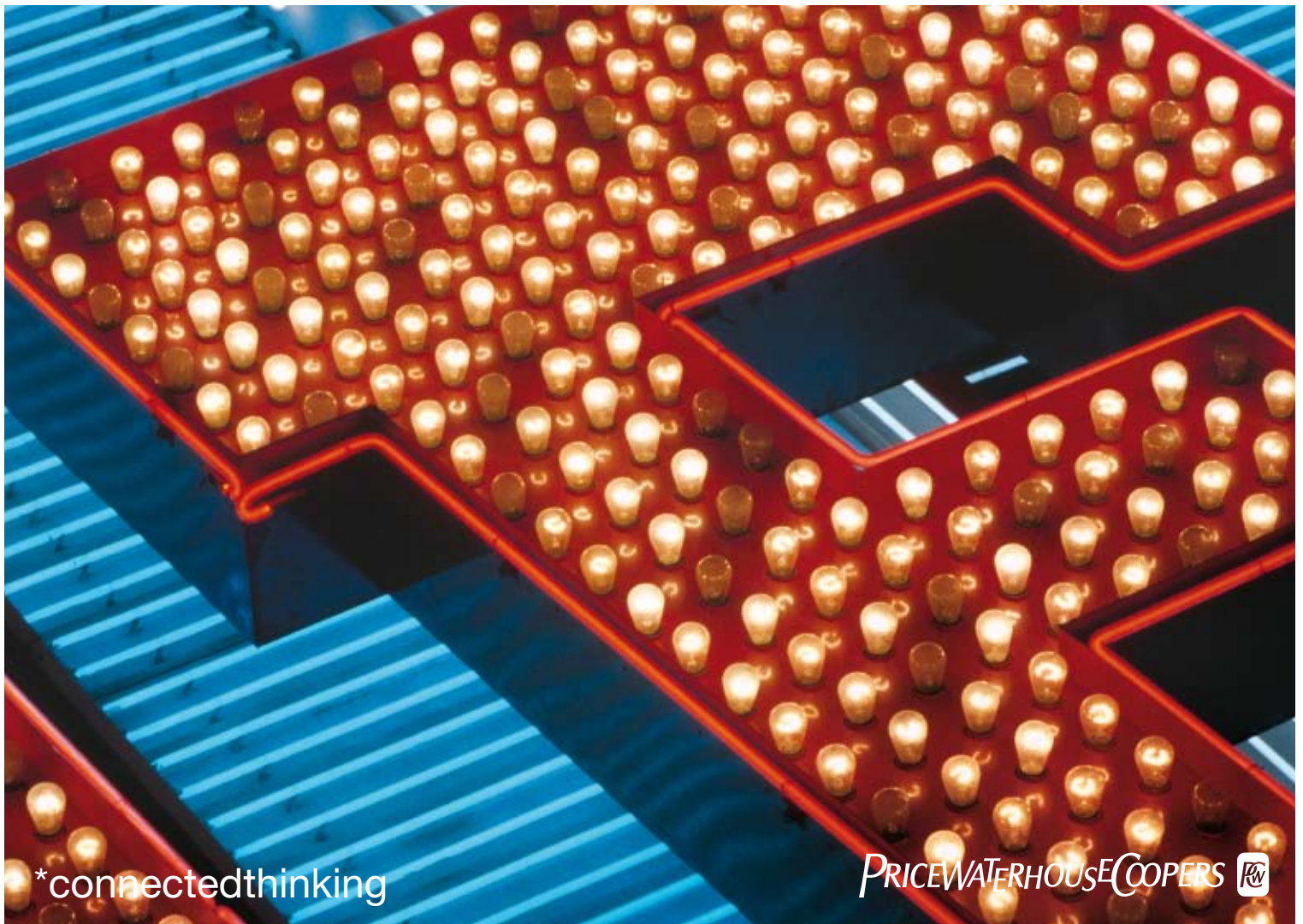


On Media

“Stay ... just a little bit longer”*



Strategy, regulation and valuation insights
from PricewaterhouseCoopers (PwC) in
the media sector.

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May 2007

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“Stay ... just a little bit longer”

On 6 December 2006 Andrew Gowers reported on the findings from his independent review into the UK intellectual property framework.¹ The 150-page report sets out 54 practical recommendations to deliver a robust IP framework, recognising its important contribution to the competitiveness of the UK economy, fit for the digital age. Many advocated change. Recommendation 3, however, appealed for the status quo. “*The European Commission should retain the length of protection on sound recordings and performers’ rights at 50 years*”, as did Recommendation 4, “*Policy makers should adopt the principle that the term and scope of protection for IP rights should not be altered retrospectively.*”

Many stakeholders disagreed - in response, a large number of recording artists and their trade associations placed a full-page advertisement in the Financial Times calling for “fair play” for musicians.

As an input into the Gowers review, PricewaterhouseCoopers (PwC) investigated the economic impact of an increase in the length of the copyright term on sound recordings for the British Phonographic Industry (BPI). Whilst Gowers accepted some of our points, he decided that potential costs of copyright extension exceeded the benefits we estimated.

“Welcome to the Jungle”

Why is the length of copyright on sound recordings such a big deal? Because copyright term is time of release plus 95 years in the US, and only release plus 50 in the EU. The BPI wanted to increase the term in the EU to match that of the US to eliminate any disadvantage. This might be the case because a longer term increases revenues to the copyright-owning record industry – revenues that could potentially be used to develop the next generation of recording artists. To supplement its submission to the Gowers Review, the BPI asked us to investigate a number of economic impacts of extension of copyright on sound recordings. The article summarises how we addressed these issues and our overall conclusions:

Impacts to investigate	Our findings
1. How might copyright extension affect UK record companies in terms of revenues?	A maximum possible financial impact of copyright term extension to UK copyright holders could be £35 million over the next ten years and up to £163 million over the next fifty. However, the amount of money at stake may vary considerably depending on the number of recording sales lost by copyright-owning record companies to others when copyright expires.
2. How might copyright extension affect the value of UK record companies?	PwC could not rule out an impact of copyright right term extension in the US on the share prices of record companies.
3. Is there a marked difference between the prices of in-copyright and out-of-copyright recordings?	PwC could not identify a statistically significant difference between the prices of in-copyright and out-of-copyright recordings.
4. How might the quantity of recordings made available by record companies might be affected by the copyright status of those recordings?	An extended copyright term increases the incentive for incumbent record companies to make recordings available. However, more investigation is required in this area to determine the actual effect on availability of back catalogues.

What does this mean? Copyright extension may increase the value of record companies to shareholders, and contribute to revenues that could potentially be used to develop new artists. A copyright term extension might not lead to a significant price difference between in-copyright and out-of-copyright recordings.

¹ “Gowers review of intellectual property”, HM Treasury, 6 December 2006.

“Born in the USA”

In the US on October 7th 1998, the “Sonny Bono Copyright Term Extension Act”² (CTEA) was passed. The CTEA extended copyright on recorded music for a further 20 years to “release plus 95 years”. Other countries have similarly long terms - Mexico (75 years), Australia (70 years) and Brazil (70 years), leading Phonographic Performance Limited (PPL)³ to state that the EU, at “release plus 50 years”⁴ is “out of sync with the rest of the world.”⁵ An anomaly also exists between composers and performers within the UK – a composer benefits from a term of life plus 70 years’ copyright on a sound recording, but performers only benefit from a term of 50 years.

There has been an ongoing debate regarding this topic but until now there has been little empirical evidence to back up many of the arguments. It is the subject of a campaign by the industry “bible”, Music Week, which has attracted comments from numerous music moguls, including Sir Cliff Richard and Paul McGuinness. It was also one of Tony Blair’s policy priorities back in 2005, according to the Sunday Times.⁶ Perhaps less well known is the fact that the debate has also attracted numerous eminent economists.

So what are the music industry and the economists saying? Here’s a limited download...

For copyright extension	Against copyright extension
Liebowitz (2006): ⁷ “...there are numerous economic grounds that can be adduced to support a request for extending the copyright on sound recordings. There are clear benefits that will arise from an increase in new creations and the proposed increase in copyright are large enough to lead to measurable increases in new production.”	Lessig (2005): ⁹ “The justification from an economic perspective is absolutely baseless.”
Sir Cliff Richard (2004): ⁸ “As a performer and recording artist it seems to me that there is a manifest injustice in awarding authors a period of protection which exceeds their life by 70 years whilst at the same time allowing sound recordings to fall into the public domain within the lifetime of the artists whose performances are embodied in them.”	Akerlof et al. (2003): ¹⁰ “It is highly unlikely that the economic benefits from copyright extension under the CTEA outweigh the costs. Moreover, in the case of term extension for existing works, the sizable increase in cost is not balanced to any significant degree by an improvement in incentives for creating new works.”
	Antony Anderson from Naxos (2006): ¹¹ “Most recordings aren’t actually available. Extending to 95 years will make a lot more content unavailable.”

“Money Money Money”

What is the big deal? Because the EU copyright term is 50 years, recordings from the mid-1950s and early 1960s (most notably The Beatles) are beginning to fall out of copyright – potentially reducing the revenues to record companies and performers as shown below.

Source of income	From	to	Impact due to end of copyright
1. Music sales	Retailers e.g. HMV, digital distributors e.g. Apple iTunes	Record companies	Loss in market share to public domain specialists. This can potentially range from 0% to 100%.
2. Licence fees	3rd party users e.g. advertising companies	Record companies	Loss in licence fee income. This is an immediate and total loss for recordings out of copyright.
3. PPL income	PPL	Record companies	Loss in income. This is again an immediate and total loss for recordings out of copyright.
4. PPL income	PPL	Performers	Loss in income (same as above).
5. Royalties	Record companies	Performers	Contracts vary for each individual performer. Some pay royalties until the end of the copyright and others pay royalties in perpetuity. We therefore did not assess the impact of an extension on this income source.

So, if you extend the copyright term, record companies and performers get revenues for longer. Simple. And this would have a positive impact on both record companies and performers who hold the copyrights.

By far the largest amount at stake is the potential impact on music sales. But just how big will this impact be? Projecting the future is always difficult and more so here because we do not know how much market share will be lost from the copyright holder to other record companies when copyright expires. Given such uncertainty and lack of empirical evidence, we prepared our calculations as a range, assuming either 0% loss of market share or 100% loss of market share.

Figure 1 shows the mid-point – the impact of a 50% loss – looking at repertoire set to fall out of copyright over the next ten years. This demonstrates the impact on record company

2 “Sonny Bono Copyright Term Extension Act”, One Hundred Fifth Congress of the United States of America, 27 January 1998.

3 PPL is a music industry organisation collecting and distributing airplay and public performance royalties in the UK for record companies and performers.

4 PPL, “Gowers review of intellectual property – PPL response”, 2006.

5 Although it should be noted that the extent of copyright laws differ from country to country – for instance UK copyright legislation covers performers’ rights but the US does not.

6 “Blair sings along to Cliff’s summer holiday”, The Sunday Times, 30 July 2006.

7 Liebowitz (2006), “What are the consequences of the European Union extending copyright length for sound recordings?”, Paper prepared for the IFPI, February 2006.

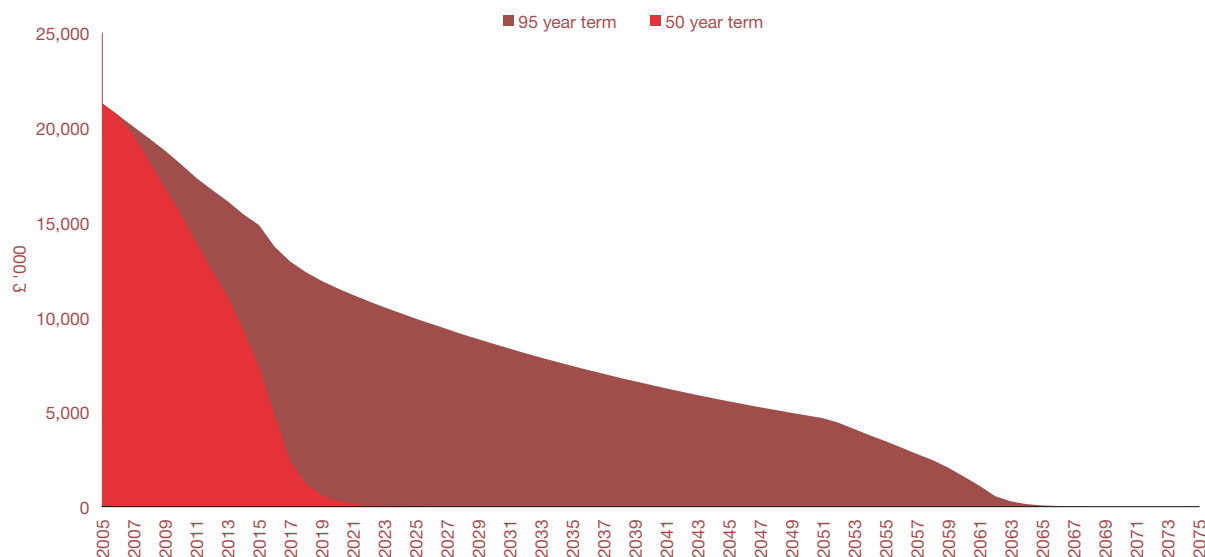
8 Sir Cliff Richard (2004), Submission to the European Commission on Working Paper SEC (2004) 995, July 2004.

9 <http://www.wired.com/news/digiwood/0,1412,67783,00.html>

10 Akerlof et al. (2003), “Copyright Term Extension Act of 1998: An economic analysis”, May 2003.

11 Open Rights Group, March 2006.

Figure 1: Impact on record company revenues from 1956 to 1965 recordings, based on a 45 year increase in term (assumes 50% loss in market share)



revenues from music sales of recordings from the 1956 to 1965 period if the term was increased to match the 95-year term applied to US-originated recordings.

And what of other revenues? If the copyright term were on a par with the US, over the next 10 years the maximum (i.e. assuming 100% loss in market share) potential impact on all sources of income to copyright holders in the UK recorded music industry would amount to £82 million (nominal) revenues. But, because we are looking into the future, we need to consider the numbers in today's money (present value terms), giving a maximum of £35 million (i.e. if you put £35 million into the bank today, you would expect to accumulate interest such that, over 10 years, the value of your deposit would grow to a total of £82 million in nominal terms).

Over the next 50 years the maximum additional revenue increases to £3.3 billion in nominal terms, equivalent to £163 million in today's money.

“All Shook Up”

A study by US economists¹² demonstrated that changes in copyright can affect share prices. We conducted an “event study” to test if there was a share price impact when the CTEA was passed in the US. The reasoning behind this is that if there is value in holding these copyrights, then extension of the copyright term is valuable to record companies and hence should be reflected in an increase in the share price.

Conducting an event study of this kind requires overcoming some difficulties. We needed to:

- Isolate the specific effect of the extension from all other factors that impact share prices, particularly given that at the time of Sonny Bono, most of the major record companies were part of much larger media businesses. Any impact might have been dwarfed by events in the rest of the business; and
- Identify when the market reacted to the news of a copyright term extension events. Markets react to “news”.

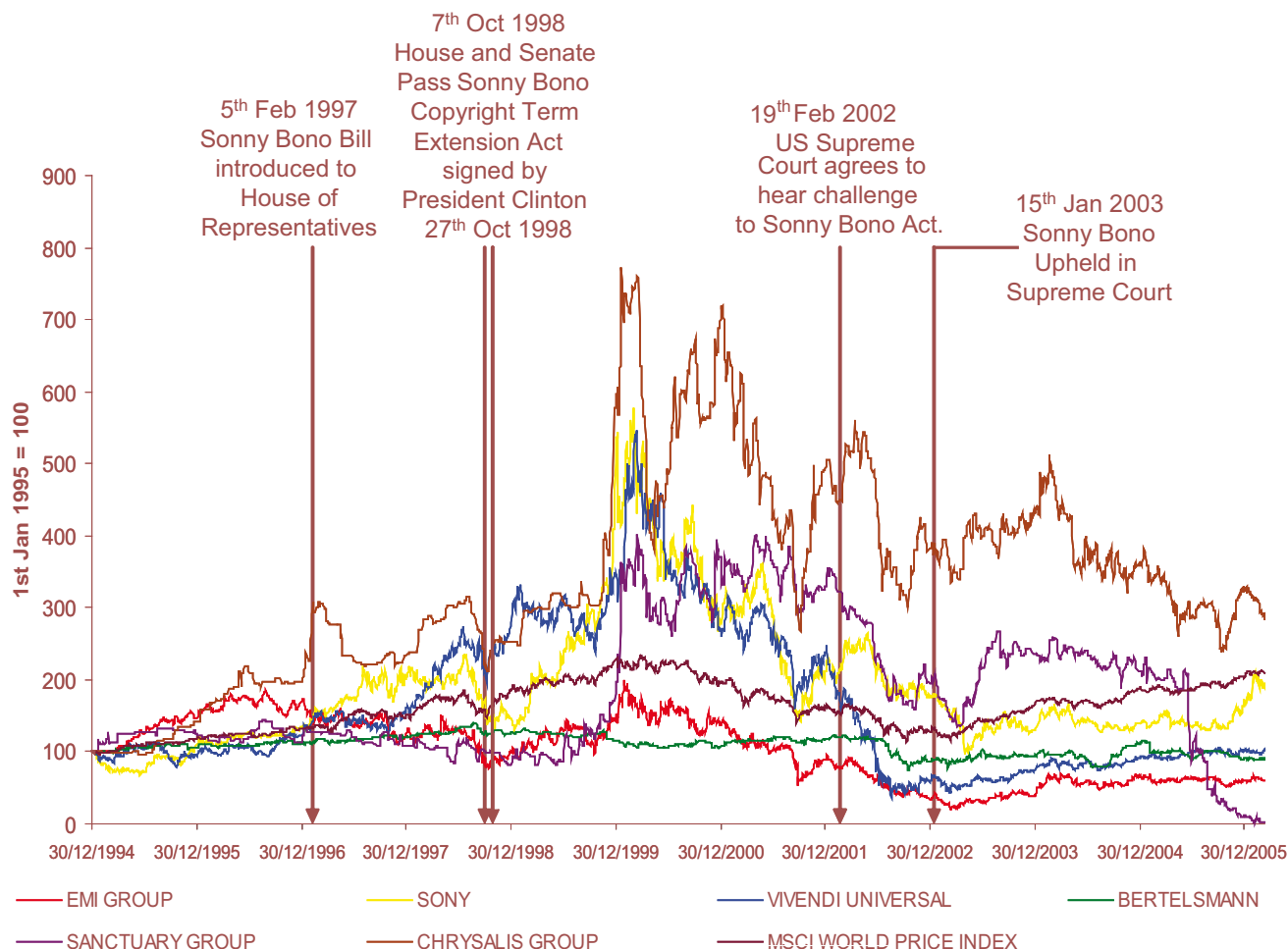
We addressed the first problem by using econometric techniques that effectively allow for some random movement due to factors other than copyright extension.

However, the second problem is a task that cannot be addressed by econometric techniques alone. Would the market react when the Act was first tabled? When it was passed by the House of Representatives or by the Senate? When it was signed by President Clinton? Or, was it before all of these events as expectations grew that such an Act would be passed (previous attempts had been made)? Or could it be that no single event will demonstrate the shift in perceived value of recording companies and that actually there was a gradual increase in perceived value as favourable legislation change seemed likely. Alternatively, might we see a decline in share prices when the Act was subjected to challenge at the Supreme Court, and then a commensurate increase when the challenge failed?

We first looked at the data on record companies over the relevant time period, as shown in Figure 2. Visual analysis suggested that any effects may be relatively small but there does seem to be a possible boost to some companies' share prices upon passing of the CTEA in October 1998.

12 Baker, M. and Cunningham, B., “Court Decisions and Equity Markets: Estimating the Value of Copyright Protection”, United States Naval Academy, Mar 2004.

Figure 2: Share price impacts of key events in the development of the Sonny Bono Act



We focused on the key dates shown and performed regression analysis to determine whether there was significant change in the direction predicted by the hypothesis that longer copyright increases value, using a variety of lags and data frequencies, relative to the market movement. While the regression analysis did not produce strongly supportive results, there were enough instances where share prices did move significantly, relative to the market movement, in the direction predicted, to indicate that we could not rule out an effect of copyright term extension on share prices.

“Ain’t No Change”

The opponents of copyright extension argue that record companies will charge higher prices to consumers for recordings if they remain in copyright, and hence increasing the term would result in these “higher” prices persisting for longer.

In order to test this proposition, we carried out a survey with a sample of over 220 retail prices of just-in-copyright and just-out-of-copyright popular and jazz recordings in the UK.

We also obtained the dealer prices for these recordings from BPI in order to test whether copyright extension might put a squeeze on retailers’ profits.

We found no statistically significant difference between the prices of in-copyright recordings and out-of-copyright

recordings for any of our samples. While those against a copyright term extension state that prices will be higher, our survey did not support this argument. That said, our survey is based on the situation now, when there are relatively few big-selling recordings out of copyright. This could change when some of the popular recordings fall out of copyright.

“I still haven’t found what I’m looking for”

Opponents of copyright extension also argue that it will reduce the availability of back catalogues: the argument goes that record companies have no interest in issuing much of their back catalogues, and are only interested in issuing the small proportion that they know will sell well. Conversely, when recordings fall out of copyright, other parties make these recordings available to the public. Is this really the case?

One key issue is incentives. The longer the remaining term of copyright, the more willing copyright holders will be to invest in making recordings available. Why would other record companies be interested in making an out-of-copyright recording available if the incumbent record company was not willing to do so when a substantial length of copyright remained on that recording?

We uncovered relatively little empirical evidence to support or refute the availability argument. In particular it is unclear whether record companies are currently failing to make large numbers of recordings available, and if so, whether third parties would be any more likely to do so if the recordings fall out of copyright:

Support copyright extension	Oppose copyright extension
Some record companies appear to be making a significant effort to make recordings available on the internet, for instance Warner has unveiled a download service comprising all Universal's classical and jazz releases, amounting to 125,000 tracks. The lower costs of making recordings available online rather than on compact disc appear to be encouraging incumbent record companies to invest in re-releasing their back catalogues.	Brooks, 2005, "Survey of Reissues of US recordings" ¹³ suggests that more recordings are released by third parties than by copyright holders. This could imply that, for some reason, copyright holders are currently unwilling to make available some recordings that third parties might do if they were out of copyright.

While it is unclear exactly how increased copyright term would affect availability, what is clear is that an extended copyright term increases the incentive for incumbent record companies to make recordings available.

“The Winner Takes It All”

To summarise:

- We estimated the maximum possible financial impact of copyright term extension to UK copyright holders at £34.9 million over the next ten years and £162.8m over the next fifty
- Our “event study” analysis, while not providing the definitive answer, could not rule out that a copyright term extension could impact share prices of record companies

So, copyright extension means more money for record companies and performers, and potentially more value for shareholders and/or more re-investment into the industry.

Also:

- Our survey of prices supports refutation of the main counterargument to copyright extension – we could not identify a statistically significant difference between the prices of in-copyright and out-of-copyright recordings
- The possible effects of copyright extension on the availability of older and more obscure recordings remain unclear and deserve further investigation

“Same As It Ever Was”

Andrew Gowers reported on his findings in December 2006. His recommendation was that the length of copyright protection on sound recordings and performers' rights should be retained at 50 years.

In reaching his conclusion Andrew Gowers took on board some of the results of PwC's study and made use of our benefits estimates for record companies and performers. He also commissioned a study by the Centre for Intellectual Property and Information Law, Cambridge University, who based their analysis on PwC's numerical findings.

Based on these two studies he concluded that increasing copyright term would result in a net loss in welfare of some £155 million in present value terms. His view was that the benefits we estimated would be outweighed by increased costs to consumers and to society as a whole (deadweight loss to use the economist's jargon).

An increase in deadweight loss assumes an increase in prices, but our pricing survey found no evidence that in-copyright works are significantly more expensive than out-of-copyright works. It is possible, however, that any increased costs from copyright extension could be passed on to consumers more generally (i.e. prices of in-copyright and out-of-copyright recordings could both rise marginally).

The next stage of the debate is in Europe. Shaun Woodward, the minister for creative industries and tourism, hinted that the door to copyright extension has not slammed completely shut:

“You can't fail to be impressed by the strength of the argument which has been made by the music industry, but that is a debate which needs to be conducted at a European level... If the consensus in Europe were to change - if the EU were to say, in six to nine months' time, due to overwhelming pressure from member state countries, that it should change the current position on this - and if the consensus in the British industry was that there should be change, then there would be one.”¹⁴

No doubt the debates will continue. Watch this space.

¹³ Brooks, T., "Survey of Reissues of US recordings", Council on Library and Information Resources and Library of Congress, August 2005.

¹⁴ Music Week, "MP urges Euro assault", 3 February 2007.

Specific services

Specific services related to this article include:

- Impact assessments of policy changes
- Evidence-based submissions to Government, regulators and competition authorities
- Commercial and accounting valuations
- Event studies (e.g. in the context of litigation)
- Price and cost benchmarking (e.g. to inform pricing strategy)

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