Distribution and Licence Deals

The decision on whether to go for a distribution or a licence deal is a difficult one. On the one hand, a distribution deal provides the development of a long-term income stream whereas a licence deal is attractive with its immediate cash offering. Ann Harrison has kindly written notes to detail the features of both types of deals. Please contact WMF if you would like any further help in making a decision.

Below are some of the key areas that have to be discussed and agreed on with first, a distribution deal and second, a licence deal. I stress that these are just by way of guidance only. This note is not intended to be in place of proper legal advice on the individual circumstances of you and your deal. It is intended to give you an overview and to help you have a better informed discussion with companies you would like to do business with internationally. ***If in doubt take independent legal advice.***

The key difference between the two is that in a **licence** deal the company you licence to usually manufactures and packages the records for the local market and sells them via their own distribution network.

With a **distribution** deal you provide finished, manufactured product to a company already packaged and they distribute it direct to the stores. You will probably also have to supply promotion people and pay extra for a telesales team or additional sales assistance if it is necessary. You will also have to cover payment of all licence fees for the use of the songs on the recordings. Check your position with MCPS member services.

In **neither case** should you **sell** your **copyright** in the record/artwork/videos etc. If they want to talk about a sale then that's a much bigger deal as you will lose all intellectual property rights and so need to know you have been properly advised on the deal and the price on offer. If in doubt ask for a written proposal and take it away to think about and get advice on.

Please note that with both a licence and a distribution deal the company you are doing the deal with will almost inevitably ask for **digital** rights. If these are to be given **non-exclusively** then it's worth considering. If its **exclusive** then think very carefully about it as an exclusive deal will mean that you cannot then offer digital download rights for that country to companies like I-tunes or aggregators like The Orchard. So you have to be as sure as you can be that you are getting the best deal you can for those rights.

Distribution deals:

Territory: in what countries do they want to do business with you? In some cases this will be a world deal (and if it is you may want to get some specific advice on it) but in most cases it will be for a limited area, for example, North America; USA and/or Canada. You can only consider doing this if you have not already granted exclusive rights in the same recordings for that country. If you have granted non-exclusive rights e.g. for a compilation then you can still do the deal but you have to tell them about these other deals so that this does not cause problems down the line.

It is possible to limit digital rights to a particular country despite the global nature of the Internet but they will often try and get world rights. So think carefully if you want to do that and whether it might screw up some other plans you may have for online sales e.g. sales off your website as downloads.

Rights granted: this could be for just physical releases or for physical and digital. It could go wider still and cover exclusive rights to grant licences to use the recordings with visual images in things like ads and films. Do you want to go that far? Do you want to grant non-exclusive rights or keep the rights out altogether because for example you already have someone on board finding these kinds of opportunities for you?

What product? The offer could be just for one single or album or it could be for your whole existing and some future output. Decide what sort of deal you want to do and don't be sidetracked into agreeing future product options unless you are as sure as you can be that this is a good and reliable company to work with.

Term – how long? A distribution deal usually runs for a minimum of one year but can be longer – they should not go beyond 3 years unless they are a very reliable and reputable company that you want to develop a longer term relationship with. Beware of deals that extend until you are not in debt to them as this could make it open ended. Even if the deal doesn't work out and there are outstanding debts there should still be an end point.

Advances: It is unlikely, unless you have a very hot product that they will want to pay and advance up-front. They may help to cover some of your manufacturing or packaging or shipping costs but all these sums are not gifts, they come out of your earnings first before you see any more money.

Royalties/Fees: In the case of a distribution deal these are usually a percentage of the gross fees they receive after discounts and free goods and after tax and are variable. If you have no track record or are in a small niche market where you are unlikely to sell many copies the percentage could be as high as 30% although **25**% is more common. The more bargaining power you have the more you can drive that figure down. Some of the big independent labels have **15**% deals and the majors are in single figures. But don't just focus on the number. Ask them to do you an example of what income comes in and what goes out before their percentage is applied and how much is payable to you at the end of the day. If they won't do that then ask for a clear explanation of what is deducted before you agree to the number.

Consider if their percentage should go down as you get more success i.e as your turnover goes up so their fee goes down so that it's a smaller amount of a bigger pie.

This line of argument is only sensibly worth running if there is a good chance of it happening otherwise you risk upsetting them.

Accounting: This is when they pay you your share and so the shorter you can sensibly make it the better but you have to be practical and most distributors will have a fairly fixed accounting system. Half at 45 days following the end of a month and the balance another 30-45 days later is common. Consider how this will affect your cash flow until the money starts to come through and make sure you aren't obliged to pay your artist money before you have got it in from the distributor.

Additional services: Distributors may offer other services like street or telesales teams. Find out what they offer and what they charge and if you can shop around to see if it's a good deal before agreeing to add this to the shopping cart.

Terms of business: The distributor will have business terms with its dealers and retail outlets on things like what discounts they get (sometimes called file discounts) and what free goods allowances they have and when they get paid.   You will be stuck with these same terms so make sure you know what they are first.   Special additional discounts for a one-off marketing campaign should be your decision.

Hidden charges: Check the small print. Do they charge you to store your stock; to put details of your stock into their computer; to return stock to you? Do they destroy returned stock? Are you happy with these charges and policies? If not talk to them about how you'd like to change it.

Rarely is a deal completely non-negotiable. If you act politely, reasonably and in an informed manner to point out your concerns it is likely that at least some will be addressed.

Licence deals:

In many ways there are overlaps with the distribution deals.

Territory: Exactly the same issues come up here as for distribution deals so have a look at that section.

Rights granted: Have a look at this section too as again some of the same issues apply. It is however much more likely that they will want a broad range of rights. They are going to act as your local label for the agreed territory and as such they want to have the most rights they can to exploit the product and make money for them and of course for you. So they will want digital rights and they will want synchronisation rights. If having thought about it you agree to include these rights on an exclusive basis you need to think whether you (or your artists if you are a label) will want creative controls over what can be done with their recordings. It is perfectly possible to agree for example that they can't grant synchronisation licences without coming back to you first for approval or that they can't remix or change a track without your approval. Be careful to keep a balance here though and not tie their hands so much that they can't properly exploit the recordings.

What Product? As with the distribution deal this could be a licence for a particular track or album or for all your existing catalogue if you are a label or an established artist. You can only grant rights where you won or control those rights and haven't already given them to someone else for that territory.

Term – how long? A licence deal is usually for a fixed period of time usually linked to release of a record. Be careful there is a commitment to release otherwise it's open-ended. That period is usually around 5 years but could be longer. Beware of deals that are for life of copyright as that is close to you selling your rights. It is rarely shorter than 5 years but is occasionally 3 years.

Options: It is likely that they will ask for an option (on which only they decide) to extent their deal with you beyond the first period e.g. for a follow up album or another year or two. This may be alright if you are confident you want a future with this licensee but consider also if you want to put in some sales targets e.g. that they get an option to sell the second album if they manage to sell 50,000 full price copies of the first album.

Advances: It is usual to expect some kind of upfront payment for the rights you are granted. This is entirely negotiable and depends on your bargaining power and your salesmanship. Don't undersell or oversell yourself and if in doubt get a written proposal, take it away and get advice on it. The advance is recoupable from your royalty earnings so you don't see any more income until you've earned it back. But you also shouldn't have to pay it back if you don't sell enough records.

Other spending commitments: Depending on your position you may want to have a commitment to a spend of a minimum or fixed amount on recording or remix costs, mastering costs, marketing or tour support. It is likely that if they agree to make these payments these will be to a large extent if not entirely recoupable from your royalty income.

Your relationship with your artists: Please bear in mind if you are a label that you may have contractual commitments to fund certain things with your artists e.g tour support and you may also have agreed to pay the artist an advance when you do a licence deal so make sure that you can cover those sums and still have some money for yourself.

Royalties: This can be quite a complex subject but I will concentrate on the headline points: There are two main types of deal – a **royalty based** on a calculation of **sales** price **or** a royalty based on a **share of** the licensee's **profits**.

In the straight royalty based on sales you need to know **how the royalty is calculated**. It is on all sales or on a percentage (in the US often 85%); what price is it based on – the retail or more often a **dealer** price. In the US there are several layers of dealer price you need to know exactly which one they mean and if in doubt ask them to work through an actual example with you. This is not stupid – it's a complex area and one you need to understand if you are to work out how much you will receive from each record sold. Then there are other deductions for sales taxes and **packaging**. There is a move in the UK to do away with packaging and reduce the royalty rate by an equivalent amount, but in other countries they still make a deduction of up to 25% or 30% of the price as a notional charge for packaging. It's an artificial means to reduce the royalty due to you so you need to know what they are doing to know what the end amount is that you will receive.

Once you know what it's based on then you can see if the percentage on offer is reasonable. A reasonable album licence royalty rate based on 100% of sales on the dealer price and with a packaging deduction of 25% is anything over 18%. There may however be good commercial reasons why you would accept less. The actual deal will vary according to your bargaining power and salesmanship and may be lower if you are taking a huge advance. The lower the advance the more you can try and increase the royalty. You can often also have increases called **escalations** based on number of sales.

There will be reductions for singles and possibly also for downloads. There will also be reductions for particular types of sales which attract a lower price e.g mid-price or budget sales. They will also try and pay half rate if they TV advertise or if they sub-licence to compilations. All these reductions are usually negotiable but the licensee will have a bottom line.

Royalties as a share of profits: with this deal instead of just recouping advances and things like recording costs, video costs and tour support, the licensee collects in all the money, deducts all costs (other than his own office overheads) and splits any net profit. Then out of your profit share if any you first recoup any personal advance you have had and don't see any more money until that has happened. The usual profit split is 50:50 but that is negotiable. Do not accept less than 50% unless there is an extremely good reason.

Accounting: this is usually twice a year and within 90 days of the end of each 6 month period so for example they calculate royalties/profit share due over the first 6 months of the year and then pay you anything you are due by 90 days after that so you'd get statement and hopefully a cheque at the end of September and end of March. Quarterly accounting is possible but less common.

Videos: they may want you to licence existing videos or to have the right to make one or more . Consider costs, who pays them, are they recoupable and what about creative controls?

Mechanical royalties: These can be a trap for the unwary particularly in licence deals for the USA and Canada. Mechanical royalties are paid by the record label to the controller of the rights in the songs on the recordings for the right to reproduce those songs on the recordings. This is at a rate that is either fixed by law or by commercial agreements. In the USA and Canada there are fixed rates but the law also allows the record labels who have to pay these royalties to pay a lesser amount by agreement. Most US and Canadian labels try and get you to agree to a lesser amount usually 75% of the full amount. This agreement is sometimes referred to as a controlled compositions clause. If you are a label and don't control the publishing you may not think you care but you do because the writer may not accept less than 100% and if it's a cover of someone's song who isn't part of the artist then you must assume they will want 100% and if they don't get it they will look to you. If you are the writer you may think you could live with 75% but if you have a deal with a publisher you can't decide that off your own bat you have to involve your publisher. Approach these clauses with caution and get advice if in any doubt as to what you are agreeing to. That could indeed be the mantra for this whole note.

Good luck

Ann Harrison

Additional reading:

"Music: the Business" by Ann Harrison, 3rd edition, published by Virgin Books and generally available at Borders or Amazon.

"The Music Business" by Donald Passman published by Penguin also has a good overview written by an American attorney.