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### Section One: Division of Streaming Revenue

On 31 January 2020, I presented a lecture to MA students on the Global Entertainment and Music Business course at Berklee College of Music in Valencia.

The subject was music streaming.

During the lecture, I presented 4 flow diagrams (see attached):

- Slide 1 –the current situation with regard to the division of streaming spoils between Spotify / record label / recording artist / publisher / songwriter.
- Slide 2 – the consequences of the introduction of Equitable Remuneration
- Slides 3 & 4 – the consideration of an alternative “Active/Passive” Model.

#### CURRENT SITUATION – SLIDE 1

See attached diagram 1.

When streams were invented, there was no new agency set up to collect revenue.

Instead, the Publishers use Mechanical Copyright Protection Society (physical record sales) and Performing Rights Society (public performance/radio play) to administer the streaming revenue.

UK Publishers view streaming as 50% physical record sale (mechanical) and 50% radio play (public performance).

Record labels view streaming differently. 100% is allocated to physical record sale. It is administered 100% as a reproduction royalty and no public performance.

There is inconsistency between record label and publishing company in the administration of streaming revenue.

#### EQUITABLE REMUNERATION – SLIDE 2

Equitable Remuneration is an alternative model proposed by Tom Gray of Broken Record.

Tom Gray has recently been appointed as Chairman of Ivor Novello.

See slide 2.

Equitable Remuneration is a blend. It combines an exclusive right with an equitable right.

Applying an Equitable Remuneration model would result in a stream being treated as part physical record sale / reproduction and part public performance for both recording and publishing revenue.

Under the Equitable Remuneration model, the recording element would replicate the publishing element under the current model.

During the lecture, I discussed Equitable Remuneration and its application to streaming. Its origins were with the World Intellectual Property Organisation. Its application is legislated in the following three European Directives:

- Related Rights Directive
- Information Society Directive
- Rental and Lending directive

The Related Rights Directive application is broad. It extends to “broadcast by wireless means or for any communication to the public” and identified that Equitable Remuneration is payable on streaming to both record label and artist.

The Information Society Directive provides the performer the exclusive right to authorise or prohibit the use of their work where the broadcast is made available to the public by wire or wireless means.

The Information Society Directive provides that Equitable Remuneration applies where the consumer accesses content from a place and at a time chosen by them. It applies to streaming.

The Rental and Lending Directive stipulates that the right to receive Equitable Remuneration by label and artist is unwaivable.

I then went on to compare this to the UK Copyright, Designs and Patents Act 1988 – Section 182.

It provides that the rights of the performer and the phonogram producer be consistent with those Directives – with one exception.

See 182D.

The one exception reads “otherwise than by its being made available to the public in the way mentioned in 182CA(1).”

182CA(1) states: “by electronic transmission in such a way that members of the public have access to the recording at their place and time of choosing”.

Consequently, streaming is excluded?

The UK Copyright, Designs and Patents Act 1998 – Section 182 would seem to be contrary to the EU legislation, which was applicable at the time.

#### ACTIVE/PASSIVE – SLIDES 4 & 3

As an alternative, I then considered an active / passive model.

Here, I distinguish between active choices – “Alexa, play me”, click on track and choose vs “passive” where Spotify reverts to a playlist algorithm.

See slides 4 and 3.

This model identifies each stream and separates them between an active choice by the user or a passive algorithm determined by Spotify.

It differentiates between streams according to user consumption.

Which streams were actively chosen by the consumer?

This is equivalent to going into a record store and making a choice.

Which streams were chosen by the Spotify algorithm, “Spotify Radio”. This is the equivalent of the Radio DJ making the choice – BBC, Radio 1.

For active choices (slide 4), Spotify would continue to account to the labels under the exclusive reproduction arrangement. The labels and artists would receive the same as currently paid.

Passive is slide 3.

For passive algorithm “radio” plays, the recording element would be administered by PPL and the publishing element by PRS.

Current convention stipulates that public performance applied to radio play in the UK is split equally between recording (PPL) and publishing (PRS).

The weighting currently applied to streaming is 55% recording and 15% publishing.

Under the Active / Passive model, for the passive plays, the recording element of 55% and the publishing element of 15% would be amalgamated, a total of 70%, and then split equally – 37.5% to PPL and 37.5% to PRS.

It does not try to combine an exclusive reproduction copyright with a non-exclusive public performance broadcast.

The distinction by usage quantum.

The model is pure.

At the end of the lecture, I asked the students how they viewed the characteristics of a stream when considering their consumption of music.

They advised that their consumption was predominantly passive, Spotify algorithms, and this was likely to continue as they were enjoying more background music, rather than making specific choices.

They anticipated this trend would grow.

## **Section Two: Resistance to change & Group Structure – Economic Considerations**

The rights holders are an amalgamation of recording and publishing.

They are dominated by 3 majors:

1. Universal Music Group
2. Sony Music Group
3. Warner Music Group

The Digital Service Providers / Distributors are dominated by Spotify – 57% of subscribers – and Amazon – 32% of subscribers.

There has been continuing growth in streaming numbers.

The subscription model employed by Spotify works.

However, when you consider inflation, in relative terms, the music industry has not been able to achieve the results previously attained in 2000 during the period of physical CD sales.

In comparative terms, it has declined.

Is there a mutual reliance between the 3 major rights holders and the 2 major distributors? Does this allow for a competitive market on pricing?

Are the rights holders able to exercise undue influence over the artists' and songwriters' creative choices and the creatives' remuneration?

Do the rights holders exercise undue influence over the distributors?

Are the distributors able to exercise impartial music choice / delivery to the public?

**Section Three: Margins and why reluctance for change – be it ER or an alternative Active / Passive Model**

In the DCMS report, it was recognised that, for Records, recording artists would be paid a 21% reproduction royalty once they had achieved 100% recoupment of their personal advance, 100% of the origination costs, 100% tour support and 50% of video costs.

This provides the record label with a margin of 79% before marketing and promo.

For Publishing, the reverse is true: 80% is receivable by the songwriter, once their personal advance is recouped, the publisher retains only 20%.

The majority of the revenue is currently distributed to the record labels. The current split is 30% Spotify, 55% Recording, 15% Publishing.

The 3 major music group rights holders combine recording and publishing under common ownership.

The Music Group has a fiduciary duty to maximise return on investment to the shareholder.

Consequently, there will be a reluctance within the Music Groups to allow the publishing share to increase to the detriment of the record label's share, sine this would reduce profitability of the Group as a whole.

Any alternative model, be it Equitable Remuneration, the Active / Passive model, or another, will be resisted.

**COMPARISON OF STREAMING TREATMENT BY RECORD LABEL AND PUBLISHING COMPANY**

The three major rights-holding groups of companies are:

	Recording market share %	Publishing market share %
Sony Music <b>Group</b>	20	25
Universal Music <b>Group</b>	32	21
Warner Music <b>Group</b>	16	12
Independent	32	42
Total	100	100

In Streaming Slide 1, you will observe the disparity when comparing the recording and publishing streaming income element.

For publishing, in the UK, 50% is deemed a mechanical and administered by MCPS, and 50% is deemed public performance and is administered by PRS.

Recording is different. 100% is classified as an exclusive right and treated as a reproduction. There is no public performance element attributable to recording.

Why is the disparity?

How does Warner Publishing reconcile its 50% allocation to mechanical and 50% allocation to public performance, whilst Warner Records applies 100% to mechanical / reproduction?

They are both under common ownership and would attend the same Board Meetings.



[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

You will observe the disparity in values between the different plan types.

As a practice, we have undertaken hundreds of royalty audits on behalf of recording artists and songwriters.

Artists' and songwriters' royalty statements fail to provide the [REDACTED] different plan types.

Instead, the music Groups consolidate them into three to five different types:

Sony Music	Breakage Streaming Subscription Streaming
Universal Music	Ad-funded streaming Digital allocations (streaming) Permanent download Subscription streaming
Warner Music	Breakage Ad Supported Audit Recovery Payment Top-Up Subscription

Within "Subscription", [REDACTED] of the different Spotify plans are blended. No distinction is made between the student rate at [REDACTED] per million and the premium rate at [REDACTED] per million.

As auditors, we are not able to assess the economic value of the rights our artists and songwriters have licenced and assigned.

Article 19 of Directive (EU) 2019/790 of the European Parliament and of the Council requires the contracting party receiving rights in protected works to provide up to date, relevant and comprehensive information to the authors and performers on the exploitation of their works and performances. <https://www.legislation.gov.uk/eudr/2019/790/article/19>

It requires:

1. Modes of exploitation;
2. All revenues generated; and
3. Remuneration due on those revenues.

To undertake the audit satisfactorily, we request the royalty rates applied to each specific plan type be stated.

These requests are continually declined on the basis that an NDA was imposed between Spotify and the record label / rights holders.

I draw your attention to Section 5 regarding Licence vs Royalty.

Here, I identify that Spotify pays Sony under a two-tier arrangement – advertisement and subscription.

For advertised revenue, it is activity based.

For subscription revenue, it is based on the number of subscribers – a licence fee.

It is, perhaps, this arrangement that is causing the suppression of the subscription plan rates, since the remuneration received by the record label is not activity based, and this amalgamation is a convenient avoidance of fair and transparent accounting.



## **Section 5: Licence vs Royalty - Recoupment**

Under the recording agreement, recording artists are paid a royalty, often 21% of record label's reproduction receipts and 50% to 60% of master usage fees for films and advertisements.

The commercial terms of an artist recording remuneration is calculated as:

1. 21% royalty in respect of reproduction
2. 50% to 60% for other usage under licences (e.g. use of master rights for film and adverts)

This is paid after recoupment of 100% personal advance, 100% origination costs, 100% tour support, and 50% of music video costs.

You will note the distinction in rates under the royalty / reproduction model, the rate is low – 21% for reproduction; for licence usage (film / advertising) the rate is high – 50% or 60%.

Reproduction includes physical records and streaming.

### **SPOTIFY AND SONY / SONY AND RECORDING ARTIST**

Please find attached 18 January 2011 Sony and Spotify agreement.

#### **Label Fees**

When reading the agreement, page 29 – 10. Label Fees – provides a minimum user rate for Ad Supported and Online Subscription and Premium Subscription.

The mechanism of calculation distinguished between Ad Supported and Other.

Ad Supported is calculated at the higher of:

1. 60% of Label Usage Percentage of Gross Revenues; and
2. per stream minimum (\$0.02250/stream)

i.e. it is activity based

Compare this to other usage, namely Online Subscription and Premium Subscription.

For Online Subscription, it is calculated at the higher of:

1. 60% of Label Usage Percentage of Gross Revenues and
2. Sony Market Share 20% x Number of Subscribers x \$3.00

For Premium Subscription, it is calculated at the higher of:

1. 60% of Label Usage Percentage of Gross Revenues and
2. Sony Market Share (say 20%) x Number of Subscribers x \$6.00

For all usage other than Ad Supported, Sony is paid based on the number of subscribers. It is not calculated with regard to streams. It is not activity based.

It is a license arrangement based on Subscribers.

This is inconsistent with the artist royalty statement which has been calculated solely on activity, the number of streams.

I.e., record label receives money from Spotify primarily under a licence (60%), yet pays artist out under a reproduction model (21%).

The two do not equate.

**Top Up Fees**

Part (b), page 30 provides for top up fees when Spotify has failed to achieve Subscriber Goal or Conversion Goal.

It is calculated using a weighted average of Online and Premium Subscribers.

The Top Up Fees perhaps appear as 'breakage' on the royalty statement.

Breakage could also be unused third party guaranteed subscription months or unused guaranteed wholesale revenue (as per Clause 10 (g))

From our royalty audits, we have not been able to determine with any certainty exactly how breakage has been calculated.

The agreement attached is dated 18 January 2011.

It is now 11 years old and will have been superseded.

We are not privy to the current agreement. We are advised that it is precluded under a mutual NDA between Spotify and Rightsholder.

## **Section Six: Warner SEC Analysis**

Please see attached Excel file "Warner SEC Analysis".

We have analysed the Warner Financial Statements for the years ended 30 September 2017 to 30 September 2021.

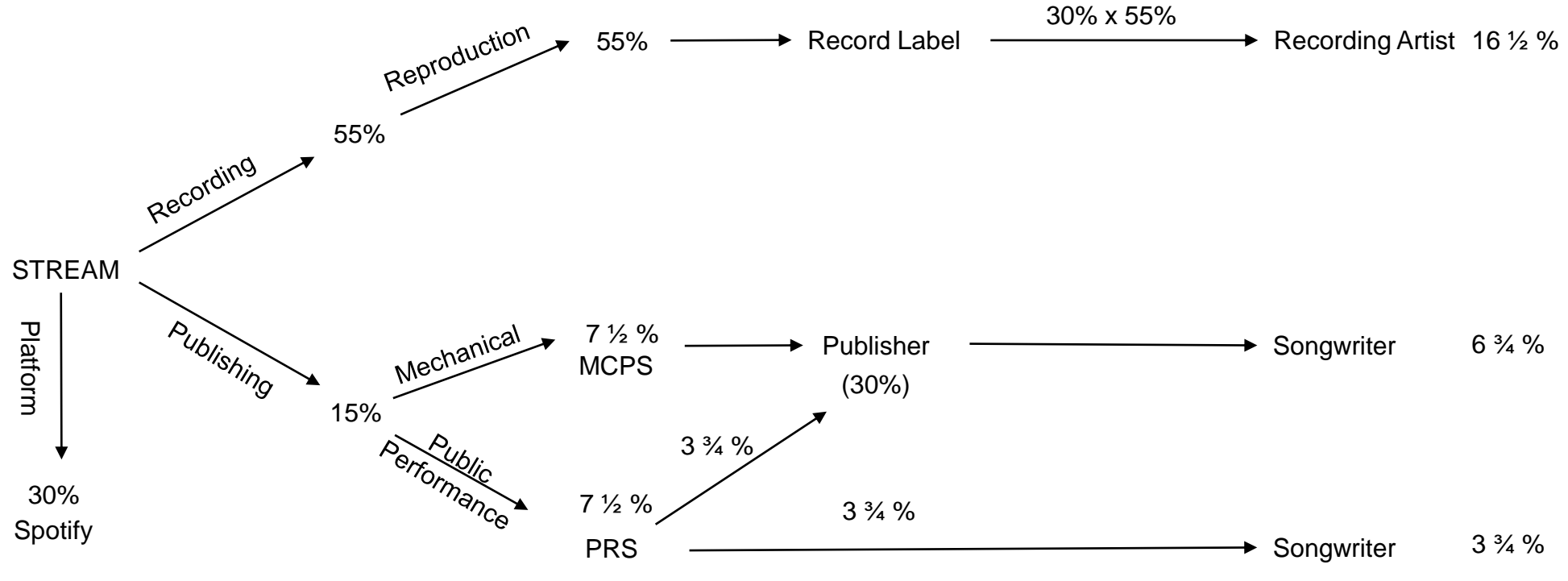
See Artist & Repertoire costs (line 28) as a proportion of recorded income.

You will observe that it has declined from 31.92% at 30 September 2017 to 28.41% at 30 September 2021.

This equates to a 3.51% reduction from the perspective of Warners.

This equates to an 11% reduction from the perspective of the recording artist.

# Current situation



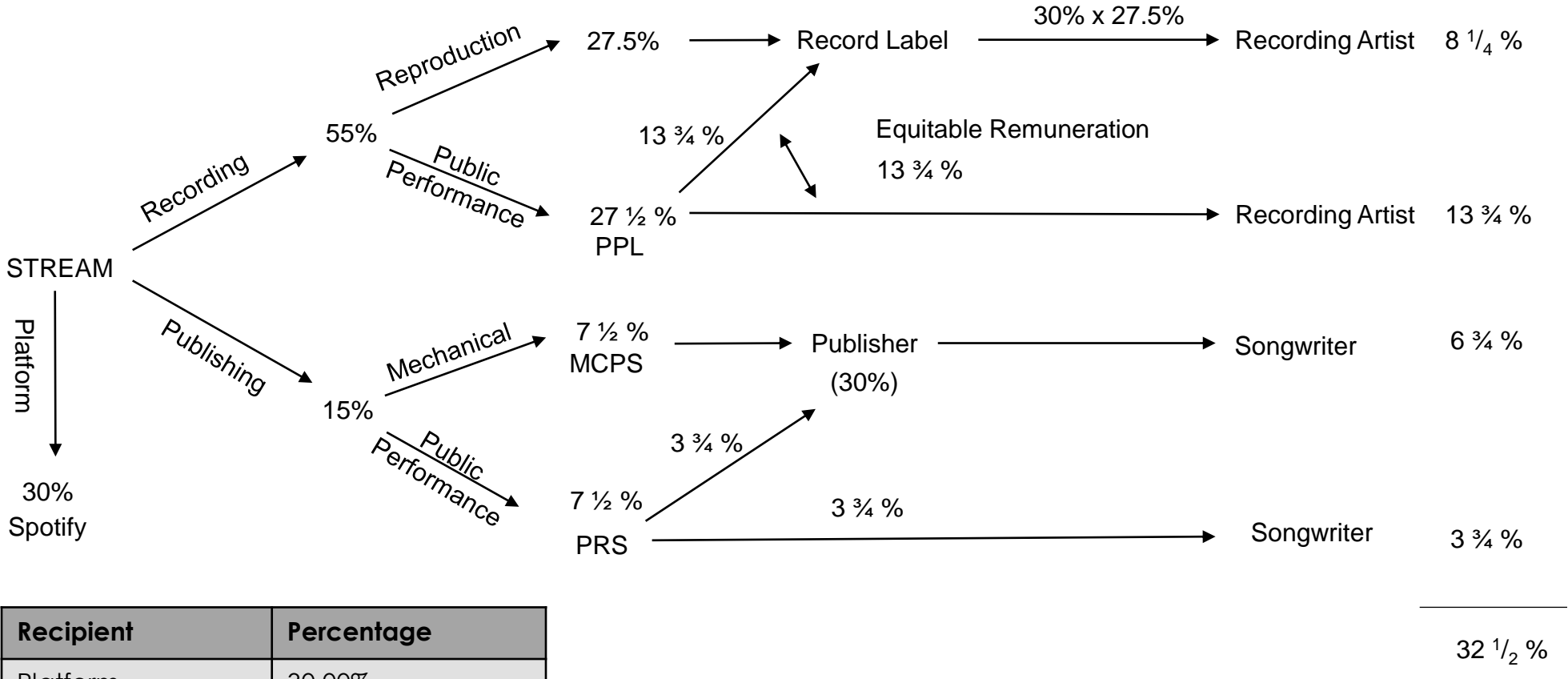
Recipient	Percentage
Platform	30.00%
Record Label	38.50%
Recording Artist	16.50%
Songwriter	10.50%
Publisher	4.50%
	<b>100.00%</b>

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27 %

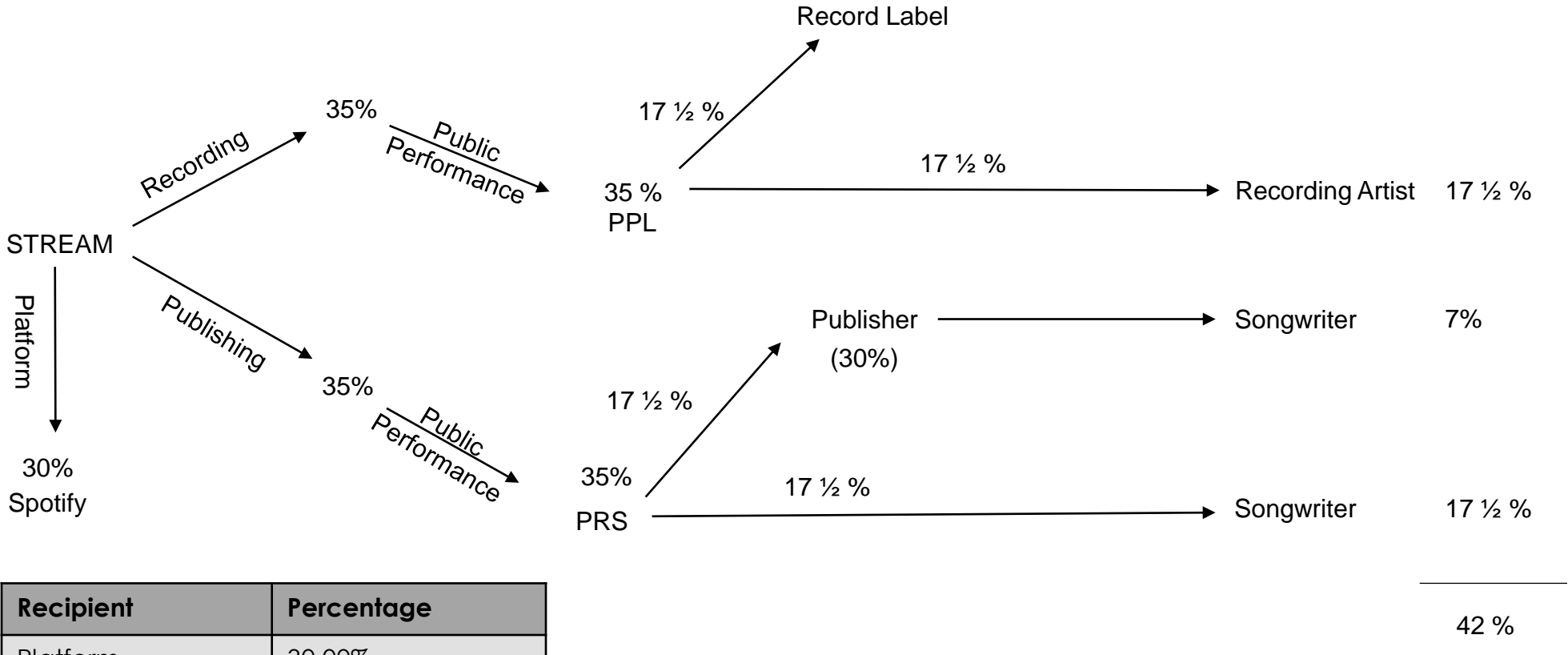
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# Equitable Remuneration



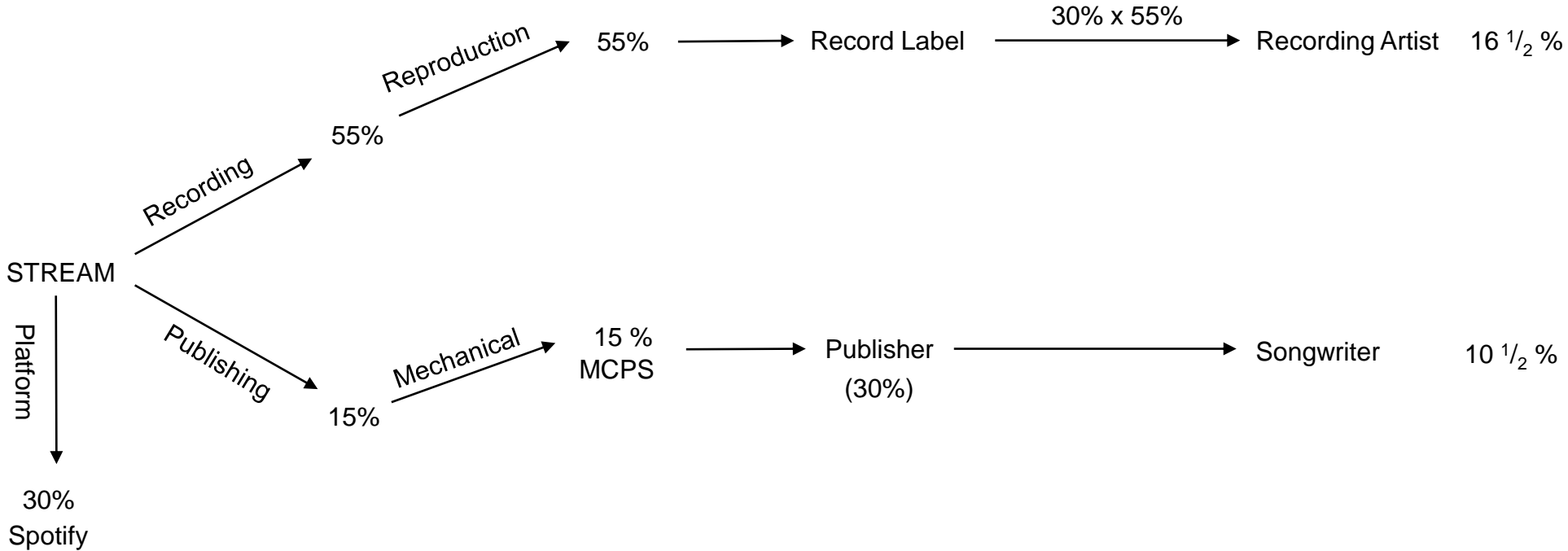
Recipient	Percentage
Platform	30.00%
Record Label	33.00%
Recording Artist	22.00%
Songwriter	10.50%
Publisher	4.50%
	<b>100.00%</b>

# Passive user/public broadcast



Recipient	Percentage
Platform	30.00%
Record Label	17.50%
Recording Artist	17.50%
Songwriter	24.50%
Publisher	10.50%
	<b>100.00%</b>

# Active user/CD Sales



Recipient	Percentage
Platform	30.00%
Record Label	38.50%
Recording Artist	16.50%
Songwriter	10.50%
Publisher	4.50%
	<b>100.00%</b>

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27 %

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# World Intellectual Property Organisation (WIPO)



## WIPO Copyright Treaty 1996

Performance and Phonogram Treaty, Article 10

**Performers** shall enjoy the **exclusive right** of **authorising** the **making available** to the public of their performance fixed in phonograms, by wire or wireless means, in such a way that members of the public may access these from a place and at a time individually chosen by them.



WIPO Performances and Phonogram Treaty, Article 14

**Producers of phonograms** shall enjoy the **exclusive rights** of **authorising** the **making available** to the public of their phonograms by wire or wireless means in such a way that members of the public may access them from a place and at a time individually chosen by them.



# European Economic Community



Related Rights Directive	Information Society Directive	Rental and Lending Directive
92 / 100 / EEC – Article 8	2001 / 29 / EC – Article 3	2006/115/EC
19 November 1992	22 May 2001	12 December 2006
Equitable Remuneration	Authorise and Prohibit Right	Unwaivable Equitable Remuneration

# Related Right Directive



92/100/EEC – Article 8, 19 November 1992

## Article 8, Broadcasting and communications to the public

1. Member States shall provide for **performers** the **exclusive right** to **authorise or prohibit** the broadcasting by wireless means and the **communications to the public** of their performances, except where the performance is itself already a broadcast performance or is made from a fixation.
2. Member States shall provide a right in order to ensure that a single equitable remuneration is paid by the user, if a phonogram published for commercial purposes, or a reproduction of such phonogram, is used for broadcasting by wireless means or for any communication to the public, and to ensure that this **remuneration is shared between the relevant performers and phonogram producers**. Member States may, in the absence of agreement between the performers and phonogram producers, lay down the conditions as to the sharing of this remuneration between them.

# Information Society Directive

Article 3, 2001/29/EC, May 2001



## Article 3 - Right of communication to the public

1. Member States shall provide authors with the **exclusive right** to **authorise or prohibit any communication** to the public of their works, by **wire or wireless means**, including the making available to the public of their works in such a way that members of the public may access them from a place and at a time individually chosen by them.

2. Member States shall provide for the **exclusive** right to **authorise or prohibit** the making available to the public, by **wire or wireless means**, in such a way that members of the **public** may access them from a **place and at a time** individually **chosen by them**:

(a) for **performers**, of fixations of their performances;

(b) for phonogram producers, of their phonograms;

(c) for the producers of the first fixations of films, of the original and copies of their films;

(d) for broadcasting organisations, of fixations of their broadcasts, whether these broadcasts are transmitted by wire or over the air, including by cable or satellite.

3. The rights referred to in paragraphs 1 and 2 shall not be exhausted by any act of communication to the public or making available to the public as set out in this Article.



# Rental and Lending Directive

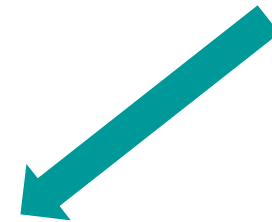
Directive 2006/115/EC - 12 December 2006

On rental right and lending right and on certain rights related to copyright in the field of intellectual property.

Intention of Directive (Published alongside Directive.);

12) it is necessary to introduce arrangement ensuring that an unwaivable equitable remuneration is obtained by authors and performers who must remain able to entrust the administration of this right to collecting societies representing them.

Related Rights Directive	Information Society Directive	Rental & Lending Right Directive
92 / 100 / EEC – Article 8	2001 / 29 / EC – Article 3	2006/115/EC
19 November 1992	22 May 2001	12 December 2006
Equitable Remuneration	Authorise and Prohibit Right	Unwaivable Equitable Remuneration



**The Copyright Design and Patents Act 1988  
(The Act) – Section 182**



## 182CA

### Consent required for making available to the public

- 1) A **performer's rights** are infringed by a person who, without his consent, makes **available to the public** a **recording** of the whole or any substantial part of a qualifying performance by electronic transmission in such a way that members of the **public may access** the recording from a **place** and at a **time** individually **chosen** by them.
- 2) The right of a performer under this section to authorise or prohibit the making available to the public of a recording is referred to in [F 472 this Chapter] as “making available right”.]



## 182D

### Right to equitable remuneration for exploitation of sound recording.

1) Where a commercially published sound recording of the whole or any substantial part of a qualifying performance –

(a) Is played in public, or

(b) Is communicated to the public otherwise than by its being made available to the public in the way mentioned in section 182CA(1).

The performer is entitled to equitable remuneration from the owner of the copyright in the sound recording.



## Section 182 CA(1)

(1) A performer's rights are infringed by a person who, without his consent, makes available to the public a recording of the whole or any substantial part of a qualifying performance by electronic transmission in such a way that members of the public may access the recording from a place and at a time individually chosen by them.



Recorded Music - Revenue by Type	For the Fiscal Year Ended Sept-30					Reference 2021
	2017	2018	2019	2020	2021	
	\$ Million	\$ Million	\$ Million	\$ Million	\$ Million	
Digital	1,692	2,019	2,343	2,568	3,105	P50
Physical	667	630	559	434	549	P50
Total Physical and Digital	2,359	2,649	2,902	3,002	3,654	P50
Artist services and expanded-rights (tour, merchandise)	385	389	629	525	599	P50
Licensing (adverts, films)	276	322	309	283	291	P50
<b>Total Recorded Music</b>	<b>3,020</b>	<b>3,360</b>	<b>3,840</b>	<b>3,810</b>	<b>4,544</b>	P50
Artist and repertoire costs	964	1,054	1,178	1,148	1,291	P60
Product costs	628	700	827	771	962	P60
<b>Total cost of revenues</b>	<b>1592</b>	<b>1754</b>	<b>2005</b>	<b>1919</b>	<b>2253</b>	P60
General and administrative expenses	478	573	522	875	569	P60
Selling and marketing expenses*	465	521	550	627	726	P60
Distribution expenses*	66	67	79	95	113	P60
<b>Total selling, general and administrative expenses</b>	<b>1009</b>	<b>1161</b>	<b>1151</b>	<b>1597</b>	<b>1408</b>	P60
<b>Recorded Music - Net Profit</b>	<b>419</b>	<b>445</b>	<b>684</b>	<b>294</b>	<b>883</b>	
	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	
Artist Repertoire costs as a proportion of recorded income	31.92%	31.37%	30.68%	30.13%	28.41%	

Selling and marketing costs as a proportion of recorded income	15.40%	15.51%	14.32%	16.46%	15.98%
Distribution costs as a proportion of recorded income	2.19%	1.99%	2.06%	2.49%	2.49%
Recorded Music Net Profit as a proportion of income	13.87%	13.24%	17.81%	7.72%	19.43%
Recorded Music Net Profit (exc.admin) as a proportion of income	29.70%	30.30%	31.41%	30.68%	31.95%

\*\$71m removed from Selling and Marketing expenses and \$35m from Distribution Expenses in 2019 in relation to EMP purchase

	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	Ref
OIBDA Recorded Music - USD \$ (Millions)	451	480	623	349	936	P58
OIBDA Recorded Music - % of Recorded Music Revenue	15%	14%	16%	9%	21%	P58
OIBDA Recorded Music - % of Recorded Music Revenue – Share based compensation removed	n/a	n/a	17%	19%	21%	P58