

# New Pandora CEO faces royalty fight with artists

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This undated image provided by Pandora shows the former head of the digital advertising company aQuantive, Brian McAndrews, named as Pandora's new chief executive. After working at General Mills and ABC, McAndrews took small Seattle-based digital advertising agency Avenue A and grew it into aQuantive, the digital ad business that Microsoft bought for \$6 billion in 2007. (AP Photo/Pandora)

One of the biggest challenges facing Brian McAndrews, the new CEO of

Pandora, will be renegotiating the royalty rates the Internet radio giant pays to the music industry.

If Pandora doesn't prevail, the outcome could impede the company's growth and hamper its ability to compete with services such as Apple's iTunes Radio, which launches next week.

For each song Pandora streams to listeners it pays a fraction of a penny to [recording labels](#). The companies begin negotiations before the federal Copyright Royalty Board in January and both sides are already digging their heels in.

Just like past disputes, the haggling could drag on for years while the government plays referee. In the end, users might have to listen to more ads between songs or pay more in [subscription fees](#) to avoid them.

McAndrews, 54, was appointed Pandora's CEO on Wednesday. He told The Associated Press that the royalty fight is "a ways off" and that he'll rely on the counsel of co-founder Tim Westergren and outgoing CEO Joe Kennedy.

"I'm confident we'll be prepared and do the right thing," he said.

"I do share Pandora's longstanding belief that musicians should be fairly compensated for their work," McAndrews said, adding that the existing patchwork of laws was "created piecemeal over decades" and "doesn't serve any one very well."

Pandora allows users to listen to music on computers, smartphones or other Internet-connected devices. It's free as long as listeners put up with a few ads. For each song Pandora streams, it pays the music industry a royalty fee, which in aggregate amounted to over \$200 million last year. The royalty rate is set by the U.S. government.

McAndrews is the former CEO of [digital advertising](#) company aQuantive, which was sold to Microsoft for \$6.3 billion in 2007. Pandora hired McAndrews in an effort to boost the money it makes from advertising.

While McAndrews said he'd focus on boosting ad revenue, [music royalties](#) are Pandora's biggest hurdle to profitability. The fees are the main reason Pandora posted another net loss in the quarter through July, despite revenue rising 55 percent.

Overcoming these costs has proven difficult. In February, Pandora restricted listeners to 40 hours of free mobile listening per month, in an attempt to limit royalty expenses. But it reversed the move in August after listener hours began falling.

Analysts have raised concerns about the bind Pandora is in, too.

"They're kind of stuck in this situation where they can't get to profitability from growing their users. They need to get to profitability from giving their users less content," said Rich Tullo, an analyst with financial services firm Albert Fried & Co. "That's a kind of tough position to be in as a company."

What's different about the upcoming fee negotiations is that Pandora's survival is no longer in doubt.

Since the company debuted on the stock market in the summer of 2011, Pandora has raised the cash to weather major setbacks. The company's stock has jumped 135 percent over the last year. Analysts expect that in the fiscal year through January, Pandora will post its first positive earnings per share since becoming a publicly traded company.

Pandora's revenue, which hit \$427 million last year, is more than 20

times what it made in 2009, the last time it reached a deal with the recording industry.

It now has 72.1 million monthly users, and some 2.5 million people have activated Pandora in their car dashboards. Apple Inc. will launch iTunes Radio in an operating system upgrade next Wednesday. The free service will then be available to hundreds of millions of iPhone and iPad users, and could cut into Pandora's dominance.

Some artists believe they haven't been compensated enough for their contributions to Pandora's success. Many of them want a bigger share of the riches music streaming is generating.

David Lowery, frontman for the alternative rock band Cracker, blogged in June that he could make more from the sale of a single T-shirt than the \$16.89 Pandora paid him for a million plays of the band's 1993 hit "Low" in the final three months of last year.

While he acknowledges he made \$50,000 in royalties last year across all streaming and sales formats, Lowery told The Associated Press his fight is about the future, because services like Pandora are displacing other forms of listening.

"If we don't get the webcasting rights right for songwriters, we're screwed," Lowery said.

Pandora argues that royalty rates are already too high and it has tried numerous tactics to drive them down. In June, it bought a South Dakota radio station to qualify for the lower fees charged to station owners. The company also backed a now-defunct bill in Congress that would have lowered its rates.

Internet-powered music services are becoming more and more important

to the industry. So-called "access models" made up 15 percent of the music industry's \$7.1 billion in revenue last year, up from just 3 percent in 2007, according to the Recording Industry Association of America.

Because Pandora's 2009 deal with record labels and publishers now acts as a benchmark for other companies, including Apple, any fee reductions in a new deal with Pandora would have a ripple effect across the industry.

"That's why everybody in the industry is very exercised about these rates," says RIAA President Cary Sherman.

Pandora pays record labels about \$1,200 for every million song plays. The labels split the payments with performers. The rate goes up \$100 each year through 2015, when the current deal expires.

Pandora pays another \$200 or so per million plays to session musicians, songwriters and publishers.

In all, the payments amounted to more than \$214 million last year, or roughly 50 percent of Pandora's fiscal 2013 revenue.

Pandora has pointed out that, as a percentage of revenue, that's more than the \$300 million paid by Sirius XM, or about 9 percent of revenue, and the \$500 million paid by the entire traditional radio industry, or only 3 percent.

David Oxenford, a copyright attorney who has represented Pandora, says the Copyright Royalty Board's likely first step when hearings start in January will be to give the music industry and Pandora six months to come to a deal on their own.

Pandora is also fighting separate battles in court with the two major

songwriters' societies, Broadcast Music Inc. (BMI), and the American Society of Composers, Authors and Publishers (ASCAP), over songwriting royalties. It's a separate challenge that McAndrews will also have to navigate.

Still, even as they attack Pandora, [music industry](#) executives acknowledge that they share a future with the company.

"We want Pandora to be a raging success," said Paul Williams, president of ASCAP. "But their success should be our success, too."

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