

**ENCLOSURES TO  
BIEM COMMENTS VERSION 1.5 – 28 August 2002**

**ENCLOSURE 1 :**

**Extract of the Minutes of the BIEM/IFPI Negotiating Committee (London, 11 May 1983) – Original version**

“Ensuite, M. GOLDSTEIN a indiqué que le principe des déductions pour pochettes et cassettes devait absolument être maintenu parce que, les contrats entre producteurs et artistes comportaient le mêmes système de déduction, à quoi M. WILLEMSSEN répond que le BIEM n'a jamais négocié pour le compte des artistes, de sorte que l'IFPI ne peut lui opposer une situation à laquelle il est totalement étranger. »

ENCLOSURE 2 : Report from Mr Brian Hindley

Draft

**COMPETITION ISSUES  
IN THE  
ADMINISTRATION  
OF  
MECHANICAL RIGHTS**

by

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## INTRODUCTION

The owner of a copyright in a musical composition or a song has a legal right to authorise and to forbid the use of the copyrighted work in sound recordings -- a “mechanical right”. Hence, producers will seek consent to use works covered by copyright; and consent will normally entail a fee of some kind, usually a royalty.

Mechanical rights are typically administered by a mechanical-rights collecting society (a society). A society holds a repertoire of mechanical rights, derived from the copyrights of its members -- authors, composers and publishers to whom authors and composers have assigned their rights. The society issues licences to record works in its repertoire and it collects the corresponding royalties. After deducting a commission, it then distributes the royalties to the owner of the relevant copyright. Societies are typically based on a particular national jurisdiction, and most national jurisdictions have only one society.

Most Societies, however, are members of the Bureau International des Sociétés Gérant les Droits d'Enregistrement et de Reproduction Mécanique (BIEM). Each member of BIEM agrees that the recording of any work in its repertoire can be licensed by any other member. In effect, therefore, each BIEM member is able to issue licenses, not merely for works in its own repertoire, but for any work in the repertoire of any BIEM member.

The repertoires of different Societies, however, vary greatly, and some are more valuable than others. Why should society A, whose repertoire contains many valuable and widely-used works, give society B the right to licence works in that repertoire solely on the basis that B allows A to licence works in its much less valuable repertoire? Further conditions are needed to make the BIEM arrangement feasible.

The primary condition is that BIEM members agree to charge a standard rate of royalty for licences<sup>1</sup>. Thus, collecting society A can accept the BIEM contract secure in the knowledge that society B cannot undercut A in the sale of licences for the use of works in the A repertoire.

This note examines competition issues that might arise from this set of arrangements. The BIEM standard contract, however, is based upon two antecedent institutions: copyright and national collecting societies. Both have aspects that call for clarification, seen from the standpoint of competition policy. Before turning to the central issues, therefore, these aspects are briefly discussed.

## COPYRIGHT AND COLLECTING SOCIETIES

Without copyright -- if musical works could be freely recorded, without authorisation from any person beyond the management of the recording company -- authors and composers would have difficulty in obtaining a remuneration when their work was used in sound recordings, and might well find it impossible to obtain a remuneration.<sup>2</sup> Without collecting societies, they would find it difficult to collect the remuneration that the institution of copyright makes possible and to control that the use of their works is in line with the authorisation granted.

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<sup>1</sup> BIEM members can “depart from the standard contracts established by BIEM to the extent that they are subject to legal provisions of a compulsory nature” [Article 7 (4) of the BIEM Statutes]

<sup>2</sup> In certain circumstances, composers and authors may be able to obtain remuneration for the recording of *new* works, even in the absence of copyright. In the nineteenth century, European authors of books received substantial payments from publishers in the US even though their works could not be copyrighted in the US at the time. US publishers valued the ability to be the first with a book on the US market, and they paid to obtain that position.

## **Copyright**

A world without copyright has an element of superiority over one with copyright. If authors and composers receive less payment, or no payment, for work reproduced in a recording, for example, the producer of the recording will have to pay less to make it, and may therefore sell copies of the recording for less. The counterpart of that advantage, though, is a heavy cost.

The cost derives from the fact that if composers and authors are not paid when their work is used in recordings, the incentive to create is diminished, and fewer songs and pieces of music will be created. Recordings of such songs and compositions as are still produced may cost less to produce, since the authors and composers do not have to be paid, and they might therefore be sold at a lower price. But the flow of new songs and compositions is likely to be smaller. Seen from that standpoint, a world without copyright is likely to be impoverished, relative to one with copyright.

Most countries have decided that they prefer to encourage new composition, even at the cost of more expensive recordings. Accordingly, they have enacted copyright laws.

Despite that decision, though, much discussion of issues relating to copyright and other intellectual property still turns on the trade-off between the price of goods and services subject to intellectual property rights and the flow of new goods or services of that type. Often, discussants fail to acknowledge that they are in fact talking about the trade-off.

Cheaper recordings can always be obtained by reducing the returns to composers and authors of songs. That in itself, though, is a poor reason for restricting the scope of copyright or limiting the ability of the owners of copyright to exploit the rights. Cheaper recordings obtained by reducing remuneration to right owners will serve the public interest only if lower prices of current recordings create a social benefit that is greater than the social cost imposed by a reduced flow of original works in the future.

It is not easy to demonstrate that a proposed subtraction from copyright will have such a beneficial outcome, when all effects are accounted for; nor is it easy to show the reverse. The burden of proof is therefore hard to carry, and the side that is deemed to bear it will typically lose any dispute.

## **Collecting Societies**

A right of authors and composers to prevent unauthorised recording of their work is not sufficient to ensure that authors and composers are rewarded when their work is used in recordings. The right to prevent unauthorised recording implies that composers and authors can negotiate the conditions under which they will authorise reproduction of their work, but it does not imply that they have the time and energy and skills to successfully undertake such a negotiation, or to effectively enforce its outcome.

Negotiation of conditions, though, is likely to be time consuming and costly. If the negotiated conditions are to be meaningful, moreover, the adherence to them of authorised producers of sound recordings must be ensured, and action taken against breaches, and infringement by unauthorised producers of sound recordings must be identified, and action taken against the infringement. These are expensive activities, especially in a business like sound recording, that is world-wide in scale.

Performance of these tasks, however, is essential to the effective functioning of the copyright system. There is a clear case for the holder of the copyright to employ an agent. Typically, that agent is a mechanical-rights collecting society.

## **COMPETITION ISSUES**

Neither the intrinsic nature of copyright nor that of collecting societies seem to fall within the proper

scope of competition law. But the fact that there are a number of societies means that competition between them is in principle possible. That possibility inevitably prompts the question as to whether competition between them -- or more competition between them -- might be beneficial in some dimension, and, if so, whether such beneficial competition is blocked by membership of BIEM.

### **Competition between collecting societies**

Broadly speaking, competition between societies is possible on two fronts. They can compete:

- (a) for contracts with record producers; and/or
- (b) for the mandates of authors and composers.

These two dimensions are connected: the mandates of authors and composers being necessary to win contracts with record producers (and *vice versa*). Competition in the two dimensions, however, raises different issues.

#### ***Competition for contracts with record producers***

In the absence of a BIEM minimum royalty, competition between societies for contracts with recording companies raises the possibility that the royalty rates of authors and composers will be driven down. A fall in royalty rates is not the same thing as a fall in remuneration to authors and composers, but it clearly raises the possibility that their remuneration will fall.

Any discussion of competition between societies must take into account the possibility that competition will reduce the remuneration of authors and composers. To provoke such a fall in their returns would on its face be inconsistent with the public-policy objective of copyright law, which is to increase revenues to authors and composers.

#### ***Competition for the mandates of authors and composers***

Competition for the mandates of authors and composers, on the other hand, is in itself likely to further the public interest expressed in copyright laws. An owner of a mechanical right who is a member of a society receives a remuneration equal to the royalties received by societies for the use of the work covered by that right, less the commission charged by the society. Societies competing for the mandates of authors and composers have an incentive to attract authors and composers by charging a lower rate of commission, and therefore an incentive to reduce administrative costs.

The general issue is often referred to as “the principal-agent problem”. Agents are hired by principals to serve the interests of principals. But agents have interests of their own, which are not usually the same as those of principals. Agents may therefore sometimes be inclined to pursue their own interests, at the expense of principals -- the principal-agent problem arises.<sup>3</sup>

Competition between agents is a possible means of limiting the ability of agents to act against the interest of principals. In the case of societies (agents) this outcome is not merely a private concern of holders of copyright (principals): it also has a substantial public-interest component, which derives from the fact that copyright is established for the benefit of authors and composers. If societies take an unduly high proportion of the income stream generated by mechanical rights, authors and composers receive an unduly low proportion; a situation that would run counter to the aims of copyright.

The consequences of competition between societies depend, however, on whether or not there is a

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<sup>3</sup> Dental patients who wonder whether their expensive dental work is really necessary are concerned with the principal-agent problem; which sometimes also troubles, for example, the clients of lawyers; persons using professional agents to sell houses; and shareholders, when they wonder in whose interest “their” managers are running “their” company.

standard royalty rate -- that is to say, in European terms, whether or not BIEM is permitted to negotiate and enforce such a standard rate. The easiest case is the one which in fact exists, in which the BIEM standard contract determines royalty rates. After a brief discussion of it, the more difficult case in which there is no agreed royalty rate is taken up.

### **Competition when there is an agreed royalty rate**

In the presence of the BIEM standard contract, competition between societies cannot erode the agreed rate. Moreover, as a consequence of the single royalty rate, all societies in effect share a common repertoire. societies can compete to win contracts from recording companies, but they cannot compete on the basis of price (that is, royalty rates), and they cannot compete by offering different repertoires. Competition between them must, therefore, be on the basis of levels of service to producers of sound recordings.

Societies can also compete for the adherence of composers and authors. In this competition, price *can* be a factor -- as can levels of service, though, in this case, service to copyright owners. Price can be a factor because the members of a society receive the BIEM royalty *less* the commission charged by the society to cover its costs of administration. A society that reduces its costs of administration can charge a lower commission and so offer greater net remuneration to copyright holders, attracting them to membership of it.

### **Competition when there is no agreed royalty rate**

The situation in which there is no BIEM royalty rate is more difficult to analyse. In part, that is because the situation is hypothetical; in part because it yields many more possible permutations than the case in which the BIEM contract regulates relations between societies; and in part because the outcome depends crucially on factors beyond the market for mechanical rights -- in particular, technology and the actions of competition authorities.

Whatever the details of the final outcome of removing the BIEM standard contract, however, the market for mechanical rights will possess -- or fail to possess -- certain characteristics. If there is no agreement on rates of royalty between societies:

- (a) Societies will not share their repertoires;
- (b) hence, competition between societies will entail competition between rival repertoires; and
- (c) not only will there be no agreed BIEM royalty rate -- there is no ground for a presumption that a society will charge the same royalty rate for all of the works in its repertoire; nor even a basis for believing that it will charge a fixed royalty rate for any one work.

#### **(a) *No sharing of repertoires***

The right of a BIEM member to licence works in the repertoire of other members, is conditional upon agreement that the same rate of royalty is collected whichever BIEM member issues them. There is no basis other than a uniform and agreed rate of royalty on which that reciprocal outcome could be achieved: society A will not agree to society B issuing licences for recording of works in the repertoire of A if B can then charge a lower rate of royalty than A.

Even if societies were willing to offer each other a right to issue licences for works in their repertoire in the absence of an agreed royalty rate, the outcome of competition between societies to issue licenses for the same works without an agreed royalty rate probably would be a general fall in royalty rates and a reduction in the revenues of authors and composers. In terms of public policy, this outcome is not desirable -- the object of copyright is to *prevent* remuneration of holders of

copyrights being determined by freely-operating competitive processes.

The collapse of co-operation that would follow the removal of a common royalty rate has another economic consequence, in the form of increased transaction costs. Without the standard contract, a producer of sound recordings will often have to deal with several societies to obtain permissions for a single sound carrier. With the standard contract, producers of sound recordings can obtain all of the licences they need from one society.

The requirement of dealing with several societies is likely to bear most heavily on small and locally-based producers of sound recordings. The requirement would therefore create a barrier to the entry and expansion of such companies and would reinforce the global dominance of the five major producers of sound recordings (Universal; EMI/Virgin; Warner; Sony; and BMG, who between them have about three quarters of the world market for sound recordings).

**(b) Competition between repertoires**

Without sharing of repertoires, one society will try to promote works in its repertoire, at the expense of those in other repertoires. Royalty rates will inevitably be a part of this competition.

**(c) Different rates for different works in the same repertoire**

The implication of competition between repertoires is that a substantial *ad hoc* element is likely to enter the pricing of musical works.

In the current situation, royalty rates are not open to negotiation. If there were no BIEM standard contract, however, the royalty rate for any particular work will be a matter of negotiation between a producer of sound recordings and the society of which the right owner is a member. Such negotiations are unlikely always to end with the same royalty rate being charged. A society will therefore have no royalty rate that is standard and given. At best, a society will state a royalty rate as its standard, but in fact will offer a variety of discounts, so that the stated rate is an aspiration, not a reality.

More complicated pricing structures may appear. A protected musical work or fragment has the characteristic that it does not cost a society (or the composer or author) anything to authorise a further copy -- marginal cost to them is zero. That situation is frequently associated with multiple prices (for example, train or airline tickets), or with quantity discounts. In the absence of the BIEM standard contract, it is entirely possible that such complex pricing schemes will develop for mechanical rights.

The idea of “the” royalty rate for the use of works in a particular repertoire has no clear meaning in a world in which the negotiated royalty rate varies between different works in the same repertoire, and may even vary for the same work. Whatever definition of the phrase is used, however, there is no ground for a belief that it will be standardised across repertoires.

Diversity of royalty rates is not necessarily undesirable in itself, from an economic standpoint. Diversity, however, will have consequences that some will regard as *politically* undesirable. The European Commission and the member states of the EU, for example, may desire a state of affairs in which all authors and composers, whatever their member state of residence, receive the same royalty rate. Clearly, however, that cannot be guaranteed in the world described above.

EU members may be willing to accept a situation in which royalty rates differ, so long as there is no bias for or against composers and authors from particular member states. In the absence of a BIEM-standard royalty rate, however, not even that can be guaranteed. Whether or not there is a BIEM standard royalty rate, an author is probably better off, other things equal, to work in a language that has many native speakers; and better off still if that language is a widely understood and widely used as a second language. With a BIEM standard royalty rate in place, however, this advantage cannot



translate itself into differences in royalty rate: without such a standard royalty rate, it can and may display itself in royalty rates for songs which differ systematically between languages.

### **Other factors affecting the outcome of competition without BIEM**

These characteristics, however, might be affected, and even obliterated or reversed, by a number of other factors. Two of these are especially important.

#### ***Tendencies towards amalgamation of societies***

A possible long-run outcome of competition between societies in the absence of the BIEM standard contract, unless the competition authorities prevent it, is that competing societies merge themselves into one super-societies (or, possibly, more than one, but with broadly non-competing repertoires -- one for “serious” music; one for pop; and so on). Such an EU-wide (or wider) organisation might then restore standard royalty rates. That would falsify some of the comments above about the effects on the market of an absence of BIEM.

More importantly, though, it would call into question any competition-policy rationale for restricting the BIEM standard contract in the first place. It is difficult to see how a single super-society could be preferred to multiple societies co-ordinated by BIEM from the standpoint of competition policy. Indeed, a super-society would do away with the possibility of competition between societies for the accounts of authors and composers, and therefore would arguably be inferior to multiple societies for authors and composers.<sup>4</sup>

Intermediate steps might precede the emergence of a super-society; and might produce some of the same outcomes even without the creation of a super-society. For example, pairs or groups of societies might create alliances between themselves. Any such movement in the direction of re-creating the BIEM structure, however, would call into question the good sense of abolishing that structure in the first instance.

Competition authorities, of course, might block developments of this kind, refusing to countenance the creation of a super-society or the cementing of alliances that might take the market for mechanical rights in that direction. Such a stance on the part of competition authorities, however, would again bring into question the sense of abolishing the BIEM structure, under which neither of the developments to which competition authorities might object is necessary.

#### ***Competitive structure of the record industry***

At the moment, the record industry is a long way from the textbook model of perfect competition: as noted below, roughly three quarters of the global market for sound recordings is held by five companies (Universal; EMI/Virgin; Warner; Sony; and BMG). In itself, this fact sharpens some of the points made above: an industry with such a concentrated structure, for example, clearly has the potential to exploit to the maximum divisions and competition between societies.

The record industry, however, may be affected by new technologies of sound recording and new means of distributing sound recordings (in particular, the internet). In due course, these new technologies may make possible a more competitive sound-recording industry.

Low costs of obtaining licences to record will facilitate such a development. The need to obtain permissions and licences from a number of different society, and possibly to negotiate different conditions for each licence, favours large producers over small, and therefore the existing less-than-

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<sup>4</sup> “Arguably inferior” because such a super-society might be able to charge producers of sound recordings higher royalty rates than prevail when there are several societies. A super-society exploiting its position could take a higher rate of commission and still leave copyright holders better off than they are with several societies.

perfectly-competitive structure of the industry producing sound recordings over the structure that might emerge if new entrants to the industry faced low instead of high transactions costs.

By reducing transaction costs, therefore, the BIEM standard contract may facilitate the appearance of a more competitive industry. There can be little doubt that such a development would benefit both the creators of works recorded *and* purchasers of recorded music.

### **CONCLUDING COMMENT**

Intellectual property rights are created to make competition less perfect than it would otherwise be. Tension between the objectives of competition policy and the aim of rewarding the creators of material subject to copyright is inevitable.

Ways of resolving that tension that are superior to the BIEM standard contract, however, are difficult to identify. One side of the copyright trade off can always be favoured over the other, but, such arguments aside, the BIEM standard contract appears to yield benefits, both economic and cultural, that cannot be obtained in any other way.

ENCLOSURE 3 : Letter from R. Mooij to G. Taylor



## MEMORANDUM

To : Geoff Taylor - IFPI  
CC : PPD-ARP working group BIEM

From : Ronald Mooij

Date : 3 September 1999

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Dear Geoff,

Below is a comparison between the formulas of royalty calculation, based on PPD and on ARP, assuming that an eventual changeover will be done on the basis of the maintenance of the economic status quo.

**PPD model:**

$((\text{PPD} - \text{Packaging deduction}) - \text{Adjustment for discounts}) \times 11\%$

or

$((11\% - \text{Packaging deduction}) - \text{Adjustment for discounts}) \times \text{PPD}$

**ARP model:**

$((\text{ARP} - \text{Packaging deduction}) - \text{Adjustment discounts outside invoice}) + \text{uplift}) \times 11\%$

or

$((11\% - \text{Packaging deduction}) - \text{Adjustments discounts outside invoice}) + \text{uplift}) \times \text{ARP}$

Whereas:

PPD is currently defined in the standard agreement.

Packaging deduction is an estimated value, negotiated for each contract period

Adjustment for discounts is an estimated average value negotiated for each contract period.

ARP remains to be defined (cash-in, or invoiced price)

In the case of ARP, the calculation of the packaging deduction should be recalculated on the basis of a study into the actual cost of packaging.

Adjustment for discounts granted outside the invoice should be defined, and is a figure that will be different from company to company.

Uplift is an adjustment to bring the result of the calculation back to the same money value as in the case of a royalty calculation on the basis of PPD, this will also vary from company to company, depending on the value of adjustments for discounts granted outside the invoice.

### **Retentions**

Retentions to allow for returns etc. are not taken into account in both calculation models, however the retentions should be totally redefined in the case of a calculation based on the ARP, to allow for factors that are currently irrelevant. Revision on the basis of the final definition of ARP.

With best regards,

Yours sincerely,

Ronald Mooij

## ENCLOSURE 4 :

**CONSUMER ELECTRONICS RETAIL DISTRIBUTION**

*Changes in product mixes, demographic shifts due to an ageing population, ever increasing space requirements and changes in channels of distribution such as Internet and TV shopping all represent significant challenges to consumer electronics retailers.*

- These factors, coupled with increasingly intense competition within the sector, mean that the global consumer electronics retail environment continues to be extremely tough. For the larger retail groups, geographic expansion, both within their own immediate local markets and on a global level, combined with a wider range of product offerings, has been the way forward.
- Non specialist retailers such as supermarkets and hypermarkets have also increased their level of CE activity. These stores tend to be very price aggressive, often using low priced CE products as ‘call birds’ to generate store traffic for their main product sectors.
- The smaller independent retailers, whether truly independent or a part of buying/marketing groups, have continued to see their share of the market decline. These retailers do not have the financial capability to match the ranges or prices of the large retailers.
- Online activity continues to have an impact on the market. Initially, Internet sales were through ‘first mover’ dot coms, most of which have now folded. However, their place has been taken by the traditional ‘bricks and mortar’ retailers, the majority of which have now developed some kind of online capability.

*Major retailers go global.*

- Global expansion is becoming a key way for the major retail groups to increase their turnover. China, South East Asia and South America are seen as major growth areas by most retailers due to the fact that the retail distribution environment in these regions is less developed.
- US mass merchandiser Wal-Mart currently operates 17 stores across Asia and 545 in South America. It has also moved into the European market, primarily the UK and Germany, by investing in local supermarket chains.
- Many of the major European hypermarkets/supermarkets – which for years have been important in their own territories – have expanded outside their domestic markets. This is particularly the case with the French hypermarkets Carrefour and Auchan. Carrefour has been the most aggressive of the two, operating 641 stores in South America, 103 in Asia and three in Japan, compared to Auchan’s seven in South America and 19 in Asia. (Auchan does not currently operate any stores in Japan.)
- Although UK based Kingfisher’s main activity is currently focused within Europe, it is also beginning to move into other markets within Asia and Latin America, while Germany’s Metro is making expansion into Asia its major priority.
- As stores become more active in the global market, they are increasingly looking to alter their purchasing policies. Many retailers have moved towards more centralised purchasing because it is felt that this offers them the best system for negotiating discounts, as well as being able to keep control of all the products that they stock.

*Buying groups.*

- Many small independent dealers use the purchasing power of buying groups to compete with the major chains. This provides them with the opportunity to use a much larger brand name and to benefit from a group’s buying strengths and co-operative advertising. In some cases they also get access to exclusive products and/or deals.
- These groups are generally co-operative purchasing arrangements between consumer electronics

retailers, although some are now including co-operative operational support and marketing.

➤ The world's largest buying group is Expert Global Inc., which has 7,332 stores in 22 countries. Of these, 3,073 are in Europe. Expert's closest competitors are Electronic Partner with 6,500 stores and Euronics International BV, which has in excess of 6,000 stores. Both Electronic Partner and Euronics operate only in Europe.

*The RETAIL DISTRIBUTION MARKET REPORT is published as part of Understanding & Solutions' Digital Consumer Electronics and Home Entertainment Watch service. It provides an overview of the consumer electronics retail environment in Europe and the USA, and reviews the performance of the key consumer electronics retailers and retail groups.*

ENCLOSURE 5 : Australian Copyright Tribunal decision



## Copyright Tribunal

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### ***Universal Music Australia v EMI Music Publishing Australia Pty Ltd [2000] ACopyT 5 (14 June 2000)***

Last Updated: 16 June 2000

#### **COPYRIGHT TRIBUNAL OF AUSTRALIA**

#### **Universal Music Australia v EMI Music Publishing Australia Pty Ltd**

#### **[2000] ACopyT 5**

**COPYRIGHT TRIBUNAL** - mechanical royalties - application for determination of amount of royalty and manner of payment - interim orders - nature of power - whether restricted by relief that may be granted under [ss 152A](#) and [152B](#) of the [Copyright Act 1968](#) (Cth)

[Copyright Act 1968](#) (Cth) [ss 55](#), [152A](#), [152B](#), [160](#)

*Owners of "Shin Kobe Maru" v Empire Shipping Co Inc* (1994) [181 CLR 404](#), referred to

*Reference by Australasian Performing Right Association Limited* (unreported, Copyright Tribunal, 7 October 1994), applied

#### **UNIVERSAL MUSIC AUSTRALIA and Others v EMI MUSIC PUBLISHING AUSTRALIA PTY LIMITED and Others**

**CT 2 of 1999**

**TRIBUNAL: FINKELSTEIN DP, PROFESSOR PEARCE, MS BOWNE**

**DATE: 14 JUNE 2000**

**PLACE: SYDNEY**

**IN THE COPYRIGHT  
TRIBUNAL**

CT 2 of 1999

**BETWEEN:**

UNIVERSAL MUSIC AUSTRALIA and Ors  
Applicants

**AND:**

EMI MUSIC PUBLISHING AUSTRALIA PTY LIMITED and  
Ors

Respondents

**TRIBUNAL:** FINKELSTEIN DP, PROFESSOR PEARCE, MS BOWNE

**DATE:** 14 JUNE 2000

**PLACE:** SYDNEY

## REASONS FOR DECISION

### THE TRIBUNAL

1 The exclusive right of songwriters and composers to authorise the mechanical reproduction of their work is subject to the compulsory licensing system in the [Copyright Act 1968](#) (Cth). The licence system has its origins in the Berne Convention for the Protection of Literary and Artistic Works 1886 and was first introduced in Australia when the [Copyright Act 1912](#) (Cth) made applicable the [Copyright Act 1911](#) of the United Kingdom. An Australian manufacturer is entitled to reproduce a musical work by making a record, (which term includes a compact disc and a cassette tape) upon compliance with the conditions in s 55. In return for the licence, the manufacturer must pay a royalty to the owner of the copyright in the musical work. In the absence of an agreement or a determination by the Copyright Tribunal, the royalty is an amount equal to 6.25 per cent of the retail selling price of the record.

2 Songwriters usually assign their copyright in a musical work to a publisher. The terms and conditions of the assignment will vary from case to case, but it is a common feature of such agreements that both the songwriter and the publisher will take a share of the royalty. A division of 80 per cent to the songwriter and 20 per cent to the publisher is not uncommon, although in the early days of the recording industry the position was much less favourable to the songwriter.

3 Since the 1970s various agreements have regulated the payment of royalties by record manufacturers to most copyright owners. The agreements were negotiated by representative organisations, the principal bodies being Australian Record Industry Association Limited (ARIA) representing approximately 80 record manufacturers and Australian Musical Copyright Owners Society Limited (AMCOS), whose business is managed by Australasian Performing Right Associated Limited (APRA), representing most publishers.

4 The latest agreement was made on 20 April 1990 and amended by Heads of Agreement and Further Heads of Agreement, each dated 10 May 1995. The term of the agreement expired on 31 December 1999. The parties, through their representative organisations, have been unable to complete negotiations on a further agreement. For this reason the manufacturers have applied to the Tribunal under s 152A, to determine the amount of royalties to be paid to the owners of copyright for a period of not less than four years commencing on 1 January 2000 and under s 152B, to determine the manner in which the royalties are to be paid.

5 The hearing of the application will occur early next year. In the meantime, however, ARIA contends that an interim arrangement should be put in place and this is the matter that is presently before the Tribunal. The power of the Tribunal to make an interim order is found in s 160 which provides:

*"Where an application or reference is made to the Tribunal under this Act, the Tribunal may make an interim order having effect until the final decision of the Tribunal on the application or reference."*



The precise ambit of this power will need to be considered.

6 Before considering whether an interim order should be made pending the resolution of the applications under ss 152A and 152B, it is necessary first to explain the principal features of the expired agreement. We should point out that the agreement is a detailed and comprehensive document comprising 26 paragraphs, many of which contain sub-paragraphs, and 12 schedules. It is the product of lengthy and detailed negotiations. There are many provisions in the agreement which the Tribunal would not have the competence to order in an application under s 152A or s 152B. What follows are the main elements of the agreement before it was amended.

7 The royalty payable on records made in or imported into Australia and sold by wholesale was 10 per cent of the published price to dealer (commonly referred to as PPD), being the published catalogue price of the record including the cost of insurance and freight and any surface charges but excluding sales tax. The royalty payable on records made in Australia or imported into Australia and sold by retail was 7.28 per cent of the recommended retail price, being the maximum suggested selling price, excluding sales tax. The royalty payable on records sold by wholesale or retail was to be no less than 1 cent in respect of each musical work included on the record. No royalty was payable on promotional records. Promotional records were defined as records disposed of at no charge. They included records supplied to a radio or television broadcaster or to the operator of a venue at which records were played for entertainment. The manufacturers were entitled to a credit against royalty in respect of records supplied on a sale or return basis, if those records were returned to the manufacturer. In the case of records that were exported for sale, no royalty was payable when exporting to specified countries. In all other cases the applicable rate of royalty was payable except that the list price or the recommended retail price was the invoice price plus 20 per cent. Specific provision was made for the calculation of royalty on records imported to satisfy a specific order by a member of the public. One element in the calculation was the list price or PPD. Records in the form of compact discs attracted royalty at 90 per cent of the applicable rate.

8 The amendments that were introduced by the Heads of Agreement included the following. The rate of royalty on records sold by wholesale was reduced to 9.306 per cent of the list price. The rate of royalty on records sold by wholesale was reduced to 5.73 per cent of PPD including sales tax, or 6.4 per cent of recommended retail price excluding sales tax. The rebate on compact discs was removed. There was a change to the definition of PPD to take account of the situation where there was more than one catalogue price. The new definition also provided that discounts, incentives, bonuses and the like were not to be taken into account. The minimum royalty was increased to 5 cents with different rates for compact discs and cassette tapes.

9 The reason why the representative organisations are unable to reach a new agreement for the payment of royalties is their disagreement on whether it is appropriate to continue to use the list price as the basis upon which the royalty is to be calculated for records that are sold by wholesale. Wholesale sales, in particular the wholesale sale of compact discs, constitute by far the largest number of records sold.

10 Discounting from the list price has always been a feature of the wholesale record market. But ARIA says that since about 1990 there has been a significant increase in the rate of discounting. The evidence provides some support for this contention although the degree of discounting is uncertain. The following are some of the factors that have led to discounting. Discounts are offered to sell new releases of recordings by new artists. Volume rebates or discounts are offered to attract sizeable orders. Large record retailers have significant "buying power" and are able to demand discounts even on smaller selling lines. Competition from other forms of entertainment induce manufacturers to sell records at prices substantially below the list price.

11 Two other important features have contributed to a reduction in the wholesale selling price of records. First, there are the changes to the *Copyright Act* made in 1998 to allow parallel importation of records from other countries without the consent of the local copyright owner. Second, the retail market has become more competitive. As a result, retailers have come to expect discounts, especially on compact discs. A number of witnesses have described this practice as one that is now "firmly entrenched". Personal experience provides some confirmation for this view.

12 These changing market conditions have caused manufacturers to form the opinion that it is undesirable that mechanical royalties should continue to be paid as a percentage of the list price. They say that the list price no longer reflects the underlying value of a record. The manufacturers argue that the royalty should be a fixed percentage of the actual retail selling price of a record. That is, the royalty should be paid on the revenue received by the manufacturers and not on what they regard as an artificial value.

13 Needless to say, the publishers and other copyright owners strongly resist any change to the basis upon which mechanical royalties are paid. APRA points out that there has always been discounting and the royalty rates that have applied over the years have taken this into account. The copyright owners also contend, with some force, that some benefit must accrue to the manufacturers by maintaining a list price that is much higher than the selling price, otherwise the list price would be reduced. Thus it is to be presumed that the maintenance of differential pricing provides benefits which outweigh the burden of a royalty assessed on the list price.

14 APRA also criticises the basing of a royalty on the actual selling price of a record. One criticism is the alleged unfairness of a record company being able to shift to a publisher some of the cost of discounting a record when the discounting is intended to promote sales of other records. Another criticism is that certain discounting, a concept which has a rather wide meaning, is in reality no more than a component of the cost of selling a product which should be borne by the manufacturer and not be transferred to the copyright owner.

15 For present purposes it is neither necessary nor appropriate to determine whether a royalty based on the actual selling price is to be preferred over a royalty based on the list price. Nor is it necessary to consider whether some other method of calculating mechanical royalties would produce an equitable result between licensor and licensee. What can be said, however, is that the manufacturers' attempt to shift the royalty base away from the list price should not be seen as a frivolous case. The evidence suggests that changes in market conditions and market behaviour have reduced the profitability of selling records. The maintenance of a royalty based on the list price of a record, at least when the list price varies significantly from the actual selling price, may unduly burden the manufacturer to the advantage of the copyright owner. On the other hand, the manufacturers set the list price and, in that sense, are responsible for the position about which they now complain. These are issues that will have to be investigated in detail and may be resolved at the final hearing. In the meantime, it is appropriate to approach this application for interim relief on the basis that the Tribunal may find that the manufacturers are entitled to the whole or part of the relief they seek.

16 The precise order that the manufacturers seek is that as from 1 January 2000 the amount of royalty to be paid and the manner of payment is to be in accordance with the expired agreement as amended by the two Heads of Agreement, save that the royalty be calculated as a percentage of the actual selling price. They also ask for an order that the difference between a royalty based on the list price and a royalty based on an actual selling price be paid into an interest-bearing account pending the resolution of the proceedings.

17 The first point that arises in respect of this proposal is whether there is jurisdiction to make the orders sought. The issue arises in the following way. To take advantage of the statutory licence to make a recording, it is necessary for the licensee to pay the prescribed royalty to the copyright owner: s 55(1)(d)(ii). The prescribed royalty is the amount agreed between the manufacturer and the owner of the copyright or, if there is no agreement, the amount fixed by the Tribunal. In the event that there is neither an agreement nor a determination by the Tribunal as to the royalty to be paid, the royalty prescribed by statute is 6.25 per cent of the retail selling price of the record: s 55(6). The Tribunal's power to fix the royalty is restricted; the royalty cannot be less than 1 cent in respect of a record: see s 55(5).

18 The interim order sought by the manufacturers involves the continuation of an agreement which provides that no royalty is to be paid on records distributed free of charge for promotional purposes and on records sold on a sale or return basis. The publishers say that the Tribunal cannot make an interim order under s 160 which has this effect. That is, they contend that because the Tribunal does not have power to determine that no royalty is to be paid on certain records in an application under s 152A, it follows that the Tribunal could not make such an order under s 160. The publishers go further and say that if no royalty is paid in respect of a record, a statutory licence will not subsist in respect of that record. Perhaps another way of putting the argument is that if the Tribunal does not fix a royalty for a particular record then the royalty that is to be paid is the royalty prescribed by s 55(6), namely 6.25 per cent of the retail selling price of the record.

19 In *Reference by Australasian Performing Right Association Limited* (unreported, Copyright Tribunal, 7 October 1994) the Tribunal considered the ambit of s 160. The Tribunal had been invited to make interim orders in applications under ss 154 and 157 for the determination of royalties to be paid by commercial television stations for the right to broadcast music. It was proposed that the Tribunal make orders, the effect of which would have been to alter retrospectively the royalties that had been paid. It was argued that the Tribunal did not have power to make retrospective orders when it determined royalties under ss 154 and 157 and accordingly no such power could subsist under s 160. That is to say, so the argument went, the ambit of the power conferred by s 160 was confined by the nature of the final relief that could be granted.

20 The Tribunal was prepared to accept, without deciding, that there was no power to make retrospective orders under s 154 or s 157. However, as regards s 160 the Tribunal did not accept that the power was circumscribed in the manner argued. The Tribunal said (at 12):

*"The whole thrust of Part VI of the Act, which is entitled "The Copyright Tribunal", is to enable the Tribunal to achieve an appropriate balance between the interests of copyright owners, whose work is to be the subject of a licence, and the interests of those who wish to make use of that work for a reasonable fee and on reasonable terms and conditions. We see no reason why the ambit of s 160 should be circumscribed by the provisions of ss 154 and 157 assuming that it is correct to say that those sections do not authorise a final decision which has a retrospective effect."*

Later, the Tribunal said (at 13):

*"[We] do not construe [ss 154 and 155] as limiting the wide words of s 160 which, in our opinion, empower the Tribunal to make an order which, in a particular and common sense way, will provide appropriately for the period up to final determination."*

21 We would apply this reasoning in the present case while accepting that the position is not precisely analogous. The now expired agreement, that had been reached by arm's length negotiations, provided the copyright owners with what they regarded as adequate recompense for the right to manufacture and sell records. The provision of free records for promotional purposes had the potential to benefit both the manufacturers and the copyright owner by increasing demand for their

product. Thus, although no royalty was payable on promotional records the expectation, no doubt, was that the royalties actually received overall would be higher. The same is true of records provided on sale or return. Placing records into the hands of a retailer will encourage sales. In some cases a retailer might not take a large quantity of stock unless it had the right to return any stock that was not sold. So, while it is true that no royalties were payable in respect of two classes of records the purpose of these provisions was to increase the overall royalty payable to the copyright owner.

22 We would be reluctant to find that the Tribunal lacks the power to allow such an arrangement to continue on an interim basis. We agree that there is force in the argument that the legislation contemplates that a royalty be paid on every record sold. But in the end we are of the opinion that the very wide powers conferred by s 160 do permit the Tribunal to make an interim order along the lines sought. As was said in the judgment of the High Court in *Owners of "Shin Kobe Maru" v Empire Shipping Co Inc* (1994) [181 CLR 404](#) at 421:

*"It is quite inappropriate to read provisions conferring jurisdiction or granting powers to a court by making implications or imposing limitations which are not found in the express words."*

The same is true of the powers given to the Tribunal.

23 We should now explain why the manufacturers ask for the establishment of a retention fund. Under the expired agreement royalties are payable quarterly. Upon receipt of a royalty payment, the publisher is often required to account for a share of the royalty to some other person, eg to an artist or songwriter. All parties accept that once the publisher has accounted for a share of the royalty there is no practical means of recovering that share from the recipient. Accordingly, if it turns out that royalties paid under any interim arrangement exceed those that are finally determined to be payable, the overpayment will not be recovered. That money will be lost by the manufacturers. The establishment of a retention fund is designed to overcome this problem. If there is no reduction in royalty then the retention fund can be released to the copyright owners. If the rate of royalty is reduced then some or all the fund can be returned to the manufacturers.

24 As regards the suggestion that an interim order should change the basis of calculating royalty from the list price to the actual selling price, we are quite satisfied this should not occur. First, even if the discounting which we have briefly described should produce a reduction in the royalty, this can be achieved by ways other than adoption of a royalty that is based on the actual selling price. Second, any change to the current practice will require the parties to alter their method of accounting for royalty purposes. While this may not be as difficult as was first thought, it will cause the parties to incur considerable expense. It is an expense that may turn out to be unnecessary. Third, all that an interim arrangement need achieve is a measure of protection to the manufacturers against the risk that they may not be able to recover royalty overpayments. Finally, a change to the present method of calculating the royalty, even if it is only for the purposes of an interim order, might be seen as an indication that the Tribunal is of the view that the manufacturers' arguments will be adopted. The Tribunal has certainly not formed any such view. Nor has it formed a contrary view. If an interim order is made, the maintenance of the present position of calculating the royalty is less likely to cause misunderstanding.

25 The immediate question then is whether any interim order should be made. AMCOS says that it is unnecessary for the Tribunal to intervene. It has indicated its willingness to continue the past arrangement until the Tribunal is able to resolve the applications. AMCOS will not, however, agree that any part of the royalty that is payable under the old arrangement should be retained in trust.

26 This position is unsatisfactory. It puts the manufacturers at some risk, a risk that we think is unacceptable in the circumstances. We are of the opinion that an interim order should be made that a

royalty be paid and that the manner of payment be in accordance with the expired agreement as amended. What should be the rate of rate of royalty that is to be paid? Should a retention fund be established?

27 As we have said the principal object of the establishment of a retention fund is so that "some measure of justice can be done between the parties", to quote from the applicants' written submissions. Against this, the publishers say that the Tribunal simply has no information which would enable it to form even a tentative view as regards what portion of the royalty should be put into a retention fund. They also point to certain aspects of the calculation of the levels of discounting that suggest that the figures that have been produced are neither reliable nor reflective of the true position. Accordingly they contend that it is unsafe for the Tribunal to act on the evidence for the purposes of the creation of a retention fund.

28 We accept that there is uncertainty concerning the rate of discounting. Produced in evidence was a table showing the discount rate for six major record companies in the years 1995 through 1999. The table shows that each company was discounting against its list price in 1995. The discounts ranged from 1.72 per cent to 8.65 per cent. The rate did not increase noticeably over the next three years, except in the case of one company. But in 1998 and 1999 a number of companies did increase significantly the rates of discount.

29 The table seems to reflect the opinion, expressed at a meeting of the ARIA Finance Committee, that the earlier figures did not appear favourable to ARIA's argument. However the later figures, especially those taken when parallel importation commenced to have an effect on the market, does provide some support for the manufacturers' arguments.

30 It seems to us, on balance, that it is reasonable to accord to the manufacturers some of the protection they seek. This may be achieved by ordering that, pending the final determination of the applications, the previous agreement as varied by the two Heads of Agreement be continued, save that the rate of royalty shall be that specified in the agreement less 7.5 per cent, subject to any adjustment that the Tribunal might hereafter make when it finally disposes of the applications. In the meantime the amount that is deducted should be placed into an interest-bearing account. An order along these lines might also have the effect of avoiding the difficulty that the Tribunal may not be able to make a retrospective order.

31 Orders to give effect to these reasons will be made on the undertakings proffered by the applicants. Those undertakings were to the effect that:

(a) within 60 days after the end of each quarterly period until a final decision of the Tribunal, the applicants will pay the amount deducted for that quarter from the rate of royalty that is specified in the agreement (as varied) into an interest-bearing account in the names of the solicitors for ARIA and the solicitors for AMCOS;

(b) the applicants will maintain accounting records with respect to the calculation of the amount to be paid into the account which would permit an auditing of the accounts at the order or direction of the Tribunal and the payment of the amount in the account to any person in response to an order or direction of the Tribunal;

(c) the applicants will submit to such orders (if any) as the Tribunal makes in relation to the payment of the amount in the account and will pay such funds as are assessed by the Tribunal or as it may direct, to any person whether or not a party, adversely affected by the operation of the interim order of the Tribunal or any continuation thereof;

(d) the applicants will to pay to the respondents an additional amount by way of interest on any money received by the respondents out of the account, such amount being calculated as the difference between the amount of interest actually earned on the funds in the account and the amount of interest that would have been received had the interest rate applicable to the account been a rate that is 1.5% above the average 90-day bank bill swap rate as published in the Australian Financial Review (the average calculated over the period between 1 January 2000 and the date of payment) and applied to the account on the last business day of each calendar month.

32 The applicants should bring in short minutes of order within 14 days.

I certify that the preceding thirty-two (32) numbered paragraphs are a true copy of the Reasons for Decision herein of the Copyright Tribunal constituted by Finkelstein DP, Professor Pearce and Ms Bowne

Associate to the Deputy President:

Dated: 14 June 2000

Counsel for the Applicants: Mr A J L Bannon SC  
Mr R Cobden

Solicitors for the Applicants: Gilbert & Tobin

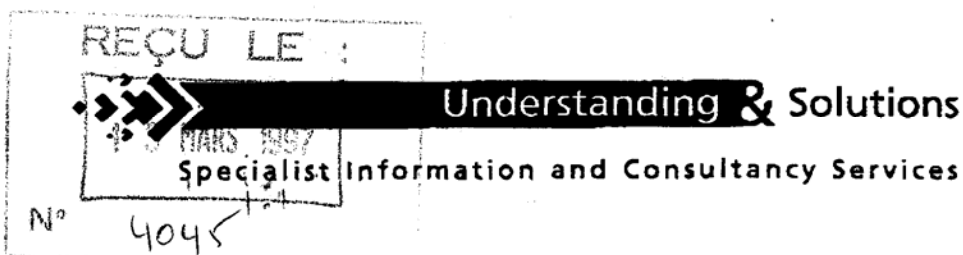
Counsel for the Respondents: Mr R J Webb  
Mr M Green

Solicitors for the Respondents: Banki Haddock Fiora

Date of Hearing: 14, 15, 16 March 2000

Date of Decision: 14 June 2000

ENCLOSURE 6 : Understanding &amp; Solutions' views on tracks

**FACSIMILE**

YOUR FAX: 00 331 45 63 06 11      OUR FAX: +44 1582 472946

TO: LAURE MAGHERINI      DATE: 12 MAR 1997

COMPANY: BIEM      OUR REF: MS/sab/3.8.12

COPY TO: RONALD MOOIJ

FROM: MAGGIE SCOTT      PAGE(s): 3

If there are any problems with this transmission, please ring Julia/Nikki on +44 1582 607744

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•> Dear Laure

I hope you are well.

Further to our recent conversation, please find below our views on whether the number of tracks on a compilation increases its sales.

After speaking to several of our contacts within the compilations industry, it is apparent that generally it is the repertoire on the compilation that tends to make a difference in terms of sales, rather than the number of tracks. A Hits compilation is the key successful repertoire type and tends to sell better than a themed album.

The number of tracks may have an influence on "best of" album sales, although we do not strictly count these as true compilations, we consider compilations to be multi artist titles. If the consumer is faced with two "best of" albums by the same artist then they are more likely to go with the one with more titles as it is perceived as better value for money.

On a separate note, following up from your recent meeting with Sarah, 40% of music sales are made in "Rest of World" territories. The top ten rest of world music markets ranked in order of size are India, China, Russia, Indonesia, Brazil, Canada, Mexico, South Korea, Australia and Taiwan. Collectively, these ten music markets account for 76% of all Rest of World music sales. I have attached a full breakdown for your interest.

•> Understanding & Solutions Limited,  
8 Kensworth Gate,  
200-204 High Street South,  
Dunstable, Beds, LU6 3HS, England.

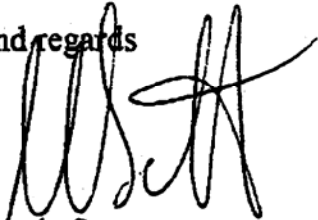
•> Telephone:  
(01582) 607744  
Facsimile:  
(01582) 472946.

•> Company  
Registration  
Number  
2293034.

I am continuing to work on the other areas raised in your meeting with Sarah and will forward the information to you as soon as possible.

In the meantime, I hope the attached is of use to you.

Kind regards

A handwritten signature in black ink, appearing to be 'M. Scott', written over the typed name.

Maggie Scott



ENCLOSURE 7

## Record companies' accounting practices to be probed by joint Senate hearing in California

Phil Hardy, phil.hardy@informa.com

[Music and Copyright Issue 232, 17 July 2002](#)

The accounting practices of the record industry, especially in regard to artists' royalty payments, are to come under official scrutiny in the US. Later this month the California Senate's Judiciary Committee and the Select Committee on the Entertainment Industry are to hold a joint hearing into the industry's accounting practices.

The move follows a growing number of complaints and lawsuits brought against record companies by artists this year, most recently by Courtney Love and the Dixie Chicks (see M&C 201/1). Last week Michael Jackson added his voice, accusing SME of conspiring to cheat artists - particularly black artists - out of royalty payments. Jackson's complaint has been widely seen as self-seeking (see below), but it highlights the fact that the past practices of record companies have not been as transparent as they might have been, especially concerning black artists. Even attempts to redress inequalities, such as the lawsuit brought on behalf of black artists against the American Federation of Television and Radio Artists for failing to collect health and benefit payments from record companies, have met with numerous difficulties (see M&C 229/15).

The California Senate Entertainment Committee is chaired by Senator Kevin Murray, sponsor of the bill seeking to end the current restrictions applicable to the length of recording contracts signed in California (see M&C 231/2).

Murray noted that in almost every case a record company is found to be owing an artist money when it is independently audited. If the hearing reveals a pattern of under-payment, Murray will seek to introduce legislation mandating payment equivalent to punitive damages awarded in a lawsuit.

US record industry association RIAA, which has been invited to give evidence to the hearing, said that improper behaviour by its members was the exception not the rule.

However, there is ample evidence that the practices the joint hearing will be examining are commonplace. Earlier this year UMG agreed to pay \$4.75m in settlement of a class action suit filed by the singer Peggy Lee, who claimed that she and other Decca recording artists had been underpaid royalties due between 1950 and 1960 (see M&C 221/14). The estates of Buddy Holly and Bing Crosby are engaged in a separate, similar, lawsuit. Love's case against UMG is still pending, while the two sides attempt to negotiate an out-of-court settlement (see M&C 230/15).

The large number of similar lawsuits is unusual. Accounting disputes between artists and record companies have usually been settled before they reach court. This happened in the case of the Dixie Chicks (see M&C 231/15) and also when an audit of SME by the Harry Fox Agency in the US found that the company had sold soundcarriers in Latin America which it claimed had been made for promotional purposes in the US (see M&C 186/15).

The case of Michael Jackson is more complicated. Observers have suggested that he is using the growing artists' rights movement, which has been spearheaded by the Recording Artists' Coalition (see M&C 229/5), to pressure SME into breaking its contract with him so that he can gain ownership of his master recordings sooner. Jackson is under contract with SME until 2004. Under the terms of the contract SME has the rights to his master recordings until 2010. After 2010 Jackson will be able to license his recordings to another record company. According to the Los Angeles Times, Jackson's contract, which gave him a reported 50% royalty rate of net record company receipts, also required SME to pay recording and video costs, as well as marketing and promotion expenses. Reportedly SME paid \$25m in advances to record *Invincible*, but other sources say that Jackson paid his own recording costs.

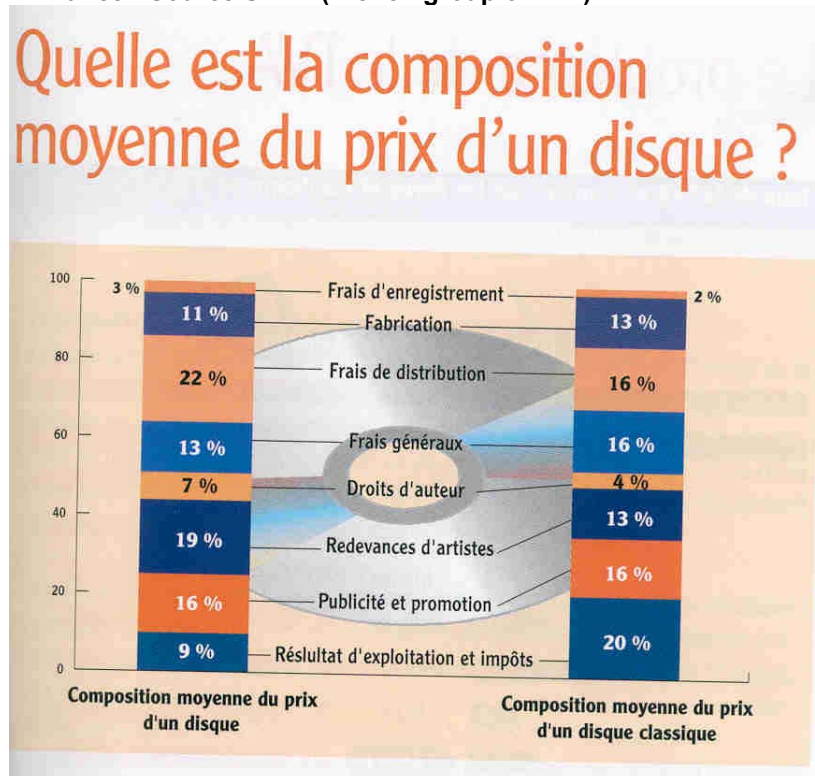
SME, which said it spent \$26m promoting *Invincible*, noted that Jackson did little himself to promote the album, renegeing on a proposed concert tour, pulling out of a promotional tour of Europe, failing to complete one video and not appearing at all in a second one. *Invincible* has sold 5m units to date.

Enclosure 8 : Breakdown of CD pricing by component costs (average for Western Europe)  
 Source : Understanding & solutions

**BREAKDOWN OF CD PRICING  
 BY COMPONENT COSTS:  
 2001  
 WESTERN EUROPE  
 % TOTAL DEALER PRICE €**

<b>Trade (dealer) price</b>	<b>€8.34</b>	
<b>Costs</b>	<b>%</b>	<b>Price</b>
Overheads	20%	€1.67
Manufacture (includes bare disc, jewel box & inlay)	5%	€0.42
Artist Royalties	12%	€1.00
Mechanical Royalties	9%	€0.75
Distribution	10%	€0.83
Marketing	25%	€2.09
Returns	3%	€0.25
<b>Total Costs</b>	<b>84%</b>	<b>€7.01</b>
<b>Operating Profit Per CD</b>	<b>16%</b>	<b>€1.33</b>

In France : Source SNEP (French group of IFPI)



## In the Netherlands : Source NVPI (Dutch group of IFPI)

<b>PPD</b>		<b>€12.75</b>
Discounts	15%	€1.91
<b>Average Price</b>		<b>€10.84</b>
<b>Costs</b>	<b>%</b>	<b>Price</b>
Overheads	9%	€1.15
Manufacture (includes bare disc, jewel box & inlay)	11%	€1.40
Costs of Music	30%	€3.83
Mechanical Royalties	9%	€1.15
Distribution	2%	€0.25
Marketing	15%	€1.91
Total Costs	84%	€9.69
Operating Profit Per CD	9%	€1.15

ENCLOSURE 9: Comparison of price in Europe

a- Study made in 2000, comparing the PPD applied by the Major producers benefiting from a CL contract (Universal with MCPS (UK); Sony with SDRM (France), EMI with BEL (a joint venture of SDRM/GEMA and MCPS) and Arcade with STEMRA – Netherlands).

	MCPS			SDRM			STEMRA	
	Universal			Sony	EMI	Virgin	Time Life	Arcade
<b>Artist:</b>	Shania Twain	Bon Jovi	ABC	Mariah Carey	Blur	J. Jackson	Various	Eddy Grant
<b>Product:</b>	Come on Over	Bon Jovi	Look of Love	When you believe	13	The velvet	Rock and Roll Era V	Best of Hit Collection
<b>Cat number:</b>	5580002	8149822	5501452				51633	9902361
<b>Period</b>	Q3 and Q4 1999***			Q3 and Q4 1999			Q3 and Q4 1999	
<b>Territory</b>	<b>CD Full Price PPD in EURO</b>	<b>CD Mid Price PPD in EURO</b>	<b>CD Budget PPD in EURO</b>	<b>PPD Euro</b>	<b>PPD Euro</b>	<b>PPD Euro</b>	<b>PPD Euro</b>	<b>PPD Euro</b>
Austria	11.26	7.19	Ns	13.01	12.52	8,67/12,27		
Belgium	12.27	7.68	5.06	Ns			11.34	11.53
Denmark	12.75	7.65	4.56	12.70			11.52	12.08
Finland	12.61	6.54	Ns	13.78	11,93 / 13,56	13.57	13.09	
France	13.22	8.31	Ns	3.46			11.74	13.64
Germany	12.02	4.46	3.03	11.34	11.93	11.93	11.11	
Greece *	11.78	7.51	4.56	9,13 / 9,31			11.50	
Ireland	15.34	11.39	Ns	Ns				
Italy	12.39	7.75	Ns	12.48				
Netherlands	12.25	7.17	4.54	13,17/12,86			13.21	10.71
Norway	12.42	8.03	Ns	12.72	12.84	9,97/12,22	14.00	12.42
Portugal	12.47	7.86	5.74				12.28	
Spain	12.08	7.39	3.67	12.76			11.56	10.70
Sweden	11.82	6.85	4.96	12.67			11.50	11.94
Switzerland	12.90	9.38	Ns	15.82			13.14	
United Kingdom	15.37	9.61	Ns				13.78	

Exchange rate (on 25 October 2000) :

1 Euro = 7,4507 DKK    7,9689 NOK  
 339,542 GRD    43,5232 SKK  
 0,5776 GBP    8,4625 SEK  
 1,5034 CHF

\*Greece has no minimum value but instead a minimum dealer price (3,800)

\*\* Minimum royalty presuming 9.009% of Minimum price.

\*\*\* except France (Q2 1999)

b- Comparison of the Western European average trade price (whole sale price) and retail price

Territory	Average trade price	Average retail price
	€uro	€uro
Austria	8.40	14.53
Belgium	8.65	12.11
Denmark	7.64	12.36
Finland	8.34	14.36
France	8.27	13.30
Germany	7.20	10.10
Greece	7.04	11.26
Italy	10.06	14.42
Netherlands	6.05	10.28
Norway	7.86	14.85
Portugal	7.58	11.93
Spain	5.60	10.15
Sweden	8.31	13.96
Switzerland	10.60	12.71
United Kingdom	8.28	15.43

Source : Understanding & Solutions - Music Market report March 2001

The two preceding tables show that despite a lower royalty rate applied in UK, British prices are not significantly lower than the prices applied in continental Europe.

c- The following table on the 10 year evolution of CD price in national currencies and in €uro, shows the absence of direct influence of the change in the royalty rate agreed between BIEM and IFPI and the retail price.

*Note for ease of reference : evolution of the BIEM rate :*

from 1<sup>st</sup> January 1990 to 31 December 1990 : 9,504% on the PPD except for CD format benefiting from an introductory deduction decreasing the rate to 8,448%

from 1<sup>st</sup> January 1001 to 30 September 1992 : 9,504% PPD % [11 – 4 %(deduction for rebate) -10% (packaging deduction)]

from 1<sup>st</sup> October 1992 to 30 June 1997 : 9,306% [11 – 6 %(deduction for rebate) -10% (packaging deduction)]

from 1<sup>st</sup> July 1997 to 30 June 2000 : 9,009% [11 – 9%(deduction for rebate) -10% (packaging deduction)] – this rate is still applied, despite the non-renewal of the BIEM/IFPI contract.

## 10 YEAR DEVELOPMENT OF CD ALBUM PRICING

### Average Retail Price Local Currency

	Currency	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	
Austria	Asch	214.40	211.80	211.20	212.98	213.44	206.62	202.02	204.40	212.27	214.94	214.94	214.94	
Belgium	BFr	689.34	704.23	704.42	662.75	603.15	551.65	522.00	535.35	533.71	531.62	512.32	512.32	
Denmark	DKr	146.60	146.60	146.00	132.00	113.80	112.30	104.79	97.25	97.25	96.55	96.30	96.30	
Finland	FMk	86.74	89.80	90.25	95.62	96.35	95.94	97.62	99.54	102.61	102.10	96.76	95.76	
France	FFr	102.48	102.11	101.74	100.82	99.73	98.97	98.87	98.34	98.13	96.17	93.77	90.77	
Germany	DM	24.49	24.71	23.94	20.33	18.91	18.69	19.69	20.77	20.72	21.40	21.64	21.64	
Italy	Lire	21030	21265	21387	22460	22551	22260	21836	21622	21868	23660	25530	27930	
Netherlands	Gld	35.93	35.05	35.39	32.80	27.89	26.07	24.63	24.35	24.21	24.50	24.46	23.46	
Norway	NKr	130.90	129.95	130.20	130.60	130.80	130.96	131.57	130.60	131.19	131.85	127.55	127.55	
Spain	Pts	1666.35	1638.55	1569.70	1618.20	1747.60	1809.50	1782.85	1870.98	1827.74	1824.70	1827.61	1830.61	
Sweden	SKr	121.40	120.46	120.87	121.17	123.17	123.80	123.85	125.94	129.88	138.50	136.48	133.48	
UK	£	9.93	10.15	10.42	10.69	10.98	11.38	12.04	13.15	13.63	13.01	12.73	12.73	
<b>BIEM rate</b>		<b>8.448%</b>	<b>9.504%</b>	<b>9.306%</b>				<b>9.009%</b>						
			<b>01/01/1991</b>	<b>01/10/1992</b>					<b>01/07/1997</b>					
<b>In Euro</b>		<b>1990</b>	<b>1991</b>	<b>1992</b>	<b>1993</b>	<b>1994</b>	<b>1995</b>	<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	
Austria		15.58	15.39	15.35	15.48	15.51	15.02	14.68	14.85	15.43	15.62	15.62	15.62	
Belgium		17.09	17.46	17.46	16.43	14.95	13.68	12.94	13.27	13.23	13.18	12.70	12.70	
Denmark		19.74	19.74	19.66	17.77	15.32	15.12	14.11	13.09	13.09	13.00	12.97	12.97	
Finland		14.59	15.10	15.18	16.08	16.20	16.14	16.42	16.74	17.26	17.17	16.27	16.27	
France		15.62	15.57	15.51	15.37	15.20	15.09	15.07	14.99	14.96	14.66	14.29	13.29	
Germany		12.52	12.63	12.24	10.40	9.67	9.56	10.07	10.62	10.59	10.94	11.06	11.06	
Italy		10.86	10.98	11.05	11.60	11.65	11.50	11.28	11.17	11.29	12.22	13.19	14.19	
Netherlands		16.30	15.90	16.06	14.88	12.66	11.83	11.18	11.05	10.99	11.12	11.10	10.10	
Norway		17.58	17.45	17.49	17.54	17.57	17.59	17.67	17.54	17.62	17.71	17.13	17.13	
Spain		10.01	9.85	9.43	9.73	10.50	10.88	10.72	11.24	10.98	10.97	10.98	11.98	
Sweden		13.05	12.95	12.99	13.03	13.24	13.31	13.31	13.54	13.96	14.89	14.67	14.67	
UK		15.82	16.18	16.61	17.04	17.50	18.14	19.18	20.96	21.72	20.73	20.29	19.29	

Source : Understanding &amp; ;

d. GEMA CL agreements : example of prices practiced in Europe, according to central licensing agreement concluded by GEMA- see attached herewith a table on the PPD evolution during the application of the Amendment No. 7.

ARTIST TITLE CAT. NO:	GEMA/BMG No Mercy My Promise 743214 1227200			GEMA/WARNER Mc Kennitt, Loreena The Book of Secrets 630194042			GEMA/EMI Radiohead OK Computer 07243 85522925		
	CD Full Price - PPD		% change	CD Full Price - PPD		% change	CD Full Price - PPD		% change
	2nd half 97	2nd half 99		2nd half 97	2nd half 99		2nd half 97	2nd half 99	
Territory									
AUSTRIA	11.48	11.48	0.00%	11,85	11,85	0%	11.81	12.30	4.15%
BELGIUM *	10.80	---		11,77	11.80	0.25%			
CZECH REPUBLIC				10,27	10.43	1.55%	---	---	
DENMARK	11.95	11.95	0.00%	11,95	11,95	0%	12.75	13.02	2.12%
FINLAND	12.61	12.78	1.35%	11,52	12.03	4.43%	12.97	13.07	0.77%
FRANCE *	13.42	---		13,03	13.11	0.61%			
GERMANY	12.04	12.04	0.00%	11,86	11,86	0%	11.88	12.12	2.02%
GREECE *	10.60	11.19	5.57%	---	---				
HUNGARY				7,41	8.90	20.10%	---	---	
IRELAND **	---	---		---	---				
ITALY *	10.33	---		---	---				
NETHERLANDS	11.23	12.25	9.08%	11,80	11,80	0%	11.89	14.99	26.07%
NORWAY	12.30	12.67	3.01%	12,42	13.18	6.11%	12.24	12.86	5.07%
PORTUGAL *	---	---		---	---				
SLOVAKIA	---	---		---	---				
SPAIN *	---	---		---	---				
SWEDEN	11.34	11.94	5.29%	11,70	12.29	5.04%	11.70	12.53	7.09%
SWITZERLAND	10.98	11.31	3.01%	12,90	12,90	0%	12.64	13.23	4.67%
UNITED KINGDOM **	---	---		---	---				

Exchange Rate 25. Oct. 2000: 1 EURO

≡	34,9541 CZK	7,9689 NOK
	7,4507 DKK	43,5232 SKK
	339,542 GRD	8,4625 SEK
	262,88 HUF	1,5034 CHF
	0,5776 GBP	

other EURO-Countries: fixed rate

\* licensed by SDRM (for EMI CLA)

\*\* licensed by MCPS (for EMI CLA)

**Comments :** The table mentioned example of PPD applied within Centralised licensing deals between GEMA and 3 Majors.

Example of PPD are given as at the beginning of the application of the 9.009% royalty rate, after a decrease of 3% from 9.306%, and at the second half of 99, period during which, the royalty rate was unchange

On PPD side, some changes appear in the table : in 6 countries within BMG's deal from 1.35% in Finland to 9% in the Netherlands;

in 7 countries within Warner's deal : from 0.25% in Belgium to 20.1% in Hungary;

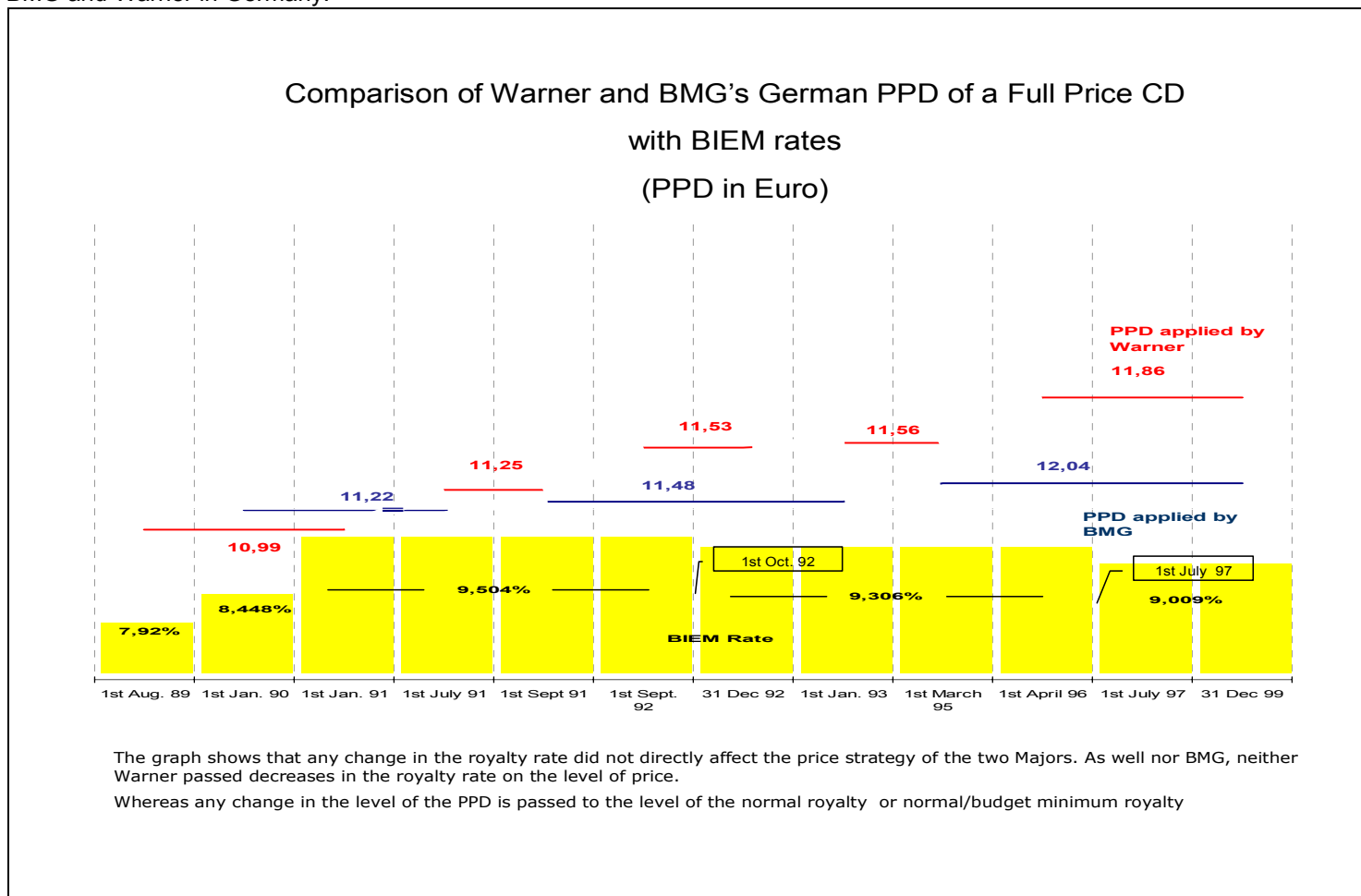
in 8 countries within EMI's deal from 0.77% in Finland to 26.07% in the Netherlands.

In addition, changes within the same country are not linear also. For example in the Netherlands while PPD increase by 26% within EMI, it remains unchanged for Warner and increase by 9% for BMG.

In Austria, BMG and Warner did not change PPD in between the two dates but EMI increased by more than 4%.

In short increase and decrease in the PPD was not link to change in the BIEM royalty rate.

The enclosed graph is another example on how the PPD level have been set independently to the royalty level : here are shown PPD applied by the two Majors BMG and Warner in Germany.



Finally, according to the enclosed chart it can be seen that the minimum royalty as well as the budget minimum royalty are set at a uniform level between the 3 Majors and have been decreased from 1997 to 1999 according to the price basis agreed upon the German society and the German group of IFPI

**MINIMA COMPARISON IN THREE CEL CONTRACTS  
(in Euro)**



ARTIST TITLE CAT. NO:	GEMA/BMG				GEMA/WARNER				GEMA/EMI			
	No Mercy My Promise 743214 1227200				Mc Kennitt, Loreena The Book of Secrets 630194042				Radiohead OK Computer 07243 85522925			
	Normal Minimum Royalty		Budget Minimum Royalty		Normal Minimum Royalty		Budget Minimum Royalty		Normal Minimum Royalty		Budget Minimum Royalty	
Territory	2nd half 97	2nd half 99	2nd half 97	2nd half 99	2nd half 97	2nd half 99	2nd half 97	2nd half 99	2nd half 97	2nd half 99	2nd half 97	2nd half 99
AUSTRIA	0.5450	0.5014	0.3110	0.2856	0.5450	0.5014	0.3110	0.2856	0.5450	0.5014	0.3110	0.2856
BELGIUM	0.5126	0.5126	0.3907	0.2922	0.5126	0.5126	0.3907	0.2922	0.5126	0.5126	0.3907	0.2922
Czeck Rep				---	0.3147	0.3147	---	---	0.3147	0.3147	---	---
DENMARK	0.5436	0.5838	0.3825	0.3288	0.5436	0.5838	0.3825	0.3288	0.5436	0.5838	0.3825	0.3288
FINNLAND	0.5298	0.5971	0.3700	0.3532	0.5298	0.5971	0.3700	0.3532	0.5298	0.5971	0.3700	0.3532
FRANCE	0.5427	0.4955	0.3799	0.2825	0.5427	0.4955	0.3799	0.2825	0.5427	0.4955	0.3799	0.2825
GERMANY	0.4960	0.4960	0.2827	0.2827	0.4960	0.4960	0.2827	0.2827	0.4960	0.4960	0.2827	0.2827
GREECE	---	---	---	---	---	---	---	---	---	---	---	---
HUNGARY				0.3271	0.2854	0.4679	0.2587	0.3271	0.2854	0.4679	0.2587	0.3271
IRELAND	---	---	---	---	---	---	---	---	---	---	---	---
ITALY	0.6089	0.6089	0.4261	0.4261	0.6089	0.6089	0.4261	0.4261	0.6089	0.6089	0.4261	0.4261
NETHERLANDS	0.5218	0.5082	0.3857	0.2904	0.5218	0.5082	0.3857	0.2904	0.5218	0.5082	0.3857	0.2904
NORWAY	0.5208	0.5835	0.3639	0.3325	0.5208	0.5835	0.3639	0.3325	0.5208	0.5835	0.3639	0.3325
PORTUGAL	0.5886	0.5676	0.3541	0.3236	0.5886	0.5676	0.3541	0.3236	0.5886	0.5676	0.3541	0.3236
SLOVAKIA	0.1923	0.1861	---	---	0.1923	0.1861	---	---	0.1923	0.1861	---	---
SPAIN	0.4538	0.4815	0.3179	0.2745	0.4538	0.4815	0.3179	0.2745	0.4538	0.4815	0.3179	0.2745
SWEDEN	0.4904	0.5436	0.3427	0.3072	0.4904	0.5436	0.3427	0.3072	0.4904	0.5436	0.3427	0.3072
SWITZERLAND	0.5321	0.5321	0.3060	0.3060	0.5321	0.5321	0.3060	0.3060	0.5321	0.5321	0.3060	0.3060
UNITED KINGDOM	---	---	---	---	---	---	---	---	---	---	---	---

Exchange Rate 25. Oct. 2000: 1 EURO =

34,9541 CZK    7,9689 NOK  
 7,4507 DKK    43,5232 SKK  
 339,542 GRD    8,4625 SEK  
 262,88 HUF    1,5034 CHF  
 0,5776 GBP

other EURO-Countries:  
 fixed rate

ENCLOSURE 10 : SDRM Comparison of BIEM and US rate

**Extrait d'une étude effectuée par la SDRM sur la comparaison redevance France / Licence US effectuée sur les CD Polygram au 1er semestre 1996 (voir documents d'origine ci-joint)**

PPD moyen H.T France en €	Redevance (9,306%) en €	Nombre d'œuvres par support	Redevance par œuvre en €	Licence US convertie en €	% licence US / redevance œuvre
13.23 €	1.2307	12 œuvres	0.1026	0.05403	52.66
		14 œuvres	0.0879	0.05403	61.47
		16 œuvres	0.0769	0.05403	70.26
		18 œuvres	0.0684	0.05403	78.99
		20 œuvres	0.0615	0.05403	87.85

**Etude comparée, effectuée par la SDRM sur les CD Universal au 2ème semestre 2001**

PPD moyen H.T France en €	Redevance (9,009%) en €	Nombre d'œuvres par support	Redevance par œuvre en €	Licence US convertie en €	% licence US / redevance œuvre
13.89 €	1.2513	12 œuvres	0.1043	0.0838	80.35
		14 œuvres	0.0894	0.0838	93.74
		16 œuvres	0.0782	0.0838	107.16
		18 œuvres	0.0695	0.0838	120.58
		20 œuvres	0.0626	0.0838	133.87

**Commentaires :**

Alors qu'au 1/96 la redevance BIEM restait nettement supérieure à la licence US, au 2/01 la différence diminue fortement mais la redevance BIEM reste supérieure à la licence US:

pour un CD LP de 14 titres, au 1/96 la licence US représente 61,5 % de la redevance BIEM par oeuvre. Au 2/01 la licence US représente 93,7 % de la redevance BIEM par oeuvre.

Par ailleurs, depuis le 1er janvier 2002 la licence US est passée de 7.55 à 8 cents par oeuvre (0,0888 EUR). Si l'on reporte cette licence sur les données du tableau pour le 2ème semestre 2001, la licence US devient supérieure à la redevance BIEM à partir du 1er janvier 2002

**ENCLOSURE 11** : Comparison between the manufacturing costs of a CD album and the lowest royalty to be paid under the BIEM standard Contract (minimum budget : 57% of the normal minimum royalty )

*Note : This table should be completed once societies have replied*

**Manufacturing Costs / Budget Minimum  
2002**

	Minimum Budget in 2002	CD Manufacturing Cost per unit	Quantity
Austria	0.2900	0.30	3000
Belgium	0.2921	0.45	3000
Denmark	0.3500	0.65	
Finland	0.3400	1.35	
France*	0.2824	0.65/0.73 [OPO] or 0.80 [Sonopress]	500
Germany	0.2827		
Greece	?		
Italy	0.4370	Around 0.33/0.335	
Netherlands	0.2900	0.60**	500
Norway	0.3600	0.65	
Portugal	0.3200	0.94	1000
Spain	0.4815	Around 0.57/0.60	5000
Sweden	0.3000	0.65	
Switzerland	0.3143	N/A	

€0.22 per CD for over 300 000 units / €0.62 per CD for 1000/2000 units  
Or €0.40 per CD for 10 000 units

€ Around 0.36/0.39 for 150 000 CDs

*Information received from Australia :*

In 1998, the cost of producing a CD with a jewel case and a five colour, twelve page booklet was \$AUD1.48 (€0.82) on a manufacturing run of a minimum of 1000.

A similar run today would cost less than 1 dollar (€0.55): a raw CD with no booklet or plastic case would be less than 50 cents (€0,28). The printing of the CD booklet is now done direct from computer , there is no plate making involved- and this has cut the price of preparing the artwork considerably CD mastering charges have also dropped in cost.

\* Underlines the difficulty to have reliable figures, considering that the plant investigated knows perfectly the Authors society

\*\* jewel box and inlay costs not included, will be about 0.80 € per CD

## ENCLOSURE 12 : 10 years evolution of the market of Singles (Source : IFPI statistics)

## Evolution of the Single markets in the USA, in the UK and Europe (in Millions Units)

	Austria	Belgium	Denmark	Finland	France	Germany	Greece	Italy	Netherlands	Norway	Portugal	Spain	Sweden	Switzerland
1991	2.1	5.8	0.8	0.7	21.6	27.4	-	0.9	7.9	0.7	0.1	1.1	4.0	-
1992	2.0	3.8	0.8	0.6	16.9	29.3	-	1.1	4.2	0.7	0.0	1.2	3.3	1.0
1993	2.7	3.2	0.7	0.4	20.8	41.0	-	1.5	5.7	1.1	0.0	0.8	2.9	1.9
1994	3.1	3.4	0.7	0.3	17.3	44.8	-	1.5	5.9	1.4	0.1	0.9	2.8	2.1
1995	3.0	3.7	0.5	0.3	24.1	49.6	-	1.5	7.9	1.8	0.1	0.9	2.4	2.5
1996	2.8	4.8	0.8	0.3	31.6	53.2	-	1.4	7.9	1.8	0.1	0.9	3.0	2.8
1997	3.2	6.2	1.1	0.4	43.5	55.3	-	2.2	7.8	2.0	0.3	1.9	3.5	4.8
1998	3.1	8.7	1.2	0.5	40.9	56.8	0.8	3.6	6.6	1.9	0.6	1.5	4.4	3.4
1999	3.7	8.4	1.3	0.5	37.2	57.1	1.0	5.0	5.4	1.7	1.0	2.4	5.8	3.3
2000	3.7	8.3	1.5	0.6	38.0	54.9	1.2	4.0	5.4	1.1	0.8	1.9	5.6	3.3
2001	3.0	7.1	1.2	0.7	39.1	51.7	1.2	4.3	5.0	1.0	0.4	2.4	4.4	3.1

	Total Continental Europe	USA	UK	% change		
				C. Europe	USA	UK
1991	<b>73.1</b>	96.7	56.3			
1992	<b>64.9</b>	111.6	53.0	-11%	15%	-6%
1993	<b>82.7</b>	108.4	56.2	27%	-3%	6%
1994	<b>84.3</b>	102.1	63.0	2%	-6%	12%
1995	<b>98.3</b>	102.4	70.7	17%	0%	12%
1996	<b>111.4</b>	113.2	78.3	13%	11%	11%
1997	<b>132.2</b>	117.0	87.0	19%	3%	11%
1998	<b>134.0</b>	87.7	79.4	1%	-25%	-9%
1999	<b>133.8</b>	75.3	80.1	0%	-14%	1%
2000	<b>130.3</b>	40.3	66.1	-3%	-46%	-17%
2001	<b>124.6</b>	21.4	59.5	-4%	-47%	-10%

The main feature of the Single market :

The first thing to underline is that the single market does not follow the path of the album market. Singles has always been considered as a market attracting young consumers due to the affordable price of the carrier, to the possibility to have a wide variety of artists and to discover new artists/repertoire. Across the last decade the evolution of the single market has been rather volatile, going up and down at the rhythm of a price evolution, titles availability, other competition products availability (video games..), the appearance of CD-R copying and the expansion of Internet MP3 file availability.

According to IFPI figures, the Single market of the USA has experienced a dramatic collapse over the last four years, whereas the western European one has known a slight decrease in the last 2 years, decrease more important in the UK.

N.B. no limitation in term of tracks to be record on the sound carriers exits in the USA and the UK.

## ENCLOSURE 13 :Mark-up evaluation on Universal territories

we have tried to recalculate the mark-up in the country listed in the annex. Taking as point of departure average trade and retail prices published by the research company Understanding and Solutions, we assume that the average discount is the one announced by Universal to calculate the dealer price. The result is totally different from Universal calculation.

**Study based on album CD average prices**

Territory	A	B	C	D	E	F	G	Mark-up weighted according to market size
	Average Trade Price ** Euro	Dealer Price	Average Retail Price** Euro	VAT	Retail Price VAT excluded	Mark up country per country	M€uro*	
Belgium	8.75	7.31	12.71	21%	10.50	30%	260.8	1.18%
France	9.64	8.05	13.84	20%	11.57	30%	2 043.2	9.20%
Germany	7.16	5.98	11.01	16%	9.49	37%	2 378.7	13.03%
Italy	10.01	8.36	14.42	19%	12.12	31%	586.3	2.69%
Netherlands	7.71	6.44	10.88	18%	9.26	30%	486.9	2.20%
Spain	7.30	6.10	11.01	16%	9.49	36%	685.1	3.63%
Sweden	9.24	7.72	14.45	25%	11.56	33%	319.5	1.57%
							<b>6 757.2</b>	<b>33.50%</b>

\* IFPI Statistics

\*\*Understanding & Solutions - Music Market report August 2002

(Und & Sol confirms that trade price is the published price)\*

**METHODOLOGY**

Dealer Price (B) = A less 16.5% average discount as Universal's estimate

Mark-up country per country (F) :  $(1 - [\text{Dealer price (B)} / \text{Retail price E}]) * 100$

In H : each mark-up is weighted according to the size of its market in value term (according to IFPI publications)

**The average retailer mark-up is 33.5% of the retail price VAT excluded**

CATALOGUE: MID & LOW-PRICE — EDITED BY ADAM WOODS

# RETAIL DISCOUNT CAMPAIGNS: HOW LOW CAN YOU GO?

Ongoing retail discount campaigns, which are successfully shifting massive quantities of music product, rely on increasingly interdependent relationships between labels and retailers. Adam Webb reports how both sides are benefiting, even when the backscratching gets a bit rough

It is hard to avoid retail price promotions, these days. Storefronts once dominated by new releases and the Top 40 have been given over to near-permanent sales and catalogue promotions, as retailers strive to profit in an increasingly competitive market. The knock-on effect is that the time delay between full-price issue and cut-price offer is shifting.

Yet the implications of discounting are far-reaching says Union Square Music director of marketing Steve Buryan. While some labels welcome the increased sales and profile these promotions undoubtedly bring, others are concerned with the changing power balance between themselves and the retailers. This, in turn, has transformed sales and marketing for everyone from the majors to budget-price compilation specialists.

"We know that that promotions are a crucial part of every retailer's business and they're a crucial part of our business. So we try to be in as many as we can and our sales force takes every opportunity it gets to mention how we think our titles will be useful for their promotions." As Buryan recognises, discount campaigns are now firmly established as part and parcel of the retail landscape.

The majority of current campaigns run on a multi-buy basis — with the inducement of a combined discount (in the case of HMV's two-for-£22, Virgin's five-for-£50 or Vital's two-for-£20 offers) or a free product (in the case of Borders's forthcoming three-for-two campaign).

According to Andrew Williams, campaign buyer for Borders, this promotion was initiated by the retailer itself.

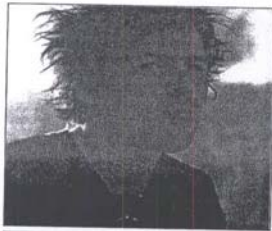
"We approached all our suppliers with the kind of mechanic we were looking to run and the kind of price points we wanted to buy at," he says. "I generally have an idea in the back of my head of the kind of titles I want from each supplier, so I can then cherry-pick those titles from the inevitably long list of product they offer us. Once the campaign is up and running, suppliers will start coming to us with suggestions for future inclusions. Once again, I cherry pick from these lists to get the right kind of titles for our stores."

The degree of liaison between retailers and labels in deciding which products will be promoted and at what price, depends ultimately on the size of the label and the strength of its catalogue. For majors such as BMG catalogue, the process is very much a two-way affair, with the sales department offering strategically-priced titles around the store's promotion mechanic.

**'Retailers are happy because they know loss leaders will fly out of the shops, and we're happy because they will then take loads of our titles that wouldn't be quite as lucrative'**

— John Reed, Sanctuary

As BMG catalogue marketing manager Charlie Stanford asserts, "I'm a great believer in working closely with retail and finding out what they think. If a retailer came up to me and said, 'you should definitely look at doing this', I would really consider it, because they are the people selling the product at the end of the day." At the other end of the spectrum, it is



On the cut-price racks (clockwise from top left): Ryan Adams, Madonna, Kid Rock, Alicia Keys

more a case of "just keeping on their [the major retailers'] radar," according to Buryan, and forwarding new releases to campaign managers.

"Union Square are a very good company for them to work with, because we have so many titles and so many different price points, and because they know we are very keen to support these promotions. And, because they know that, they will come to us and say, for instance, 'We're going to do a two-for-£10 promotion and we'd like to

include some of your titles, do you want to come and talk to us about it?' And then negotiations start."

**'I'm a great believer in working closely with retail and finding out what they think'**

— Charlie Stanford, BMG

For larger companies such as Sanctuary, with a considerable catalogue of its own, the relationship is more one of give and take. Working through national sales manager Henry Yori, the company will typically offer several of its best titles at a hugely discounted dealer price, on the basis that retailers will take other lesser known Sanctuary titles. In a classic case of swings and roundabouts, the label will take a hit on these "loss leaders" but will gain in other ways.

According to John Reed, general manager of Sanctuary Special Markets, "Retailers are happy because they know loss leaders will fly out of the shops and we're happy because they will then take loads of our other titles that wouldn't be quite as lucrative. We've shipped enormous quantities of some titles and barely made a penny, but if you look at the bigger picture and the level of support we get across our catalogue, then we win."

The benefits of discount campaigns are obvious for retailers. Essentially, customers are far more likely to purchase two CDs for £22 than one for £12.99, hence the reliance on campaigns and their perennial presence at the storefronts. Andrew Williams estimates that the titles in Borders' ongoing three-for-£18 campaign sell approximately five times the volume they would at full-price, accounting for between 10% and 20% of all stock sold. This has positive effects beyond measurable financial gains. "We are dramatically increasing the volume of catalogue product we sell, while maintaining our margin and our competitiveness," says Williams. > p26

## The retailer: MVC

Mike Mulligan, music category manager at MVC, is hopeful that the current classic CDs £6.99 mid-price campaign is highlighting the fact that MVC positions itself as a specialist retailer.

The promotion is arranged by decade, from the Sixties to 2000, with four defining titles, such as The Band or Blondie, highlighted for each. We felt that a straight A-Z made it difficult for customers to find an adjacent title and that they would probably shop within the decade with which they were most familiar. The campaign is now in its final week and we've done a roaring trade. I'm not sure of the exact figure, but I'd say promotions account for up to 20% of our total sales.

Product rotation is essential as customers have become far more aware of bargains and prepared to shop around. Multi-format promotions, across CDs and DVDs, are one way of overcoming this and encouraging traffic in all parts of the store. When the mid-price promotion concludes at the end of this week, MVC will start its Easter campaign, which will combine a stock clearance and striking new deals with suppliers.

For MVC, these deals will certainly be retailer-driven, with the store more than prepared to make suggestions to labels and distributors regarding what will work on the shop floor. Mulligan views negotiations between the two parties as mutually beneficial. Campaigns governed by price breaks are getting freed. The onus is now on the retailer to seize the initiative, he says.



Blondie



**CATALOGUE: MID & LOW-PRICE** — EDITED BY ADAM WOODS

"And of course the customer is getting better value for money, which should hopefully increase our brand loyalty." Titles are reviewed and restocked approximately every three months, an effective method of rekindling interest in stock across the genres. This, and a close relationship with labels and distributors, is seen as the key to a successful promotion. "All a campaign like this needs to be successful is a bit of trust on the part of both sides. In other words, I need to trust the label that if I take 100 copies of a product rather than 10 copies, I will be able to sell them, and they need to trust me that if they give me 40% discount rather than 20%, I will buy substantially more units from them."

This "no-lose" scenario is certainly recognised by the majors, who successfully use retail campaigns as a marketing tool to prolong their product's shelf life. Raul Chatterjee, head of sales at Warner Music, believes the relationship is "very much a two-way process, with both parties mutual beneficiaries". When *Best Of The Pogues* dropped to mid-price after Christmas, it sold 40,000 copies in one month, the same figure it sold in its first month at full-price precisely a year earlier. Other recent successes for Warner have been Madonna's *Music* (more than 100,000 units sold since its dealer price was cut) and Alanis Morissette's first two "grown-up" albums. Dropped temporarily

**"We are being asked for higher discounts and there comes a point where we can't afford to put titles into campaigns; an inability to deliver that level of discount can mean no support in future campaigns"**

— Independent label source

to mid-price in the wake of her new album, *Under Rug Swept*, Jagged Little Pill and Supposed Former Infatuation Junkie have since sold 38,000 between them. Charlie Stanford has long noted the effectiveness of such temporary price drops. "There was a time when I first started when all the reductions were permanent, from full to mid-price," he says. "Now, we tend to be a bit more savvy about the way we actually promote the back catalogue and drop full-price albums to mid-price for anything from a day to a three-month period. A great example of that is *Dixie Dancin'*. Last year it was one of our top mid-price bestsellers and it was constantly in the compilation charts. That happened because we had three drops last year from full to mid-price, timing them to coincide with big retail campaigns, and we sold massive bulk orders. We also found that when it goes back up to full-price, the orders didn't dry up. They slowed, obviously, but they still continued and no doubt we'll be doing more of those in the coming months."

The reason for making such temporary

**The indie catalogue specialist: MCI**

At MCI, sales and marketing director Danny Keene is gearing up for the forthcoming HMV sale. At close 11-year relationship with the retailer has seen their Music Club series, featuring artists such as Dionne Warwick, Bob Marley and All Green, become one of the bestselling budget ranges in the UK. A significant proportion of these will occur at sales time when prices will be reduced from £5.99 to £3.99 (relative to a CD single).

"HMV, along with the other retailers, have been very supportive to MCI," says Keene. "Working closely with their campaign manager Graham Davidson, we will be aiming to shift units across the board and there is no doubt that campaigns are now an essential part of our business."

The retail chain will be using MCI's Rave Anthems as part of its advertising campaign. Part of the Decadence imprint, these three-CD boxes are the result of a year-old cooperative venture with Ministry of Sound. "It's a good combination, as Ministry deal with licensing and packaging, while we are specialists in catalogue marketing," says Keene. "These relationships can only breed confidence when we negotiate with retailers."

The two companies have even branched out of the budget market to produce the TV-advertised album *Celtic Chillout*, which entered the charts three weeks ago at number 17. A forthcoming £3.99 budget campaign with Asda's distribution partner Handelman highlights the importance of building close relationships within the sector.



price drops are numerous. It could be that an album has reached the end of its life-cycle, having dropped out of the Top 200 and exhausted its promotional life as a new release; that it coincides with an awards

show like the Brits or Mobos; or that a new release is expected to raise interest in an artist's back catalogue. The end result, as described by Stanford, is a sort of sophisticated juggling act, with prices constantly on the move in response to market conditions. "Nine times out of ten, with every title we temporarily reduce to mid-price, you'll do three, four, five, six, seven times more than at full price. The great thing about mid-price is that you do see a huge uplift in sales and, for us, it's been like that since I've been doing the job for the past three years, and it's continuing like that. We are still seeing — on the right titles, reduced at the right time — a massive uplift in sales."

While the majors are actively stimulating their sales, the budget specialists rely on a customer's propensity to impulse-buy during multi-purchase campaigns. This offers the chance, not only to shift the significant stock volumes that would not be possible from the AZ racks, but also to raise label profile without a big marketing spend. For this reason, titles are commonly offered up for

promotion almost immediately.

For Laurie Adams, managing director at Delta Music, campaigns are an "essential sales tool for promoting our product, particularly in low seasons, when retailers need to encourage customers to keep spending. From our point of view, these campaigns can also gain us extra precious retail rack space, which is hard-won in competition with heavily-promoted product from major labels. The fact that the product is heavily discounted does not seem to affect the sales at a higher price during the rest of the year."

For Union Square, the budget compilation album *Funk Soul Brothers*, released on their Metro imprint, is a typical success story. "It gets picked up every time in the two-for-£10 or the four-for-£20 promotions. People see the names on it like Curtis Mayfield, Roy Ayers and Bobby Womack and at that sort of price it looks worth a punt. The great thing is, we're not reliant on spending a lot of marketing money to tell the consumer about the product. It's working as an impulse purchase."

But, if the major and budget labels are thriving on campaigns, for others the drive to discount prices is proving a contentious issue to say the least. One sales manager at a leading independent label complains that

the chains are too inflexible when it comes to liaising over discount terms.

"Slowly, over the course of the past three or four years, as campaigns have become the core of high street retail, the price mechanic has dramatically lowered in RRP value. This effectively means that we are being asked for higher and higher discounts and there comes a point where we just can't afford to even put these titles into campaigns. Parallel to this, they often dictate what price they think these albums should be. For example, a title that has steadily sold through at £9.99 is then requested to be £6.99; an inability to deliver that level of discount can sometimes mean no support in future campaigns."

One label that is working around this kind of catch-22 situation is Sanctuary. In addition to using loss leaders as a means of accessing rack space and promoting slower-selling stock, John Reed offers another example of how the company makes discounting work for itself. "With John Holt's 1,000 Volts Of Holt — a real reggae evergreen — we've created a deluxe double CD edition, but we're also keeping the original available because in that way we can actually target a given campaign. So if there is a campaign aimed at mid-price, we can still keep our luxury John Holt album at full price around £8.29 while the original is available at around £5.50. So if a retailer wants the John Holt album it gives us the flexibility to give them the product that fits in with the price of their campaign. Part of the reason we would have the two editions in the UK market is because of campaigns."

In this way, the label has increased control over what precisely is discounted and by what percentage. "It's give and take. Sanctuary has certainly benefited from having a good relationship with mainstream UK retailers and giving them what they want for campaigns, where other companies have felt that they couldn't compromise in that way. You suffer slight pain financially, but in the long term you benefit because, if you haven't got the retailers on your side you become marginalised." Recent successes include Dolly Parton's *Little Sparrow*, which was re-racked after Christmas following her TV appearances with Graham Norton in *Dollywood*.

Given that retail campaigns are here to stay, such tactics are surely the way forward. As Reed says: "You have to work on the premise that you miss most of the people most of the time and anything you can do to get to people has to be a good thing."

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**The major label: Warner Music**

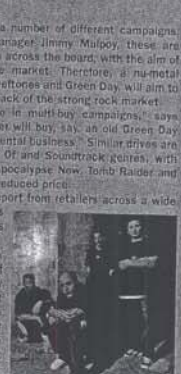


Alanis Morissette

Warner Music is currently running a number of different campaigns. According to senior accounts manager Jimmy Mulpooy, these are constructed in negotiation with retailers across the board, with the aim of profiting from dominant genres in the market. Therefore, a nu-metal promotion, including Kid Rock, Staind, Dillinger and Green Day, will aim to sell a variety of mid-price titles on the back of the strong rock market.

"The majority of mid-price sales are in multi-buy campaigns," says Mulpooy. "So the hope is that a customer will buy, say, an old Green Day album at mid-price and we'll gain incremental business." Similar drives are also being made on the booming *Best Of* and Soundtrack genres, with titles such as *The Best Of The Corrs*, *Apocalypse Now*, *Tomb Raider* and *The Beach* being offered to retailers at reduced prices.

Mulpooy adds: "We are looking for support from retailers across a wide range of our catalogue, and campaigns have become instrumental to our sales and our marketing." Aside from these discounts on back catalogue, the strategic process of temporary drops has become increasingly part of a product's shelf life. Recent sales success for Alanis Morissette's *Jagged Little Pill* and Supposed Former Infatuation Junkie at mid-price, after the release of her current *Under Rug Swept* album, are testament to this.





Comments on Universal complaint version history:

Version 1.1:

First distributed version

Version 1.2

Added comment to footnote 57

Comments from Jeremy Fabinyi added ( can be identified by different colour of the comments box)

Added 2 comments on page 38 re power of retailers

Added comment on first page of complaint re 2,5% return of value and the effect on the net rate paid by Universal

Added comments on page 19 re-online.

Added comments from Thierry Desurmont (TD)

Added comments from Ed Murphy

Version 1.3

§1.9 - Added Comparison between US:UK and BIEM royalty

§1.10 - Extract of the minutes of a BIEM/IFPI Negotiating Committee – 3 May 1983 + enclosure

Comments on price elasticity of a CD offer – Brian Hindley reports + enclosure

Fax to G. Taylor on ARP/PPD study

Added minimum royalty changes since 1975

§ 5.14 – Added comments from J. Fabinyi on Australian Copyright Tribunal decision + enclosure

§ 5.37 - Added comments tracks and increased sales of record + Enclosure

Enclosure 7 : Press Article : Record companies' accounting practices to be probed by joint Senate hearing in California” – Music & Copyright, 17 July 2002

Version 1.4

§1.9 Added Comments from Ralph Peer

SDRM Comparison between US and BIEM rate (enclosure 10)

§1.10 Added Comments on CD price and tables enclosed :

CD pricing breakdown (Understanding & Solutions)

Comparison of PPD applied by producers signatories of a central licensing agreement

European Comparison of price applied (Understanding & Solutions )

10 years of CD prices evolution compared to mechanical reproduction rate agreed between BIEM and IFPI

Added Comments from B. Hindley's report on “Price control and mechanical rights” (to be sent separately by fax), on minimum royalty and maximum tracks provisions.

§ 5.1 (iv) Added comments of the decision of the Italian Anti-trust authorities ( 9 October 1997) to be sent separately by fax)

(v) . Added comments form B. Hindley's report on “Price control and mechanical rights”

§5.26 Added Enclosure 11

§5.27 Added comments + enclosure on singles market

Version 1.5

Added Comments on Annex 6 and Annex 8 (+ enclosure 13)

§1.9, §5.45; §5.29. §5.30 - Added Comments from Peter Xanthopoulos

§ 1.10. §4.14. § 3.1.1. §3.1.2. §3.2.1. §5.1 (iii). §5.7. §5.19. §5.24. §5.27. §5.30. §5.37.- Added GEMA (e-mail 21/8/02)

§ 1.9 Typing error in Japan Tariff

Enclosure 8 : break down of CD pricing of France and the Netherlands

Enclosure 9 : Added example of GEMA

Enclosure 11 : Added figures from Italy, Spain and the Netherlands

Enclosure 13 : Evaluation of Mark-ups