STRONGER THAN KRYPTONITE?
INALIENABLE PROFIT SHARING SCHEMES IN
COPYRIGHT LAW

Guy A. Rub*

Abstract
Starting in 2013, authors of copyrighted work and their successors will be able to terminate every assignment and license 35 years after execution. These termination rights are inalienable and are expected to have a substantial impact on some industries, and in particular, the music industry.

This Article provides the first in-depth economic analysis of these inalienable rights. It explores the traditional justifications for the inalienability of termination rights and finds them unconvincing and lacking. Termination rights seem to be rooted in a romantic perception of a starving, unsophisticated artist, a description that is neither accurate nor justifies inalienability.

The Article shows that when competition among buyers of copyrighted work is limited, inalienable termination rights might promote economic efficiency. Those rights allow the creator to sell her work in two steps. Initially, the pre-termination rights are sold when the seller lacks market power, but later, when the value of the work is known, the author can sell her post-termination rights as a monopolist. This can increase the incentives to create. The main costs of this system include the misallocation of risk from risk neutral buyers to risk averse sellers, the misallocation of wealth from poor authors to rich one, an end-game problem—the need to control the externalities between the parties as termination approaches, and the problem in reassembling the various rights after termination. The Article makes three suggestions for improving this system: vesting termination rights sooner, allowing the parties to contract around them when the time of termination approaches, and forcing the author

* Assistant Professor of Law, The Ohio State University Michael M. Moritz College of Law. I would like to thank Stefan Bechtold, Omri Ben-Shahar, Rebecca Eisenberg, Stephanie Hoffer, Ariel Katz, Margaret Radin, Aaron Romanello, Andres Sawicki, Kathryn Spier, Peter Swire, Chris Walker, Tal Zarsky, and the participants of the Workshop for Junior Researchers on the Law and Economics of Intellectual Property and Competition Law organized by the Max Planck Institute in Munich, 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 of the Ohio Junior Scholars' Workshop for their valuable comments as well as Christopher Matgouranis and, Matthew Gherlein for outstanding research assistance. All remaining errors are, of course, my own.
to grant the transferees compulsory licenses.

The analysis suggests that while termination rights might have been economically desirable in the past, nowadays their costs probably outweigh their benefits in all major copyright industries. The Article further shows that adopting a similar mandatory resale royalties system in the fine art industry, which is common in foreign jurisdictions and is currently being considered by the U.S. Copyright Office, is undesirable.

Introduction .............................................................................................................................. 3
Part I: Termination of Transfer and other Inalienable Profit-Sharing Mechanisms ................. 7
  A. Termination of Transfer as an Inalienable Right ......................................................... 7
  B. Termination of Transfer under Section 203 ................................................................. 10
  C. Termination of Transfer under Sections 304 (c)-(d) .................................................... 11
  D. Exceptions to the Termination of Transfer Power ....................................................... 14
  E. Inalienable Profit Sharing Mechanisms in Other Jurisdictions .................................... 16
Part II: Termination of Transfer as a Mandatory Profit Sharing Scheme ................................. 19
  A. The Desirability of Profit Sharing Arrangements ........................................................ 20
  B. Profit Sharing and Contractual Default Rules............................................................. 23
  C. Rights against Downstream Buyers: Profit Sharing and Property Law ....................... 25
Part III: The Unconvincing Traditional Justifications for Termination Rights......................... 29
  A. Creators as Non-Sophisticated Weak Parties: The Starving Artist Myth .................... 30
  B. The Uncertain Future Value of Copyrighted Works .................................................... 34
  C. Collective Action Problem Among Buyers.................................................................. 35
Part IV: The Ex-Ante Effect of Inalienable Profit Sharing Schemes: Termination of Rights and Incentives to Create ............................................................... 37
  A. Competitive Markets with Risk Neutral Participants .................................................. 37
  B. Competitive Markets With Marginally Diminishing Utility of Wealth and Risk Aversion ....................................................................................................................... 40
  C. Non-Competitive Markets with Risk Neutral Participants ........................................... 43
  D. Non-Competitive Markets with Diminishing Utility of Wealth and Risk Aversion ....... 46
  E. Sooner Vesting of Termination Rights ....................................................................... 46
  F. The Model, Droit de Suite, and Employees’ Compensation Rights ............................. 48
  G. Termination Rights and Irrationality ........................................................................... 49
Part V: The Ex-Post Effect of Inalienable Profit Sharing Schemes: Inefficiencies Immediately Before and After Termination ................................................................. 52
  A. The End-Game Problem: Externalities on the Eve of Termination ............................. 52
  B. The Problem of Shared Work: Joint Authorship and Ownership, Complementary and Derivative Work ................................................................................................................. 56
  C. Comparing the Mechanics of Termination Rights, Droit de Suite, and Employees’ Compensation Rights: Property vs. Liability Rules ........................................... 64
Part VI: Abolishing Termination Rights ................................................................................. 67
  A. When Are Termination Rights Desirable? ................................................................. 67
  B. The Current State of the Copyright Industries ............................................................. 68
Conclusion ................................................................................................................................ 75
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 which allows authors to terminate every sale and every license they executed after a few decades. The successors of Jerry Siegel and Joe Shuster, the creators of Superman, are attempting to use this mechanism and terminate the agreement that assigned the copyright in Superman to DC Comics and its licensee Warner Brothers. 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 company. In doing so they will take advantage of Section 203 of the Copyright Act, which provides that, starting in 2013, every author can terminate any sale of copyright and any license 35 years after its execution. This termination right—which some have called “a time bomb”—is non-transferable and non-waivable and it can be exercised “notwithstanding any agreement to the contrary.” This Article provides the first in-depth economic analysis of these inalienable termination rights.

Termination rights stand out in our copyright system. Part I of this work 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 doctrine 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 all of the European Union and in most other foreign jurisdictions, 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, including by a study

---

5 See infra Subsection I.E.1.
that the U.S. Copyright Office is currently conducting. Patent law, in some jurisdictions, also provides an inalienable right for compensation for employees who develop commercially successful inventions in the scope of their employment. The common theme among these legal mechanisms is that they force the creator and her assignee or licensee to share some of the future profits from the work or invention.

Part II addresses the efficiency of profit sharing arrangements. The analysis shows that those arrangements are a way to align the incentives of creators and their assignees and licensees, especially if the two are entering a long term relationship. As such, various profit sharing arrangements are common in the copyright industries.

If a legal system wishes to encourage profit sharing arrangements it can do so with three different legal mechanisms. First, the desirability of profit sharing arrangements should be taken into account in the design of contractual default rules in copyright. Specifically, the 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 the creator a transferable right to receive additional future profits from her work. The advantages of this mechanism as a penalty default rule were not appreciated in the literature to date. Another level of legal protection of profit sharing arrangements can be provided by property law. Indeed, contractual profit sharing arrangements might not be strong enough 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 a profit sharing arrangement are explored in Part II.

The third level of legal protection of profit sharing arrangements is inalienability. This is the choice that was made by Congress when enacting the Copyright Act of 1976. Congress seems to have accepted a common supposition that protecting authors by giving them “a second bite of the apple” requires making termination rights mandatory. This choice, and whether, when, and how it might promote the goals of our copyright systems or the welfare of authors, is the focus of Parts III-VI.

Part III considers the traditional justifications for the inalienability of the termination rights and finds them unconvincing and lacking. The termination of transfer mechanisms seem to be rooted in a romantic

---

6 See infra note 70.
7 See infra Subsection 1.E.2.
8 See infra text accompanying notes 82-84.
perception of a starving, unsophisticated artist, who is taken advantage of by a shrewd and possibly dishonest buyer. This description, however, is neither accurate nor does it justify inalienability. Another common justification is the uncertainty regarding the future value of a copyrighted work prior to commercial exploitation. Uncertainty, though, is not a convincing reason for inalienability. On the contrary, the high uncertainty justifies allowing the risk averse author to transfer the risk to a risk neutral buyer. In fact, William Landes and Richard Posner have succinctly concluded that this aspect in itself should make droit de suite undesirable as reducing the incentives to create. Landes and Posner are correct in claiming that mandatory profit sharing arrangements might misallocate risk but their short analysis fails to take into account all the economic effects of those mechanisms.

The myth of the starving artist, while incorrect in itself, might be just a straw-man for the real economic factors that are in play with respect to termination rights. Part IV provides a detailed and novel model to analyze the effects of those rights on the creators’ compensation and the incentives to create. This part shows that under certain conditions inalienability can be economically justified. This can happen when a certain market failure exists—when the competition among buyers of copyrighted works (e.g., book publishers, record companies) is limited. In that case, mandatory termination rights allow the creator to sell her work in two steps. First, the creator sells her pre-termination rights for a price that reflects the buyer’s superior market power. Then, separately, the creator sells her post-termination rights. Those rights, by law, can be sold only decades after publication, when the value of the work is well established. In this market, the creator is a monopolist of the rights to her work and thus the price will reflect the creator’s superior market power. Overall, with termination rights, the combined expected price for the work, before and after termination, is expected to increase, which is socially desirable. Indeed, higher compensation to authors increases the incentives to create and the number and quality of works produced.

The advantages of selling the post-termination revenue stream years after publication should be compared with the disadvantages of this regime. The model developed in Part IV shows that this system might allocate risk from risk neutral parties to risk averse ones in a way that, in itself, might make the costs of termination rights higher than their benefits. In addition

---

9 See infra Section III.A.
10 See infra Section III.B.
termination rights might inefficiently transfer wealth from poor artists to rich artists, which raises both efficiency and distributive justice concerns. On the other hand, if termination rights are desirable, making them available more than 30 years after publication makes little sense. By that time, the demand for copyrighted works is low, especially when brought to present values, and therefore the benefits from termination rights are too small. Therefore, the Article suggests that termination rights should vest earlier. Early vesting will also mitigate the problem of misallocation of risk and wealth.\textsuperscript{12}

Part V analyzes two additional drawbacks of the termination rights: one of them emerges on the eve of termination and one shortly thereafter. When termination is approaching the author’s and the publisher’s incentives are inefficiently misallied. Such misalignment is sometimes called an end-game problem. Thus, for example, shortly before termination the publisher might invest too little in promoting the work. The Article suggests that even without a change in the statute this problem can be substantially mitigated by allowing the parties to reach contractual solutions notwithstanding the inalienable termination rights. Therefore, the highly controversial practice of rescinding old transfers and re-granting them, as a way to avoid termination,\textsuperscript{13} is consistent with the goals of the Copyright Act, solves the end-game problem, and should therefore be enforceable.

An additional significant drawback of the termination rights mechanism has to do with the way Congress chose to give the author a second bite of the apple. Unlike droit de suite, which gives the author a right for 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 authors who died, 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 all the rights required to commercially exploit a work, prior to its production, primarily by entering into a series of complex contractual arrangements. The Copyright Act, by allowing the various authors to terminate these contracts, undoes the publisher’s bundling. Therefore, exploitation after termination will typically require the consent of all those individual owners. Unfortunately, this multi-party negotiation is typically expensive and can sometimes fail, which will result in underuse of the copyrighted work—a phenomenon known as the tragedy

\textsuperscript{12} See infra Section IV.E.

\textsuperscript{13} See infra text accompanying notes 203-209.
STRONGER THAN KRYPTONITE?

of the anticommons.14

The Article suggests several ways to address this problem. The scope of several doctrines in copyright law 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 a legislative reform by granting the artists just a right for an additional compensation, e.g., in the form of forcing compulsory licenses, instead of a property right.16 This switch from property rights protection to liability rights protection,17 similar to the form of protection common in Civil Law countries, will promote efficiency.

Part VI considers whether, instead of modifying the termination rights system, Congress should abolish it altogether. It is shown that mandatory profit sharing schemes 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 related 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 in other major copyright industries, including the film industry, the software industry, and probably the music industry. The continuous decrease in the barriers to entry in many copyright industries expects 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 an inalienable resale royalties rights, similar to droit de suite. Such a mechanism cannot be justified in a well-functioning competitive industry, such as the fine art industry.

PART I: 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

---

15 See infra Subsection V.B.2.
16 See Section V.C.
and initially grants those rights to the author of the work. 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. In the United States, this power to transfer the rights in the work is not just an incidental side effect of the copyright regime but, in many respects, it is the main reason for its existence. Indeed, because copyright law is perceived as a tool to incentivize authors to invest the resources needed in creating creative works, authors must have the power to transfer and license those rights in order to have substantial monetary gains.

Therefore, in most cases, the rights created by copyright law are transferable, waivable, and licensable. In the United States there are very few narrowly tailored exceptions to this rule. The scope of moral rights under the Copyright Act is a good example of Congress’ hostility to inalienable rights. Moral rights, which are common in Civil Law systems, 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. 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 the ratifying

---

20 This principle, in the United States, is also expressed in the Constitution. U.S. Const. art. I, § 8, cl. 8 (empowering Congress to enact the Copyright Act (to secure “to Authors … the exclusive Right to their respective Writings”) in order “To promote the Progress of Science and useful Arts”). See also Mazer v. Stein, 347 U.S. 201, 219 (1954) (“The copyright law … makes reward to the owner a secondary consideration … 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, and 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). Jeanne Fromer has recently suggested that in many cases these approaches can complete rather than compete with one another. Jeanne C. Fromer, Expressive Incentives in Intellectual Property, 98 Va. L. Rev. 1745 (2012). An analysis of the inalienable legal mechanisms explored in this Article under natural rights theories is beyond the scope of this work.
countries to protect such rights. When, eventually, in 1989, the United States ratified the Berne Convention it adopted an extremely narrow version of moral rights by passing the Visual Artists Rights Act of 1990 (VARA). Those rights are not just narrow, applying only to relatively few “work[s] of visual art,” but they are also waivable.

Considering this 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. Thus, for example, the author of a song may unilaterally terminate a license allowing a record company to record it; 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.” In addition, termination rights cannot pass testate (by a will), but instead they must pass intestate, to successors designated by the Copyright Act.

---

26 Id. 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 very few provisions in the Copyright Act that explicitly prohibit it. See generally Guy A. Rub, Contracting around Copyright: The Uneasy Case of Unbundling of Rights in Creative Works, 78 U. CHI. L. REV. 257 (2011) (exploring the literature on the subject). In several instances in recent years courts have held that contracting around some core copyright doctrines is enforceable. See, e.g., Montz v. Pilgrim Films & Television, Inc., 649 F.3d 975 (9th Cir.2011) (en banc); Forest Park Pictures v. Universal Television Network, Inc., 683 F.3d 424 (2d Cir. 2012).
27 17 U.S.C. §§ 203(a)(2), 304(c)(2) (2006). 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, with whom he was married for 18 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 Group (USA) Inc. v. Steinbeck, 537 F.3d 193, 196 (2d Cir. 2008). See also Ray Charles Found. v. Robinson, CV 12-2725 ABC FFMX, 2013 WL 358174 (C.D. Cal. Jan. 25, 2013) (allowing seven of Ray Charles’ children to terminate certain assignments made by Charles and thus frustrating his clear intent to leave
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 there is much in common between these two sections, they differ in their rationale 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, starting in the first federal copyright statute—the Copyright Act of 1790—copyright protection was granted, subject to certain formalities, upon publication, for a period of protection, which could be extended by another period of protection. Thus, for example, before the Copyright Act of 1976 became effective, copyright lasted for a period of 28 years from the date of publication, which could be extended by another 28 years. The 1976 Act provides for one term of protection, originally for the life of the author plus 50 years.

Switching from a dual term of protection to a unitary term, denied authors a right for 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 renewal period. A transfer of the rights in the renewed 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 was alive 28 years after publication when renewal was available. If the author died prior to renewal, an assignment was valid only if the statutory successors of the right to renew assign that right. Consequently, it became a standard practice to have the authors assign their rights in the first and second period and to have the author’s spouse sign on such assignment agreements as well.

---

32 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, of course, guarantee that the rights in the renewed 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, the children of the
Therefore, having one protection period instead of two denied the author the ability to get back 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. 33 Section 203 is the result of these efforts.

Section 203(a)(3) provides that the author can terminate all transfers 35-40 years after the date of the execution of the grant (typically the date of the agreement) being terminated. 34 A notice of such intent to terminate must be served not less than two or more than ten years before the date of termination. 35 Section 203 applies to grants executed after January 1, 1978 (the effective date in of the Copyright Act of 1976) and therefore, termination under this provision is possible starting in 2013. Consequently, to date, this provision was not subject to extended litigation but it is expected to generate many legal disputes to be considered by federal courts in the years to come.

C. Termination of Transfer under Sections 304 (c)-(d)

Unlike Section 203, which provides a termination rights after 35 years for work 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 56-61 years after the date in which copyright in the work was secured 36 and the second can be exercised 75-80 years after the date in which copyright in the work was secured. 37 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. 38

34 However, if the grant covers the right of publication, termination is available 35-40 from the date of publication or 40-45 years from the date of execution of the grant, whichever is sooner. 17 U.S.C. § 203(a)(3) (2006).
35 These formalities, as well as additional formal requirements specified in Sections 203 and 304 have been strictly enforced by courts. See, e.g., Burroughs v. Metro-Goldwyn-Mayer, Inc., 492 F.Supp. 1320 (S.D.N.Y. 1980); Nance v. Equinox Music, No. 09-cv-7808, 2010 WL 4340469 (N.D. Ill. October 22, 2010).
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 56 years. When the term of protection was extended, Congress thought that it would be wrong to grant an additional protection period as a windfall to the current copyright owners and instead wanted to give it to the authors. 39 Similarly, when Congress enacted the Sonny Bono Copyright Term Extension Act of 1997, 40 extending the duration period by an additional 20 years, it granted the authors a chance to terminate transfers and to exploit the copyright in this period.

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 used this provision to terminate their transfers. 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 Not

39 From an economic perspective this justification seems weak. If extension of copyright duration is a windfall then there is no economic justification to grant it at all as it does not incentivize creation. In fact, one may even doubt whether, under those circumstances, such an extension promotes “the progress of Science” and thus authorized by the Constitution, U.S. Const. art. I, § 8, cl. 8. See supra note 20. When such an argument was raised before the Supreme Court it was rejected partly because the Court did not believe that it is a windfall at all. Eldred v. Ashcroft, 537 U.S. 186, 189 (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, as the protection offered her, a copyright not only for the time in place when protection is gained, but also for any renewal or extension legislated during that time.”) (emphasis added). If 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 a real harm. Prior to the extension, the assignee/ licensee (typically a publisher or a record company) was entitled to a monopoly for a certain period (i.e., 56 years under the Copyright Act of 1909) followed by unlimited competition. At that later period, when the work is in the public domain, the assignee/ licensee cannot stop entrance to the market but it enjoys a first mover advantage. When Congress extended the copyright duration but allowed the author to terminate the transfer, the assignee/ licensee is denied its potential revenues in this later period.


41 For example, in the last 10 years, Superman, which 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), two additional high budget movies that are planned in the near future, and a successful TV series (Smallville); Batman, who first appeared in 1939, was the main character of what is known as the Dark Knight trilogy—three critically acclaimed mega hits released in 2005-2012 (two of them earned more than $1 billion each), as well as several animation TV series and computer games; Spiderman, first appeared in
surprisingly, several cases regarding Section 304 dealt with this industry, and more are expected in the next few years. The most significant of those, a dispute that arose in 1997 and has been litigated since 2004, deals with the copyright to Superman. Superman was created in the 1930s by Jerry Siegel and Joe Shuster, who were paid the then market rate for their work—$130. The statutory heirs of Siegel used the termination window provided by Section 304(c) and filed a notice of termination in 1999, 61 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 battle between the Siegel family and DC Comics and Warner Brothers, the assignee of some of the copyright in Superman. The statutory successor of Siegel’s co-creator, Joe Shuster, have notified DC comics and Warner Brother of their intent to exercise their right under Section 304(d) to terminate Shuster’s transfer in 2013, 75 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.

1962, was the main character in 4 mega-hit films released since 2002 (with the fifth expected to be released in 2014), which earned more than $3 billion worldwide, as well the subject of a Broadway show. Many other comics superheroes star in mega-hits movies in recent years including the Green Lantern (first published in 1940), Captain America (1941), the Fantastic Four (1961), Thor (1962), the X-Men (1963), and Iron Man (1963).

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 adversely affected by 45 notices of termination, to become effective in 2014, filed by the successors of Jack Kirby, the creator of some of Marvel’s most known storylines, including “X-Men” and “Fantastic Four.” This transaction was later completed and in 2011 a District Court held that those termination notices were meritless because Kirby’s work was made for hire. Marvel Worldwide, Inc. v. Kirby, 777 F. Supp. 2d 720 (S.D.N.Y. 2011). At the time of writing an appeal of this decision is pending before the Second Circuit; see also Marvel Characters, Inc. v. Simon, 310 F.3d 280 (2d Cir. 2002) (analyzing with termination rights of Joseph Simon, one of the co-creator of Captain America).

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., CV 10-3633 ODW RZX, 2012 WL 4936588 (C.D. Cal. Oct. 17, 2012) (“…the 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 were paid very generously to continue to develop the story on this emerging successful superhero. Id. (“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.”).


D. Exceptions to the Termination of Transfer Power

Sections 203 and 304 provide several exceptions to the right of the creator of copyrighted work to terminate transfer. In this Subsection the main exceptions will be reviewed.

The most important exceptions have to do with the definition of authorship itself, and in particular, with 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 those cases, the employer of the creator or the person who commissioned the work, is the author and initial owner. In these cases termination of transfers is unavailable. 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 ways 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.” Courts apply 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. In practice, this part of the definition typically applied to salaried employees, e.g., most software engineers.

The second way in which a work might be considered made for hire is if it was specially ordered or commissioned as such. However, while this allows the creator and the party ordering the work to contractually create a work made for hire status, this power is limited to nine enumerated categories of work. The scope of some of those categories is broad and include, inter alia, all motion pictures. The scope of other categories, and in particular “collective work” and “compilation,” is unclear and leaves many questions unanswered: for example, can a record company argue that a

---

50 This test can sometime create difficulties in distinguishing salaried employees and independent contractors. Thus, for example, one of the difficult questions in the litigation between the successors of Jerry Siegel, one of Superman’s co-creator, and Warner Brothers, is what parts of the Superman storyline were created as a work made for hire while Siegel was an employee of DC comics and what parts were not. Siegel v. Warner Bros. Entm't Inc., 658 F. Supp. 2d 1036 (C.D. Cal. 2009).
record is a collective work or a compilation? Does a “best hits” record fit this definition? If the answer is positive the transfer of rights in these works cannot be terminated. These questions and similar ones are expected to be litigated in the years to come.

Another important source of uncertainty is found in “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.” While the rationale for this provision is quite clear as a way to protect the derivative creator, the statutory language creates a host of difficulties. First and foremost, the definition of “derivative work” is in itself open to interpretations. Thus, 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.” Can a record company argue that a sound recording is a derivative work of the lyrics, and thus even if the writers terminate their transfers, the record company can still utilize the record? The term “utilize,” which is not defined in the Copyright Act, is not 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 album to be used in a movie?

Finally, another main source of vagueness is found in the provisions that provide that the termination power “may be effected notwithstanding any agreement to the contrary.” 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

54 See infra Subsection V.B.2.d. The most famous example for 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. at 207. In that case, governed by the Copyright Act of 1909 that did not include a derivative work exception, the Court held that a production company formed by James Stewart and Alfred Hitchcock could not continue to reproduce or publicly display the classic movie “The Rear Window.” This injunction was issued after Sheldon Abend terminated the license that allowed the production company to use “It Had to Be Murder,” a short story that the movie was based upon. Abend, a literary agent, bought the copyright in the story for a small amount from Chase Manhattan Bank, the executor of the estate of Cornell Woolrich, the author of the short story who died without ever getting married or having children.
56 See Nimmer et al., supra note 52.
compensate the licensee?\footnote{See Peter S. Menell & David Nimmer, \textit{Pooh-Poohing Copyright Law's 'Inalienable' Termination Rights}, 57 J. COPYRIGHT SOC'Y. 799, 827 (2010).} 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?\footnote{See infra Subsection V.A.2 for a discussion on this issue; \textit{See also Loren, supra note 32, at 1344; Menell & David Nimmer, id.}}

Those are some of the difficult questions that are expected to be litigated in the years to come. This Article does not offer a full doctrinal answer to all those questions but the analysis it provides sheds light on the economic effects of the decisions faced by courts.\footnote{See infra Subsection V.B.2.}

\section*{E. Inalienable Profit Sharing Mechanisms in Other Jurisdictions}

The termination of transfer mechanism, which grants authors an inalienable non-waivable right to have a second bite of the apple, is unique to U.S. federal law.\footnote{Copyright law in Britain provided the author a second bite of the apple until 1814. \textit{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 (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 copyright law. However, this right was not included in the final version of the bill which was enacted in 2002. 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, 414-16 (2004). Currently there is no similar right to terminate in Civil Law countries.} However, in other jurisdictions creators of intangible goods are in sometime granted an inalienable non-waivable right to receive additional compensation once their creation is proven to be commercially successful.\footnote{Interestingly, I am not familiar with any legal system that forces the creator to pay the buyer if her work turned out to be worth less than expected. \textit{See generally John Henry Merryman, The Wrath of Robert Rauschenberg}, 41 AM. J. COMP. L.103, 111-12 (1993) (suggesting that the logic of droit de suite justifies compensation the initial buyer if the value of the work decreases over time).} In this section I will briefly mention two such mechanisms: 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 the recent decades. The common theme among termination rights, droit de suite, and employees’ right for compensation—allowing creators to receive additional compensation for successful creations—will
be further explored and compared 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. In most jurisdictions this right cannot be transferred or waived.

While many jurisdictions recognize this right, including in a recently adopted EU directive, the scope of the right and the exceptions to it vary from one country to another. In France and Germany, for example, future royalties used to be based on the gross resale price while in Italy on the capital gains. In the UK the right is limited to resale in public auctions.

Federal law in the United States does not recognize such a right, and there is no international obligation to enact it. However, Congress has, from time to time, considered adding it to the Copyright Act and recently, at Congress’ request, the U.S. Copyright Office has begun conducting research as to the desirability of such an initiative.

---


66 See Merryman, supra note 62, at 104.

67 See U.S. COPYRIGHT OFFICE REGISTER OF COPYRIGHTS, DROIT DE SUITE: THE ARTIST’S RESALE ROYALTY, iii (1992); Monroe E. Price, Government Policy and Economic Security for Artists: The Case of the Droit De Suite, 77 YALE L.J. 1333 (1968). In Europe the law has recently changes as a result of the passage of The EU Directive, which, in Article 4, directs the member countries to base the calculation of resale royalties on the gross resale price.


California is the only state that created a similar statutory right to resale royalties. This legislation was passed in 1976\textsuperscript{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.\textsuperscript{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.\textsuperscript{73} Therefore, an employee might assign her rights for future inventions for no compensation at all beyond her salary, even if the invention turned out to be extremely valuable to the employer.

In many other countries the law is different. In recent decades many countries have enacted laws that regulate the compensation that an employee is to receive for inventions. Those arrangements cannot be contracted around. In Austria for example—the first country to recognize such inalienable employees’ compensation rights—the employee is given an inalienable right to receive “adequate” royalties in addition to the salary.\textsuperscript{74} The law in Japan provides that employees shall receive reasonable compensation for their intellectual labor.\textsuperscript{75} British law is more limited and provides that in exceptional circumstances, for example if the employee’s invention resulted in a patent that provides outstanding benefits to the


\textsuperscript{72} Estate of Graham v. Sotheby's Inc., 860 F. Supp. 2d 1117, 1119 (C.D. Cal. 2012). At the time of 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 but the court did not address those issues as it accepted the defendant’s position regarding the violation of the Commerce Clause.

\textsuperscript{73} See 35 U.S.C. § 261 (2006); Teets v. Chromalloy Gas Turbine Corp., 83 F.3d 403, 407 (Fed. Cir. 1996) (“contract 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 type 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).

\textsuperscript{74} Ying, supra note 66, at 767-68. 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.

\textsuperscript{75} Id. at 773-74.
employer, the employee is entitled to an additional compensation, determined by a court.\footnote{\textcite{Morag PEBERDY & ALAIN STROWEL, COVINGTON & BURLING LLP, EMPLOYEE’S RIGHTS TO COMPENSATION FOR INVENTIONS- A EUROPEAN PERSPECTIVE, 8 (2009-2010).}}

3. Other Inalienable Rights in Commercially Successful Works

While the droit de suite doctrine and the rights of employees with respect to their invention were recognized in many countries, various foreign jurisdiction apply 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 “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 of the work.\footnote{\textcite{William Cornish, The Author As Risk-Sharer, 26 COLUM. J.L. & ARTS 1, 8-10 (2002); Hilty & Peukert, supra note 61.}} Croatian copyright law includes a similar provision.\footnote{1 COPYRIGHT THROUGHOUT THE WORLD § 11:32.} French law provides that an author is entitled to proportional remuneration out from the commercial exploitation of the work, and such right cannot be waived contractually.\footnote{Cornish, \textit{supra} note 77, at 7.}

**PART II: TERMINATION OF TRANSFER AS A MANDATORY PROFIT SHARING SCHEME**

The legal rules that were explored in Part I—termination of copyright transfer, droit de suite, and employees’ compensation rights—give the creator a right to have a share of the future profits from successful creations. These arrangements can be analyzed by exploring four questions: First, do profit sharing arrangements—between the creator and her buyer\footnote{I loosely use the term buyer to refer to an assignee of the copyright or a licensee. In most cases the distinction between the two is immaterial as the author can terminate sales and licenses alike.}—make sense and do they have an economic function? Second, how should the desirability of those arrangements, if they are indeed desirable, affects the design of contractual default rule? 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 those questions—the rationale and the effects of inalienability. However, to put that question in context, in this Part I will briefly discuss the first
three questions.

A. The Desirability of Profit Sharing Arrangements

This Subsection will suggest that profit sharing arrangements are common in many situations including in many copyright industries. Those arrangements are chosen by the parties, even if the law does not mandate them, as they serve important economic functions.81

Indeed, profit sharing arrangements are not rare. They are common in the context of agency relationships as they partly align the interests of the agent and the principle,82 and are sometimes encouraged by law.83 They are extremely valuable in long-term relationships as 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 of each of them creates an externality that affects the utility of the other, might be efficient.

Copyright industries provide strong support to this argument.84 In many copyright industries (but certainly not in 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 advantage. 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.85

---

81 Obviously, the efficiency of those arrangements, as explored in this Subsection, might explain why they are common but not why the law should sometimes make them mandatory. This point is simple but it is occasionally not made explicit in some of the literature on the topic. See, e.g., Solow, supra note 56, 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 (2012).


84 Similar arrangements exist in the 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); U.C. Patent Policy, http://www.ucop.edu/ott/genresources/pat-pol_97.html (last visited January 19, 2013) (declaring that the University of California system requires pre-assignment of all patent rights of her employees but that it also provides a royalty sharing plan).

85 DONALD S. PASSMAN, ALL YOU NEED TO KNOW ABOUT THE MUSIC BUSINESS 83-
The typical compensation structure in the book publishing industry is quite similar. In other industries that produce literary work the typical arrangements are different. Thus, for example, most people who write for a newspaper, either as employees or as freelancers, are paid a predetermined fixed amount.

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

Finally, in the fine art industry, artists typically share the profits from

---


89 Hollywood studios are notorious in 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 just the fixed amount. See generally Mark A. Weinstein, Profit-Sharing Contracts in Hollywood: Evolution and Analysis, 27 J. LEGAL STUD. 67 (1998); Gabriel Snyder, How Movie Stars Get Paid, GAWKER (Apr. 2, 2009, 8:00 pm), http://gawker.com/5196154/how-movie-stars-get-paid.

90 In the fine art industry I include those creators who produce and typically sell a single (or very few) physical object of each of their works, e.g. a painting or a statue.
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. 91

Indeed, this short review suggests that profit sharing schemes, although not mandatory by law, are common in the copyright industries, and take many forms. This conclusion is not surprising. A profit sharing scheme involves transaction costs that are typically economically justified only when the actions of one actor affects 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 that this deal will cover just 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. 92 Therefore, the record company will demand a long term commitment by the artist. On the other hand, having a long term arrangement for fixed compensation might create a principle-agent problem because the artist might have too little incentives to produce additional commercially successful work and to promote her existing work. 93 A related problem exists in those cases in which the artist’s future actions can affect the value of her older work. If the artist was already fully paid for those works she might not take into account this externality. 94

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 legislator nor a governmental agency needs to decide if profit sharing is desirable in some situations and not in others, and if it is desirable, in what form. Market participants, who are better informed than any governmental actor (which faces a principle-agent problem of its own), make those decisions routinely. 95 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,

91 Merryman, supra note 62, at 105-07.
93 Hansmann & Santilli, supra note 86, at 265.
94 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. See generally infra note 151.
95 See generally the famous story by Leonard Read “I, Pencil” (discussing how 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.”)
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 has to be analyzed. Second, the ways in which property law right might need to reflect the general desirability of profit sharing arrangement should be explored. And third, the need of having 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.\(^{96}\) Thus, if most authors and publishers prefer a certain profit sharing arrangement, making such an arrangement the default rule might save them transaction costs in negotiating and drafting such an arrangement. This argument is not convincing in this context. 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 be desirable by a majority or even a significant minority of authors and publishers.\(^ {97}\) 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. In other words, the transaction costs in reaching those 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”\(^ {98}\)—is drafted in a way that is undesirable to the better informed party, that party will typically prefer to contract around that rule. A suggestion to contract around the default rule conveys information from

---


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

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, record company or other 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 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 mentioned, this regime granted the author a right to keep all the copyrights in the work in the renewed copyright period, but allowed the parties to contract around such a right. As this default rule is detrimental to the buyer, it incentivizes it to suggest to the author to contract around it. That suggestion, by itself, conveys valuable information to the less informed author: The author is informed that she has a waivable right to receive the copyright back upon renewal and she is informed that the other side—e.g., the publisher—finds it worthwhile to buy this right from her. With this information the author can rationally negotiate her rights in the renewal period. Indeed, several commentators that have harshly criticized this regime as ineffective and even illusory, might have failed to appreciate the value of default rules in conveying information to the authors.

In theory, a similar regime can exist to deal with the problems addressed by droit de suite or the employees’ compensation right regime. The law can set a default rule that gives the creator of fine art a right to resale royalties and an employee a right for 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

---

99 See *supra* text accompanying notes 30-32.

100 As explained in Part I of this Article, that regime did not allow the author to freely transfer the rights in the renewed period if she passed away prior to renewal.

101 It should be noted that authors are not always poorly informed. See *infra* note 104. However, it is reasonable to assume that the vast majority of buyers (including publishers, record companies, and most other intermediaries) are very well informed as repeat players.

102 See, e.g., Lydia Loren, *supra* note 32, 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 59, at 802 (noting that the “judicial interpretation of the 1909 Act frustrated [Congress’] intent by upholding advance assignments of renewal terms”); Litman, *supra* note 33, at 904 (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) (suggesting that this decision reduces fragmentation in copyright).
salient. For example, the law can provide that the employee right for compensation can be waived only in a separate document and not if such a waiver is buried in the boilerplate of a long employment agreement. This arrangement and similar ones can guarantee the flow of information and warn the less informed party—the artist, author or employee—that she is waiving her legal rights.

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. Therefore, they cannot bind downstream buyers. Some have suggested that this is one of the main justifications for the existence of moral rights. The argument is that if it is efficient for the artist to exercise moral rights (e.g., the right for integrity of the work) after the work is sold, contracts cannot typically achieve the


104 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 buyer or employer. Under these conditions the buyers or employers will not compete on the terms and inefficiently harsh unilateral terms will be included in the agreement. See, e.g., Guy A. Rub, Market Solutions to the Boilerplate Problem, CAN. BUS. L. R. (forthcoming 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 on 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 to the terms of the contract and assist 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, 725-27 (2011) (arguing that while disclosure, including of boilerplate provisions, rarely substantially improve 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 III 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. See generally MARGARET JANE RADIN, BOILERPLATE 82-109 (2013).


desired level of control. Instead, a stronger legal mechanism, i.e., inalienable moral rights, is required. This Section explores if a similar argument can justify either the creation of property rights that will protect the profit-sharing arrangements and/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. In other words, the author of a book, for example, 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 extinguish by the first resale.

The legal system can solve this downstream buyers problem by granting the authors a servitude in the copyright or, in case of fine art, in the items in which it is embodied. It can also solve this problem by making a profit sharing arrangement inalienable. 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.107 In other words, 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.108 Servitudes typically create two related problems: First, they increase the transaction costs in the market 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

---

107 This also means that if the creation of a property interest is allowed, it will serve as just a lien and not an affirmative equitable servitude. See generally, Equitable Servitudes—Creation and Kinds—Obligation to Work Copyrights and Pay Royalties, 45 HARV. L. REV. 586 (1932) and the references there; Zechariah Chafee, Jr., Equitable Servitudes on Chattels, 41 HARV. L. REV. 945 (1928); Zechariah Chafee, Jr., The Music Goes Round and Round: Equitable Servitudes and Chattels, 69 HARV. L. REV. 1250 (1956).

108 Hansmann & Santilli, supra note 106, 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 the skepticism toward servitudes in personal property); But see supra note 107.
notice problem or information cost problem. Second, by fragmenting the ownership in the item, servitudes discourage future changes in it. This can lead to a tragedy of the anticommons problem because future changes will require the consent of several right-holders and not just one. Molly Shaffer Van Houweling called this “the problem of the future.”

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, registration provides considerable benefits 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 it could substantially reduce the transaction costs in verifying the legal rights. In addition, transactions in the copyright of a work are not common and thus the social costs of the servitudes are limited.

Notice might be a bigger 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. However, creators in this industry usually create

109 See, e.g., Shaffer Van Houweling, supra note 108, at 893.

110 This phenomenon occurs once an economic activity requires the consent of many property right holders. Then, transaction costs rises, holdouts occurs, and an underuse of the resource can be expected. See generally Heller, supra note 14. The tragedy of the anticommons in the context of termination of transfers will be explored in detailed in Section V.B. of this Article.


112 Shaffer Van Houweling, supra note 108, at 900.


114 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 rights granted by the Convention “shall not be subject to any formality.” Berne Convention for the Protection of Literary and Artistic Works, Article 5, 828 U.N.T.S. 221 (Sept. 9, 1886, revised in 1908, 1928, 1948, 1967, 1971). However, rights that are not granted by the Convention can be subject to formalities. This is why some rights, such as the right for statutory damages, require prior registration. 17 U.S.C. § 412 (2006). Termination rights of course are not granted by the Berne Convention and thus can be subject to formalities, including registration.

115 Shaffer Van Houweling, supra note 108.

116 See supra note 90.
very few copies, typically one, of each work and therefore establishing an effective notice system for those unique pieces of art might not be very expensive.\textsuperscript{117} Modern digital technology can further reduce those costs.

If the law makes profit sharing mandatory and inalienable the buyer does not need to spend resources in exploring whether such an arrangement is in place. The buyer knows that profit sharing is required and can evaluate the item she purchases accordingly. On the other hand, registration of the rights will probably still be helpful in order to reduce the cost in locating the author with whom the profits are to be shared. In addition, the cost of information (in verifying the rights of the author) under an inalienable profit sharing regime is cheap also because the profit sharing arrangement is standardized by the statute. Therefore the buyer does not need to explore the exact nature of an idiosyncratic arrangement created by the parties.\textsuperscript{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. The law can also limit such servitudes by the value of the underlying work and thus eliminate the information cost of the servitudes in common low value transactions.\textsuperscript{119}

The problem of the future exists when servitudes are attached to the intellectual property right or the items in which a work is embodied. If the need arises to put the work into a new use for which the profit sharing scheme is not efficient, the consent of both the owner and the servitude holder will need to be secured. However, limiting the servitude holder to just the author and her successors might significantly mitigate this problem. The problem of the future is of course even worse under an inalienable profit sharing regime. Indeed, the solution to a difficulty in contracting (caused by the tragedy of the anticommons) is not to legally prohibiting

\textsuperscript{117} See Hansmann & Santilli, supra note 86, at 266 (discussing the need to have a recording system for fine art).


\textsuperscript{119} This limitation can be implemented in many ways. For example, the law can dictate that a servitude will require profit sharing only for future sale of over a certain amount (similarly, as mentioned, in Civil Law countries droit de suite typically apply only above a certain threshold, see article 3, The EU Directive, supra note 65) 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 generally Shaffer Van Houweling, supra note 108, at 914-15 (discussion the significant of keeping transaction cost low compared to the total cost of an item); Guy A. Rub, The Economics of Kirtsaeng v. John Wiley & Sons: The Efficiency of a Balanced Approach to the First Sale Doctrine, 81 FORDHAM L. REV. RES GESTA, 41, 52 (2013) (discussing the different effects of information costs in cheap and expensive products with respect to rights that run with the product).
contracting at all.\footnote{In other situations inalienability can help overcome difficulties in future negotiation. \textit{See generally} Lee Anne Fennell, \textit{Adjusting Alienability}, 122 HARV. L. REV. 1403 (2009). However, as further explained in Part V, inalienable termination rights themselves create fragmentation in the copyright in the work. In comparison, a system of voluntary servitudes allows the parties to overcome such fragmentation.}

The conclusion is that it is unclear whether property law should allow the creation of servitudes that guarantee that the author’s right for 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.\footnote{In fact, it is possible that even under current law, property rights that strengthen profit sharing schemes can be created by perfecting security interests in the copyright and/or the items in which it is embodied. Security interest in copyright can be secured by either registration pursuant to 17 U.S.C. §205 (2006) and/or Article 9 of the U.C.C., \textit{see generally}, U.C.C. § 9-906 (1977). The form of perfection has been subject to conflicting court opinions, \textit{see} Alicia Griffin Mills, \textit{Perfecting Security Interests in IP: Avoiding the Traps}, 125 BANKING L.J. 746 (2008). Security interest in the tangible items in which the work is embodied might be perfected pursuant to article 9 of the U.C.C.} 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.

\textbf{PART III: THE UNCONVINCING TRADITIONAL JUSTIFICATIONS FOR TERMINATION RIGHTS}

The previous Part showed that profit sharing arrangements are common in the copyright industries and in many cases desirable. It was suggested that default rules that provide broad rights to creators might be justified and possibly a property regime that makes the profit sharing regime a right in rem (against the world). 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 main arguments have been raised to justify these mechanisms: first, authors, as sellers, are less sophisticated and are in poor bargaining positions compared to the buyers. Second, the future value of a specific copyrighted work is uncertain. The Supreme Court, for example, has 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.”122 Barbara Ringer, the Copyright Registrar, 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 or conjectural and the author (regardless of his business ability) is necessarily in a poor bargaining position.”123 However, those explanations, which will be explored in this Part, do not provide, by themselves, a good justification for inalienability. This Part also finds unsatisfactory another justification for inalienability, sometime raised in the context of droit de suite: the need of one buyer to control the arrangement between other buyers and the artist.

A. Creators as Non-Sophisticated Weak Parties: The Starving Artist Myth

The first argument—focusing on the lack of sophistication of the creator—is not convincing for two reasons: first, inalienability is rarely the solution to a lack of sophistication and second, the notion of the weak starving artist is more of a myth than a real problem that justifies such an extreme solution.

The typical cure for a weak bargaining position is improving the bargaining process, especially by providing better information to the less informed party, and not by denying that party the power to freely contract. Henry Hansmann and Marina Santilli put it 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.”124 Indeed, in most cases the law does not prevent a seller from selling her property, even very valuable property, to a more sophisticated buyer.125

123 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) (internal citation omitted) (authored by Barbara A. Ringer). See also Loren, supra note 32, at 1342-46.
124 Hansmann & Santilli, supra note 106. Trebilcock made a similar argument when analyzing an agreement between an author and a record company. J. Trebilcock, The Doctrine of Inequality of Bargaining Power: Post-Benthamite Economics in the House of Lords, 26 U. TORONTO L. J. 359 (1976). But see Ben-Shahar & Schneider, supra note 104 (arguing the in many cases providing better information to an unsophisticated party is complex and it typically fails to improve that party’s decision making process); see also supra note 104.
125 An official comment to Section 2-302 of the Uniformed Commercial Code, which deals with unconscionable contracts or clauses, made this point perfectly clear: “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.”
It is also doubtful that creators are indeed so feeble as to justify such a powerful paternalistic mechanism. Indeed, termination of transfer, like droit de suite, and the discussions that surround these mechanisms seem to be rooted in a romantic notion of the artist and his weaknesses. 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”. Monroe Price called it “the theology of droit de suite,” and he cynically described it:

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... droit de suite is La bohème and Lust for Life reduced to statutory form.

The Supreme Court was no less critical when it considered whether the right of an author in the renewal period should be assignable:

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

---

U.C.C. § 2-302, comment 1 (1977). See also supra note 104. In contrast, the law typically prohibits transactions in items that are associated with the seller’s personhood, such as her body parts or her sexual services. See generally, Margaret Jane Radin, Market-Inalienability, 100 HARV. L. REV. 1849 (1987). However, in the United States, the scope of copyright doctrines is typically not determined by considering the author’s work as part of her personhood. See generally supra note 20.

126 Merryman, supra note 62, at 107-08.

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.\textsuperscript{128}

This romantic notion is nevertheless prevalent, and is typically promoted by a story of the suffering of a famous artist. When droit de suite was enacted in France the story of the hungry wanderings of Jean-François Millet’s grand-daughter while a painting by her grandfather was sold for a million francs, more than 1,000 times the amount he originally paid, received much media attention.\textsuperscript{129} In the United 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:

\begin{quote}
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 the 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.\textsuperscript{130}
\end{quote}

This story, while commonly cited, is not only anecdotal but it is also historically incomplete and misleading. What Congressman Currier failed to mention is that for most of his life Twain was not a starving unappreciated artist who needed to support a tubercular wife while the massive profits from his creations were earned by greedy publishers. Mark Twain was very much appreciated during his lifetime and he has made considerable sums in royalties on his books.\textsuperscript{131} He did not need to worry much about his wife’s wellbeing as she came from a very wealthy family. Twain did lose

\textsuperscript{128} Fred Fisher Music, 318 U.S. at 656.

\textsuperscript{129} Price, \textit{supra} note 127, at 1334-35; see also Michael B. Reddy, \textit{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, ‘100,000 francs, gone!’”, while two children in rags sitting in the front row shouted, ‘Look, one of Papa's paintings!'”).

\textsuperscript{130} \textit{Hearings before the Committees on Patents of the Senate and House of Representatives 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 in \textit{Fred Fisher Music}, 318 U.S. at 653; see also Bently & Ginsburg, \textit{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).

\textsuperscript{131} GEOFFREY C. WARD & DAYTON DUNCAN, MARC TWAIN 124 (2001).
considerable amounts of money but not by selling his creations for pennies to a greedy publisher. Twain lost them 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 go into the publishing businesses.\footnote{Id, at 140-41, 156-57.}

As the Supreme Court implicitly noticed,\footnote{Fred Fisher Music, 318 U.S. at 653-54.} the story of Mark Twain actually shows that even under the default rules regime, pursuant to the Copyright Act of 1909, authors were able to protect their interests and enter a deal with a publisher without selling their right in the renewal period.

While the story of Mark Twain might just be a bad example, stories like it convinced legislators to pass laws that are designed to protect creators by giving them inalienable rights. Those laws were passed without conducting an in-depth economic analysis and with too much emphasis on the romantic notion of the starving artist. Those sporadic examples are well known and are therefore likely to cause the impression that the phenomenon they are describing is much more common than it actually is.\footnote{Behavioral economics calls this phenomenon the availability bias. For a discussion of this bias and its effect on lawmakers see, e.g., Christine Jolls, Cass R. Sunstein & Richard Thaler, A Behavioral Approach to Law and Economics, 50 STAN. L. REV. 1471, 1518-19 (1998); Ben-Shahar & Schneider, supra note 104, at 480 (“Trouble 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.”).} However, as a few commentators suggested,\footnote{E.g., Price, supra note 127; Trebilcock, supra note 124.} it is doubtful that such a description is accurate.\footnote{Randall K. Filer, The ‘Starving Artist’ – Myth or Reality? Earnings of Artists in the United States. 94 J. POL. ECON.56 (1986); Richard E. Caves, Creative Industries: Contracts Between Art and Commerce 78-81 (2000) } Most artists do not seem to starve. Moreover, the transactions in which they sell or license their rights are not entered in a hurry or under massive pressure and they are typically signed after real consideration, in many cases after consulting with an agent and/or a lawyer who are repeat players.\footnote{See supra note 104. The need to protect weak transactors from aggressive tactics might justify a right, even an inalienable right, for a “cooling-off” period, during which the weak party is allowed to cancel the deal. See generally 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 & Contemporary Problems 63, 66 (2011). However, in a typical deal between an author and a buyer such tactics are not common as the parties usually do not lack information or time to consider the transaction and its value. Moreover, if the problem would have been just harsh tactics, a short cooling-off period would have sufficed.}

In addition many creators are members of a powerful professional association that also protects their interests. Moreover, even if
many artists were indeed starving, the profit sharing mechanisms, which would grant just the most successful of them considerable sums after many years, seems like a poor solution to this problem.\footnote{Merryman, supra note 62, at 117 (“The droit de suite is not designed. . . to come to the aid of needy artists. . . if success strikes, the income from resale proceeds will be trivial in comparison with that from first sales . . . Even if, as the folklore has it, there were injustice to artists in the art market, the droit de suite would seem unlikely to correct it.”). Merryman also wonders how the law cannot trust the artist to effectively negotiate her resale rights but trust her to set the initial sale price of the work, which is significantly more crucial to her financial wellbeing. Id., at 123. Some of those considerations will be further explored in Part IV of this Article, and in particular in Subsection IV.b.2.} In fact, other legal mechanisms, including the doctrine of duress under contract law,\footnote{See generally Melvin Aaron Eisenberg, The Bargain Principle and Its Limits, 95 HARV. L. REV. 741 (1982)} might provide a much better protection in that extreme case.\footnote{The Supreme Court had also suggested that allowing the author to assign her rights does not mean that any assignment should be enforced if made “under oppressive circumstances.” The Court suggested, in dictum, that “courts should not make themselves instruments of injustice by lending their aid to the enforcement of an agreement where the author was under such coercion of circumstances that enforcement would be unconscionable.” Fred Fisher Music, 318 U.S. at 656-57.} Indeed, the romantic myth of the starving artist is a weak justification for the strong paternalism of the termination of transfer mechanisms. Part IV of this work provides a more nuanced and careful analysis of the artist’s position in the marketplace.

\section*{B. The Uncertain Future Value of Copyrighted Works}

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

\begin{quote}
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.\footnote{Loren, supra note 32, at 1329.}
\end{quote}

This justification, in itself, is weak. While it is true that prior to commercial exploitation the value of the work is difficult to evaluate,\footnote{See generally Caves, supra note 136, at 2-3.} 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. The risk can be placed, in whole or in part, on the author or the buyers—typically an intermediary (e.g., a publisher or a record company). As further analyzed below, the termination mechanisms place some of the risk—the risk of whether the work will be commercially profitable in 35 years or not—on the author and prevent her from transferring this risk to the publisher.

Typically, it is socially efficient to transfer risk to parties that can better handle that risk. The parties themselves typically know which of them can better handle risk and thus mandatory rules that prevent risk assignment are not common. 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 risk it is facing is considerably smaller than the risk of any single artist. For that reason some commentators have suggested that droit de suite rights are inefficient as preventing the transfer of risk (in that case, some of the risk of future profitable resale) to the party that can best handle it.

C. Collective Action Problem Among Buyers

While termination rights are typically justified by the artist’s weakness or by the uncertainty regarding the value of the work, the literature on droit de suite provided an additional justification that might be applicable to termination rights as well.

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

---

143 See infra Section IV.B.
144 As mentioned, Section 203 (as well as Section 304(c)-(d)) prevents the author from selling her post-termination rights. This also means that the author cannot buy insurance to deal with this risk.
146 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. This justification is not applicable to termination rights.
147 See, e.g., Landes & Posner, *supra* note 11, at 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”); Hansmann & Santilli, *supra* note 86, at 262.
149 In technical terms this means that the cross elasticity of demand between the two
If this is the case, when the buyer of the work (either of the physical object in which it is embodied or the copyright in the work) evaluates it, she takes into account all the relevant externalities to date. The buyer is however unable to evaluate what future actions of the creator, including her future work, will affect the value of the work the buyer is now purchasing. The creator, as a seller, will want to guarantee to the buyer that the creator’s future actions will likely increase the value of the good sold, e.g., by creating successful new works. Having an inalienable profit sharing scheme—either by a termination of transfer rule or because of the droit de suite doctrine—is a way for the buyer to increase the likelihood that it will be in the creator’s best interest to improve her reputation and produce successful work in the long term.

While this is a valuable argument, for several reasons I do not believe that it is a significant one. First, in most cases the creator will have a strong incentive to improve her reputation as she receives significant benefits from such reputation. The most obvious benefit is a higher demand for works she will sell in the future. Other possible benefits such as respect in her community are non-transferable by nature and positively correlate with good reputation. Second, the buyer can incentivize the creator to improve her reputation by entering into a contractual profit sharing scheme with the creator. It is true that without an inalienable profit sharing mechanism the buyer cannot be sure that the seller will have a monetary interest in the success of her works sold to other buyers. However, it is likely that other buyers will similarly care about the creator’s reputation and therefore, in most cases, if a profit sharing scheme is in a buyer’s best interest it will likely be in the best interest of other buyers. The same is true for the author. Moreover, once the author’s entered into a profit sharing agreement that will incentivize her to internalize the effect of her future actions on her old work, she will likely require such an arrangement from future buyers. The author’s reputation is now a public good to the

works is positive, or that the works are complementary goods.

150 Hansmann & Santilli, who have suggested that the collective action problem might support inalienability, eventually also concluded that a resale royalty right (droit de suite) should be voluntary. See Hansmann & Santilli, supra note 86, at 278-79.

151 Merryman gives a wonderful example how a sale of one of Robert Rauschenberg’s early works for a consideration amount, for which Rauschenberg, much to his frustration, was not directly compensated, caused a sharp increase in the price of Rauschenberg’s other old works, many of them still in his possession as well as his new work and made Rauschenberg a millionaire. Merryman, supra note 62, at 111. Similarly, the creators of Superman earned considerable amounts, as employees of DC Comics, once their work became commercially successful. See supra note 43. See also infra Subsection IV.b.2.

152 See supra Section II.A., where similar arrangements were explored.
buyers and the author will therefore want all buyers to appreciate it by demanding a profit sharing arrangements.

**PART IV: THE EX-ANTE EFFECT OF INALIENABLE PROFIT SHARING SCHEMES: TERMINATION OF RIGHTS AND INCENTIVES TO CREATE**

It was shown that the myth of the starving artist, which publically justified the enactment of the termination of transfer rules and similar mechanisms in foreign jurisdiction, is false. However, it is possible that this myth was just a straw-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 will provide an in-depth analysis of the economic effects of termination of transfer and similar inalienable profit sharing arrangements. This Part IV explores the ex-ante effects of the inalienable right to terminate a transfer. This analysis will focus on the ways in which this legal mechanism can affect the income of the authors and the incentives to create.\(^{153}\) While the focus of this part will be on the termination of transfer mechanism pursuant to the U.S. Copyright Act, the analysis will also be applied to droit de suite and employees’ compensation rights, 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 which assumes that the creator and the buyer are 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 be later relaxed.

The structure of many transactions in the copyright industries including in the book publishing industry and in the recording industry is quite simple. The publisher considers many creators and eventually chooses who

\(^{153}\) 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 ex-post rights with respect to externalities affect the investment decisions ex-ante). In fact one of the main benefits of property rights in general and the main justification for intellectual property rights relies of this need to create ex-post allocation which will efficiently incentivize ex-ante investment. See generally W. Landes & R. Posner, The Economic Structure of Intellectual Property Law 13-14 (2003) (discussing the dynamic benefits of property rights).
it would like to sign. The agreement, once reached, is typically for a long term and covers several works, although, at least in the recording industry, the company is given an option to terminate it at certain times during that term. The agreement will typically include an assignment of the author’s copyright to the publisher (or a permanent license, typically an exclusive one). Uncertainty is high. Although the buyer spends resources trying to choose successful authors to sign, most authors who successfully go through this elimination process will fail commercially. It is very difficult for the author or the buyer to know, when the initial agreement is signed, if she will turn out to be an unusual commercial success. For simplicity I will assume that the parties do know what the likelihood of major commercial success is. Major commercial success in this context—stardom—will be defined as having considerable income from old works at the time of termination. Let’s mark this probability of superstardom as $p$.

In competitive markets among buyers, each buyer’s willingness to pay is equal to the expected benefits that such a buyer expects to have 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.

The sellers in this market, the authors, vary in their willingness to accept. Some of them will be willing to accept low amounts but others who will face higher costs, especially opportunity costs, will have a higher willingness to accept.

Mandatory termination rights mechanisms will affect the prices in this market. The buyer must assume that the stream of revenues it will get

---

154 See generally Caves, supra note 136, at 52-72 (discussing the publisher role as a gatekeeper).
155 Passman, supra note 85, at 104-107.
156 See, e.g., Menell & Nimmer, supra note 59, at 802.
157 See, e.g., Caves, supra note 136, at 61 ("roughly 80 percent of albums and 85 percent of single records released fail to cover their costs").
158 See, e.g., Caves, supra note 136, at 2-3.
159 As will be explained in Section E below, because Section 203 allows termination only after 35 years very few artist will be considered successful under this definition.
160 As suggested in Part II 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 all cases, the publisher will need to base every payment the author receives before the value of the work is determined, including the advantages, on the expected income from an average author.
161 While most assume that denying the buyer a share of future profits will cause a price decrease in the initial sale, e.g., Randall K. Filer, A Theoretical Analysis of the
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. Denying it from the buyer lowers its average income per signed author and, because the contract price is equal to the expected (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 \( T \). 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. This group of superstars will therefore terminate their transfer. 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 is a monopolist who sells one 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 did not change the creator’s expected income. It initially reduced it by \( pT \), but it also gave the performer a chance—equal to \( p \)—to get an additional \( T \) of income in the future (all in present day value).

---

\(^{162}\) While only superstars can expect to have significant commercial success after decades they vary in the magnitude of that success. 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).
B. Competitive Markets With Marginally Diminishing Utility of Wealth and Risk Aversion

One important factor that was not considered in Section A is the decrease in the marginal utility of wealth. This factor, which will be considered in this Section, is important and will have a significant effect on the desirability of termination rights.

A decrease in the 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 10% 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.”163 This subsection will demonstrate that once this effect is taken into account, termination of transfer is ex-ante inefficient in competitive markets because it decreases the total social utility by misallocating both risk and wealth.

1. Termination Rights and Allocation of Risk

Individuals typically do not make decisions—in this case the decision of whether to create—based on expected value. If individuals are not risk neutral they base their decision on the certainty equivalent164 of the possible outcomes. If individuals are risk averse their certainty equivalent will be lower than the expected outcome of a risky situation.

Termination of transfer allocates risk to the author. Instead of getting a fixed amount as compensation, the fixed payment is reduced by pT in return for having a chance to participate 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 of their compensation.

Unfortunately, because a young artist’s work is a considerable asset to her, then as a result of the decrease marginal utility of wealth, she is practically certain to be risk averse with respect to it.165

---

163 DAVID D. FRIEDMAN, LAW’S ORDER: WHAT ECONOMICS HAS TO DO WITH LAW AND WHY IT MATTERS 63(2000).
164 Certainty equivalent is a guaranteed return that one would accept rather than taking a chance of an uncertain return,
165 See Hansmann & Santilli, supra note 86, 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 decrease in 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
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, with practical certainty, 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.

2. Termination Rights and Reallocation of Wealth

A related downside with termination rights has to do with the reallocation of wealth over time and among creators. While, as explored in Section A, as a whole, 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. Without it, under this model, all artists will receive the same compensation, and with it, everybody will initially receive less but superstars will eventually, after termination, receive more. Therefore, this rule transfers wealth from young artists to older superstars.

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 A) could increase the utility of young artists, who are typically poor, more than the utility of older superstars, who are typically wealthy. Therefore, artist would probably prefer not to transfer income from their young poor self to their old wealthy self. Indeed, this

163, at 63-65.

Psychological research in recent decades shed light on the complex preferences of authors. For example, Sprigman, Buccafusco, and Burns found out that authors place considerable weight on the right of attribution. Christopher Jon Sprigman, Christopher J. Buccafusco, & Zachary C. Burns, What’s a Name Worth?: Experimental Tests of the Value of Attribution in Intellectual Property, B.U. L. REV. (Forthcoming, 2013). Marvin Zuckerman explored the ways in which artists (and others) try to satisfy their Sensation seeking. MARVIN ZUCKERMAN, SENSATION SEEKING: BEYOND THE OPTIMAL LEVEL OF AROUSAL (1979). Nevertheless, I do not believe that these studies suggest that when it comes to pure major financial decisions the typical artist, unlike most other individuals, prefers a risky financial situation over a certain one.

166 The problem of misallocation of risk and misallocation of wealth are related (and in some respect they are two effects of the same phenomenon) because they both result from the decrease in marginal utility of wealth. This decrease causes most individuals to be risk averse with respect to major assets and to prefer to earn an extra dollar when they are poor than when are wealthy. See generally Friedman, id., id.

167 Hansmann & Santilli, supra note 86, at 262. See also Subsection VI.B. 2. It should be noted that many legal rules are designated to incentivize individuals to save money when they are young to be used when they are older. These rules help those individuals
misallocation of wealth from the poor to the rich might not just be unfair, but it is 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. 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 a certain chance to receive a considerable amount in a few years, when (and if) they are already very successful. This simply cannot, in itself, increase their expected revenues or their incentive to create.

Therefore, by reallocating wealth from young authors to older superstars and by reallocating risk from buyers to sellers, the termination rights mechanisms, while keeping the total wealth of the 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.

overcome their bounded willpower problem. See, e.g., RICHARD H. THALER & CASS R. SUNSTEIN, NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH AND HAPPINESS 103-17 (2000). However, this seems like a very weak justification to the termination mechanism, partly because the beneficiaries from this mechanism are typically very few, very successful, and very rich superstars.

Exploring in depth the reallocation of wealth from distributive justice perspective is beyond the scope of this work.

See, e.g., Hansmann & Santilli, supra note 86, at 265.

Artist might however misperceive their chances of success. See infra Section G.

It is well known that during the legislative process of the Copyright Act of 1976 various artists’ groups (e.g., the authors’ guild) strongly supported the enactment of termination rights. Can one infer from this support that notwithstanding the analysis is this Part, termination rights are valuable to artists? I believe that the answer is negative. The difficult question this Part tackles is how to compare the various effects of termination rights and in particular the expected decrease in the initial compensation of artists with 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 the artists’ groups, in which established artists were heavily represented, supported the enactment of termination rights.
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.

When a buyer has market power—when competition is limited—it faces an upward sloping supply curve. The buyer knows that paying a lower price will decrease the supply of available works. As the compensation to creators decreases, more of them will switch to pursue other opportunities. The buyer will set a price that will maximize her revenues.\(^{172}\) This price will be lower than the average revenues per artist and therefore a deadweight loss will be created. Deadweight loss is a form of an economic waste that results from prices in non-competitive markets that do not match the marginal costs and benefits.

In an oligopsony, some sellers 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 from the transactions between the buyer, typically a publisher or record company, and users of the work if it would have been created, as well as the positive externality (spillover) that copyrighted work typically creates.\(^{173}\)

The following graph illustrates this argument:

\(^{172}\) 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 purpose of this Article the exact ways in which the prices in the oligopsony are determined are immaterial, although it is assumed that they 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, and in the monopolistic interactions with the buyers of the work, what price to charge them. Because I assume that the price in the first market is fixed, it does not affect the price in the second market.

In this graph, A is the expected net revenue for an author but B is the price that a buyer will pay in this non-competitive market. 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:

---

174 B is typically assumed to be a fraction of A. $B = \alpha A$. The graph presents a case of a linear supply curve, which means that $\alpha = 0.5$. 
Mandatory termination rights reduce the expected net revenue per author by pT. In the graph, A represents the expected benefits 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.175

However, when termination is exercised, the shoe is on the other foot. Now the artist is a monopolist (of her work). The few buyers will compete with one another and the artist is likely to be able to keep most of the post-termination revenue stream (practically all of T).176 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 to receive an amount close to T. Therefore, the total compensation, denoted by E in the graph, is expected to be higher than B.177

In other words, inalienable termination rights increased the total expected compensation of the author. There is an intuitive explanation to 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 facing an oligopsonist, she sells a part of her asset (the expected pre-termination revenue stream) in that market but another part (the post-termination revenue stream) later, as an established artist and a monopolist. Therefore, the author can extract a bigger share of the revenue stream of 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 MNK, but the deadweight loss with termination is a smaller triangle UWK. This means that some artists, who are willing to accept more than B but less that E, will not produce the work without termination rights but will produce it with it. Their surplus is represented by NMVW. Society will also benefit from the surplus in the interactions that will occur between the

175 In other words B-D < pT. The reason for this is that the author’s compensation is proportional to the expected revenues of the buyer. B = αA and D = αC. Therefore B-D = αA-αC=αA-α(A-pT)= αpT<pT. For example, if the supply curve is linear, as presented in the graphs, a monopsonistic buyer will pay a price that is half her expected revenues. If the expected revenues are decreased by pT, the author’s compensation will decrease by pT/2.

176 It should be noted that the Copyright Act allows the author to enter agreements with respect to the post-termination right 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) (2006); Bourne Co. v. MPL Communications, Inc., 675 F.Supp 859 (SDNY 1987).

177 If B-D < pT, then E=D+pT > B.
buyer and the users who will buy this product from it.  

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

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

Indeed, Section C suggests that in a non-competitive market the expected total wealth of the author increases. However, because authors maximize utility and not just wealth, and because authors are probably risk averse and prefer to earn more when they are poor than when they are wealthy, it is inaccurate to consider their expected wealth (denoted E above) as the sole measurement of their benefits. Because 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 will be received under a regime in which inalienable termination rights are not available.

Indeed, on the one hand, termination of transfer increases the artist’s expected revenue by allowing her to sell part of her assets as a monopolist, but on the other hand, it reduces her utility by forcing her, a risk-averse individual, to bear more risk and by transferring wealth from poor to rich artists.

E. Sooner Vesting of 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, termination should be available sooner than it currently does.

When termination is available only a few decades after the work is created, as is the case under current law, the value of the post-termination stream of revenue (denoted T) becomes exceptionally small. This is because of the decrease in the demand for copyrighted works over time and the need to bring this stream of revenue to present value (at the time of negotiation).

There is no doubt that the demand for practically all works decreases

---

178 See supra note 173 and the accompanying text.
179 See supra note 34 and the accompanying text.
over time. In one study, 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 4% for musical work and 9% for books.\textsuperscript{180} Using these figures, a musical work is expected to generate about 72% of its total revenues within the first 30 years after publication and books about 94%. It is possible that the demand for very successful work, which typically is the subject of termination rights, decreases slower than the demand for less successful work. Classics are classics.\textsuperscript{181} Nevertheless, with extremely rare exceptions, the demand for even a very successful work is substantially lower 30 years after publication.

In addition, the post-termination stream of revenues must be brought to present values at the time of negotiation. Even if a very low annual discount rate of 3% is used, only 41% of the revenues in the 30\textsuperscript{th} year will remain when brought to present day values. Using 7%\textsuperscript{182} leaves only 13% of the income in the 30\textsuperscript{th} year.

Considering both factors shows the small value of the post-termination stream of revenues under Section 203.\textsuperscript{183} If termination is exercised 35 years after publication then using 3% as a discount rate, only 8% of the total value of an average music work and little more than 1% of the value of an average book will be in the post-termination revenue stream.

Therefore, because the post-termination revenue stream is small, then the reduction in the deadweight loss is also proportionally small. Indeed, currently, the impact of termination rights on incentives is not significant

\textsuperscript{180}William M. Landes & Richard A. Posner, \textit{Indefinitely Renewable Copyright}, 70 U. CHI. L. REV. 471, 506 (2003). A full discussion on the methodology used by Landes and Posner is outside the scope of this Article. The exact annual decrease in demand for copyrighted work is not material to the point made in this Section of the Article.

\textsuperscript{181}There is sporadic anecdotal evidence the supports this claim. The music of Elvis Presley, recorded in the 1950s, 60s and 70s, the Beatles, recorded in the 1960s, or that of Jimi Hendrix, who died in 1967, and the books of Theodor Geisel (Dr. Seuss), whose most famous work was created in the 1950s, still produce considerable sums annually. See \textit{Top Earning Dead Celebrities}, FORBES.COM, http://www.forbes.com/special-report/2012/1024_dead-celebrities.html/ (last visited Feb. 12, 2013). See also \textit{Old Albums Pass New in Sales}, SEATTLE WEEKLY. (Jul. 11, 2012), http://www.seattleweekly.com/2012-07-11/music/greatests-hit/.


\textsuperscript{183}Of course, the value of the post-termination revenue stream under Section 304 is much smaller because there are available more than 50 years after publication.
enough. Making the termination available earlier will increase those benefits and will give this mechanism more teeth. Thus, for example, if termination is exercised 10 years after publication then using 3% as a discount rate, 46% of the total value of an average music work and 26% of the value of an average book will be in the post-termination revenue stream (instead of, as suggested above, 8% and 1% respectively, under the current regime).

In addition, earlier termination will significantly mitigate (but not eliminate) the problem of misallocation of risk and wealth. Termination will then be available to more creators (those whose work is commercially valuable after the shorter vesting period, this means that $p$ will increase) and therefore the risk associated with termination rights (the risk of not-having valuable post-termination revenue stream) will be lower. Moreover, with shorter vesting period wealth will be transferred from young, and typically poor creators, to slightly older and probably moderately wealthy successful artists instead, as is the case now, to very wealthy old superstars. Therefore, the loss of total utility as a result of misallocation of risk and wealth will decrease with the vesting period.

The main downside to making termination available soon, at least from an ex-ante perspective, is that if the fixed costs of producing and distributing a work (e.g., a book or a record) are significant, the publisher or record company might not be able to recoup them. In most modern markets, unless termination becomes available very shortly after publication, this seems highly unlikely.

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

The model developed in the previous sections analyzes the ex-ante effects of termination of transfer. 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 are 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.

184 The 35 years period which is currently used in Section 203 was heavily negotiated before the enactment of the 1976 Copyright Act. See STAFF OF H. COMM. ON THE JUDICIARY, 89TH CONG., COPYRIGHT LAW REVISION, PART 6, SUPPLEMENTARY REPORT OF THE REGISTER OF COPYRIGHTS ON THE GENERAL REVISION OF THE U.S. COPYRIGHT LAW: 1965 REVISION BILL 71-76 (Comm. Print 1965); Litman, supra note 33, at 891-93.

185 Using the terminology of the model presented in Section C, this means that $C$, the expected pre-termination net revenue per signed artist (not considering the artist’s compensation) is negative.
Nevertheless, from the buyer’s perspective both are just reductions in 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 employer’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 not determined by a market transaction.186 This, for purposes of the model presented in this part, is practically irrelevant. The additional compensation to the creator is equivalent to the post-termination stream of revenues under a termination of transfer rule (denoted T) and is given in full to the creator upon a certain future event.

Therefore, the analysis is very similar. If, and only if, the level of competition among buyers is low then creators can benefit from a mandatory profit sharing mechanism, but those benefits must be compared to the misallocation of risk and wealth caused by those rules.

G. Termination Rights and Irrationality

The model developed in this Part of the Article implicitly assumed 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 literature187 suggests that individuals do not always act rationally in their decision making process. 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 in this Subsection I would offer several ways in which it can affect the desirability of termination rights, as explored by this model.

Behavioral law & economics literature explores several phenomena that

---

186 Section V.C of this Article discusses in length this ex-ante difference between droit de suite and employees’ compensation rights on one hand and termination of transfer on another hand.

might affect the desirability of the termination mechanisms. For example, the availability bias suggests that salient events seem more likely than non-salient events. 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) some might value the likelihood of stardom more than it actually is. If an artist experiences this bias she might attribute too much value for her post-termination rights and might agree to accept too little for her pre-termination rights or decide to create when it is inefficient to do so.

Bounded willpower, another phenomenon explored by behavioral economics, a form a myopia, causes people to attribute too much value to short-term gains over long-term ones. Many people, for example, save too little for their retirement, which might require 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.

The most relevant irrationality bias in this context is probably the over-optimism bias. This phenomenon causes people 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. Similarly, it was explored that most creators suffer from this bias and believe that the chances of commercial failure of their work is smaller than the general probability of such a failure. If that is the case, then creators might misperceive the

---

188 See, e.g., KAHNEMAN, supra note 187, at 129-36; Jolls, Sunstein & Thaler, supra note 134, at 1518-19. The availability bias was mentioned earlier in this Article because it may actually contributed to the decision to enact the termination mechanisms in the first place. See supra note 134.

189 See supra note 157.

190 See, e.g., Jolls, Sunstein & Thaler, supra note 134, at 1479; OREN BAR-GILL, SEDUCTION BY CONTRACT: LAW, ECONOMICS, AND PSYCHOLOGY IN CONSUMER MARKETS 21-22 (2012)

191 As discussed above, see supra note 167, limited willpower is a weak justification to the inability of termination rights in their current form because the solution for artists bounded willpower, myopia, and focus on short-term profit should not be to transfer wealth primarily to superstars.

192 See, e.g., Jolls, Sunstein & Thaler, supra note 134, at 1524-25.


likelihood of stardom—denoted \( p \)—and thus would place too much weight of the post-termination revenue stream.

It is difficult to know how common these phenomena are in the 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 appear relevant to the copyright industries.

Experts, for example, appear to be partly immune to many of the biases that affect laypersons, especially when they are dealing with repeated transactions.\(^{195}\) Most of the buyers in the copyright industries, e.g., record companies’ and publishers’ executives, are probably experts. Many of the sellers (although certainly not as many of the buyers) are assisted by experts, e.g., lawyers and/or agents.\(^{196}\) In addition, the biases described above are usually attributed to System 1 in our minds, which generally controls, intuitive, automatic, fast, affective and heuristic-based decisions. Individual also use System 2 which is slow, effortful, conscious, and rule-base, and can, in some cases, override the intuitive judgment of System 1.\(^{197}\) The transactions in the copyright industries typically take time, which allow the parties to carefully consider them.\(^{198}\) This might suggest that the transactors’ System 2 is evoked during the negotiation, which might also mitigate the psychological biases described above.

Therefore, I believe that it is fair to assume that almost all buyers in the copyright industries as well as many of the sellers are primarily acting rationally. It is also fair to assume that the optimism bias is probably 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, to the extensive use of voluntary profit sharing arrangements. The sophisticate buyer knows that the value of the seller’s share in their profit sharing arrangements is small because it heavily depends on unlikely commercial success. However, the artists-buyer irrationally overvalues her share, and thus agrees to other disfavored terms (e.g., small advantages) just to get a higher share of the profits. For example, if an author willingness to accept is $10,000, the buyer, instead of paying that amount can offer the author $5,000 plus 10% 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 payment of $8,000, not considering risk aversion) irrationally believing and her work will be substantially more successful than the average similar kind

\(^{195}\) See generally KAHNEMAN, supra note 187, at 140-144, 234-44.
\(^{196}\) See supra note104.
\(^{197}\) See generally KAHNEMAN, supra note 187, at 20-24.
\(^{198}\) See generally supra note 137.
of works. In other words, irrationality might cause author to agree to accept too little upfront, 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 over-optimistic, then from a policy perspective, society needs to be concerned with their decision 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 bargaining skills, should therefore consider limiting profit-sharing arrangements and not mandating them.

PART V: THE EX-POST EFFECT OF INALIENABLE PROFIT SHARING SCHEMES:
INEFFICIENCIES IMMEDIATELY BEFORE AND AFTER TERMINATION

The discussion in Part IV implicitly assumed that the termination of transfer process itself is costless. Prior to termination the buyer (typically, the publisher) owns the rights and post-termination the author owns the rights and she can freely and easily exploit them, including by negotiating another deal with any competing intermediary. The discussion in this Part will show that this description is oversimplified.

Two main problems make the termination process more difficult and costly: first, with termination approaching, the incentives of the publisher and the creator get misaligned in a way that can cause one party to impose a negative externality on the other (or prevent him from benefitting from a positive externality). The second problem, which is probably more harmful than the first, is the difficulty in bundling rights from multiple authors for multiple works after termination. This Part explores those problems and offers two partial solutions: 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

The author and the intermediary (e.g., 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 cause an externality to the other party. For example, the publisher typically determines how much to invest in promoting the work. Such 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, e.g., by creating other successful work, by participating in promotional events, and so on. Here also, the costs of those actions, including opportunity costs, are paid by the author 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 be 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, 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 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 externalities problems contractually. 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, however, might not be a cheap process. Asking the author to contribute to any investment that might change the value of the work might be prohibitively costly in terms of transaction costs. This is typically solved by agreeing on those arrangements ex-ante. Those agreements are part of the standard contractual profit sharing arrangements that were explored in Part II.

The problem is much more difficult to solve or mitigate when the law limits the parties’ freedom of contract. Thus, regardless of any contractual arrangement, current European law 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. In the United States, the parties’ ability to come up with a contractual solution to the externalities problem

201 See The EU Directive, supra note 65, and supra note 67.
on the eve of termination is limited by the author’s possible inability to trade her post-termination rights. Therefore, a publisher, for example, 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., best-hits record) on the eve of termination, even if a later release might be more socially desirable.  

2. Rescission and Re-grant of Transfers

One method used by the author or her successors on one hand and the licensee or assignee on the other hand, to enter into a binding contract regarding the parties’ rights on the eve of termination and thereafter is to rescind the original license and re-grant it. It is however highly controversial whether those actions supersede and replace the original grant and thus prevent its termination or does the inalienable nature of termination rights preclude such a construction.

In Milne v. Slesinger, 203 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 them by a 1930 agreement that was subject to termination starting in 1986. Termination notice could have been served as early as 1976. In 1983, 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 the earlier agreement is not subject to statutory termination pursuant to Section 304(d). 204

---

202 A possible real life example is Warner Brother's 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 are vested. Chris Schrader, Legal Woes Could Divide 'Superman' Franchise in Two, SCREENRANT (2012), http://screenrant.com/superman-movie-legal-battle-siegel-shuster-schrad-117539. It is currently not clear whether the rights in Superman will be terminated (and if is so when). See Larson v. Warner Bros., No. 11-44863, D.C. No. 2:04-cv-08400-ODW-RZX (9th Cir. Jan. 10, 2013); see generally supra text accompanying notes 41 - 45.

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

204 In a recent decision a federal court in California reached a similar result and held that the statutory successors of Joe Shuster—one of the creators of Superman—cannot exercise their termination rights in 2013 because of a 1992 agreement that superseded the original 1930s agreement and re-granted DC Comics a license. DC Comics v. Pac. Pictures Corp., CV 10-3633 ODW RZX, 2012 WL 4936588 (C.D. Cal. Oct. 17, 2012). At the time of writing an appeal of this decision is pending before the Ninth Circuit. 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 Inc., 2:04-CV-08400-
In *Penguin Group (USA) Inc. v. Steinbeck*, the Second Circuit held that a termination notice with respect to the work of John Steinbeck is 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.

Although such contractual arrangements might address and substantially mitigate the end-game problem, these decisions came under harsh criticism. Peter Menell and David Nimmer, for example, have stated that those cases “have eviscerated [the] clear congressional command” as Congress’ intent was to shield “authors from the pressures of unequal bargaining power that has produced unremunerative transfer in the creative arts.” 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.” They expressed 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.”

Applying the analysis in Part IV 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 his rights for a “second bite” when she initially sells her rights. The model developed in Section IV.C shows that if buyers in this transaction have market power it can allow them to extract lower prices, which reduce the authors’ compensation and the incentives to create. *Milne* and *Steinbeck*, in sharp contrast, allowed renegotiation of the rights decades after publication. At this stage, as explained in Section IV.C, the value of the work is known and the author’s successors have the bargaining power. They have a monopoly on the rights...


206 Menell and Nimmer, supra note 58, at 802. See also Bently & Ginsburg, supra note 61, at 1584-86 (criticizing both decisions as inconsistent with the Copyright and possibly with its policy); but see Loren, supra note 30, at 1368-69 (suggesting that the Ninth Circuit was correct in Milne in holding that the 1930 was successful rescind 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. See Loren, id., at 1370-71; Menell and Nimmer, supra note 58, at 819-24.

207 Menell and Nimmer, supra note 58, at 814.

208 Id., at 815.

209 Id., at 815-16.
to use the work.

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, the Walt Disney Productions company, who produced the first Winnie-the-Pooh movie a few years earlier, was willing to pay generously to remove this threat. This analysis suggests that this 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 termination notice exists. 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 have extracted a payment that reflects their future termination rights. At this stage, authors and their successors are not subject to any “pressures of unequal bargaining power.” Unlike in the initial sale, at this stage, they have the bargaining power.

Therefore, the parties should be allowed to negotiate new arrangement prior to termination, including through rescind and re-grant. Enforcing those agreements not only mitigate the end-game problem, but it also does not eviscerate or frustrate Congress’ intent. These agreements reflect the power given to authors and their successors by the termination rights mechanisms and they therefore advances the goals that led to their enactment.

B. The Problem of Shared Work: Joint Authorship and Ownership, Complementary and Derivative Work

When exploitation of a work after termination requires the consent of multiple right-holders, those parties must reach an agreement regarding this usage. This Subsection explains the difficulties in reaching such agreements and how various doctrines in copyright law affect the scope of the problem.

1. Stand-alone work and Shared work

I define stand-alone work as a work that is owned, including post-termination, by a single entity and that can sustain its economic value independently of other works. A shared work is defined in the negative. It is

210 “The Many Adventures of Winnie-the-Pooh” was released in 1977.
211 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 one as 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, SUITE 101 (June 10, 2008), http://suite101.com/article/winnie-the-pooh-and-cheetah-girls-a55429.
a work that is not a stand-alone work.

Books, in many cases, are stand-alone works. When Mark Twain got the copyright in “The Innocents Abroad” back,\(^{212}\) a work he created himself, he had the full power to exploit the work. He could have offered every book publisher to publish the book and share the stream of income the book enjoyed post-termination only with the new publisher.

Most successful copyright works of our time are shared works. This claim is trivial when it comes to movies or software but it is also typically true for most records.\(^{213}\) Let’s examine, for example, Bruce Springsteen’s most successful album—“Born in the U.S.A.”\(^{214}\) Let’s assume that Springsteen terminates the recording agreement he made with Columbia Records in which he (likely) assigned or exclusively licensed all his rights in the album. Can Springsteen, like Mark Twain, now release the album, either by himself or with another record company, and enjoy the future income stream of this record? Probably not. Springsteen probably does not have all the rights he needs to do it.

The famous front cover of the album—a close-up picture of Springsteen’s rear in front of an American flag—was taken by Annie Leibovitz. She probably either assigned the copyright in the picture or licensed the usage to Columbia Records, and she, like Springsteen, can probably terminate this transfer. Springsteen might also not be the sole author of the recordings. Some members of Springsteen’s band, the E-Street Band, who played in the album, might argue that their creative playing, at least in some tracks, made them co-author of the recordings. Clarence Clemons, the saxophone player and possibly the most famous member of the band, other than Springsteen, passed away in 2011. His termination rights, if he had any, now belong to his fifth wife and his four children. The album also benefited from the creativity of Bob Clearmountain, a prominent mixer who worked on the album, who might be able to assert authorship.\(^{215}\) Luckily, Springsteen

---

\(^{212}\) See supra text accompanying note 130.

\(^{213}\) The digital revolution is making shared work even more common as it allows individuals to easily create joined works. Wikipedia and open source software are extreme examples of this phenomenon. See generally Molly Shaffer Van Houweling, supra note 102.

\(^{214}\) 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 is soon to be entitled to terminate the recording agreement with respect to those albums that still sell well. See generally infra note 264.

\(^{215}\) This passage 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
wrote all the tracks on the album and thus, at least in this case, there is no need to separately deal with the writers of the songs.

The problem of using shared work after termination is not limited to copyright law. The album name and maybe the names of several tracks might be trademarks, and those rights presumably belong to the record company and are not subject to termination. Finally, termination of transfer does not give the author any right in the master records. The rights in those physical objects are controlled by personal property law and not copyright law and thus the record company will continue to own them.

2. The Authors’ Veto Power and The Tragedy of the Anticommons

When the transfers pertaining to a shared work, like “Born In The U.S.A.,” are terminated, no single person, not even Bruce “The Boss” Springsteen, has the rights to publish the album post-termination, at least not in its pre-termination form.

The various parties will likely need to negotiate an agreement and they are expected to run into a market failure known as the tragedy of the anticommons. This phenomenon exists when the rights that are needed to effectively use a certain resource—in this case an album—are held by many individuals whose consent is required. In those cases, transaction costs substantially increase with the number of contracting parties, holdouts are expected, and the result is underuse of the resource in question.

It is clear, that if after the termination of transfer each author and co-author, including, e.g., the writers, performers, designers, as well as the former publisher, will have a veto power with respect to future use of the
work, the tragedy of the anticommons will emerge and will be difficult to resolve.

In addition termination with respect to some work might be staggered, which can make the problem 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 veto power in 2015 only to face another veto power, from the composer, in 2020.

Various copyright law doctrines address some, but not all, of those concerns regarding the authors’ veto power. The scope of some of these doctrines is vague and their future interpretation can have a significant effect of the magnitude of the tragedy of the anticommons problem.

In order to know the scope of the author’s veto power one must know the reason that caused the work to be shared in the first place.219 Those reasons have to do with joint authorship, the mechanisms of statutory succession, the fact that some works are complimentary and typically sold together, and the rules regarding derivative works. These reasons will be explored in order:

a. Joint authorship

Joint authorship is a complex concept in copyright law. The Copyright Act defines joint work succinctly.220 The case-law developed a high threshold for joint authorship that goes beyond the language of the Copyright Act.221 Thus, the contribution of each joint author must be original enough to be independently copyrightable222 and that all joint authors must intend to have their contribution merged into inseparable unitary whole and to be joint authors.223

---

219 The topic of veto power cuts across many doctrines in copyright law. A full analysis of all issues raised by those doctrines is well beyond the scope of this paper. This Article just sketches those issues. See generally, Shaffer Van Houweling, supra note 102.

220 “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 (2006).

221 Many commentators believe that the reason for such a high threshold is the need to prevent accidental creation of joint authorship. See 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).

222 See, e.g., Erickson v. Trinity Theatre, Inc., 13 F. 3d 1061 (7th Cir. 1994).

223 See, e.g., Thomson v. Larson, 147 F. 3d 196 (2d Cir. 1998).
Having such a high threshold, or even raising it, is desirable because it minimizes fragmentation of the copyright 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.

If the joint authors signed the assignment or license together, then only the holders of the majority of the termination interest can exercise the termination rights.\(^\text{224}\) Moreover, an agreement signed by the holders of the majority interest is binding on all termination right holders.\(^\text{225}\) Forcing the majority of joint authors to agree to termination and allowing them to bind the minority substantially mitigates the tragedy of the anticommons by increasing the chances that some of the joint-authors will be working collectively and denying the veto power from each minority group of joint authors.\(^\text{226}\) On the other hand, a recent court decision that allowed a holder of a minority interest to terminate his transfer just because he signed a separate document\(^\text{227}\) defeats the purpose of the specific arrangements regarding joint authorship\(^\text{228}\) and does not serve the public interest. It adds additional fragmentation to the post-termination copyright regime.

Once the termination is effective the joint authors hold the work as tenants in common: each joint author 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 author a powerful right but not as powerful as a veto power. Indeed, no single co-author has the power to prevent others from using the work by holding-up her consent, but each has the power to cause harm to the market power of her co-authors 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 the agreement by the majority of right-holders that will bind all right-holders.

b. Statutory succession

Another possible source of post-termination break up in the rights emerges once an author (who might be a sole author or a joint author) dies.

---


\(^{226}\) This requirement was heavily negotiated prior to the enactment of the Copyright Act of 1976. See Bently & Ginsburg, supra note 61, at 1568.

\(^{227}\) Scorpio Music S.A. v. Willis, 11CV1557 BTM RBB, 2012 WL 1598043 (S.D. Cal. May 7, 2012). This ruling allows Victor Willis, the former lead singer of the Village People, to terminate his rights, as a joint author, in many of the group’s hits.

The Copyright Act provides an elaborate list of statutory successors. For example, the Act provides that upon the death of Clarence Clemons, one half of his termination interest (assuming he was an author) passed to his spouse and the other half was divided between his four surviving children.

The status of the statutory successors is similar to that of the joint authors. The holder of a majority termination interest in the work must exercise the termination. Once termination is exercised it applies to all statutory successors. Therefore if the spouse of Clarence Clemons and one of his children decide to terminate his transfers, the spouse and all four children will be joint owners of his interest. Those owners are also tenants in common and thus, while none of them has a veto power, all of them can grant non-exclusive licenses to the work and thus, in many cases, effective exploitation of the work will require the consent of the majority of the right-holders, who can bind the minority.

c. Complimentary works

Shared works can also be created when it is beneficial to distribute a work with another separate work. From an economic perspective those works are complementary goods. In those cases, the consent of each author is required post-termination and therefore each has a veto power. Thus, as the picture on the cover of “Born in the U.S.A.” in clearly a separate work from the album, the consent of Annie Leibovitz is required to produce the album with the cover post-termination. Distinguishing complimentary works from joint authorship, while sometimes difficult, is thus very significant.

d. Derivative work

Derivative work is a work based upon one or more preexisting works, e.g., a movie script that is based on a book, or a movie sequel. Exploitation of a derivative work typically requires a license from the owner of the underlying work (or her licensee), and the owner of the derivative work (or her licensee). Thus, a public display of a Superman movie requires a license with respect to (at least) the underlying story of Siegel and Shuster, and the movie of Warner Brothers. In practice, before termination, derivative authors typically own the copyright to the underlying work or

---

230 See supra Subsection a.
232 17 U.S.C. §101 (2006). The definition is of course more complex and it raises a host of difficult legal questions that are beyond the scope of this work. Future litigation regarding termination of rights might require the courts to clarify the scope of the term.
233 There are exceptions to this rule. See infra note 244.
have an assignable license to it that allows them to license the use of the derivative work together with a license to the underlying story.

Derivative works are not only common, but they also provide an extremely powerful veto power to the underlying author. This veto power is powerful because, inter alia, it is extremely difficult to sever the underlying work from the derivative work. Indeed, in some cases an author veto power in 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 don’t have that option. 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.

As mentioned, 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.” While this language is vague, courts should read it broadly. Otherwise, the authors of the underlying work would have tremendous leverage on the derivative creator, which can result in underuse of the derivative work and a chilling effect on the 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 that case, the possible exploitation of the derivative work might be determined just by the scope of the derivative work exception. Reading the term “utilized” broadly is therefore desirable and it should include making new copies of the work even if they are slightly different from the original work. Thus, 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—as “utilizing” the derivative work—it is likely that making a new movie, and maybe even making new merchandises of Superman, will require a license from the statutory successors of Siegel and Shuster. The statutory successors of Siegel and Shuster, even if they all agree to work together,

---

234 See supra text accompanying note 53.
might also find it difficult to exploit Superman post-termination. Superman is an extreme example of multi-layered work that incorporates the creation of many creators. The original work of Siegel and Shuster, the rights in which are subject to the current termination litigations, does not include many elements of the Superman story as we know it today. In addition Siegel’s successors had already conceded that post-termination they will not own the trademarks to Superman nor the copyright to it in other countries. Thus post-termination, Siegel and Shuster statutory successors will find it difficult to produce a Superman sequel on their own.

3. 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 guarantee 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.”, the record company 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). 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. 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 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. Imagine that someone (e.g., a band member, a technician, a designer or a photographer) does not give the record company the required license prior to recording: that individual will be easily replaced by someone else.

This point of view sheds light on a real concerning element in the

---

236 For example, in the original story, Superman was unable to fly but just to 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 cannot get the copyright to them. See Siegel v. Warner Bros. Entm't Inc., 542 F. Supp. 2d 1098 (C.D. Cal. 2008).

termination of transfer mechanism: terminating the licenses and assignments destroys the main tools—these contracts—that allows the industry to concentrate the rights needed for commercial exploitation with one entity—the intermediary publisher or record company—and thus overcome the tragedy of the anticommons.

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

The previous Section of this Part of the Article suggested that modern copyright works are typically shared and thus they require difficult re-assemblance after termination of transfer. The previous Section also suggests how the Copyright Act can be interpreted to mitigate some of those problems. 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 additional usage of her work. A similar regime exists in Civil Law countries when the law mandates profit sharing arrangements.

Indeed, the termination of transfer mechanism under U.S. law, as well as droit de suite, and employees’ compensation rights in Civil Law countries create inalienable profit sharing mechanisms. However, the ways in which these systems achieve this sharing differ. U.S. law returns the rights to the authors. Droit de suite and employees’ compensation rights mechanisms do not give the author any property rights but only a right for compensation. Under droit de suite the amount of compensation is determined by the statute238 while under employees’ compensation rights it is either determined by the statute, by an administrative body, or by a court.239

Comparing these different mechanisms requires consideration of a well-known problem in the Law & Economics literature: choosing whether to protect an entitlement with a property rule or a liability rule.240 Under all regimes the creator has an entitlement for 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 nobody is allowed to take it 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 returns to the author and nobody can

238 The EU Directive, supra note 65, art. 4, See also Netanel, supra note 63, at 23-26.
239 See Ying, supra note 73, at 766-76.
240 Calabresi & Melamed, supra note 17; see also Bebchuk, supra note 153.
use it without her consent.

In contrast, if an entitlement is protected by a liability rule, others are allowed to take it without the entitlement holder’s consent subject to compensation, to be determined by law. This is the method used by droit de suite and employees’ compensation rights. For example, even when an employee’s invention turns out to be extremely valuable to the point in which the law grants the employee a right to receive a special compensation, the employee cannot exercise this right by preventing the employer from exploiting the work. Instead, the employee can only demand monetary compensation.

In their seminal work, Guido Calabresi and Douglas Melamed have suggested that the choice between those mechanisms should depend on the magnitude of the transaction costs. When transaction costs are low, property rules are typically superior as they allow the parties to reach an efficient deal. When transaction costs are high, liability rules might be preferred. Liability rules requires the law to evaluate the compensation, and while the law, and in particular courts, are typically not as informed as the parties, this imperfect mechanism might be better than relying on a property rule because, with high transaction costs, the parties will not be able to reach an efficient deal.

The analysis in Section B showed that, as most modern commercially successful works are shared work, transaction costs are expected to be high. In a tragedy of the anticommons situation, reaching a deal among parties that have veto power (which might even be staggered) might be difficult and expensive. Therefore, protecting the rights of authors of shared work with a property rule might be inefficient. 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, the author will be entitled to an additional compensation. Alternatively, the author might be allowed to terminate all transfers but she will be obliged to

\[241\] Calabresi & Melamed, supra note 17, at 1106-10.

\[242\] If the liability rule system tries to imitate the current property rule system, the right for additional compensation should be available 35 years after the grant of an agreement to exploit the work. However, the analysis in Part IV of this Article suggests that the author’s rights should be available sooner. If the rights are limited to monetary compensation they can be exercised just a few years after publication, when the value of the work becomes apparent.
grant a compulsory license, likely an exclusive one, to the original transferee upon request.

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

243 If the Copyright Act is modified to force the author to grant non-exclusive compulsory license the problem explored in Section B will be only 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 its competition and thus deny it 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 possibly cause holdouts in multi-party negotiations. Therefore, if Congress attempts to solve the problem discussed in Section B by introducing compulsory licenses, those licenses might need to be exclusive.

244 In specific circumstances the Copyright Act already grants compulsory licenses, although not exclusive ones. For example, Section 115(a) allows the making and distributing 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 which had been restored. The rationale of this Section—allowing the continued exploitation of previously created work—is similar to the rationale for forcing compulsory licenses after termination of transfers.

245 The EU Directive, supra note 65, art. 4.

246 Thus, the fees for compulsory licenses pursuant to Section 115 is determined by “copyright royalties judges,” who are Article 1 judges, 17 U.S.C. § 801 (2006), pursuant to administrative procedures prescribes by the Copyright Act, 17 U.S.C. § 803 (2006), while the fees for compulsory licenses pursuant to Section 104A are determined by a federal district court. 17 U.S.C. § 114A(d)(3)(B) (2006). See generally Peter DiCola & Matthew Sag, An Information-Gathering Approach to Copyright Policy, 34 CARDOZO L. REV 173 (2012) (discussion how different entities deal with the need of evaluating the fees for compulsory licenses).

247 The choice between the various types of liability rules protection 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 50% royalties post termination). See generally Louis Kaplow, Rules Versus Standards, 42 DUKE L.J. 557 (1992). In addition the decision maker biases, and in particular the hindsight bias, the inclination to perceive events that have already occurred ex-post as more likely ex-ante, see generally Jolls, Sunstein & Thaler, supra note 134, at 1523-24, should be considered. See Engel & Kurschilgen, supra note 161, at 696-697 (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 full analysis of the design of compensation rules is beyond
PART VI: ABOLISHING TERMINATION RIGHTS

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

A. When Are Termination Rights Desirable?

The previous Parts of this work suggest that the main justification for inalienable profit sharing rules has to do with the ability of these legal mechanisms to reduce the deadweight loss in the interaction between the creator and her buyers. The less competition among the buyers, the bigger the deadweight loss and the higher the benefits from 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 who are worse in handling it and the misallocation of wealth to wealthy superstars.

If there is a need for such an inalienable profit sharing scheme then it should be given real teeth by allowing the creator to receive her share of the profits soon. In the context of termination of transfer that means making the right vests sooner than it currently does.

In addition to the inefficient allocation of risk and wealth, termination of transfer can cause a misallocation of incentives on the eve of termination, a problem that can be mitigated by allowing the parties to contract around the termination rights. Termination right can also cause a tragedy of the anticommons and underuse of shared work, especially if the rights in the work are highly fragmented post-termination. This problem can be solved by protecting the authors’ interests with a liability rule and not a property rule.

With those factors in mind, the desirability of the termination of transfer can be examined.

the scope of this Article.
The desirability of the termination rights in various copyright industry will be explored in this Section. The analysis will show how the factors described in Part A play out in each such industry.

1. The Book Publishing Industry

The book publishing industry had a special historical function in the development of copyright law. This industry had a significant role in the emergence of copyright law, and many of its current doctrines were originally developed to deal with rights in books. The book publishing industry was dominant in the discussions that led to the enactment of the Copyright Act of 1909 and the Copyright Act of 1976.

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. Therefore, this industry probably experienced a deadweight loss problem similar to the one explored in Section IV.C. Because books are the archetype stand-alone work, the tragedy of the anticommons is typically a non-issue. Finally, because the

---

248 The first copyright statute in the Common Law world, the Statute of Anne of 1710, covered only books. See Statute of Anne, 1710, 8 Anne, c. 19. In the United States, the first federal copyright act, the Copyright Act of 1790, covered only maps, charts, and books. See Act of May 31, 1790, ch. 15, 1 Stat. 124 (repealed 1831).

249 See, e.g., Harney v. Sony Pictures Television, Inc., 11-1760, 2013 WL 68568 (1st Cir. Jan. 7, 2013) (“Courts and commentators have noted that copyright concepts developed for written works 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.”).

250 In both eras the author’s right to receive a second bite of 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, e.g. The Author’s League, took part in those discussions and in particular in the drafting of the termination of transfer provisions. Copyright Law Revision: Hearings Before Subcomm. No. 3 of the H. Comm. on the Judiciary, 89th Cong. 92-94 (1965). Sound recordings, in comparison, were not even protected by federal copyright law prior to 1972.

251 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”).
publication of books at the time involved significant fixed costs, termination of transfer could not have vested shortly after publication. Under these 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. According to one study, in 2002, for example, the nation’s largest trade book publisher\textsuperscript{252} held only an 8.12\% market share. The second largest publisher held only a 4.23\% market share.\textsuperscript{253} The U.S. census data indicates that in 2007, the four largest book publishing firms in the U.S. had only a 33.4\% market share,\textsuperscript{254} down from 40.7\% in 2002.\textsuperscript{255}

The Justice Department determines market concentration by calculating the Herfindahl–Hirschman Index.\textsuperscript{256} A market that has an HHI below 1,500 is considered non-concentrated.\textsuperscript{257} Between 1995 and 2004 the HHI for the consumer book-publishing industry was between 284 and 650, with an average of 417.\textsuperscript{258} This means that this industry was very competitive in that decade.\textsuperscript{259}

The barriers to entry to the book publishing industry were reduced in the digital era and will likely continue to decrease in the foreseeable future,\textsuperscript{260} as high quality copying becomes more accessible and the publication

\begin{itemize}
  \item \textsuperscript{252}Trade books are those published by a commercial publisher and intended for general readership.
  \item \textsuperscript{253}ALBERT N. GRECO, THE BOOK PUBLISHING INDUSTRY 65 (2d ed. 2011).
  \item \textsuperscript{256}The Herfindahl–Hirschman Index—marked HHI—is calculated by squaring the market share of each firm competing in the market and then summing the resulting numbers. UNITED STATES DEPARTMENT OF JUSTICE: HERFINDAHL-HIRSCHMAN INDEX (2012), available at http://www.justice.gov/atr/public/guidelines/hhi.html.
  \item \textsuperscript{257}UNITED STATES DEPARTMENT OF JUSTICE : HORIZONTAL MERGER GUIDELINES ch. 5.3 (2010), available at http://www.justice.gov/atr/public/guidelines/hmg-2010.html#5c.
  \item \textsuperscript{258}ALBERT N. GRECO, CLARA RODRIGUEZ & ROBERT WHARTON, THE CULTURE AND COMMERCE OF PUBLISHING IN THE 21ST CENTURY 13 (2006).
  \item \textsuperscript{259}The actual level of competition might be somewhat lower because, arguably, some companies in this industry were engaged in limited collusion. Ken Auletta, Paper Trail, NEW YORKER, June 2012, at 36-37. Nevertheless, this collusion was arguably limited to e-books policy and it is doubtful that massive long-term collusion can emerge and be sustainable in such a fragmented industry with low barriers to entry.
  \item \textsuperscript{260}See ALBERT N. GRECO, THE BOOK PUBLISHING INDUSTRY 65 (2d ed. 2011).
process is becoming cheaper. E-books, a growing segment in this industry, are especially cheap to produce. Distribution of books is also getting easier. In the past product placement in book stores presented a significant factor in the industry that helped make market concentration possible. With more and more books sold online such concentration is becoming substantially more difficult. In fact, nowadays, self-publishing is becoming easier and most people can produce a book using software that is available to the ordinary user.

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

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 possibly Bruce Springsteen, Billy Joel, Van Halen and many others, will be able to terminate their copyright transfers from the late 1970s. The rights in some of their albums are still worth millions.

Unlike the book publishing industry, the music recording industry is concentrated and had become even less competitive in recent years, especially due to mergers of several major companies. Thus, since the 2004 merger between Sony Music and BMG Music, the four big record

---


262 Id. Amazon itself holds a 27% market share of the entire book industry in the United States.

263 Amazon, for example, through its affiliated company “CreateSpace,” offers an easy to use self-publication tool. See CreateSpace, AMAZON, http://www.amazon.com/gp/seller-account/mm-summary-page.html?topic=200260520. The market share of books that were initially self-published increases in recent years. One such book, Fifty Shades of Grey, first published in 2011, became one of the most commercially success books of all times.

264 Larry Rohter, Record Industry Braces for Artists’ Battles Over Song Rights N.Y. TIMES, Aug. 15, 2011, at C1. It should be noted that termination of transfer is available 35 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 following 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. UNITED STATES COPYRIGHT OFFICE, ANALYSIS OF GAP GRANTS UNDER THE TERMINATION PROVISIONS OF TITLE 17 (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 and thus subject to the work made for hire doctrine and cannot be terminated. See Nimmer et al., supra note 52; Roher, id.
companies control close to 90% of this market,\textsuperscript{265} compared with about 70% in the 1950s\textsuperscript{266} and about 50% in the early 1970s.\textsuperscript{267} The HHI for this industry is currently high—2,208\textsuperscript{268}—and it might get as high as 2,782, which the Justice Department considered “highly concentrated,” if another proposed merger in this industry—between Universal Music Group and EMI Music—occurs.\textsuperscript{269}

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.

This, the analysis in Part IV suggests, 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 this industry. As explained in Section V.B, records are typically shared work whose distribution post-termination will require the consent of several individuals. Therefore, termination rights, which give veto power to many of those individuals, might be costly. The benefits are minimal because a vesting period of 35 years leaves too small a revenue stream to the terminating authors and thus the reduction in the deadweight loss is only marginal.\textsuperscript{270} Moreover, the distortion in the allocation of risk and the


\textsuperscript{266} Alexander Belinfante & Richard L. Johnson, Competition, Pricing and Concentration in the U.S. Recorded Music Industry, 6 J. CULTURAL ECON. 11, 13 (1982).

\textsuperscript{267} Id.

\textsuperscript{268} Written Statement of the American Antitrust Institute Before the Senate Judiciary Comm., Subcomm. on Antitrust, Competition Policy and Consumer Rights, Hearing on Universal Music Group’s Proposed Acquisition of EMI’s Recorded Music Division, 112th Cong. 4 (2012).

\textsuperscript{269} Id., at 5. Some have suggested that in the digital age “technology is allowing many creators to disseminate their work themselves.” Shaffer Van Houweling, supra note 102, at 615. Joel Waldfogel, who is conducting an extensive research on the modern distribution methods used by the music industry, found that barriers to entry in the industry were substantially lowered in recent years, which allows more creators that are not affiliated with a major record company to have a significant commercial success. Joel Waldfogel, And the Bands Played on: Digital Disintermediation and the Quality of New Recorded Music. Available at 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.

\textsuperscript{270} This claim was furthered explored in Section IV.E, where it was shown that even if
transfer of income from the young artist 35 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 megastar recording artists are able to extract considerable income throughout their career from other sources including other records, touring, and advertising campaigns. Consequently, in most cases, those megastars that are going to be able to earn considerable income through their post-termination rights are very rich when their termination rights vest. In other words, denying income to the 25 year old struggling Bruce Springsteen so that the 60 year old multimillionaire Springsteen can get slightly richer seems undesirable.

As suggested in Parts IV-V the Copyright Act can 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 in order to reduce the costs of the system and shortening the vesting period substantially, in order to increase the benefits. Indeed, it seems that the fixed costs of production and distribution in the music industry are not very high, especially in recent years,271 and the industry is profitable enough to be able to handle earlier terminations of transfers.

While the termination right system in its current form seems inefficient in the music industry, it is unclear whether, with the proposed modifications, the benefits will outweigh the costs. Those benefits in reducing the deadweight loss should also be compared with other legal rules which might achieve this reduction. Those alternative rules might include tighter merger controls in the industry,272 reducing barrier to entry by, for example, fighting payola273 or by interpreting the fair use doctrine broadly,274 and more. A full analysis of those possibilities and their advantaged and disadvantages, is beyond the scope of this work.

---

a very low discount rate is used the authors will be able to get back, using termination of transfer, only 8% of the value of their work.
271 See supra note 269.
274 Interpreting the fair use defense narrowly requires the producer to secure more licenses, which increase the transaction costs and the barrier to entry to the industry. 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 (6th Cir. 2005), makes the production of music more expensive, especially for 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).
3. **The Film Industry and Software Industry**

The film industry and the software industry are being discussed together because they present a common problem. Under current law, with a few exceptions that will be explored 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, sometimes hundreds or thousands of them. Granting even limited power to those individuals with respect to the final product will cause a transaction costs nightmare. In fact, with so many possible creators even a compulsory licensing system will 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. As mentioned, termination of transfer does not apply to work made for hire and therefore, as a general matter, both industries will not need to deal with the effects of Section 203.

The film industry, however, routinely creates derivative works using pre-existing works. The typical examples are movies that are based on previously published books. In those cases, as the producer of “Rear Window” or “Superman” discovered, and as was discussed in Part V, the industry will need to deal with the termination of the rights in the underlying book. 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 Royalties Rights**

As mentioned, including inalienable resale royalties rights—similar to droit de suite—in the federal Copyright Act was considered from time to time and the U.S. Copyright Office has recently begun another study on the topic.

The industry presents a unique twist to the profit sharing issue because unlike the other main copyright industries, it is based on the sale of physical objects and not intangible rights. This might affect the costs of a

---

275 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, see supra note 51, and most creators in the software industry are salaried employees who create the work within the scope of their employment, see supra text accompanying notes 48-50.

276 See supra text accompanying note 49.

277 See supra note 54.

278 See supra text accompanying notes 41-45.

279 See supra note 70.

280 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 similarly to
voluntary profit sharing scheme. As discussed in Part II, effective contractual profit sharing scheme fails to address the problem of downstream buyers. The ability to create servitude in favor of the artist might therefore be valuable to the parties. However, as explored in Section II.C such arrangements will probably require a separate registration system and procedures to locate and compensate the authors and their successors, which will probably increase transaction costs and create some fragmentation of rights. 281 A detailed cost-benefit analysis might explore whether such a system is desirable.

However, as it was shown in Section II.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 justified only if there is insufficient competition among the buyers of fine art. This is not the case.

Unlike many other creative industries, fine art can and is 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 50 companies controlling only about 40% of the market. 282 There are also more than 17,500 museums in the country. 283 Barriers to entry in this market are low and thus it is unlikely that market concentration will develop in the future.

Therefore, as this is a highly competitive industry, there is no real justification to inalienable rights of resale royalties. 284 The artists in this

281 See generally Hansmann & Santilli, supra note 86, at 276.
284 Hansmann & Santilli reached a similar conclusion when they analyzed the
industry are just not feeble individuals who must face massive powerful buyers.

CONCLUSION

This Article provides an in-depth analysis of the economics behind the termination of transfer provisions of the Copyright Act and comparable mechanisms under foreign law. It was shown that profit sharing mechanisms might be desirable as voluntary arrangements, and that the law might encourage their creation and enforcement. However, the cost of inalienable termination rights mechanism, in its current form, outweigh its benefits.

The Article proposed several modifications to the termination rights rules, including: Termination should vest earlier, contracting around the right should be allowed on the eve of termination, and the author’s interests should be protected by a liability rule and not property rule. However, even with those modifications, it is unclear if the continued existence of termination rights is economically justified, especially in the modern reality of decrease in the barriers to entry in many copyright industries. The Article also suggests that there is no convincing justification for establishing in this country an inalienable resale royalties right for fine art, similar to the droit de suite doctrine under European law.

desirability of those rights. Hansmann & Santilli, supra note 86, at 278-79.