

Distribution Agreement Fact Sheet

What is a Distribution Agreement

A distribution agreement states the rules under which an artist or small indie label can have its records and albums manufactured and/or distributed by a specialist distribution company, or the distribution arm of a larger label. The deal also states how funding for manufacture and distribution will work and the ways in which the large company will earn money from sales of the albums.

When do you need a Distribution Agreement

Artists or indie labels should look at entering into a distribution agreement only once they have completed their album and have the final product that they want to release to market.

Why do you need a Distribution Agreement

It can be difficult to promote and sell physical copies of an album or EP by yourself. This is because you would need to enter into contracts with all major music retailers in which you may see yourself paying high rates for selling your CDs to these retailers.

Specialist distributors are well established and have already developed huge networks and negotiate favourable rates with all retailers. By getting your product through distributors you have the opportunity of 'piggy-backing' off their favourable rates as well as having the opportunity to distribute your product to places and through networks you would never have had the chance of securing by yourself. This is the same for both digital and physical distribution.

It's important to note that in a digital world, distribution agreements become less valuable to indies and artists. This is because digital technologies allow individuals many of the same opportunities that major labels have to promote their music over the internet. It is recommended that indies and artists work out whether their distributor has significant networks/skills in the digital environment to warrant using their digital distribution services.

How to use this Fact Sheet and included Checklist

Included with this fact sheet is a checklist of many of the issues the parties should agree on. The checklist will give you a quick idea of the key terms of a distribution agreement whilst this fact sheet provides added details on key clauses. For ease of reference, all clause numbers used in the checklist will be mirrored in this fact sheet.

By referring to both these resources, we believe that you will be in a position to better decide whether or not to sign on that dotted line, and how better to negotiate getting there!

Key Terms of a Distribution Agreement

Clause 3 Term

Options for Album

The distributor usually requires that they have the option to distribute the artist's next release. That is, once the term of this agreement ends, the distributor can decide whether they want to distribute the next album or simply finish up their relationship with the artist. This option prevents the distributor from being forced to decide at the outset of the agreement whether or not they will release two albums or just one – instead, they can wait to see how the first album sells, review their financials and then decide whether or not they will release album two.

Territory

It is important for an artist to decide in which territories a distributor will have exclusive rights to sell its music. In deciding this, the artist must research the distributor and their ability to distribute product across the world. If the distributor is small, artists should consider whether that distributor has the resources and networks to adequately distribute the artist's release.

As noted above, distribution of music over the internet is increasing. The artist or label may feel that they do not need a distributor to release their music across the internet as the artist or their management can manage this without too much difficulty. It's therefore important to think about varying the territories between physical and digital to maximise the artist's rights and potential income under a distribution agreement.

Clause 6 Rights

Under a distribution agreement, the artist usually gives the distributor the exclusive right to reproduce, manufacture, distribute and sell the artist's release in a territory.

In addition to these 'core' rights, distributors now commonly require that they retain rights that had previously only been provided under a master licence agreement (for more information on this, please see our Master Licence Agreement Fact Sheet and Checklist). These additional rights may allow the distributor to sell individual songs on TV shows and films (known as synchronisations). Distributors will request these rights because they allow them to find additional ways to promote and earn income from the release.

Distributors also ask for the right to dictate and vary the price of releases they sell. For example, if they find that a CD is not selling well, they would generally drop the cost of that CD to encourage sales at the lower rate.

Clause 7 Delivery

There are generally 2 types of distribution agreements:

1. Where the artist gives the distributor the fully mastered CD and artwork images which are then manufactured, pressed and finally sold to retailers; and
2. Where the artist manufactures the CDs themselves and gives all of their stock to the distributor to distribute and sell to retailers.

In the first case, the artist should understand which digital formats the distributor requires in order to correctly and most effectively make the CDs. If mistakes occur, the artist may miss out on releasing their products at key times – which could be a disaster for their marketing campaigns and touring schedules.

Clause 8 Distribution Services

Usually in a manufacturing and distribution agreement (also known as a P&D – pressing and distribution – deal) the distributor makes the physical release and stores those products in their premises. The P&D deal usually states that the artist is the owner of those products (CDs, for example) that are stored.

It is also common for distribution agreements to make reference to point of sale advertising and promotion. This is the advertising for releases that you see inside CD retail stores. Distributors may be required to provide retailers with such advertising and ensure that they are being displayed in the appropriate ways.

Clause 9 Advance And Distribution Fees

Distributor's Advance

Advances are the up front payments a distributor may choose to pay to the artist. A distributor's advance may be offered as a one off payment used to entice an artist to sign with the particular distributor, as well as to give them some start up income to help them survive during the initial roll out of their release. Note that this is a loan and is not free money – it must be paid back at some point and will usually be deducted before the artist sees any income from sales.

Distributor's Fee

Distributors are usually paid a percentage from all of sales – ranging from 15%–25%. Sales are calculated less returns, meaning that if the distributor sells 2,000 copies to a retailer, but then the retailer returns 500 copies the fee that the distributor will keep will be based on 1,500 sales.

Artists must also note that prior to being paid, the distributor will take out additional deductions to cover any special costs of sale. For example, it is common for distributors to give retailers discounts if they buy an artist's CD in bulk. This discount is then reflected in the artist's payment.

Reserves

Reserves are best explained by use of an example:

If a distributor sells 2,000 CDs to a retailer for \$2,000 (i.e. \$1 per CD) and that retailer returns 500 CDs, the distributor must then return \$500 to the retailer, being the money they paid for the 500 CDs.

But, what if the retailer returned the CDs after the distributor has paid out the artist on the basis of 2,000 CDs? It means that the artist was paid too much – as the artist income was calculated on 2000 sales, when it should have been 1,500 sales. The distributor usually includes what is known as reserves to create a buffer to protect the distributor from such returns.

Reserves are an estimation of returned goods that the distributor thinks they will get over a period of time.

They are known as reserves because when paying the artist, they hold an amount of money in reserve just in case more CDs are returned during an accounting period. If there is money left over in the reserve account at the end of the next period – that income is then given to the artist.

To prevent a distributor from taking extremely high reserves (and therefore delaying payments to the artist), artists usually require that reserves be capped at a certain percentage of income – usually around 20%.

Clause 10 Termination

Once the distribution agreement is terminated, the distributor may require an additional time to sell off any of its physical stock of any CDs. The sell off period is usually 6 months following termination of the agreement.

If the artist provided all the stock to the distributor, then the distributor would be required to return any remaining stock. Alternatively, if the distributor manufactured all of the CDs, then the artist would have the chance to buy back the remaining copies.