

FINANCIAL MATTERS

Royalties In The Age Of The Internet

By Todd Brabec & Jeff Brabec

The online/digital world has dramatically changed the way music is licensed in all media in addition to affecting the composer and songwriter fees and backend royalties associated with any project. For film and television composers and songwriters and for those who license pre-existing compositions to audio visual productions and other projects, many new opportunities have arisen for additional exploitation.

But with those opportunities have come increasingly complex contracts, new royalty structures and rates, expansions of the "grant of rights" notion and increased requests for new types of licensing models, some of which challenge long-standing practices of compensation and rights.

This article explains many of the areas you need to be aware of and the concepts involved in this "new world of traditional/online/digital media and distribution."

Television

Because of the myriad of distribution platforms and ancillary uses, television continues to be an extremely valuable media for the use of music...whether score, theme music, newly written songs or pre-existing compositions.

In this world of multi-media platforms, the licensing of existing material (e.g., contemporary hit songs, standards, newly released records, etc.) can take on many variations depending on the program, how the music is used, the rights being requested, the budget of the production, the expectations of the audience, and the marketability and commercial exploitation avenues available.

There are many variations depending on whether the show is a new series, established hit, drama, comedy or music-centric, contestant-based format (e.g., *American Idol*, *The*

Voice, *Dancing With The Stars*, *America's Got Talent*, etc.).

For example, many successful series license music via an "all media life of copyright" synchronization agreement which ensures that for a one-time payment, the producer can distribute the program via all existing and future media platforms, including home/personal use video. In most cases, theatrical distribution is excluded from this license arrangement, as is out-of-context promotional use. Depending on the series, there may be additional fee options included for the use in promo spots for a limited period of time (including downloads from digital services such as iTunes), a negotiation as to mechanical rates for soundtrack album or single sales and, in some cases, even a "hold back" period for a short period of time after the initial broadcast as to previously unexploited songs.

Other major types of licensing arrangements are an "all television with home video option" and an "all television and home video license"; both usually providing for the show's producer to turn the license into an "all media" one for a separate fee if the original license was for less than such media and to "life of copyright" if there was a shorter duration.

As opposed to scripted series, the music centric and dance programs (*The Voice*, *Dancing With The Stars*, etc.) are licensed in a much different manner usually on a shorter term and multi-option basis. For example, the original territory for the license sometimes may be for the U.S. and Canada (rather than the world) and the term might be for 1 to 5 years rather than life of copyright. Fees are also many times based on the timing of the composition and whether it is used in recaps or is repeated in future episodes. There are

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The online/digital world has changed how music is licensed, how contracts and deals are negotiated and structured and how composer and songwriter compensation is arrived at.

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usually separate fee options for use on websites, streaming, audio downloads, ringtones, ringbacks, apps, electronic sell through and out-of-context advertising. *So You Think You Can Dance* even has an option to use a clip using a composition on the large screen on stage during the live tour which occurs after the season ends each year.

Television scoring contracts are usually work-for-hire agreements and the grant of rights normally covers all media and distribution platforms now or hereafter known.

Album and Single Sales (Mechanical Royalties)

At one time, film and television soundtrack albums and singles sold well. With the proliferation of illegal file sharing, piracy and single song download preferences, mechanical royalties (the amount paid to a music publisher and songwriter by a record company for the sale of one song) have dropped significantly. Regardless, this area can be an important source of income for some composers and songwriters. For example, the song for the James Bond film *Skyfall* sold over 460,000 individual track downloads in the U.S. alone during the first two weeks after it was released prior to the film's opening.

In 2008, the Copyright Royalty Board (CRB) set mechanical rates for the period 2008-2012 for the sale of physical recordings, permanent digital downloads, limited downloads, on-demand streams and master tones. The primary rate was 9.1 cents per song sold on a physical recording or digital download with a rate of 1.75 cents per minute if the recording was over 5 minutes. For limited downloads and interactive streams, rates were based on a percent of the online music service's revenue (10.5%) with minimums and reduced by whatever fees were being paid to ASCAP, BMI and SESAC. The rate for master tones was 24 cents per download.

In early 2012, NMPA, RIAA and DIMA entered into an industry-wide agreement which would cover the years 2013 to 2017. The draft of

regulations has been submitted to the Copyright Royalty Judges for approval. Under these regulations, the 2008 rates and configurations would be continued with five new subscription and non-subscription services at new rates added to the mix.

The new royalty bearing categories for music publishers, songwriters, composers and lyricists are:

Paid Locker Services—Subscription based locker providing on demand streaming and downloads.

Purchased Content Lockers—A free locker provided to a purchaser of a permanent digital download, ringtone or CD where the music provider and locker have an agreement.

Limited Offerings—Subscription based service offering limited genres of music or specialized playlists.

Mixed Service Bundles—A music service combined with a non-music product, such as a mobile phone.

Music Bundles—Music products such as CDs, ringtones and digital downloads being bundled together.

The rates for the new categories involve the greater of a percentage of service revenue, total content costs (payments to record companies for sound recording rights) and, in the case of limited offerings, a per subscriber figure.

As to the actual royalties generated, physical and download sales are relatively easy to calculate. For example, 100,000 download single-track sales will generate \$9,100 in writer and music publisher income (9.1 cents x 100,000). Controlled composition clauses may reduce that amount with respect to physical sales, but in most cases, not for digital sales.

For all the other configurations, the payments to date have been small. For example, approximately 832,000 quarterly plays on one bundled subscription service might generate \$438 in total writer and publisher royalties with a per play rate of \$0.000527. The figures for a stand-alone portable subscription service for approximately 330,000 plays might currently generate approximately \$240 with a per play rate of \$0.000725. These royalties are arrived at after 25 different line item calculations which include service revenue, number of subscribers, label payments and performance royalties, among other fac-

tors...a not uncomplicated exercise. It is anticipated, however, that as subscription services become more successful and more prevalent, the payments will increase.

ASCAP/BMI/SESAC

The Performance Right—the world of ASCAP, BMI, SESAC and foreign societies—represents the most valuable composer and songwriter continuing source of income. Though traditional media (television, radio, etc.) have had their share of recent challenges, the area still remains strong as to overall license fees and composer and songwriter royalties, particularly if your works are part of a successful television show or a hit song on radio. The Internet and digital media area, on the other hand, has thus far not produced license fees or distributions of any significant nature.

To put this area into perspective, total ASCAP, BMI and SESAC annual receipts are in the area of \$2 billion. Of that amount, television (network, local and cable) represents approximately \$600 million, radio \$450 million, general licensing \$225 million, royalties from foreign societies \$700 million (most of it writer money as many publishers collect directly through sub-publishers) and new media in the area of \$70-75 million.

The majority of license fees in the online/new media area are the result of rate court decisions as well as settlements negotiated as a result of those decisions. Under the ASCAP and BMI consent decrees with the government, if a user and ASCAP or BMI cannot come to an agreement as to what reasonable license fees should be, either party can go to court (Southern Federal Court in New York) where a trial is held with a judge making the decisions as to what interim as well as final license fees should be as well as what is actually licensable. Rate court cases as well as settlements in the new media area have involved AOL, Real Networks, Yahoo, Netflix, Hulu, YouTube, AT&T, MobiTV, Verizon, Spotify, Ericsson, Rhapsody and Pandora, among many others.

Regardless of the size of the license fees (most deals in this area are confidential and the fees relatively small), major services and sites are being surveyed by the PROs and royalties are being distributed to composers and

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songwriters based upon the streaming of television shows, films, records and songs.

As to payments, total license fees from a service and the accumulation of streams are two of the primary factors considered. The type of use distinctions between theme, score and feature continue to apply in new media ASCAP, BMI and SESAC distributions. Other aspects of their television distribution systems though do not apply including Nielsen ratings, audience measurement, time of day factors, theme bonuses, etc.

Further, practically every current PRO traditional media license fee renegotiation or negotiation now covers online/digital items such as digital broadcasts, mobile wireless platforms, webcasts, and multicasts, among many others.

Video Games

Video game scoring contracts many times tend to be somewhat similar to feature film contracts in the sense that they are work-for-hire agreements and include all distribution platforms, media and systems "now known or hereafter invented" with fees based on a finished and accepted per minute of music basis, a package fee or the reaching of certain milestones in the process with backend royalties set forth in a schedule attached to the agreement or in the body of the agreement.

Songs, on the other hand, can generate significant continuing royalties based on the type of game they are in.

Most video games pay a one-time synch license fee to the publisher to put the song into the game, with no additional royalties. The term of the license is usually short (five to seven years instead of life of copyright, which is the norm for a feature film). The Master Use sound recording license is normally on a most favored nations (MFN) basis with the song.

Other types of games though (e.g., Dance Central, Guitar Hero, etc.) negotiate per unit royalties, per unit royalties with escalators, sales plateau increases as well as royalties based on a composition being downloaded by a

consumer into a game (the latter many times on a percentage of revenues versus a set penny per composition rate).

Some examples of these writer/publisher deals are:

1. 0-500,000 units sold = 1 cent per unit; 500,000-1,000,000 = 1.3 cents; 1,000,001 plus = 1.5 cents per unit.
2. \$10,000 to put the composition into the game; an additional \$4,000 at 350,000 units sold; plus \$5,000 for every additional 250,000 units sold.
3. Downloadable Content (DLC): 15-20% of net revenues as defined less third party distribution fees. Bundled compositions (2 or more compositions sold in a package) share pro-rata to revenue.

Motion Pictures

Most feature film scoring contracts are work-for-hire agreements and include all media and distribution platforms including the Internet. Composers need to look to their PROs for performance monies from traditional media as well as new media uses. The primary sources of this income include network, local, cable and foreign country television, pay per view and theatrical exhibition royalties from foreign country movie theaters (an average of 1% of the box office for all music uses).

In the case of pre-existing songs though, new language is being inserted into synch agreements to cover the online world. For example, a media clause in current synchronization licenses might read "distribute in any and all Media and by any and all means, now or hereafter known, including, without limitation all forms of television, all "on demand" services, all online, digital and wireless technologies and other transmissions capable of being experienced by means of any interactive devices or any future storage delivery and/or retrieved devices or systems." An additional clause stipulates that the "viewer is not invited to manipulate the composition in any manner which is not possible using traditional analog home entertainment equipment."

The amount of the synchronization fee depends on a number of factors

including how the song is used, the overall film budget, the timing of the use, whether there are multiple uses, whether uses are thematic or used over the opening or closing credits, the term and territory as well as any guarantee of inclusion on a soundtrack album.

Another valuable area is the licensing of existing compositions and master recordings and the additional fees for the out-of-context use in film trailers. The media can be all forms of television, videos, radio, online, digital and wireless, linear audio web streaming, etc. There may also be additional fees for its use in the "making of" programs and featurettes as well as home/personal entertainment media menus.

Advertising Commercials

For certain compositions (television theme songs, recognizable score, songs from films), the advertising market can be profitable depending on, among other things, whether it is a radio, television or internet commercial, a nationwide or limited territory campaign, whether there are options for other media and delivery systems as well as other countries of the world, whether lyrics are being changed or added and whether all advertising rather than only product category exclusivity is being requested.

As to some of the new types of agreement clauses brought on by the digital online world, the following example should help:

Agreement lists composition title and product name with a term of one (1) year with an option to renew for an additional year at a 15% increase. Territory is the United States and Canada with the world as it pertains to the Internet. Media includes all TV including network, syndication, cable and satellite use with Internet included but not limited to client, agency and third party websites. Included is a New Media App for iPad and industrial use.

As some commercials are being used in motion picture home videos, in motion picture theatres during previews and on mobile phones, rights for home video, theater promos and mobile phones may also be negotiated. Internet use should be non-exclusive and should be limited to streaming/non-downloadable use of the spot and subject to websites having a valid U.S. performance rights license and subject

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to the fees, rules and regulations of any foreign performance rights society.

Fees for well-known compositions in major campaigns can range from \$150,000 to over \$1,000,000 depending on the territory and rights granted. In addition, performance monies will also be generated by ASCAP, BMI and SESAC though the rates are on the low end of their payment schedules.

Apps

This new area of exploitation can be very valuable depending on the success of the individual app since the licensing formulae are usually based on a percentage of net receipts after the deduction of the distribution fee (30% in the case of iTunes) and, in some cases, the developer fee.

Musical compositions are licensed at either 25% or 50% of the net revenue with the primary question being the definition of net revenue (e.g., is a distributor fee being taken off the top or is there a distributor and developer fee being deducted). If a master recording is also involved, the fees are usually conditioned on a most favored nations (MFN) basis with the fee paid for the recording.

The platforms usually include all digital media such as the iPhone, Android, iPad, other mobile and hand-held devices as well as Internet and social networks and are from three to five years in duration but can be longer. Accounting is usually on a quarterly basis. Some agreements have the suggested retail price of the app actually in the contract (e.g., 99 cents for a two-song bundle, etc.) so that you know what the actual royalty calculation will be when a song is downloaded in the app. Others only specify the formula being used.

The following example should give some perspective as to a representative licensing formula in this area.

99¢	Retail Price
- 30¢	Distributor Fee (30%)
69¢	Gross
- 35¢	Developer Fee (50%)
34¢	Net
x 50%	Publishing Fee
17¢	Royalty

Interactive Dolls and Toys

Many of these types of uses involve children's products (Hasbro tooth tunes, pre-programmed instruments, animated pets, etc.). As to the rights granted, the license will specify how the composition will be used ("as part of a digital/voice music chip embedded in your product," etc.), indicate the territory and term of the license (U.S. and Canada, the world, 3 years with a sell off period, etc.) and a maximum duration of use (e.g., 2:00).

Writer and publisher royalties are usually either a negotiated per unit penny rate (e.g., 10-25 cents per unit but can be more) or a percentage of the wholesale or retail price. The licensee will be prohibited from changing the basic melody, altering the fundamental character of the music, changing or adding lyrics or using the title as the name of the product.

E-cards

Electronic cards represent an ever-increasing number of sales in the 5 billion unit greeting card business. The all format song licenses in this area define both the "physical everyday and seasonal card" and the electronic card that is "perceived via an electronic device and may be delivered via electronic transmission (e.g., via the Internet, mobile phone, cable television or other electronic delivery media not yet in existence)." Further, the song clip may only be distributed by either secure streaming or other secure file format intended to restrict further distribution or playback.

The territory for these deals is usually the world with a term of three to five years plus a sell-off period with a maximum sound duration specified (60 seconds) and a royalty of a percent-

tage of sales (e.g., 5%) or a per unit royalty (e.g., 15¢ per card). Many times consumers are given permission to sample the song on an online website to see if they want to purchase it. Masters are normally licensed on a MFN basis.

Ringtones/Ringbacks

Pursuant to the Copyright Royalty Board, ringtones generate a writer/publisher combined royalty rate of 24 cents per download. This rate is good until December 31, 2012, but an extension to December 31, 2017 is expected to be enacted. Based on ASCAP rate court decisions involving AOL, Real Networks, Yahoo, and Verizon, no performance right exists in the download of a ringtone. Previews of ringtones on a company's website though are licensable by the U.S. PROs.

Ringbacks on the other hand, are normally licensed as a percentage of the actual retail selling price to the consumer with a minimum royalty specified (e.g., 10% of the price to the consumer with a floor of 12.5 cents). All licenses have a sound duration specified and the territory is either the U.S., the U.S. and Canada or the world.

Direct Licensing

Performance Right Organizations (PROs) utilize various types of negotiated or court set license agreements with the users of music including the blanket license, the per program license, per segment license and "through to the audience" license. Regardless of these licenses, the contracts that writers and publishers sign with ASCAP, BMI and SESAC are non-exclusive and give them the right to direct or source license a work, thereby bypassing the PRO license entirely.

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Direct licensing has been around since at least 1950 and many television and film scoring and song contracts contain language covering situations as to what happens when a broadcaster does not have a current PRO license or when the PRO is prevented by law from issuing such a license. Various solutions are set forth including a negotiation "in good faith" to arrive at a fee, or an arbitration, or a reference to current PRO fees or no additional fee.

The direct license issue has recently been in the spotlight again due to the 2011 notification to ASCAP by EMI Music of their intent to withdraw from ASCAP the licensing of their online digital music rights with a similar 2012 notification to ASCAP and BMI from Sony/ATV as well as the 2010 ASCAP and BMI rate court cases with background music supplier DMX where judges approved a blanket license adjusted by the amount of music directly licensed by the user—a "carve out blanket license/adjustable fee blanket license."

To make intelligent decisions in the field, you need to know the traditional licensing structures of the PROs with their long history of negotiations, license fees, litigation and actual royalty payments, as well as the possible ramifications of a direct or source license as to the terms, payments, and other contractual obligations and considerations both in the United States and worldwide. Also important are whether the license provides for continuing royalty payments (i.e., "licensee shall

have no further responsibility with respect to U.S. performing right royalties") whether it affects additional media and areas of exploitation and how it affects any writers, co-writers, publishers or co-copyright owners. What rights are actually being delivered and whether one has the right to grant those rights is also an important consideration.

This information is essential regardless of whether you are happy with past or current PRO licensing or are in a situation where you are contemplating a direct or source license, have been asked to consider one, or are being forced to enter into one.

Summary

The online/digital world has changed how music is licensed, how contracts and deals are negotiated and structured and how composer and songwriter compensation is arrived at. This article has gone through many of the changes in the traditional world of music as well as showing new opportunities for music use created by the digital/online environment—all of which should be of help in understanding, surviving and succeeding in today's world of music. ■

Todd Brabec, former ASCAP Executive Vice President, and Jeff Brabec, Vice President Business Affairs BMG Chrystalis, are the co-authors of the book Music, Money and Success: the Insider's Guide to Making Money in the Music Business.

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