VIEWPOINT REED SMITH

MAKING A DEAL WITH DIGITAL

The dispute between YouTube and indie labels may be grabbing headlines - but that's just the tip of the tussle between rights-holders, artists and digital streaming services

DIGITAL

■ BY GREGOR PRYOR, HEAD OF MEDIA AND TECHNOLOGY PRACTICE AT REED SMITH LAW FIRM

It is said that the people who bite the hand that feeds them usually lick the boot that kicks them. As we see digital music move from an early adopter model to a mass market driver of growth and success in our industry, it's time we take a closer look at who is doing the feeding and who is doing the kicking.

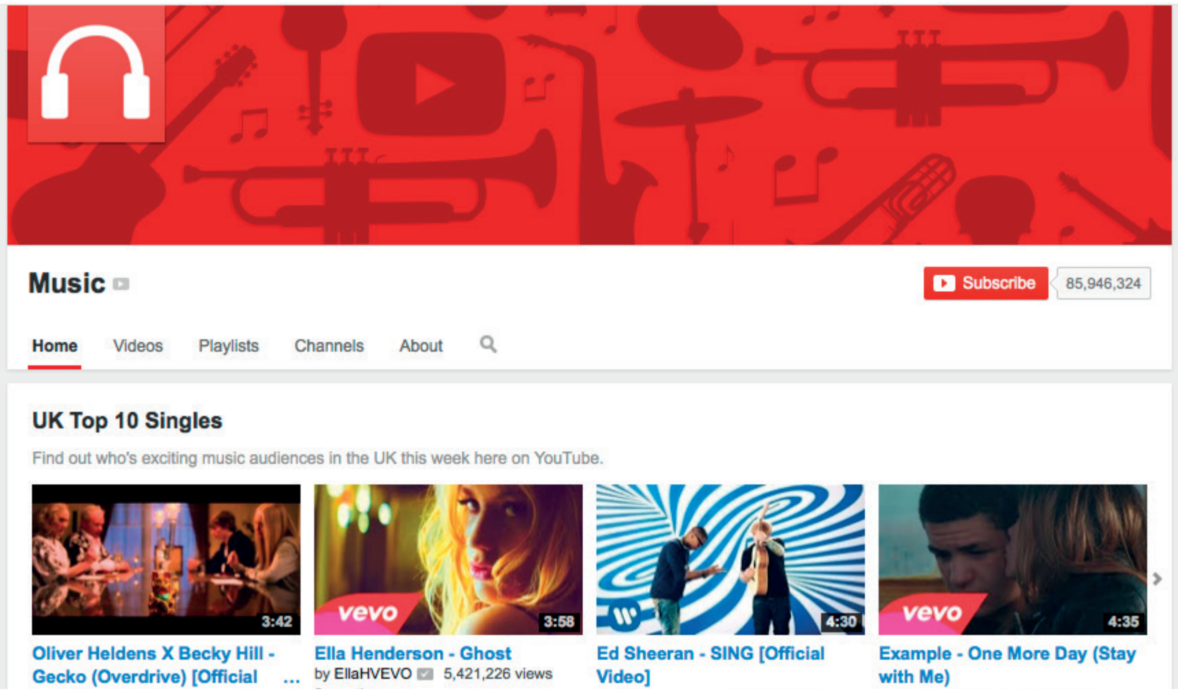
It was recently announced that on-demand music streaming data will count towards official UK chart rankings, alongside single purchases and downloads. This should not surprise anyone. As downloads decline and we move towards the fabled 'celestial jukebox' that consumers love, it's only natural that we measure the success of a song by how many times it is listened to. This metric recognises talent and artistic (and, indeed, commercial) endeavour on the part of artists, labels and publishers. It should result in a chart system that is more reflective of today's music market.

Nonetheless, it's clear that not everything is rosy in the world of digital streaming. First, a row has broken out between the independent labels and YouTube concerning the licence terms which Google, as owner of YouTube, is putting forward for smaller labels. Second, the artist community continues to be vocal in its claims that artists are insufficiently remunerated for streams of their songs on legitimate streaming services. Although neither of these arguments are altogether clear cut, there is merit in both of them: parts of the YouTube licence agreement, leaked online this week, are patently onerous and labels would be ill-advised to agree to them without negotiation; artists are not receiving a share of all of the money received by labels and publishers from digital services and do not have transparency concerning how royalty streams are derived from them.

There are, however, more deep-rooted problems. From our time advising online and mobile music companies on hundreds of licensing transactions, we have experienced:

- Rights-holders claiming royalties for songs where they cannot demonstrate that they own or control them;
- Insistence on most favoured nations clauses which have the effect of raising royalties to the highest levels, on dubious legal footing and often dressed up as something entirely different;
- Unequivocal negotiations, on a 'gun to the head' basis; either agree to our over-reaching terms or remove our content (and suffer the death of the service);
- Failure to send royalty invoices to services for months, sometimes years;
- Refusal to allow recoupment of advances, while simultaneously insisting on minimum guarantees far in excess of even the most optimistic growth projections.

One of the most pernicious trends of all, though, is the sharp increase in royalty pricing in the last five years, against a backdrop of static consumer pricing for digital services. Publishers are the most eager protagonists of this, believing that they deserve to receive the same royalties as the labels. Labels, for their part, try to control and throttle services rather than let them adapt to serve consumers. Meantime, services are resigned to making small revenue margins while making significant capital investments. The majority of digital music services operate at a loss.



ABOVE
YouTube: The Google-owned platform has been at the centre of the latest streaming dispute between services and rights-holders

"We need a positive approach to licensing that rewards artists and services alike"
GREGOR PRYOR, REED SMITH

Hopefully, the days of the grizzled, under-performing fat cat music executives living off the sweat of the artist's brow whilst plundering the company coffers are numbered. It is invigorating to see artists holding labels and publishers to account. Artists should celebrate success and achievement and punish poor label or publisher performance by moving their rights somewhere else. That said, they also have a duty, along with their managers, to negotiate fair royalty terms at the outset, along with transparent accounting and audit procedures. It's no use complaining that you don't receive enough money when you have no contractual right to receive it in the first place.

In hip-hop parlance, by squeezing the digital services and insisting on royalty increases and huge advances and guarantees for limited licence agreements, our industry is taking the dumb, short, easy money. Entrepreneurs like Daniel Ek, Janus Friis, Alexander Ljung and Sean Parker have taken big bets on the growth of the digital economy, persuading high-profile investors to back their ideas and long-term vision. Think that's easy?

Y-Combinator is, according to Forbes, one of the world's leading start-up incubators and accelerators. A footnote in their website concerning how to work alongside investors is revealing. It says "record labels… are effectively a rogue state with nuclear weapons. There is nothing we or anyone else can do to protect you from them, except warn you not to start startups that touch label music." Investors know that the last ten years are littered with failed music start-ups.

The multi-nationals are also wavering. While Google is maligned for its attitude towards indie labels, it still continues to invest in YouTube and has launched Google Play, ploughing billions of dollars into the music industry. Apple has effectively doubled down with its acquisition of Beats. But other technology companies are less keen, licking their wounds and looking to other forms of entertainment to drive revenue. Broadcasters focus instead on sport. Other device manufacturers turn away from digital music. Facebook and Twitter, controlling the biggest and most engaged audience online, rely on other services to power music.

There is much to celebrate. Many of the executives in digital divisions of labels and publishers are an enlightened breed, keen to try licensing innovative new models on fair, reasonable and non-discriminatory terms. Major artists are recognising their value in the food chain, achieving a seat at the table in negotiations and requiring transparency and fairness. Some digital services are growing at a phenomenal rate, even though they are not yet making money.

There is still, though, much change needed. We have an opportunity to bring exciting new music to the largest audience ever possible in the history of mankind. To achieve this, we need strategic, long-term vision and a positive approach to licensing which rewards artists and innovative services alike, while allowing fair compensation to rights-holders who try to feed the digital economies rather than kick them.