

6 Financial performance of the PRS

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Introduction

6.1. The PRS collects revenue for the performance of its members' works and distributes that revenue to its members. In so doing, the PRS incurs costs which it deducts from the revenue collected. The surplus after deduction of these costs is then allocated across its members, the basis of such allocation being determined by the PRS. This chapter first summarizes the financial performance of the PRS and its business of administering the performing rights of its members. It then reviews the cost allocation methods used by the PRS and how the PRS sets cost recovery rates for its different revenue streams. This is followed by an explanation of the steps the PRS undertakes to distribute its revenue and includes consideration of the timing of and information available on revenue received from overseas societies. Finally, the cross-subsidies which we consider exist within the PRS are examined.

The PRS's results, 1990 to 1994

6.2. The PRS prepares its financial results on a historical cost basis. The results for the last five financial years are summarized in Table 6.1 and are the results of the Society, excluding its then subsidiary, IMRO.¹ IMRO became independent of the PRS with effect from 1 January 1995. Consequently, in Table 6.1, the revenue from the Republic of Ireland is separately disclosed as operations now discontinued.

TABLE 6.1 PRS: summary of results

	<i>£'000</i>				
	<i>1990</i>	<i>1991</i>	<i>1992</i>	<i>1993</i>	<i>1994</i>
Royalty revenue:					
Continuing operations	120,758	126,786	135,616	147,911	158,633
Operations now discontinued	<u>2,539</u>	<u>3,472</u>	<u>4,456</u>	<u>4,909</u>	<u>4,656</u>
	123,297	130,258	140,072	152,820	163,289
Investment income	<u>7,741</u>	<u>6,629</u>	<u>4,949</u>	<u>3,864</u>	<u>3,700</u>
Total income	<u>131,038</u>	<u>136,887</u>	<u>145,021</u>	<u>156,684</u>	<u>166,989</u>
Administration expenses	23,754	26,348	27,794	27,847	28,683
Exceptional item	-	-	4,000	-	-
Total costs	<u>23,754</u>	<u>26,348</u>	<u>31,794</u>	<u>27,847</u>	<u>28,683</u>
Surplus on ordinary activities before tax:					
Continuing operations	104,806	107,141	108,890	124,098	133,879
Operations now discontinued	<u>2,478</u>	<u>3,398</u>	<u>4,337</u>	<u>4,739</u>	<u>4,427</u>
	107,284	110,539	113,227	128,837	138,306
Tax on surplus on ordinary activities	<u>(503)</u>	<u>(73)</u>	<u>(740)</u>	<u>333</u>	<u>750</u>
Surplus before appropriations	106,781	110,466	112,487	129,170	139,056
Amounts appropriated	(523)	(454)	(477)	(324)	(310)
Transfer to/from distributable reserves	<u>(200)</u>	<u>(50)</u>	<u>1,350</u>	<u>(350)</u>	<u>(400)</u>
Net distributable income	<u>106,058</u>	<u>109,962</u>	<u>113,360</u>	<u>128,496</u>	<u>138,346</u>

Source: PRS.

6.3. The revenue collected is disclosed in the PRS's accounts as the PRS's revenue as the Society receives the income from performing rights in its own right and not as an agent for its members. The investment income is income earned by the PRS on the distributable income which has been collected by the PRS and is awaiting distribution to members.

6.4. The exceptional item in 1992 arose from the write-off of previously capitalized PROMS costs relating to systems not in use within the business, following an independent assessment of the viability of PROMS. The PRS has recently reached a settlement with the project managers of PROMS, LBMS, under which the

¹IMRO is incorporated in the Republic of Ireland and, until 31 December 1994, licensed the rights of the Society within the Republic of Ireland. PRS membership in the Republic of Ireland represented some 3 per cent of the total membership of the PRS.

PRS is to receive £2.4 million payable in nine instalments over five years. The PRS intends to account for this income on a receipts basis.

6.5. The Society is subject to UK corporation tax. However, for tax purposes, amounts due from the PRS to members and affiliated societies are treated as a deductible expense. Consequently, PRS distributions are subject to UK tax in the hands of the members. The tax credits in 1993 and 1994 arose as a result of over-provision in respect of prior years.

6.6. Amounts appropriated comprise copyright promotion, donations and awards.

6.7. The income, costs and surplus on ordinary activities before tax set out in Table 6.1 have been adjusted to eliminate the effect of inflation by taking 1990 as the base year and adjusting subsequent years by reference to the annual RPI. The RPI-adjusted figures are set out in Table 6.2. On an RPI-adjusted basis, total income, total costs and surplus on ordinary activities before tax in 1994 compared with 1990 show increases of some 11.6 per cent, 5.7 per cent and 12.9 per cent respectively.

TABLE 6.2 PRS results adjusted for RPI

	£'000					Average annual percentage increase over period %
	1990	1991	1992	1993	1994	
Total income	131,038	129,322	132,126	140,562	146,187	2.8
Total costs	<u>23,754</u>	<u>24,892</u>	<u>28,967</u>	<u>24,982</u>	<u>25,110</u>	1.4
Surplus on ordinary activities before tax	<u>107,284</u>	<u>104,430</u>	<u>103,159</u>	<u>115,580</u>	<u>121,077</u>	3.1
Total costs to total income as a percentage	18.1	19.2	21.9	17.8	17.2	

Source: MMC.

Royalty revenue

6.8. As can be seen from Table 6.1, royalty revenue has increased steadily over the period at an average rate of 7.3 per cent a year. The main sources of royalty revenue are public performance and broadcasting in the UK and overseas royalty revenue. Table 6.3 gives an analysis of royalty revenue from 1990 to 1994 by these three main sources plus royalty income arising in the Republic of Ireland. Royalty income from the Republic of Ireland is shown net of the cost of the Dublin office. All royalty revenue is net of write-offs and provisions for bad debts.

TABLE 6.3 Analysis of royalty revenue

	£'000				
	1990	1991	1992	1993	1994
Public performance	38,428	41,235	43,600	48,411	50,187
Broadcasting	44,339	45,863	48,031	50,687	55,001
Overseas	<u>37,991</u>	<u>39,688</u>	<u>43,985</u>	<u>48,813</u>	<u>53,445</u>
	120,758	126,786	135,616	147,911	158,633
Republic of Ireland (now discontinued)	<u>2,539</u>	<u>3,472</u>	<u>4,456</u>	<u>4,909</u>	<u>4,656</u>
Total	<u>123,297</u>	<u>130,258</u>	<u>140,072</u>	<u>152,820</u>	<u>163,289</u>

Source: PRS.

6.9. The PRS accounts for its royalty income as follows:

- (a) Public performance revenue (or general licence revenue) is accounted for on an invoiced basis except that an adjustment is made to defer the income relating to the following year in respect of unpaid invoices.
- (b) Broadcasting revenue is accounted for on an accruals basis.
- (c) Income from affiliated societies is calculated on an accruals basis.
- (d) Income from agency territories represents amounts received, or confirmed as receivable, which relate to the financial year or earlier, and is shown net of local expenses and taxes.

6.10. There follows a brief consideration of the most significant events which have had an impact on the Society's revenue from 1990 to 1994.

Public performance revenue

6.11. The public performance revenue has increased year-on-year from 1990 to 1994 at an average rate of 6.9 per cent. During this period the PRS has instituted a policy of operating regional offices in preference to a central licensing operation. The PRS told us that, in every case, the regional offices have achieved in their first two years approximately twice the growth rate of licensing income that was previously being achieved when the activity was administered from London. From the autumn of 1989 to April 1994, five regional offices were opened at a rate of one a year.

6.12. The six tariffs which have experienced the most significant changes in invoiced revenue in the period 1990 to 1994 are set out in Table 6.4. To arrive at the revenue included in the annual accounts the invoiced revenue is subject to year-end adjustments such as refund reserves and bad debt reserves. Consequently, invoiced revenue will always be greater than the amount of total revenue shown in the published accounts. The 1990 accounts included a provision of £3.6 million for refund of royalties in respect of tariff JMC, the tariff for members' clubs, following a Copyright Tribunal decision which reduced the tariff rates. We have deducted this provision from the 1990 invoiced figure for tariff JMC to aid comparability with the figures disclosed in the accounts.

TABLE 6.4 Six tariffs with significant changes in invoiced revenue in 1990 to 1994

	£'000					Average annual percentage increase over period %	
	1990	1991	1992	1993	1994	Increase 1990 to 1994	
C-Cinema	1,406	1,337	1,837	1,892	2,371	965	14
JMC-Members' clubs	1,317	2,049	3,775	3,957	3,600	2,283	29
LP-Popular concerts	752*	517*	1,271*	3,805	2,347	1,595	33
P-Public houses	9,356	10,320	9,749	11,736	12,255	2,899	7
RS-Shops and stores	4,057	4,514	4,649	5,337	5,395	1,338	7
SAM-Local authorities	2,205	2,925	3,318	3,185	3,190	985	10
	<u>19,093</u>	<u>21,662</u>	<u>24,599</u>	<u>29,912</u>	<u>29,158</u>	<u>10,065</u>	11
Total invoiced	<u>39,772</u>	<u>43,309</u>	<u>46,017</u>	<u>50,338</u>	<u>51,595</u>	<u>11,823</u>	7
Total per accounts	<u>38,428</u>	<u>41,235</u>	<u>43,600</u>	<u>48,411</u>	<u>50,187</u>	<u>11,759</u>	7

Source: PRS.

*During these years the PRS raised 'manual' invoices for some tariff LP revenue. The amount of revenue invoiced in this way cannot be determined as a full analysis of manual invoices was not given in the Licensing Division's statistical reports.

6.13. The PRS considers that the increase in cinema revenue in 1992 and later years is probably due to a sustained increase in cinema attendance from 1991. In addition, the number of screens licensed increased from 1,220 in 1990 to 1,499 in 1994. The increase in invoiced revenue between 1991 and 1992 was partly a result of one large chain being invoiced in 1992 for 1991 arrears. The continued increase from 1992 is also due in

part to a new tariff C which was negotiated in 1992 and is being phased in over seven years from January 1993.

6.14. The increase in invoiced revenue from members' clubs, particularly in 1992, occurred because the 1991 figure was low due to refunds made as a result of the Copyright Tribunal decision.

6.15. The LP revenue included in Table 6.4 excludes payments by local authorities for live popular concerts as the PRS was unable to provide a five-year analysis. Total invoiced revenue from local authorities is disclosed separately in the table. In 1994 invoiced revenue from local authorities under tariff LP totalled some £668,000. The large increase in tariff LP revenue in 1993 is due partly to the 'manual' invoices being included in the overall invoicing report. In addition, the PRS informed us that over the whole period there was an increase in the number of premises and events licensed under tariff LP. The PRS attributes the fall in 1994 to a dramatic decrease in activity at the top end of the popular live music market during this year, which resulted in the LP revenue falling for the first time in ten years. There were few very large tours at all and only one stadium event-Bon Jovi at Milton Keynes Bowl. Wembley Stadium held no concerts in 1994 compared with eight in 1993 and 12 in 1992-these 20 events were worth £730,000 to the PRS.

6.16. The PRS told us that during the period 1990 to 1994 there was an increase in the number of featured musical events held in public houses (featured musical events include live performances, karaoke and discothèques). The PRS believes it is this change in the nature of public house entertainment which has led to an increase in the use of music by public houses.

6.17. As regards tariff RS, the PRS notes that many small shops have closed down due to the recession. However, the PRS believes the number of larger type stores has increased and, as the tariff is based on the area of the premises from which music can be heard, this has resulted in the overall increase shown in Table 6.4. The PRS notes that there has been no significant increase in the number of times tariff RS has been applied.

6.18. The PRS attributes the increase in tariff SAM, Local Authorities, over the period to the regionalization of licensing activities whereby more resources have been allocated to the administration of these accounts which has resulted in increased and more timely invoicing of local authority accounts.

Broadcasting

6.19. Broadcasting revenue has increased at a slower rate than public performance revenue with an average annual increase of 5.5 per cent. The income from BBC television and radio and from ITV together accounted for some 75.4 per cent of the total UK broadcasting revenue in 1994 and increased over the period at an average rate of 4.6 per cent a year. The increase in the number of independent radio stations has had an impact on the level of broadcasting royalty revenue, although this revenue fell in 1991 and 1992 due to the impact of the recession on the amounts of advertising revenue generated by the radio stations.

Overseas

6.20. Overseas revenue accounts for approximately a third of the PRS's total royalty revenue. This reflects the high use and popularity of UK music overseas. The revenue from affiliated societies and overseas agencies has increased at an average annual rate of 8.9 per cent. As well as increased music usage, the Society also attributes this to two other factors. The first factor is that the PRS has focused on its international relations operations and enhanced the levels of its visits to and liaison with affiliated societies with the aim of identifying and pursuing increased revenues to which PRS members might be entitled. The second factor is the devaluation of the pound when the UK left the ERM in 1992 which overall had an upward effect on the sterling value of the overseas income received. The PRS estimates that approximately 50 per cent of the increase in overseas revenue in 1992 and 1993 was due to exchange rate movements.

6.21. The largest single sources of foreign royalties for the PRS arise from the two major US collecting societies, ASCAP and BMI, four of the European collecting societies (Germany, France, the Netherlands and Italy) and from Japan. In 1994, together these seven societies accounted for 66.1 per cent of income from affiliated societies.

6.22. In most cases, the PRS is a net recipient as regards the overseas societies. In 1994 it received in total £52.4 million from affiliated societies but allocated only £28.0 million to members of those societies. The one exception is the USA; in 1994 the PRS received £12.7 million from the US societies but paid over £21.4 million to them.

Administration costs

6.23. As can be seen from Table 6.1, total administration costs have increased each year throughout 1990 to 1994. In Table 6.5 we show administration costs expressed both as a percentage of total revenue and also as a percentage of total domestic licensing income. The latter percentage is shown as the majority of the PRS's administration costs are incurred in collecting the domestic licensing revenue. On both bases, administration costs as a proportion of income fell in 1993 and 1994 below the level incurred in 1990.

TABLE 6.5 PRS: administration costs compared to total revenue and to domestic licensing revenue

	<i>per cent</i>				
	<i>1990</i>	<i>1991</i>	<i>1992</i>	<i>1993</i>	<i>1994</i>
% of total revenue	18.1	19.2	19.2	17.8	17.2
% of domestic licensing revenue	27.8	29.1	28.9	26.8	26.1

Source: PRS.

6.24. The percentages for 1992 are calculated before taking into account the exceptional costs of £4 million which relate to the writing off of the PROMS expenditure. If the exceptional costs are included, the percentage of administration costs to total revenue is 21.9 per cent and to domestic licensing revenue is 33.1 per cent.

6.25. The PRS Yearbook analyses costs over four categories: personnel, accommodation, operating and other. The largest category of expenditure is personnel costs which in 1994 totalled £18.1 million and accounted for 63.2 per cent of total administration costs. These costs have fallen as a proportion of total costs in the last two years notwithstanding that termination payments in 1994 totalled some £1.0 million (3.4 per cent of administration costs).

6.26. The other main category of expenditure is operating costs which in 1994 totalled £6.7 million and accounted for 23.4 per cent of total administration costs. These costs have risen substantially in 1993 and 1994 compared with 1991 and 1992 levels of £4.9 million. The majority of the increase in 1994 is due to costs provided regarding the MMC inquiry (provision of £0.5 million) and legal expenses incurred of £1.1 million. The legal expenses are principally concerned with three actions: U2 (members of the PRS), Mr R J Abrahams (ex-employee) and LBMS (consultants employed on the PROMS project). Taken together, the termination payments, MMC inquiry costs and legal costs in 1994 total some £2.6 million or 9.1 per cent of total administration costs.

6.27. A meaningful comparison of the level of administration costs incurred by overseas societies with those incurred by the PRS has not proved possible. This is discussed further in Chapter 9.

The PRS's cash flow and investment policy

6.28. Due to the nature of its business, under which it has to distribute virtually the whole of its royalty income to its members, the PRS does not have large amounts of retained distributable reserves building up on its balance sheet. For the last financial year, 1994, the total revenue of the PRS was £167 million, whereas the retained reserves at 31 December 1994 amounted to some £0.8 million. Most of the cash flow comprises net cash inflow from operating activities and amounts paid out to members and affiliated societies. Summarized balance sheets of the PRS for 1990 to 1994 are included in Appendix 6.1.

6.29. The royalties collected by the Society in any given year cannot be distributed immediately on receipt by the PRS but have to be held until the work of analysing the performances which have taken place over the appropriate period has been completed. Therefore, the PRS is always in the position of holding substantial sums which are in the process of being allocated to its members and affiliated societies. To ensure that there are sufficient liquid funds available at each of the four distribution dates, a high proportion of the royalties awaiting distribution is placed on short-term deposit. As the PRS is continually collecting royalties there is, in effect, a permanent investment fund.

6.30. The overall investment policy for this fund is determined by the General Council. Its implementation is entrusted to the Finance Committee which meets with the Society's professional Fund Managers to agree the criteria to which the Fund Managers will operate. Early in 1993 the General Council decided that none of the Society's funds should be invested in equities, due to the potential downside risk, and the Fund Managers disposed of all equity holdings during 1993. The PRS told us that the decision to move investments out of equities was taken by the Finance Committee and was contrary to the advice of management. No advice was sought from external advisers. An analysis of investments held at 31 December 1994 is given in Table 6.6.

TABLE 6.6 Analysis of investments held by the PRS at 31 December 1994

	<i>£'000</i>	
	<i>Book value</i>	<i>Market value</i>
Listed investments (fixed interest securities)		
The Stock Exchange	24,771	24,151
Other stock exchanges	<u>3,943</u>	<u>4,006</u>
	<u>28,714</u>	<u>28,157</u>
Bank deposits	1,567	
Short-term deposits	<u>19,500</u>	
	<u>49,781</u>	

Source: PRS.

6.31. The market value of investments at 31 December 1994 was lower than the book value by £0.6 million. The book value has not been written down to market value as it is the Society's view that this is only a temporary diminution. The short-term deposits are spread across a range of building societies and other financial institutions such that at 31 December 1994 no one deposit exceeded £2 million.

6.32. The income generated by the investments and short-term deposits in 1994 is set out in Table 6.7. The return has been calculated based on the net income earned and on the average balance of investments (calculated on a quarterly basis) and of short-term deposits (calculated on a monthly basis) held during the year. The large loss on realization of investments includes foreign currency losses of £0.6 million.

TABLE 6.7 **Income earned from investments and short-term deposits in 1994**

	<i>£'000</i>	
	<i>Investments</i>	<i>Short-term deposits</i>
Total income earned	2,399	1,932
Less loss on realization of investments	<u>(714)</u>	<u>-</u>
Net income earned	<u>1,685</u>	<u>1,932</u>
Average holding during the year	30,513	34,196
		<i>per cent</i>
Return	5.5	5.6

Source: PRS.

6.33. Listed investments are generally not held as short-term investments and it is more appropriate to consider the average return over a number of years rather than for one year in isolation. The PRS recently changed its investment strategy and so there is little history on which to assess the return achieved on fixed interest securities. However, the Society's return on long-term investments over the past five years is approximately 7.8 per cent a year. In comparing this with any published performance tables it should be borne in mind that the PRS utilizes or pays out to its members all interest received and realized net capital gains rather than reinvesting such monies in the fund.

6.34. In addition to placing funds in investments and short-term deposits, the PRS's preference in setting up regional offices has been to purchase freehold properties using their cash, although this has not always proved possible. The net book value of freehold property at 31 December 1994 was £3.3 million.

Cost allocation methods

6.35. The PRS exists to collect and distribute revenue on behalf of its members for the performance of their works. Apart from its investment income, the PRS only has one other source of income, that from the performance of works. Therefore, all of its costs have to be recovered from that income. The PRS recovers its costs by deducting them from the revenue earned prior to distributing that revenue to its members. Cost recovery rates are calculated and applied to the various distribution sections.

6.36. There is a charge for joining the PRS of £50 for writers and £250 for publishers (both inclusive of VAT). This income is used to reduce the overall costs of the PRS. For 1994, the joining fees totalled £78,000 and represented less than 0.3 per cent of total administration costs. There is no annual membership fee and no other charges are levied by the PRS on its members for any other services it performs for them.

6.37. The PRS's view on administration costs is that, in an ideal world, all costs would be specifically allocated against the revenue giving rise to those costs. However, where costs do not directly relate to revenue a compromise solution has to be found.

6.38. The PRS informed us that, due to the integrated nature of the PRS operations, costs can be analysed meaningfully only against broad revenue streams. For example, licensing inspectors and support staff are responsible for licensing the thousands of premises which use music and for collecting the revenue. However, one set of premises such as a public house may contribute to several different revenue streams—live performances, discothèques, juke-boxes. In addition, much of an inspector's time is spent on identifying premises which are not licensed but should be. Nonetheless, for some costs the PRS is able to undertake specific allocations. For example, the costs of the department which handles the distribution of income from television performances are apportioned across the income arising from the various television companies. The apportionment is based on the time spent by the department's staff on the distribution aspects of each of the television companies as estimated by the department manager.

6.39. This section of the chapter explains the methods which the PRS adopts to allocate costs against royalty revenue. It goes on to show how the administration costs are expressed as a percentage of revenue for

each of the PRS's main revenue streams and how, using this information, the PRS then sets cost recovery rates for each of the distribution sections.

Analysis of costs

6.40. For internal management reporting purposes, the PRS divides its operations into a number of divisions such as licensing, membership, repertoire, distribution. However, these divisions do not necessarily incorporate all the costs associated with a 'function'. For example, there are several departments within the Distribution Division which deal with various aspects of the distribution process: accounting, general, overseas, radio, television, research and general management. But there are also other divisions which incur distribution-related costs such as the Information Technology Division and the Music Services Department. The PRS does not produce management information which analyses the costs on a strictly functional basis, although this was done as part of the Business Process Review (BPR) carried out by various members of PRS senior management in 1992/93.

6.41. A cost/benefit analysis was undertaken (based on 1992 costs) as part of the BPR in an attempt to demonstrate how much it cost to produce the business outputs. The BPR team noted that they had difficulty in obtaining statistics to measure the benefits and provide work unit costs. In addition, where measures did exist they were not always measuring the most appropriate throughput, as, for example, with distribution queries from members. The queries were measured on the number of letters received rather than the number of works and performances of those works queried. The PRS told us that it has since carried out further research on members' queries.

Direct and indirect costs

6.42. As noted above, the PRS identifies some costs as being directly attributable to specific sources of revenue. These costs are described herein as direct costs. All other costs are described as indirect costs. The split of direct costs and indirect costs in each of the last five financial years is summarized in Table 6.8. This shows that, although a greater proportion of the costs are matched to specific revenue streams than was the case five years ago, the majority of the costs (58 per cent) still are not directly attributed to any particular revenue stream or streams. The main change occurred in 1994; it was not due to any inherent change in the costs themselves but was due to the General Council requiring management to reappraise indirect costs to determine if any of the costs could be related to specific revenue streams. This reappraisal used information gained from the BPR and resulted in a proportion of both the IT costs and the central property costs being transferred from indirect costs to direct costs.

TABLE 6.8 PRS: summary of direct and indirect costs, 1990 to 1994

	1990		1991		1992		1993		1994	
	£'000	%	£'000	%	£'000	%	£'000	%	£'000	%
Direct costs	8,185	34.5	8,693	33.0	9,053	32.6	8,976	32.2	12,043	42.0
Indirect costs	15,569	65.5	17,654	67.0	18,741	67.4	18,871	67.8	16,640	58.0
Total costs	<u>23,754</u>	<u>100.0</u>	<u>26,347</u>	<u>100.0</u>	<u>27,794</u>	<u>100.0</u>	<u>27,847</u>	<u>100.0</u>	<u>28,683</u>	<u>100.0</u>

Source: PRS.

Allocation of costs

6.43. In allocating costs to revenue source, the PRS has four main revenue headings: public performance, broadcasting, agency territories and affiliated societies. The headings for public performance and broadcasting are further subdivided as follows:

- (a) Public performance UK
 - Live music
 - Public reception
 - Other
- (b) Public performance Republic of Ireland
 - Public reception
 - Other
- (c) Broadcasting
 - BBC
 - ITV
 - GMTV
 - Channel 4/S4C
 - Satellite and cable
 - Commercial radio
 - RTE
 - Irish independent radio
 - Irish satellite and cable

6.44. The extent to which administration costs are identified as direct costs rather than indirect costs affects the relative amount of administration costs deducted from one source of revenue compared with another. This is demonstrated by considering, as examples, two sources of revenue in 1994:

- (a) revenue from a work performed in a discothèque (other public performance UK), which is typical of most types of work in the public performance category; and
- (b) revenue from a work broadcast on BBC television.

The level of administration costs deducted, expressed as a percentage of gross revenue, has been calculated on three different bases, as follows:

- (i) no costs are identified as direct costs with all costs categorized as indirect and allocated across domestic licensing revenue in proportion to turnover;
- (ii) direct costs and indirect costs are identified and allocated on the basis adopted by the PRS for 1994 revenue; and
- (iii) as for (ii) but all IT costs and central property costs are categorized as indirect costs. (In 1994 a proportion were categorized as direct costs.)

The cost percentages are set out in Table 6.9. This shows that the member who has a work broadcast on the BBC benefits from a greater degree of cost allocation whereas the reverse is true for the member whose work is performed in public. The actual cost recovery rate set by the Distribution Committee will not always be the same as the cost allocation rate as the intention is for recovery rates to smooth out any one-off or short-term fluctuations. The actual cost recovery rate set in 1994 is given in Table 6.9 by way of information.

TABLE 6.9 **Effect on net revenue of proportion of direct costs to indirect costs based on 1994 figures**

	<i>Cost recovery as a percentage of revenue</i>	
	<i>Discothèque</i>	<i>BBC broadcast</i>
Basis (i)-all administration costs treated as indirect	26.1	26.1
Basis (ii)-1994 basis	29.8	15.9
Basis (iii)-1994 basis except all IT costs and property costs treated as indirect	29.7	17.4
1994 cost recovery rate	31.0	16.0

Source: MMC/PRS.

Allocation of direct costs

6.45. Some or all of the costs of certain of the divisions are identified as direct costs and these are set out for the last five financial years in Table 6.10. This shows that two divisions account for the majority of the direct costs. For 1994, Licensing Division and Distribution Division (excluding distribution accounting and general management) accounted for 69.7 per cent of direct costs. As already noted, in 1994 a proportion of the IT costs (26.2 per cent) and central property costs (29.8 per cent) were included in direct costs for the first time.

TABLE 6.10 **Direct costs, 1990 to 1994**

	<i>£'000</i>				
	<i>1990</i>	<i>1991</i>	<i>1992</i>	<i>1993</i>	<i>1994</i>
Licensing Division	4,543	4,986	5,556	5,583	5,419
Distribution Division (part)	2,339	3,037	2,895	3,068	2,969
Information technology (part)	-	-	-	-	1,227
Broadcasting administration and liaison	156	175	272	209	301
Debt collection	175	178	211	-	367
Overseas (net of recoveries)	389	113	119	116	1,017
Central property (part)	-	-	-	-	743
Tribunal costs	584	204	-	-	-
Rounding	(1)	-	-	-	-
Total direct costs	<u>8,185</u>	<u>8,693</u>	<u>9,053</u>	<u>8,976</u>	<u>12,043</u>

Source: PRS.

6.46. In 1994 licensing costs accounted for 19 per cent of total costs and 45 per cent of direct costs. The PRS tends to focus on the number of premises which are licensed rather than the number of licences issued; a single licence can be issued as a circuit licence to cover a chain of premises such as stores or public houses. At the end of 1994 there were 150,940 licences covering 257,779 premises.

6.47. The licensing inspectors account for 25 per cent of the costs of the Licensing Division and most of their time is spent on relicensing premises where the previous proprietors have left, some 26,000 to 28,000 a year. Some types of premises take up more of their time than others—typically public houses have a high turnover of proprietors compared with factories. Office staff are concerned with the issue and reassessment of ongoing licences and with debt collection and correspondence. Costs do vary by individual premises, for example premises using a lot of live music can generate more queries and correspondence than those not using live music. Also, the circuit licences are relatively cheap to administer measured on a 'per premises' basis.

6.48. An increase in PRS general revenue will not necessarily result in a corresponding increase in licensing costs. For example, a 5 per cent increase in revenue due to an increase in tariff rates or increased music use at existing licensed premises will have little impact on licensing costs. However, if the increase in revenue is due to an increase in the number of premises then it will cause licensing costs to increase. The average licensing officer handles about 2,500 premises. A 5 per cent increase in the number of premises equates to approximately 13,000 additional premises (workload of five inspectors). Therefore, although it is possible that some of the additional work could be absorbed by existing staff, such an increase would certainly give rise to the need for additional inspectors and support staff.

6.49. The methods used to allocate the direct costs to the different revenue streams vary by division:

(a) *Licensing Division.* The costs relate only to public performance, the costs of negotiating the broadcasting licences being included in broadcasting liaison, legal management and general management depending on the actual personnel involved. The regional managers estimate the time spent on gathering programmes and the corresponding proportion of costs is allocated against live music revenue. The remaining licensing costs (92.8 per cent in 1994) are allocated between public reception and other public performance in proportion to income.

(b) *Distribution Division.* The division is concerned with all distribution matters and is subdivided into separate departments dealing with general, overseas, radio, television, research, accounting and

general management. The only costs not included in direct costs are those concerned with accounting and general management. The costs of the other departments are split in proportion to the time spent on the different revenue streams as estimated by the relevant PRS manager. For the radio and television performance departments a further adjustment is made to reflect that radio and television logs are used to distribute public performance revenue. The costs (as estimated) incurred by the radio and television departments in analysing the BBC returns are spread between radio and public performance and between television and public performance in proportion to revenue (taking only that element of public performance revenue which is distributed by radio and television logs).

- (c) *Information technology.* Certain IT costs (performance posting, data preparations, licensing) are allocated based on machine usage of the direct cost divisions.
- (d) *Broadcasting administration and liaison.* These costs are spread in proportion to time spent (as estimated).
- (e) *Debt collection.* This is the cost of debt collection for general licensing and is spread over UK public performance sources in proportion to income.
- (f) *Overseas costs (net of recoveries).* This represents the costs of the personnel dealing with affiliated societies and agency territories and includes the cost of providing the societies with repertoire information.
- (g) *Central property costs.* Central property costs are allocated to each of the 'direct' departments in proportion to the floor area occupied compared with the total floor area occupied by the PRS in London. The property costs of each department are then allocated as described in (a) to (f) above.

Allocation of indirect costs

6.50. Those costs which cannot be attributed to specific sources of revenue are included in indirect costs. The indirect costs for 1994 are listed at Appendix 6.2. There are two categories of indirect costs: general costs (i) and general costs (ii). General costs (i) are those indirect costs which relate to both UK and overseas revenue. General costs (ii) are those indirect costs which relate only to UK revenue. In deciding to which category a cost belongs, the PRS takes the view that the PRS exists to collect income within the UK for its members and so all costs should be borne by that income. However, where costs only arise because of the existence of the overseas income, these costs are borne by that income alone.

6.51. As an example, the cost of dealing with members' queries is borne by UK and overseas revenue as queries can arise on both sources of revenue. By contrast, the cost of works registration is borne by UK revenue alone as the existence of overseas revenue does not impact on the level of costs arising.

6.52. Both general costs (i) and general costs (ii) are allocated to the revenue streams in proportion to revenue received.

Cost allocation by revenue stream

6.53. Table 6.11 shows the allocation of the PRS's total administration costs to revenue source expressed as a percentage of the revenue in each category. This shows that, in general, UK public performance revenue costs approximately 50 per cent more to administer than the broadcasting revenue. The principal reason for this is the cost of the Licensing Division which is all attributable to public performance revenue. The revenue arising in the Republic of Ireland appears to cost much less to administer than that arising in the UK. This is misleading, however, because the statistics are based on the net revenue remitted after deducting the costs of the Dublin office. If the costs of the Dublin office are taken into account, then the administration costs as a percentage of Irish revenue for 1994 are as follows: public reception 49.7 per cent, other public performance 47.9 per cent, RTE 13.7 per cent, Irish independent radio 11.7 per cent and Irish satellite and cable 9.6 per cent.

TABLE 6.11 Allocation of the PRS's total administration costs to revenue source expressed as a percentage of revenue

	<i>per cent</i>				
	<i>1990</i>	<i>1991</i>	<i>1992</i>	<i>1993</i>	<i>1994</i>
Public performance, UK:					
Live music*	-	-	27.2	30.8	32.5
Public reception	32.5	33.5	36.3	30.8	30.1
Other	32.8	33.8	35.9	30.4	29.8
Public performance, Republic of Ireland:					
Public reception	11.2	10.5	11.3	10.2	9.0
Other	16.4	13.7	9.1	6.7	9.4
Broadcasting:					
BBC	18.7	20.3	20.0	18.4	15.9
ITV	20.6	22.4	22.2	20.3	18.0
GMTV	23.3	24.8	25.0	26.0	28.8
Channel 4 and S4C	24.1	27.4	25.3	23.5	20.9
Satellite and cable	18.5	22.1	21.7	21.9	22.0
Commercial radio	22.4	27.0	27.4	23.5	22.1
RTE	11.5	10.8	11.5	10.1	8.2
Irish independent radio	11.1	11.0	10.4	14.1	6.1
Irish satellite and cable	6.2	5.5	6.0	6.0	3.9
Agency territories	28.0	27.7	19.7	25.4	22.8
Affiliated societies	4.3	3.9	4.1	4.3	5.4

Source: PRS.

*Prior to the introduction of the LMDP, live music was included within the category 'other public performance'.

Public performance UK

6.54. The most costly revenue to administer is that arising from live music which is distributed based on programme information. In Table 6.11, live music revenue is the revenue collected from significant venues and festivals and from major events and concert tours together with the pop and classical subsidies and which is distributed according to programme information. The proportion of this live music revenue taken up by administration costs has increased during the period 1992 to 1994. As can be seen from Table 6.12, which shows the direct and indirect costs allocated to live music, this is due to a change in the mix of direct costs to indirect costs combined with a decline in the amount distributed for live music revenue. From 1992 to 1994 the amount of revenue collected (including the pop and classical subsidies) as live music fell by 51.2 per cent (due principally to the abolition of the pop subsidy after 1992: details of the pop subsidy are included in paragraph 6.157) but the direct costs set against this revenue rose in absolute terms by 5.2 per cent. This was due in part to direct costs not falling in line with revenue distributed (the abolition of the pop subsidy had no effect on the costs of licensing or of processing live music returns; the general distribution and research costs actually show an increase in 1994 compared with 1992 of 12.9 per cent) and to additional categories of costs being included in direct costs (IT and central property costs).

6.55. Public reception describes the income received from licensees for playing music which is itself a broadcast or cable diffusion such as the performance of works on the radio, television or satellite channels. The costs allocated to this source of revenue increased in 1992. This was due to live music being treated separately for cost allocation purposes for the first time in this year which affected the allocation of the licensing costs as a whole, rather than to any increase in the actual costs themselves. This also explains the increase in the costs allocated to other public performance in 1992. Other public performance comprises the performance of a work which is not a live performance nor a broadcast or cable performance, either directly or indirectly. It includes performances by mechanical means such as juke-boxes and discothèques.

TABLE 6.12 Direct and indirect costs allocated to live music, 1992 to 1994

	£'000					
	1992		1993		1994	
Royalty revenue	<u>11,295</u>		<u>6,458</u>		<u>5,508</u>	
Direct costs	912	(29.7%)	859	(43.1%)	959	(53.6%)
Indirect costs	<u>2,159</u>	(70.3%)	<u>1,132</u>	(56.9%)	<u>829</u>	(46.4%)
Total costs	<u>3,071</u>		<u>1,991</u>		<u>1,788</u>	

Source: PRS.

Public performances in the Republic of Ireland

6.56. Those costs which can be directly attributed to the Irish income, such as certain distribution costs, are allocated against the Irish revenue streams. However, the indirect administration costs allocated to Irish revenue are restricted to take into account the fact that the revenue has already borne IMRO's administration costs and does not utilize all the PRS services. The same principle is applied to the Irish broadcasting revenue. The significant reduction in costs allocated to other public performance as a percentage of revenue is due to a containment of direct costs coupled with a strong growth in revenue.

Broadcasting

6.57. In general, the broadcasting revenue has benefited from the move to identify those costs which can be allocated directly to the various revenue streams. As can be seen from Table 6.11, the costs borne by GMTV are proportionately higher than other streams of broadcasting revenue. This is because the cost of broadcasting administration and liaison is high in comparison with the small amount of revenue generated (1994 revenue of £295,000). In 1994 this cost represented 7.5 per cent of revenue whereas for the BBC the same cost represented only 0.3 per cent of revenue.

6.58. The figures for commercial radio are analysed further by the PRS between Virgin 1215, Classic FM and other stations. Virgin 1215 and Classic FM generate higher costs than the other commercial stations because their output is subject to a full census, whereas sampling is applied to the other commercial stations. In addition, the costs allocated to Classic FM are higher than those allocated to the other stations (1994-33.3 per cent of revenue) due to the input required from the Music Services Department which accounts for nine percentage points. The classical nature of the station's output and the fact that less than 25 per cent of its music output is controlled by the PRS (that is, less than 25 per cent comprises works in the PRS's repertoire) means that the expert knowledge of the Music Services Department is required in the analysis of the music logs. The PRS told us that if Classic FM's music output consisted of repertoire controlled 100 per cent by the PRS, the cost recovery rate would fall to less than 12 per cent.

Allocation of costs against income arising overseas

6.59. The proportion of total costs allocated against income arising in agency territories and affiliated societies has risen from an average of 7.0 per cent in 1990 to 1993 to over 10 per cent in 1994, as can be seen from Table 6.13. However, over this five-year period, overseas income as a proportion of total income has remained fairly constant showing a small rise from 29.6 per cent in 1990 to 31.4 per cent in 1994. The increase in costs allocated is due to an increase in direct costs. This has arisen due to better identification of those costs which are specific to overseas income plus an increase in the number of staff which are servicing the affiliated societies.

TABLE 6.13 **Costs allocated against overseas income**

	<i>£'000</i>				
	<i>1990</i>	<i>1991</i>	<i>1992</i>	<i>1993</i>	<i>1994</i>
Included in:					
Direct costs	927	848	915	1,003	2,298
General	<u>801</u>	<u>797</u>	<u>940</u>	<u>1,179</u>	<u>633</u>
	<u>1,728</u>	<u>1,645</u>	<u>1,855</u>	<u>2,182</u>	<u>2,931</u>
% of total costs	7.3	6.2	6.7	7.8	10.2
% of overseas income	4.7	4.3	4.4	4.6	5.7

Source: PRS.

6.60. The PRS has a policy that no administration costs are charged against overseas income remitted from affiliated societies in the USA or the EC. The reason the PRS initially gave us for this is that the affiliated societies in the USA and most of the affiliated societies in the EC do not levy such a charge against their overseas income. Consequently, the PRS considers that its membership would be unfairly disadvantaged if it were to deduct these costs when other societies made no such deduction. The PRS subsequently told us that the policy was applied in the first instance to income from ASCAP and BMI in order to discourage the PRS's members from splitting their membership between the US collecting societies for their US rights and the PRS for their rights in the remainder of the world. When the UK joined the EC, the PRS was prohibited from preventing a member from splitting membership territory by territory in Europe due to the GEMA rules (see paragraphs 4.18 to 4.21). The policy was therefore extended to revenue from countries of the EC to discourage the PRS's members from splitting membership.

6.61. We have been informed by ASCAP, one of the US collecting societies, that it deducts 3.5 per cent from overseas income prior to distribution to cover administration costs. SACEM, the French society, told us that it levies a charge of 4.5 per cent.

6.62. The administration costs which are not recovered from the income arising in the USA and the EC are recovered from that portion of the investment revenue (non-licence revenue) which is deemed to have been earned by the overseas income. The effect of this on PRS members is considered later in this chapter under the section on cross-subsidies (paragraph 6.146ff).

Administration cost recovery rates

6.63. The PRS has to recover all its administration costs from revenue received before making its distributions to members and affiliated societies. In doing so the PRS told us that it tries to ensure that the cost recovery rates applied to the major categories of revenue reflect the costs associated with those major categories of revenue. The PRS has identified two main areas where their method of cost allocation results in distortion. These are:

- Small broadcasters who may use as much music as large broadcasters and therefore incur similar levels of costs for analysis and distribution purposes but who generate far less income for the PRS. (ILR stations pay a royalty based on their net advertising revenue.) If this is not compensated for by sampling, the proportion of costs to revenue will be considerably higher compared with the large broadcasters.
- Live music from significant venues where direct costs are largely incurred per concert whereas the revenue from these individual concerts can vary dramatically from a few hundred pounds to in excess of £50,000.

6.64. The PRS has addressed the first of these distortions by setting a separate recovery rate for Classic FM and other stations where a decision not to sample means that distribution costs are proportionately higher. The PRS has addressed the second of these distortions by setting the recovery rate for live pop events at significant venues which individually generate revenue of at least £500 (major pop events) to 25 per cent of revenue with a maximum of £1,250 per event.

6.65. We set out in Table 6.14, for 1994, a comparison of the costs allocated to each source of revenue against the costs actually recovered. As previously noted, the actual cost recovery rate does not always equate to the cost allocation rate as in setting the actual recovery rates the Distribution Committee looks to smooth out any one-off or short-term fluctuations.

TABLE 6.14 PRS administration costs in 1994-comparison of allocated costs to actual recovery rates

	<i>Administration costs allocated</i>		<i>Administration costs recovered</i>	
	<i>£'000</i>	<i>%</i>	<i>£'000</i>	<i>%</i>
Public performance, UK:				
Live music	1,788	32.5	1,446	25.5
Public reception	1,727	30.1	1,721	30.0
Other	11,603	29.8	11,872	30.6
Public Performance, Republic of Ireland:				
Public reception	35	9.0	36	9.5
Other	153	9.4	103	6.3
Total public performance	<u>15,306</u>	<u>29.3</u>	<u>15,178</u>	<u>29.1</u>
Broadcasting:				
BBC	4,638	15.9*	4,478	16.0
ITV	2,433	18.0	2,430	18.0
GMTV	85	28.8	68	23.0
Channel 4 and S4C	587	20.9	617	22.0
Satellite and cable	592	22.0*	346	20.0
Commercial radio	1,925	22.1	1,977	22.8
RTE	140	8.2	162	9.5
Irish independent radio	34	6.1	69	12.5
Irish satellite and cable	15	3.9	29	7.5
	<u>10,449</u>	<u>17.5</u>	<u>10,176</u>	<u>17.7</u>
Agency territories	236	22.8	258	24.8
Affiliated societies	<u>2,694</u>	<u>5.4*</u>	<u>887</u>	<u>1.7†</u>
	<u>2,930</u>	<u>5.7</u>	<u>1,145</u>	<u>2.1</u>
Non-licence revenue/shortfall	-	-	<u>2,184</u>	<u>59.0</u>

Source: PRS.

*The programme logs for royalties received from affiliated societies for cable transmission of programmes received by satellite uplinked in the UK are analysed by the PRS. The administration costs allocated to the BBC include the cost of analysing the logs of the BBC retransmitted in Europe. Similarly, the satellite and cable costs include the cost of analysing the logs of MTV Europe. In the analysis of administration costs recovered, such costs (and the appropriate revenue) have been included under the affiliated societies heading. If administration costs recovered was shown on the same basis as administration costs allocated, the percentage recoveries would be as follows: BBC 15.8 per cent; satellite and cable 20.4 per cent; affiliated societies 1.3 per cent.

†Excluding USA and EC societies, actual rate levied was 5 per cent.

6.66. For all but one of the 16 revenue sources listed in Table 6.14, the cost allocation rate differs from the cost recovery rate. The magnitude of these differences is summarized in Table 6.15.

TABLE 6.15 1994 instances of a difference between cost allocation rate and cost recovery rate

	<i>Number</i>
No difference	1
Up to 0.5 percentage points	4
Between 0.6 and 1.0 percentage points	2
Between 1.1 and 2.0 percentage points	4
Between 2.1 and 5.0 percentage points	2
Over 5.0 percentage points	3

Source: MMC.

Note: Based on actual rate levied on affiliated societies and on the BBC and satellite and cable figures as adjusted per the note to Table 6.14.

6.67. The greatest discrepancy between allocation rate and recovery rate arises in the area of live music, the recovery rate being some seven percentage points less than the allocation rate. Part of the resulting shortfall is met by an over-recovery of costs from other public performance revenue with the remaining shortfall funded by non-licence revenue.

6.68. The recovery rate for major pop events of 25 per cent subject to a maximum of £1,250 per event was set in 1993 based on 1993 budget figures. At that time the cost per major pop event was calculated at £994, of which £298 arose from direct costs. Total costs allocated to major pop events accounted for 25 per cent of that revenue, of which 17.5 per cent was due to indirect costs. The PRS considered two ways of expressing these results:

- (a) set the recovery rate at 25 per cent of revenue-this would overstate the cost for large value events but under-recover the direct costs for the smaller events; and
- (b) set the recovery rate at £994 per event-this would overstate the cost for small events but would under-recover the indirect costs for the large events.

6.69. The PRS considers that the policy actually adopted offers an acceptable and realistic compromise. The PRS accepts that, although the policy eliminates the excess recovery of direct costs from the largest events, it does not enable full recovery of the direct costs of the smaller events nor full recovery of all the indirect costs.

Cost recovery rates applied to distribution sections

6.70. The basis of cost recovery is approved by the Distribution Committee. The actual cost recovery rates are calculated by management and applied to the appropriate distribution sections. For example, 'classical events' is allocated a recovery rate which is applied to the section which holds that income (Section 10-UK live (classical) significant venues-tariff LC). Similarly, one recovery rate is allocated to 'Other public performances' which is then applied to the nine sections which contain the appropriate income such as Section 12-UK recorded (discotheques). The process adopted by the PRS to allocate revenue to the various distribution sections is discussed later in this chapter under 'Distribution of revenue' (paragraphs 6.77 to 6.104).

6.71. The cost recovery rates are agreed in time for the main public performance distribution which occurs in July of the year following that in which the revenue was earned. (Distribution of public performance revenue for major events is included in all four distributions.) The broadcasting revenue (including public reception revenue) for January to June is distributed in October in the year that the revenue is earned and for July to December it is distributed in the following April. Consequently, at the time of the October distribution the recovery rates have not been determined and so the rates for the previous year are applied. The rates are determined in time for the April distribution with the actual rate applied at April taking into account any under- or over-recovery the previous October. In Table 6.16 we show the 1992 recovery rates used in distribution 933 and the 'averaged' rates used in distribution 941 for UK broadcasting revenue in order to achieve the set cost recovery rates for 1993 income.

TABLE 6.16 1993 UK broadcasting revenue-cost recovery rates applied

	<i>Distribution 933</i>	<i>Distribution 941</i>	<i>per cent Cost recovery rate set</i>
BBC	20.0	16.0	18.0
ITV	21.0	19.0	20.0
GMTV	25.0	25.0	25.0
Channel 4 and S4C	25.0	21.0	23.0
Classic FM	39.0	32.6	35.0
Virgin 1215	27.5	24.2	25.0
Local commercial radio	25.0	21.4	23.0
BSkyB, Superchannel and MTV	20.0	20.0	20.0
Other satellite and cable	20.0	20.0	20.0
Public reception	30.0	30.0	30.0

Source: PRS.

6.72. The UK public reception revenue, net of administration costs, is added to the following broadcasting revenues pro rata to the gross revenues in these sections: BBC, ITV, TV-AM, Channel 4, S4C, ILR, BSkyB, Children's Channel, Lifestyle Television, Lifestyle Satellite Jukebox and Screensport. Similarly, the net Irish public reception revenue is added pro rata to certain of the Irish broadcasting sections.

Publication of cost recovery rates

6.73. In its yearbooks the PRS gives the total administration costs which have been deducted from the main revenue streams: public performance, radio and television, Republic of Ireland, agency territories and affiliated societies. The administration costs are disclosed in monetary terms and as a percentage of revenue. In the detailed notes which accompanied its distribution of income statements in July 1995 the PRS published the cost recovery rates which had been applied to each section of revenue.

Deductions from non-licence revenue

6.74. Some costs are not deducted from the royalty revenue but are deducted from the non-licence revenue. Included in Appendix 6.3 is a diagrammatic explanation of how the non-licence revenue which arose in 1993 (approximately £3.9 million) was utilized and distributed.

6.75. Deductions from the non-licence revenue include donations and awards, any shortfall on recovery of total administration costs, expenditure on copyright promotion, transfer to reserves and any shortfall brought forward from the previous year. The net result in 1993 was that all non-licence revenue deemed to arise from domestic collections was absorbed by the deductions. Therefore, a distribution of non-licence revenue was made only to those members who received foreign income. Out of the total figure of £3.9 million earned, only £0.5 million was actually distributed to PRS writer and publisher members being just 14 per cent of the gross amount.

6.76. The 1993 annual accounts of the PRS include a tax credit of £333,000. This is a net figure resulting from a tax credit for withholding tax suffered on overseas income of £2,143,000 and a UK corporation tax charge of £1,810,258. The withholding tax is borne by the overseas revenue prior to it being remitted to the UK. To the extent that withholding tax is recovered, it is credited to those members who generate the overseas income by adding it to their share of the non-licence revenue. The UK corporation tax charge is borne by the recipients of the domestic income. However, the UK tax charge in 1993 was significantly higher than the 'normal level' as capital allowances were waived in order to obtain maximum benefit from withholding tax set-off. The PRS estimates that a normal level for the UK tax charge if all capital allowances are claimed is between £350,000 and £500,000. Therefore, although tax-efficient for the Society as a whole, the recipients of the domestic portion of non-licence revenue had their income reduced by some £1.3 million.

Distribution of revenue

6.77. This part of the chapter explains how the PRS approaches the distribution of its main revenue sources, what information is given to members on their distribution statements and the frequency with which distributions are made. It then goes on to examine how the PRS attempts to compensate those members whose performances of works are missed by the PRS due to the application of sampling or other causes. Finally, it looks in detail at one area within the distribution of public performance revenue which has generated considerable criticism from the members of the PRS, the LMDP.

6.78. The prime objective of the PRS is to collect revenue from the users of PRS repertoire and to distribute that revenue to the members of the PRS and affiliated societies after deducting the administration costs. We consider the distribution of each of the main sources of revenue separately—public performance, broadcasting, overseas—as the method is different in each case. (At the time of our review, the 1994 income had not been fully distributed. We therefore based our review on 1993 income distributed in 1993 and 1994.)

6.79. Of the three main revenue sources, the most complicated to collect and distribute is that arising from public performance. There are over 250,000 users (or venues) which are extremely diverse and include

industrial premises, doctors' waiting rooms, public houses and aircraft. In addition, one venue can encompass several types of performance. As an example, a public house may play a radio, play cassette recordings, have a juke-box and also have live music performances.

6.80. In an ideal world, the revenue arising from the performance of a particular work at a particular venue would be distributed to the interested parties in that work. In reality, however, the resources necessary to monitor every performance in order to secure this result would be so large that it is unlikely that there would be any revenue to distribute, once administration costs had been met.

6.81. Broadcasting is more straightforward in that there is not the same diversity in the type of users and the broadcasters maintain records of what is broadcast. In addition, two of the users, the BBC (television and radio) and ITV, account for a large proportion of the broadcasting revenue: 75.4 per cent in 1994. All performance of works broadcast by the BBC (with the exception of BBC local radio), ITV, GMTV, Channel 4 and national commercial radio are logged and the revenue from these organizations (net of administration costs) is distributed to the interested parties in those works. For satellite broadcasters, cable operators, BBC local radio and ILR, the performances of works are subject to sampling and the revenue is distributed accordingly.

6.82. With overseas revenue, the PRS receives information from the affiliated societies which details the works performed and the income due. The PRS undertakes checks on the accuracy of the distribution information as regards the allocation between writer, composer and publisher for every identified work. However, the identification of the particular works rests with the affiliated societies.

6.83. Revenue from agency territories is treated in the same way as the PRS's direct collections as if it arose from UK licensees. The PRS receives programme returns from licensees in agency territories and analyses these returns to identify the works used. The PRS then distributes the revenue to the interested parties in the works featured.

Public performance (general) revenue

6.84. The income which the PRS receives from its licensees is initially analysed by tariff group. The PRS then allocates this income to eight pools which are subdivided into sections, at which point information on music usage is applied to enable distribution to PRS members and overseas societies. The following narrative relates to the analysis of general revenue from the UK, Channel Islands and Isle of Man. IMRO now administers the performing right in the Republic of Ireland. Up to 31 December 1994 the PRS administered these rights and treated revenue from the Republic of Ireland separately. However, it was identified and distributed in a similar way to the UK revenue.

6.85. The following paragraphs describe how the public performance or general revenue is classified into 18 revenue groupings and then split:

- (a) between live and mechanical means of performance; and
- (b) between certain specific mechanical means of performance and miscellaneous mechanical means of performance;

to arrive at eight pools of general licence income (see Appendix 6.4), namely, background music, aircraft, discothèques, juke-boxes, cinemas, public reception, miscellaneous recorded and miscellaneous live. Each pool is then classified into sections and it is to each section that the PRS applies actual repertoire information or that repertoire information which is deemed as being most appropriate. The sources used by the PRS to produce repertoire information are discussed in paragraphs 6.96 and 6.97. Only when this stage has been completed will the appropriate administration expense deductions be applied against the gross amount in each distribution section to calculate the distributable revenue.

6.86. In distributing the general revenue where specific performance information is not received, the PRS told us that it tries to balance equity with economy. To do this, the first step is to make an assessment of the repertoire which is most likely to be played in different venues and by different means. Once this has been

done, those streams of revenue considered likely to relate to similar repertoire can be pooled and allocated to interested parties according to an objective measure of the likely profile of that repertoire, such as radio logs.

6.87. Domestic general licence revenue is received by the PRS under 41 tariffs. The PRS then combines the revenue from those tariffs on the basis of similarity of the premises or type of premises in which the music is performed. This results in 18 revenue groups, some comprising just one tariff, eg cinemas-tariff C, and some comprising a number of tariffs, eg educational establishments-tariff N (educational establishments controlled by local education authorities), tariff UC (university colleges and other institutions) and tariff PPS (private and public (independent) schools). The revenue collected from local authorities relates to a number of different tariffs and is allocated to the appropriate revenue groupings at this stage. The 18 groupings of public performance revenue are included in Appendix 6.4.

6.88. General revenue in the 18 revenue groups is then split between live events and mechanical means of performance. Mechanical revenue indicates that music has been performed either by recorded means such as record and tape players or on radio and television sets.

6.89. For many of the tariffs revenue can be split between live and mechanical because of the way the charge for the licence is calculated. Information on separate 'factors' such as the number of radios, television sets or juke-boxes, the number of live events taking place annually and the capacity of the premises is established by the PRS for a number of tariffs in calculating the annual charge for the licence. However, not all tariffs provide the PRS with information on the method or type of music use. One example is tariff HC for holiday camps which is based on a set charge based on the number of beds occupied per night over the year. No specific analysis of the means of performance at those premises can be done, since the information is not collected as a requirement of the licence.

6.90. Where information on the type of music usage is not identified by the tariff, management applies a best estimate of the most likely split. The reason for making the split between live and mechanical means of performance is to ensure that the total revenue can be apportioned to the revenue pools for live or recorded for allocation by the Distribution Committee to the most appropriate sections. Appendix 6.4 shows the split between live and mechanical performances for 1993 general (public performance) revenue.

6.91. The revenue from live performances is distributed in accordance with the LMDP. As regards income generated in 1993, approximately 45 per cent was distributed against programme information and 55 per cent was distributed using radio logs. The PRS told us that no scientific research has been undertaken to judge the appropriateness of radio logs to live performances. The Society informed us that the advantage of radio logs is that the PRS has already done the radio analysis from the distribution of revenue from radio broadcasts. Therefore, it costs very little to run that analysis again against a different income stream. The PRS told us that it can alter the repertoire to be used for allocation of income purposes by varying the selection of the radio stations.

6.92. The revenue from mechanical means of performance is further analysed into six specific identifiable major usages: background music, aircraft, discothèques, juke-boxes, cinemas and public reception, with the remainder placed in the miscellaneous recorded revenue pool.

6.93. The public reception revenue is collected from a variety of premises for the public performance of music in programmes broadcast on radio and television sets installed in the premises. This revenue is specifically identified in the year of collection and transferred for distribution with the main broadcasting revenue. The public reception revenue, net of administration expenses, is allocated to various broadcasting sections (eg BBC, ITV, ILR) pro rata to the gross revenues in those sections.

Breaking down the pools into sections

6.94. Each of the eight pools encompasses the accumulation of all revenue earned from a similar usage, eg discothèques. However, it is unlikely that the repertoire used in a discothèque in a holiday caravan park will be the same as that used in a designated discothèque venue. To take account of this, the pools are subdivided into sections. The aim is that each section will include revenue arising from the performance of a similar repertoire. One pool may be divided across several sections. As at April 1995, there were 14 different sections for UK general revenue. These are listed in Table 6.17.

TABLE 6.17 UK general revenue sections, April 1995

01 UK general live and recorded (radio logs)	17 UK recorded (featured music events)
02 UK recorded (background music operators)	18 UK recorded (singles)
05 UK recorded (individual events)	23 UK live (major individual events)
10 UK live significant venues (tariff LC)	52 UK live significant venues (tariff LP)-under £500 events
11 UK recorded (albums)	68 UK recorded (airlines)
12 UK recorded (discotheques)	73 UK recorded (audio-visual)
14 UK films (cinemas)	99 UK recorded (juke-boxes)

Source: PRS.

6.95. The explanation of how the pools are broken down into sections is best done by means of example. Appendices 6.5, 6.6 and 6.7 contain examples of how revenue collected under three different tariffs is allocated to individual sections.

6.96. Once the revenue has been allocated to the individual sections, the PRS has to decide what basis to use to distribute the income in any one section. For sections which comprise revenue earned from live performances at significant venues (Sections 10, 23 and 52) actual programme information is used. However, for those sections where information on the actual works performed is not available, the PRS identifies an alternative source of information which it considers will most closely reflect the actual repertoire used. Therefore, the section which contains the revenue from live performances not held at significant venues (Section 1) is distributed using selected radio logs as the PRS considers that these logs will mirror to a great extent the repertoire performed at the non-significant venues.

6.97. Most of the sections which contain royalties from performances given by recorded means are distributed by reference to statistical data obtained from sources other than the licensees. These include monthly record sales charts for both singles and albums/cassettes (until 31 December 1994 the monthly top 500; subsequently the entire CIN chart subject to practical volume limitations), a published dance chart and tape programme subscriber data supplied by background music contractors. Additionally, returns of authenticated record sales for minority styles of music are accepted from members in respect of works featuring on records achieving minimum annual sales of over 1,000 but unlikely to be included in the published monthly charts. To illustrate, the PRS considers that the works performed in a designated discothèque venue will bear a direct relationship to the singles sales charts (40 per cent), the album sales charts (10 per cent), the *Music Week* dance charts (10 per cent) and selected radio logs (40 per cent). Therefore, the revenue in the appropriate section (Section 12, UK recorded (discotheques)) is distributed on this basis. However, the PRS considers that the works performed in a holiday caravan park will be different to those performed in, say, a London discothèque. Consequently the revenue from the caravan park discothèque is allocated to a different section (Section 17, UK recorded (featured music events)) and is distributed on the following basis: singles sales charts, 25 per cent; album sales charts, 25 per cent; selected radio logs, 50 per cent. Royalties from film performances in cinemas (allocated to Section 14, UK films) are distributed by reference to returns of the films exhibited at each cinema, latest box office factors and the music cue sheets drawn up by the producer of each film.

6.98. Each of the works identified as a result of the analysis of such statistical data receives points. The number of points depends on the number of times a work is performed and the duration of the work. Other factors may also be relevant. For live performances, the number of points increases with the audience capacity of the venue (see Appendix 6.9). For performances by means of films or videograms, a distinction is made between featured use and background use, featured use attracting 1.4 times as many points as background use. The principles applied to determine the number of performances of a particular work vary depending on the type of statistical data involved. For monthly record sales data, the number of performances of a particular work will be based on a direct proportion of the number of chart sales of the record containing that work.

6.99. The total number of points which have been awarded to works within a particular section is calculated and divided into the distributable revenue for that section. This establishes the value of a point for that section for a particular distribution date and, therefore, the amount of money each work is to receive from that pool.

6.100. The creation of distribution sections from the pools of general revenue and the identification of repertoire to be applied to each section is undertaken by the Distribution Committee of the General Council, assisted by observer members of the committee from the three main Writers' Guilds, the Incorporated Society of Musicians and the Music Publishers Association (MPA) and with the advice and input of PRS management.

6.101. Each May, management presents the committee with schedules outlining the pools of revenue and the sections. It is up to the committee, subject to final approval by the General Council, to approve the treatment of a section in accordance with the previous year's practice or to amend the proportion of revenue allocated to a particular section. It may also review the programme information used to distribute the revenue in a section. Distribution Committee decisions are normally endorsed by the General Council.

Broadcasting

6.102. The broadcasting revenue is distributed on the basis of returns received from the broadcasters. The level of music returns processed by the PRS in respect of works appearing in broadcasts and cable services in the UK is generally determined by reference to the level of royalties paid by the broadcaster. This is summarized in Table 6.18.

TABLE 6.18 **Level of music returns processed by the PRS**

<i>Broadcaster</i>	<i>Programme analysis</i>
<i>Radio</i>	
BBC national and regional radio	Full
BBC World Service	Full
BBC local radio	3 days a month*
Independent national radio (eg Classic, Virgin, Talk Radio UK)	Full
ILR	Sample-level linked to level of Net Advertising Revenue
<i>Television</i>	
BBC1 and 2 (including regional programmes)	Full
Independent stations (terrestrial)	Full
Satellite	Sample linked to level of royalty paid
Cable-only channels	Sampled according to income but not less than 10%

Source: PRS.

*Except live or locally recorded performances which are analysed in full.

6.103. Once the works have been identified, weighting and multipliers are applied. There are published station values for broadcasters which weight a performance based on the potential audience for the broadcast. For instance, a performance on the ITV network will receive more points than a performance in one ITV region only. However, no distinction is made for the time of day that a performance is broadcast. Consequently, a work performed at peak audience times receives the same rate as when that work is performed at an off-peak time. Multipliers are applied based on the type of use and the duration of a work appearing in a broadcast. Certain types of performance such as featured uses and opening music for a programme are given more weight than background music. The cash values which were earned for musical items broadcast between July and December 1993 are set out in Appendix 6.8. Examples of the calculation of points awarded to the performance of works are included at Appendix 6.9.

6.104. For radio broadcasts there is a separate multiplier for works with durations over 60 seconds. This gives a higher value to longer works of any genre in recognition of the greater creative effort required.

Overseas

6.105. The PRS receives distribution statements from the affiliated societies which can be in paper form or on computer tape. The levels of detail and accuracy vary from one society to another and the PRS told us that all distribution statements require an element of further research by the PRS to clarify the details supplied. The PRS checks against the registered share for each work, the share applied by the affiliated society to each writer interested party and, where relevant, the publisher for the period/date of performance in the territory concerned.

Distribution statements

6.106. The distribution statements issued to the members with their payment specifies each work title for each different income source, the member's contractual (fractional) share, the section code and the sum generated. When both performance and distribution precede formal registration, the Society's plan of division is applied to calculate a 'deemed' share relationship (such works are identified by an asterisk on the statement). The sum paid can be adjusted up to three years following distribution by reference to the actual share relationship when this is registered by the members.

Distribution frequency

6.107. The four main distributions each year take place in the middle of April, July, October and December. Domestic broadcasting income is distributed in April and October; general revenue is distributed in July with a payment on account in December.

6.108. Income from affiliated societies and major live events in the UK and overseas is distributed at each of the four main distributions.

6.109. The PRS told us that it should be possible to consider implementation of more frequent main distributions once IS facilities are developed. The Society stated that interim distributions could be made more frequently now but would result in increased cost in processing paperwork and adjustments. There is a weekly payment run which enables the PRS to make adjustments or payments on account (in respect of major live events) in between the four main distributions. Adjustments are made where monies are due to members following the resolution of an outstanding query or where royalties have been released from suspense.

6.110. The PRS considers that the nature of its activities does not lend itself to a continuous payment system. Much of its income relates to blanket licences for public performances in which the musical works are not identified in advance. Similarly, broadcasting revenue cannot be allocated until full or sampled music returns are received from the broadcasters and analysed by the Society. Broadcasters are required to report music use to the PRS within 35 days following transmission.

Unlogged performances

6.111. As not all performances are subject to 100 per cent census, there will be works performed which are not logged by the PRS and which therefore will not be included as being due a share of the revenue. In order to compensate members whose works have been missed due to the methods of performance logging adopted by the PRS, the PRS has two compensation schemes. In recent years these have been described as the Unlogged Performance Allocation (UPA) and the Special Allocation. From 1995, the UPA has been replaced by a revised scheme known as the Performance Compensation Allocation (PCA).

6.112. The term UPA to describe allocation payments on members' statements was first used in 1984. Various UPA-type schemes had already existed for many years until, in 1986, a scheme was announced which continued unchanged until 1993. The 1986 scheme stipulated a minimum payment of £30 for a writer member progressing to £250, with proportional payments to publishers and affiliated societies.

6.113. UPAs were paid to all writer and publisher members of the PRS and affiliated societies who had received at least one logged performance credit in the preceding two years. As a general principle, the UPA

levy was funded by those sections where the distribution was not based on actual programme information or was based on incomplete programme information.

6.114. On the recommendation of the Live Music Working Group, the minimum UPA for writers was increased to £75, progressing to £375, for the July 1993 distribution with a corresponding rise for publishers. This was as a result of a change in the LMDP which put greater importance on the UPA (due to a decrease in the number of significant venues providing programme information) and brought pressure from members to increase payments.

6.115. The impact of the increase on the funding sections was not appreciated by the General Council until after the announcement of the increase had been made. Once the impact was appreciated following the distribution in 1993, the Council decided that the level of funding was unacceptable as, for a large number of the funding sections, the aggregate loss suffered by the individual high-income members by incurring a deduction of 11.24 per cent was much greater than the UPA sum gained back by those members from the scheme. Therefore, the UPA at July 1994 was paid out at its previous 1986 policy level based upon a minimum of £30 to writers.

6.116. The PRS looked at the possibility of a computerized financial modelling facility which would enable the PRS to forecast the results of a change in distribution policy. The PRS told us that this model has not been developed due to modelling logic problems, technical problems and other tasks being assigned a higher priority.

6.117. The number of PRS members who received payments under the UPA scheme in 1991 to 1994 is set out in Table 6.19, in absolute terms and as a percentage of the total membership at the end of the year. In each year, approximately two-thirds of the UPA funding was paid to PRS members with the remaining third being paid to affiliated societies.

TABLE 6.19 Number of members who received UPA payments in 1991 to 1994

	<i>Writers and copyright owners</i>	<i>Publishers</i>	<i>Total</i>	<i>Percentage of membership*</i>
1991	17,448	2,172	19,620	80.2
1992	18,143	2,177	20,320	79.0
1993	18,462	1,519	19,981	74.7
1994	20,030	1,614	21,644	78.8

Source: PRS.

*For this calculation, total membership has been taken as the average of the opening and closing figures for each year.

Performance Compensation Allocation

6.118. In 1994 the General Council decided that payments under the UPA scheme should cease from 1995 onwards. The Council considered that the scheme as it had developed in 1993 had become too high a proportion of distributed revenue and that this was inequitable to the higher contributors to PRS income. The interim arrangement used in 1994 was not seen to be a satisfactory solution and the General Council proposed to introduce a new scheme in its stead.

6.119. The result is the PCA scheme which is a flat rate compensation payment to low-earning members only. The flat rate will apply equally to writer and publisher members. Only those members receiving royalties in the range of £25 to £500 a year will qualify and there will be only two bands of payment: a payment of £25 for members with royalties between £25 and £50 a year and a payment of £50 for members with royalties between £50 and £500 a year. Affiliated societies will also receive PCA. The total PCA paid to affiliates will bear the same ratio to the PCA paid to PRS members as do the total royalty payments to affiliates compared with the total royalty payments to members. Funding will be restricted to that part of general live and recorded revenue which is distributed over radio logs due to the absence of specific programme information.

6.120. The first PCA payments (which related to earnings in 1994) were made in the second distribution of 1995, D952. The number of members who received payments and the total funding required is set out in Table 6.20. Corresponding details for UPA payments made in 1994 are included for comparative purposes. As can be seen, the numbers of members who now receive compensation for the performance of works not picked up by the PRS's sampling methods has halved. Of the writer members, approximately 4,000 who no longer receive a payment are the higher-earning members, those earning more than £500 a year. The remaining 6,000 no longer receiving payment are those who earn less than £25 a year. The PRS did not undertake any research to determine whether or not the new method of allocation provided a more accurate population than the old method of those members affected by the lack of a 100 per cent logging of all performances of works. The sole aim of the General Council in requiring the change to the PCA was to effect a cost-cutting exercise.

TABLE 6.20 Comparison of PCA payments and UPA payments

	<i>Number</i>	
	<i>UPA 1994</i>	<i>PCA 1995</i>
PRS writer members who received payment	20,030	10,215
PRS publisher members who received payment	<u>1,614</u>	<u>861</u>
Total	<u>21,644</u>	<u>11,076</u>
		<i>£'000</i>
Total funding (includes funding of affiliated societies)	2,263	600

Source: PRS.

Special allocation

6.121. For members who have earned no royalties at any distribution in a year and who are not eligible for a UPA (now PCA), a claims procedure exists for payment of a single Special Allocation covering live, recorded or local radio performances. This applies to works of all genres-popular, classical and those of a more specialist nature. A claim has to be supported by evidence of 15 minutes performed duration in the PRS sampled performance areas during the previous year. Where claims are substantiated, a flat rate payment of £25 is made to writers and publishers. About £10,000 is set aside from general revenue to fund the entire scheme and a proportionate sum is included in the PCA payments made to affiliated societies.

Live Music Distribution Policy

6.122. Prior to 1986, income from live music performances was distributed based on a combination of sampling and full census analysis of programmes from thousands of venues at which classical and non-classical music was performed. The PRS told us that this had been a time-consuming and resource-intensive system. A new scheme was introduced in 1986 following a detailed review by the General Council in an attempt to provide a better-controlled distribution at a lower cost.

6.123. The 1986 policy made a distinction between three genres of music-serious, light classical and non-classical. No change to the pre-1986 policy was made in respect of concerts of 'serious' or 'classical' music for which the Society continued to attempt to collect 100 per cent programme returns from all venues at which the music was performed. This also applied to light classical music from 1988 onwards. For live performances of light classical (pre-1988) and non-classical music, the PRS did not collect programmes unless the royalty charged for a single event, or the aggregate royalty for a tour, was £200 or more.

6.124. The PRS told us that under the policy 70 per cent of net distributable revenue was distributed by reference to radio logs. The remaining 30 per cent of the net distributable revenue was distributed between classical works (by reference to programmes received), works featuring in an event which generated a royalty

of £200 or more (by reference to programmes received) and works representing certain minority styles of music through the reliance on information provided by certain responsible bodies such as The English Folk Dance and Song Society. (The responsible bodies forwarded to the PRS lists of works performed over the previous quarter based on information provided to the responsible bodies by their members.)

6.125. After its introduction, the 1986 policy was criticized by members on several grounds. The system of obtaining and analysing all programme returns for classical music was regarded by the popular music membership as giving classical composers and publishers an unfair advantage. For their part, the classical membership complained that the PRS did not obtain all the programme returns it could. The PRS staff found it difficult to obtain programmes and to educate the responsible bodies. Also, considerable staff time was needed in analysis and in following up members' queries. The licensees, who had to submit programmes for classical concerts, found it difficult to recognize the music styles according to the PRS definitions.

6.126. At a special meeting on 21 February 1989, the General Council decided to review the 1986 policy in order to make more fair and accurate distributions over a wider range of music styles. The result was the LMDP which came into effect in 1992.

6.127. The basic principle of the current policy is to collect all programmes of all works when played live either at:

- (a) any one of the significant venues; or
- (b) at a performance which is part of one of the significant festivals; or
- (c) in an event or concert tour where the aggregate royalty to the PRS is £500 or more.

Royalties from live music which fall within (a) to (c) above are distributed on the basis of programme information. All other live music royalties are distributed using radio logs. This policy is set out in the Members' Handbook. However, the link between this policy and the distribution procedures is not set out clearly, particularly the fact that popular music performed live at a venue other than one designated as significant or where royalties in excess of £500 were payable would not be logged and so would not count for distribution purposes.

6.128. In addition, as from 1 January 1994, the PRS also accepts complete classical concert programmes for performances at non-significant venues on the condition that no further research has to be carried out by the PRS in processing the programmes. This is the Unsolicited Programmes Scheme. A condition of the scheme is that the event must have been licensed under tariff LC, so classical performances at non-LC venues will not be covered. All programmes processed under this scheme are deemed to have taken place in a venue up to 200 capacity for the purposes of distribution. The number of unsolicited programmes that will be accepted by the PRS in any one year is capped by reference to the number of classical programmes being processed from significant venues in the same year.

6.129. Originally, in 1992, there were 550 significant venues. This was subsequently reduced to 426 significant venues in 1994. The criteria for inclusion in the list of significant venues depends on audience capacity and a minimum number of concerts per year, for which an admission fee is charged, and which is licensed under the concert tariffs LP or LC (prior to 1994, venues licensed under other tariffs could qualify as significant venues). The smaller the audience the greater the minimum number of concerts required and vice versa. So a venue with audience capacity fewer than 200 must hold a minimum of 50 concerts a year whereas a venue with audience capacity of 1,000 or more need only hold five concerts in a year to qualify as a significant venue. The list of around 50 significant festivals is compiled based on similar principles. Both lists are reviewed annually.

6.130. The PRS stated that the new policy is better than the old in that:

- it uses more information about what is actually being performed live than the previous policy;
- the PRS has access to more programme information which means that the number of members entitled to receive live music royalties has increased for major events; and
- more members are receiving money for live performances since the previous policy did not cover so many music styles (the collection of programmes for any genres other than classical was severely restricted).

6.131. The PRS also noted that the proportion distributed by reference to radio logs has fallen which has resulted in some members receiving less than they did under the previous distribution policy.

6.132. Table 6.21 gives the programmes used for distribution purposes, 1991 to 1994. It also gives the number of major tours and events represented by those programmes. The PRS was unable to supply information as to the number of events represented by the classical and other programmes on a consistent basis, year by year. The table shows that in 1994, and following the reduction in the number of significant venues, the PRS has slightly less programme information overall under the LMDP than it did under the 1986 policy. However, the amount of information which it uses for classical events has fallen substantially whereas the amount of information on works performed at tariff LP events has increased.

TABLE 6.21 Programmes used for distribution purposes, 1991 to 1994

	<i>Total programmes (A+ B+ C)</i>	<i>Classical programmes (A)</i>	<i>Classical as a % of total %</i>	<i>Other programmes (B)</i>		<i>Programmes for major tours or events (> £200) (C)</i>	<i>Number of major tours or events covered (> £200)</i>
1991	20,700	11,300	71	1,600		7,800	860
<i>Significant venues and significant festivals only (wef 1.1.92)</i>							
		<i>(Tariff LC)</i>	<i>%</i>	<i>(Tariff LP < £500)</i>	<i>(Other tariffs < £500)</i>	<i>(> £500)</i>	<i>(> £500)</i>
1992	31,500	5,500	24	5,000	12,000	9,000	1,710
1993	26,500	5,900	22	5,500	8,300	6,800	1,510
1994	18,300	6,100	34	5,800	0	6,400	710

Source: PRS.

Notes:

1. A programme is treated as a list of works performed by a performer or group of performers on an occasion. For classical events there is usually one programme for each classical concert. For a major tour or event many programmes could be received, ie two programmes would be received for one concert with a headline and a support act. Programmes collected will be disregarded (and so not included in the above figures) if they have been inadequately verified.

2. The above figure for total programmes represents performances that took place during that year, or previous years, and were distributed in the July distribution of the following year. The exception is major events and tours which could have been distributed in any one of the four distributions up to and including the July distribution.

6.133. The number of tours for which the PRS received programmes which were used for distribution purposes in 1992 and 1993 increased significantly compared with 1991. This was due in part to the processing of a backlog of outstanding programmes and in part to the increased efforts of PRS staff in pursuing and obtaining programmes. The decrease in 1994 is as a result of the significant reduction in the actual number of events in that year (as referred to in paragraph 6.15). The other programmes in 1991 relate to programmes from service bands which were used for distribution purposes under the 1986 policy. Although the PRS received information from the responsible bodies, it comprised the number of works rather than programme information. The PRS told us that this means it does not have a consistent way of measuring programmes reported by most of the responsible bodies. However, the PRS told us that the amount of money distributed

using information from the responsible bodies was only a few thousand pounds. For 1992 and 1993 performances distributions were made for concerts and events in significant venues not licensed under tariffs LP or LC, such as universities, public houses and clubs. This practice ceased for 1994 performances, as explained in paragraph 6.129. The number of classical programmes used in 1994 includes 1,500 programmes for performances in non-significant, tariff LC venues which were accepted as part of the Unsolicited Programmes Scheme.

6.134. The PRS did not produce to us any evidence to support its contention that more members are receiving money under the new policy because it covers more music styles. However, the PRS stated that in its view the new policy was bound to cover more music styles than the 1986 policy as the 1986 policy positively discriminated against non-classical genres. Classical writers could submit programmes from any event; other genres (jazz, folk, popular, ethnic) could only submit programmes if the event generated revenue of at least £200 (hence the small number of 'other programmes' in 1991).

6.135. Certain of the writers and publishers considered that the new policy covers fewer music styles in that the more specialist types of music, such as folk, jazz and brass bands, were less likely to receive payment for live performances under the new policy. The minutes of the Live Music Working Group noted that an analysis of classical PRS writers showed that 39 per cent of them had fared better under the new policy but that 61 per cent had fared worse. In addition, a survey of ten classical publishers (which represented 90 per cent of the classical field) showed a drop in their earnings of between 10 and 50 per cent following the introduction of the new policy.

6.136. Under the 1986 policy, the PRS stated that radio logs were used to distribute 70 per cent of live revenue. From Table 6.22, which shows live revenue collected in 1993 and distributed in 1994, some 55 per cent of live revenue was distributed over radio logs for that year.

TABLE 6.22 **Live revenue collected in 1993, distributed in 1994**

		<i>£'000</i>	
	<i>Total</i>	<i>Distributed by programme information</i>	<i>Distributed by radio logs</i>
Pop concert revenue	3,807		
Pop subsidy*	<u>564</u>		
	4,371	4,086	285
Classical music	783†		
Classical subsidy	<u>1,304</u>		
	2,087	2,087	-
Other significant performances (not LP/LC)	106	34	72
Miscellaneous live	7,362	-	7,362
Difference	<u>(97)</u>	<u>-</u>	<u>(97)</u>
Total	<u>13,829</u>	<u>6,207</u>	<u>7,622</u>
Percentage of total	100	44.9	55.1

Source: PRS.

*Re performances which took place in 1992.

†Includes £259,000 of local authority income.

6.137. The cost of running the new scheme does not appear to be materially less than the cost of running the old scheme, being in the region of £500,000. The reduction in the number of significant venues listed in 1994 was a result of cost-benefit considerations undertaken by the PRS. The proportion of royalties allocated to performances identified as being live but non-concert events at the venues subsequently dropped totalled £34,000 in 1992 whereas the cost of collection, analysis and research totalled some £150,000.

Revenue receipts from overseas societies

6.138. The PRS told us that almost all the affiliated societies operate distribution systems similar to that of the PRS. However, the time-lag between the actual broadcasts or performances in a foreign country and the receipt by the PRS of the royalties collected by the affiliated society in that country can vary significantly between countries. In some cases the time-lag can be quite short; the time-lag between royalties earned by ASCAP and distributed by the PRS varies between 9 and 15 months. In other cases, the time-lag can be longer. Royalties received from the Netherlands and distributed in July 1994 related to the 12 months ended 31 December 1992, a time-lag of between 18 and 30 months.

6.139. The difference in the time-lag for the various societies arises because some societies report to the PRS quarterly, others bi-annually and others annually (most continental European societies). Indeed, the PRS told us that some affiliated societies do not distribute on a regular date at all.

6.140. The PRS informed us that it pays particular attention to world-wide tours of PRS members and asks affiliated societies to pay the related royalties early, either by prompt collection and accounting or by means of an advance against their future distribution. To date, most of the affiliated societies have declined to do either but, since 1992, the PRS has obtained advance payments from seven affiliated societies in respect of eight tours.

6.141. The new contract of reciprocal representation which the PRS is attempting to get adopted by the affiliated societies specifically addresses timing of payments-royalties for a live event which exceed £5,000 to be remitted within 90 days of receipt by the affiliated societies, other royalties to be remitted at the same time as the Society makes a similar allocation to its members and at least once a year.

6.142. The PRS receives revenue from the overseas societies accompanied by financial distribution statements which generally identify the PRS interested party, the share, the work or film title, the sum attributable and the performance source (eg general or broadcasting).

6.143. The PRS told us that it provides to its members, via the detailed distribution statements, all the information that the PRS receives from the foreign affiliates with two exceptions:

- (a) The sources of general and broadcasting are combined. The PRS informed us that work is currently in progress to show these two sources separately on members' statements.
- (b) For the sake of efficiency, royalties from some affiliated societies are amalgamated with others and only one foreign statement is used to distribute the aggregate receipts. This practice occurs when the revenue from the societies is considered too low to make independent analysis efficient. In 1994 this represented only 0.4 per cent of overseas income. The statements not used are checked for high-earning titles and these are paid separately.

6.144. The PRS told us that it recognizes the need to improve the quality of data it receives from affiliated societies. To this end, the Society's new reciprocal contract includes provisions for more detailed information and the right to audit the other societies' accounts. However, these provisions will only be enforceable when the new contract is adopted and, at the present time, there is considerable uncertainty as to whether the affiliated societies will agree to adopt the new contract in whole or in part.

6.145. The PRS does not have information as to the amount deducted by the affiliated societies prior to the distribution of royalty income to the PRS. Again, the new reciprocal contract addresses this by imposing a stated maximum (negotiable) administration charge. Many of the affiliated societies deduct a social and cultural charge of up to 10 per cent of all income as well as an administration charge. In some instances, the PRS charges a reciprocal percentage before remitting income to those societies. However, the imbalance between 'imports' and 'exports' means that PRS members are the net losers. To illustrate, Germany makes a 10 per cent deduction for social and cultural purposes. The net income received from Germany in 1994 was £7.2 million compared with £1.1 million allocated by the PRS to Germany.

Cross-subsidies

6.146. Cross-subsidies occur within the PRS due to the movement of both revenues and costs between groups of members. Such movements are motivated by:

- attempts to support specific categories of members;
- attempts to redress perceived imbalances;
- lack of adequate cost allocation procedures; and
- less than 100 per cent logging of performances.

6.147. The PRS operates two formal cross-subsidies in terms of taking gross revenue earned by one group of members and reallocating portions of it to another group of members. These are the classical subsidy and the EES. A pop subsidy was introduced in 1992 but this lasted for one year only.

6.148. In most, if not all, organizations there are certain costs which do not increase or decrease directly in line with the number of items manufactured or sold. Some organizations do not attempt to allocate all such costs against specific goods or services. Those organizations which do allocate them use a variety of different methods such as in proportion to direct costs, headcount, floor space. The PRS has to recover all of its costs from its members and it does so by allocating its costs against the various revenue streams. Therefore, in addition to the formal cross-subsidies, a description of which follows, there are other, less transparent cross-subsidies which arise as a result of the PRS's cost allocation procedures. Cross-subsidies also arise as a result of the PRS's distribution policies. We consider the extent and quantum of these hidden subsidies.

Classical subsidy

6.149. For many years the PRS has provided a subsidy on distributions to members and affiliates on works performed at classical concerts licensed under tariff LC. A sum taken from general live and recorded public performance revenues is added to the amounts collected under tariff LC to reach an agreed minimum amount. This amount is then allocated, for distribution purposes, over the works in classical music programmes collected from live events. Consequently, the writers and publishers of classical music gain at the expense of those who receive distributions from the general live and recorded public performance revenue. As this is distributed using radio logs (BBC radio, local radio and Classic FM), the losers are the writers and publishers whose works are broadcast on these stations.

6.150. The agreed amount in the classical pool increases annually in line with the RPI, the base year being 1992, the year that the LMDP was adopted. The gross value of the classical pool (before recovery of administration costs) in 1994 was nearly £2.2 million. Of this, nearly £800,000 of revenue was raised from tariff LC and £1.4 million arose from the subsidy, giving a subsidy to actual revenue ratio of 1.75:1.

6.151. The revenue from classical works performed at venues not licensed under tariff LC goes into the miscellaneous live revenue pot. It is not possible to quantify the amount of this 'unidentified classical revenue'. However, part of the subsidy of £1.4 million will be a reallocation of this revenue to the classical revenue section and so, to that extent, the subsidy is reduced.

6.152. The PRS informed us that the existence of a subsidy to classical distributions stemmed from a view, widely shared by many of the PRS's affiliated societies, that there was a cultural significance attached to classical composition. There were proportionately fewer performances of such works in comparison with the number of performances of a great many popular works where repetition was synonymous with success. There had therefore been an acceptance within the music industry, both in the UK and abroad, that in order to protect the classical genre some form of subsidy was desirable to enhance the value of individual classical performances.

Earnings Equalisation Scheme

6.153. This scheme commenced in 1970, its purpose to provide extra income for long-established writer members of the PRS who have experienced a drop in their earnings from the PRS. Eligibility depends on age and length of membership of the PRS and the level of current earnings compared with the level of past earnings. The PRS told us that the scheme was for members who, in the past, had collected substantial royalties from the PRS but who now were experiencing a considerable fall in their royalty income and were in need of some financial help. Therefore, the writer members who benefit will tend to be the writers whose style of music is no longer in fashion. Since 1994, the scheme has been funded from the PRS writer members' share of non-licence revenue.

6.154. Any living member may qualify for a payment if that member is at least 50 years old and has completed 25 years' membership. To calculate what payment, if any, is due under the scheme the member's annual earnings since joining the PRS are adjusted to present day values using the RPI and an average of the best 25 years, the adjusted average annual earnings, is calculated. The adjusted average annual earnings are compared with the member's current annual earnings and up to 50 per cent of the difference between the two is the allowance payable.

6.155. There are maximum and minimum levels within which an allowance is paid. In respect of payments made in 1993, no allowance was paid to a member if the actual earnings exceeded £8,615 or if the adjusted average annual earnings were less than £1,376. The maximum allowance payable to a member was £2,579. In 1993, 552 writer members received a total of £750,787.

6.156. Included in Appendix 6.3 is a diagrammatic explanation of how the non-licence revenue which arose in 1993 was utilized and distributed. The total non-licence revenue was approximately £3.9 million. Of this, £2.8 million was deemed to be due to PRS writer members (after the tax adjustment but prior to any of the subsequent adjustments set out in Appendix 6.3). The cost of the EES in 1994 at £0.75 million represented some 27 per cent of PRS writer members' non-licence revenue earned and some 19 per cent of total non-licence revenue.

Pop subsidy

6.157. In 1992 the General Council decided to subsidize popular concerts by doubling the royalty value attributable, as recompense for the Copyright Tribunal only setting tariff LP at 3 per cent rather than the 6 per cent requested by the PRS. The effect of this subsidy in 1992 was to increase the revenue paid out on popular concerts from a total of £5.0 million to a total of £8.4 million. The subsidy was funded by miscellaneous live income and was discontinued after 1992, the General Council having decided that it did not want this subsidy to continue. The pop subsidy mirrored the classical subsidy in that the writers and publishers of the music performed live at venues gained at the expense of those eligible for distributions from the general live and recorded public performance revenue.

Administration costs charged against overseas income

6.158. The administration costs which are not recovered from income from affiliated societies in the USA or the EC are recovered from that portion of the non-licence revenue which is deemed to have been earned by the overseas income. As shown in Appendix 6.3, in 1993 some £3.1 million of the non-licence revenue was deemed to be due to PRS writer members and publisher members in respect of overseas revenue. Of this, some £1.5 million, being 48 per cent, was deducted to meet the administration costs incurred by the USA and EC income. The effect of this on an individual member's net earnings from performance of works overseas is set out in Table 6.23. This compares the total costs deducted from a PRS member's revenue arising in a USA/EC country with the total costs deducted from a PRS member's revenue arising in a country outside USA/EC territories, say Australia. As can be seen, members whose works are performed in the USA or the EC gain at the expense of those members whose works are performed in other territories. This affects mainly writer members as most publishers collect their revenue direct from the affiliated societies through sub-publishers.

TABLE 6.23 Illustrative example of effect of cost subsidy on USA/EC income in 1993

	£	
	<i>Works performed in the USA</i>	<i>Works performed in Australia</i>
Licence revenue generated	1,000	1,000
Gross non-licence revenue attributable to £1,000 of licence revenue	<u>67</u>	<u>67</u>
Administration costs at 5% of licence revenue	-	50
USA/EC administration costs recovered from non-licence revenue (48%)	<u>32</u> <u>32</u>	<u>32</u> <u>82</u>
Total administration costs to total revenue (%)	3	7.7

Source: MMC.

Cross-subsidies arising from cost allocation methods

Membership Division

6.159. All the PRS's costs are deducted from revenue prior to distribution of that revenue. However, some costs are incurred on behalf of members irrespective of whether they earn any revenue from the PRS. A cost in this category is the cost of certain of the Membership Division activities; such activities comprise organizing members' surgeries, registering members' details and maintaining up-to-date information on members (but exclude answering queries). Therefore, all of the membership benefit but the non-earning members do not pay for this benefit. The PRS estimates that the basic cost of maintaining up-to-date information of a member on its files (included in the costs of the Membership Division) and providing a member with the Yearbook, PRS News and other communications (included in the costs of the Public Affairs Department) is about £20 to £25 per member a year. It is noted that in charging members a joining fee, publisher members pay five times the rate of writer members. Using the same ratio, these basic costs could be recovered by charging writer members £25 a year and publisher members £125 a year.

6.160. Currently, the cost of the Membership Division (excluding membership queries) is included as an indirect overhead which is recovered from domestic revenue only. The recovery rate in 1994 was 0.67 per cent. Consequently, a member earning £100 of gross revenue contributes just 67p to the Membership Division, a member earning £1,000 gross contributes £6.70, while a member earning £100,000 gross contributes £670.

6.161. Under the current system of cost allocation, the members of affiliated societies who receive payments from the domestic licence revenue contribute towards the cost of the Membership Division. Members of affiliated societies received approximately £24 million net revenues in 1994 (being approximately £34 million of gross revenue), thereby contributing over £200,000 towards the costs of the Membership Division. Therefore, in respect of membership costs, the high-earning members of the PRS and members of affiliated societies are subsidizing the low-earning and non-earning members of the PRS. (It should be noted that PRS members who receive income from affiliated societies will similarly be subsidizing the membership costs of those societies.)

Registration of works

6.162. The cost of registering a work is included as an indirect overhead and recovered from domestic revenue only. The PRS informed us that most of the costs relating to registration of works are incurred in the registration of full details of active works and in updating their records when the publishers change catalogues. The PRS told us that the registration of a new work in skeletal form costs under £1.

6.163. The PRS also told us that of all the new works registered in any one year, approximately 25 per cent were the works of PRS writer members. The remaining 75 per cent were the works of overseas writers and were registered by the UK sub-publisher member of the PRS. This enables the sub-publisher to receive payment for the performance of such works direct from the PRS rather than via the affiliated societies. (A similar practice exists overseas whereby UK writers' works are registered with the affiliated societies by sub-publishers in the particular country. Consequently, the distribution of overseas income by the PRS is predominantly to PRS writer members, not to PRS publisher members.)

6.164. Not every member who earns revenue in any one year will necessarily register a work in that year. However, by treating the cost of registering works as an indirect overhead, all revenue-earning members will bear a charge for works registration in proportion to the amount of revenue they earn. Similarly, the change in publisher ownership of a catalogue will not have a direct correlation to the profile of revenue earners. Consequently, PRS members who earn revenue but do not register works in a particular year subsidize the publishers who change catalogues, the sub-publishers who register the works of overseas writers and the writers and publishers who register works which are then performed infrequently.

Proportion of revenue versus activity-based cost

6.165. Many costs, both direct and indirect, are allocated by the PRS in proportion to revenue. However, many of the costs vary with the number of individual transactions rather than the size of any particular transaction. From the distribution curve of earnings by members related to number of performances (as discussed in Chapter 5), it can be seen that generally the high earners have a large number of works performed whereas the low earners have very few works performed. Hence, the number of transactions (and thus costs incurred) mirrors to some extent the amount of revenue received.

6.166. Nevertheless, the system does give rise to cross-subsidies as the revenue increases with the duration of the performance of the work. Some examples to illustrate the extent of this, based on broadcast performances, are included in Table 6.24. There is a lack of information available within the PRS on the cost of carrying out specific functions per item processed. However, the BPR, based on 1992 costs, produced cost per unit figures for the manual posting of performances and it is these cost per unit figures which are used in Table 6.24. (The BPR cost calculations (see paragraphs 6.40 and 6.41) did not take into account auto-matched performances.) The BPR noted that in many cases a work unit statistic indicates performances posted where a single posting can represent multiple performances having taken place. Hence, the unit cost is the cost of a single performance *posting*. Therefore, the unit costs shown in Table 6.24 may be somewhat overstated. The performance posting cost expressed as a percentage of revenue is based on 1993 costs incurred. The cash values for the broadcasts have been taken from distribution D941 which covered performances in the period July to December 1993.

6.167. As can be seen, in most cases works with a duration of one minute do not bear the full cost of posting the performance when costs are allocated on a revenue basis. Conversely, works lasting three minutes or more bear more than the true cost of posting the work. The differential will be even more marked in the case of the performance of commercials where several performances will be posted at the same time based on information as to the number of showings of a particular commercial.

6.168. There is obviously a cross-subsidy here between works. Whether or not it affects the distribution of income between members depends on whether the longer works are concentrated among a few members or spread over a large number of the members.

TABLE 6.24 Illustrative examples for cost of posting performances

	Duration			£
	1 minute	3 minutes	20 minutes	
<i>BBC TV</i>				
Gross revenue:				
-featured	81.18	243.53	1,623.55	
-background	57.99	173.95	1,159.68	
-interval	11.60	34.79	231.94	
Cost of posting performances at 0.97% of revenue:				
-featured	0.79	2.36	15.7	
-background	0.56	1.69	11.2	
-interval	0.11	0.34	2.2	
Cost of posting performances per unit per BPR	<u>0.57</u>	<u>0.57</u>	<u>0.57</u>	
<i>GMTV</i>				
Gross revenue	9.65	28.99	193.20	
Cost of posting performances:				
-at 4.42% of revenue	0.43	1.28	8.54	
-per unit per BPR	<u>0.37</u>	<u>0.37</u>	<u>0.37</u>	
<i>BBC Radio 1</i>				
Gross revenue	10.61	50.96	407.68	
Cost of posting performances:				
-at 0.49% of revenue	0.05	0.25	2.00	
-per unit per BPR	<u>0.11</u>	<u>0.11</u>	<u>0.11</u>	
<i>ILR West Sound</i>				
Gross revenue	2.18	10.46	83.68	
Cost of posting performances:				
-at 2.86% of revenue	0.06	0.30	2.39	
-per unit per BPR	<u>0.13</u>	<u>0.13</u>	<u>0.13</u>	

Source: MMC based on PRS information.

Live performances

6.169. The recovery rate for administration costs on major live pop events is 25 per cent of revenue but is capped at £1,250. The average cost of a major pop event (both direct costs and indirect costs) was calculated by the PRS at £994. Therefore, any concerts which raise revenue for the PRS in excess of £3,976 are subsidizing other performances up to a maximum subsidy of £256. Conversely, a concert which generated just £500 of revenue for the PRS would only contribute £125 to overheads—a shortfall on the average cost of some £869.

6.170. The majority of the shortfall in administration costs recovered from major live pop events is recovered from other sources of public performance revenue (such as discothèques and juke-boxes) with a small amount being recovered from broadcasting revenues.

Broadcasting subsidizing public performance

6.171. The main cost of administering public performances—licensing—is borne entirely by public performance revenue. In addition, certain other costs—logging, posting performances and distribution—are allocated between public performance and broadcasting based on man-hours. Indirect costs are allocated to broadcasting and public performance in proportion to revenue and are significant at some 58 per cent of total costs. Due to the complexity of administration of the public performance revenue compared with the broadcasting revenue and consequently the larger number of people required to be involved, it is not

unreasonable to assume that a greater proportion of the indirect costs relate to public performance than to broadcasting. However, the PRS does not accept this assumption and it should be noted that the amount of indirect costs which relate to public performance rather than broadcasting has not been quantified.

6.172. If the assumption is correct, the broadcasting of works will be subsidizing the public performance of works as the gross revenue generated by the two sources is more or less the same. However, we do not know if those PRS members who receive broadcasting income are a markedly different group from those who receive public performance income. (Some public performance income is distributed using radio logs.) If the two are similar then there will be little cross-subsidy arising between members.

Cross-subsidies due to distribution policies

6.173. Under the LMDP only revenue from significant venues, from major individual events grossing £500 or more of PRS fees, or tours whose aggregate fees reach £500 or more, is distributed based on programme information. Revenue collected from non-significant venues for live performances is placed in the general pot and distributed against radio logs. Therefore, in this instance, the less well-known writer performers playing their own works who have not yet broken into broadcasting will be subsidizing the better-known works which do get air time. As an example, a composer might regularly perform his own works in a public house. The public house will pay the PRS a fee for this and other public performances under its blanket licence. However, the current distribution policies do not enable the composer to collect any of that revenue from the PRS.

6.174. The licence fees paid to the PRS by the broadcasters take into account the audience size of each broadcaster. However, unlike the US collecting society ASCAP, when distributing the income from each broadcaster the PRS does not link the rate paid for the performance of a broadcast work with the time of day that the work is broadcast and hence with the size of the audience. One might expect the performance of works at peak audience times to command higher rates than those broadcast at off-peak times. Hence, those works with wide public appeal are subsidizing those which appeal to a more limited audience. As with some of the other cross-subsidies discussed, this results in a cross-subsidy between works. Whether it also results in a cross-subsidy between members depends on whether the introduction of different rates to reflect the size of audience would have a significant impact on the distribution of income between members.