

# **A Call For Fair Play: Pandora Royalty Wars**

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## **Abstract**

Since the performance right was established by President Roosevelt during the 1909 Copyright reform, setting fair royalty rates for the use of intellectual property has been an ongoing issue for publishers, labels, artists, and songwriters. However, as the recorded music industry has grown and transformed in the digital age, this has become increasingly complicated. Digital transmission of music has revolutionized and facilitated listeners' ability to enjoy their favorite music, making it accessible over countless new mediums, which now require their own set of royalty standards. This project investigates the disparities in royalty rates between the different forms of radio, including terrestrial radio, satellite radio, and Internet radio. More specifically, it analyzes why such variances are actually unsustainable for some companies such as Pandora, who have innovative, valuable business model but very little profit margins.

Since controversy over royalties is a century old issue and includes numerous parties, key aspects of this project will include a thorough explanation of its origins, stakeholders, and how each party is affected by the present circumstances. More importantly, this project aims to establish alternative models for Pandora that could help increase revenue and ensure a sustainable future if the legal advocacy campaign is not successful. Results from a survey sent to the primary demographic for Pandora listeners will help establish models that support revenue growth without diminishing the site's quality, purpose, or number of site users.

## Introduction

For over a century, radio has been an omnipresent part of people's lives. In fact, for quite some time, radio was the primary source of entertainment and news. Of course, with the advancement of technology, other mediums of entertainment, such as television, have permeated into our daily routines making radio seem less prevalent. Despite this, radio still thrives with over 90% of people over the age of 6 listening to the radio every week<sup>13</sup>. With such a popular agency for recreational listening, radios soon grew from the household to cars, reaching 96% of automobile users. It is therefore no stretch of the imagination that with the creation of the Internet, digital music was bound to affect radio.

Presenting listeners with streaming music, either for free or for a monthly subscription, Internet radio has become a competitor for terrestrial and satellite radio for almost 20 years. One of today's most popular models of Internet radio is Pandora, which has been working diligently for 14 years to create a successful and profitable business that caters to each listener's specific taste. Unlike terrestrial radio, it's interactive, personalized, and for the most part, portable. However, as a result of the additional qualities that Internet radio possesses, stations are required to pay performance royalties to SoundExchange, an organization that collects royalties on behalf of the artist or label, which seriously affects their ability to create a profit. It is important to note this, because many webcasters argue that this is a skewed

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<sup>13</sup> Keith, Michael C. "Chapter 1: State of the Fifth Estate." *The Radio Station Broadcast, Satellite & Internet*. 8<sup>th</sup> ed. Burlington, Mass: Focal, 2010. N. pag. Print.

requirement, since terrestrial radio only pays songwriters and publishers. In addition to this, webcasters such as Pandora are required to pay a higher percentage of rates than satellite stations, which are also subject to performance royalty rates. In fact, in 2012, Pandora paid over 60% of its revenue, about \$258.7 million, while satellite stations such as Sirius only paid 12.5%<sup>8</sup>.

Essentially the issue of performance royalty rates amounts to the fear of unfairness for one side or another. If royalty rates are set too high, webcasters' ability to provide music to listeners will be hindered. If rates are set too low, artists and other stakeholders are being cheated of the monetary returns they have worked hard to earn. That being said, the vast difference in royalty rates required by different mediums of radio creates an unfair bias towards certain business models, limits potential revenue, stifles innovation and restricts ability to hear new artists. Though it is unrealistic to have equal rates across all forms, royalty rates for Internet radio should be lowered so that they are more comparable with that of satellite radio, in order to preserve an effective form of radio entertainment. If this cannot be done, Pandora must establish changes to its current model to cultivate a serious growth in revenue.

## **Changes in the Recorded Music Industry & Radio**

It's important to note that the transition from terrestrial and satellite radio to Internet radio is a natural progression for the recorded music industry, and as such, should not be inhibited by current royalty rates. Digital music continues to benefit the

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<sup>8</sup> Christman, Ed, Alex Pham, and Glenn Peoples. "The Pandora Wars." *Billboard* 10 Aug. 2013: n. pag. Print.

music industry by expanding global audiences, bettering consumer experiences, and enabling the use of new and more convenient devices<sup>9</sup>. It benefits numerous industries including but not limited to “digital and social media platforms, device manufacturers search engines, retailers and entertainment venues, broadcasters, merchandisers, and concert promoters”<sup>9</sup>. In fact, the recorded music industry realizes the value of the transition to the digital world and invests about 26% of its revenues back into it. Beyond this, artists stimulate an incredible amount of commentary on music using the digital world, comprising 67% of social media discussions<sup>9</sup>. In other words, music is both an impressive asset and part of the digital world.

It is only natural then that digital music translated to the next generation of radio: Internet radio. Now, unlike terrestrial radio, which has limited stations to broadcast from, web casters have limitless channels to utilize. In 2012, a study showed that 39% of Americans listened to Internet radio in just one month<sup>25</sup>. According to Warner Music Group’s Stephen Bryan, “half of music consumers prefer a lean-back, radio style experience. There is a big opportunity to migrate these consumers to digital radio services and make it very convenient to discover new music and build a collection.”<sup>9</sup> And that’s exactly what Pandora is doing. As of 2013, Pandora represents 8% of all radio

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<sup>9</sup> Domingo, Placido, and Frances Moore, comps. *IFPI Digital Music Report 2013: Engine of a Digital World*. Rep. 10th ed. N.p.: n.p., 2013. Print. Digital Music Report.

<sup>25</sup> Villasenor, John. "Digital Music Broadcast Royalties-The Case for a Level Playing Field." *Issues in Technology Innovation* 12 (n.d.): n. pag. Web.

<sup>9</sup> Domingo, Placido, and Frances Moore, comps. *IFPI Digital Music Report 2013: Engine of a Digital World*. Rep. 10th ed. N.p.: n.p., 2013. Print. Digital Music Report.

listeners, primarily between the ages of 18-25 years and continues to grow annually, showing an increase of 2.4% in one year<sup>8</sup>. A predominant factor in Pandora's ability to reach and grow its user-base is its ability to be digitally portable. With the advancement of technology, Pandora has the capability of reaching users via 60 brands of cars and 650 home consumer goods, including cell phones and tablets. In other words, Internet radio is able to not only infiltrate long-established areas of radio listening, but also in homes, on the go, and essentially wherever one chooses.

## **Pandora**

Beginning in 2000, Pandora has worked hard to fulfill its mission to "play only music you'll love". Based on its 73.4 million registered active listeners, it would seem as though it is succeeding. But what makes them so unique? Pandora has set itself apart from terrestrial radio, satellite radio, and even other forms of Internet radio. It has established itself as a truly innovative company by constructing the station to cater to all three parties involved: the listeners, the artists, and the advertisers.

Pandora has been working for over a decade to perfect and grow its Music Genome Project, which to date remains as the most extensive analysis of music. Through this project, Pandora has established a system to create countless playlists to cater to the listeners' personal music desires. A team of music analysts listens to every song in Pandora's library and collects details about each, such as "melody, harmony, vocals,

instrumentation, rhythm, and lyrics”<sup>1</sup>, which then allows each song to be matched to countless playlists based on these characteristics. This permits each user to have a targeted series of songs based on the initial selection of a song, composer, genre, etc. What’s more outstanding, however, is that Pandora furthers this personalized selection process by making it interactive. Users can click a “thumbs up” or “thumbs down” icon to let Pandora know which songs they do or do not like, enabling Pandora to cultivate an even more individualized series of songs. Users can ultimately create up to 100 stations through this method. Terrestrial radio, on the other hand, is controlled by a DJ, and typically results to playing top hits, songs of only one genre, or songs that cater to the location of the station. This therefore means that the choice is in the hand of the listener, which makes Pandora not only idiosyncratic, but also truly user-friendly. Its labor-intensive system demonstrates that Pandora’s prime focus is to put together stations based on individual desires and musical characteristics, rather than pushing a commonplace playlist with repetitive song choices.

Its unique technique is not the only reason Pandora has flourished. Its “freemium” model has certainly played to its benefit, because it has added value to the more traditional radio forms, terrestrial radio or satellite radio, and yet it’s still free. Of course an organization cannot survive by simply offering a free product, which is why advertisements have become an integral part of Pandora’s business. Because Pandora has, as previously noted, a visual interactive aspect, ads can be both visual and audio, which is a huge asset to potential advertisers. What sets it apart from terrestrial radio on

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<sup>1</sup> “About the Music Genome Project.” N.p., n.d. Web. 05 Feb. 2014

the consumer-side, however, is that terrestrial radio plays five to ten times more ads per hour than Pandora<sup>13</sup>. Furthermore, Pandora offers a monthly subscription called *Pandora One*. For \$3.99 a month, listeners can listen to hours of music ad-free at a higher quality. And though many would still choose the free model, an article by the Harvard Business Review comments that by offering both models, businesses can draw in a much larger customer base. According to the article, a “freemium” model draws in a “critical mass” that then draws in a second audience base that is willing to pay for a higher-quality version of the product<sup>26</sup>.

The business is not so simple, however. Artists, labels, publishers, and songwriters assert that they are receiving insufficient rewards for their intellectual property. In 2012, it was discovered that songwriters for well-known performers such as Beyoncé and Christina Aguilera, obtained a mere \$587.39 in royalties for 33 million plays for one song on Pandora<sup>18</sup>. Of course this seems unjust, especially considering how crucial performance royalty rates have become for songwriters since the advancement of digital music and the decrease in CD sales. But it is also important to note that very few terrestrial or satellite stations would ever pay this allotment in one month to any artist. Typically, a monetary figure of that size would be for the total monthly royalties to all artists that a terrestrial or satellite station would pay. One must also consider the promotional benefits that Pandora offers for all of these key participants. Pandora’s

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<sup>13</sup> Keith, Michael C. “Chapter 1: State of the Fifth Estate.” *The Radio Station Broadcast, Satellite & Internet*. 8<sup>th</sup> ed. Burlington, Mass: Focal, 2010. N. pag. Print

<sup>26</sup> Gupta, Sunil, and Carl F. Mela. “What Is a Free Customer Worth?” Harvard Business Review (2008). Print.

<sup>18</sup> Sisario, Ben. “Pandora Suit May Upend Century-Old Royalty Plan.” *The New York Times*. The New York Times, 13 Feb. 2014. Web. 07 Apr. 2014.

library is home to over 35,000 artists, including many new and less-popular artists<sup>1</sup>. Unlike terrestrial and satellite radio stations, Pandora's music genome project plays whatever song is most pertinent to the current playlist, regardless of what's popular, bringing light to countless new artists and creating new fan bases. In addition to this, because Pandora utilizes both audio and visual components, for every song played Pandora presents the artist's name and album title, an image of the album cover, and the lyrics. The visual element reaffirms in users mind who the artist is and gives substantial information to find more songs by said artist. In essence, it establishes a connection between listener and artist. Terrestrial and satellite radio cannot offer these supplementary details, giving Pandora, artists, and other stakeholders an incredible advantage.

## **Where It All Began and Key Stakeholders**

February 13, 1915 marked a day in history for songwriters everywhere with the foundation of the American Society of Composers, Authors and Publishers, also known as ASCAP<sup>17</sup>. Prior to this date, songwriters predominantly earned a living from a percentage of sheet music and piano roll sales. While the copyright laws included the right on licensing reproduction, it did not initially include ownership rights on performances up to this point. As part of the 1909 revision of the copyright law,

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<sup>1</sup> "About the Music Genome Project." N.p., n.d. Web. 05 Feb. 2014

<sup>17</sup> Sanjek, Russell, David Sanjek, and Russell Sanjek. "Chapter 13: ASCAP versus the Broadcasters." *Pennies from Heaven: The American Popular Music Business in the Twentieth Century*. New York: Da Capo, 1996. N. pag. Print.



President Roosevelt included the performance right. However, not until *Herbert V. Shanley Co.* was awareness raised about this new right to collect royalties on performance. Finally, legal action was taken. Victor Herbert, a composer of countless popular works including *Naughty Marietta* and *Babes in Toyland*, filed a complaint asserting a monetary compensation for his song being played on a player-piano at Shanley's restaurant<sup>2</sup>. Ultimately the U.S. Supreme Court ruled in favor of Herbert, claiming:

The performance of a copyrighted musical composition in a restaurant or hotel without charge for admission to hear it but as an incident of other entertainment for which the public pays infringes the exclusive right of the owner of the copyright to perform the work publicly for profit under the Act of March 4, 1909, c. 320, § 1(e), 35 Stat. 1075.<sup>12</sup>

As a direct result of Herbert's efforts and victory, ASCAP became a necessary protection for songwriters. From its onset, ASCAP's mission has been, "to assure that music creators are fairly compensated for the public performance of their works and that their rights are properly protected"<sup>3</sup>.

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<sup>2</sup> "ASCAP Is Founded." *History.com*. A&E Television Networks, 13 Mar. 2014. Web. 25 Mar. 2014.

<sup>12</sup> *Herbert V. Shanley Co.* - 242 U.S. 591 (1917). U.S. Supreme Court. 22 Jan. 1917. Print.

<sup>3</sup> "ASCAP." *www.ascap.com*. N.p., n.d. Web. 07 Apr. 2014.

Currently ASCAP is home to 500,000 American composers, songwriters, and publishers<sup>3</sup>, and its library holds 8.5 millions songs totaling to 90% of commercially available songs in the U.S.<sup>20</sup>. ASCAP, and other licensing organizations, preserve their members' rights by providing licenses for all "non-dramatic public performances" under a consent decree from the United States Justice Department<sup>19</sup>. These licenses are called "blanket licenses", which require registered restaurants, radio stations, stores, and other businesses to pay an annual fee for the right to play a song within ASCAP's catalog. From these licenses, ASCAP can then allocate royalties to all its members. In one year alone, ASCAP distributed \$650 million in royalties<sup>3</sup>.

Naturally, ASCAP has not persisted without resistance. As early as 1931, there has been opposition and struggles in determining fair rates. After a lengthy series of back and forth negotiations resulting in practices such as a point system and payola, broadcasters felt as though ASCAP was attempting to monopolize the business, pushing stations to only play songs from competing organizations, such as BMI<sup>17</sup>. BMI, short for Broadcast Music Incorporated, was founded in 1939 to present and protect songwriters' public performances, specifically in genres such as jazz, blues, and country. Like ASCAP, BMI serves as the middleman between songwriters and broadcasters and it currently

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<sup>20</sup> Sisario, Ben. "Proposed Bill Could Change Royalty Rates for Internet Radio." *The New York Times*. The New York Times, 23 Sept. 2012. Web. 1 Apr. 2014

<sup>19</sup> Sisario, Ben. "Pandora Wins a Battle, but the War Over Royalties Continues." *The New York Times*. The New York Times, 20 Mar. 2014. Web. 22 Mar. 2014.

<sup>17</sup> Sanjek, Russell, David Sanjek, and Russell Sanjek. "Chapter 13: ASCAP versus the Broadcasters." *Pennies from Heaven: The American Popular Music Business in the Twentieth Century*. New York: Da Capo, 1996. N. pag. Print.

represents about 8.5 million musical compositions. Eventually the courts ruled in favor of ASCAP, claiming that radio stations must partake in business with ASCAP as it does with other organizations in order to not stifle competition.

However, after almost a century of existence, it has become evident to many that ASCAP is a crucial component to ensuring fair royalty rates for the music industry, and a disintegration of their company would be detrimental for all. In the words of Paul Williams, a former songwriter and now president of ASCAP, "No other organization, and certainly no single publisher, can negotiate, track, collect, distribute and advocate for music creators on the scale that we do, with the same level of accuracy, efficiency and transparency across so many different media platforms."<sup>18</sup>

## **Copyrights, Rates, and Inconsistencies**

The Copyright Royalty Board (CRB) is a government faction that is responsible for setting appropriate rates for copyright licenses. There are presently two different forms of copyright for songs. The first is for musical composition, which is intended for a songwriter and their publishers. The second is for the sound recording copyright, which is held by artists and record labels<sup>25</sup>. Making payola, which involved record companies paying radio stations to play their songs, illegal made many broadcasters unhappy, it also led to their exemption from paying sound recording performance royalties to artists under the Digital Performance Right and Sound Recordings Act of 1995 and later the

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<sup>18</sup> Sisario, Ben. "Pandora Suit May Upend Century-Old Royalty Plan." *The New York Times*. The New York Times, 13 Feb. 2014. Web. 07 Apr. 2014.

<sup>25</sup> Villasenor, John. "Digital Music Broadcast Royalties-The Case for a Level Playing Field." *Issues in Technology Innovation* 12 (n.d.): n. pag. Web

Digital Millennium Copyright Act of 1998. Typically musical composition rates are paid to ASCAP or BMI, and the sound recording rates are paid to SoundExchange.

While terrestrial radio benefited from these acts, satellite radio and webcasters were not so fortunate. Under the DMCA of 1998, copyright law was altered to include two different standards. The first, “Pre-existing satellite digital audio radio service”, such as Sirius XM, were held to the 801(b) standard. This section incorporates the following objectives:

- A. *To maximize the availability of creative works to the public.*
- B. *To afford the copyright owner a fair return for his or her creative work and the copyright user a fair income under existing economic conditions.*
- C. *To reflect the relative roles of the copyright owner and the copyright user in the product made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, risk, and contribution to the opening of new markets for creative expression and media for the communication.*
- D. *To minimize any disruptive impact on the structure of the industries involved and on generally prevailing industry practices.* <sup>25</sup>

The second, “New subscription services” and “eligible non-subscription transmissions”, such as webcasters, were to be enforced by the “willing-buyer and willing-seller” principle, which states the following:

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<sup>25</sup> Villasenor, John. "Digital Music Broadcast Royalties-The Case for a Level Playing Field." *Issues in Technology Innovation* 12 (n.d.): n. pag. Web.

*In determining such rates and terms, the Copyright Royalty Judges shall establish rates and terms that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller. In determining such rates and terms, the Copyright Royalty Judges shall base its decision on economic, competitive and programming information presented by the parties, including—*

- (i) Whether use of the service may substitute for or may promote the sales of phonorecords or otherwise may interfere with or may enhance the sound recording copyright owner's other streams of revenue from its sound recordings; and*
- (ii) The relative roles of the copyright owner and the transmitting entity in the copyrighted work and the service made available to the public with respect to relative creative contribution, technological contribution, capital investment, cost, and risk.<sup>25</sup>*

In 2007, the Copyright Royalty Board determined that rates for sound recording royalties would not be paid as a percentage of revenue, but rather as a per performance fee. During this year webcasters, such as Pandora, would be required to pay a \$0.0011 per performance and by 2010 they would be required to pay \$0.0019 per performance<sup>25</sup>. Though the CRB claimed the per-performance rates would benefit webcasters, they are in actuality detrimental to the financial stability of countless

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<sup>25</sup> Villasenor, John. "Digital Music Broadcast Royalties-The Case for a Level Playing Field." *Issues in Technology Innovation* 12 (n.d.): n. pag. Web.

webcasters and Pandora in particular. After the 2007 change in rates, Pandora collected a \$0.0004 per performance marginal profit. In other words, money spent on sound recording performance royalties amounted to 40% of Pandora's revenue and would decrease profit margins by 46%<sup>24</sup>; and this was just in 2007. By 2010, these rates would increase causing Pandora to lose money for each song it played.

In addition to the laws established in 1995 and 1998, the Webcasters Act of 2009 also instituted methods of royalty payments for sound recording royalties. It was decided under this act that webcasters had to pay the more profitable of two choices: a minimum of 25% of its revenue to labels or a per-listener rate of \$0.0012<sup>20</sup>. Sirius radio, a satellite station, only had to pay 12.5% of its revenue. However, in reality, Pandora paid 60% in 2012. Originally Pandora hoped to break even by the time it reached 7.5 million listeners. However, under CRB's change in regulations, Pandora can now only hope to break even by 13.8 million listeners at minimum.

## **Recent Happenings**

Pandora's popularity is continuing to grow, which means that its audience could reach up to 2 billion listeners as of 2015<sup>8</sup>. While this is an incredible growth in a relatively short period of time, it could result in serious financial troubles. As such, on

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<sup>24</sup> Villasenor, John. "New Legislation Might Finally Fix the Messy Internet-Radio Royalty System." *Slate Magazine*. N.p., 24 Sept. 2012. Web. 03 Apr. 2014.

<sup>20</sup> Sisario, Ben. "Proposed Bill Could Change Royalty Rates for Internet Radio." *The New York Times*. The New York Times, 23 Sept. 2012. Web. 1 Apr. 2014.

<sup>8</sup> Christman, Ed, Alex Pham, and Glenn Peoples. "The Pandora Wars." *Billboard* 10 Aug. 2013: n. pag. Print.

June 11, 2013, Pandora acquired KXMZ-FM, a terrestrial radio station in South Dakota. By procuring KXMZ, Pandora seeks to obtain a Radio Music License Committee license. The RMLC, a non-profit organization that parallels the intentions of organizations such as ASCAP and BMI, works on behalf of radio broadcasters to attain fair license fees. In fact, RMLC, ASCAP, and BMI work together to negotiate rates that are appropriate for all participants. Pandora hopes its purchase of KXMZ, and therefore its license with RMLC, will result in lower rates based on the precedent set by iHeartRadio, who paid the reduced rate of 1.7% to ASCAP and BMI due to their ownership of several terrestrial radio stations<sup>8</sup>.

This strategic move by Pandora has earned considerable reproach. The National Music Publishers' Association president, David Israelite states, "Any shred of credibility that Pandora had as the songwriter's partner is now gone."<sup>8</sup> In fact, the issue was taken to the Federal Communications Commission to decide the matter. On March 14, 2014 the rate court judge arbitrated that Pandora will continue to pay the 1.85% of its annual revenue to ASCAP, despite ASCAP's assertion that it should receive 3%<sup>7</sup>. This is a clear win for Pandora, and yet it is still on the higher end of what Pandora could have hoped for, and still higher than iHeartRadio's rates. Countless publishers have attempted to relinquish their digital rights with ASCAP and BMI in order to avoid this rate, but to no

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<sup>8</sup> Christman, Ed, Alex Pham, and Glenn Peoples. "The Pandora Wars." *Billboard* 10 Aug. 2013: n. pag. Print.

<sup>7</sup> Christman, Ed. "Rate Court Judge Rules Pandora Will Pay ASCAP 1.85% Annual Revenue." *Billboard*. N.p., 14 Mar. 2014. Web. 14 Mar. 2014.

avail. It doesn't seem, however, that this will be the end of this debate once Pandora's license ceases on December 31, 2015.

In similar news, SoundExchange has recently released its 2014 rates for statutory licensing. For commercial webcasters, such as Pandora, must comply with the following<sup>27</sup>:

**Minimum Fees.**

1. **Amount:** \$500, per station or channel, not to exceed \$50,000 (if a service has more than 100 stations or channels). All payments must be accompanied by a signed and completed minimum fee Statement of Account.
2. **Recoupability of Minimum Fee:** The minimum fee is credited against monthly liability accrued within the same calendar year. Services do not submit additional payment for that year until they have exceeded the minimum fee.
3. **Due date:** Annual, on or before January 31. New services beginning streaming on or after February 1 are required to pay minimum fees within 45 days after the end of the month in which streaming first occurs.

**Liability Rate, Payment and Statements of Account.**

1. **Rate:**
  1. **2014:** \$0.0023 per performance
  2. **2015:** \$0.0023 per performance

## **SWOT Analysis of Pandora**

In order to properly analyze where Pandora stands in the digital music industry and how it can better itself, it is important to recognize both its positive aspects and where it can better itself. Besides the aforementioned advantages of Pandora, there are several other notable characteristics. First and foremost, it is the leading model of

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<sup>27</sup> "SoundExchange 2014 Rates." *SoundExchange*. N.p., n.d. Web. 05 Mar. 2014.



Internet radio. It has exceeded all other forms of webcasting, both in finances and popularity, and it has established itself as an innovative business model. Additionally, as a result of its portable capabilities, it has become one of the three top companies, just behind Google and Facebook, in mobile advertising revenue. Likewise, it has countless opportunities that it can and should exploit. On account of its success with mobile advertising, it is in a sound position to obtain a share of the broadcast radio advertising. Furthermore, it is now available in 100 car models, and to date has had 2.5 million users take advantage of this feature. This is extremely crucial, considering half of radio listening occurs in cars<sup>13</sup>. More importantly, however, as this seriously sets itself apart from other radio forms, Pandora is accessible by mobile phones. In the United States mobile service industry, 41% of phone products are now smart phones<sup>8</sup>, which is an incredibly large market for Pandora to access. Lastly, its ability to expand internationally is staggering. Because Pandora, unlike American terrestrial and satellite radio stations, can be accessed through the internet and mobile phones, the same stations generated by the Music Genome Project can be retrieved essentially anywhere.

Despite its many strong points, Pandora also has one major weakness, aside from its inability to reduce royalty rates in the near future. Though Pandora has the opportunity to embrace mobile ad revenue, for example, through cell phones and tablets, this in turn means a decrease in desktop ad revenue. It has become apparent that companies are leaning towards buying ad space on mobile devices more often than on

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<sup>13</sup> Keith, Michael C. "Chapter 1: State of the Fifth Estate." *The Radio Station Broadcast, Satellite & Internet*. 8<sup>th</sup> ed. Burlington, Mass: Focal, 2010. N. pag. Print.

<sup>8</sup> Christman, Ed, Alex Pham, and Glenn Peoples. "The Pandora Wars." *Billboard* 10 Aug. 2013: n. pag. Print.

desktop sites. According to a recent New York Times article, desktop ad spending will decrease by \$1.4 billion during 2014, which is a 9.4% reduction from 2013 <sup>20</sup>. This may prove to be detrimental to Pandora, who was initially created as a desktop application.

What's more, Pandora has several potential threats to its business. Especially with the current royalty rate discrepancies, radio adversaries' growth, such as Sirius XM and iTunes Radio, could prove to be an unwelcomed competition to Pandora during a time of financial distress. It should also be noted, that iTunes Radio royalty rates, unlike Pandora, have been arranged directly with labels and publishers, which may prove to be beneficial for them. Additionally, if Pandora seeks to grow its revenue by increasing advertisements, its primary source of income, it is likely that the ads could be interpreted as a hindrance and deter old and new listeners. Finally, in recent years artists and rights owner groups have begun utilizing public relations as a platform to deter the use of Internet radio as the predominant medium of music listening. As long as Pandora remains in its current financial system negative press can only further burden them.

## **Suggested Areas of Improvements and Methods**

Based on the analysis I have extracted from Pandora's strengths, weaknesses, opportunities, and threats, there are several broad areas of improvement I would recommend for Pandora's business model in order to enhance its revenue stream. To determine what solutions would work best, I created a survey (i.e Figure 1) to better

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<sup>20</sup> Sisario, Ben. "Proposed Bill Could Change Royalty Rates for Internet Radio." *The New York Times*. The New York Times, 23 Sept. 2012. Web. 1 Apr. 2014.

understand people's listening preferences. My survey was composed of twelve questions, either multiple choice or "yes" or "no", that were targeted to interpret what actual users would approve as a change without stopping their use of Pandora. Composed on Survey Monkey, it was sent out over the course of several weeks via email.

Questions 1 and 2 asked their age and gender since Pandora's primary listening base is between the ages of 18-25. All encompassing, however, my subjects ranged in age from 18-25, 25-40, 41-60, and 61 and over. This would allow me to see how relevant my results would be. I then wanted to know how often people listen to music on a weekly basis and how many actually purchased the music they listened to, rather than listening to it for free. I felt that this question would allow me to comprehend the likelihood of any subscriptions being bought, in order to deduce whether a change in subscriptions was a worthy suggestion. Questions 3 and 4, made the previous questions more pertinent to Pandora by asking how many of the hours spent listening to music was done so via radio. Questions 5 and 6 supplement this idea even more by inquiring what form of radio, terrestrial, satellite or Internet, users preferred using and if they already had a subscription to either satellite radio or Pandora.

I then shifted the focus to test what new implementations would either attract or deter users. In particular, I queried if current ad volume was acceptable or too much in order to ascertain whether or not increased ad volume would discourage users. Similarly, I asked if the re-implementation of a 40-hour music listening cap would push people away. The next set of questions was targeted towards artists. Specifically, I wanted to know how many of those polled were involved in the creation of music, and of those that were, would they be willing to pay Pandora for a heightened involvement

with the site. Finally, to close my survey, I decided to give my subjects a chance to share their own opinions and contribute what, if anything, would prompt them to purchase a Pandora subscription. As such, I offered them several answer options, such as lowering the fee from \$3.99 to \$2.99 per month, the option of music videos, more interactivity, more skips, and lastly an “other” choice, which allowed my subjects to recommend suggestions of their own.

## **Results**

For the most part my results corresponded well to my original suggestion plans. Of a total of 100 people surveyed, about 70% were between the ages of 18-25 (i.e. Figure 2). This was pivotal for my results, because this meant that I was dealing with Pandora’s target audience. More importantly, it indicated that my results, and ultimately my proposals, would be germane for Pandora. In terms of gender, 55% were female, which therefore didn’t suggest that sex had anything to do with the outcomes (i.e. Figure 3).

For the questions that were concentrated on listening preferences, several general and important results were identified. To begin with, a majority of those polled, about 1/3, listened to 10 to 20 hours of music in any given week (i.e. Figure 4). Of these 10-20 hours spent listening to music, a leading group of 40% dedicated 1-3 hours to listening to music via the radio (i.e. Figure 5). Moreover, 63% of my subjects said their radio tendencies leaned towards AM/FM radio (i.e. Figure 6), but Pandora followed closely at 52%. Satellite radio, on the other hand, was only chosen by about 20%. This response was quite important, considering that satellite and Pandora are the only ones that offer a subscription. This meant that listeners simply preferred the model of

Pandora to satellite or that they would be more willing to pay Pandora's fee instead of one for satellite.

For results that were more specific to Pandora I discovered that 35% of my subjects already purchased the \$3.99 monthly subscription (i.e. Figure 8). Additionally, 62% felt that ad volume was "ok" rather than "too much" (i.e. Figure 9), and 75% stated that they wouldn't be affected by a song listening cap being put into affect (i.e. Figure 10). Again, these results in particular were key in my intended suggestions. Moreover, the usage of music videos on the site did not increase the likelihood that a user would purchase a subscription (i.e. Figure 7). That being said, for my final question, a majority proclaimed that of all the reasons listed that would incite them to purchase a subscription, an increased interactivity on the site would be their first choice (i.e. Figure 13). This response therefore signaled that a change in the manner in which Pandora functions was the single most crucial adaptation that needed to occur. This was also an interesting result, because Pandora prides itself on its ability to be interactive for its users. Lastly, but most significantly, was the feedback from the questions aimed at the artists that were polled. Of the 100 surveyed, 38% were in some way involved with creating music (i.e. Figure 11). More importantly, however, a majority of this 38% announced that they would in fact pay a separate fee to Pandora in order to have more involvement or analysis done by the site (i.e. Figure 12).

The comment section on the final question was also quite valuable while determining what changes would be best suited for Pandora. Several of the comments suggested that users would prefer sites with more ability to make their own playlists or even just a greater say in the music that was played, rather than just a thumbs up or a

thumbs down. Furthermore, they offered that the ability to have greater variety within a genre was important to them, as was the potential to look up what other people were listening to. This in particular was interesting, because they noted that the “community feel” within a music site, such as what Spotify offers, was greatly appreciated and encouraged. Another set of comments implied that if the price of a monthly subscription were to decrease to \$2.99 that it would in fact increase their desire to purchase one. However, these same subjects also noted that if the price remained at \$3.99 they would still consider purchasing a subscription should Pandora increase the quality or quantity of what was offered at that price. In other words, the current format of Pandora, as well as what was offered, was insufficient for its current subscription price. On a similar issue, several users commented that increased ad volume would push them to pay for a subscription, but it would not dissuade them from continued use of Pandora.

## **Conclusions and Suggestions**

Based on the conclusions I have drawn from my survey and overall analysis of Pandora’s business model, there is a clear demand for change. While Pandora is currently the leading Internet radio, there are countless streaming sites that offer ideal functions that Pandora is not capitalizing on. Similarly, while Pandora should continue to focus on its musical content and its status as user-friendly, they are not in a secure enough financial situation where they can forego revenue in order to maintain the appearance of an almost commercial free site. As a result, I would put forward several suggestions that Pandora can implement with ease.

First and foremost there is an omnipresent desire for increased interactivity. While my initial reaction was to resolve this through the addition of music videos, my subjects blatantly rejected this. Therefore, I would recommend that Pandora consider offering users the capacity to look up other users activity or be able to share their own activity via social media. At present, you can share an individual song through Facebook or Twitter, but you cannot have a constant feed being shared. Essentially this means more work on the part of the user, which is usually a deterrent. Therefore, if Pandora created a means by which the user would not have to continuously share each song, but rather select the option to have an ongoing stream of shares, Pandora can create an environment in which users can feel constantly connected with one another. They can also offer the option of permitting users to have a greater say in their individual playlist. For instance, if a user were to input an artist into the search box, Pandora could present the listener with the entire list of songs that the Music Genome Project creates. Then, users can either select the songs they want to hear and immediately refuse those that they don't. Additionally Pandora can offer the opportunity for users to put the playlist's songs in whatever order they choose, so that the flow of the playlist is even further catered to the listener's desires.

Another choice Pandora has would be to re-implement a song listening cap. Currently people can listen to unlimited songs, which means that Pandora is responsible for paying royalties for each song played. At one point Pandora put a 40-hour per week listening cap into effect but removed it when its potential for mobile advertisement revenue skyrocketed. Now, however, while Pandora is still generating considerable mobile ad revenue, they are losing far more money to royalty rate fees, proving that they

are no longer in a position of financial success to permit this. If a cap were re-established, whether it's per week or per day, it will reduce the amount of royalties Pandora is required to pay. Moreover, because my subjects indicated that their use of Pandora is averaged at 1-3 hours per week, there is no need to offer an unlimited option for the few that do listen to over this amount. Similarly, these same subjects declared by a clear majority that the use of a listening cap would not deter their usage, demonstrating that its use would only save Pandora money.

A further imperative fact determined from my survey was that a slight increase in ad volume would work. The data gathered from my survey indicates that ad space per hour is tolerable, especially in comparison to terrestrial radio. As such, Pandora is in a favorable position to advance even further in this method of revenue through two opportunities. Based on the fact that Pandora is already a leading company for mobile ad space, Pandora should seize the opportunity to either moderately amplify ads on mobile devices, or increase ads on its desktop version. The latter may be the better option since Pandora hasn't fully recognized it's potential in desktop ad revenue. The comment section of my survey augments this idea, by proving that a raise in ads will not impede any users, but may instead push people to buy a subscription in order to avoid them. Either way, Pandora will benefit, as it will be able to heighten its revenue growth through either advertisers or subscription fees, without losing listeners.

Lastly, and quite interestingly, is the fact that Pandora could improve its revenue by creating a fee for independent artists that submit their music to Pandora. As it stands, artists can submit their songs to be reviewed by the Music Genome Project with the hopes of it being accepted and incorporated into its library. Since the artists I poled



overwhelmingly declared that they would pay for their music to be in Pandora's library, I recommend that Pandora create a supplemental fee option for after an artist's song is approved. In other words, once an artist's work is accepted into the library, they could have the opportunity to pay for spotlight opportunities. An example of this could be ad space on the site's page for an artist's music. Another option could be to have a banner that flows across the top of the site with upcoming information about an artist or a tour. Furthermore, Pandora could offer a fee to have additional information posted about an artist while their song is being played. Pandora's current page layout includes, for each song played, the name of the song, the name of the artist, the album cover, the song lyrics, a brief "about the artist" section, and a list of the top-related artists. Therefore, the fee could include an elongated "about the artist section" or a listing of other songs or albums by the artist. I also encourage the idea of offering a fee for further analysis of an artist's song by the Music Genome Project. This analysis could incorporate how users have responded to a song through the interactive aspect of Pandora or potentially what playlists a song is being put into to get a deeper understanding of what listeners search for in order to find said song. Of all my suggestions, I feel that this would be the most advantageous for Pandora. Unfortunately, due to the current royalty wars, Pandora is being depicted as greedy and lacking support for artists. This method would therefore not only improve its revenue, but it would also show that it is an ally to artists and continue with a precedent that it's already established, which is to not just play popular music, but to play only music that people will love.

## Final Comments

It is unforeseeable that the issue concerning royalty rates for Internet radio will change for the better in the near future. In fact, in addition to its current battles, Pandora has just recently been hit by a lawsuit from the top leading labels in the music industry. The lawsuit is pushing for Pandora to pay royalties to labels and performers for songs created before 1972, since current U.S. copyright law does not include this as a required royalty for Internet radio<sup>15</sup>. In essence, unless Pandora begins to implement changes to its present model or assert new methods for revenue growth, its financial situation will not become any stronger in years to come. Through my general analysis of U.S. copyright law, royalty rate standards, Pandora's business model as a whole, as well as my survey, I would strongly contend that the methods I proposed will only encourage maximal revenue growth. Furthermore, I maintain that all my suggestions will not in anyway decrease the quality of Pandora, and likewise, will not push current users to other Internet radio sites. Pandora has proven itself to be unique and innovative. It is now time for it to re-establish itself as both of these qualities and recreate itself to stand out and above the royalty issues. In short, I would offer if Pandora can't change an issue out of its immediate control, it is time it fix itself.

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<sup>15</sup> "Pandora Hit with Label Lawsuit Over Royalties." *RAIN News*. N.p., n.d. Web. 19 Apr. 2014

**Figure 1**

Music Listening Preferences
<p><b>1. What is your age?</b></p> <p><input type="radio"/> a. 18 – 25</p> <p><input type="radio"/> c. 26 – 40</p> <p><input type="radio"/> d. 41 – 60</p> <p><input type="radio"/> e. 61+</p>
<p><b>2. Indicate your gender</b></p> <p><input type="radio"/> a. Female</p> <p><input type="radio"/> b. Male</p>
<p><b>3. How would describe your music listening preferences</b></p> <p><input type="radio"/> a. Listen to music more than 20 hours a week and buy music frequently</p> <p><input type="radio"/> b. Listen to music more than 20 hours a week but rarely buy music</p> <p><input type="radio"/> c. Listen to music between 10-20 hours a week and buy music frequently</p> <p><input type="radio"/> d. Listen to music between 10-20 hours a week but rarely buy music</p> <p><input type="radio"/> e. Listen to music less than 10 hours a week but buy music frequently</p> <p><input type="radio"/> f. Listen to music less than 10 hours a week and rarely buy music</p>
<p><b>4. Indicate your radio listening habits?</b></p> <p><input type="radio"/> a. Over 10 h per week</p> <p><input type="radio"/> b. 4-10h per week</p> <p><input type="radio"/> c. 1-3h per week</p> <p><input type="radio"/> d. none</p>
<p><b>5. Indicate your radio listening habit</b></p> <p><input type="checkbox"/> a. AM/FM Radio</p> <p><input type="checkbox"/> b. Satellite/XM</p> <p><input type="checkbox"/> c. Pandora</p> <p><input type="checkbox"/> d. Streaming Services</p>
<p><b>6. Would you purchase a subscription if you could view music videos on Pandora?</b></p> <p><input type="radio"/> a. Yes</p> <p><input type="radio"/> b. No</p>

7. 5. Do you purchase subscriptions to any of these services, mark all that apply?

- ☐ a. Satellite/XM
- ☐ b. Pandora
- ☐ c. Streaming Services

8. Is the current ad volume on Pandora

- ☐ a. Too Much
- ☐ b. Ok
- ☐ c. Could handle a few more

9. If Pandora only allowed 40 hours of free listening per week would that limit your current usage?

- ☐ a. Yes
- ☐ b. No

10. If Pandora only allowed 40 hours of free listening per week would that limit your current usage?

- ☐ a. Yes
- ☐ b. No

11. Are you involved in creating music in any way?

- ☐ a. Yes
- ☐ b. No

12. If you answered "Yes" to #9 would you pay a small fee to have your music featured on Pandora?

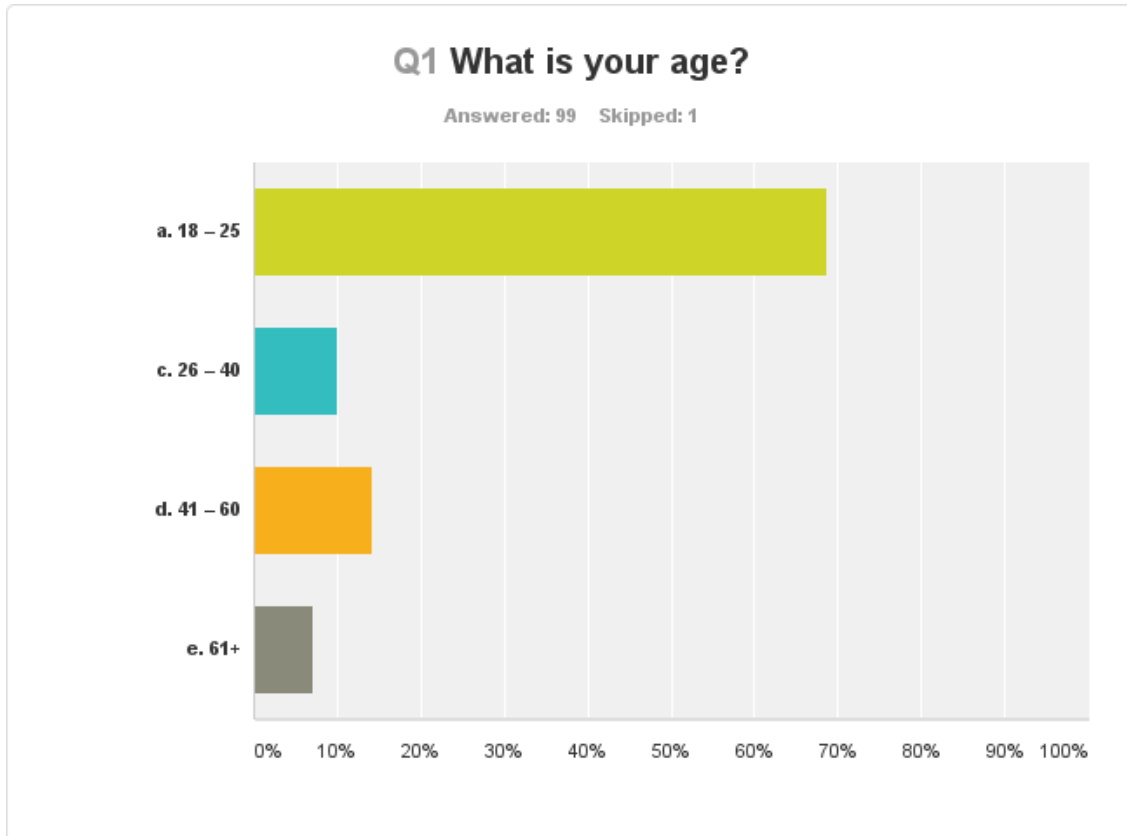
- ☐ a. Yes
- ☐ b. No
- ☐ c. Not Applicable

13. Would any of the following changes help you consider purchasing a subscription to Pandora?

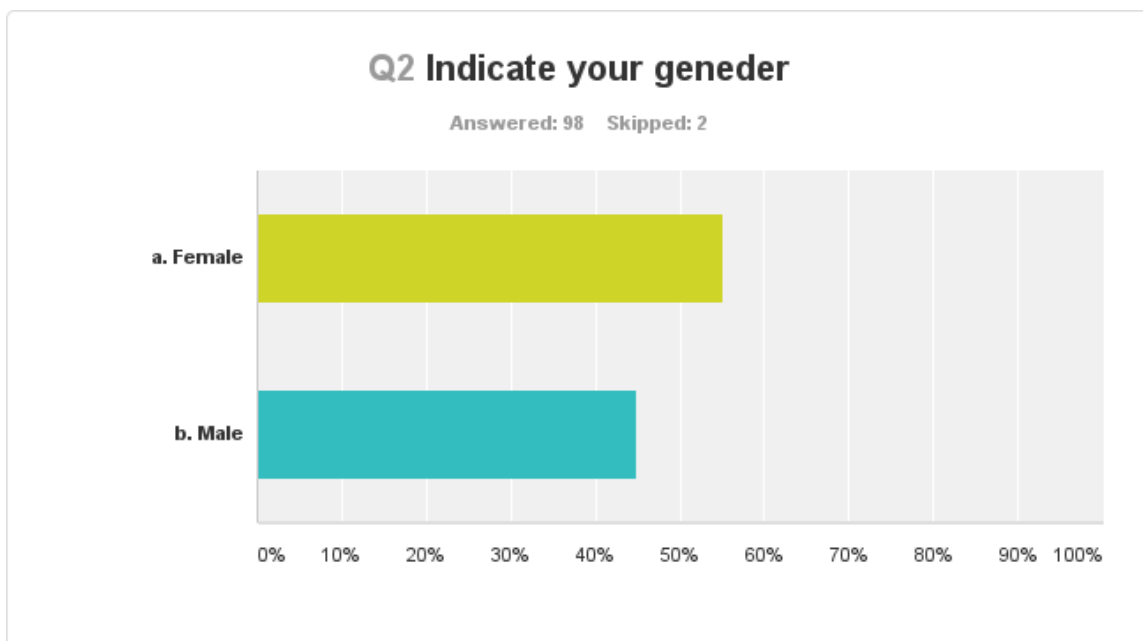
- ☐ a. Lowering the fees from \$3.99 per month to \$2.99 per month
- ☐ b. More interactive options on music choices, such as searching for specific songs, making playlists, sharing music
- ☐ c. Music videos
- ☐ d. Increased options in skipping tracks that come up
- ☐ e. Other suggestions:

Other (please specify)

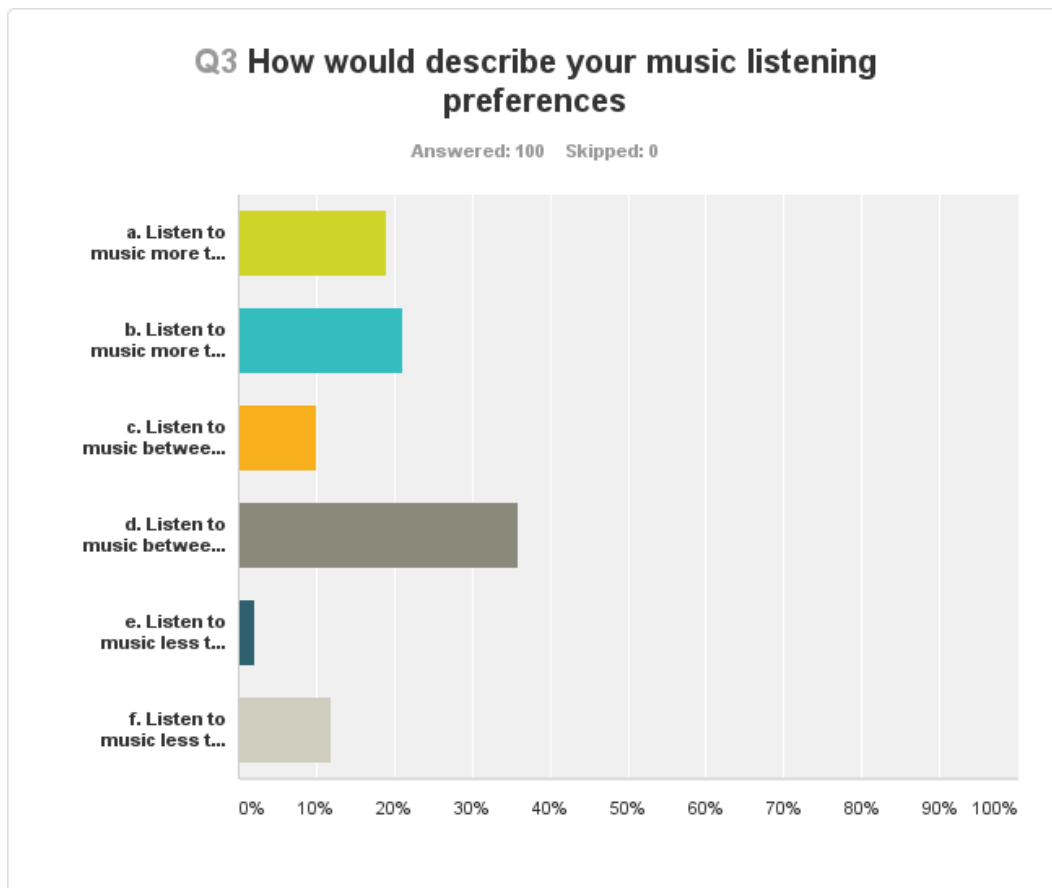
**Figure 2**



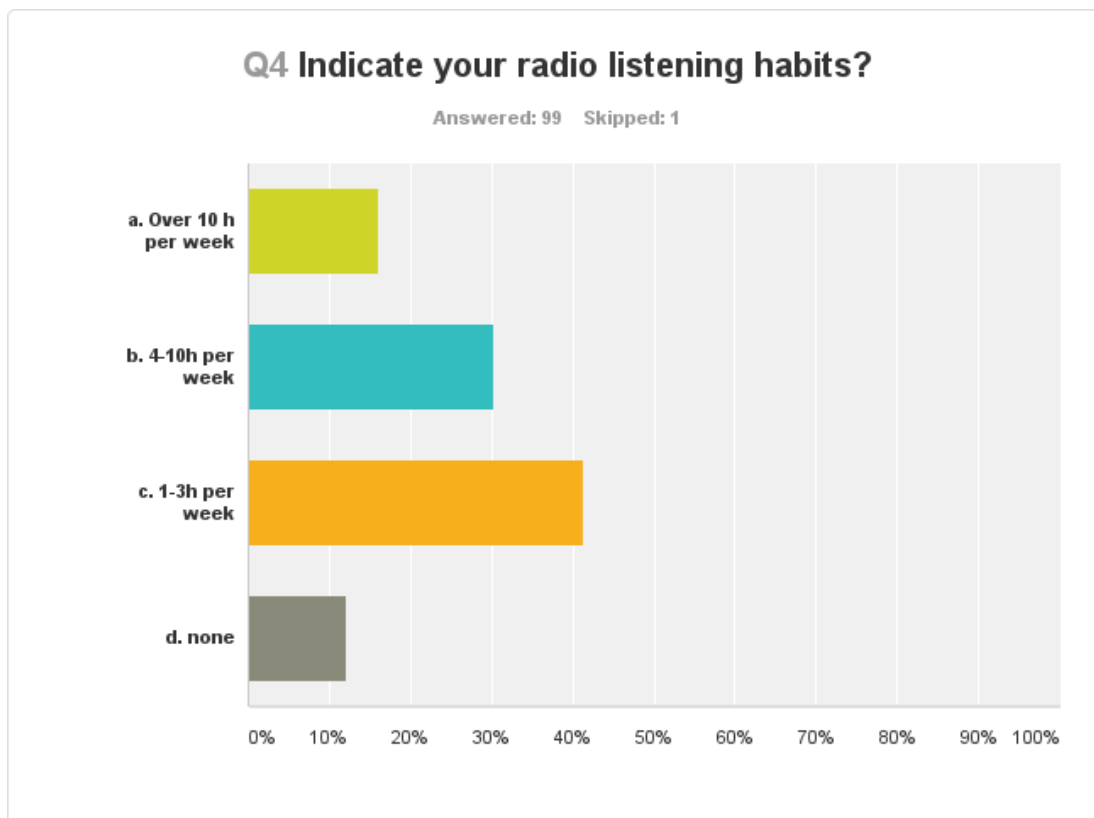
**Figure 3**



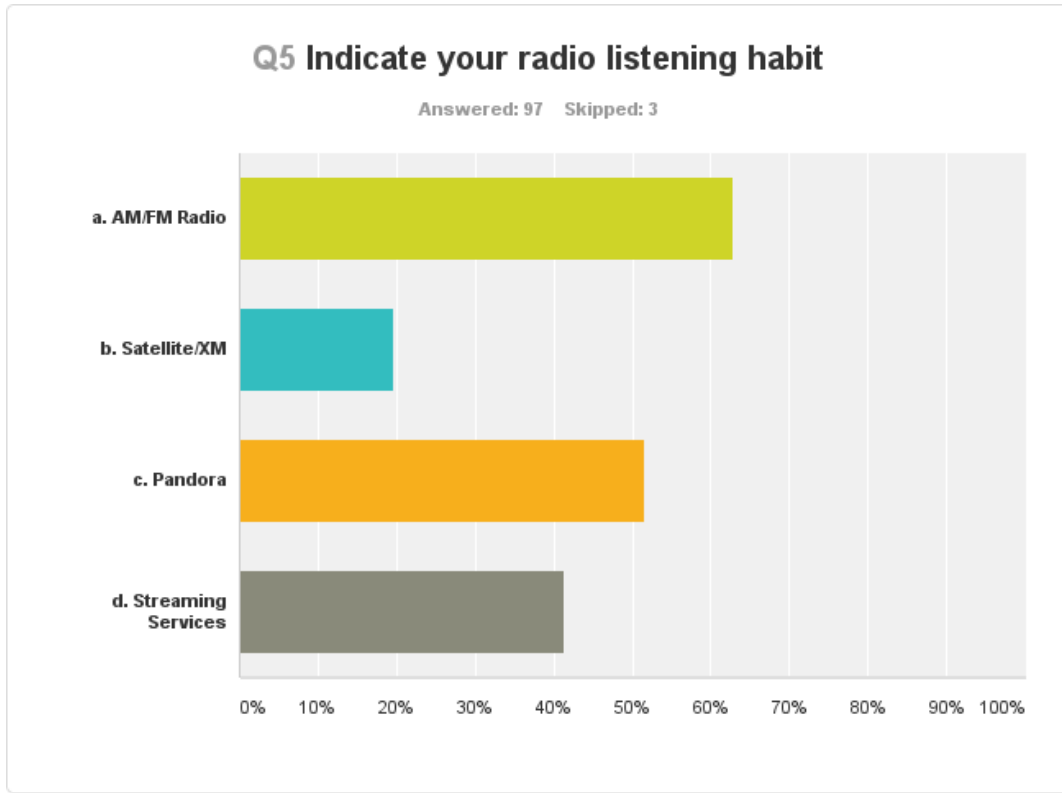
**Figure 4**



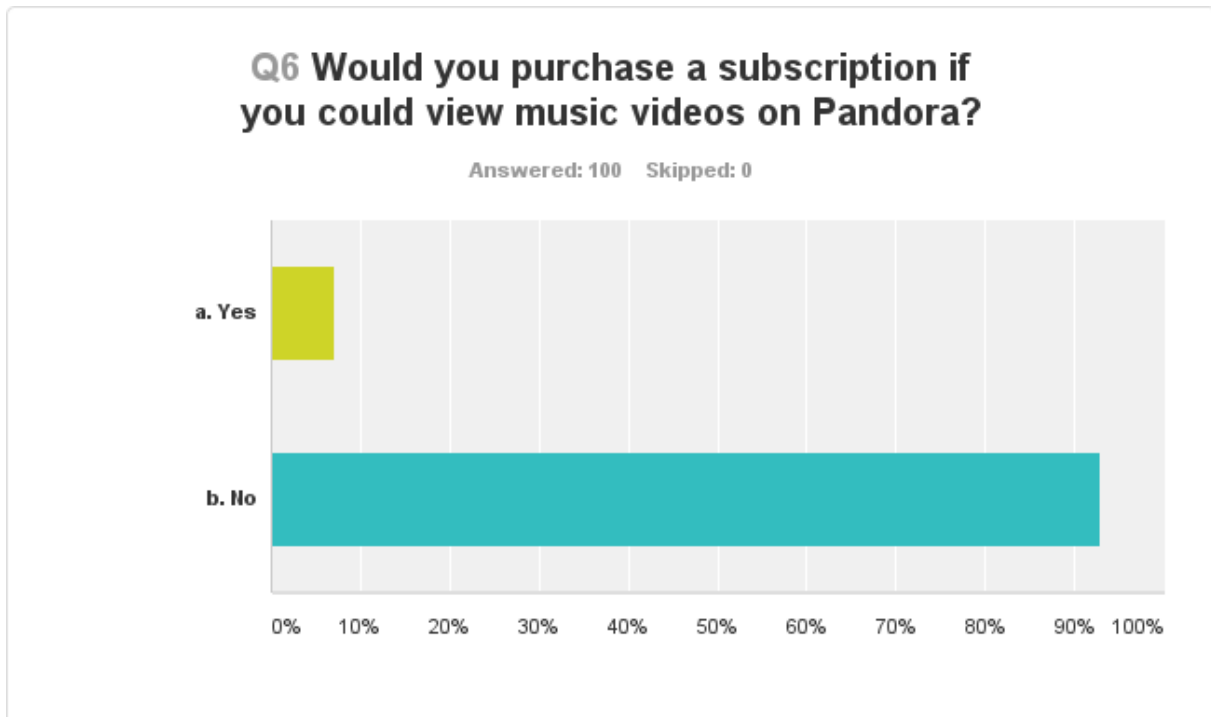
**Figure 5**



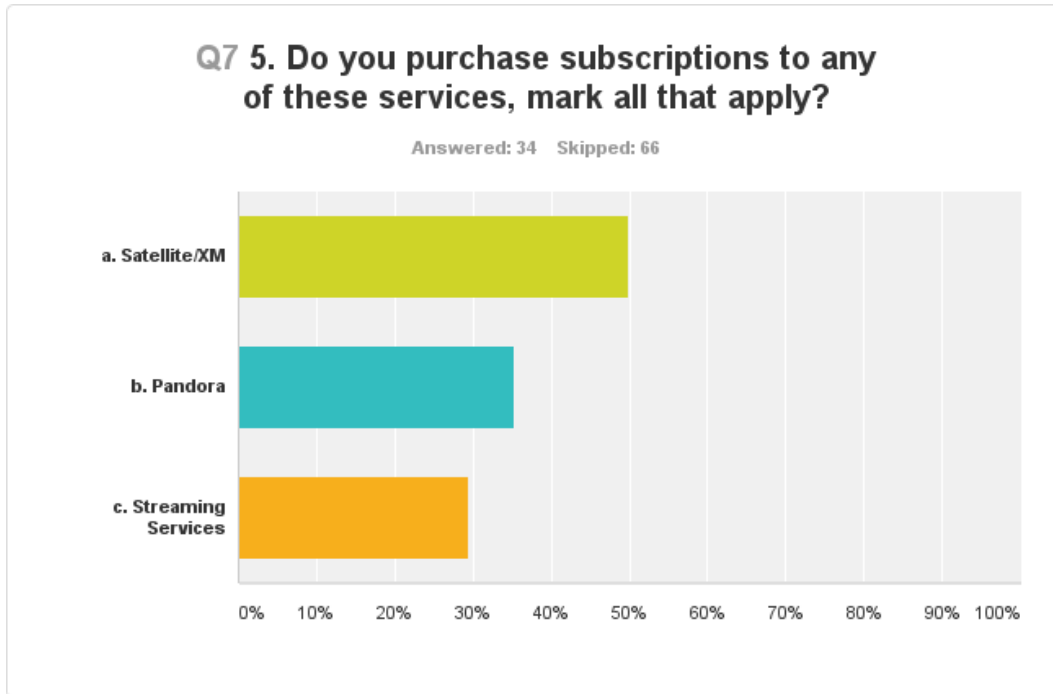
**Figure 6**



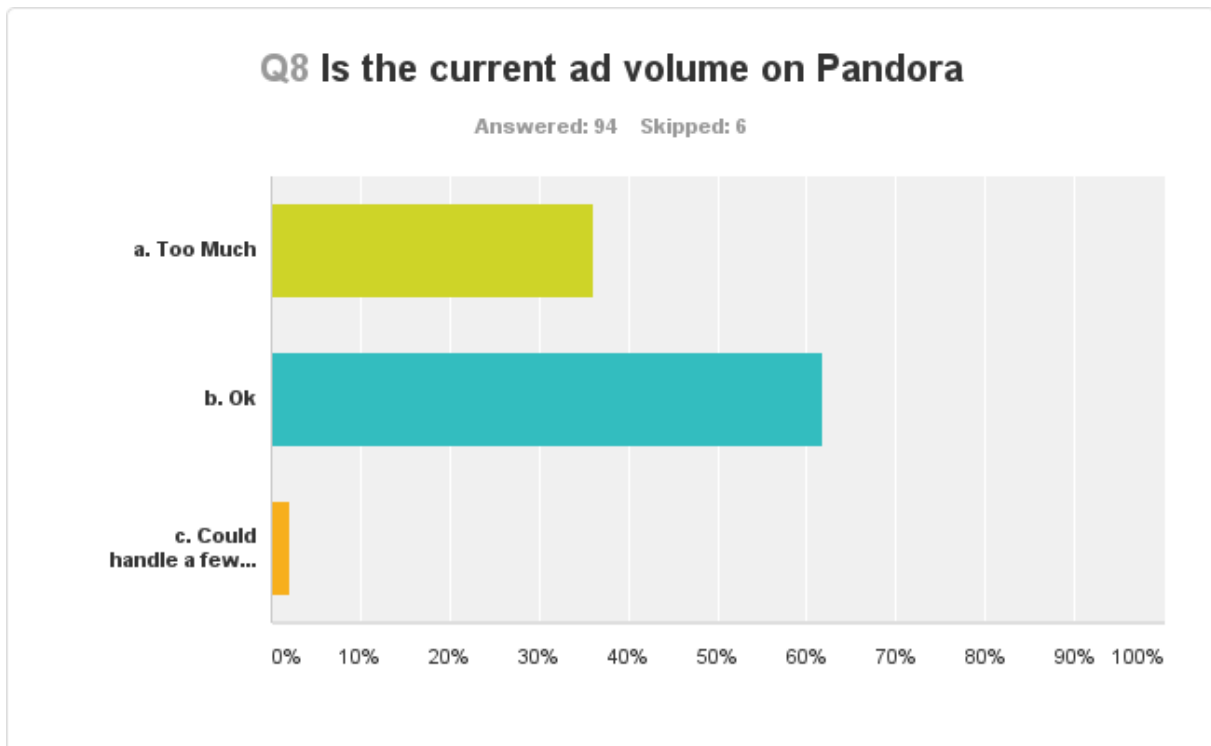
**Figure 7**



**Figure 8**

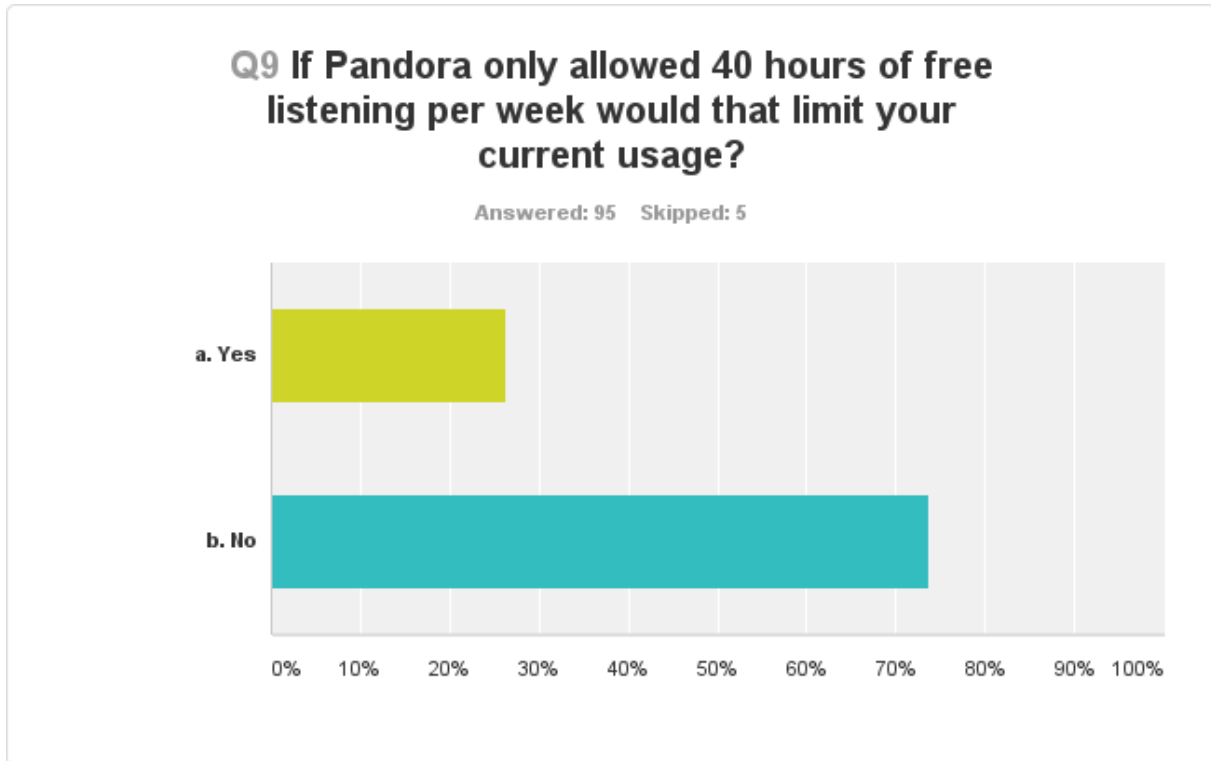


**Figure 9**

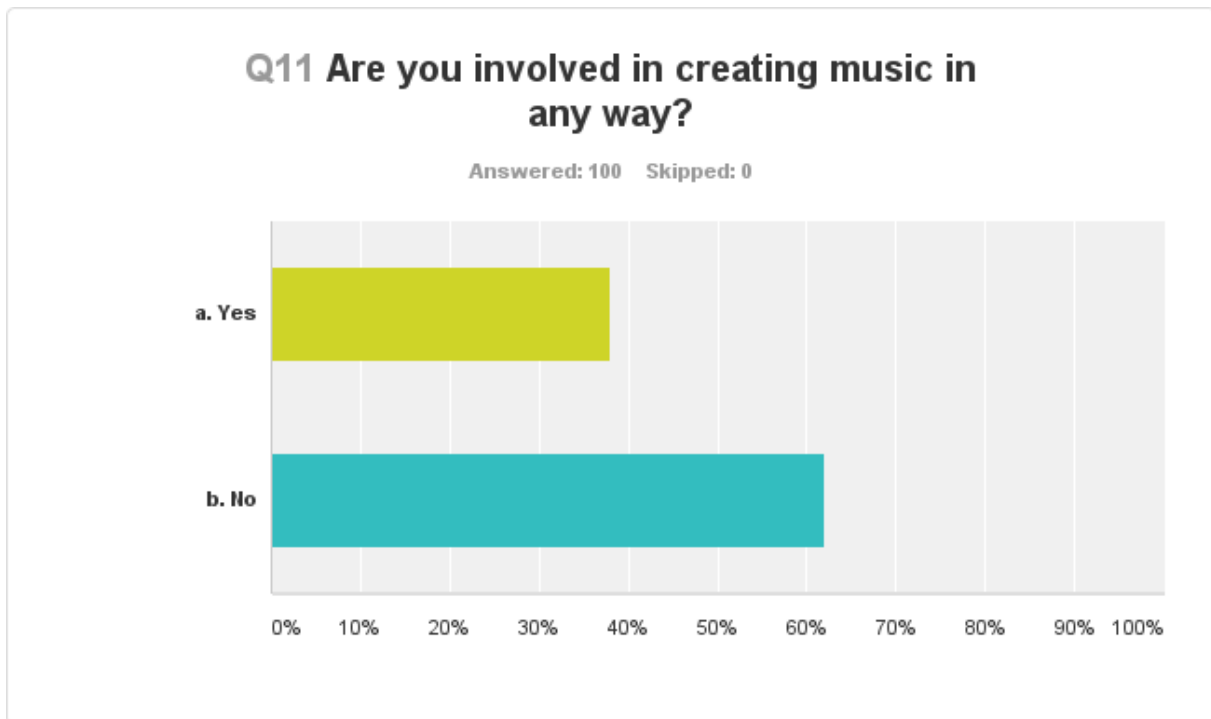




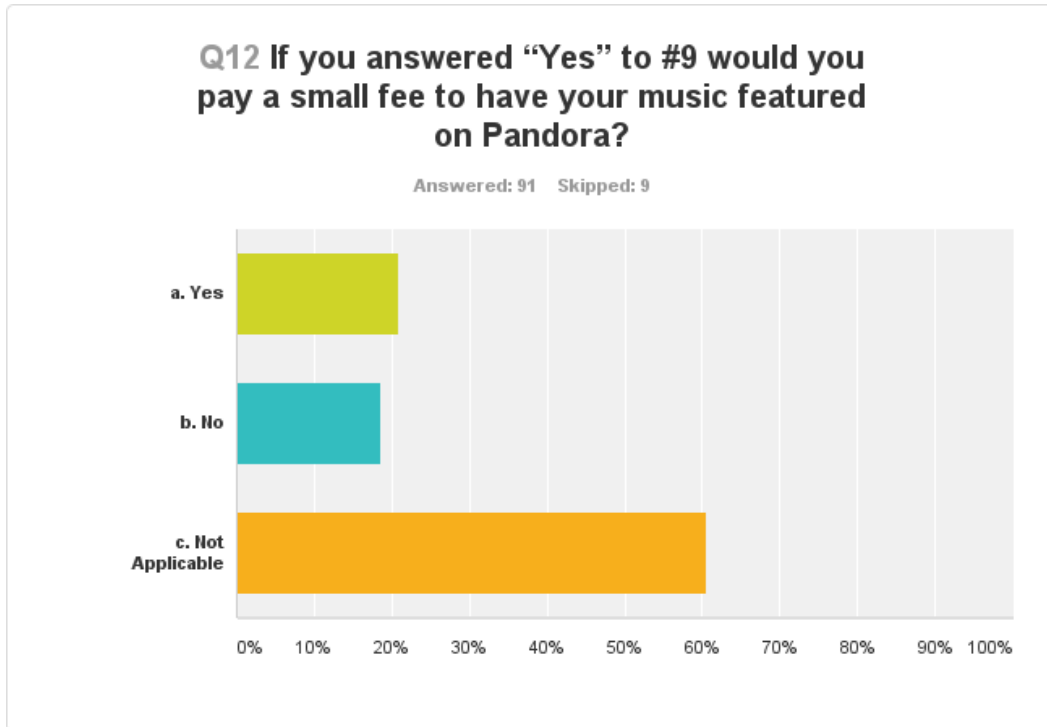
**Figure 10**



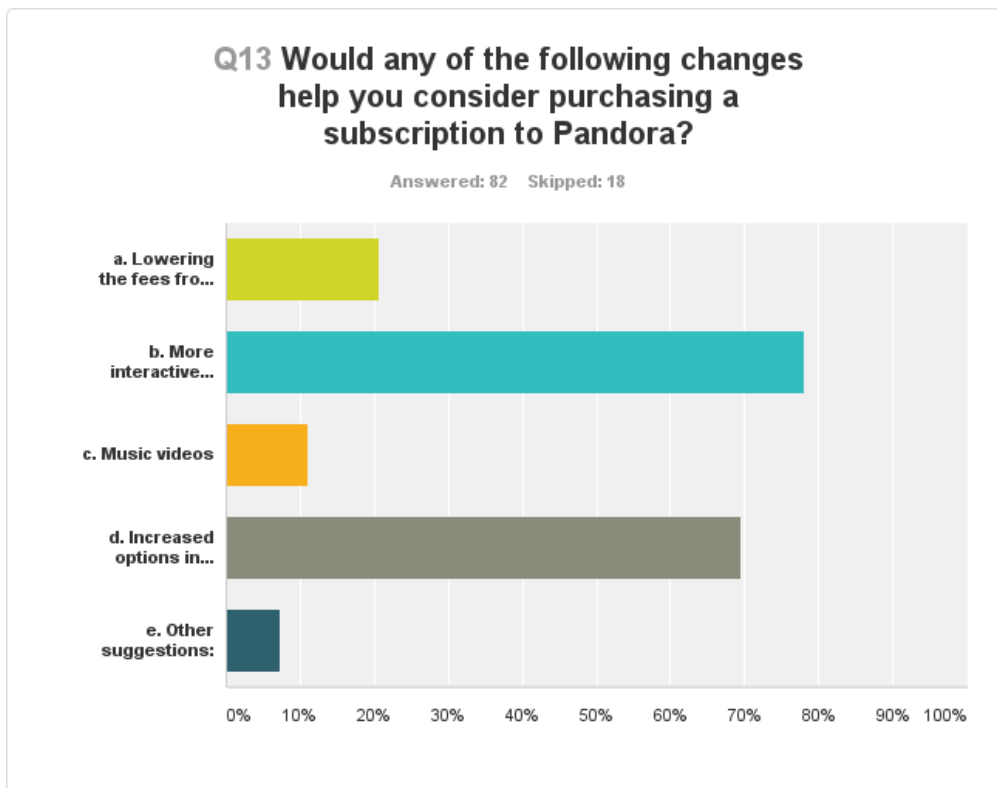
**Figure 11**



**Figure 12**



**Figure 13**



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