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Artists Press for Their Share

Many Musicians Say Record Companies Often Pocket Royalty Overpayments

By Hannah Karp

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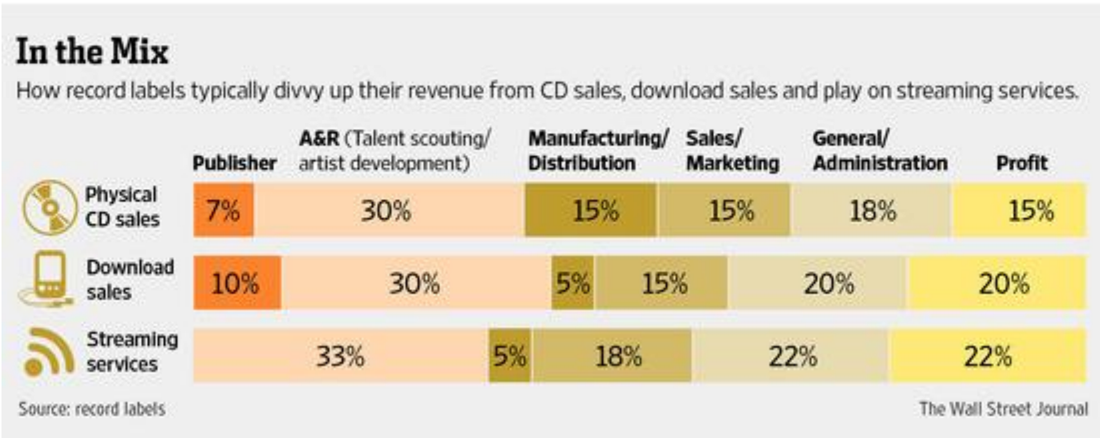
Bands like Bon Iver, shown, that record on indie labels are now being promised a share of 'breakage' money. As revenue from music-streaming grows, musicians are starting to shift their focus from their initial gripe (about how it pays a fraction of a cent per stream) to a tougher question: how their own record companies and publishers should be divvying up payments.

Record labels pay artists a fairly standard royalty rate on digital downloads and CD sales—generally between 10% and 20%, depending on the artist's star power. But when it comes to streaming through Spotify AB and other services, there is little agreement on how much to share with artists out of the revenue that labels get, especially when labels sometimes get money above actual royalties, as rights agreements often call for minimum guarantees.

The big record companies have mostly been applying their artists' existing royalty rates on sales to streaming, but there is wide variation. Some artists are negotiating to keep as much as 50% of streaming revenue, arguing that licensing their music to these services is more akin to placing it in a film or advertisement, in which case artists typically get half the fee.

Several independent labels have offered a 50-50 split on streaming to all their artists, though one of the biggest, Beggars Group, said recently it would be ending that practice because it was costing the label too much.



Subscription music services generated $1.1 billion last year for record companies, up from $734 million the year before—figures that don't include the common minimum guarantees paid to the labels, according to the International Federation of the Phonographic Industry. Though still small, subscription streaming is the fastest-growing piece of the $15 billion global recorded-music pie for labels and artists, as CD sales continue their yearslong decline and download sales begin slipping as well.

Music attorney Donald Passman said artists are likely to start negotiating higher royalty rates on streaming revenue than they get on sales, in part because streaming costs are lower.

"We're in early phase [of streaming technology] now, and artists are not getting paid what I think they will over time," said Mr. Passman.

One piece of the money discussion concerns a special area known as "breakage." Breakage involves the surplus funds that can exist when a music service's advance payment, or minimum guarantee, to a record company or publisher exceeds the royalties earned. How that money should be shared is an even thornier question.

Some streaming-service executives said it is common for the big record companies to demand advances far in excess of what they are likely to earn from actual royalties pegged to usage. While the most successful streaming services, such as Spotify, are unlikely to overpay for music, smaller startups could end up doing so, needing to secure rights to music as they struggle against their bigger competitors.

Smaller players such as Rdio, Microsoft Corp.'s Xbox Music and Nokia Corp.'s Nokia Music Unlimited, have guaranteed more to labels than they have generated in usage-based royalties, people familiar with the matter said. Such advance payments are usually made in a lump sum to cover the time span of a licensing deal, typically two to three years.

Earlier this month in Washington, where lawmakers are considering a broad overhaul of copyright law, indie label co-founder Darius Van Arman noted how significant breakage can be. Testifying at a music licensing hearing, Mr. Arman said that independent record companies were set to receive $1 million in breakage from two licensing deals. In one deal, he said, the breakage was more than half of what was earned in royalties, and in the second deal, the breakage was almost five times what was earned.

Google Inc. agreed in 2012 to pay Warner Music Group more than $400 million upfront to license the label's music for three years, for both its free YouTube site and its subscription offerings including a paid YouTube service, which has yet to launch. Should that amount exceed the royalties generated by actual song-playing, Warner Music intends to share the extra advance money with artists, as has been its recent practice, according to a person familiar with the matter, but record labels aren't necessarily obligated to do so.

The industry is shifting toward sharing more of such breakage, which has been amounting to tens of millions of dollars a year. In the past, Vivendi SA's Universal Music Group, the world's biggest record company, generally pocketed the breakage, according to a person familiar with the matter. But the company's current leadership intends to share breakage more evenly with artists, part of an effort to lure talent, this person said.

Warner Music and Sony Corp.'s Sony Music Entertainment have generally sought to divvy up breakage among their artists for at least the past five years, according to people familiar with the matter, though they keep the same slice of each artist's breakage as they do of the artist's record sales. Warner Music Group is owned by Access Industries.

More than 700 independent labels formally pledged last week through the Worldwide Independent Network trade group to share breakage from digital services with their artists.

But keeping track of micropayments is complicated, and there is little accountability, especially in small overseas markets, according to people close to some record labels. It can be especially difficult to know if foreign subsidiaries pocket advances from smaller regional or local music services, they said.Some artists signed to labels that claim to share breakage say they have never seen digital breakage show up on their income statements, though such an item could be easily missed, as the statement for a single work nowadays may tabulate hundreds of thousands of individual payments. When breakage is itemized on income statements, there is no detail about which service it came from, royalty accountants say.

One accountant said that music publishers—which represent songwriters—tend to be more opaque than record companies when it comes to how they calculate, collect and report streaming royalties, creating discrepancies between what two co-writers might earn in revenue from the same song. For example, in a case where two of this accountant's clients, signed with different publishers, co-wrote a song, one of the writers has earned $200,000 more from the same song over the past year than the other, this person said.

Sony/ATV Music Publishing Chief Executive Martin Bandier said his company didn't share extra advance money with songwriters. But, he added, there wasn't much to share: "The problem is we don't get a lot."