Written evidence submitted by Patreon, Inc

Patreon, Inc. response to Inquiry on the Economics of Music Streaming

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Patreon is grateful for the opportunity to submit evidence on the economics of music streaming. Patreon is a membership platform that makes it much easier for creators and artists to earn income. The platform, which was started in 2013 by musician and video creator Jack Conte and his college roommate Sam Yam, has become a top income-generating solution for over 200,000 creators. To date creators have earned over £1.5 billion pounds ($2 billion US dollars) through Patreon's subscription-style payment model. Within this evidentiary submission, we will focus on what we know best: the impact of music streaming on artists, both independent and those signed to major labels. We will also point to some promising alternative business models, such as direct-to-fan distribution, membership for artists, and alternatives to the traditional record label, such as label services companies, independent distributors, and block chain monetization. And above all we will appeal to your moral compass to persuade you to the point of view that the people who create a thing as irreplaceable and nourishing to our humanity as music (the artists) ought to be the main beneficiaries of its exploitation.

We are very familiar with the stories of the thousands of musicians who now use Patreon to connect directly with their fan base, build strong communities, and fund their art. Patreon’s CEO and co-founder, Jack Conte, is an independent musician who personally experienced the impacts of the changes in the music industry that coincided with the rise of music streaming platforms. Back in 2013, Jack’s band went from earning $58k/year of iTunes download revenue, to a mere $6k/year of streaming revenue. His story is just one among the global community of artists, including those in the UK, who experienced something similar. That doesn’t mean that streaming companies are the *cause* of that decline in revenue. It may have happened anyway due to the rise of rampant music piracy and the way it trained listeners that music should be free.

Now, however music streaming is the dominant way most people on the planet listen to music, with major streaming companies capturing about 50% of all music industry revenue. It’s important to examine the impact of their business models on the artists that create the music they deliver. It is even more critical that we address this matter now as COVID-19 has decimated musicians’ dominant source of income: live performances. BPI has reported that UK record label incomes have been growing steadily over the past 3 years due to a surge in music streaming revenue, but artists are raising the alarm about their incomes dwindling to dangerously low levels. What is behind this disparity?

Music streaming and its impact on artists
Independent artists have experienced particularly severe impacts as the music industry turned to digital distribution models such as streaming. Music listeners have been taught to expect music to appear on streaming services like Spotify or Apple Music, which generate a small fraction of the revenue for artists than what they previously earned from physical album sales. Record sales could previously provide revenue in a way that streaming simply cannot match because of the volume of streams required to level up with someone actually buying a physical album / digital download.

Streaming services typically pay music labels around 52 percent of the revenue generated by their subscription and advertising businesses. The label then pays the artist a royalty of anywhere from 20% to 50% of the original 52%. So the artist ends up with the smallest piece of the pie. Is that a fair deal? And if it isn't, who should right this wrong - the record labels, or the streaming companies?

In a recent interview we published with independent musician André Anjos, the producer behind the electronic-pop pseudonym, RAC, he revealed that although his album, Strangers, is a success both with listeners and critics (Spin magazine named it one of 2014's best pop albums, and on Spotify alone, its two lead singles — "Let Go" and "Cheap Sunglasses" — have 44 million streams combined), he won't be able to earn any money from the millions of streams. This is due to the structure of record label contracts, *and* a side effect of the low per stream payouts of streaming companies. In a deal he signed with a record label, André was given an advance of $350,000 upfront from which he had to pay for the recording of the album, marketing and other expenses of releasing an album, and living expenses for the duration of the process. Once the album was released, all the royalties went to the record label until that advance was paid back. And even with millions of streams of those songs, he still hasn't earned enough to pay back that original advance.

Some have said we should consider streaming services to be the equivalent of songs being played on the radio. Radio is free, but there are commercials. And it was a great way to discover new music when by chance you heard a new song you liked, and then you wanted to buy the album. But now, there is no album to buy, and no incentive to further compensate the artist. The listener can simply put that song on repeat and listen to it as many times as they like with no further transaction. The song may get more streams, but those only pay a fraction of a penny and don't add up to much for the vast majority of artists.

Alternative and more equitable business models
So if the current system isn't fairly compensating artists, are there better alternatives? We believe there are many. Regarding streaming companies, one way to make their business model more fair to artists is a new payment structure that ensures that a share of each individual user's money goes to the artists they actually listen to, rather than being pooled together with all subscription revenue. Under the current model music streaming services like Spotify acquire two classes of licenses for the music they host: Sound Recording License agreements or "master" recordings, which cover the rights to a particular recording, and Musical

Composition License Agreements, which cover the rights of the composer or songwriter.

When it comes to the master rightsholders, both ad revenue and subscription revenue generated by the streaming service is pooled, and - minus the services' cut which is typically 30% - that revenue is then divided and paid out by market share between the major labels, collective independent rightsholder Merlin, and a number of other rightsholders and distributors all with their own, separate deal structures. The market share is determined by the total number of monetized plays generated across all owned accounts, claimed by or belonging to each rightsholder. So for any individual subscriber, their money is pooled and paid out according to what is popular on the service, not according to the artists they listened to.

It's worth noting that for the vast majority of consumers, their entry into streaming music is through the most popular platform-curated playlists, comprised of tracks which are primarily owned by major rightsholders whose leverage allows them preferred placement on said playlists. This in turn generates more streams for the largest chosen artists owned by major rightsholders and means that a large portion of ad and subscription revenue is funneled straight to a small subset of rightsholders at the top.

In comparison, in a user centric model an individual's subscription fee, or the ad revenue generated by the tracks they listen to, would only be distributed to the master rightsholders of the songs they've streamed - rather than split across all tracks and artists on the platform and based on overall streams. KT Tunstall, a Scottish artist who spoke in support of this model as part of the Broken Record campaign, said, "Besides giving the consumer a direct relationship to their favorite artists, it's also moral rights. This has many other benefits. Niche music, regional tastes, classical and jazz all start to see money. More money stays in regional and national economies, and smaller artists finally have a chance at funding… The economics and culture of streaming needs to change and put music makers, and significantly, music lovers, at its heart."

An additional model that we believe is more equitable for artists is direct-to-fan distribution through platforms like Bandcamp. Artists and labels use Bandcamp to directly upload tracks and offer them for sale at prices and terms they control. Listeners can buy tracks and then may download and stream them on Bancamp's app and website as many times as they like. While artists set their own prices, fans can choose to pay extra or buy merchandise as an additional means to support artists they love. Bandcamp does not charge for uploading music, and takes a 15% share of revenue from any sales made on their website. Their fee goes down to 10% after an artist has sold at least $5,000 USD.

As artists search for ways to create on their own terms and find fairer models, new services and models have sprung up that allow a more DIY approach that gives them more control, and more potential upside, on their own creative output. For example, there are label services companies which, in contrast with traditional record labels, provide many of the services that labels tend to provide, such as marketing, promotion, and tour management, but do not ask to own the rights of the music. This allows artists to choose the services they want and need, maintain control of their music and their careers, and capture more of the revenue from their creative output. This is a far more equitable model. And for forward thinking and entrepreneurial artists, there are platforms like Zora that allow artists to leverage the block chain to tokenize their creations and profit from their appreciation on the secondary market. André Anjos, RAC, released a limited edition cassette tape of his new album, Boy, with only 100 available copies. Copies can be bought and sold in Zora's block chain marketplace, and artists can reel in additional profits if their products are in high market demand. Zora charges a 1% trading fee on the consumer side and keeps up to 10% of generated revenues.

Another promising business model that can be part of the solution is membership for artists through platforms like Patreon, which facilitate direct connection and funding between artist and fan. An artist's fans can pay a monthly or annual subscription to Patreon in exchange for access to exclusive content and a behind-the-scenes look at the creative process which fosters a deeper connection. In this way fans can financially support content of the artists they are passionate about, and artists can develop deeper ties with fans and retain full ownership of their creative process. Thousands of musicians in the UK earn a full time living through membership on Patreon and other platforms, and we believe this is a very equitable model where the artist is fairly compensated for what they contribute to the world. For example, Patreon's fee structure is that we take a small percentage of the revenue that artists earn from membership subscriptions, just 5 to 12% depending on which services the artist chooses. Patreon believes the artist should own the relationship with their fans, not tech platforms, so we give artists full access to patron data such as email addresses. Total revenue generated for musicians on Patreon and the number who make over £750/mo on the platform has more than doubled since Oct 2019, a promising sign that membership can be part of the solution for artists.

We believe that in today's market, artists can no longer rely on a single revenue stream such as album sales, merch sales, or streaming, and due to COVID touring has been eliminated as a revenue source for the foreseeable future. Artists must become more informed business people in order to protect themselves, diversify revenue streams, and forge their own path. We are inspired by the example of young artists like Lisa Vitale of the band Terror Jr. They were signed to a major label early on, and then learned that they could do for themselves much of what the record label was doing, and without signing away the rights to their music. Now Lisa manages the band herself, and employs the help of a label services company that handles some aspects of promotion, distribution, rights management, etc. for a fair fee without requiring to own any rights to the music.

In conclusion, we believe that the current music streaming model does not adequately compensate artists for the value they give the world. But there is not one simple fix. We must examine the unfair payout model of music streaming companies, but also recognize the role that music labels play in perpetuating that system. The user centric model can be part of the solution here. In addition, artists need other revenue streams and business structures that give them more control over their careers and ownership of their creative output. Creativity is an essential talent that drives the largest industries on the planet and generates trillions of dollars in economic activity. The artists themselves deserve a greater share.

We appreciate the Committee's inquiry into the economics of music streaming. Patreon believes that guided by the right policy environment, creators in the United Kingdom could benefit immensely from expanded economic models, and concepts that allow for a greater recoupment of income from streaming. At the Committee's request we are willing to provide additional background, information, and insights into this matter in the future.