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ECADonomics

Understanding Brazil's unique model of collective rights management

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The past five years have seen much high-level talk about collective rights management, cross border licensing and the apparent need for a global repertoire database. Interestingly much of this has been held at the continental level of the European Commission; yet one of the key drivers for the need for reform is global in both nature and namesake – the World Wide Web. Awareness of existing models of collective rights management from around the world can help inform the current debates; hence the need to understand the unique model that currently operates in Brazil.

ECAD is Brazil's central bureau for the collection and distribution of both authors' and neighbouring rights, and this unique model allows for domestic competition to take place amongst ten membership societies. Put more bluntly, one body (as opposed to two or more) gets the money in and sends the money out for both sets of rights. The purpose of this paper is not to propose nor endorse the Brazilian model, but simply to get to grips with its economic structure and properties in order to enlighten the current debates about collective licensing at home and abroad.

Why Brazil?

In most countries, authors' rights and the neighbouring rights in sound recordings are collected by separate societies, each a 'domestic monopoly' in their own field. This often leads to criticism of duplication in the back office function of collection and distribution of royalties, as well as confusion over who should be paid what amount. The USA is an extreme case on two fronts in that it has had competition for authors' rights for the best part of a century, whilst it has a fledgling collective rights management organisation for neighbouring rights in the form of Sound Exchange.

Brazil is different in that it has one body that collects and distributes royalties for both sets of rights, with competition then taking place for royalty distributions, and therefore voting rights, amongst ten domestic 'membership societies'. Brazil therefore, is an exception to the rule in that it avoids much of the duplication of rights administration (i.e. documentation and distribution), and prevents the confusion of who the rights' users need to pay to use music legally. This functional separation provides us with an interesting case study in market structure in the unconventional market of musical copyright.

Underneath the umbrella of ECAD

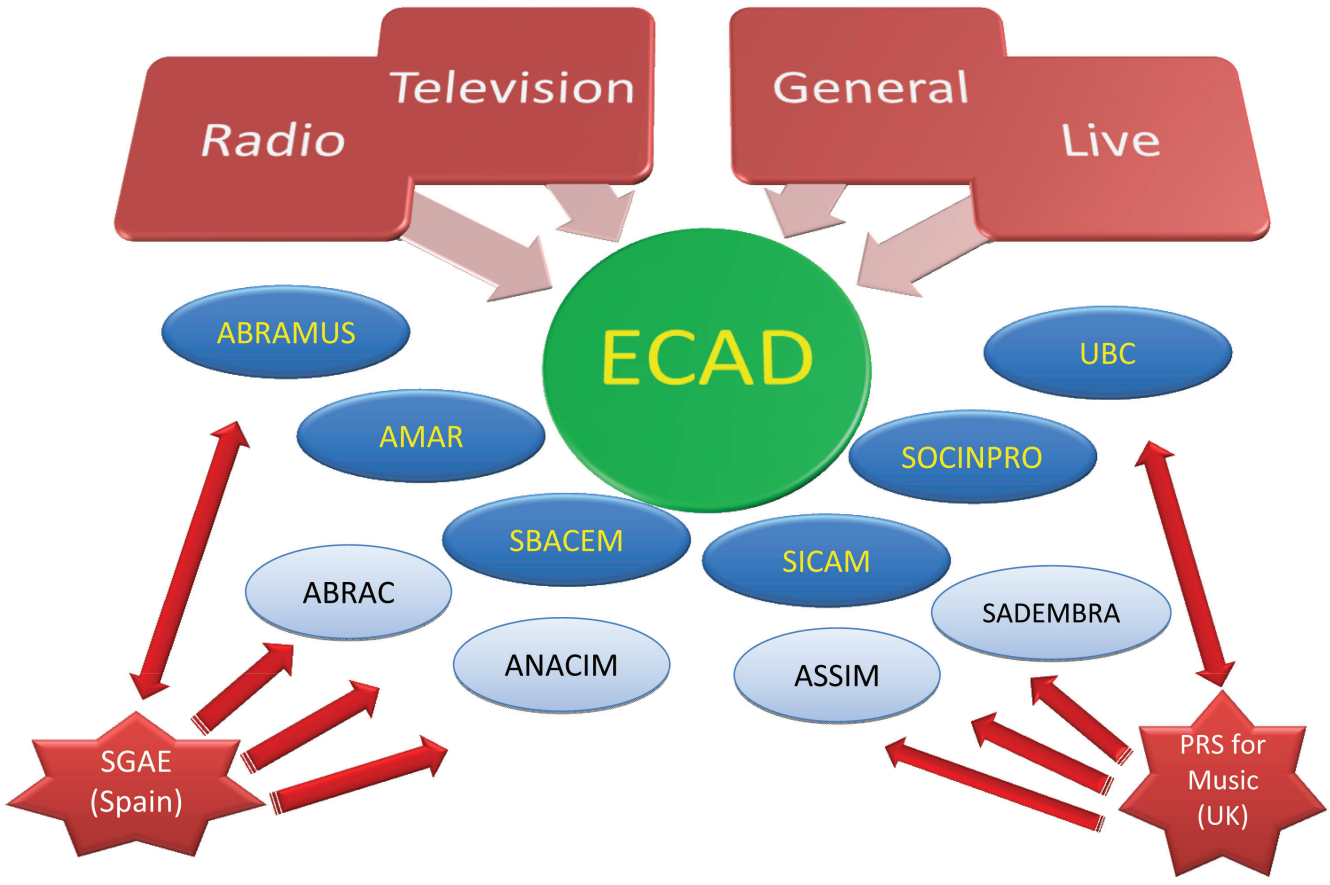
ECAD's story began as a result of the government and cultural elite seeing their market for licensing authors' rights dissolve into an 'anti-commons', where too much fragmentation leads to underuse of an economic good. An anti-commons leads to market 'gridlock'; a term coined by the author Michael Heller in his book *The Gridlock Economy*. He argued that when gridlock happens, the action of 'patent pooling' provides a rational response as it helps keep transaction costs down, prevents further fragmentation and solves coordination. As will be explored later, the design of ECAD

PRS for Music represents 75,000 songwriters, composers and music publishers in the UK and protects the rights of international songwriters through over 100 arrangements with international bodies.

subscribes to these three properties of patent pooling, or collective licensing, however it's important to bear in mind the historical importance of government intervention which allowed it to come into being in the first place.

Until 1973, disparate authors' societies attempted to collect separately from users for their members' rights. The confusion this caused was a convenient excuse for users to delay or refuse payment. Brazil's first law specifically on authors' rights was passed later that year, creating the supervisory National Council of Authors' Rights and ECAD, the Central Office for the Collection and Distribution of Rights. The National Council was dissolved in 1990, and in 1998 a new law was passed accepting the principle of 'free association' with any authors' rights society, proscribing government interference in such societies, and confirming the status of ECAD.

ECAD is best viewed as an umbrella organisation; it collects royalties for performing and neighbouring rights and allocates them among its six full-member societies – ABRAMUS, AMAR, SBACEM, SICAM, SOCINPRO and UBC – and its four associate members – ABRAC, ANACIM, ASSIM and SADEMBRA – which then forward them on to their members. It is worth noting at this early stage that mechanical 'reproduction' rights do not flow through ECAD; rather they are licensed by publishers and labels directly. The chart below illustrates how the ECAD model works.



The Brazilian Way: The chart shows how the ECAD model works. Umbrella rights organisation ECAD collects royalties for performing and neighbouring rights and distributes them to its six full-member societies (dark blue) and its four associate members (light blue) which then pass them on to their members. ECAD does not have direct links with overseas collecting societies. Most international societies have a reciprocal agreement with one of the Brazilian societies, and unilateral agreements with the others to ensure that the smaller Brazilian societies' members' rights are represented abroad. ECAD is unable to receive money which it has not licensed itself.

ECAD entry rules

Any new society may apply for membership of ECAD. There are certain rules establishing the official relationship between the central body and the individual societies, which can be found in ECAD's statutes. The societies are admitted to one of two levels of membership: full members have a seat on ECAD's General Assembly. Associate members have to collect through ECAD, but have no voting rights. The number of votes each society has is in proportion to its total income. Decisions regarding distribution or collection matters (eg: changes in the rules) require a simple majority. Changes to the statutes require a 2/3 majority. It is theoretically possible for a society to fall back to 'Associate' membership level, but this is not usual.

When a rights holder affiliates with a Brazilian society, the administration of their rights are simply mandated to that society. Writers usually assign both their mechanical and performing rights to their publishers, with the performing right share being paid via the society network. Any mechanical licences are therefore negotiated between the record company and the publisher, although some societies do administer mechanical rights too, albeit on a small scale.

ECAD is not allowed to represent authors and composers, nor foreign societies, directly, as this function is devolved to the membership societies which compete with each other for members by using their expertise and intelligence, and by investing in quality and excellence of services. In terms of operational costs, ECAD deducts a fixed 17% from its collections to cover costs. A further 7.5% of gross is retained by the societies for their own costs.

Dealing with data

The ownership of ECAD means that the individual membership societies are responsible for membership, documentation, membership services and international relations. Certain societies, especially the larger ones, may process the distribution to refine it for the benefit of its members. Both ECAD and the societies have to invest in the development of IT systems and data management. ECAD uses the administration fee for this purpose, although the general budget and strategic plan for each year is approved by the General Assembly of the societies.

ECAD and the individual societies have developed the centralised works database. This is unique inasmuch as it contains both the ISWC [1] details of the original 'creators' of the work (writers, composers and publishers) and also the details of any recordings of the work which have been made (ISRC [2]). This enables ECAD to easily and accurately match each use of a song to the correct performing and neighbouring right holders. Societies are responsible for providing details of their members' works to the database. Despite its centralised nature, ECAD may not amend or edit data which has been entered by the societies. One of the most intuitively obvious merits of this approach is that, by managing both ISWC and ISRC together, this functional model prevents duplication of economic resources (time, labour and money), whilst allowing for further coordination in developing data solutions.

Money in centrally, money out democratically

ECAD licenses rights users in the same way as any other collecting society does with their main sources of income being radio and TV broadcasters, live events and 'general users' (shops, restaurants, hotels, cinemas etc.). Concerts and other live events are licensed purely for the author's right; other uses of music are licensed jointly for author's and neighbouring rights, as there is invariably a sound recording used. All royalties collected – except from live performance – are split as to 2/3 to authors' rights and 1/3 to neighbouring rights. Tariffs and licence fees are negotiated by ECAD directly with the users, ensuring that market rates are applied. However, the absence of a specialised copyright tribunal in Brazil can make the tariff setting exercise difficult and time consuming.

A summary of the five main areas of licensing activity by ECAD is offered below:

- **Radio** stations licensed by ECAD are mostly affiliated to ABERT, a broadcasters' association which gives collective bargaining power to the rights user.
- **Television** is split into 'open' (ie: terrestrial 'free-to-air') and subscription TV; and accounts for around a quarter of ECAD's collections. Recent court cases have recognised the right of the copyright owner to set a de facto tariff of 2.5% for the use of their works [3].
- **Cinema** collections have grown considerably in the last decade as ECAD has got to grips with licensing. Most Latin American countries follow the US exemption whereas ECAD has endorsed the European laws by recognising this performing right in cinema.
- **Live performance** is the one area where ECAD's collections are purely for author's rights. As no sound recording rights are involved, the original creators (writers and publishers) of the works performed are the sole beneficiaries of ECAD's highest tariff.
- **Digital** is licensed by labels and publishers directly to Digital Service Providers whilst some unpublished works are licensed by individual societies; the public performance of works and recordings is therefore limited to webcasting and simulcasting.

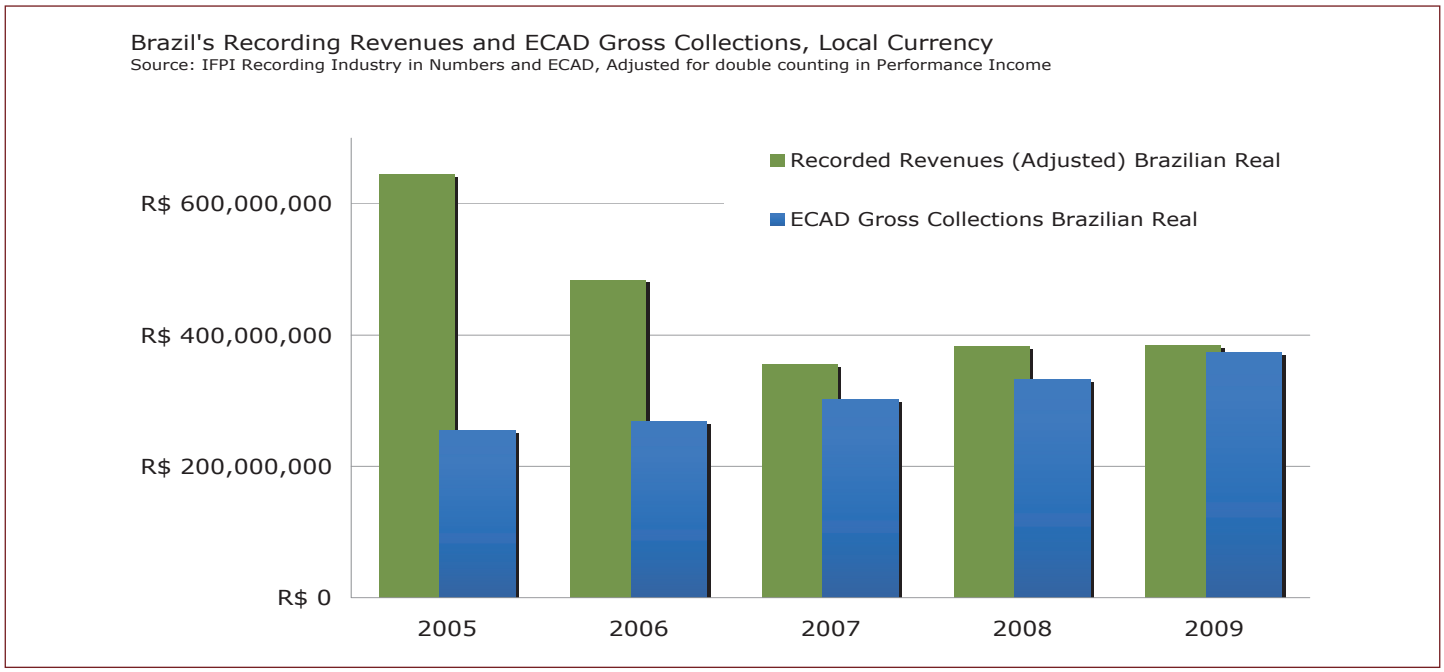
How has ECAD performed, financially?

The financial performance of ECAD has been impressive, with collections growing by at least 10% year on year since 2006, totalling BRL374m in 2009. This is in stark contrast to the steep decline in recorded music revenues over the same period. In addition to growth of established revenue sources, ECAD has focused on increasing the number of 'general' licensees – bars, restaurants, academies, commercial halls and stores. In 2008 it launched Mobile ECAD Tec, a technology designed to speed up licence requests, and the ECAD Tec Sound, which automates identification of musical works. Productivity has also risen, as distributions increased by over 17% between 2008 and 2009, outstripping the 12.6% rise in collections over the same period.

The chart overleaf illustrates a 'changing of the guard' by plotting recorded revenues and ECAD collections in the local currency of Brazilian Real. Whereas ECAD collections have grown by 47% between 2005 and 2009, recorded music revenues (excluding performance right income) have fallen by 40% over the same time period. To translate this point, converting these numbers into US dollars and adjusting for double counting of performance rights has the two revenue streams at neck-and-neck at around USD $200m for 2009. Going forward, whilst Brazilian recorded revenues would appear to have bottomed out and are now edging northwards, ECAD gross collections are expected to continue to show double digit growth for 2010 and beyond. These contrasting stories need to be interpreted carefully, as piracy will have had a dramatic effect on consumer facing recorded revenues whilst business-to-business licence environment which ECAD collects from will be more insulated.

[1] International standard musical work code;
[2] International standard recording code;

[3] The socio-economic structure of Brazilian society means that 'pay TV' is still something of a luxury for many people. TV Globo – the third largest commercial television network in the world – is a hugely important presence in Brazilian society.



Getting to grips with competition

Now we have got under the umbrella of the unique ECAD model of collective rights management, we turn to how competition arises under this market structure. As any regulator should know, there are good and bad forms of competition and the notorious 'waterbed effect' can mean that pushing down with an intervention in one part of the market can cause economic anomalies to rise up elsewhere. ECAD offers some interesting examples of this, in that much of the competition in Brazil is displaced, with societies competing for players who are outside of ECAD: namely publishers and overseas reciprocal contracts.

Brazil's unilateral and reciprocal representation

Royalties for writers who are members of overseas societies are treated by ECAD in exactly the same way as those for Brazilian writers. At distribution international royalties are passed to the Brazilian membership society with which the overseas society has a reciprocal agreement. This system works as follows: a collecting society – eg: *PRS for Music* – agrees to collect its Brazilian royalties through one of the 10 ECAD member societies – in this case, UBC. This means that all PRS members' royalties are paid by ECAD to UBC, and then passed on (after deduction of commission) to *PRS for Music* in London.

However, when royalties are collected in Britain by PRS for writers of Brazilian works, the system is a bit more complicated: not all Brazilian writers are members of UBC. So, PRS has unilateral agreements with most of the other membership societies in Brazil, to ensure that their writer members are paid for the use of their works in the UK. These unilateral agreements mean that PRS collects for – and pays royalties to – the members of ABRAMUS, ASSIM, SOCINPRO, UBC etc., but that only UBC passes Brazilian royalties on to London.

Competing for those contracts

At the domestic level, competition is fostered through increasing levels of expertise, intelligence, investing in quality and excellence of services. Domestic competition for members is one of the most striking aspects of the ECAD model; however competition for publisher catalogues and international reciprocal contracts is perhaps even more important with regards to revenue and therefore voting power.

PRS for Music, for example, has a long-standing successful reciprocal relationship with UBC. If another Brazilian society were to acquire its repertoire (ie: if UBC were to lose it) that would mean that the new society's number of votes would increase within the ECAD general assembly. Similarly, UBC's votes – and income – would be reduced.

Another important factor to boost votes and influence is, of course, publisher members. Although the author may assign all his rights to a publisher, it remains for the author to determine which society his share of performing rights will flow through. Publishers are akin to 'super members' in this competition for distribution, as their 'weight' is derived from the net publisher share which is generally represented by one society. As a result, one good major publisher can be worth several large overseas collecting societies. Similarly, for those societies which represent neighbouring rights holders, the presence of a major record company on your books can also healthily increase your income and – crucially – your voting rights.

Providing services to members, therefore, can mean not only keeping writers happy, but also attending to the often conflicting demands of publishers, record companies and overseas societies. A dominant society within ECAD could attempt, in theory, to amend the distribution rules in favour of neighbouring rights and away from performing rights; the 'balancing act' the societies have to play between its members, however, can help to prevent such 'abuses of power'.

Who should benefit when competition produces economic gains?

When a market produces gains, who should gain? That might be at the discretion of the regulator, especially if it is the intervention of the state which delivered the gains. That could also be at the discretion of the technological advancement, and the creative destruction that it leaves behind. It could also come down to the more conventional 'economic clout', as the actions of one major player can cause others to follow. What follows as an example is a recent case study in the Brazilian 'waterbed effect', where the market structure leads to efficiency gains from within the ECAD, but its member societies chose different strategies to react, with some claiming the gains for themselves and others passing the gain onto their membership.

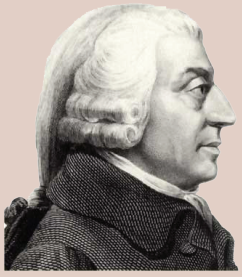
In 2009, the governing board of ECAD were split on what to do with the gains of a reduced administration cost. At stake was one percentage point, or USD $2.2 million, as ECAD were lowering their cost of administration from 18% to 17%. The dispute centred on whether the membership societies should exploit the 'waterbed effect' by raising their deduction by a fraction of that percentage point gain or should the benefit be passed on to the songwriters in its entirety? The outcome of this story was similar to that of the competitive form of collective rights management in the USA. Different membership societies of ECAD communicated different messages to their current and potential members regarding the cost of administration – with some passing the benefit on, and others choosing to withhold it. Competition, in its purest form, is about choice and what is interesting here is that these membership governed organisations were choosing different strategies.

Can the benefits of ECAD be replicated elsewhere?

We can conclude this case study by considering how the lessons learned from the ECAD model can be transferred to other collective rights management scenarios. A central body built on the ECAD model can take on board the 'money in' function and the task of matching that money to the works of artists and writers. A central repository could also function as a works registration and documentation hub and proceed to allocate income through common distribution rules. This could, in theory, pass down advantages and disadvantages to its membership societies. On the plus side, the scale effects could potentially reduce costs whilst allowing member societies to concentrate on servicing their members. The disadvantages for member societies would be in giving up control of their data, ceding their independence in licensing and distribution and - as with any coalition or consortia - continually having to compromise in decision making.

This case study also allows you to re-think some 'what if' scenarios about how things would work back in Brazil, should the rules and structure of the market change. For example, what if ECAD was to be broken up, based on authors' and neighbouring rights and how would this affect the distribution ratios? Furthermore, what if the incentives to pursue legal action were recognised as asymmetric, where small societies can no longer free-ride from larger societies' litigation expenditure? Finally, what if Brazil was to join the US, UK and Sweden as the fourth 'net exporter' of repertoire with more money coming in than is being sent out? What is beyond the scope of this Insight paper is to explore the dynamics of Brazil being a net importer of repertoire, (sending out more money that it brings in), which is striking given how recognised Brazilian music is on a world stage. This is a country that names its main serving airport after the late great Antonio Carlos Jobim after all!

There is another way one can approach the pros and cons of the market structure of collective licensing in Brazil: the division of labour. Put more bluntly, this functional analysis of ECAD suggests there is merit in doing what you're good at, and outsourcing what you're not. Ironically, given the nationality of two of the authors, this case study in ECADONOMICS from Brazil brings us back to Scotland and the founding father of modern economics: the philosopher Adam Smith, who argued that productive labour should be made even more productive by deepening the division of labour. This deepening the division of labour means under competition lower prices and thereby extended markets.



> It is the great multiplication of the productions of all the different arts, in consequence of the division of labour, which occasions, in a well-governed society, that universal opulence which extends itself to the lowest ranks of the people
>
> **Adam Smith, *The Wealth of Nations***