From Owning to Using Music: Transactional Music Attorneys Struggle With A Changing Landscape and Its Financial Realities

By John Simson[1] and Ken Abdo[2]

It is nearly impossible to describe the momentous seismic shift that we have all witnessed over the past fifteen years with each new technological development and method of delivering music to consumers; it is probably enough to say that it's been a hell of a ride!

Transactional music attorneys have seen the transformation of five major labels into three major entertainment companies: no longer able to achieve the return on investment from CD sales that fueled their enormous growth in the 1980's and 1990's, they have tried to re-invent themselves as leaner, more agile, marketers and branders of recording artists. Record company executives have long claimed that it was record company money that built brands through the recordings they funded and released together with the promotion and marketing they advanced and administered. Tour support was frequently the only way that new bands could afford to tour and grow a fan base. Is it more surprising that for decades record labels didn't try to share in touring and that their attempts to share in other revenue streams, most notably merchandize and publishing, were on a "right to match" another company's offer and not compelled under the terms of the record deal? Now it is expected that

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recording agreements for new acts will contain “360” terms under which companies will participate in some, if not all entertainment related revenue streams generated by the artists they sign.

When examining the lower margins generated by single downloads and the deconstruction of the CD into individual digital download tracks, it becomes clear that the record companies’ return on investment is far lower than in the past. This means there is now far less to invest in developing bands. That critical development work is now left to the bands themselves or smaller independent labels. The companies don’t want to get the ball rolling. They want to acquire rolling balls. What does this mean for the lawyer who is asked to negotiate a deal? There is far less money now than was traditionally advanced in all recording and publishing deals which leaves less for legal fees.

The challenge for artists to make a living (let alone a killing) in the digital world has been well documented, with a new development emerging nearly each and every day. The resulting challenge for the entertainment bar has been less visible and not nearly as compelling! Fewer major label deals and less money in the deals that do happen has created angst amongst the transactional entertainment bar and for good reason. Those who bill on a percentage of revenue with very successful clients who earn significant amounts touring are less likely to be affected. But those whose stock and trade has been shopping and negotiating “baby band” deals may need to rethink their business model.

For the well positioned practitioner, the shift in the creation and delivery of entertainment has created new revenue opportunities. Music consumption is greater than it ever has been – even if it’s no longer measured in CD sales or even digital download sales. More and more companies want to learn about how they can use music, want to be involved in some way with recording artists and their brand. These Companies know that licensing of these rights can be confusing and difficult and that they need experts who can navigate these issues successfully.

The music economy and consumer habits are irrevocably moving from owning music to using music. As we’ve transitioned from an industry of purchased goods to one of access, the “listens” and “plays” have become the new purchases. Monetizing those uses has become paramount. The number of tracks streamed daily by Pandora, Spotify and other online services is staggering. Billions, yes, billions of tracks are being streamed daily. Revenue growth at Pandora and Sirius/XM Satellite Radio has been geometric. Sirius/XM, which launched a little over a decade ago, generates over $3 Billion in annual subscriber revenue in the United States alone and continues to grow in Canada and contributes about $250 Million in revenue to SoundExchange for artists and labels and additional revenues to songwriters and publishers. Pandora has not monetized as well as satellite radio but will still pay recording artists and labels well over $100 Million in 2012, and Pandora only exists within the United States due to licensing issues in other countries.

A recent NPD study quantified U.S. internet listening at 96 Million listeners per week while over-the-air radio still remains dominant with around 240 Million weekly listeners. It is clear that internet radio listening is growing quickly and that over-the-air radio is on a slow but steady decline. U.S. recording artists certainly understand the importance of this shift as they are able to monetize their streams on internet radio yet still are not paid from over-the-air radio spins. It is interesting to note that Clear

Channel has recently made private deals to share over-the-air radio revenues with artists and labels at Big Machines Records and Glassnote Records in exchange for steep discounts in what they pay for their online streaming. Will this trend continue with more and more labels signing private deals with the larger radio conglomerates which are trying to build online radio services? If the radio chains are hoping to give away some share in today's terrestrial radio revenue in exchange for dramatically reduced rates for streaming, it may be a wise business move. Though the terms of these private deals have not been disclosed, sources claim that in exchange for a small pro-rata share of over-the-air money, internet rates have been slashed far below the rates that SoundExchange currently collects from broadcasters who stream their signal on the internet. For Clear Channel and its "I Heart Radio" and CBS Radio, whose properties include Last.fm and who stream for AOL and Yahoo, these deals may be fabulous investments over the long term.

For the practitioner, this new area of revenue and growth requires a new found level of expertise: are private deals in the marketplace going to replace collective management of rights? What should my artists' share of such deals be? Is the discount being given for online streaming too steep? Can I protect my artist from these direct deals and ensure that they receive the equivalent of what they would have received under statutory license? It has forced the attorney to become more aware of legislative and regulatory battles, whether in Brussels, London or Washington, D.C. and to understand how these skirmishes will affect their clients' revenue streams in the end.

Another aspect of this shift in the music industry from purchases of goods to purchases of subscription or access to ad-supported listens is that the attorney must also become well-versed in issues surrounding subscription services like Spotify and Deezer... Should their clients participate in these services or withhold rights if they can? While Spotify and its equity investors claim the evidence doesn't support the claim that they have a substitutional impact on sales, some major artists like Taylor Swift and the Black Keys have withheld their content in recent months believing that these hold backs may increase full sale downloads and increase their overall revenue by doing so. They reason that if one can listen to a recording at anytime, why would that customer ever buy the recording? Consequently, these artists have withheld rights to their recordings believing that they will sell more copies if they're not available as on-demand streams.

For years it was understood that recorded music was a "penny business" over which pennies publishers, writers, labels and artists would fight. What has developed in the last decade is a micro-penny business in which services like Pandora pay twelve hundredths of a penny per stream (2012 statutory rate for Pureplay webcasters) and Spotify pays similarly small rates for each stream. The difficulty for the lawyer is the increasingly longer agreements and concomitant work in a constricting music economy. Royalty statements now fill thousands of pages. They contain incredible detail on a track-by-track basis which when added up may total a thousand dollars for a small label, a hundred thousand dollars for a good size independent and in the millions of dollars for a major (whose statements may be over 30,000 pages long!)

How do lawyers adapt in this new economy? The traditional album deal was the reference standard in the industry. Now, it may be a singles deal or a demo deal with far less money invested to control the

downside losses. Furthermore, the publishing deal that was often linked to the release of an album on a major label is also in decline. The deconstruction of the CD means that consumers are more likely buying the hits and not the entire album. Hence, publishers are selling one track and not 10 or 11. As the economics force these deals into lower advances for writers and artists, the lawyers too must adjust billing. Can an artist afford or even want to hire skilled attorneys at an hourly based fee for these deals when the cost of legal fees may now be out of proportion with the advances? Is taking a percentage of the deal the only way to make these fee arrangements work? If the percentage remains the same (traditionally 5%-10%) and the revenue is less, the lawyer is making less per transaction. In this way, the impact of the new music economy on artists is symmetrical with their lawyer.

While there have been some landmark deals over the past decade between recording artists and "non-traditional" partners: Jay-Z with LiveNation and Madonna with LiveNation, most notably, those are few and exceptional. Perhaps what is most surprising is that we have not seen technology companies, in any appreciable way, become the new record company. While talk of this emerging phenomenon was the rage a decade ago, it simply has not happened. While technology companies have made some strategic partnerships with artists, they are more similar to the endorsement or sponsorship deals of years past and not groundbreaking or creating a new landscape for recording artists or their lawyers! We have seen a few corporations add a record label to their product line, hoping to use music as a branding experience, but we've seen those same attempts over the past thirty years with mixed success. Perhaps those lawyers who have been dealmakers in the past with record companies and publishers need to think more broadly about who their clients' future partners might be.

Attorneys may also need to think more creatively about their clients' traditional output. If the sale of CD's is in decline, why not sell the rights to your next CD to a major player, be they retail or service business for their exclusive use? Imagine if Garth Brooks or Carrie Underwood's next release was only available to hear in-store at Wal-Mart or on Wal-Mart's website; Bruno Mars only available in H&M.

Newsflash: The demise of the major labels isn't imminent. Yes, there are fewer and they are more consolidated than ever, but that was the inevitable forces of the market at work when no one would assist these large corporations in combating piracy and the theft of their works. Half as many people to do twice as much work: the need for economies of scale is clear. What is also clear is that the three remaining majors own huge catalogues of valuable recordings, many of which they will likely control for many years to come: until 2067 in the United States (when the first copyright in sound recordings attached in 1972, Congress provided that any "pre-1972" work covered by common law or state copyright would expire by 2047, later extended to 2067 by the Sonny Bono Copyright Extension legislation) and roughly 2060 in Europe based upon the recent extension of sound recording copyrights to seventy years. The potential reversion of sound recording copyrights in the U.S. commencing in 2013 may create another new growth area for the entertainment bar: whether in litigation over ownership of sound recordings or in renegotiation with the current owners for the recovery of works in the future. While most of the ink has been written about the decline of the majors and the piracy that has gutted their sales, a parallel story has been the rise of the DIY artist who now has the tools to compete online with major label artists. But has the evidence borne this out?

It is certainly true that we've seen a rise in companies designed to assist unsigned and independent artists in all facets of their career: SonicBids, ReverbNation, TuneCore, CD Baby, the Orchard; digital distributors like IODA, InGrooves and IRIS all trying to ensure that DIY and independent product is available on digital services. But at what cost? What business model?

Many artists are forced to pay "load fees" to get their work uploaded. Many never recoup those fees. While there have been one or two DIY major success stories, that is not the case for most artists who fight day in and day out to emerge from a very cluttered and unfiltered universe. New filters are emerging, whether blogs or the Music Genome Project or EchoNest or other services that try to assist consumers in finding things they like. Tastemakers are still important, they matter. But as most artists find out, sooner or later, it is hard to compete with artists on major labels who have hundreds of thousands and sometimes millions of dollars behind them in marketing and promotional costs, not to mention the relationships that these labels possess with the major television programs that showcase new and developing artists alongside superstars.

The good news for niche artists and artists who in previous generations would have had a hard time finding the money to record and an outlet for their recordings once finished, technology has made it cheaper to record and it is easier to self-release than it has ever been.

What is still a challenge is for these DIY artists to afford competent counsel who have been used to charging "major label rates" and who are priced out of the DIY market. How does the entertainment bar handles this new explosion of DIY artists who are in constant need of help but who can't afford the hourly rates of most entertainment law firms? While the agreements proffered by many of these new companies are far shorter than major labels, the rights being requested are important and can have serious consequences. Perhaps a discounted hourly or negotiated rate is offered, but often, when these artists are quoted rates, even at the lower end of the experienced entertainment bar's spectrum, they simply turn away as they can't afford the expense.

The transformation of the past decade has been monumental for our industry and the challenge to the entertainment bar no less so. Acquiring new areas of expertise, whether they be in technology, in regulatory matters affecting copyright and entertainment or in collective management of rights, have been a positive development for the practicing entertainment attorney. But the challenges of a world with new services daily, each with a different business model, some with no business model, and more and more paper, whether in the form of contracts or royalty statements to examine and fewer and fewer dollars for all but the most successful superstars has created an environment much different than that which existed before the turn of the century. Lawyers must be more knowledgeable and creative than ever to continue to expand their practices and to become even more effective advocates for those they represent.

The Artist Attorney's Expanded Role in the New Music Business[1]

By Kenneth J. Abdo[2]

The Old and the New Music Business

The old music business started when Thomas Alva Edison's words "Mary had a little lamb," came scratching off a mechanical cylinder in 1877 thus birthing the gramophone and the recorded music era. About 100 years later in 1972, and occasioned by the commercial introduction of cassette tape technology, the U.S. Copyright Act was amended to create a Copyright in sound recordings. About 10 years later, in the mid 1980's, vinyl records and cassette tapes began to be replaced by digital compact discs. About 10 years after that, in the mid 1990's, CD sales dominated. By 2007, the full implication of alternative digital distributions was recognized as the industry started irrevocably turning away from physical music products as the economic standard. At this point, 130 years after it was created, the recorded music business lost its old groove.

In the new music business, the entire concept of buying music to own is evaporating into the cloud and migrating into other digital platforms. Major recording companies have consolidated and downsized. The new music business is becoming more decentralized. Developing artists are finding ways to finance, record, distribute, and promote their recorded and live music performances effectively without the assistance and services provided through a traditional record company. All recording deals for new artists (and even re-negotiated deals for some established artists) are based on smaller recording funds (recording budget and advances) and required the artist to share revenues with the company from all artist income sources via the so-called 360 deals. *American Idol, The Voice, The X-Factor* and similar music/contest-based deals provide that winning contestants assign ownership and /or control of all recording merchandising, touring and management rights to the TV production entity or one of its subsidies. For a developing artist in general, there is less development money available under any recording, publishing and/or development deals. Furthermore, it is more difficult for developing artists to attract bona fide talent agents, personal managers, business managers, attorneys, record labels, and/or publishers until the artist proves they have real commerce, i.e., a demonstrated audience and the ability to pay for professional services. To distinguish themselves, artists must be extraordinary…for starters. They also must be more

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[1] Article appeared in Building Your Artist's Brand as a Business (IAEL 2011)

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entrepreneurial. This reality will certainly create a new generation of artists that are perhaps as adept at business as they are at music.

Most businesses are operated through a business entity and the entertainment business is no different. The corporate form is very common. For the purpose of understanding the functions of the artist's advisory team, a comparison to the traditional executive team for companies may be useful. Other chapters in this collection explore such comparisons in greater detail. The major difference however is that traditional corporations usually engage key team members as full-time employees of the company. The artist's team is comprised of independent advisors with whom the artist contracts for services. In this schematic and in this new and highly consolidated music business, the entertainment attorney's role is akin to serving as the artist's general counsel.

The Artist's Team

Agent: A music agent's work is generally limited to soliciting and procuring engagements for live performances, personal appearances, endorsements, sponsorships, and other entertainment related opportunities which can extend to reality television and film. In the U.S. agents are highly regulated and must be licensed. The rules and laws for same vary state to state.

Personal Manager: The artist's principal career advisor is the personal manager whose duties include daily management and strategic career development planning. They are usually fully involved with all artist business and logistics. Unlike agents, personal managers are not required to be licensed through state administrative agencies. Personal managers are usually engaged under a contract for a term of years and are paid a commission usually from 15% to 20% on a negotiated net income applicable to all entertainment revenue sources earned by the artist. A negotiated post-term sunset commission on net is also commonly paid. There are other important services provided to the artist which may be available through the management company or via the manager's relationships. Such services may (or may not) be included in the personal management commission. The services may also be arranged with third parties who report to the personal manager such as a tour manager or an outside publicist.

Other such third party services providers may include a technologists and social network staff, promotion and marketing executives, etc. As recording companies are downsized, management companies are providing (or arranging for such services directly)which were traditionally provided by the recording company. Sometimes the company will provide the artist additional funds for these services, to be managed by the manager, as a recoupable advance to the artist.

Business Managers: In the United States, most business managers are also Certified Public Accountants or have them in their firm. Their services are provided independently from the personal management company. Business managers work closely with personal managers to oversee the finances of the artist's business including accounting for income, payment of expenses, bookkeeping, and filing tax returns. The fee for services is either on an hourly basis or, more commonly, 5% of the artist's net revenue calculated essentially on the same basis as the personal manager's commission. However, the services agreement is generally not for a pre-set term of time nor is there a post-term sunset provision.

Entertainment Attorneys: The artist's entertainment attorney is engaged to negotiate contracts, render advice on legal and business matters, advocate the artist's position, protect the artist's legal interests, and oversee the work required and provided by other attorneys from time to time. The practice of entertainment law is broad. For a music artist whose career expands into multiple entertainment mediums and media (music, film, TV, theater, literary publishing, etc), domestically and internationally, a variety of legal expertise may be required. If the entertainment attorney's firm does not provide this expertise, the entertainment attorney is generally charged with identifying and engaging outside counsel on behalf of the artist. Such legal services may include litigation, immigration, real estate, criminal defense, estate planning and more.

The Expanding Entertainment Attorney's Role

As general counsel of the artist's brand and businesses, the entertainment attorney's role expands further when the artist enters into multiple agreements such as recording, distribution, music publishing, merchandising, sponsorships, endorsements, private financing, live performances (and their broadcast), etc. In addition, burgeoning and multiplying new digitally-based exploitation and distribution alternatives have necessitated the need for transactional attorneys to educate and advocate across many media platforms. In addition, the artist's business may involve transactions or litigations in various jurisdictions both domestically and internationally.

With even minor success, an artist's business and brand building transactions are part of interstate and international commerce. It is now expected that the transactional entertainment attorney not only have substantive knowledge needed to negotiate contracts but that he/she has a complete understanding of the music business in general which includes all issues related to licensing matters on new and evolving digital platforms. New precedent is being established as licenses and these deals are often driven by new technologies.Attorneys are often a part of creating architecture and deal term precedents.

As the artist's brand and businesses expand, so does the need to address other ancillary brand protection issues such as rights of publicity, privacy, and use of name and likeness. Counsel may be required on non-entertainment matters such as estate planning, family matters (from pre-nuptial agreements, adoption, to divorce and post divorce matters), wealth management, active and passive outside business investments, real estate transactions, and other legal matters. As the artist gets older and inevitably passes on, the estate matters are pronounced. The estate (with related control and governance issues) may become the client while attorneys work with family members, trustees, and personal representatives of the estate. Some attorneys are even appointed as trustees or personal representatives of these estates and perhaps heirs.

Relationships are Essential

Some attorneys are more proactive than others with respect to identifying and bringing income producing and career enhancing opportunities to their clients by way of their relationships. In this regard, the attorney's role may at times overlap those of the agent or managers. Such efforts may include seeking (or shopping) a recording agreement, packaging the artist to play on a hit television show for the purpose of promoting a song or album, connecting artists with others for co-writing, recommending various producers or other creative or business people for possible collaborations. Taking into account the foregoing, the entertainment attorney will work in tandem with the manager and/or the agent to help create symbiotic relationships among each other and with other third parties. In addition, because the attorney-client relationship is one built on the duty of loyalty and trust, the artist may look to the attorney to help build (or rebuild) a his/her team by recommending the artist to managers, business managers and agents with who the attorney may have established relationships.

Notwithstanding the proactive (non-legal) work they may be willing to undertake, the entertainment attorney is ultimately responsible for making sure all legal and business details are addressed and resolved. Attorney work is highly valued when all transactions are properly evaluated, documents are fully negotiated, and final agreements are fully distributed. As the artist brand expands across new products and in various countries, there also needs to be ongoing vigilance to make sure that registered rights are renewed, notice deadlines do not lapse, and intellectual property rights (including an artist's name and likeness, publicity, and privacy rights) are protected. However, a particular entertainment attorney may be desirable just as much for who they may know as what they know because certain personal and strategic relationships help create opportunities and help expedite legal and non legal tasks.

Compensation for Attorney Services

Attorney services are usually secured under the terms of a written agreement. Clients can terminate this agreement at any time subject to payment for services rendered. If the agreement provides for compensation based on an hourly rate, the rate for the attorney's services should be stated in the agreement. Hourly rates for very experienced entertainment attorneys range from $300 to $500+ per hour.

Percentage or contingency fee (a fee dependent on an outcome) must be in writing. A customary percentage fee ranges from 5% to 10% of a negotiated and defined net income earned by the client (often calculated similarly to the personal manager's commission) or on a particular deal. The exact percentage depends on the value the attorney brings to the deal-making (perhaps including shopping or bringing the deal to the artist), the risk of time, and whether the attorney will be responsible for working on non-income generating tasks as well and income generating deals. The earning capacity of the client is also a factor. For example, it is reasonable with an established artist to take a lower percentage of the income than with a new act. Some arrangements are hybrid where a lower contingency fee is expected if coupled with a reduced hourly fee. In both the hourly rate and the contingency fee arrangements, the client usually pays the out-of-pocket costs specifically expended because of a direct need for an artist such as delivery costs, travel related costs, filing fees, etc. Larger costs usually require pre-approval by the artist as a condition for payment.

The client may pay the contingency fee for the attorney's past services even after the representation is terminated. Depending on the nature of the work, the length of time services were rendered on a speculative fee basis and the actual income received by the attorney for this work, a negotiated sunset provision and payment may granted to an attorney. If the attorney provided general services on a contingent fee basis, the sunset period could extend from 6 months to perhaps as long as income may be received on certain transactions where the attorney helped to procure and secure a deal for the client.

In many states, contingent fee agreements must be in writing, signed by the client, and state the method by which fees are to be determined, the percentage or percentages that shall accrue to the attorney in transactional matters or in litigation matters, in the event of litigated matters: settlement, trial, or appeal, The agreement must clearly notify the client of any expenses for which the client will be liable regardless of outcomes.

Most states in the U.S. require hourly and contingent fees to be reasonable. Under the Model Rules promulgated by the American Bar Association, which are adopted in some form by most U.S. states, attorneys can consider the following criteria in determining a reasonable fee: "the time and labor required, the novelty and difficulty of the questions involved, the skill requisite to perform the legal service properly; . . . the fee customarily charged in

the locality for similar legal services; the amount involved and the results obtained; . . . the experience, reputation, and the ability of the attorney or attorneys performing the services required; and whether the fee is fixed or contingent." These criteria offer attorneys great flexibility and protection in charging fees.

Conclusion

Representing music artists gives rise to opportunities to work with the artist's team ranging from a strategic advisor on legally technical matters, to functioning as the general counsel charged with overseeing all legal matters affecting the artist's professional career and personal matters. There are also opportunities to help expand the artist's business and brand by assisting seeking and securing income producing opportunities. An experienced attorney is often the most familiar with the deal points and architect of various transactions. Along with this experience, many helpful relationships are developed. It is a business where attorneys are valued for not only what they know but who they know. As the new music business is becoming more decentralized and global, there there are fewer opportunities for developing artists to work with traditional recording companies. Contemporary recording, distribution and promotion options have created the ability for artists to self-develop and to operate artist-owned entertainment businesses creating he option to assign (or not) exploitation rights to other companies. Technology is creating new and expanding exploitation platforms for artist content. As a result, in the new music business, the entertainment attorney's role is expanding axiomatically.

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