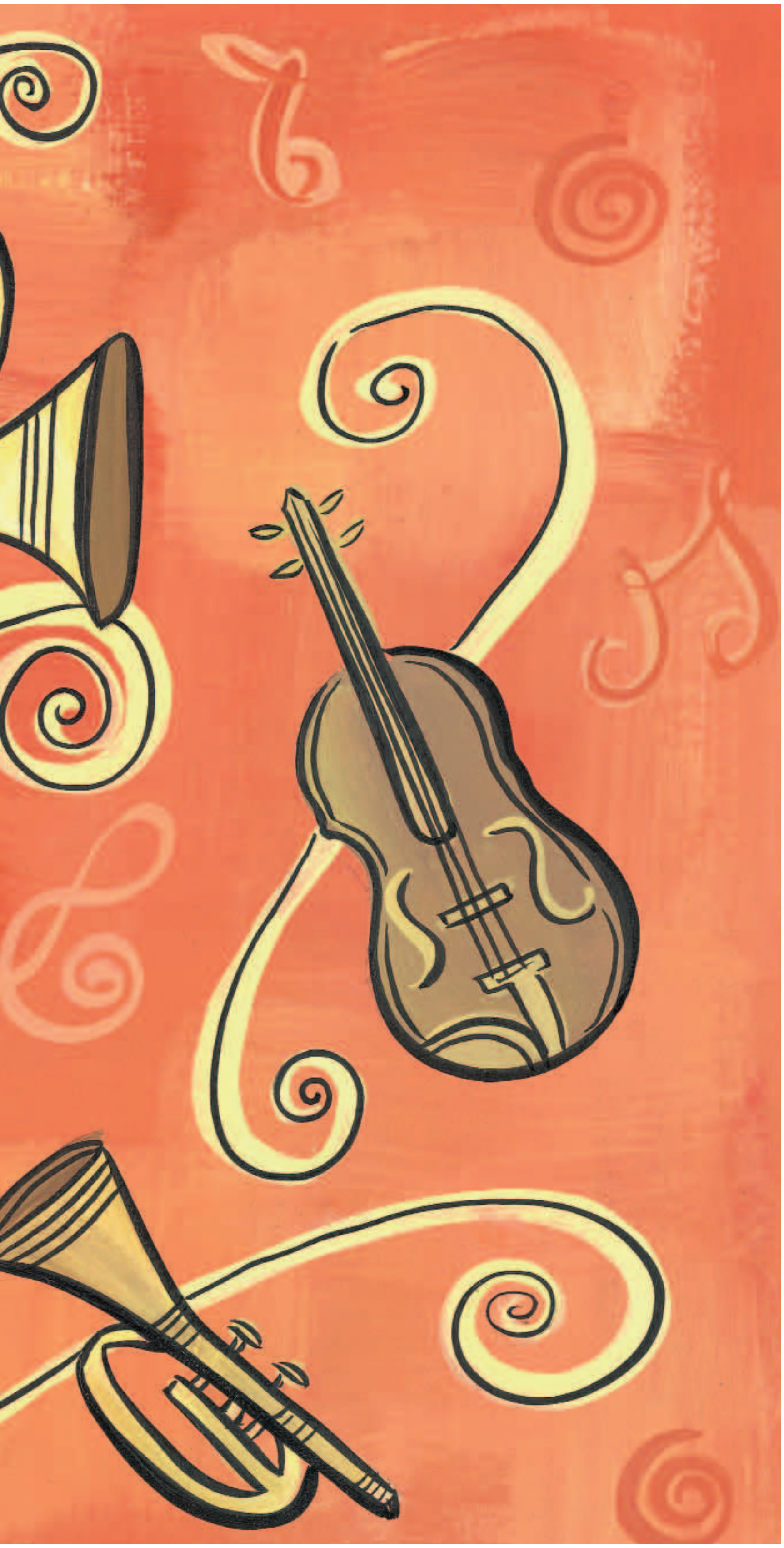
# Tug of War in the

# Music Biz

## Squabbling over the Entertainment Dollar or a Slice of the Music Business Pie



by Jerry Bailey

The music industry is—more than ever—as unpredictable as Tennessee's springtime weather. While nobody can do much about the weather, it seems everybody is trying to alter the music industry for personal advantage, with varying degrees of success.

The record industry feeds on change. Entertainers from previous decades still draw large audiences and sell respectable numbers of albums, but the younger generation of listeners always wants its own icons. New acts broke through the haze with limited results last year, and profits were elusive. The weak economy, Internet file sharing, congressional tampering, and the fickle minds of young consumers are forcing the music industry to build a new business model. On the local front, many observers say the country music industry is still suffering from a long hard winter—one that has lasted about three years and shows little sign of letting up. Nashville's record labels have pruned their staffs, artist rosters, and promotion budgets. Almost everyone agrees business is going to get better, and it has been worse—but that's little consolation when stockholders grow impatient.

Some people always find a way to make money, even in the worst of times. Those who've been around long enough to have a sense of country music history are quick to point out the cycles of their industry—swinging like a pendulum, but continuously growing. New talent, like the first robin of spring, still finds its way to the top of the record charts. Names like Cyndi Thompson, Steve Holy, and Chris Cagle offer hope for a better year. On Music Row, the decision-makers plot their strategies and watch to see who will be the next Garth Brooks, Shania Twain, or Faith Hill. Careers rise and fall at the whim of radio programmers and country fans. Will the next superstar be Southern-traditional like Alan Jackson, cowboy-cool like George Strait, or outlandishly hip like the Dixie Chicks? Viewing the success of the *O Brother, Where Art Thou?* soundtrack, some observers are betting bluegrass will enjoy a growth surge with young performers such as Nickel Creek. On the heels of Garth's announced retirement, Music Row has been praying for a new Messiah. Anxiety has replaced confidence. As months turned into years, winter coats have become year-round attire in a figurative sense on Sixteenth Avenue.

Country album sales recovered slightly during 2001, but ended the year 7.4 percent below 1998 levels. Country music sold 67.2 million units, up 1.3 million units from 2000, according to SoundScan's Year-End Music Industry Report. The top five country albums for 2001 accounted

continued on page 4

continued from page 3

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for seven percent fewer units than in 2000, while the top 10 selling albums were down three percent. It's still cold out there.

For other types of music, business isn't much better. The Recording Industry Association of America (RIAA) recently announced the number of units shipped domestically from record companies to retail outlets, record clubs, and mail order fell 10.3 percent in 2001. Total U.S. shipments dropped from 1.08 billion units shipped in 2000 to 968.58 million in 2001. The dollar value of all music product shipments, according to the RIAA, decreased from $14.3 billion in 2000 to $13.7 billion in 2001—a 4.1 percent decrease. (One bright spot was Christian and gospel music, which enjoyed a sales spike after September 11.) The year 2001 marked the first decline in CD sales in a decade. Four of the five big record companies—BMG, EMI, Warner, and Sony—reported lower earnings last year. Only Universal managed to show growth.

Some success stories did surface last year, but not enough to carry the industry. Three very different artists claimed big pieces of the cake. Reggae crossover artist Shaggy scored with the best selling record of 2001, according to the RIAA. His album *Hotshot* was certified six times platinum. Following closely behind with sales of three million copies were Irish new age artist Enya with *A Day Without Rain* and the 'N Sync CD *Celebrity*. In the world of country music, the soundtrack to *O Brother, Where Art Thou?* sold three million copies, was crowned Album of the Year at the 2001 Country Music Association Awards in October, and won the Album of the Year Grammy. Garth Brooks came through late in the year with the release of *Scarecrow*, his 14th album for Capitol Nashville. Certified for sales of more than three million copies, it was the best selling country record of the year. His *Double Live* record added another million as well and has been certified for sales of more than 14 million copies. All told, Brooks further lengthened his lead as the highest certified solo artist in history with his cumulative sales now topping 104 million.

While record sales were generally soft, the industry's problems didn't stop there. Music lovers didn't go to concerts as in the good old days. According to *Pollstar* magazine, concert attendance was off 12 percent during the first six months of 2001. After the September 11 terrorist attacks, many artists cancelled tours, fans stayed home, and the concert business came to a standstill. Disillusioned fans pointed to high ticket prices and growing add-on service fees facilitated by consolidation of the companies dominating the concert business. Concertgoers often chose another form of entertainment rather than submit to a shakedown at the Ticketmaster box office. According to *Amusement*

*Business*, Tim McGraw had the top grossing country tour of 2001 with $23.5 million. Brooks and Dunn's "Neon Circus" tour ranked second among country acts with $17.6 million in ticket sales.

Conflicting opinions for the entertainment industry's poor business climate are not hard to find. Record companies primarily blame Internet theft of their music. At its peak in early 2001, the Napster online file-sharing service had 80 million registered users and downloaded as many as three billion songs each month. For the record companies, competing with such services is like trying to sell ice at the North Pole.

"This past year was difficult in the recording industry, and there is no simple explanation for the decrease in sales," said Hilary Rosen, President and CEO of the RIAA. "The economy was slow, and September 11 interrupted the fourth-quarter plans, but a large factor contributing to the decrease in overall shipments last year is online piracy and CD-burning. When 23 percent of surveyed music consumers say they are not buying more music because they are downloading or copying their music free, we cannot ignore the impact on the marketplace."

Napster was hobbled by federal courts later in the year, but other peer-to-peer file-swapping services such as Music City, KaZaA, and Audiogalaxy, among many, continued to exchange millions of songs per week. One company that tracks online piracy activities, NetPD, recently reported that 2.5 million copyrighted and generic files exchanged hands in a six-minute period, a typical tally. Web services that encourage swapping face their own lawsuits from record companies and music publishers, but they may not yield as quickly as Napster. The Napster successors don't store titles in a central network that can be easily shut down, and the software creators say they don't know what files their users are sharing. Each user's computer becomes a virtual server, making prosecution much more difficult. As the legal wheels slowly turn, millions of music consumers are losing interest in paying for music. Consumers complain that the price of commercially recorded CDs has gotten too high, or that the quality and quantity of music on the typical record company offering is too low. At the same time, sales of blank CD-R disks—used by computer owners to create their own custom albums from songs downloaded from the Internet—is booming. Sales of blank disks increased 50 percent last year, reaching 1.2 billion units, while about 750 million pieces of prepackaged music were sold last year in the United States. Growing numbers of consumers prefer to build their own CDs, selecting only the songs they like, spending a fraction of what they might spend on record company products.

Internet theft of copyright materials extends beyond music, and pirates operating under the nose of indifferent governments are growing bolder. One Taiwanese website was selling streams of new and classic Hollywood movies for $1 each. The site offered thousands of American movies along with Japanese and Chinese films. For a $1 fee, users received three days of unlimited access to RealVideo versions of each movie. Taiwan's copyright laws are similar to those of many other nations, and the website appears to be operating illegally, but enforcement by that government has been notoriously weak. The International Intellectual Property Association (IIPA) estimates that in the year 2000, American companies lost more than $550 million due to piracy in Taiwan.

The immediate problems are formidable, but copyright owners are forging new weapons for their war against piracy. A Dutch businessman recently stopped distribution of the KaZaA file trading application while he contends with separate lawsuits against him in the Netherlands and the United States. Even more promising, an international pact to protect artists and the music industry will go into force in May. The treaty was fully ratified on February 20, when Honduras became the 30th country to join formally, according to an announcement by the World Intellectual Property Organization (WIPO). The new accord, called the WIPO Phonograms and Performances Treaty (WPPT), bars unauthorized exploitation of recorded and live performances on the Internet. WIPO noted that the pact also gives recording artists and record companies the right to use technology to block the unlicensed reproduction of their work on the Internet.

Bertelsmann Music Group (BMG) and Napster announced an agreement last October to develop a membership-based music distribution service that would pay royalties to artists, record com-

continued on page 6

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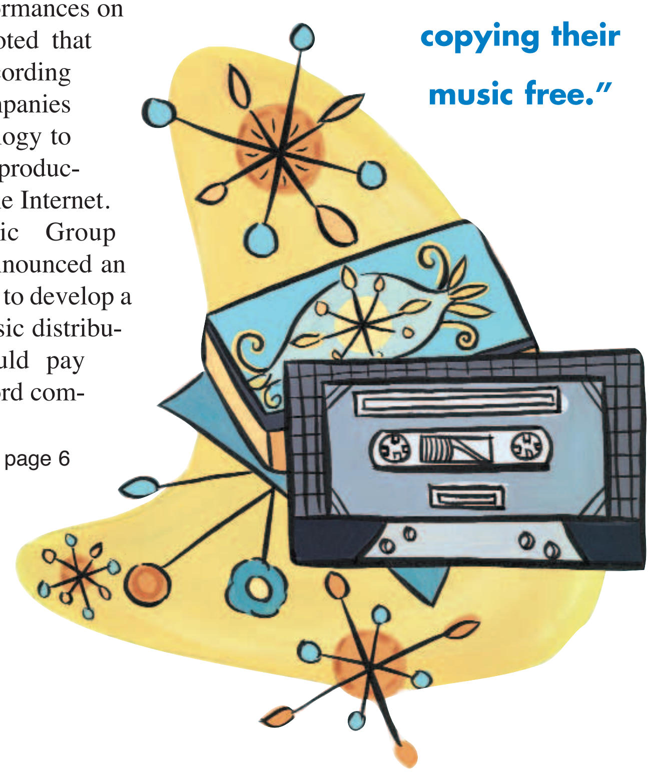

continued from page 5

**Record companies have created their own Internet music services.**

panies, and songwriters. A slimmed-down version of Napster went online earlier this year, offering users a much smaller catalog of songs for a monthly fee. In the meantime, the record companies have created their own Internet music services. Launched in December, Pressplay offers subscribers access to a wide assortment of music through streaming, downloading, and CD-burning. Pressplay gives fans access to a vast online library, including music from the world's three largest record companies—Universal, Sony, and EMI. Pressplay and BMI announced an agreement in late January for use of the 4.5 million songs in the BMI repertoire, representing 300,000 songwriters and music publishers. MusicNet is another online subscription service with major label support, operated by EMI, BMG, and Warner with RealNetworks. Most major labels also offer downloads for a price from their own websites, but reviewers have been lukewarm in their reviews of these services. Their future, of course, hangs on the outcome of lawsuits to shutter free file-swapping websites. Consumers are not inclined to pay for music they can get free elsewhere.

A few signs of hope are emerging from the quagmire of lawsuits, loss statements, and congressional lobbying. One digital music subscription service announced recently that it had negotiated through the tricky licensing issues plaguing other companies and is moving toward a healthy business model. MusicMatch's Radio MX has become the largest music-only subscription service. Listeners can't choose specific songs or the order in which they are played, but can select what type of music they want to hear, along with the artists that are randomly played. Such restrictions on how music is delivered are important in distinguishing webcasts, the Internet equivalent of radio, and online music services, which offer a greater sense of music ownership.

Even if the Internet and the pirates who prowl its waters were to vanish tomorrow, Nashville's music makers would be far from content. For as many years as anybody can remember, whenever country music profits have fallen, a verbal war has broken out between radio and record companies. Neither can exist without the other, and neither is entirely in control of its fortunes. If country radio loses listeners, programmers blame the labels for not giving consumers what they want to buy. When record company profits slip, record promoters blame radio stations for not playing the songs consumers want to hear. Currently, country radio market share is the lowest in a decade, well below the peak years of the mid-1990s. The latest controversy focuses on consolidation of radio station ownership. Clear Channel Communications owns more than 1,200 stations, as well as SFX, the nation's largest concert promotion company. Some record executives think such consolidation strangles artists who stray from the mainstream. Some go so far as to argue that the demographic of country music listeners is being altered by radio stations following conservative playlists.

While the country music industry worries about a declining audience in its market segment, some lawmakers are complaining that, on a larger scale, radio stations and record moguls are entirely too cozy in selecting what music is played. Rep. John Conyers, Jr. (D-Mich), plans to launch federal hearings this year to address complaints about payments to radio stations for playing certain songs. It's been 40 years since the federal payola statute was enacted and more than a decade since a major payola investigation. While it's illegal to air a song for money without telling listeners, record companies spend an estimated $100 million per year to influence broadcasters. Companies allegedly sidestep the law by hiring independent promoters who pay stations annual budgets to avoid the appearance of paying for individual plays.

Even as record companies pay radio stations under the table, they are exploring new avenues to win back from radio some of that money through Internet broadcasting. The pair have been at odds in recent years over how much record companies should be paid, if anything, when radio stations stream their signals over the Internet. The debate began in 1995 when Congress enacted the Digital Performance Right in Sound Recordings Act (DPRA), which envisioned Internet digital music broadcasting as a form of online radio. The Digital Millennium Copyright Act (DMCA) reinforced that law in 1998. The record companies asked the U.S. Copyright Office to convene a Copyright Arbitration Royalty Panel (CARP) to settle the dispute over royalty rates. In February, the panel suggested a rate about 10 times higher than that proposed by the webcasters, but half as much as the record companies sought. After the CARP recommendation, some webcasters began forecasting doom, or at least a difficult future, for their businesses.

The record companies created a new performance rights collection agency called SoundExchange early last year to collect and distribute the performance royalties from webcasters as well as from cable and satellite subscription services. Later in the year, the five major label groups—Sony, Universal, BMG, EMI, and Warner—agreed to allow SoundExchange to pay artists directly for the 2001 distribution cycle. This was a victory for recording artists because their share of the royalties would not be applied toward any un-recouped advances they might owe the record companies.

For each step forward, the record companies take two steps back, for they also appear to be losing ground in their relationships with the artists they promote. California state senator Kevin Murray (D-Culver City) launched an attack against the music industry on behalf of stars like Courtney Love and Don Henley, who claim the record companies have too much control over their careers. Murray introduced a bill before the state legislature in January to repeal an amendment the music industry won in 1987 that ties recording artists to personal contracts longer than talent in other industries such as film and television.

Executives from nine record companies sent a letter to Murray opposing repeal of the amendment. They contend less than 10 percent of the recordings released each year are able to generate a profit. They insist on the need for the long duration of recording contracts to help the companies turn a profit. On the opposing side, several stars formed a group known as the Recording Artists Coalition (RAC), saying young artists are forced to accept impossible terms when signing recording contracts. If the artists later break those contracts, they can be sued for millions. Sheryl Crow, Stevie Nicks, Carole King, and Don Henley are among those who spoke out in support of the Murray bill.

The rights of recording artists are also finding a sympathetic ear in Washington. Last fall, Congress passed a work-for-hire bill that repeals a 1999 law initiated by the RIAA that made sound recordings a new category of "work made for hire" under the U.S. Copyright Act. The 1999 change in the law took away the termination rights granted to artists to reclaim authorship of their recordings in the future. The new law restores that eligibility. Sen. Orrin Hatch (R-Utah), the chairman of the Senate Judiciary Committee and a major supporter of the repeal measure, promised to further address the rights of recording artists and their relationship to record labels in the coming year.

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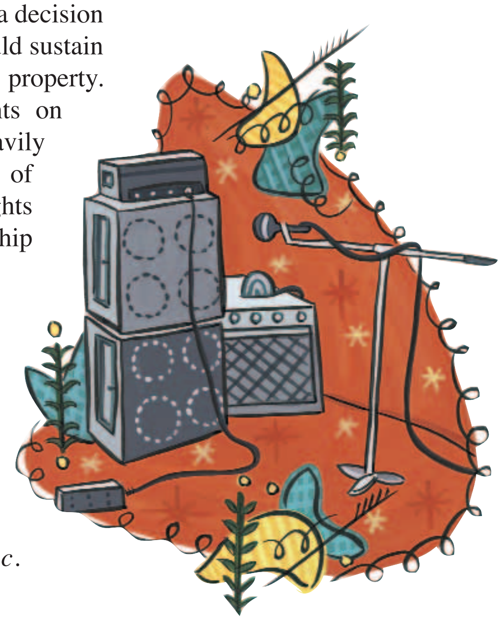
The transition of the music industry kept a frantic pace in 2001, and upcoming months could be even more unpredictable. Beleaguered songwriters and publishers, along with book authors and other inventors, will face a decision from the U.S. Supreme Court that could sustain or reduce the life of their intellectual property. The Court agreed to hear arguments on whether Congress has sided too heavily with creators in setting the duration of copyright protection. While copyrights lasted only 14 years in 1790, ownership is now recognized for 70 years beyond the life of the creator.



Nothing remains unchanged for long in the music business. As quickly as an issue is declared dead, somebody digs up a skeleton. ■

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