



GAO

Accountability • Integrity • Reliability

United States Government Accountability Office  
Washington, DC 20548

February 26, 2010

The Honorable John Conyers, Jr.  
Chairman  
The Honorable Lamar Smith  
Ranking Member  
Committee on the Judiciary  
House of Representatives

The Honorable Jason Chaffetz  
The Honorable Charles Gonzalez  
The Honorable Sheila Jackson-Lee  
The Honorable Dan Lungren  
House of Representatives

Subject: *Preliminary Observations on the Potential Effects of the Proposed Performance Rights Act on the Recording and Broadcast Radio Industries*

The recording and broadcast radio industries combined generated over \$25 billion for the U.S. economy in 2008. These industries provide jobs for a range of skilled workers, including songwriters, producers, engineers and technicians, and radio announcers, among others. At the same time, recording studios and radio stations allow musicians, vocalists, and performers to share their talents with listeners across the nation. Through their work, the recording and broadcast radio industries contribute to the everyday American experience by creating and delivering music to people in their homes, cars, and workplaces. Beyond providing a popular form of entertainment, the recording and broadcast radio industries have helped music become a prominent feature of American culture.

Music, like other forms of creative art, is protected by copyright law. Congress is considering legislation that would expand copyright protection for sound recordings. In particular, the proposed Performance Rights Act<sup>1</sup> would eliminate an exemption that currently allows analog, nonsubscription AM and FM radio (broadcast radio stations) to broadcast a sound recording without acquiring permission from and paying a royalty to the copyright holder, performers, and musicians. The act would amend the statutory license for nonsubscription transmission services to include terrestrial broadcast stations. Under the amendments to the statutory license, a radio station would pay a royalty based on its revenue and its status as a commercial or noncommercial station. (See table 1.) Furthermore, the proposed act exempts some uses of music, such as music in broadcasts of religious services and the incidental use of music by nonmusic stations.

---

<sup>1</sup>H.R. 848, 111<sup>th</sup> Cong. (2009). The Senate has a companion bill—S. 379, 111<sup>th</sup> Cong. (2009). While the House and Senate bills differ in detail, both bills include a statutory royalty with a tiered structure where all broadcast radio stations with revenue below \$1.25 million would pay a flat annual fee; the proposed flat fee in each bill is different.

**GAO revised this correspondence on June 7, 2010, to reflect changes in attribution and the addition of an e-supplement. To view the e-supplement online, click on <http://www.gao.gov/products/GAO-10-707SP>.**

**Table 1: Statutory License Royalty in the Proposed Performance Rights Act (H.R. 848)**

Type of broadcast radio station	Radio station annual revenue	Proposed royalty
Commercial	\$1.25 million and above	Royalty rate to be negotiated between broadcast radio stations and copyright holders or set by the copyright royalty judges <sup>a</sup>
	\$500,000 to \$1,249,999	\$5,000 per year
	\$100,000 to \$499,999	\$2,500 per year
	Less than \$100,000	\$500 per year
Noncommercial	\$100,000 and above	\$1,000 per year
	Less than \$100,000	\$500 per year

Source: GAO analysis of H.R.848.

<sup>a</sup>The copyright royalty judges are housed in the Copyright Royalty Board, an establishment created within the Library of Congress for this purpose. The judges are responsible for determining and adjusting the rates and terms of statutory copyright licenses and determining the distribution of royalties from the statutory license pools.

Under the House bill (the proposed act), revenues from the proposed statutory royalty would be divided among recipients as follows: 50 percent would be paid to the copyright holder,<sup>2</sup> 45 percent would be paid to the featured performer or musician, 2.5 percent would be paid to background musicians, and 2.5 percent would be paid to background performers and vocalists.<sup>3</sup> A designated third party would collect and distribute royalties directly to the featured performer or musician.<sup>4</sup> Finally, existing royalties paid to publishers, songwriters, and composers are to be unaffected by the proposed royalty.

In response to your request that we determine the potential effects of the proposed Performance Rights Act, we reviewed (1) the current economic challenges facing the recording and broadcast radio industries, (2) the benefits both industries receive from their current relationship, (3) the potential effects of the proposed act on the broadcast radio industry, and (4) the potential effects of the proposed act on the recording industry. This letter provides preliminary findings based on ongoing work. As discussed with staff from the House Committee on the Judiciary, we intend to issue a final report that will provide additional information on the value of the current relationship between the broadcast radio and recording industries through analysis of revenue data, as well as additional information on the potential revenues generated from stations that would not make a flat annual royalty payment.

To meet the objectives of this report, we reviewed relevant reports and analyses about the broadcast radio and recording industries and interviewed stakeholders from both industries,

<sup>2</sup>The sound recording copyright holder is often the record company, but may also be the primary performer.

<sup>3</sup>Statutory royalties for background musicians would be paid to the American Federation of Musicians and distributed to its members according to their performance on sound recordings. Statutory royalties for background vocalists and performers would be paid to the American Federation of Television and Radio Artists.

<sup>4</sup>While the proposed statutory license requires direct payment to musicians and performers, agreements between record companies and artists could take into consideration this additional source of revenue. Record companies and others in the recording industry have signed a Memorandum of Understanding indicating that record companies will not attempt to recover any performance royalties from the musicians or performers.

as well as officials from government agencies. We analyzed data on broadcast radio stations' revenues from 2008 and estimated the annual revenues of all commercial broadcast radio stations. We classified commercial broadcast radio stations as either music or nonmusic based on the station's primary format.<sup>5</sup> Based on commercial music stations' revenues, we calculated the number of commercial stations that would be required to pay a royalty at each of the royalty levels and determined the potential transfer of revenues from the broadcast radio industry to the recording industry for the proposed royalty payment. We assessed the reliability of data and determined that the database was sufficiently reliable for the purposes of our report. From the recording industry, we met with the four largest record companies, as well as independent record companies and trade associations that represent the industry, such as the Recording Industry Association of America. We also interviewed performing rights organizations that distribute existing royalties. We interviewed recording industry experts and individuals that work in the industry such as managers, accountants, lawyers, and unions that represent musicians and performers, as well as musicians and performers themselves. From the broadcast radio industry, we met with station owners and operators, broadcast industry experts, and trade associations that represent the industry, such as the National Association of Broadcasters. Furthermore, we interviewed officials from the Federal Communications Commission's (FCC) Media Bureau to understand FCC's involvement in broadcast radio, and the Library of Congress' Copyright Office to understand its role relevant to U.S. copyright law.

We conducted this performance audit from June 2009 through February 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. A more detailed description of our scope and methodology is contained in enclosure I of this report.

## **Results in Brief**

Based on our review of the recording and broadcast radio industries and the proposed Performance Rights Act, we found the following:

- According to industry stakeholders, both the recording and the broadcast radio industries face economic challenges. Digital technology and piracy have decreased the sale of records, the recording industry's main source of revenue. Economic conditions and the fragmentation of listeners among newer media platforms, such as the Internet and mobile devices, have reduced advertising sales, broadcast radio's primary revenue source.
- Both the recording and broadcast radio industries benefit from their current relationship, according to industry stakeholders. The recording industry receives broadcast radio airplay, which promotes sales for sound recordings and concert tickets. For the radio industry, sound recordings attract listeners to radio stations that sell advertisements.
- The proposed act would result in additional costs for broadcast radio stations. Costs from performance royalties would vary based on whether the station broadcasts music and its gross annual revenue. Stations may also face administrative costs from record-keeping and playlist reporting requirements as well. According to broadcast industry stakeholders, some radio stations that are unable to adjust to these new costs may reduce staffing levels; change from music to nonmusic programming, such as news, talk, or sports; or discontinue operations.

---

<sup>5</sup>By relying on the primary format, we did not classify radio stations with a music-oriented secondary format as a music station.

- The proposed act would result in additional revenue for record companies, musicians, and performers. Musicians and performers whose songs are broadcast on the radio would receive an additional income stream. According to recording industry stakeholders, record companies could use the additional revenue to invest more heavily in the creative process of music.

We provided a draft of this report to FCC and the Library of Congress. In its letter, FCC emphasized the financial difficulties in the broadcast radio industry. FCC and the Library of Congress also provided technical comments we incorporated as appropriate.

## Background

A copyright is an intellectual property interest in an original work of authorship fixed in any tangible medium of expression, including books, movies, photographs, and music, from which the work can be perceived, reproduced, or otherwise communicated either directly or with the aid of a machine or device. The Copyright and Patents clause of the U.S. Constitution authorizes Congress to “promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive right to their respective writings and discoveries.” In the music industry, copyrights confer to their owners certain exclusive rights, such as the right to authorize or control the reproduction, distribution, and public performance of a piece of music. The reproduction and distribution of music includes the sale of copies of music in a variety of formats, such as compact discs (CD), vinyl records, and digital downloads. The public performance of music may include broadcast radio transmissions or digital transmissions, such as use on AM or FM radio or satellite radio.

Copyright law applies to recorded music in two ways: the musical work and the sound recording of that work. The musical work refers to the notes and lyrics of a song, and the copyright holder is often the publisher, songwriter, or composer. The performance of the lyrics and melody in a fixed recording, such as the recording on a CD or vinyl record, are protected as the sound recording. Record companies are often the owners of the copyright to the sound recording. Typically, different individuals or entities hold the copyrights for the musical work and sound recording of a piece of music, although one individual or entity can hold both copyrights. For example, the song, “I Will Always Love You,” was part of the soundtrack for the movie, *The Bodyguard*, in 1992. The copyright holder of the musical work is the songwriter, Dolly Parton, who owns both the words and music. However, the copyright holder of the sound recording, as performed by Whitney Houston, is the record company, Sony Music, to whom the soundtrack is registered.

Copyright holders may use a license to grant third parties legal permission to use musical works and sound recordings. A license provides legal permission for the use of copyrighted material by a group or an individual other than the copyright holder. Permission for the use of the material typically requires the payment of a royalty and compliance with other conditions of the license. As shown in table 2, third parties, such as AM and FM broadcast radio, satellite radio, and Internet radio, must obtain a license for the public performance of a copyrighted musical work. However, under current law, copyright protection does not apply to the performance of sound recordings played over broadcast radio and therefore a license is not required.<sup>6</sup>

---

<sup>6</sup>The Digital Performance in Sound Recording Act (1995) created for the first time an exclusive public performance right for copyright owners of sound recordings, limited to certain performances made by then existing satellite and cable digital subscription services, and it exempted performances made by broadcasters over the air. Three years later, the Digital Millennium Copyright Act (1998) expanded the protection to reach performances offered by webcasters and new subscription services, and it retained the exemption for terrestrial broadcasters.

**Table 2: Legal Protection of Public Performance of Copyrighted Material by Type of Transmission**

Type of radio transmission	Type of copyright license needed and royalty paid	
	Musical work	Sound recording
Broadcast radio	✓	
Satellite radio	✓	✓
Internet radio, including simulcasts of broadcast radio	✓	✓
Cable radio	✓	✓

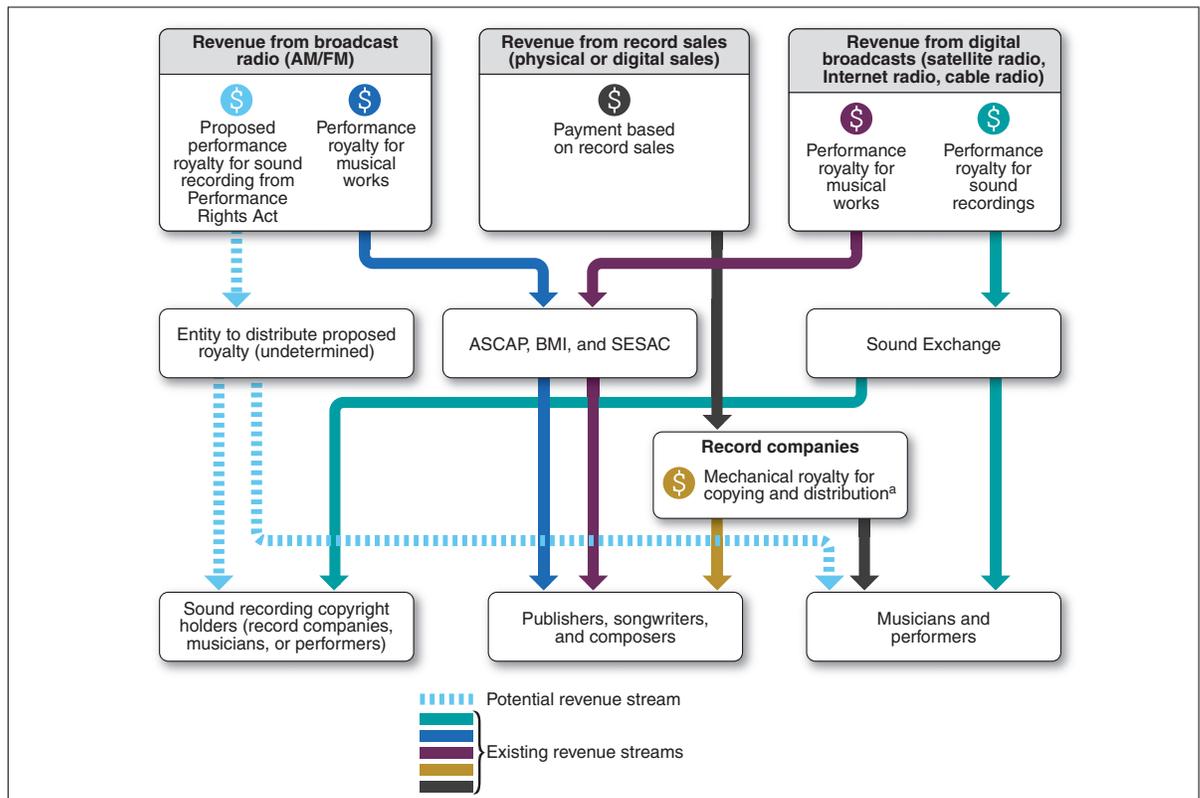
Source: GAO.

Royalties for the public performance of musical works and sound recordings are collected and distributed by performing rights organizations (PRO) and Sound Exchange. PROs such as The American Society of Composers, Authors, and Publishers (ASCAP), Broadcast Music, Inc. (BMI), and SESAC, negotiate and distribute licenses and royalties for the public performance of musical works. These PROs represent songwriters, publishers, and other copyright holders of musical works. Sound Exchange, established by the Recording Industry Association of America (RIAA), negotiates and administers licenses and royalties for the public performance of the sound recording for digital transmissions, such as satellite radio. Sound Exchange represents record companies, featured musicians and performers, and other copyright holders of sound recordings.

Various individuals and groups from the recording industry are involved with the creation of music and receive revenues from royalties and sales. The featured musicians and performers are the bands and artists individuals hear on broadcast radio and whose music individuals purchase. Session or background musicians and performers are the individuals that primarily work in recording studios and perform the music heard on a recording or provide background vocals to a recording. In addition, songwriters, composers, and publishers are involved with writing the words and melody of a song. These individuals and groups share in the revenues generated through royalties paid by broadcast radio and digital transmissions and from record sales.<sup>7</sup> Figure 1 shows how recording industry revenues are distributed among the various entities involved in the creation of a recording.

<sup>7</sup>The recording industry receives revenue from additional sources, but the sources we discuss represent the largest and most relevant for our reporting. For example, songwriters and publishers receive royalties when their music is broadcast at restaurants and bars.

**Figure 1: Revenue Flows from Broadcast Royalties and Record Sales**



Source: GAO.

<sup>a</sup>The record company is required to pay the copyright holder for the musical work a mechanical royalty for each record manufactured. This is typically paid directly to the copyright holder or through a third party entity, the Harry Fox Agency.

The broadcast radio industry in the United States consists of 14,441 licensed broadcast radio stations. Of all licensed stations, 11,162 are commercial and 3,279 are noncommercial. Over 65 percent of stations in operation have music formats, and approximately 18 percent have nonmusic formats such as news, talk, or sports.<sup>8</sup> Approximately 17 percent of stations in operation are religious stations with both music and talk formats.

Since 1996, the broadcast radio industry has experienced an increase in the total number of commercial radio stations but a decrease in the number of commercial station operators. FCC reported a 6.8 percent increase in the number of commercial stations between March 1996 and March 2007 and a 39 percent decrease in the number of radio station owners for the same period.<sup>9</sup> At the same time, the number of stations owned by the two largest operators increased from 62 and 53 stations to 1,100 and 300, respectively.

**According to Industry Stakeholders, the Recording Industry and Broadcast Radio Industry Are Experiencing a Number of Economic Challenges**

Due to a decrease in physical record sales, the recording industry has experienced a decline in sales revenue. The decline in record sales has been due in part to changes in the industry from the advancement of digital technology. The broadcast radio industry has also experienced declines in revenue generated from advertising sales. Both the current economic

<sup>8</sup>The music format categories in this report include stations that have both music and nonmusic programming and stations reporting formats that do not clearly indicate whether they have music or nonmusic programming.

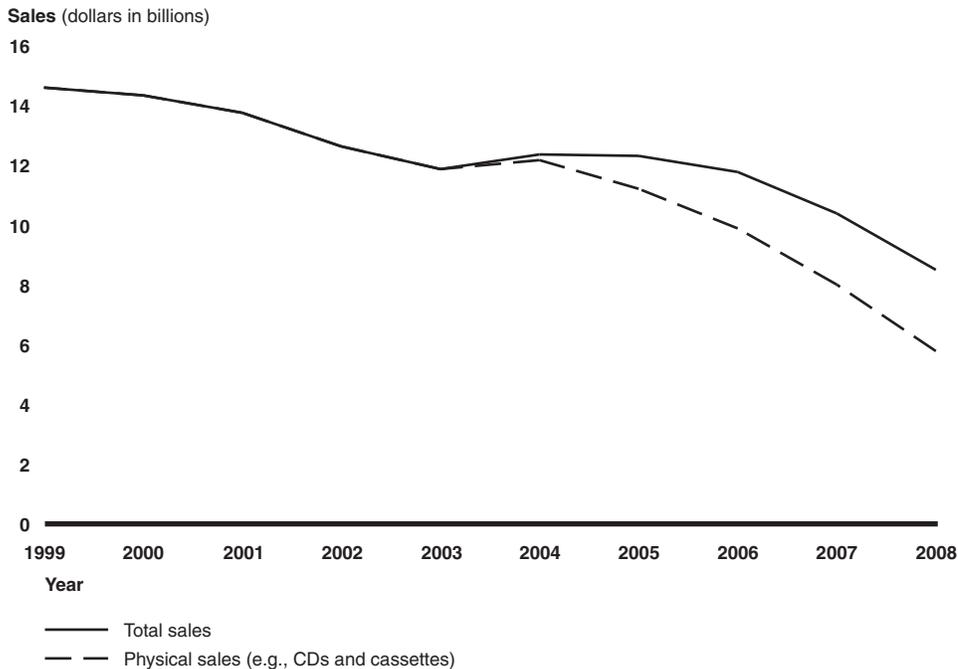
<sup>9</sup>FCC, Media Bureau, *Review of the Radio Industry, 2007*.

downturn and competition from other outlets, such as the Internet, have contributed to the decline in advertising revenue.

Declining Sales Revenue in the Recording Industry, Facilitated by Digital Technology, Has Reduced the Resources Available for the Development of Artists

According to RIAA, the recording industry has experienced declining record sales since the late 1990s. As shown in figure 2, revenue from the sale of physical records, such as CDs and cassettes, has declined by approximately 60 percent from 1999 to 2008. This decline has been partially offset by the sale of digitally downloaded music, which represented approximately 30 percent of sales in 2008. However, the revenue generated from digital sales has not fully offset the revenue lost due to the decline in physical record sales because most digital downloads are single songs, which often sell for 99 cents, and not full records, which often sell for \$10 or more.

**Figure 2: Total Revenues and Revenues from Physical Record Sales Based on Units Shipped, 1999 through 2008**



Source: RIAA.

Stakeholders from the recording industry identified the following three changes in the industry, all related to developments in digital technology, that have contributed to the decline in physical record sales:

- *Ease of illegal download and distribution.* Piracy, or the illegal copying and distributing of music, and particularly the illegal digital uploading and downloading of music, has contributed to the decline in record sales. Stakeholders with whom we spoke said that the ability to acquire music on-demand, without paying for a copy that would be retained, has led to a culture where younger listeners think all music should be free.
- *Increase in purchase of singles.* The evolution of legal digital downloading through sources such as iTunes® has led consumers to purchase more single songs and fewer full records. According to RIAA, in 2008, 95 percent of digital downloads were singles. While these downloads generate revenue for the recording industry, the revenue is

not sufficient to offset the revenue lost from the decline in physical record sales, according to recording industry stakeholders.

- *Shift to on-demand listening.* Technologies, such as the Internet, enable listeners to hear music on-demand without buying it; this technology has shifted listeners' behavior to music "access" and away from the purchasing behavior that historically supported the recording industry. Rather than purchase a physical or digital copy of a record or song, listeners select a song or type of music for listening.

According to industry stakeholders, less revenue from record sales has led to fewer resources for record companies to develop musicians and performers and fewer opportunities for session musicians and performers. Record companies invest in musicians and performers with the hope that the act will become popular and provide a return on its investment through record sales and concert tours, among other things. Because of decreasing revenues derived from music, record companies and musicians have less incentive to invest in music. According to stakeholders with whom we spoke, the decline in revenues has meant that record companies cannot invest in as many new musicians and performers. For example, a major record company indicated that in the past 5 years the musicians and performers it has under contract have dropped by approximately 28 percent.<sup>10</sup> The reduction in revenues has affected session performers and musicians by decreasing work opportunities. That is, as record companies sign fewer artists, there are fewer recording sessions where the professional session musicians and performers primarily work.

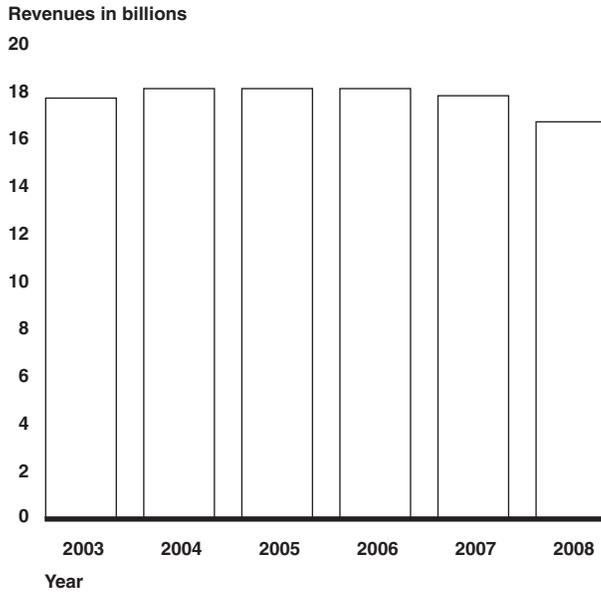
#### Broadcast Radio Industry Has Experienced a Decrease in Advertising Revenue

Since 2006, the broadcast radio industry has experienced declining advertising revenue. As shown in figure 3, from 2003 through 2008, radio industry revenues have declined about 8 percent from their peak of \$18.1 billion.

---

<sup>10</sup>Many stakeholders with whom we spoke said that more music is being created than ever before. Thus, the fact that fewer musicians and performers are being signed to contracts does not prevent music from being made but, according to recording industry stakeholders, does affect the quality of music.

**Figure 3: Broadcast Radio Revenues, from 2003 through 2008**



Source: BIA/Kelsey (2009).

For radio, advertising represents the primary source of revenue, and stakeholders identified two factors that have contributed to the decline in radio advertising revenue:

- *Economy.* The current economic decline has hurt many areas of the economy and has been a factor in the decline of radio advertising revenue. For example, automobile dealers have historically advertised on radio, but the economic downturn has forced some automobile dealers to close; this has reduced a revenue source for radio.
- *Consumer fragmentation.* Broadcast radio revenue has also decreased due to the fragmentation of consumers across a greater number of media platforms. According to stakeholders with whom we spoke, listeners have more entertainment options to fill their free time, such as the Internet and mobile devices. Greater numbers of entertainment options take listeners away from the radio, and advertising revenues are based in part on the number of listeners. In addition, with greater fragmentation, advertisers spread the dollars that were previously dedicated to radio across more media platforms, such as the Internet.

**According to Industry Stakeholders, the Recording and Broadcast Radio Industries Each Benefit in Several Ways from Their Current Relationship**

The recording industry benefits from its relationship with the broadcast radio industry by receiving broadcast radio airplay, which promotes the sale of records and concert tickets. The broadcast radio industry benefits by using sound recordings to attract listeners, which in turn generates advertising revenue for radio stations.

The Recording Industry Benefits from Its Relationship with the Broadcast Radio Industry through Airplay That Promotes Record and Concert Ticket Sales

According to industry stakeholders, broadcast radio promotes sound recordings for the recording industry by introducing listeners to new music and increasing listeners' exposure to music, which can lead to record and concert ticket sales.<sup>11</sup> Stakeholders from both the

<sup>11</sup>There is little empirical research examining the impact of radio airplay on record and concert ticket sales. Dertouzos, in a paper prepared for the National Association of Broadcasters, found that radio airplay contributed to increased record sales. Alternatively, Liebowitz found that radio airplay does not benefit overall record sales.

recording and broadcast radio industries told us that broadcast radio is the leading means by which listeners discover new music. Radio stations help this discovery process by announcing artists' new records and upcoming concerts before or after broadcasting sound recordings. As listeners' awareness increases, record companies benefit from corresponding increases in record and concert ticket sales. Additionally, record companies' past and current practices illustrate that radio airplay provides benefits for the industry. The historical record of illegal payola activity illustrates that the recording industry has been willing to pay the broadcast radio industry for airplay.<sup>12</sup> For example, in 2004, New York opened an investigation into payola practices by the four major record companies. This investigation resulted in settlement agreements with the record companies.<sup>13</sup> In response to the findings in New York, FCC investigated broadcast radio's involvement in payola activities and entered into consent decrees with four major broadcast radio companies.<sup>14</sup> FCC noted the commission continues to receive payola complaints since it entered into the payola decrees in 2007. In addition, record companies employ staff dedicated to the promotion of music to radio. Both activities—illegal payola and legal promotion—exemplify the importance of radio airplay to a sound recording.

While broadcast radio airplay helps promote sound recordings, this promotion can vary and has declined in recent years according to recording industry stakeholders:

- *Promotional value varies according to several factors.* Recording industry stakeholders indicated that the promotional value provided by broadcast radio airplay varies according to the musician and performer, genre, age of each sound recording, and factors related to the audience. (See figure 4.) A new artist with little prior exposure to radio's broad audience receives more promotional value from airplay than a well-known, established performer like Madonna. Similarly, new or recently-released sound recordings receive more promotional value from airplay than catalog<sup>15</sup> sound recordings like Ben E. King's "Stand By Me," which was originally released in 1961. Finally, promotional value can vary by genre; for example, country music has closer ties to radio, and its audience relies more on radio than other genres.

---

See James N. Dertouzos, *Radio Airplay and the Record Industry: An Economic Analysis*, a paper prepared for the National Association of Broadcasters, June 2008; and Stan J. Liebowitz, "The Elusive Symbiosis: The Impact of Radio on the Record Industry," *Review of Economic Research on Copyright Issues*, vol. 1, no. 1 (2004).

<sup>12</sup>According to FCC, payola is the practice of payment of money or other consideration to a station in exchange of airplay of music. A station that plays a musical selection in exchange for such consideration must air an announcement, at the time the song is broadcast, disclosing the arrangement and identifying who furnished or on whose behalf the consideration was furnished.

<sup>13</sup>The settlement with each company was similar in nature and included a donation to music education and appreciation programs (over \$30 million total donation) and admission of its payola practices.

<sup>14</sup>The consent decree with the broadcast radio companies included a voluntary contribution to the U.S. Treasury (\$12.5 million total contribution) and agreement to implement specific reforms over a 3-year period to help end payola practices.

<sup>15</sup>Catalog music is defined as music that has been released for more than 18 months.

**Figure 4: Factors Affecting Promotional Value from Airplay Received by the Recording Industry**

Lower promotional value	Factors affecting promotional value	Higher promotional value
Performers and musicians who <ul style="list-style-type: none"> <li>• are well-known or established</li> <li>• are not currently on tour</li> <li>• have not recently released a new record</li> </ul>	<b>Performer and musician</b>	Performers and musicians who <ul style="list-style-type: none"> <li>• are new, relatively unknown artists</li> <li>• are currently on tour</li> <li>• have recently released a new record</li> </ul>
Song genre does not match radio station genre	<b>Genre of music</b>	Song genre matches radio station genre
Music that has aged to catalog status	<b>Age of sound recording</b>	Music that has not aged to catalog status, especially a sound recording within the first nine months following its initial release.
Audience has less reliance on radio <sup>a</sup>	<b>Audience</b>	Audience has greater reliance on radio

Sources: GAO and RIAA.

<sup>a</sup>“Reliance on radio” is a function of one or both of the following: the audience’s access to alternative listening technologies, and the audience’s preference for radio over other listening technologies. For example, an audience could have less reliance on radio if it has access to broadband technology which would allow the use of the Internet for music listening.

- *Promotional value of broadcast radio has decreased.* Recording industry stakeholders with whom we spoke said that the promotional value of broadcast radio has decreased over time due to the emergence of competing technologies. When broadcast radio was the sole means for the promotion of sound recordings, the recording industry could focus on having sound recordings played on broadcast radio. Listeners who liked what they heard on the radio bought physical records for personal use. While broadcast radio remains the most common place to discover new music, new technologies, such as satellite radio, video games, and the Internet (including digital Webcasting, iTunes®, and artist Web sites), offer alternative platforms that promote sound recordings and compete for radio’s listeners. Because some new platforms enable listeners to hear music on demand without buying it, listeners have shifted to music “access” and away from the purchasing behavior that historically supported the recording industry. As a result, airplay leads to fewer sales and therefore has less promotional value today than before alternative platforms existed.

The Broadcast Industry Benefits from the Use of Sound Recordings to Attract Listeners and Generate Advertising Revenue

The broadcast radio industry benefits from its relationship with the recording industry through the revenue generated from selling advertising. Radio provides content that matches listeners’ tastes based on market research and other factors. Radio stations seek to attract as many listeners as possible and an audience whose demographics will appeal to advertisers. As mentioned previously, advertising is the primary source of revenue for broadcast radio stations, and many stations use music to attract listeners.<sup>16</sup> Commercial radio stations

<sup>16</sup>Broadcast radio also uses other forms of content, such as talk, sports, and news and information.

broadcasting music comprise approximately 70 percent of all commercial radio stations, illustrating that music is the most popular form of content. Further, we found that the revenues from commercial radio stations broadcasting music comprised approximately 80 percent of all commercial broadcast radio revenues.

Broadcast radio industry stakeholders acknowledge that they benefit from using music as content, but said they already pay for licenses that allow them to use the musical works. As mentioned previously, music has two types of copyright protections: the musical work and the sound recording. While broadcast radio stations do not pay a royalty for sound recordings, they do pay approximately 3 percent of their revenues to PROs to purchase licenses for the use of the musical works, which allow radio stations to legally broadcast music.<sup>17</sup> The PROs collect these fees and distribute them among their membership, which includes publishers, songwriters, and composers. PRO members' royalty payments vary in size based on the licensing fees paid by radio stations and the type of performance.<sup>18</sup>

### **The Proposed Performance Rights Act Would Result in Additional Costs for Broadcast Radio Stations**

The proposed Performance Rights Act would result in both financial costs, in the form of royalty payments for the use of sound recordings, and administrative costs, in the form of potential reporting requirements. These financial and administrative costs may lead some stations to make adjustments, such as reducing staff levels, switching to a nonmusic format, and ceasing operation, according to broadcast industry stakeholders.

#### Broadcast Radio Stations Would Pay Different Royalties Depending on Their Use of Music, Commercial or Noncommercial Status, and Annual Revenues

Under the proposed Performance Rights Act, the statutory royalty paid by broadcast radio stations would vary according to the stations' format and gross annual revenues. As previously mentioned, as of November 2009, there were 14,441 licensed broadcast radio stations, of which 11,162 were commercial radio stations. Of the 11,162 commercial stations, 7,886 have a music format. Commercial stations with a music format represent the majority of stations affected by the proposed act. As shown in table 3, 67 percent of these radio stations would pay a flat royalty, with the remaining stations paying a royalty that would be negotiated or set by the copyright royalty judges; however, these remaining stations generate 79 percent of all advertising revenue for commercial music stations. Of the 3,279 noncommercial radio stations, approximately 41 percent of these radio stations would pay an annual flat fee of either \$500 or \$1,000 because they have a music format; the remaining noncommercial stations do not have a music format.<sup>19</sup>

---

<sup>17</sup>To determine the percentage of revenue paid by the broadcast industry to PROs, we expressed the annual licensing fees paid to PROs as a percentage of broadcast industry revenue.

<sup>18</sup>Type of performance can include broadcast radio, Internet, cable television, and live concerts.

<sup>19</sup>The lack of existing revenue data on noncommercial broadcasters prevents us from identifying how many stations would fall into each rate level.

**Table 3: Number of Commercial Music Stations within Each Royalty Payment Level, Based on the Proposed Performance Rights Act**

Proposed royalty rate based on revenue	Commercial music stations		
	Number of stations	Percent of stations	Percent of advertising revenue
Royalty rate to be negotiated or set by the copyright royalty judges	2,598	33%	79%
Flat fee of \$5,000 per year	2,600	33	16
Flat fee of \$2,500 per year	2,215	28	5
Flat fee of \$500 per year	473	6	<1

Source: GAO analysis of BIA/Kelsey data.

Note: GAO analysis based on data available as of November 23, 2009.

Stakeholders Identified Several Potential Effects Arising from the Proposed Performance Rights Act

The proposed act would result in additional costs for the broadcast radio industry in the form of royalty payments and reporting requirements. As discussed previously, most broadcast radio stations will be required to pay a royalty for the use of a sound recording. In addition, radio stations that broadcast music will have to track and report each sound recording. While some radio stations have automated systems for this, representatives of commercial and noncommercial stations said that others cannot afford this technology or the staff required to track and report this information.

Due to these burdens, stakeholders from the broadcast industry identified the following potential effects:

- *Staff reductions.* Broadcast radio stations might reduce staff, which represents the largest cost for many radio stations. While some radio stations have already reduced staff as a result of the decline in revenue mentioned previously, stakeholders indicated that other stations may be forced to lay off additional staff.
- *Changing to nonmusic formats.* According to the National Association of Broadcasters, radio stations might switch from a music format to a nonmusic format, such as talk or news, to avoid the additional costs of a royalty. However, the feasibility of switching from a music format to a nonmusic format would also be determined by market factors. For example, if there are many talk radio stations in a market, a station may not switch to talk radio because the market cannot support another station of that format. While switching to nonmusic formats may occur, among stations retaining a music format, a royalty should not cause stations to change the genre of music it plays or the variety of music because stations already make these decisions based on ratings data and market research. Furthermore, the proposed royalty does not vary based on the genre of music played by a radio station.

- *Discontinued operation.* Some stakeholders reported that broadcast radio station operators currently struggling to earn a profit may go out of business entirely. Broadcast industry stakeholders said that the additional burden of any cost may be too much for some station operators to handle and might force these stations to close operations. However, operators encountering financial difficulties can sell their licenses, and FCC officials stated that the commission continues to receive a high volume of applications for licenses. The commission also noted that the substitution of a new station operator to provide service would not be easily or expeditiously attained, possibly creating a loss of service to a community.

**The Proposed Performance Rights Act Would Result in Additional Revenue for Record Companies, Musicians, and Performers, Which Could Lead to More Investment in Music, According to Recording Industry Stakeholders**

The proposed Performance Rights Act would result in additional revenue for the recording industry. Specifically, new revenue could come from two sources: royalties paid by broadcast radio in the United States and royalties paid by broadcast radio in foreign countries.

- *U.S. royalties.* As mentioned previously, approximately 67 percent of commercial music stations have annual revenues of less than \$1.25 million. We estimate that royalties from these stations will generate approximately \$18.7 million in annual revenue for the recording industry. The remaining 33 percent of commercial music stations have annual revenues of \$1.25 million or higher. Because the royalty rates for these stations would be either negotiated or set by the copyright royalty judges, we do not know what the royalty rates would be at this time. For our final report, we intend to provide estimates, based on prior decisions of the copyright royalty judges, of the revenues generated from stations that would not make a flat annual royalty payment.
- *International royalties.* Currently, musicians and performers from foreign countries receive a performance royalty when their music is broadcast on radio in other countries. Musicians and performers from the United States whose music is broadcast on foreign radio do not receive these performance royalties because the United States does not have a reciprocal performance royalty. If the proposed act were passed, U.S. musicians and performers could begin receiving royalties from foreign countries. However, existing trade agreements and foreign laws would influence these international royalties, and we do not know when or how much revenue U.S. musicians and performers would receive.

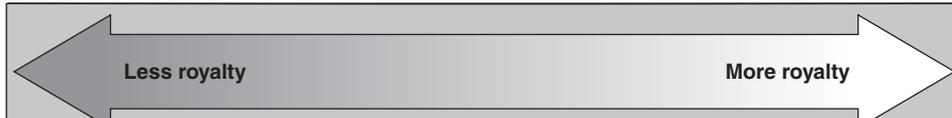
The proposed act, along with the extent to which a sound recording is broadcast on radio, will determine the amount and distribution of royalty revenues to record companies, musicians, and performers. As mentioned previously, 50 percent of the revenue from a statutory royalty would be paid to the copyright holder, typically the record company; 45 percent would be paid to the primary musicians and performers; and the remaining 5 percent would be shared by background musicians and performers. The amount of royalties received will be determined by how often the sound recording is played on broadcast radio.<sup>20</sup> As figure 5 shows, various factors, including the musicians and performers, genre of music, and role in creation of the music, would influence the amount of royalty revenue an individual or company receives. For example, Taylor Swift, the performer with the most radio airplay in 2009, would receive more revenue than a performer that receives less airplay. Furthermore, stakeholders reported that the amount of royalty received by musicians and performers will differentially affect their overall income. For example, for a performer who would receive a high royalty payment because

---

<sup>20</sup>Sound Exchange distributes royalties paid by satellite radio to performers and musicians based on how often their sound recordings are played. We assume that performers and musicians will receive royalties paid by broadcast radio in a like manner.

a sound recording is played frequently, the performance royalty may have less of an overall impact on their income because of other income streams, such as income from sales of records and concert tickets.

**Figure 5: Factors Affecting the Level of Royalty Payments Received, Based on the Proposed Performance Rights Act**

		
	Factors determining the level of royalty received	
Less popular performer or musician with few songs or spins on broadcast radio	<b>Performer and musician</b>	Popular performer or musician with many songs or spins on broadcast radio
Performer or musician whose music matches a genre with few stations dedicated to that type of music, such as jazz	<b>Genre of music</b>	Performer or musician whose music matches a genre of music that is played by many radio stations, such as adult contemporary
Session musicians and performers that perform on the recording of a song played on the radio <sup>a</sup>	<b>Role in creation of music</b>	Copyright holder will receive the largest percent of royalty <sup>b</sup>

Sources: GAO and RIAA.

<sup>a</sup>Session musicians and performers will share 5 percent of the royalty.

<sup>b</sup>As previously indicated, the copyright holder is typically the record company. A featured musician that holds the copyright, as can be the case with more popular musicians and performers would receive 95 percent of the royalty.

Stakeholders with whom we spoke said that the additional revenue from a performance right would benefit record companies, musicians and performers, and session musicians differently, but could lead to more investment in the creation of music. By increasing the revenues derived from a song, the act could encourage record companies and musicians to make additional investments in music. According to record companies, the additional revenue from performance royalties would allow the companies to sign new musicians and performers and to retain musicians and performers under contract for a longer period of time. Additional revenue for artists and musicians would allow these groups to remain working in the music industry. Session musicians and performers would benefit from the royalty revenue directly, and also indirectly since the royalty revenue would likely lead to additional studio work arising from record companies' potential increased investments in music.

### Agency Comments

We provided a draft of this assessment to the Federal Communications Commission and the Library of Congress. In its letter, FCC emphasized the financial difficulties in the broadcast radio industry. In particular, FCC cited the recent bankruptcy filing of the nation's third largest holder of licenses, the negative impact that station layoffs might have on the public interest, and the possible loss of service when a station discontinues operation. FCC also suggested that we clarify how we classified stations as music or nonmusic and provided other technical comments that we incorporated where appropriate. FCC written comments appear as enclosure II. The Library of Congress also provided technical comments that we incorporated as appropriate. (See [GAO-10-707SP](#) for the Copyright Office's written comments.)

---

As arranged with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to the Chairman, FCC; Register of Copyrights, Library of Congress; and interested congressional committees. This report will also be available at no charge on the GAO Web site at <http://www.gao.gov>.

If you or your staffs have questions about this report, please contact me at (202) 512-2834 or [goldsteinm@gao.gov](mailto:goldsteinm@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this assessment were Mike Clements (Assistant Director), Namita Bhatia Sabharwal, Christine Hanson, Eric Hudson, Bert Japikse, and Jonathon Oldmixon.



Mark L. Goldstein  
Director, Physical Infrastructure Issues

Enclosures

## Enclosure I: Scope and Methodology

This report examines the potential effects of the proposed Performance Rights Act, H.R. 848. In particular, the report provides information on (1) the economic challenges facing the recording and broadcast radio industries, (2) the benefits both industries receive from their current relationship, (3) the potential effects of the proposed act on the broadcast radio industry, and (4) the potential effects of the proposed act on the recording industry.

To assess the status of both the recording and broadcast radio industries, the benefits both receive from their current relationship, and the potential effects on both industries, we reviewed relevant reports and analyses of both industries and interviewed stakeholders from both industries, as well as government agencies. To identify relevant stakeholders from the recording industry, we constructed a judgmental sample that consisted of the four largest U.S. record companies, as well as independent record companies that varied with respect to the number of artists signed to each company, the genres of music produced, and the geographic location of each company. We also interviewed trade associations that represent the industry, such as the Recording Industry Association of America. We also interviewed performing rights organizations that distribute royalties for the musical work licensees and the digital performance of sound recording licensees. We interviewed industry experts and individuals that work in the industry, such as managers, accountants, lawyers, and union groups who represent musicians and performers, as well as musicians and performers. We also constructed a judgmental sample of stakeholders from the broadcast radio industry, including station owners and operators that varied with respect to station revenue, market size, geographic location, and genre. We interviewed broadcast industry experts and trade associations that represent the industry, such as the National Association of Broadcasters. Furthermore, we interviewed officials from the Federal Communications Commission's (FCC) Media Bureau to understand FCC's involvement in broadcast radio, including licensing, regulation, and oversight; to gain information about available data on broadcast station ownership; and to identify broadcast industry and other stakeholders to execute the engagement. We obtained relevant legislation and federal regulations that establish FCC's rules for broadcast radio. We obtained FCC reports on broadcast license requirements and ownership. We also interviewed officials from the Library of Congress' Copyright Office to understand its role relevant to U.S. copyright law; to gather information on laws relevant to the proposed act; to discuss Congress' previous legislative activities involving music and copyrights; to review relevant copyright history; to identify stakeholders to execute the engagement; and to understand how the proposed act could affect the Library of Congress. We also spoke with a copyright royalty judge to understand the rate-making process. We gathered information on other industries that pay performance rights for the use of sound recordings, including digital and satellite radio and television, as well as information on how royalties are assessed and distributed in these industries. We reviewed independent and industry analyses of the value of sound recordings to radio and the value radio provides to sound recordings. We also reviewed previous congressional considerations of a performance royalty for broadcast radio in the United States and gathered information about the existence of performance royalties in countries outside the United States.

To assess the potential effects of the proposed act on the broadcast radio industry and the recording industry, we analyzed data from 2008 on broadcast radio stations' revenues. Using the BIA Media Access Pro database, we determined the annual revenues of all commercial broadcast radio stations. Before conducting our analyses, we addressed certain features and limitations of the data to enhance the precision of our results. We identified commercial and noncommercial stations, their primary and secondary formats for each station, as well as "dark" stations not currently broadcasting. We classified commercial broadcast radio stations as either music or nonmusic based on the station's primary format. We did this in order to compare revenue for music versus nonmusic stations and to eventually determine the royalty rate each station would pay. Next, we imputed station revenue for sister stations that did not

report revenue information.<sup>21</sup> We accomplished this by identifying the sister stations that reported revenue and allocating the total reported revenue between that station and its nonreporting sister station. We also had to impute the total revenues for nonreporting stations that were not sister stations, which accounted for approximately 40 percent of the stations. In order to do this, we ran a regression using the primary license coverage population, format category, license class, and whether it was an Arbitron market, as the explanatory variables. Based on this, we were able to develop predicted revenues for the nonreporting stations and scaled this to \$4 billion, the unaccounted-for total revenues of the broadcast radio industry. To calculate the number of commercial stations that would be required to pay each of the three royalty fees provided by the act, as well as the number of stations that would be required to pay a royalty rate determined by the copyright royalty judges, we identified commercial stations with revenues that corresponded to each of the three flat-fee rate categories stated in the act. To determine the potential transfer of revenues from broadcast radio industry to the recording industry we multiplied the number of stations in each rate category by the respective rate and summed these figures to arrive at a partial estimation<sup>22</sup> of the royalty income that the act would generate.<sup>23</sup> The total income cannot be calculated until the copyright royalty judges determine a rate for stations whose revenues exceed \$1.25 million. We assessed the reliability of data by (1) performing electronic testing of required data elements; (2) reviewing existing information about the data and the system that produced them; and (3) interviewing BIA officials about measures taken to ensure the reliability of information in BIA Media Access Pro. On the basis of our review, we determined that the information in the BIA Media Access Pro database was sufficiently reliable for the purposes of our report.

We conducted this performance audit from June 2009 through February 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

---

<sup>21</sup>Sister stations are stations owned by the same individual or group of owners in the same market area.

<sup>22</sup>Rate information for noncommercial stations is not included.

<sup>23</sup>These results were checked using STATA software.

## Enclosure II: Comments from the Federal Communications Commission



Federal Communications Commission  
Washington, D.C. 20554

February 22, 2010

Michael E. Clements, Ph.D.  
Assistant Director, Physical Infrastructure Team  
U.S. Government Accountability Office  
441 G Street, N.W.  
Washington, D.C. 20548

Re: GAO-10-428R

Dear Dr. Clements:

Thank you for the opportunity to review and comment on the Government Accountability Office (GAO) Draft Report, *Preliminary Observations on the Potential Effects of the Proposed Performance Rights Act on the Recording and Broadcast Radio Industries* (the "Draft Report").

While the Draft Report does not contain any specific recommendations for action by the Federal Communications Commission (the "Commission" or "FCC"), it does note that the proposed Performance Rights Act (the "PRA"), which is contained in H.R. 848, as well as S. 379, would, with certain limited exceptions, obligate broadcast radio stations that air sound recordings to pay royalties that would go to the recording copyright holder(s), performers and musicians. As the Draft Report notes, under the proposed legislation, the amount of the royalty that a radio station would pay would be based upon both the level of its revenues and its status as a commercial or a noncommercial educational station. In light of the Commission's jurisdiction over broadcasting, we have a great interest in the subject of your Draft Report, in particular your assessment of the potential impact of this proposed requirement on radio licensees.

In that discussion, we suggest that the Draft Report might elaborate more on the distressed financial state of the radio industry. As you note in the draft, economic conditions and the fragmentation of listeners among newer technologies have reduced radio advertising revenues, the industry's primary revenue source. This drop in advertising revenues apparently continued during 2009: the Radio Advertising Bureau reported last week that radio industry advertising sales were about eight percent lower than those during 2008. As a result of these forces, particularly since the crisis in the financial markets in September 2008 and the resulting economic downturn, the radio industry has seen a number of licensees seek bankruptcy protection. For example, in December 2009, the nation's third largest holder of radio licenses sought such protection. Financial pressures from the need to service debt levels have forced other radio licensees to restructure their financing arrangements with their lenders. In many such cases, facing major potential losses from licensee defaults, creditors have been forced to convert their rights into station equity positions, and then tend to favor bare bones operations to preserve asset value. These conditions have also resulted in broadcast employee layoffs, declining station values and sale prices, and a dearth of available financing for broadcast station acquisitions. As

a result, the number of radio station sales and the total valuation of such transactions have also decreased substantially.

The Draft Report observes that the financial burden from the proposed new PRA royalties might force some stations to lay off yet additional personnel in order to cut costs. This discussion might note the potential impact on the public interest from those actions, particularly on the ability of stations to meet the objectives of localism, diversity, and competition that are the basis of the Commission's regulation of broadcasting. For example, the necessity to make staff cuts would conceivably diminish the ability of a radio station to continue to provide service to its community. Such service includes not only the music and other entertainment programming that a station's listeners enjoy, but also the local news and information upon which they rely. This news and information programming can be critical at times of emergency, such as natural disasters, adverse weather, and other crises.

The Draft Report also acknowledges the possibility that the financial burden from the proposed royalties might compel a licensee to shut down its station operation entirely. Such a situation would similarly deprive the station's listeners of the entertainment, news, and information of interest to the members of their community, a result contrary to the public interest as discussed above. In light of the general economic conditions and the financial state of the radio industry, the substitution of a new station operator to provide that public service would not be easily and expeditiously attained, possibly prolonging the loss of service to the community. The decreasing values of stations and absence of financing sources for broadcast transactions noted above have made the sale of stations, particularly those that are failing, much more difficult to accomplish. Even if the licensee chose to simply surrender its station authorization to the Commission for future assignment (an unlikely proposition, given its investment in its broadcast facility), the Commission's process of opening the authorization to interested applicants and ultimately selecting a licensee from those filers could be lengthy.

We also recommend that the definition of payola contained in footnote 11 of the Draft Report be changed. The draft fails to note that it is not the provision to a station of consideration for airplay that is illegal, it is the failure of the station to disclose the arrangement in an announcement aired at the time that the song is played. Our proposed substitute language is as follows:

Payola is the practice of the payment of money or other consideration to a station in exchange for the airplay of music. Under Section 317 of the Communications Act of 1934, as amended, and Section 73.1212 of the FCC's Rules, a station that plays a musical selection in exchange for such consideration must air an announcement, at the time that the song is broadcast, disclosing the arrangement and identifying who furnished or on whose behalf the consideration was furnished.

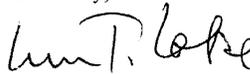
Also on the subject of payola, the Draft Report could note that the Commission has continued to receive payola complaints since April 2007, when it entered into the four consent

decrees with four large radio licensees discussed at page 13 of the Draft Report. We also have entered into two other payola consent decrees with radio licensees since that time (in October 2008 and March 2009). This suggests that the practice continues to some degree and, accordingly, that station airplay is still viewed as having some impact on music sales.

As a final matter, we have not reviewed the accuracy of your analyses of stations, their revenues, or formats, or the initial projection of the aggregate PRA payments contained in the Draft Report. Similarly, we have not verified the validity of the data upon which you have relied for such analyses. However, we note that footnote 7 of the Draft Report acknowledges an apparent lack of precision in the classifications of "music" and "non-music" stations contained in the BIA Media Access Pro database. That database provides the basis for the projection of the number of commercial music stations that would be required to pay the royalties at each payment level under the Performance Rights Act contained in Table 3 and the projected aggregate royalty amount. At a minimum, we suggest that the Draft Report more prominently note that caveat or provide a more detailed explanation of your classification methodology.

Again, thank you for the opportunity to comment on the Draft Report. To the extent that we can be of further assistance, please do not hesitate to contact me or my staff.

Sincerely,



William T. Lake  
Chief, Media Bureau

---

---

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.

---

---

## GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

---

## Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site ([www.gao.gov](http://www.gao.gov)). Each weekday afternoon, GAO posts on its Web site newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to [www.gao.gov](http://www.gao.gov) and select "E-mail Updates."

---

## Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's Web site, <http://www.gao.gov/ordering.htm>.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

---

## To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: [www.gao.gov/fraudnet/fraudnet.htm](http://www.gao.gov/fraudnet/fraudnet.htm)

E-mail: [fraudnet@gao.gov](mailto:fraudnet@gao.gov)

Automated answering system: (800) 424-5454 or (202) 512-7470

---

## Congressional Relations

Ralph Dawn, Managing Director, [dawnr@gao.gov](mailto:dawnr@gao.gov), (202) 512-4400  
U.S. Government Accountability Office, 441 G Street NW, Room 7125  
Washington, DC 20548

---

## Public Affairs

Chuck Young, Managing Director, [youngc1@gao.gov](mailto:youngc1@gao.gov), (202) 512-4800  
U.S. Government Accountability Office, 441 G Street NW, Room 7149  
Washington, DC 20548