

BY BEVERLY BARTSCH

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## THE BUSINESS OF MAKING MUSIC

## Where the Money Goes

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**“When the money’s gone, will you be my friend?”** All of us could sing that Cher song at some point in our lives, but for an artist, the ring of that tune is especially loud. Where *does* all that money go?

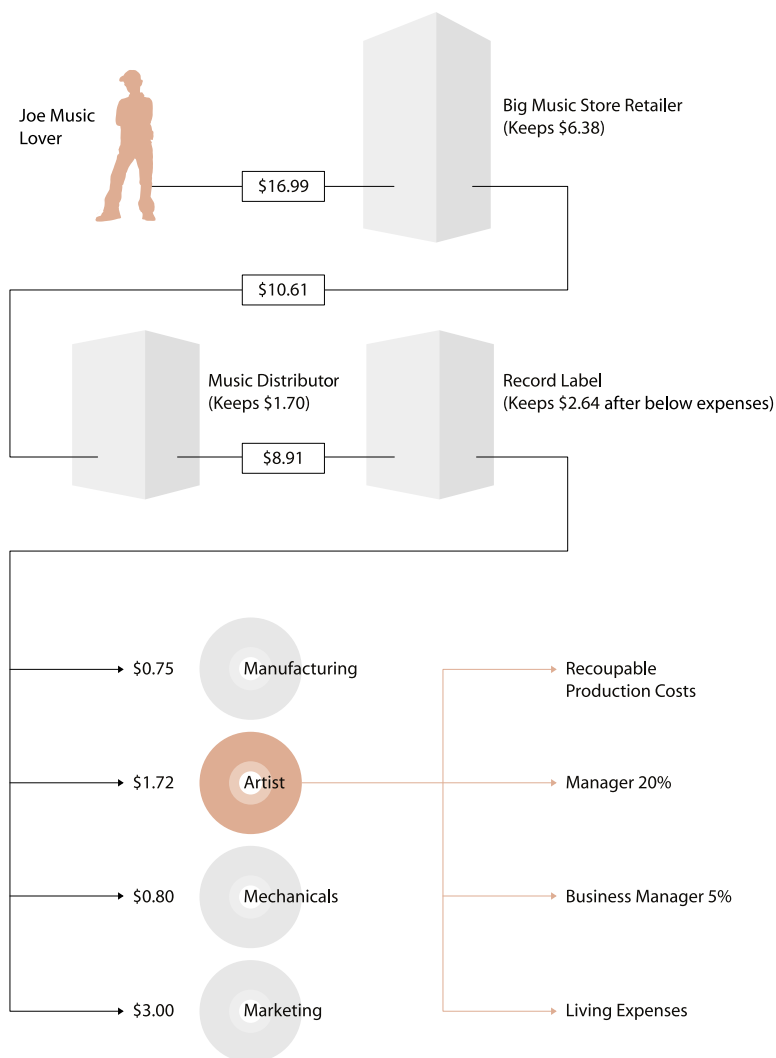
The record-buying public understands on a conceptual level that all \$16.99 of the purchase price plunked down for a CD doesn’t go directly to the artist. But few probably understand just how many forks are in that money pie waiting to get their chunk of change. It’s probable the artist doesn’t even know the flow of cash. This information comes to me from a former record-label executive who, when he first joined the music business wanted to understand for himself just how the money was spent.

## LET’S FOLLOW THAT MONEY.

Just one note before we start: All terms of any deal are always negotiable. The figures listed in this example are typical but just an example.

Joe Music-lover has just purchased a brand-new CD at a major music retailer: Big Music Store.

1. Joe pays Big Music Store \$16.99 plus tax in most states. (We all know the government gets their share, so I won’t go into that.)
2. Big Music Store Retailer then pays the distributor based on the “card price” for that CD. The card price is the cost of a CD for the retailer. This price at \$10.61 is per CD before any discounts. Often, major labels give the retailer a 5 percent discount off the card price. The retailer pays the card price to the distributor regardless of what the retail price in the store is. This is why a company like Big Music Store can sell a brand-new release for \$9.99. They will still pay the card price to the distributor, so they are losing money right away on that sale. However, they are using that hot new CD as a loss leader to get the buyers into the store, and then they will sell the buyer a nice



## ON THE ARTIST'S SIDE

Artist Royalty	\$ 1.72 (per unit)
Unit Sales 200,000 (200,000 x \$1.72)	\$ 344,000.00
Less: Recoupable Costs	\$ 250,000.00
Net Royalties to Artist from Label	\$ 94,000.00
Less: Manager Commission (\$194,000 commissionable income x 20 percent)	\$ 38,800.00
Less: Business Manager Commission (\$194,000 commissionable income x 5 percent)	\$ 9,700.00
<b>Artist's Gross Profit</b>	<b>\$ 45,500.00</b>

new stereo on which to play that CD. The ability of the major retailers to sell the CDs at losses is something a boutique or mom-and-pop music retailer would not be able to do. The retailer is making \$6.38 per CD if the CD is sold at full retail. Out of this money, the retailer must pay their entire overhead, the salaries, the marketing for their store, etc.

3. The distributor collects the card price from each retailer (i.e. Big Music Store) on each CD sold and accounts back to the record label. The distributor, of course, must make money on the services they provide to the record label. This distributor fee ranges from 14-18 percent. For the sake of our example, let's say the distributor fee is 16 percent. The distributor withholds their fee (\$1.70 per CD=\$10.61 x 16 percent) from the card price before remitting those funds to the record label.

4. The record label's net sale on the CD Joe bought is now \$8.91. The record label has an assortment of costs and expenses that must come out of this money:

a. First there is the cost of manufacturing. This is not the cost of producing the tracks on the CD, but the cost of putting the final tracks on the actual materials, the disc itself. This is actually a pretty small factor on a per unit basis, approximately 75 cents per unit. Note: the costs of production (the musicians, the studio, the gear rental, the background vocalists, the producer, the arrangers, the travel costs associated with any personnel for recording purposes, the artwork and the mastering) are all allocated out of a separate fund, and the artist has to recoup these costs before earning any royalties. Production is not a cost to the record company unless the project doesn't recoup.

b. The next expense is the one all artists are waiting for—their royalty. Again, all contracts are negotiable, and artist royalties could range from 10 percent to 25 percent. This is the stated contract rate, based on the suggested retail price that the artist is earning off each CD sold. For our example, let's say the artist is getting a 15 percent royalty rate. Well, 15 percent of a \$16.99 CD retail selling price would mean that the artist will get \$2.55. However, the record label can deduct packaging allowance, typically 20-25 percent, and a free goods allowance, typically 10 percent. So, based on a full retail sale, the artist would actually get \$1.72 if the packaging deduction was at

25 percent. Hold that number in your head; we're going to come back to it.

c. The next expense is mechanicals. This is the required statutory rate that the record label must pay on all songs. The rate is currently at \$0.08 per track (or side) on the record. If an album has 10 sides, the label would be required to pay the publisher of the songs—assuming one publisher had all 10 songs—a total of \$0.80 per album. There are rules that cover songs over five minutes in length and more than 10 songs on an album. This is a point that would have been negotiated at the time of the contract. For our example, let's assume only 10 songs and none of them over 5 minutes long. The mechanical money now has a trail it follows, as well. The ASCAP website has more information on mechanicals (<http://www.ascap.com/musicbiz/money-mechanicals.html>) and control compositions (<http://www.ascap.com/musicbiz/money-clauses.html>), as do BMI's and SESAC's sites.

d. The record label now has \$5.64 in gross profit on the CD Joe purchased. Compared to the artist's \$1.72, you might be thinking, good grief, the label is making all the money. Maybe, but there are some more expenses to be accounted for. Marketing is a crucial and substantial expense for the record label. Artists want to know that the label is out there getting the word out on their project. It takes promotional personnel, print, radio and TV ad buys, promotional events, promotional radio tours and showcases, not to mention radio singles sent to the stations, promotional media kits—both print and electronic—and postage and telephone calls to get the word out. An established artist might have a marketing budget of \$1 per sales unit, while a new or slow-selling act could have a \$5 per unit marketing budget. At this point, depending on how much the label has spent on marketing, there may not be any profit left for the label. Let's say the label spent \$3 per unit on marketing. That brings the gross profit down to \$2.64.

e. Out of the remaining funds, the label has its basic overhead expenses, the largest two of which are salaries for the entire label staff and office rent. Since this can vary so much depending on size of the label and where in the country the office is located, I won't attempt to quantify this number.

**DID YOU FOLLOW THAT MONEY TRAIL?** That's just on the label side. Let's think of it now from the artist's perspective. Remember our artist in the example above is paid \$1.72 per unit. For the sake of this example, let's assume that the recording budget is \$200,000 and that the video for the first single cost \$50,000 to produce. That \$250,000 is recoupable from the artist to the record company before any royalties would be paid. That means the artist would have to sell 145,349 CDs (at full retail price, by the way) in order to recoup that budget. So in order to follow the money trail on the artist, let's say he sold 200,000 units (way to go!), for a total of \$344,000 in gross earnings.

1. Before the artist gets paid the first dollar, the label must have recouped from the artist all the costs of production as well as any advance. Our artist now has \$94,000 in gross profits (\$344,000 less \$250,000).
2. Next, the artist will have to pay the manager. Managers typically take 15-20 percent of the artist's earnings. Now, they may not commission all of the production dollars, but they could. It all depends on how the contract was written. Let's say that only \$100,000 of the total production and video budget is commissionable.

\$344,000 less the non-commissionable production funds of \$150,000 is \$194,000—the amount of the commissionable income. If, for example, the manager's contract were 20 percent, the commission would be \$38,800, which leaves our artist with \$55,200 (\$94,000 less \$38,800).

3. The other key team member who could be paid by percentage is the business manager. The business manager fee is typically 5 percent of commissionable income as determined by the manager's commissionable amount. So, 5 percent of \$194,000 is \$9,700, leaving the artist with \$45,500.

If the artist in our example releases one project a year and sells 200,000 units, after his two major expenses he is making the equivalent of \$45,500 in annual salary, which would be paid in quarterly installments based on actual sales in the prior quarter. Out of this money, the artist has to pay his lawyer as well as monthly personal living expenses including rent or mortgage, car payment, medical insurance, kids' tuition, taxes, retirement, and probably a lot of hair salon styling and coloring fees. Hopefully this has shed a little light on the financial trail of your CD sales. ■