ON THE IMPACT OF PROPOSED BILL **AB 1385** TO THE CALIFORNIA MUSIC COMMUNITY

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INTRODUCTION

It is interesting to me how regulations that are economically harmful for musicians are often couched in terms of fairness and freedom, sentiments which quickly become rallying cries but often undermine the livelihoods of the very people shouting from the rooftops. Such is the case of Assembly Bill (AB) 1385 in California, which seeks to remove the right of record labels to pursue damages if a recording artist leaves after seven years and has not delivered the number of recordings for which they have contracted (and been paid) to create as part of their signed agreement.

> THE LOGICAL CONSEQUENCE OF AB 1385 IS THAT RECORD LABELS WILL REDUCE THEIR RISK - WHICH WILL ULTIMATELY HURT CALIFORNIA RECORDING ARTISTS.

The bill's proponents claim that this would remove a restriction on recording artists that does not exist for workers in other fields under California law. They purport that it locks artists into a personal services contract for years.

However, this argument is fundamentally untrue: no one is forcing artists to remain under contract. What the California law recognizes is that musicians are unique, and that the structure of their business relationship with their label is unusual. For example, recording artists' contracts typically aren't based in increments of time, like a television season.

Record label agreements typically provide for a non-returnable advance payment to the artist. That advance of future royalties – often totaling hundreds of thousands (or, in some cases, millions) of dollars – is given to an artist at an agreement's outset. The artist might or might not be able to deliver the number of creative works agreed with the label contemplated during the agreed-upon term. If the artist doesn't deliver those albums, the record label has not only lost the money they advanced to the artist but also finds itself without the music they were promised. Existing California law provides balance to that equation.

AB 1385 seeks to add a further restriction, that a label must exercise its option for an artist's next project under the contract within six months of delivery or release (whichever is sooner). Given the nature of modern music distribution and marketing, artists often want the label to take more time to consider whether to exercise an option. Moving the option exercise window up to six months from delivery, and making it statutory and nonwaivable, can be counterproductive for both the artist and the label. While we hear about surprise music release "drops" from major artists, even in those instances it can take months if not years to prepare a project for commercial release and promotion to the point of success, especially for a new or developing artist.

The logical consequence of AB 1385 is that record labels will reduce their risk - which will ultimately hurt California recording artists. Labels will sign fewer artists, reduce the amount of money they advance to artists, and be faster to drop an artist if the label loses confidence that the artist's music can become commercially successful.

This might benefit a tiny number of the wealthiest mega-star artists. Their powerful managers and attorneys can "shop" for new deals without damaging their artists' careers, at least in the short term. They can sell their next project before the last one has been released.

> THE PROPOSED LEGISLATION WILL COMPEL LABELS TO LESSEN INVESTMENT IN NEW AND DEVELOPING ARTISTS AND DECREASE INFORMATION REQUIRED FOR EXERCISING OPTIONS ON FUTURE RELEASES.

But for the vast majority of working class and emerging artists with label deals, or those in more niche genres, the results of this contraction in record label risk tolerance could be devastating. The proposed legislation will compel labels to lessen investment in new and developing artists and decrease information required for exercising options on future releases.

THE FUNDAMENTALS

Record labels have always done four fundamental things: discover promising artists; connect artists with talented collaborators to make the music as good as it can be; connect music with the potential for good commercial outcomes; and as those positive outcomes happen, share the economics. Over the last two decades, digital technology has transformed the way music is created, released, discovered, and consumed and has remade how record labels are organized to create value for artists and fans. I wrote about how the modern record label has responded to this challenge in my 2019 paper, "Same Heart New Beat,"[i] which I am in the process of updating this year.

Proponents of the bill claim there is less for labels to do in an era when distribution to digital music services has become commoditized. If this were true, merely making a track or album available on digital music services would be sufficient to establish and sustain careers for music creators. But there is a big difference between theoretical discoverability on a streaming service and having a realistic chance at becoming one of the world's most popular and enduring artists, and that is the space where labels create enormous value for artists and fans. Although it is possible today for artists to create and self-distribute their music and gain a following, talented self-distributed do-it-yourself (DIY) artists seldom reach the levels to become a household name.

Consistent with the explosion in the number of new channels for artist discovery including TikTok, Spotify, Apple Music, Amazon and hundreds of others, labels create highly customized social, visual, and interactive, and unique podcast content and gaming experiences built around their artists' music for each unique channel. Labels strategize with editorial and curatorial staff at the services to maximize visibility of their music on key playlists and programs for developing and career artists, develop new shows and license music for use in film, television, videogames, and new advanced technology platforms while simultaneously servicing the market for physical CD's and vinyl records and still compete for scarce radio airplay slots.

Streaming now accounts for 83% of annual recorded music revenue, according to the RIAA's data for 2020. Although a few services dominate music consumption in many territories, labels maintain commercial agreements with hundreds of digital service providers. One label recently shared with me that they have licensed over 450 services worldwide.

Labels provide essential services to artists in all genres and at all levels of career development, not just those signed directly. For example, in addition to Sony's venerable owned and operated labels Columbia, Epic and RCA, the company's independent distribution platform The Orchard services over 25,000 label clients representing 347,000 artists distributing over 12 million tracks.

> "LABELS CREATE ENORMOUS VALUE FOR ARTISTS AND FANS."

The amount of available data on music discovery and consumption has exploded as music has transitioned from an ownership to an access business. One major label receives data on roughly three *billion* micro-transactions a day that needs to be aggregated and curated in a way that gives artists simple and useful visibility across hundreds of digital service providers globally, that all need to be processed and clearly contextualized.

It has become essential for the industry to be able to attract and develop talented executives capable of extracting actionable insights from an ocean of chaotic data about music consumption to identify potential and help build careers. However, more data about music discovery doesn't mitigate risk in the signing and artist development process. More data about unsigned artists proves there may be interest in an artist's music. But it is magical thinking to believe that data de-risks signings.

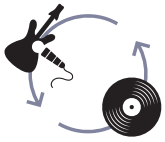
And there is so much music. Two years ago, labels and digital distributors uploaded 40,000 tracks to music services each day. Services now upload 60,000 tracks per day – a third more, so it is harder than ever to break through. This requires investment, expertise, "boots on the ground."[ii] Music creation itself is now being further democratized in the way digital photography and the use of digital filters became easily accessible and built into smartphones, and shareable on social networks. In the near future, 30% annual growth in new sound recordings will likely look puny. Labels pick the best, make it as good as it can be and help it find an audience.

THE HEART OF THE PROCESS

Labels meet artists wherever they are with highly specialized staff and scalable infrastructure geared to the way fans now discover and consume music.

1 WHERE IT BEGINS

The relationship between artists and labels is constantly evolving



2 NOT WHAT, BUT HOW

The core functions labels provide have not changed

DISCOVER ARTISTS / AMPLIFY THEIR VISION / DEVELOP TALENT / MAXIMIZE COMMERCIAL POTENTIAL / NURTURE

3 GROWING TOGETHER

Labels invest heavily in

INFRASTRUCTURE + STAFF + TECHNOLOGY

4 ARTIST SERVICES — MUCH MORE THAN SALES:

DEVELOP NEW OPPORTUNITIES WITHIN THE STREAMING ECOSYSTEM / BUSINESS OF BUILDING AND SCALING ARTIST BRANDS / MORE THAN MANUFACTURING AND SELLING RECORDS

* Adapted from "Same Heart. New Beat. How Record Labels Amplify Talent in the Modern Music Markeplace", by Larry S. Miller. http://musonomics.org/modernlabelreport.

My current research indicates the number of signings has increased; the pace has accelerated from signing to release; and A&R and marketing spend have dramatically increased. One major label finance chief told me this year that gross spend per signing has *doubled* over the last five years. But if record labels need to bake in additional risk to account for future losses due to additional exposure in the late innings of an artist-label relationship, all this can change. If long term partnership is truncated after payment of advances but before the minimum delivery commitment occurs, the fundamental economics will have to accommodate a new reality. This will hurt second and third-quartile artists the most. To deny this is to deny gravity.

STREAMING. AND OTHER PLATFORMS.

After fifteen years of decline earlier this century, streaming is indeed the rising tide that lifts all boats. Let's examine what's in those waters. The RIAA has an interactive graph of historical revenue on its website. The year-end revenue report for 2020 shows overall US revenue is $12.2 billion, still far below the historic peak of $22.7 billion (adjusted for inflation) in 1999. Proponents of the amendments to the current law, passed at the industry's peak 20 years ago, are pushing a "happy days are here again" narrative with streaming "saving" the labels – but let's look more closely at these numbers.

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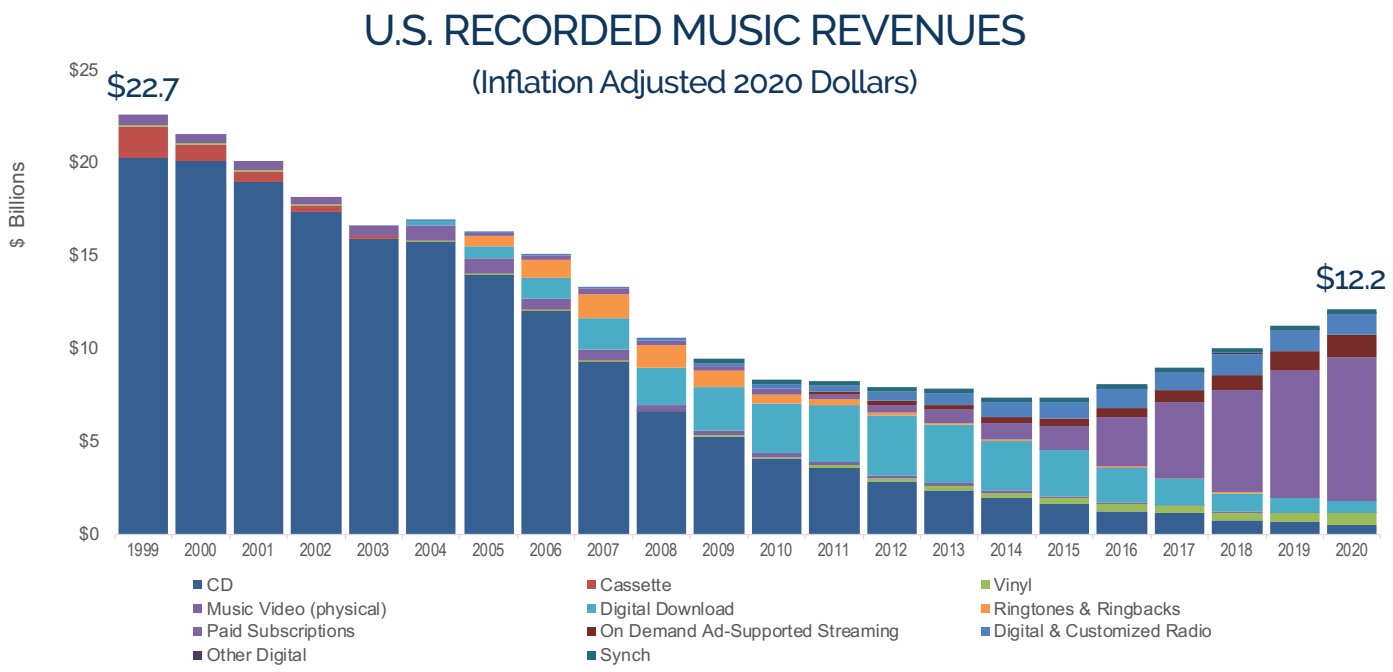
An important thing to note in the graph is that in the early 2000s, revenues originated from five sources, with the vast majority from the sale of CDs. CD revenue 20 years ago was nearly $20 billion annually (again, adjusted for inflation), alone exceeding total revenue in 2020.

However, today there are eleven broad categories of revenue tracked by RIAA industry data. While on-demand streaming



has increased, non-streaming revenue sources are larger today than anything besides the dominant format in the CD era. The implication is that music companies continue to invest in talent, but they also invest in a myriad of new distribution technologies, new platforms, and new marketing strategies.

These are also constantly evolving from the pre-digital era. A multiplicity of assets must be created, customized to each platform and customer type – and constantly updated to reflect real-time market feedback. Streaming may have reversed the decline in label revenue that began at the turn of the century as consumers abandoned physical album purchases, but their costs of doing business have increased with each new format and social media platform. While physical product was expensive, labels needed to maintain one master copy to manufacture every CD. Today, labels need a different variation of the master for every streaming format and bitrate. In the course of my current research, I learned that labels now maintain over 3000 conversion profiles for each release, many receiving multiple conversions across more than 75 audio, video, and graphics source types.

What the RIAA graph does not show is how quickly each release peaked in sales following release. In the pre-digital era, labels needed at least three to six months to press CDs and set up marketing campaigns, because first week sales were everything. Sales departments obtained advance orders from stores around the country; first day sales were the leading indicator of whether there was actual consumer demand, and by the following week, record companies had reorders or had started to worry about returns. Labels knew within the first few weeks whether an album had hit potential.

This was reflected in the way the Billboard charts were calculated, the lingua franca of sales success in the industry. Up until December 2009, the Billboard Top 200 Albums chart did not include releases that were over eighteen months old, that had dropped below position 100, and had no current single at radio. The lifetime value of a project was determined two to four weeks from release, and even for a hit, actualized in a year and a half.

Today, digital distribution speeds music to a market geared to the release of singles and in many cases, multiple versions of the same single.[iii] Ironically, it was easier 20 years ago to predict a hit 6 months from delivery than is the case today.

OPTIONS AND TIMING

This was dramatically illustrated in a 2017 report from Will Page, then Director of Economics for Spotify.[iv] Page and his team analyzed "all tracks released during April 2015 – crunching the numbers on almost three-quarters of a million songs released in that single month. Here's what we learned: 40% of those tracks had more streams between April 2016 through March 2017 than they had from April 2015 through March 2016. Put bluntly, year two earned more than year one."

To underscore this point, Page presented a case study with the major label band Imagine Dragons. He drilled into their September 2012 debut album *Night Visions*, which earned them the "breakthrough band of 2013" label from Billboard. Page wrote, "We examined all digital album sales and all streams during months 1 to 18 following *Night Visions'* release – and then did the same for months 19 to 36 … sales taper off by 33% in the second period compared to the first, whereas streams grew by a massive 177% from the first period to the second. This is what streaming momentum looks like."

> "SIX MONTHS FROM DELIVERY HOLDS LABELS TO AN UNREALISTIC TIMEFRAME FOR THE EXERCISE OF FUTURE OPTIONS."

Page continued, "Spotify has seen Imagine Dragons' catalogue maintain momentum throughout their three album releases … and doubled it. Measuring momentum over time isn't easy, not least because streaming itself is growing in both subscribers and volume." As of October [2017], Imagine Dragons are now the 14th most successful artist in the history of Spotify, and have just passed 5 billion streams. Just as well, then, that the label didn't take their 'foot off the gas' 18 months after their debut release."

Imagine that within the first six months, Interscope had to decide if Imagine Dragons was worth the continued investment? If they said yes, Imagine Dragons might not have been in a strong position to renegotiate the terms of their deal. If they had said no, Interscope would have likely stopped making any investment in this band and Imagine Dragons may not have been in a position to attract interest from other labels. How would this have helped their career? Six months from delivery holds labels to an unrealistic timeframe for the exercise of future options.

As a practical matter, successful acts renegotiate with their labels. Unsuccessful acts are released from their contracts when their options are not picked up. No label wants a successful but unhappy artist. But some artists may be wound up by their managers and lawyers that life will be better somewhere else where they can hit the reset button and wipe the slate clean, especially when faced with unrecouped advances and other costs or undelivered recordings. Only then, the label will be left holding the bag.

It's not that the California proposal might not benefit anyone. If the legislation is enacted, a tiny percentage of very successful superstar artists will be able to exploit the new law for their benefit. But record labels are rational businesses, and the cost of benefiting the few will come at the expense of less investment in working class, emerging, and niche genre California artists and the many thousands of creative and business people who support them.

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[i] Miller, Larry. "*Same Heart New Beat: How Record Labels Amplify Talent in the Modern Music Marketplace*," 2019. Musonomics http://musonomics.org/modernlabelreport

[ii] *Ibid*, page 8.

[iii] Caramanica, Jon. "Who Needs an Album? Just Keep Remaking the Song." 2021. *New York Times*. https://www.nytimes.com/2021/04/28/arts/music/songs-remixes-lil-nas-x-spotemgottem.html

[iv] Page, Will et al. "Does the music industry's definition of 'catalogue' need an upgrade?" 2017. *Music Business Worldwide*. https://www.musicbusinessworldwide.com/music-industrys-definition-catalogue-need-upgrade/