amount close to T (the post-termination revenue of the superstar). Therefore, the total compensation, denoted by E in Figure 2, is expected to be higher than B (the expected compensation without termination rights).[218]

In other words, inalienable termination rights increase the total expected compensation of the author. There is an intuitive explanation for this phenomenon: with termination rights the author gets to sell her work in two stages. Instead of selling all her rights at once, when she lacks any market power and faces an oligoposonist, she sells a part of her asset (the pre-termination revenue stream) in that market but another part (the post-termination revenue stream) later, as an established artist with market power. Therefore, the author can extract a bigger share of the revenue stream from her work.

This increase in expected compensation is socially desirable as it decreases the deadweight loss and increases the incentive to create. As shown above, the deadweight loss without termination is represented by triangle NMK, but the deadweight loss with termination is a smaller triangle WUK. This means that some artists, who are willing to accept more than B but less than E, will not produce the work without termination rights, but will produce it with them. Their surplus is represented by NMUW. Society will also benefit from the surplus from the interactions that will occur between the buyer and consumers.[219]

D. Non-Competitive Markets with Diminishing Utility of Wealth and Risk Aversion

The analysis in the previous Section suggests that in some cases inalienable rights to terminate copyright transfers are efficient. However, Section V.B discusses the misallocation of risk and wealth that is caused by termination rights. Those phenomena affect the desirability of the model presented in the previous Section.

The preceding analysis shows that in a non-competitive market the expected total wealth of the author increases. However, as authors

217. It should be noted that the Copyright Act allows the author to enter agreements with respect to post-termination rights only after the termination is effective, unless the deal is with the previous transferee, in which case such a deal can be executed after a termination notice is served. 17 U.S.C. § 203(b)(3)–(4) (2012); Bourne Co. v. MPL Commc'ns, Inc., 675 F. Supp 859 (S.D.N.Y. 1987).

218. If $\mathrm{B} - \mathrm{D} < pT$, *see supra* note 216, then $B < \mathrm{D} + pT = E$.

219. *See supra* note 213 and accompanying text.

are typically risk averse and prefer to earn more when they are young and poor than when they are older and wealthier, it is inaccurate to consider their expected wealth (denoted E above) as the sole measurement of their benefits. Rather, one should consider their overall utility. Because inalienable termination rights misallocate risk and wealth, their expected benefits will be lower than E. It is, however, impossible to know whether or not it will be lower than B — the compensation that would be received under a regime in which termination rights were not inalienable.

Indeed, on the one hand, termination of transfer increases the artist's expected revenue by allowing her to sell part of her assets when she has market power. On the other hand, its inalienability reduces her utility by forcing her to bear more risk and by transferring wealth from poor to rich artists.

E. The Efficient Vesting Period for Termination Rights

The length of the vesting period — the period of time until the author can exercise the termination rights — has a significant effect on the efficiency of the termination-of-transfer mechanism. This Section suggests that, based on the model developed in the previous Sections, the vesting period should take into account the benefits and costs of the termination mechanism and should probably be shorter.

When termination is not available until several decades after the work is created, as is the case under current law,[220] the value of the post-termination stream of revenue (denoted *T*) becomes exceptionally small. This is attributed to the decrease in the demand for copyrighted works over time as well as the need to discount this stream of revenue to its present value at the time of negotiation.

The demand for nearly all works decreases over time. In one study, Professors William Landes and Richard Posner looked at the rate of renewal registration of copyright (when such renewal was mandatory) and calculated that the annual depreciation in value is four percent for musical work and nine percent for books.[221] Using those figures, an average musical work is expected to generate about seventy-two percent of its total revenues within the first thirty years after publication, and an average book about ninety-four percent. It is possible that the demand for very successful works, which typically are the subject of termination rights, decreases slower than the

---

220. *See supra* text accompanying note 32.

221. Landes & Posner, *supra* note 114, at 506. The methodology that Landes and Posner used to calculate these figures can be challenged. However, the exact rate of the annual decrease in demand is not material to the argument made in this Section.

demand for less successful work; after all, classics are classics.[222] Nevertheless, with extremely rare exceptions, the demand for even a very successful work is substantially lower thirty years after publication.

In addition, the post-termination stream of revenues must be discounted to present value at the time of negotiation. Even if a very low discount rate of three percent is used, only forty-one percent of the revenues in the thirtieth year will remain when brought to present day value. Using seven percent leaves only thirteen percent of the income in the thirtieth year.[223]

Considering both factors, one can see that the value of the post-termination stream of revenues is small under section 203.[224] If termination is exercised thirty-five years after publication, then, using three percent as a discount rate, only eight percent of the total value of an average musical work and little more than one percent of the value of an average book will be in the post-termination revenue stream.

Therefore, because the post-termination revenue stream is small, the reduction in the deadweight loss identified in Section V.C is also proportionally small. Indeed, currently, the impact of termination rights on incentives is not significant enough.[225] Making the termination available earlier will increase those benefits and will give this mechanism more teeth. For example, if termination is exercised ten years after publication, then, using three percent as a discount rate, forty-six percent of the total value of an average musical work and twenty-six percent of the value of an average book will be in the post-termination revenue stream (instead of, as suggested above, eight

---

222. There is sporadic anecdotal evidence that might support such a claim. For example, the music of the Beatles, recorded in the 1960s, and the books of Theodor Geisel (Dr. Seuss), whose most famous work was created in the 1950s, still produce considerable sums annually. *Top Earning Dead Celebrities*, FORBES.COM (Oct. 24, 2012), http://www.forbes.com/special-report/2012/1024_dead-celebrities.html; *see also Old Albums Surpass New in Sales*, SEATTLE WEEKLY (July 11, 2012), http://www.seattleweekly.com/2012-07-11/music/greatests-hit/.

223. This is the discount rate suggested by George Akerlof, Kenneth Arrow, Ronald Coase, Milton Friedman, James Buchanan, and other prominent economists in their amicus brief in *Eldred* and used by Justice Breyer in his dissent. *See* Brief of George A. Akerlof et al. as Amici Curiae in Support of Petitioners at 7, Eldred v. Ashcroft, 537 U.S. 186 (2003) (No. 01-618), 2002 WL 1041846; Eldred v. Ashcroft, 537 U.S. 186, 254–57 (2003) (Breyer, J., dissenting).

224. Of course, the value of the post-termination revenue stream under section 304 is much smaller because it is not available until more than fifty years after publication. *See supra* text accompanying note 35.

225. The thirty-five year period which is currently used in section 203 was heavily negotiated before the enactment of the Copyright Act of 1976. *See* STAFF OF H. COMM. ON THE JUDICIARY, 89TH CONG., COPYRIGHT LAW REVISION, PART 6, SUPPLEMENTARY REP. OF THE REGISTER OF COPYRIGHTS ON THE GENERAL REVISION OF THE COPYRIGHT LAW: 1965 REVISION BILL 71-76 (Comm. Print 1965); Litman, *supra* note 31, at 891–93.

percent for music and one percent for books under the current regime).

At the same time, vesting termination rights earlier is expected to exacerbate the problem of misallocation of risk and wealth. Indeed, if termination is available sooner, the post-termination revenue stream becomes more significant and therefore will more intensively misallocate the risk and wealth of more creators.[226]

While it is impossible to know with certainty which effect will dominate,[227] it is unlikely that a vesting period of thirty-five years is efficient. Under such a system, the post-termination revenue steam is too insignificant to improve the well-being of authors, and it is unlikely to justify the ex post costs of this mechanism, as explored in Part VI.

F. The Model, Droit de Suite, and Employees' Compensation Rights

The model developed in the previous Sections analyzes the ex ante effects of the termination-of-transfer mechanism. However, with minimal modifications, it can be used to analyze the effects of droit de suite and employees' compensation rights. When future resale of a work is subject to droit de suite the expected revenues of the buyers decrease. The decrease is not by an expected post-termination stream of revenue (as is the case with termination rights under U.S. law) but by the expected resale royalties. Nevertheless, from a buyer's perspective, both are just reductions in the expected revenue streams that will cause a reduction in the buyer's willingness to pay. The same is true for the transaction between an employer and an employee. Forcing the employer to pay additional compensation to the employee reduces the expected benefits to the employer from the employee's labor and thus its willingness to pay for the employee's services. This reduction in expected revenues exists regardless of whether the buyer is operating in a competitive market or has market power.

Unlike the termination-of-transfer mechanism, when a work subject to droit de suite is resold or when an employee's invention turns out to be a success, the creator is entitled to compensation that is

---

226. Another downside to making termination available sooner is that if the fixed costs of producing and distributing a work are significant, the publisher or record company might not be able to recoup them. As further explored in Part VII, in most modern markets, unless termination becomes available very shortly after publication, this seems highly unlikely.

227. In order to accurately calculate the efficient vesting period, one must know the exact utility function of the authors (and this of course is not just private information, but also varies by author) and the exact market structure of the industry. Generally speaking, the more concave the utility function of authors, the more risk averse they are, and the later termination rights should vest. The less competitive the buyers' market, the sooner termination rights should vest.

not determined by a market transaction.[228] This, for purposes of the model presented in this Part, is practically irrelevant. All legal regimes present similar features. In all cases the creator is given an additional compensation if her creation is successful. This reduces the expected revenues of the buyer and will result, under all regimes, in a price decrease in the initial-sale market. Therefore, the analysis is very similar. Creators benefit from a mandatory profit-sharing mechanism if, and only if, the level of competition among buyers is low. However, those benefits must be evaluated in light of the misallocation of risk and wealth caused by those rules.

G. Termination Rights and Irrationality

The model developed in this Part of the Article assumes that the creator and her buyers are rational (although not necessarily fully informed). In particular, the model presumes that both parties make decisions that take into account the chance of commercial success. However, rich literature suggests that individuals do not always act rationally in their decision-making process.[229] A full analysis of the ways in which irrationality impacts the creative process in light of the right to terminate transfers is beyond the scope of this Article, but this Section offers several ways in which irrationality can affect the desirability of termination rights, as explored by this model.

Behavioral law and economics literature explores several phenomena — irrationality biases — that might affect the desirability of the termination mechanism. The most relevant irrationality bias in this context is probably the over-optimism bias.[230] This phenomenon causes many to believe that the likelihood of a bad event happening to them is smaller than it actually is. Thus, many smokers believe that they are less likely to contract lung cancer than other objectively similar smokers.[231] Likewise, most creators suffer from this bias and believe that the chances of commercial failure of their works are smaller than the general probability of such failures.[232] If that is the case, then creators might misperceive the likelihood of

228. Section VI.C of this Article discusses at length the ex post difference between droit de suite and employees' compensation rights on the one hand and termination of transfer on the other hand.

229. *See, e.g.*, DANIEL KAHNEMAN, THINKING, FAST AND SLOW (2011); Thaler & Sunstein, *supra* note 208, at 104–05; Christine Jolls & Cass R. Sunstein, *Debiasing Through Law*, 35 J. LEGAL STUD. 199, 203–06 (2006).

230. *See* Jolls, Sunstein & Thaler, *supra* note 131, at 1524–25.

231. Paul Slovic, *Do Adolescent Smokers Know the Risks?*, 47 DUKE L.J. 1133, 1136–37 (1998).

232. *See* Christopher Buccafusco & Christopher Jon Sprigman, *The Creativity Effect*, 78 U. CHI. L. REV. 31 (2011).

superstardom (denoted *p*) and thus place too much weight on the post-termination revenue stream.

Another bias explored in the literature is the availability bias, which suggests that salient events seem more likely than non-salient events.[233] Thus, airplane accidents seem more likely than they really are because they receive media attention. Similarly, because commercial success is more salient than commercial failure (although the latter is significantly more common),[234] some might perceive the likelihood of superstardom to be greater than it actually is. If an artist experiences this bias, she might attribute too much value to her post-termination rights and accept too little for her pre-termination rights, or she may decide to create when it is inefficient to do so.

On the other hand, bounded willpower is a form of myopia that causes people to attribute too much value to short-term gains and too little value to long-term gains.[235] Many people, for example, save too little for their retirement, which might justify legal intervention by encouraging or requiring people to save more. In the context of termination rights, this phenomenon might cause the reverse effect of the availability bias because creators might place too little weight on their long-term post-termination rights.[236]

It is difficult to know how common these phenomena are in transactions between creators and buyers. On the one hand, the existence of these psychological biases is well documented. On the other hand, there are known mitigating factors that are common in copyright industries' transactions. Experts, for example, appear to be partly immune to many of the biases that affect laypersons, especially when they are dealing with repeated transactions.[237] Most of the buyers in copyright industries, such as executives of record companies and publishers, are presumably experts. Many (though certainly not all) sellers are assisted by experts such as lawyers or agents.[238] In addition, the biases described above are usually attributed to "System 1" in our brain, which generally controls intuitive, automatic, fast,

---

233. *See, e.g.*, KAHNEMAN, *supra* note 229, at 129–36; Jolls, Sunstein & Thaler, *supra* note 131, at 1518–19. The availability bias was mentioned earlier in this Article because it may have contributed to the decision to enact the termination mechanisms. *See supra* note 131.

234. *See supra* note 197.

235. *See, e.g.*, Jolls, Sunstein & Thaler, *supra* note 131, at 1479; OREN BAR-GILL, SEDUCTION BY CONTRACT: LAW, ECONOMICS, AND PSYCHOLOGY IN CONSUMER MARKETS 21–22 (2012).

236. Limited willpower is a weak justification for the ineptitude of termination rights in their current form because the solution for this problem should not be to transfer wealth primarily to superstars. *See supra* note 208 and accompanying text.

237. *See* KAHNEMAN, *supra* note 229, at 140–45, 234–44.

238. *See supra* note 105.

affective, and heuristic-based decisions.[239] Individuals also use "System 2," which is slow, effortful, conscious, and rule-based, and can sometimes override the intuitive judgment of System 1.[240] Transactions in copyright industries typically take time, which allows the parties to consider them carefully.[241] This might indicate that the parties' System 2 thinking is evoked during the negotiation, which might also mitigate the psychological biases described above.

Therefore, I believe that it is fair to assume that most buyers in the copyright industries (who are typically intermediates, e.g., publishers), as well as many of the sellers, primarily act rationally. However, many other sellers, who are less experienced, might act in an irrational way more often. It is also fair to assume that the optimism bias is likely the most common phenomenon among sellers, as creators overestimate the likelihood of their commercial success. If those assumptions are correct, it might provide another explanation — a more sinister one — for the extensive use of voluntary profit-sharing arrangements. The sophisticated buyer knows that the value of the seller's share in a profit-sharing arrangement is small because it heavily depends on unlikely commercial success. However, the artist-buyer irrationally overvalues her share and thus agrees to other unfavorable terms (for example, small advances) to get a higher share of the profits.[242] In other words, irrationality might cause the author to accept too little up front and, in the marginal case, to decide to create when, considering the expected compensation, it is irrational to do so.

Mandatory profit-sharing schemes, including termination rights, seem less desirable when those phenomena are taken into account. Indeed, as explained above, if creators are overly optimistic, then from a policy perspective, society needs to be concerned with artists' decisions to make *too much* of their financial return contingent on commercial success. Termination rights, like droit de suite, only aggravate the problem. Thus, a true paternalistic policy, if motivated by the artist's poor and irrational understanding of the bargaining process, should consider limiting profit-sharing arrangements rather than mandating them.

---

239. *See* KAHNEMAN, *supra* note 229, at 20–25.

240. *See id.*

241. *See supra* note 157 and accompanying text.

242. For example, if an author is willing to accept $10,000, the buyer, instead of paying that amount, can offer the author $5,000 plus ten percent of the profits from the work. Even if similar works only make $30,000 in profits, the author might accept the offer (which, on average, is equivalent to a payment of $8,000, not considering risk aversion), irrationally believing that her work will be substantially more successful than average similar works.

VI. The Ex Post Effect of Inalienable Profit-Sharing Schemes: Inefficiencies Immediately Before and After Termination

The discussion in Part V implicitly assumes that the termination-of-transfer process itself is costless. It assumes that the buyer (typically the publisher) owns the rights prior to termination, that the author owns the rights post-termination, and that the author can freely and easily exploit those rights, including by negotiating another deal with any competing intermediary. The discussion in this Part shows that this description is oversimplified.

Two main problems make the termination process more difficult and costly. The first problem is that, with termination approaching, the incentives of the publisher and the creator become misaligned in a way that can cause one party to impose a negative externality on the other (or prevent her from benefiting from a positive externality). The second problem, which is probably more harmful than the first, is the difficulty of bundling rights from multiple authors for multiple works after termination. This Part explores these concerns and offers several partial solutions, including allowing the parties to contract around the termination rights prior to termination and granting the author only monetary compensation upon termination instead of full control.

A. The End-Game Problem: Externalities on the Eve of Termination

Both the author and the intermediary (for example, the publisher or record company) can take many actions that can affect the value of the work. Therefore, under any profit-sharing scheme, voluntary or mandatory, each of them can impose an externality on the other party. For example, the publisher typically determines how much to invest in promoting the work. Such a decision might have a profound effect on the commercial value of the work. Every dollar the publisher spends on promotion increases the value of the work, but part of this increase will be enjoyed by another person: the author. The author can also promote the work by creating another successful work, by participating in promotional events, and so on. Here also, the author bears the cost (including opportunity cost) of those actions, but the benefits are shared with the current owner of the work. Negative externalities can also exist: the author, for example, can produce unsuccessful work or become associated with some scandalous activity that will decrease the commercial value of the work.

Those externalities can distort the incentives of the parties. For example, if the publisher can increase the value of a work by $11 by investing $10 in promotional activities, she will not do so if droit de suite forces her to pay 10% of any increase in the value of the work to the author. In the context of termination rights, when the window of termination is far in the future, the owner can practically ignore it and assume that she will be the beneficiary of an increase in the value of the work. However, when a termination window is approaching, the end-game problem[243] becomes more severe and the chances of inefficient externalities increase.

1. Contractual Solutions to the Problem of Externalities

As the Coase Theorem suggests, when transaction costs are low, the parties can solve externality problems contractually.[244] Thus, the publisher who can invest $10 to raise the value of the work by $11 can contact the author, explain the need to make the investment, and require her to contribute to the expenses. This process, however, might not be cheap. Asking the author to contribute to any investment that might change the value of the work may be prohibitively costly in terms of transaction costs. This difficulty is typically solved by agreeing on those arrangements ex ante. Those agreements are in fact part of the standard contractual profit-sharing arrangements that were explored in Section III.A.

The problem is much more difficult to solve or mitigate when the law limits the parties' freedom of contract. Regardless of any contractual arrangement, current law in the European Union does not allow the owner of a piece of art to deduct promotional costs from the costs of future sale when calculating the author's resale royalties.[245] In the United States, the parties' ability to come up with a contractual solution to the externalities problem on the eve of termination is limited by the author's possible inability to trade her post-termination rights. Therefore, for example, a publisher might underinvest in promoting an author's work in the years before termination and might be incentivized to release additional works of signed authors (e.g., a best-hits record) on the eve of termination, even if a later release might be more socially desirable.[246]

---

243. *See* Russell Hardin, *Distrust*, 81 B.U. L. REV. 495, 501 (2001); Robert E. Scott, *Conflict and Cooperation in Long-Term Contracts*, 75 CALIF. L. REV. 2005, 2033 (1987)..

244. R. H. Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960).

245. The EU Directive, *supra* note 65, art. 4 (setting resale royalties as a percentage of the price of the item sold).

246. A possible real-life example is Warner Brothers' decision to hire Zack Snyder to direct the latest Superman reboot, *Man of Steel*. Some speculated that this choice was partly motivated by the company's belief that Snyder could deliver the movie faster than others and before some of the termination rights in the work would vest. Chris Schrader, *Legal Woes Could Divide 'Superman' Franchise in Two*, SCREEN RANT, http://screenrant.com/superman-movie-legal-battle-siegel-shuster-schrad-117539 (last visited Dec. 20, 2013). It is currently not clear whether the rights in Superman will be terminated (and if so, when). *See infra* note 249.

2. Rescission and Re-grant of Transfers

One method used to enter into a contract regarding the parties' rights on the eve of termination and thereafter is to rescind the original license (or assignment) and re-grant it. It is, however, highly controversial whether those actions supersede and replace the original grant and thus prevent its termination or whether the inalienable nature of termination rights precludes such a construction.

In *Milne v. Slesinger*,[247] the Ninth Circuit dealt with a notice to terminate the rights in Winnie-the-Pooh children's books. The author, A. A. Milne, granted rights in these books through a 1930 agreement that was subject to termination starting in 1986. Termination notice could have been served as early as 1976.[248] In 1983, after the author's death, the successor of the author's interest in the copyright (a trust created by the author) and the statutory successor of the termination rights (the author's only child) agreed to rescind the 1930 agreement and re-grant the rights in the books. The Ninth Circuit held that the 1983 agreement terminated the 1930 agreement and thus that the earlier agreement was not subject to statutory termination pursuant to section 304(d).[249]

In *Penguin Group (USA) Inc. v. Steinbeck*,[250] the Second Circuit held that a termination notice with respect to the work of John Steinbeck was invalid because of a 1994 agreement in which Steinbeck's wife, who inherited the copyright in his work by the power of his will, rescinded a 1938 licensing agreement and re-granted the rights in Steinbeck's work.[251]

Although such contractual arrangements might address and substantially mitigate the end-game problem, these decisions came under harsh criticism. Professors Peter Menell and David Nimmer, for example, have stated that those cases "have eviscerated [the] clear congressional command,"[252] as Congress's intent was to "shield[]

247. Milne v. Stephen Slesinger, Inc., 430 F.3d 1036 (9th Cir. 2005).

248. *See supra* text accompanying note 33.

249. *Id.* at 1037, 1043. Recently the Ninth Circuit held that the statutory successors of Joe Shuster — one of the creators of Superman — could also not exercise their termination rights because of a 1992 agreement that superseded the original 1930s agreement and re-granted DC Comics a license. DC Comics v. Pac. Pictures Corp., 12-57245, 2013 WL 6098416 (9th Cir. Nov. 21, 2013). The successors of Shuster's co-writer, Jerry Siegel, are currently dealing with a somewhat similar issue in their termination rights litigation, as Warner Brothers argues that a 2001 agreement extinguished their termination rights. Larson v. Warner Bros. Entm't, Nos. 2:04-cv-08400-ODW (RZx), 2:04-cv-08776-ODW (RZx), 2013 WL 1164434 (C.D. Cal. Mar. 20, 2013).

250. Penguin Grp. (USA) v. Steinbeck, 537 F.3d 193 (2d Cir. 2008).

251. *Id.* at 195–96.

252. Menell & Nimmer, *supra* note 58, at 802; *see also* Bently & Ginsburg, *supra* note 61, at 1584–86 (criticizing *Milne* and *Steinbeck* as inconsistent with the copyright statute and possibly with its policy). *But* see Loren, *supra* note 30, at 1368–69 (suggesting that the

authors from the pressures of unequal bargaining power that had produced unremunerative transfer in the creative arts."[253] Menell and Nimmer argue that "by making termination rights alienable, *Milne* and *Steinbeck* have resurrected *Fisher* and its unfortunate effects on authors and statutory successors[.]"[254] They express concerns regarding the effects of those decisions on the bargaining power of the statutory successors because "no occasion even arises for the statutory successors to realize any enhanced 'bargaining power' apart from their statutory termination rights . . . ."[255]

Applying the analysis from Part V suggests that Menell and Nimmer's concerns are greatly overstated. There is a profound difference between the regime that *Fisher* allowed and the one that *Milne* and *Steinbeck* create. Under *Fisher*, the author could have assigned her rights for a "second bite" when she initially sold her rights. The model developed in Section V.C shows that if buyers in the initial transaction have market power, they can extract lower prices, reducing the authors' compensation and the incentives to create. *Milne* and *Steinbeck*, in sharp contrast, allow renegotiation of the rights decades after publication. At this stage, as explained in Section V.C, the value of a work is known and the author's successors have significant bargaining power.

Thus, the holders of termination rights in Winnie-the-Pooh had a powerful threat of terminating the rights in the work and then selling them to the highest bidder. Not surprisingly, Walt Disney Productions, which produced the first Winnie-the-Pooh movie a few years earlier,[256] was willing to pay generously to remove this threat.[257] This analysis suggests that such a threat materializes as soon as the commercial value of the work is known, in many cases shortly after publication, and typically many years before the right to serve

---

Ninth Circuit was correct in *Milne* in holding that the 1930 agreement was successfully rescinded and thus not subject to termination). Loren, however, justifiably shared some of the criticism regarding the Second Circuit decision in *Steinbeck*, because, in that case, the 1994 agreement that was held to rescind and re-grant the 1938 agreement was executed by Steinbeck's widow, who did not have the majority of the termination rights at the time. *Id.* at 1370–71; *see also* Menell & Nimmer, *supra* note 58, at 823.

253. Menell & Nimmer, *supra* note 58, at 814.

254. *Id.* at 815.

255. *Id.* at 815–16.

256. THE MANY ADVENTURES OF WINNIE-THE-POOH (Walt Disney Productions 1977).

257. Disney has since released four additional movies that feature Winnie-the-Pooh and other characters created by A. A. Milne. The franchise is one of Disney's most profitable, and it still generates considerable revenues. In 2005 alone, for example, Disney earned $6 billion from worldwide sales of Winnie the Pooh merchandise. Dominic von Riedemann, *Winnie the Pooh and Cheetah Girls*, SUITE101 (June 10, 2008), http://suite101.com/article/winnie-the-pooh-and-cheetah-girls-a55429.

termination notice exists.[258] Indeed, in all the cases explored in this Subsection, the value of the work was well known at the time of the alleged rescission and re-grant, and therefore the author's successors were able to extract a payment that reflected their future termination rights. At this stage, authors and their successors are not subject to any "pressures of unequal bargaining power."[259] At this stage, they have the bargaining power.

Therefore, the parties should be allowed to negotiate a new arrangement prior to termination, including by rescinding and re-granting. Enforcing these agreements not only mitigates the end-game problem, but also does not eviscerate or frustrate Congress's intent. These agreements reflect the power given to authors and their successors by the termination-rights mechanism, and therefore advance the goals that led to their enactment.

B. Post-Termination Fragmentation of Rights

This Section explores some of the ways in which a work can be exploited after termination, and focuses on the situation, which is not uncommon, in which post-termination exploitation requires the consent of several right-holders. This fragmentation of rights might require an agreement among the right holders prior to any post-termination use of the work because each of them can otherwise veto the entire project.[260] Multi-party negotiation can be expensive and may fail, which can result in underuse of the work. This Section explores the problem of post-termination fragmentation as well as various doctrines in copyright law that affect its scope.

258. This Section suggests that enforcing rescission and re-grant agreements is consistent with the goals of the Copyright Act if they were reached after the value of the work was known. There are however reasons to instead enforce only those agreements that were reached while termination notice could have been served or while the termination window is open. First, it might be difficult to determine when exactly the value of the work becomes known but, with rare exceptions, it is known by the time of serving of termination notice; second, at that stage the identity of the statutory successors is known; and third, this should leave the parties enough time to reach a deal before the end-game problem becomes acute.

259. Menell & Nimmer, *supra* note 58, at 814.

260. The author's veto power can be exercised because reproduction or distribution of her work without a license constitutes copyright infringement, and such infringement can sometimes result in an injunction against the infringer. *See generally* eBay Inc. v. MercExchange, L.L.C., 547 U.S. 388 (2006) (holding that injunctions in patent infringement cases are subject to a multi-factor test); Christopher Phelps & Assocs., L.L.C. v. Galloway, 492 F.3d 532, 543–45 (4th Cir. 2007) (applying the same multi-factor test in a copyright infringement case).

1. The Causes for Post-Termination Fragmentation and Its Effects

There are cases in which exploitation of the work after termination is simple and can be accomplished by a single author. For example, when Mark Twain reacquired the copyright in *The Innocents Abroad*,[261] a work he created himself, he had the full power to exploit the work. He could have offered every book publisher the right to publish the book and shared the stream of income the book enjoyed post-termination only with the new publisher.

But in other cases the rights post-termination are fragmented among several entities in a way that makes future use difficult.[262] As an example, let's examine the status of the rights in Bruce Springsteen's most successful album — "Born in the U.S.A."[263] Once Springsteen terminates his recording agreement with Columbia Records, can he, like Mark Twain, then release the album, either by himself or with another record company, and enjoy the future income stream of this record? Probably not. The following paragraphs explore four conditions that can lead to post-termination fragmentation of copyright. Because all of them might be in play in cases of musical work, Springsteen probably does not have all the rights he needs to commercially exploit the work.

Joint authorship: A work might have been created by several joint authors who will have rights in it post-termination. The sound recording of "Born in the U.S.A." might be considered a joint work. Some members of Springsteen's band, the E Street Band, who played on the album, might argue that their creative playing, at least in some tracks, made them co-authors of the recordings. The album also benefited from the creativity of Bob Clearmountain, a prominent sound mixer who worked on the album, who might, along with other creative individuals, be able to assert authorship.[264]

---

261. *See supra* text accompanying note 128.

262. The digital revolution is exacerbating the problem as it allows individuals to easily create joint work. Wikipedia and open source software are extreme examples of this phenomenon. Armstrong, *supra* note 89, at 363; Van Houweling, *supra* note 103.

263. Bruce Springsteen is not a random choice. Springsteen created some of his most commercially successful work in the late 1970s and early 1980s and some believe that he might soon terminate the recording agreements with respect to those albums that still sell well. *See infra* note 311.

264. This paragraph does not suggest that any of those individuals does, in fact, have a strong claim for authorship. This is certainly not an easy claim to be made by a sound mixer. However, the possible status of each contributor as a joint author depends on detailed factual analysis and rather complex, vague, and currently controversial, legal criteria. It is, nevertheless, absolutely possible that band members or sound mixers will be recognized as joint authors in a sound recording. *See* Nimmer & Menell, *supra* note 3, at 404 ("[P]roducers, backup musicians, sound engineers, and others might . . . have a right to terminate, which could produce chaos in the exploitation of sound recordings."); MARK LEE, ENTERTAINMENT AND INTELLECTUAL PROPERTY LAW § 7:15 (2013).

Statutory succession: Upon the death of an author, her termination rights pass to her statutory successors, who might be numerous.[265] Clarence Clemons, the saxophone player and possibly the most famous member of the E Street Band other than Springsteen, passed away in 2011. Therefore, if Clemons is indeed a joint author of the albums, or of parts thereof, then upon his death his termination rights passed to his fifth wife and his four children.

Derivative work: A work might be a derivative work,[266] which may result in fragmentation of rights between the author(s) of the derivative work and the author(s) of the underlying work. It might be argued that the sound recordings are derivative works based on the preexisting lyrics and music.[267] If that is the case, then every individual who wrote lyrics or music to any track in the album will be a copyright holder post-termination whose consent might be required. Luckily, in this case, Springsteen wrote all of the tracks on "Born in the U.S.A." and thus there is no need to separately deal with the writers of the songs.

Complimentary works: Efficient commercialization of the work might require its distribution with another complimentary work. Commercialization will therefore require a license from the copyright owner of the complimentary work. For example, the famous front cover of "Born in the U.S.A." — an iconic close-up picture of Springsteen's rear in front of an American flag — was taken by Annie Leibovitz. Leibovitz probably either assigned the copyright in the picture or licensed the usage to Columbia Records, and she, like Springsteen, can probably terminate this transfer.

Post-termination fragmentation is not limited to copyright law. The album name and the names of several tracks might be trademarks, and those rights presumably belong to the record company and are not subject to termination.[268] Finally, termination of transfer does not give

---

265. The Copyright Act provides an elaborate list of statutory successors. 17 U.S.C. §§ 203(a)(2), 304(c)(2) (2012). *See also supra* note 25 and accompanying text.

266. A derivative work is based on one or more preexisting works, e.g., a movie script that is based on a book, or a movie sequel. 17 U.S.C. § 101. *See also supra* text accompanying notes 55–56. Exploitation of a derivative work typically requires a license from both the owner of the underlying work (or her licensee) and the owner of the derivative work (or her licensee). In the context of termination rights there is an important exception to this rule. *See infra* Subsection VI.B.3.c for a discussion of this exception. *See also infra* note 291.

267. *See supra* note 52 and text accompanying note 56.

268. It is possible that a publisher might not be able to sue pursuant to the Lanham Act (the federal trademark act) to prevent an author or her successors from using the work post-termination. *See generally* Dastar Corp. v. Twentieth Century Fox Film Corp., 539 U.S. 23 (2003) (holding that a former copyright owner cannot sue for "reverse passing off" under the Lanham Act with respect to copyrighted work that fell into the public domain). A full analysis of the post-termination rights under the Lanham Act in light of *Dastar* is beyond the scope of this work.

the author any rights in the master records. The rights in those physical objects are controlled by personal property law and not copyright law,[269] and thus the record company will continue to own them.

Indeed, after termination, no single person, not even Bruce "The Boss" Springsteen, will hold all the rights that are required to commercialize the album. The various parties — e.g., Springsteen, E Street Band's members, Clarence Clemons's family, Annie Leibovitz, and Columbia Records — will likely need to reach an agreement, and they will likely run into a market failure known as the tragedy of the anticommons. This phenomenon exists when the rights needed to effectively use a certain resource — in this case an album — are held by many individuals whose consent is required for such use. Transaction costs substantially increase with the number of contracting parties,[270] holdouts are expected, and the result is underuse of the resource in question.[271]

2. The Publisher as a Bundler

Another way to look at this problem is to consider the role of the intermediaries — e.g., the book publishers or record companies. One of the main functions of an intermediary is to serve as a bundler. The intermediary concentrates all the relevant rights within one entity: itself. Legally, this is done by entering into a series of transactions that guarantees that the intermediary will have all the needed rights to commercially exploit the work. Thus, it is likely that prior to the production of "Born in the U.S.A.," Columbia Records had secured a license or assignment from Springsteen, the E Street Band members, Annie Leibovitz, and from any other person that might have rights in the album (e.g., the sound mixer).[272] The record company also owns the physical master recording and the trademarks for the work. Thus, through a network of contracts, prior to termination, all the rights are owned or licensed to one entity and the problem of holdouts is

269. 17 U.S.C. § 202.

270. In addition to the problem of negotiation with multiple parties, termination with respect to some works might be staggered, which can make the problem significantly worse. Because termination rights vest 35 years after they are granted, different rights with respect to one work might be terminated in different times. For example, if a license from a writer of a book, which allows the production of a movie, was secured in 1980, and a license from a composer to use her piece as a soundtrack for the movie was secured in 1985, the studio will need to deal with the writer's veto power in 2015 only to face another veto power, from the composer, in 2020.

271. *See* Heller, *supra* note 14; Michael A. Heller & Rebecca S. Eisenberg, *Can Patents Deter Innovation? The Anticommons in Biomedical Research*, 280 SCI. 698 (1998) (discussing how the tragedy of the anticommons emerges in patent law).

272. Some of those individuals were probably salaried employees of the record company and thus the company is the author of their work under the work-made-for-hire doctrine.

eliminated. Moreover, for the record company, holdout is a minor issue because it bundles all the rights at an early stage, when substitution is very easy. At this stage, any individual (e.g., a band member, a technician, or a photographer) who refuses to grant the record company the required license will be easily replaced by someone else.

This point of view sheds light on a concerning aspect of the termination-of-transfer mechanism: terminating the licenses and assignments destroys the main tools — these contracts — that allow the industry to concentrate the rights needed for commercial exploitation within one entity — the intermediary publisher or record company — and thus overcome the tragedy of the anticommons.

3. Solutions to the Post-Termination Fragmentation Problem Under Current Law

Various copyright law doctrines address some, but not all, of the concerns regarding the fragmentation of rights among authors after termination. The scope of some of those doctrines is vague and their future interpretation could have a significant effect on the magnitude of the tragedy-of-the-anticommons problem. This Subsection explores three such mechanisms: doctrines that limit the number of authors, rules that deny authors their veto power with respect to their work, and a specific rule that allows the utilization of derivative work post-termination.[273]

a. Limiting the Number of Authors

There are two main doctrines in copyright law that determine the number of authors of a work: joint authorship and the work-made-for-hire doctrine.

Joint authorship is a complex concept in copyright law. The Copyright Act defines joint work succinctly,[274] though the case law developed a high threshold for joint authorship that goes beyond the statutory language.[275] Many commentators believe that the reason for

---

273. The problem of fragmentation of rights cuts across many doctrines in copyright law. A full analysis of all issues raised by those doctrines is well beyond the scope of this work. This Article, therefore, only outlines those issues. *See* Van Houweling, *supra* note 103.

274. A 'joint work' is a work prepared by two or more authors with the intention that their contributions be merged into inseparable or interdependent parts of a unitary whole." 17 U.S.C. § 101.

275. Thus, for example, the contribution of each joint author must be original enough to be independently copyrightable, and all joint authors must intend to have their contribution merged into inseparable unitary whole. *See, e.g.*, Thomson v. Larson, 147 F.3d 196 (2d Cir. 1998); Ericksonv. Trinity Theatre, Inc., 13 F.3d 1061 (7th Cir. 1994).

such a high threshold is the need to prevent the accidental creation of joint authorship.[276]

Having such a high threshold, or perhaps even a higher one, is desirable because it minimizes fragmentation of copyrights post-termination. In particular, courts should be extremely hesitant to grant joint authorship rights to players in a musical piece, and require clear evidence that there was intent, especially of the main performer, to create joint authorship.

The related work-made-for-hire doctrine, which was already explored in Section II.D of this Article,[277] is crucial in limiting the number of authors in some cases, particularly in the movie and software industries. Those industries are characterized by having dozens or even hundreds of creators, but, due to this doctrine, they are not granted authorship status. Instead, the employer, typically the movie studio or software company, is the author. Termination rights are not available when the work was made for hire.[278] Therefore, the broader the scope of this doctrine, the smaller the problem of post-termination fragmentation becomes.

b. Denying the Authors Their Veto Power

The Copyright Act provides specific rules to mitigate the fragmentation that is caused by joint authorship and multiple statutory successors. Those rules, when applicable, might deny some co-authors the ability to holdout by letting the majority of right holders determine the use of the work.

One such rule states that the holders of the majority of the termination rights[279] among the joint authors and the statutory successors can exercise the termination right with respect to the work. More importantly, the Copyright Act also provides that a future assignment or license signed by such majority holders is binding on all right holders.[280] Making termination contingent on agreement among holders of a majority interest and allowing such a majority to bind the minority, substantially mitigates the tragedy of the anticommons. These mechanisms increase the chances that some right

276. *See, e.g.*, Julie Katzman, *Joint Authorship of Commissioned Works*, 89 COLUM. L. REV. 867 (1989); Lior Zemer, *Is Intention to Co-Author an "Uncertain Realm of Policy"?*, 30 COLUM. J.L. & ARTS 611 (2007).

277. *See supra* text accompanying notes 46–52.

278. 17 U.S.C. §§ 203(a), 304(c) (2012).

279. To be exact, the Copyright Act provides that the holder of a majority of termination interests among the statutory successors can exercise the termination right for that deceased author and that the holder of a majority of termination interests among joint authors can terminate a grant executed by those joint authors. 17 U.S.C. § 203(a)(1).

280. 17 U.S.C. §§ 203(b)(3), 304(c)(6)(C). This rule was heavily negotiated prior to the enactment of the Copyright Act of 1976. *See* Bently & Ginsburg, *supra* note 61, at 1568.

holders will work together while they might deny the veto power from each right holder. Thus, a broad interpretation of these mechanisms might mitigate the problem of post-termination fragmentation, at least when such fragmentation is caused by joint authors or statutory successors.[281]

If a majority does not form post-termination to bind the minority, then once the termination is effective, the joint authors or statutory successors hold the work as tenants in common. As such, each of them can grant a non-exclusive license in the work but all must agree to sell the copyright or to grant an exclusive license. In that respect, the Copyright Act grants the joint authors and statutory successors a right that is powerful, though it is not as powerful as a veto power. Indeed, no single individual has the power to prevent others from using the work by withholding her consent, but each has the power to cause harm to the market power of the other right holders by granting non-exclusive licenses and thus allowing competition in the exploitation of the work. Therefore, even without the veto power, using copyrighted works effectively might require an agreement by the majority of right holders that will bind all right holders.

Finally, in several specific circumstances, the Copyright Act denies authors their veto power with respect to their work by forcing them to grant compulsory licenses.[282] This type of solution to the problem of post-termination fragmentation is further explored in Section VI.C.

c. The Derivative Work Exception

Derivative works might present the most difficult post-termination problem. These works are not only common, but they also provide an extremely powerful veto power to the underlying author. This veto is powerful because, inter alia, it is extremely difficult to sever the underlying work from the derivative work. Indeed, in some cases, an author's veto power in a non-derivative work can be avoided by providing a substitute. Bruce Springsteen, for example, always has the option of releasing "Born in the U.S.A." post-termination without Annie Leibovitz's picture. Derivative authors typically do not have that option.

---

281. Thus, for example, a recent court decision that allowed a holder of a minority interest to terminate his transfer just because he signed a separate document might not serve the public interest as it adds to the fragmentation and possibly defeats the purpose of this specific arrangement regarding joint authors. Scorpio Music S.A. v. Willis, No. 11CV1557 BTM (RBB), 2012 WL 1598043 (S.D. Cal. May 7, 2012) (allowing Victor Willis, the former lead singer of the Village People, to terminate his rights (as a joint author) in several of the group's hits).

282. *See infra* note 291.

The story of Superman is a perfect example: Warner Brothers cannot sever the underlying Superman story, written by Jerry Siegel and Joe Shuster, from their modern franchise. Thus, without a statutory exception, once the transfer of Siegel and Shuster is terminated, a license from their statutory successors will be required. The reverse is also true. The statutory successors of Siegel and Shuster, even if they all agree to work together, might also find it difficult to exploit Superman post-termination. The original work of Siegel and Shuster, which is the subject of the current termination litigations, does not include many elements of the Superman story as we know it today.[283] Therefore, after termination, without the "derivative work exception," neither Warner Brothers nor the successors of Siegel and Shuster will be able to continue to effectively exploit the Superman franchise, unless they reach a new deal.

As discussed in Section II.D, the 1976 Act partly addressed this problem by providing that a derivative work "may continue to be utilized" post-termination, provided that this privilege "does not extend to the preparation . . . of other derivative works."[284] While this language is vague, courts should read it broadly. Otherwise, the authors of the underlying work would have tremendous leverage over the derivative creator, which could result in underuse of the derivative work and a chilling effect on derivative creators. Negotiation can be extremely difficult in those cases in which more than one underlying work or more than one post-termination owner is involved. In those cases, the possible exploitation of the derivative work might be dictated solely by the scope of the derivative work exception. Reading the term "utilized" broadly is therefore desirable. Utilization should thus include making new copies of the work even if they are slightly different from the original work. For example, creating a digital version of an old movie or a slightly edited version of a classic film should be covered by the derivative work exception.

Regardless of the future interpretation of the derivative work exception, this provision provides only a partial solution to the problem. Thus, while Warner Brothers might be able to distribute older Superman movies after termination — as "utilizing" the

---

283. For example, in the original story, Superman was unable to fly; he could only leap. He was not weakened by Kryptonite, which was introduced a few years later. The original story also did not include any of Superman's famous archenemies including Lex Luthor. Some of those additional characters or elements were created in the 1940s by Siegel and Shuster. However, at that time, the two were salaried employees of DC Comics and therefore they were not the authors of those stories and their successors cannot get the copyright to them. *See Siegel v. Warner Bros. Entm't Inc.*, 542 F. Supp. 2d 1098 (C.D. Cal. 2008). In addition, Siegel's successors had already conceded that, post-termination, they would not own the trademarks to Superman nor the copyright to it in other countries. *Id.* at 1140–43.

284. 17 U.S.C. §§ 203(b)(1), 304(c)(6)(A).

derivative work — it is likely that making a new movie, and maybe even just making new Superman merchandise, will require a license from the statutory successors of Siegel and Shuster.

C. Comparing the Mechanics of Termination Rights, Droit de Suite, and Employee Compensation Rights: Property vs. Liability Rules

The previous Section suggests that commercial exploitation of copyrighted work after termination typically requires the consent of several right holders. It also suggests how the Copyright Act can be interpreted to mitigate this problem. In this Section, a more thorough and far-reaching solution will be suggested: instead of giving the author the rights to the work upon termination, the law might give her monetary compensation for future usage of her work. A similar regime exists in civil law countries where the law mandates profit-sharing arrangements. Indeed, the termination-of-transfer mechanism under U.S. law as well as droit de suite and employee compensation rights in civil law countries create inalienable profit-sharing mechanisms. However, the ways in which these systems achieve this profit sharing differ. U.S. law reverts ownership and control to authors, while droit de suite and employee compensation rights mechanisms give the author only a right to compensation. Under droit de suite, the amount of compensation is determined by statute,[285] while under employee compensation rights it is either determined by statute, by an administrative body, or by a court.[286]

Comparing these different mechanisms requires consideration of a well-known problem in the law and economics literature: choosing whether to protect an entitlement with a property rule or a liability rule.[287] Under all regimes the creator has an entitlement to a certain revenue stream from her creation. The significant difference is how this entitlement is protected. When an entitlement is protected by a property rule, no one is allowed to expropriate the property without the consent of the entitlement holder. This is precisely the mechanism used by the termination-of-transfer rules under the Copyright Act. After termination, the copyright is owned by to the author and no one can use it without her consent.

In contrast, if an entitlement is protected by a liability rule, others are allowed to make use of it without the entitlement holder's consent, subject to compensation determined by law. This is the method used by droit de suite and employee compensation rights. For example, even when an employee's invention turns out to be so valuable that

285. The EU Directive, *supra* note 65, art. 4; *see also* Netanel, *supra* note 22, at 23.
286. *See* Ying, *supra* note 73, at 766–76.
287. *See, e.g.*, Calabresi & Melamed, *supra* note 17; *see also* Bebchuk, *supra* note 193.

the law grants the employee a right to receive special compensation, the employee cannot prevent the employer from exploiting the work. Instead, the employee can only demand monetary compensation.

In their seminal work, Professor Guido Calabresi and Douglas Melamed suggested that the choice between these mechanisms should depend on the magnitude of the transaction costs.[288] When transactions cost are low, property rules are typically superior as they allow the parties to reach an efficient deal. When transaction costs are high, however, liability rules might be preferred. Liability rules require a third party (e.g., judges, governmental agencies) to determine the compensation. While those actors are typically not as well informed as the parties to the transaction, this imperfect mechanism might be better than relying on a property rule because transaction costs may impede the parties from reaching an efficient deal.

The analysis in Section VI.B shows that, as commercial exploitation typically requires multi-party consent, transaction costs are expected to be high. In a tragedy-of-the-anticommons situation, reaching a deal among parties that have veto power might be difficult and expensive. Therefore, protecting the rights of authors post-termination with a property rule might be inefficient, as the high transaction costs will prevent the parties from reaching an efficient deal to exploit the work. In this case, protecting the entitlement with a liability rule might be preferred.

Technically, there are various ways in which the Copyright Act can protect the entitlement of the author with a liability rule. For example, the Act can provide that after a statutorily predetermined period of time,[289] the author will be entitled to additional compensation. Alternatively, the author might be allowed to terminate all transfers, but may be obliged to grant a compulsory license, likely an exclusive one,[290] to the original transferee upon request.[291]

---

288. Calabresi & Melamed, *supra* note 17, at 1105-10.

289. If the liability rule system tries to imitate the current property rule system, the right to additional compensation should be available thirty-five years after the grant of an agreement to exploit the work. However, the analysis in Section V.E of this Article suggests that the author's rights should probably be available sooner.

290. If the Copyright Act is modified to force the author to grant a nonexclusive compulsory license, the problem explored in Section VI.B will only be partly solved. In some cases the author will be able to cause real harm to the original transferee (the beneficiary of the compulsory license) by granting licenses to the transferee's competitors and thus denying her monopoly revenues. The original transferee will thus need to negotiate with the author to prevent her from granting additional licenses. This might increase transaction costs and cause holdouts in multi-party negotiations. Therefore, if Congress attempts to solve the problem discussed in Section VI.B by introducing compulsory licenses, those licenses might need to be exclusive.

291. In certain circumstances, the Copyright Act already grants compulsory licenses, although not exclusive ones. For example, section 115(a) allows the making and distributing

The author's compensation under any of these suggestions can be determined in a variety of ways. Compensation can be predetermined by a formula (e.g., a percentage of the revenue stream going forward), as is done in many jurisdictions with respect to droit de suite,[292] or by a third party (e.g., a court or an administrative body), [293] as is typically done with respect to the rights of employees to be compensated for their inventions.[294]

VII. ABOLISHING TERMINATION RIGHTS

The analysis in Parts V and VI shows that several factors determine whether termination of transfer and other inalienable profit-sharing mechanisms are desirable. It also proposes several modifications to the termination-rights mechanism to increase its benefits and decrease its costs. In this Part, a more radical suggestion will be explored: that instead of fixing the termination-rights system, Congress should abolish it altogether. Section VII.A summarizes the conditions under which termination rights are efficient, while Section VII.B explores whether those conditions exist in various modern copyright industries.

of copies of some music works under compulsory licenses. Section 104A(d)(3) allows the derivative author to continue to use, under a compulsory license, the underlying work after the copyright in it has been restored. The rationale for this section — allowing the continued exploitation of previously created work — is similar to the rationale for forcing compulsory licenses after termination of transfers.

292. The EU Directive, *supra* note 65, art. 4.

293. Thus, the fees for compulsory licenses pursuant to section 115(a) of the Copyright Act are determined by "Copyright Royalty Judges," who are Article I judges, 17 U.S.C. § 801 (2012), pursuant to administrative procedures prescribed by the Act, *id.* § 803, while the fees for compulsory licenses pursuant to section 104A are determined by a federal district court, *id.* § 104A(d)(3)(B). *See generally* Peter Dicola & Matthew Sag, *An Information-Gathering Approach to Copyright Policy*, 34 CARDOZO L. REV. 173 (2012) (discussing how different entities deal with the need to evaluate the fees for compulsory licenses).

294. The choice between the various types of liability rules depends, inter alia, on a balance between the costs of litigation and the uncertainty involved in an ex post interpretation of vague legal standards (e.g., a duty to pay a court-determined "fair compensation" post-termination) and the inaccuracy of strict legal rules (a duty to pay fifty percent royalties post-termination). *See generally* Louis Kaplow, *Rules Versus Standards*, 42 DUKE L.J. 557 (1992). In addition, the possible biases of those who might be entrusted with the determination of compensation, and in particular the hindsight bias — the inclination to perceive events that have already occurred as more likely ex ante — should be considered. *See* Jolls, Sunstein & Thaler, *supra* note 131, at 1523–24 (describing the hindsight bias); Engel & Kurschilgen, *supra* note 201, at 696–97 (suggesting that, when individuals need to decide on the proper compensation to an author of a successful work ex post, their decisions are heavily affected by that success, even with full information on the ex ante low likelihood of success).

A. When Are Termination Rights Desirable?

The previous Parts of this Article suggest that the main justification for inalienable profit-sharing rules relates to the ability of these legal mechanisms to reduce the deadweight loss in the interaction between the creator and her buyers. The less competition there is among buyers, the bigger the deadweight loss, and the greater the benefits of an inalienable profit-sharing scheme. In a competitive market, there is no justification for such a system. The immediate disadvantage of an inalienable profit-sharing scheme is the misallocation of risk to risk-averse creators and the misallocation of wealth to wealthy superstars. If there is a need for such an inalienable profit-sharing scheme, then it should probably be given real teeth by allowing the creator to receive her share of the profits sooner rather than later.[295]

In addition to the inefficient reallocation of risk and wealth, termination of transfer can cause a misallocation of incentives on the eve of termination, a problem that can be mitigated if parties are permitted to then contract around termination rights. Termination rights may also cause a tragedy-of-the-anticommons problem in which some works are underused, especially if the rights in the work are highly fragmented post-termination. This problem could be resolved, however, by protecting authors' interests with a liability rule instead of a property rule.

With these factors in mind, the desirability of the termination-of-transfer rules can be examined.

B. The Current State of the Copyright Industries

This Section explores the desirability of termination rights in various copyright industries. The analysis will show how the factors described in Section VII.A play out in each industry.

1. The Book Publishing Industry

The book publishing industry played a significant role in the emergence of copyright law,[296] and many copyright doctrines were originally developed to deal with rights in books,[297] as demonstrated

295. *See supra* Section V.E.

296. The first copyright statute in the common law world, the Statute of Anne of 1710, covered only books. Statute of Anne of 1710, 8 Anne, ch. 19 (1710). In the United States, the first federal copyright act, the Copyright Act of 1790, covered only maps, charts, and books. Copyright Act of 1790, ch. 15, 1 Stat. 124 (repealed 1831).

297. *See* Harney v. Sony Pictures Television, Inc., 704 F.3d 173 (1st Cir. 2013) ("Courts and commentators have noted that copyright concepts developed for written works

by the dominant role the book publishing industry played in the discussions that led to the enactment of the Copyright Act of 1909 and the Copyright Act of 1976.[298]

Termination of transfer might have been appropriate in the book publishing industry in the past. That industry was concentrated, and had high barriers to entry as publishers had to invest considerable sums in creating and supporting the infrastructure for the physical manufacturing of books and their distribution chains.[299] Therefore, this industry probably experienced a deadweight-loss problem similar to the one explored in Section V.C. Because books are the archetypal stand-alone work, meaning that they can be commercialized after termination by the author alone,[300] the tragedy of the anticommons is typically a non-issue. Finally, because the publication of books at that time involved significant fixed costs, termination of transfer could not have vested shortly after publication. Under those conditions, inalienable termination of transfer might have made economic sense.

The modern book publishing industry is very different. It is neither concentrated nor expected to become so. U.S. census data, for example, indicates that in 2007, the four largest book-publishing firms in the U.S. had only a 33.4 percent market share,[301] down from 41.8 percent in 2002.[302] The Department of Justice determines market concentration using the Herfindahl–Hirschman Index ("HHI").[303] A market that has an HHI below 1,500 is considered non-

---

imperfectly fit the visual arts."); Rebecca Tushnet, *Worth a Thousand Words: The Images of Copyright*, 125 HARV. L. REV. 683, 684–85 (2012) ("Copyright is literal. It starts with the written word as its model, then tries to fit everything else into the literary mode . . . . Taking words as the prototypical subject matter of copyright has continuing consequences for copyright law . . . .").

298. In both eras, the author's right to receive a second bite at the apple was considered. Section 203, enacted in 1976, was in fact agreed upon in a series of discussions in the early 1960s. Various interest groups in the book publishing industry, such as The Authors League, took part in those discussions and, in particular, in the drafting of the termination-of-transfer provisions. *1965 House Hearings*, *supra* note 31, at 92-94. Sound recordings, in comparison, were not even protected by federal copyright before 1972.

299. *See* 2 JOHN TEBBEL, A HISTORY OF BOOK PUBLISHING IN THE UNITED STATES: THE EXPANSION OF AN INDUSTRY 1865–1919 11, 15 (1975) (suggesting that, until the 1960s, "literary trade publishing had the characteristics of an exclusive club," and that up until the 1910s, this industry was powerful enough to "compel authors to pay for the cost of printing plates").

300. *See supra* text accompanying note 261.

301. U.S. DEP'T OF COMMERCE, AMERICAN FACTFINDER, *Information: Subject Series — Estab and Firm Size: Concentration by Largest Firms for the United States* (2007), http://factfinder2.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=ECN_2007_US_51SSSZ6.

302. U.S. DEP'T OF COMMERCE, ESTABLISHMENT AND FIRM SIZE: 2002 (INCLUDING LEGAL FORM OF ORGANIZATION) 93 (2002).

303. The HHI is calculated by squaring the market share of each firm competing in the market and then summing the resulting numbers. *Herfindahl-Hirschman Index*, U.S. DEP'T OF JUSTICE, http://www.justice.gov/atr/public/guidelines/hhi.html (last visited Dec. 20, 2013).

concentrated.[304] Between 1995 and 2004, the HHI for the consumer book publishing industry was between 284 and 651, with an average of 417.[305] This means that this industry was very competitive in that decade.[306]

Barriers to entry into the book publishing industry have decreased in the digital era, and will likely continue to decrease in the foreseeable future,[307] as high-quality copying becomes more accessible and the publication process becomes cheaper. E-books, a growing industry segment,[308] are especially cheap to produce. Distribution of books is also getting easier. In the past, product placement in bookstores helped make market concentration possible. With more and more books sold online,[309] such concentration is becoming substantially more difficult. In addition, self-publishing is becoming easier, and most people can produce a book using software that is available to the ordinary user.[310]

Without market concentration, there is no justification for a mandatory profit-sharing mechanism. In this industry, the author might not be weak, and thus significant deadweight loss in the author-publisher interaction is unlikely.

---

304. U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES 19 (2010), *available at* http://ftc.gov/os/2010/08/100819hmg.pdf.

305. ALBERT N. GRECO, CLARA RODRIGUEZ & ROBERT WHARTON, THE CULTURE AND COMMERCE OF PUBLISHING IN THE 21ST CENTURY 13 (2007).

306. The actual level of competition might be somewhat lower because, according to the Department of Justice, some large companies in this industry were engaged in limited collusion, possibly in concert with Apple. *See* U.S. DEP'T OF JUSTICE, ANTITRUST CASE FILINGS, UNITED STATES V. APPLE, INC. (2013), *available at* http://www.justice.gov/atr/cases/applebooks.html; Ken Auletta, *Paper Trail*, NEW YORKER, June 25, 2012, at 36. Nevertheless, this collusion was arguably limited to e-books, and it is doubtful that massive long-term collusion can emerge and be sustainable among publishers in such a fragmented industry with low barriers to entry. However, the case against Apple suggests that other parts of the distribution chain of books might still be dominated by companies with significant market power such as Apple and Amazon.

307. *See* GRECO et al., *supra* note 305, at 65.

308. E-book sales accounted for twenty-two percent of all book sales in the second quarter of 2012, up from fourteen percent in the second quarter of 2011. Jim Milliot, *E-books Market Share at 22%, Amazon Has 27%*, PUBLISHERS WEEKLY (Nov. 5, 2012), http://www.publishersweekly.com/pw/by-topic/digital/retailing/article/54609-e-books-market-share-at-22-amazon-has-27.html.

309. *See id.* Amazon itself holds a twenty-seven percent market share of the entire book industry in the United States. *Id.*

310. Amazon, for example, through its affiliated company CreateSpace, offers an easy to use self-publication tool. CREATESPACE, http://www.amazon.com/gp/seller-account/mm-summary-page.html?topic=200260520 (last visited Dec. 20, 2013). The market share of books that were initially self-published has increased in recent years. One such book, "Fifty Shades of Grey," first published in 2011, became one of the most commercially successful books of all time. *See* Sarah Fay, *After 'Fifty Shades of Grey', What's Next for Self-Publishing?*, THE ATLANTIC (Apr. 2, 2012, 12:33 PM), http://www.theatlantic.com/entertainment/archive/2012/04/after-fifty-shades-of-grey-whats-next-for-self-publishing/255338/.

2. The Music Recording Industry

Termination of transfer is expected to have an impact on the music recording industry. In the next few years, a few very successful artists, including Bruce Springsteen, Billy Joel, and Kenny Rogers, will be able to terminate their copyright transfers from the late 1970s.[311] The rights in some of their albums are likely still worth millions.

Unlike the book publishing industry, the music recording industry is concentrated and has become even less competitive in recent years, especially due to the mergers of several major companies. Since the 2004 merger between Sony Music and BMG Music, the four big record companies controlled approximately seventy-five percent of the global market of recorded music[312] and close to ninety percent of the domestic market[313] (compared with about seventy percent of the domestic market in the 1950s and about fifty percent in the early 1970s).[314] Following the merger between Universal Music Group and EMI, which was completed in September 2012, there are currently only three major labels that have significant market share. Prior to that merger the HHI for this industry, based on domestic market share, was high — 2,208[315] — and it was expected to be as high as 2,782, which the Justice Department considers "highly concentrated," after its completion.[316]

---

311. Larry Rohter, *Record Industry Braces for Artists' Battle over Song Rights*, N.Y. TIMES, Aug. 15, 2011 at C1. It should be noted that termination of transfer is available thirty-five years after the grant of transfer, assuming the grant occurred after 1978. Many of the albums mentioned by Rohter are considered "gap grants": albums that were recorded after January 1, 1978 pursuant to a pre-1978 recording agreement. It is unclear if the rights in those albums can be terminated. The U.S. Copyright Office believes that they can. U.S. COPYRIGHT OFFICE, ANALYSIS OF GAP GRANTS UNDER THE TERMINATION PROVISIONS OF TITLE 17 iii (2010). Moreover, the power of recording artists to terminate their transfer is still unclear. The record companies are expected to claim that records are compilations subject to the work-made-for-hire doctrine, and thus that rights in them cannot be terminated. *See, e.g.*, Nimmer et al., *supra* note 52.

312. Jack Bishop, *Building International Empires of Sound: Concentrations of Power and Property in the "Global" Music Market*, 28 POPULAR MUSIC & SOC'Y 443, 443 (2006).

313. The Nielson Company & Billboard's 2012 Music Industry Report, Business Wire (Jan. 4, 2013, 7:12 AM), http://www.businesswire.com/news/home/20130104005149/en/Nielsen-Company-Billboard%E2%80%99s-2012-Music-Industry-Report.

314. Alexander Belinfante & Richard L. Johnson, *Competition, Pricing and Concentration in the U.S. Recorded Music Industry*, 6 J. CULTURAL ECON. 11, 13 (1982).

315. *Universal Music Group's Proposed Acquisition of EMI's Recorded Music Division: Hearing Before the Subcomm. on Antitrust, Competition Policy, and Consumer Rights of the S. Judiciary Comm.*, 112th Cong. 4 (2012) (written statement of the American Antitrust Institute).

316. *Id*. at 5. Some have suggested that in the digital age "technology is allowing many creators to disseminate their work themselves . . . ." Van Houweling, *supra* note 103, at 615. Joel Waldfogel, who is conducting extensive research on the modern distribution methods used by the music industry, found that barriers to entry into the industry have been substantially lowered in recent years, allowing more creators who are not affiliated with a

Under these conditions, it is likely that some deadweight loss exists in this industry and that some creators who might be able to produce a profitable album for a price they would be willing to accept do not end up producing that album.

As the analysis in Part V shows, high level of concentration among buyers is a required condition for inalienable termination rights but not a sufficient one. In fact, it is likely that the costs of this legal mechanism in its current form outweigh its benefits, even in the music recording industry. As explained in Part VI.B, distribution of records post-termination typically requires the consent of several right holders. Therefore, termination rights, which give veto power to many of them, might be costly. The benefits are minimal because a vesting period of thirty-five years leaves too small a revenue stream to the terminating authors, and thus, the reduction in the deadweight loss is only marginal.[317] Moreover, the distortion in the allocation of risk and the transfer of income from the young artist thirty-five years into the future seems exceptionally perverse in the music industry. Megahit records are typically not an isolated source of income for a recording artist. Most creators of megahit records are able to extract considerable income throughout their career from other sources including other records, touring, and advertising campaigns.[318] Consequently, in most cases, those megastars that would be able to earn considerable income through their post-termination rights are very rich when their termination rights vest. Denying income to a twenty-five-year-old struggling Bruce Springsteen so that the sixty-year-old multimillionaire Springsteen can get slightly richer seems undesirable.

As suggested in Parts V–VI of this Article, the Copyright Act could be amended to make the termination-rights mechanism more efficient. With respect to the music industry, this amendment should include forcing compulsory licenses post-termination and possibly shortening the vesting period. Indeed, it seems that the fixed costs of production and distribution in the music industry are not very high, especially in recent years,[319] and the industry is profitable enough to be able to handle earlier terminations of transfers.

---

major record company to have significant commercial success. Joel Waldfogel, *And the Bands Played On: Digital Disintermediation and the Quality of New Recorded Music* (June 25, 2012), http://ssrn.com/abstract=2117372. This research might indicate that, in the long run, a natural reduction in the level of concentration in the music industry should be expected.

317. This claim is further explored in Section V.E, which shows that even if a very low discount rate is used, the average authors will be able to get back only eight percent of the total value of their work by exercising their termination-of-transfer rights.

318. There are of course exceptions to this rule, including “one hit wonders.” *See supra* note 207.

319. *See* Waldfogel, *supra* note 316.

While the termination rights system, in its current form, seems inefficient in the music industry, it is unclear whether the implementation of the modifications proposed in this Article can cause the total benefits to outweigh the total costs. The benefits of reducing the deadweight loss should also be compared with other legal rules that might achieve this reduction. Alternative rules might include tighter merger controls in the industry[320] or reducing barriers to entry by, for example, fighting payola[321] or interpreting the fair use doctrine broadly.[322]

3. The Film Industry and Software Industry

The film industry and the software industry are discussed together because they present a common problem. Under current law, with a few exceptions that are mentioned below, termination of transfer is not expected to have a substantial effect on these industries. Nor should it.

Movies and software are the result of the creativity of many individuals, possibly hundreds of them. Granting even limited power to those individuals with respect to the final product would cause a transaction cost nightmare. In fact, with so many possible creators, even a compulsory licensing system would probably be much too expensive to manage.

Under current law, both industries can and do use the work-made-for-hire doctrine to concentrate all the rights in the work within the production company or the software company.[323] Termination of transfer does not apply to works made for hire and therefore, as a general matter, both industries will not need to deal with the effects of section 203.

---

320. *See generally* 15 U.S.C. § 18a (2012); Robert Pitofsky, *Proposals for Revised United States Merger Enforcement in a Global Economy*, 81 GEO. L.J. 195 (1992).

321. *See* 47 U.S.C. § 317 (2006).

322. Interpreting the fair use defense narrowly requires the producer to secure more licenses, increasing transaction costs and the barriers to entry into the industry, and creating an imbalance of wealth between major copyright intermediaries and small producers. Thus, for example, a legal rule that requires a license for every sampling of music, see Bridgeport Music, Inc. v. Dimension Films, 410 F.3d 792, 801 (6th Cir. 2005), makes the production of music less remunerative for artists and smaller producers who cannot rely on their own library of preexisting work. *See generally* Jessica Litman, *Real Copyright Reform*, 96 IOWA L. REV. 1, 10–11 (2010).

323. Motion pictures are one of the nine categories for which a work-made-for-hire status can be established contractually with respect to a specially ordered work, and many, possibly most, creators in the software industry are salaried employees who create the work within the scope of their employment. *See supra* text accompanying notes 48–51. *But see* Armstrong, *supra* note 89, at 405-09 (discussing the problems termination rights can cause for open source software).

The film industry, however, routinely creates derivative works using preexisting works, most typically movies based on previously published books. In those cases, as the producers of *Rear Window*[324] and *Superman*[325] discovered, and as discussed in Section VI.B, the industry will need to deal with the termination of the rights in the underlying books. This problem can be mitigated by either giving a broad interpretation to the derivative work exception or by the proposed switch to protection by liability rule (e.g., compulsory licenses).

4. The Fine Art Industry and Resale Royalty Rights

The fine art industry presents a unique twist to the profit-sharing issue because, unlike the other major copyright industries, it is based on the sale of a small number of physical objects.[326] This might affect the costs of a voluntary profit-sharing scheme. As discussed in Section III.C, effective contractual profit-sharing schemes fail to fully address the problem of downstream buyers. The ability to create a servitude in favor of the artist might therefore be valuable to the parties. However, as explored in Section III.C, such arrangements will probably require a separate registration system and procedures for locating and compensating the authors and their successors, which will probably increase transaction costs and create some fragmentation of rights.[327] A detailed cost-benefit analysis might explore whether such a system is desirable.

However, as shown in Section III.C, whether or not the creation of servitudes in fine art articles should be allowed, the problem of downstream buyers does not justify inalienability. Like termination rights, droit de suite, as an inalienable profit-sharing scheme, might be

324. *See supra* note 54.

325. *See supra* text accompanying notes 43–44.

326. Some have suggested that this feature, by itself, justifies the enactment of droit de suite. The rationale is that the creators of fine art cannot use copyright law like other creators can. Indeed, while copyright law is crucial to the authors of books and music, it only marginally benefits sculptors and painters. Therefore, the argument goes, because copyright primarily protects the interests of writers and musicians, sculptors and painters are entitled to their own protection mechanism. *See* DROIT DE SUITE STUDY, *supra* note 64, at ix–x. This argument is unconvincing and somewhat puzzling. It seems that the fine art industry simply does not suffer from the problem that copyright law tries to mitigate. Without copyright protection, other creative industries will suffer from a public good problem because, once the work is published, it can easily be copied in a way that will deprive the creator of most of her potential income. Copyright law aims to mitigate this problem. The fine art industry does not suffer from this problem to the same extent because, in many cases, copies of a work of art are a poor substitute for the original work, and the artist can earn most of her income from the initial sale. In other words, copyright law does not discriminate against fine art. This industry is simply better positioned to protect itself against the harm of free copying, even without legal intervention.

327. *See* Hansmann & Santilli, *supra* note 87, at 276.

justified only if there is insufficient competition among the buyers of fine art. This is not the case.

Unlike in many other creative industries, fine art is commonly sold directly to the ultimate buyers, and thus the power of the intermediaries (e.g., dealers and galleries) is limited. Moreover, there are more than 6,000 galleries and art dealers in the United States, with the largest fifty companies controlling only about 40% of the market.[328] There are also more than 17,500 museums in the country.[329] Barriers to entry into this market are low, and thus it is unlikely that market concentration will develop in the future.

Therefore, as the fine art industry is highly competitive, there is no real justification for inalienable rights to resale royalties.[330] The artists in this industry are not feeble individuals who must face massive powerful buyers.

VIII. CONCLUSION

An in-depth analysis of the economics behind the termination-of-transfer provisions of the Copyright Act and comparable mechanisms under foreign law shows that profit-sharing mechanisms could be desirable as voluntary arrangements, and that the law might encourage their creation and enforcement. The costs of inalienable termination-rights mechanism, however, outweigh the benefits.

Several modifications to the termination rights rules may improve their operation, including making termination vest earlier, allowing contracting around the rights on the eve of termination, and protecting authors' interests with a liability rule rather than a property rule. Even with these modifications, it is unclear whether the continued existence of termination rights is economically justified, especially given the reality of decreased barriers to entry in many modern copyright industries.

---

328. *Art Dealers & Galleries Industry Profile*, FIRST RESEARCH (Sept. 16, 2013), http://www.firstresearch.com/Industry-Research/Art-Dealers-and-Galleries.html.

329. *Museum Facts*, AMERICAN ALLIANCE OF MUSEUMS, http://www.aam-us.org/about-museums/facts (last visited Dec. 20, 2013).

330. Hansmann & Santilli reached a similar conclusion when they analyzed the desirability of those rights. *See supra* note 87, at 278–79.