



# NEWSLETTER

An Entertainment Industry Organization

## GEMA Answers German Mechanical Royalty Reduction Threat

*David Hirshland*

*50<sup>th</sup> Anniversary*

### The President's Corner

*Teri Nelson Carpenter*

I would like to begin by thanking Michael Morris, CCC Vice President, for the wonderful job he did in taking the helm for the February dinner meeting, "An Evening with John Lofrumento, CEO ASCAP" while I was out ill. Thank you, Michael.

February's meeting was interesting by all accounts as John LoFrumento discussed ASCAP's global strategies which also include a new co-venture MediaGuide, a revolutionary fingerprinting technology.

Tonight's meeting is Part 1 of a 2 Part series on Independent Publishing. We are delighted to have several foreign independent publishers at our meeting tonight including a US industry music publishing veteran who specializes in Foreign Publishing. We look forward to sharing the latest in music publishing from a global perspective.

Don't forget we are fast approaching our 50th Anniversary May 10, 2004. More details to follow.

One of the more dramatic developments in the ongoing process of determining what publishers and authors are paid for their compositions with regard to record sales occurred at the beginning of the year in Germany. Most publishers were given the news during MIDEM that IFPI, the German equivalent of the RIAA, unilaterally decided to reduce the mechanical rate payable by its members some forty percent - from 9.009% of Published Price for Dealers ("PPD") to 5.6% of PPD.

This aggressive attempt to restructure the internationally accepted royalty rate has of course sent shock waves through the publishing community. Although IFPI has agreed to escrow the difference until the German courts sort out the dispute, a resolution could be years in the future. This action appears to be the first major blow in the coming battle between labels and publishers over a future compensation structure associated with the new digital delivery age. As a reminder, the statutory mechanical rate in the United States is set through 2008 so its renegotiation is not that far away.

Printed below in its entirety is the response of Dr. Reinhold Kreile, Chief Executive Officer and President of GEMA to the IFPI action. In it are some dire warnings to the international publishing community.

*Open answers from GEMA to an open letter by IFPI regarding the level of audio-carrier licensing*

1. The record industry's drastic sales losses of 40 % - as lamented by the German General Manager of IFPI, Gerd Gebhardt - are also lamented by the composers, lyricists and their publishers. As is the way with copyright, they too receive a share of these sales. The 40% drop in the sales of the record industry leads to an equivalent drop in the income of the musical creators.

If the industry now intends to recover its losses at the expense of the authors by paying them only 5.6% of the Published Price for Dealers (PPD) from the remaining turnover rather than the remuneration of 9.009% as has been paid for decades, then it is seriously misjudging the value of intellectual property. By acting in this way it is smothering all musical creativity. That is why GEMA has opposed a reduction to the percentage rate in all national and international negotiations conducted over the past few years.

The German copyright legislators - like those of every other civilised country - require that the remuneration for the creator of the work, his reward, should be "equitable". Such an equitable rate has always been considered to be about 10%. The difficult situation in the

music industry is therefore already adequately taken into account with a rate of 9.009%. But when the record industry, and in particular the 5 so-called Majors (Universal, Warner, Sony, EMI and BMG), now wish to pay only a little more than half of the current equitable royalties, then this really is a case of rate cutting or "sweating". This crass expression from the early days of capitalism accurately describes the present situation. The 5 Majors, the powerful financial oligopoly of audio-carrier producers, want to reorganise their affairs at the expense of the authors. The IFPI audio-carrier producers do not intend to make the CDs cheaper - and are not even claiming to want this. All they want is to reduce their costs and generate more revenue for themselves. They want to force down the authors' remuneration and increase their own profit margin.

2. This strategy will not prove successful. The German courts will not accept such expropriation.

Only recently, for instance, the German Court of Justice and Munich Higher Regional Court rejected an attempt by the major record producers to reduce the royalty rate from 9.009% by making a deduction of 12% for audio carriers advertised in the media. In this case, the courts agreed with GEMA and made it quite clear that it was up to the producers to produce and sell and up to the musical creator to create the work in return for a reasonable share of the sales. These rulings hurt the Majors - which explains why they overreacted with these new attacks - but they are legally valid and right.

3. The audio-carrier majors, the leading organisations of the German and international IFPI, will not be successful with their well-contrived underhand plan to pay the authors (via GEMA) only half of the current remuneration, while the other half is deposited with the court until such time as the court reaches a final decision - which could take years and years. In financial terms, this escrow agreement is meant to immediately force the authors and their publishers to their knees.

The implications of such horribly well thought out interpretation practices are indeed grave. While this

deposit does not actually help the apparently destitute audio-carrier industry itself, because it first has to pay the full PPD rate, the authors and their publishers would then be 40% short; this 40% would be sitting in the escrow accounts. It could come to more than 40 million euro a year that GEMA cannot distribute to its rightholders.

For those publishers belonging to the same group as the audio-carrier producers - i.e. for the groups Universal, EMI, Warner, Sony and BMG - an in-house settlement might well be found at first.

But for the independent publishers, as well as for all the composers, this escrow arrangement is a threat to their very existence. Are the independent publishers, as is being rumoured in IFPI circles, to be reduced to such financial straits that the only option left open to them is to be "rescued" by the IFPI group publishers, or in other words taken over?

4. The current royalty level of 9.009% of the PPD, which the General Manager of IFPI for no comprehensible reason does not think is realistic any more, is precisely that the rate is realistic. It has been agreed by both sides as a percentage, it applies in good times and bad. In the course of the past 20 years, the authors have shown understanding for the record industry over and over again. With the mutual agreement of the record industry, they reduced the original rate of 11% to slightly above 9.009% in several stages. But enough is enough. More reductions would not be consistent with the value of musical creativity. The remuneration of the author must stay fair. None of the IFPI negotiators would agree to a 40% cut to their salaries. With what internal justification it is now reasonable to expect this of the authors? No, the limit of reasonableness for the remuneration reduction sought by IFPI has been reached.

5. And the attempt by the General Manager of IFPI to drive a wedge between German and foreign, in particular Anglo-American, authors is also doomed to failure. How is the existence of national German repertoire to be secured in the future with

a lower remuneration? The Anglo-American authors and their right-holders - where they are not represented by IFPI group organisations - are resisting the sell-out of their rights just as vehemently.

6. All the same, IFPI - as it openly underscores - intends not only to plunder the royalties for CD production, but also the remunerations for new distribution systems of the future. As the IFPI General Manager makes only too clear, the current royalty dispute is in fact all about discrimination against the authors in the digital future. Then it will not be long before the "equitable" remuneration for the new distribution channels is lowered. But the principle enshrined in all the legal systems of Europe also applies here, namely that the remuneration for creative work is equitable if it amounts to about 10% of the price paid by the end user for this work.

7. GEMA does have the "good will" called for by IFPI to reach an agreement with IFPI about an equitable remuneration on this basis, as prescribed by the law. But the authors will not go to Canossa - and this historical image will undoubtedly be well understood.

*Prof. Dr. Reinhold Kreile, Chief Executive Officer and President of GEMA*

## UPCOMING MEETINGS

### Apr 20:

Part 2 of our Publisher Series  
"U.S. Independent Publishers"

### May 10

50th Anniversary Celebration  
A Very Special Evening!

## California Copyright Conference

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