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A COMPARISON OF RESPONSES TO THE RECORD RENTAL INDUSTRY UNDER JAPANESE AND U.S. COPYRIGHT LAW

Robert Adachi and Michael Fedrick*

I. INTRODUCTION

The record rental industry was a fast-growing business in both the United States and Japan during the early 1980s. It profited by renting out copyrighted sound recordings to consumers without the authorization of the holders of those copyrights. Copyright holders in the music industry perceived the growth of a record rental business as a threat to their ability to generate royalties from the sale of musical recordings. The music industries of both Japan and the United States therefore pressured their respective governments to strengthen the legal protection afforded copyright holders.

The Congressional response to lobbying by the music industry has resulted in the demise of the U.S. record rental industry. The record rental business in Japan, however, continues to thrive in spite of the changes in the copyright law adopted by the Japanese Diet. In order to understand why the record rental industry has fared differently in the two countries, the legal responses in Japan and the United States to the challenges posed by that industry must be examined in light of the copyright laws of both countries as well as the history of the dispute between record makers and lenders of sound recordings.

II. REGULATION OF THE RECORD RENTAL INDUSTRY IN JAPAN UNDER COPYRIGHT LAW

A. The Growth of the Record Rental Industry in Japan

Record rental shops in Japan operate in much the same way as video rental stores do in the United States. A customer normally pays an initial fee to the record rental store, which then grants that

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customer the right to rent phonograph records, cassettes, or compact discs from the store. Subsequently, that consumer may rent the aforementioned types of recordings upon presentation of a membership card.

Frequently, record rental establishments also provide consumers with a variety of other services, such as photocopying and the sale of blank cassettes. Consumers often buy blank cassettes, rent compact discs at the record rental shops, and then return home to record their musical selections. The shops therefore offer consumers, often at substantially lower costs, an alternative to purchasing phonograph records, cassettes, or compact discs.

The record rental industry in Japan has experienced phenomenal growth. In 1981 alone, the number of rental record shops in Japan grew from about 800 to over 1,050,¹ more than one per day every business day of the year. By 1986, the total number had risen to 2,424.² Currently, it is estimated that there are over 7,000 such establishments in Japan.³ Many of these shops operate without closing for holidays, and entrepreneurs have even established shops in the United States in order to rent Japanese compact discs to American consumers.⁴ When the Japanese music industry detected this explosive growth, it looked to the Japanese copyright law for protection.

B. The Current Structure of the Japanese Copyright Act

The Japanese Copyright Act (hereinafter "Copyright Act"), a statutory body of law, primarily governs copyrights (*chosakuken*) in Japan.⁵ Since Japan is a civil law country, there is no common law copyright action. Protection under the Copyright Act is extended to works (*chosakubutsu*)⁶ and neighboring objects (*rinsetsuhogobutsu*).⁷ Works include "productions in which thoughts or sentiments are expressed in a creative way and which fall within the literary, scientific, artistic, or musical domain."⁸ Neighboring ob-

1. K. ABE, CHOSAKUKEN TO SONO SHUHEN [COPYRIGHT AND ITS PARAMETERS] 217 (1983).

2. S. KAWABATA, REKODO SANGYOKAI [THE RECORD INDUSTRY] 209 (1987).

3. Telephone interview with Neil Turkewitz, Associate General Counsel, Recording Industry Association of America, 1020 Nineteenth Street, N.W., Suite 200, Washington, D.C. 20036 (Feb. 12, 1990).

4. A store which lends Japanese compact discs to consumers was established in Los Angeles, California in 1989.

5. Chosukaken Ho [Copyright Act], Law No. 48, 1970. (Hereinafter "Copyright Act").

6. *Id.*, art. 1.

7. *Id.*, art. 89.

8. Z. KITAGAWA, DOING BUSINESS IN JAPAN, § 8.02[2] (1990). See also Copyright Act, art. 2.

jects are defined as performances, the production of phonorecords,⁹ and broadcasts.¹⁰

The creator of a work receives protection under the Copyright Act from the time the work is created until fifty years after the death of the creator.¹¹ In contrast, performers, producers of phonorecords, and broadcasters holding copyrights for neighboring objects receive protection under the Copyright Act for a period of thirty years from the date of initial performance, phonorecord production or broadcast.¹²

Protection under the Copyright Act confers certain exclusive rights upon the holder of a copyright. At present, a creator of a work is granted a right of reproduction,¹³ a right of broadcast,¹⁴ a right of public recitation,¹⁵ a right of public exhibition¹⁶ and presentation for viewing,¹⁷ a right to rent out,¹⁸ as well as a right to translate his or her work.¹⁹

The Copyright Act grants performers holding copyrights for their performances (a neighboring object) a right to record²⁰ or broadcast²¹ those performances. Performers also currently have a right to rent out produced recordings of their performances.²² Record producers who reproduce their phonorecords²³ retain a right to rent out the reproductions.²⁴ The Copyright Act also covers a broadcaster's right to reproduce neighboring objects for which he or she retains a copyright.²⁵

No official system of copyright registration exists in Japan. In order to minimize disputes regarding the formation and ownership of copyrights, however, it is possible to register the date of first publication or the date of first public disclosure. Such registrations create a presumption that the registry date corresponds to the date of first publication, broadcast, recitation, or performance.²⁶ No filings

9. As defined under the Copyright Act, phonorecords include records, tapes, and compact discs. See Copyright Act, art. 2(1)(5).

10. KITAGAWA, *supra* note 8, at § 8.02[2].

11. Copyright Act, art. 51.

12. *Id.*, art. 101.

13. *Id.*, art. 21.

14. *Id.*, art. 22.

15. *Id.*, art. 23.

16. *Id.*, art. 24.

17. *Id.*, art. 25.

18. *Id.*, Art. 26.

19. *Id.*, art. 27.

20. *Id.*, art. 91.

21. *Id.*, art. 92.

22. *Id.*, art. 95.

23. *Id.*, art. 96.

24. *Id.*, art. 97.

25. *Id.*, arts. 98-100.

26. *Id.*, art. 76.

or registrations are necessary in order to form a copyright.

C. Lack of Protection for Copyright Holders Prior to 1985

As initially promulgated in 1970, the Copyright Act did not grant copyright holders exclusive control over rentals of phonorecords of both works and neighboring objects through record rental establishments. However, as the popularity of record rental stores increased during the 1980s, two opposing views emerged concerning the legal status of the stores. In his book *Copyright and Its Parameters*, Professor Koji Abe summarized the view taken by the Japan Record Association, the group representing the interests of the record making industry:

The demand made by the thirteen record makers that the record rental industry cease doing business was premised on the following argument: (1) producers of phonorecords hold an exclusive right to reproduce records under Article 96 of the Act; (2) Article 2(1)(15) defines reproduction as material reproduction by audio, visual or other form of recording; (3) thus, reproductions of audio recordings from records fall within the right of reproduction held by record makers; (4) the act of reproduction encompasses the act of providing opportunities to reproduce records by rental to a third party at a profit; (5) the act of renting records to customers at a profit with knowledge that the customer will reproduce the record on cassette tape should be treated as an act of reproduction under the Act; (6) thus, the record rental industry is engaged in an act which violates record makers' copyrights of neighboring objects.²⁷

Professor Abe also summarized the view of the Japan Rental Record Association, a group formed by a conglomerate of record rental stores to counteract the organized efforts of the Japan Record Association. According to the record rental industry, the rental of records to consumers was merely a lease with limited conditions. Hence, the record rental shop had no control over what the consumer or lessee did with the record, as long as it was not damaged. Furthermore, the lessee's right to record the phonorecord at home was protected under Article 30 of the Copyright Act. Thus, since the Copyright Act did not codify an exclusive right to rent out phonorecords, the copyright holders had no cause of action against the record rental industry or the lessees.²⁸ In addition, the Japan Rental Record Association protested that its members were being singled out for attack, when in fact private consumers and the makers of cassette tapes and recorders were just as much to blame for the loss of royalties, if any, by the record makers.²⁹

27. ABE, *supra* note 1, at 223-24. (This passage was translated from Japanese to English by one of the authors of this comment).

28. Copyright Act, art. 30.

29. ABE, *supra* note 1, at 224.

Based on his analysis of the two viewpoints, Abe concluded that the legal liability of the record rental industry depended on whether the leasing of phonorecords by record rental shops and the reproduction engaged in by consumers were regarded as a single act or as separate acts under the law.³⁰ If rental and recording were treated as a single act, then the record makers would have a cause of action based upon an expansive interpretation of the right of reproduction. If the acts were separate, record rental establishments would be shielded from liability under the Copyright Act.

To the extent that Japanese court decisions had less impact than judicial rulings in the United States as legal precedent, the judiciary was effectively prevented from taking steps to resolve the dispute by further defining the scope of the right of reproduction. In effect, the record rental shops remained protected from legal liability during this period of confusion. Finally, the Japanese Diet sought to resolve this issue in 1985 by promulgating revisions to the 1970 Copyright Act.

D. The 1985 Revisions to the Copyright Act

The Diet determined that the act of rental was separate from the act of recording phonorecords. However, a new statutory right was created in order to protect the interests of copyright holders. The revised statute grants an exclusive right to rent out phonorecords or recordings, or works and neighboring objects (*taiyoken*). Under the 1985 revisions, creators of works retain a right to rent out their works as part of the group of rights granted under their copyrights.³¹ Performers³² and phonorecord producers³³ retain a right to rent out recordings of their neighboring objects. In this manner, the Diet sought to avoid the impractical and politically unpopular alternative of forcing the renting public to comply with a statutory cause of action, while providing protection for copyright holders by establishing a cause of action against the record rental industry.

The mechanics of the *taiyoken* are fairly simple. As soon as a copyright is established with respect to either a work or a neighboring object, the copyright holder is vested with a bundle of rights which now include a *taiyoken* for the term of the copyright. The *taiyoken* grants the creator of a work, performers, and record makers an exclusive right to rent out recordings of their material. Thus, rental with the intent to profit without the permission of the holder of the copyright violates the rights vested in the copyright holder

30. *Id.* at 225-26.

31. Copyright Act, art. 26(2).

32. *Id.* art. 95(2).

33. *Id.* art. 97(2).

and subjects record rental shops to liability.³⁴ Liability under the Copyright Act encompasses fines of up to one million yen or penal servitude as determined by the courts.³⁵

Although the *taiyoken* established a legal cause of action in favor of copyright holders, record rental shops nonetheless continue to exist in large numbers across Japan. This is because Japanese copyright holders have decided to allow record rental shops to continue operating under licensing agreements. Under these agreements, record rental shops may continue to rent out phonorecords to the public in return for a royalty for each phonorecord the record rental shop lends. For example, an agreement regarding the rental of compact discs made in April, 1985 provided that the Japan Record Association receive royalties of between 50 and 80 yen for each compact disc rented.³⁶ The reasonable amounts of the royalties allow the record rental shops to maintain their trade, and at the same time enable the record making industry to receive more revenue from their products.

The *taiyoken* is, however, limited in the protection it affords to holders of copyrights. Foreign recordings, for example, are currently not covered by the Copyright Act. It is estimated that foreign copyright holders lose one billion dollars a year in lost royalties due to rentals.³⁷ Also, the revisions allow a performer or record maker to prevent the rental of a phonorecord for at most one year.³⁸ Although allowing Japanese copyright holders to recover some royalties previously lost entirely to the record rental industry, the *taiyoken* nonetheless leaves record rental shops in a very favorable position in Japan.

III. REGULATION OF THE RECORD RENTAL INDUSTRY IN THE UNITED STATES UNDER COPYRIGHT LAW

A. The Appearance of Record Rental Shops in the United States

Record rental establishments began appearing in the United States at about the same time as they did in Japan. By 1984, according to industry estimates, there were approximately 200 record rental shops operating in the U.S.³⁹ Although the record rental in-

34. *Id.*, art. 113.

35. *Id.*, art. 119.

36. KAWABATA, *supra* note 2, at 209.

37. Turkewitz, *supra* note 3.

38. Copyright Act, art. 95(2)(2); Copyright Act, art. 97(2). *See also Id.*

39. H.R. REP. NO. 987, 98th Cong., 2nd Sess. 2 (1984), citing *Copyright: Audio and Video Rental: Hearings on H.R. 1027, S. 32, and H.R. 1029 Before the Subcommittee on Courts, Civil Liberties and the Administration of Justice, House Committee on the Judiciary*, 98th Cong., 1st Sess. (1983). (Joint statement of AGAC/The Songwriters Guild,

dustry was growing more slowly in the U.S. than in Japan, American record makers faced essentially the same problems as their Japanese counterparts. Under the Copyright Act of 1976⁴⁰ (hereinafter "Act"), they lacked an adequate statutory basis for preventing the proliferation of record rental shops. Although a copyright holder is vested under the Act with the exclusive right "to distribute copies or phonorecords⁴¹ of the copyrighted work . . . by rental,"⁴² this right was limited by a very large exception.

B. The First Sale Exception Rule

This exception, known as the first sale rule,⁴³ was statutorily enacted into the Act.⁴⁴ This doctrine holds that when a copyright holder sells a particular copy of a protected work, he or she loses the ability to control the further sale or disposition of that copy⁴⁵. One court characterized it as an expression of the common law aversion to burdening the alienation of personal property.⁴⁶ It may, however, more broadly be seen as the reluctance of the government to interfere in an essentially private transaction. For example, federal law still makes no provision for a moral right of authors, which includes the protection of a work of art against future alteration even after it has been sold, although such a right has been accorded under some state laws.⁴⁷

The owner of a copyrighted work is therefore "entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that . . . phonorecord."⁴⁸ There is no doubt as to the intent of Congress in enacting this section of the Act. "Where the copyright owner has transferred ownership of a

National Association of Recording Merchandisers, National Music Publishers' Association, and Recording Industry Association of America).

40. Copyright Act of 1976, 17 U.S.C. §§ 101-810.

41. "Phonorecords" are defined under the Act as "material objects in which sounds . . . are fixed" other than the sounds "accompanying a motion picture or other audiovisual work." 17 U.S.C. § 101. They would therefore include phonograph records, cassette tapes, and compact disc recordings.

42. 17 U.S.C. § 106(3).

43. The first sale rule was first established by the Supreme Court in *Bobbs-Merrill Co. v. Strauss*, 210 U.S. 339, 28 S.Ct. 722, 52 L.Ed. 1086 (1908). See also, *Harrison v. Maynard, Merrill & Co.*, 61 F. 689, 690 (2d Cir. 1894). Its roots, however, may reach back to the English common law. See Chafee, *Equitable Servitudes on Chattels*, 41 HARV. L. REV. 945, 982 (1928).

44. 17 U.S.C. § 109(a).

45. "Copies" as defined in 17 U.S.C. § 101 excludes "phonorecords." Unless otherwise indicated, however, "copies" shall include copies of phonorecords for purposes of this essay.

46. *Sebastian Int'l Inc. v. Consumer Contacts (PTY) Ltd.*, 847 F.2d 1093, 1096 (3d Cir. 1988).

47. See the California Art Preservation Act, CAL. CIV. CODE § 987 (West 1983). See also, N.Y. ARTS & CULT. AFF. LAW § 14.03 (McKinney Supp. 1991).

48. 17 U.S.C. § 109(a).

particular . . . phonorecord of a work, the person to whom the . . . phonorecord is transferred is entitled to dispose of it by sale, rental, or any other means."⁴⁹

C. The 1984 Amendments to the Copyright Act of 1976

With record rental establishments in Japan approaching 20 percent of all retail record outlets by 1984,⁵⁰ record makers in the U.S. moved to resolve the problems presented by the record rental industry in this country before they grew to similar proportions. The record making industry therefore petitioned Congress to change the existing law to afford the holders of copyrights in sound recordings more protection. Congress responded by passing the Record Rental Amendment of 1984.

This amendment grants relief to the holders of copyrights in sound recordings by specifically exempting phonorecords from the first sale rule. The subsequent owner of a copyrighted phonorecord "may not, for purposes of commercial advantage, dispose of . . . the possession of that phonorecord by rental, lease, or lending, or by any other act or practice in the nature of rental, lease, or lending."⁵¹ The language "any other act or practice in the nature of rental, lease, or lending" was used to forestall attempts to circumvent the new amendments. A retailer who sold a record to be bought back a few days later at a discount would, for example, violate the new prohibitions on unauthorized lending.⁵²

In order to operate a record rental shop under the new amendment, therefore, a proprietor would first have to obtain the authorization of the holders of the copyrights to all the musical works that the proprietor wished to rent. Even if the copyright holders could be persuaded to authorize the rental of their works, the start up costs for obtaining these authorizations for any given retailer would be prohibitively high and almost assuredly would forestall such a venture.

IV. CONCLUSION

Both the U.S. and Japan were responding to the same technological changes which suddenly made the rental of phonorecords a profitable undertaking. A record rental business was not practical in the era of the phonograph record due to the ease with which phonographs developed flaws which marred their sound quality. This situation changed, however, with the introduction of compact discs. Not only did the sound quality of compact discs far surpass

49. H.R. REP. NO. 1476, 94th Cong., 2d Sess. 79 (1976).

50. *Supra* note 39.

51. 17 U.S.C. § 109(b)(1).

52. H.R. REP. NO. 987, 98th Congress, 2d Sess. 4 (1984).

that of phonograph records, but the discs themselves also survived repeated use without deterioration in sound quality. In response, both countries took steps to afford greater protection to the holders of copyrights in sound recordings. The amendments to the copyright laws of both countries were, in fact, enacted within a year of each other. Why then do record rental shops still proliferate in Japan while those in the U.S. have been forced out of business?

One reason lies in the amount of protection granted under each of these copyright law amendments. In the U.S., the amendments covered all copyrights, not just domestic copyrights. They also allowed a copyright holder to prohibit absolutely the rental of a particular phonorecord. In Japan, by comparison, foreign works were left conspicuously unprotected. Due to the popularity of American music in Japan, a record rental shop could conceivably survive if it rented only foreign works and was prevented from renting out recordings of Japanese music. Furthermore, record rental shops can only be prohibited from renting out Japanese works for a maximum of one year. After that time, they are allowed to rent out such recordings under a compulsory license provision of the Japanese copyright amendments.

Another reason for the disparity in the fate of record rental shops in the two countries is simply the timing of the enactment of their copyright amendments. In the U.S., record rental establishments were banned while they were still comparatively few in number. In Japan, over 2,000 record rental outlets were in existence by the time the Japanese Diet passed a law protecting copyright holders, and public demand for such establishments was very high. Instead of attempting to shut down the whole record rental industry, the Japanese music establishment instead decided to work with it, extracting royalties in exchange for allowing the record rental shops to continue doing business.

Although probably a prudent business decision by the Japanese music industry under the circumstances, this arrangement leaves copyright holders in a much weaker position than if record rental shops had been shut down altogether. The pervasive presence of these establishments in Japan means that the operation of an unauthorized shop could easily go unnoticed by copyright holders or by other legitimate establishments. The total absence of such businesses in the United States, on the other hand, would make the operation of one much more conspicuous.

In Japan, if and when foreign copyright holders are accorded protection equivalent to that of their domestic counterparts, the record rental industry will also pose problems for foreign record makers. Aside from being forced to allow the rental of their records at the expiration of one year, foreign record makers will have to incur the extra expense of policing the rental of their recordings to make

sure that royalties are being paid by all record rental establishments. Since many of these establishments are small businesses, this may be a formidable task.