Financial Business Models
Adding Value to Content

Payment to authors, permission costs, and subsidiary rights

PAYMENT TO AUTHORS

There are several ways of considering the main source of supply in the publishing industry – the authors and writers who create the books the publisher produces and sells. Publishers need to reach agreement and decide what is a fair rate for the job, but one that the publisher – and the market – can afford.

Publishers may be intermediaries between academic researchers or scholars and their readers. Publication is much more important to them than payment, and contributors to journals often get paid nothing. But a journalist asked to write a chapter of a book that deals with contemporary issues – anything from the water table to greenhouse gases – will expect to be paid a fee for the job on completion. Many publishers, however, want to build a long-term relationship with their authors over several years and (they hope) over several successful books. That relationship may be more like a partnership in which each side takes a risk and is prepared to wait for a return on their investment and time, the author receiving a percentage royalty based on sales of the book. But authors also need to live while they are writing, so it is often appropriate that they get a portion of their payment in advance.

From a financial point of view we need to look at two kinds of business model: fee payment based on work-for-hire, and royalty payment based on numbers of sales.

Fee based payment

For books with several different contributors, each writing separate chapters or sections, the payment of a fee based on the length of the piece or the time taken, is a practical and acceptable way of working. How should the amount be calculated, and where should such payments appear in a publisher's accounts?

Rates of payment

Many professional writers work to a standard range of payments based on the numbers of words, usually calculated per thousand. The sum per 1000 words might be between $200 and $300 (though much lower – and higher! – figures are common). The publisher may have to pay more if the writer is an expert in her field, or is required to do the work quickly because there is pressure on a deadline.

Normally, fees are paid once only. They can be broken down into staged payments – for example, 25% on signature of the agreement, 50% when the publisher receives an acceptable typescript, and the balance when the additional work (including checking proofs and layout) has been completed. It is not a large sum of money for 15 days' work (about $150 a day) but it is cash in hand, and is paid regardless of how the book sells when it is published.

Below, a margin has been worked out to show how these fees are included in calculations – and the benefit to the publisher of having to pay the fee only once. The gross margin when – if! – the book reprints can be substantially higher, as one-off costs, including the writer's fee, do not recur.

NON FICTION TITLE FOR 12-YEAR OLDS

	3000 copies @ $15 r.r.p.		**1500 copies @ $15 r.r.p.**
	FIRST PRINTING		REPRINTS
Origination costs	Writer's fee	2500	-
	Art and photographs	2500	1500
	Design & typesetting	1000	-
	Origination	1250	250
		7250	1750
PPB freight costs	Print and bind	3600	1980
	Paper *(100 gsm)*	400	200
	Freight	600	300
		4600	2480
	Total cost	**11850**	**4230**
	Unit cost	$3.95	$2.82
Sales revenue	1000 @ 35% d/c	9750	500 @ 35% d/c 4875
	1900 @ 60% d/c	11400	1000 @ 60% d/c 6000
	(100 gratis)	-	-
	Total revenue	**21150**	**10875**
	Revenue	21150	10875
	Costs	11850	4230
Margin	Margin	**9300** *(44%)*	**6645** *(61.1%)*

Royalty payment
Royalties take the form of a percentage based either on the selling price of the book, or – more commonly with academic and educational books – on the sums received (or 'net receipts') by publishers after discounts to booksellers or retailers. There is no such thing as a 'normal' royalty rate, although many publishers use 10% as a reasonable benchmark. Royalty rates can vary widely, and with some titles (particularly those with very high start-up and origination costs), a sliding scale is sometimes paid, for example: 5% of 'net receipts' up to a sales level of 3000, 7.5% up to 6000, and 10% thereafter. The argument here is that early in a book's life cycle, the publisher is still tying to recoup his start-up costs and has less margin to share with the author. But once sales have passed a certain level, the rate can increase.

Basis of royalty
Authors of consumer titles, particularly those whose agents negotiate the contract, may demand that royalties are paid on the selling price of their book, or 'recommended retail price'. The problem for publishers is that some sales channels can be serviced only by way of very deep discounts. A chain bookstore that takes large quantities of a lead title, holding stock as well as promoting the book in-store, will demand a discount of 50% or more. If a publisher pays a royalty of 10% based on a selling price of $20 but is receiving only $10 in sales revenue, then the $2 he is paying to the author (10% of $20) is, in effect, a royalty of 20% on the sum received (20% of $10).

From a publisher's point of view, paying authors on 'net receipts' means their payment are kept more closely in line with the funds available from actual sales. However, authors might argue that their income should not be dependent on how big a discount the publisher has to make – they should be getting, as far as possible, the same amount on every copy of their book that is sold. Examples of royalties paid by each method are at the end of this section.

Advances
Authors who write for a living will expect to be paid a sum up front for the work they have been contracted to do. An advance is a portion of the royalties that the book will 'earn' for the author, once it is published. This money on account serves two purposes: it is a statement of commitment from the publisher, and it allows the author to cover some of her living costs while she is writing the book.

Many authors of academic and educational books do not write for a living. The books (or contributions to publications such as journal articles) represent an important part of their individual (or their institution's) reputation – even their career advancement – but their main source of income comes from their work as teachers or researchers. Publishers of books for these sectors may have very high start-up or origination costs in the form of artwork and illustrations, and so may not be in a position to pay substantial advances. Advances represent a considerable drain on cash for publishers, particularly if a work takes two to three years to write, trial, and publish.

As a rule of thumb, it is unwise to pay an advance that amounts to more than half what would be paid in royalties when the first printing has been sold (see example below).

Advances are usually paid in stages – say, 25% on signature of the contract, 25% on delivery of an acceptable and publishable manuscript, and the balance on publication. Authors (or their agents) may demand a larger share up front, while publishers will try to conserve their cash by paying the largest portion of the advance nearest to the date when revenue starts to come in to cover that advance. A compromise could be a division into equal shares – a third on signature, a third on acceptance, and a third on publication.

Author costs and charges

If a work contains a large number of third party items for which permission for copyright clearance must be sought and paid for, it is normal for authors to share in both the work of identifying and clearing those permissions, and paying for part of them. Sometimes the publisher and author will agree a budget for text extracts (an anthology of articles or stories, for example). Up to the level of this budget, the publisher may pay for permissions. For extracts that exceed the budget, the author will carry the charge – normally in the form of deductions from their royalty earnings. The same principle can apply to photographs, too.

Most contracts also stipulate that if authors make editorial changes to their work when it is in proof form (as opposed to merely correcting printer's errors) then a ceiling is placed on the cost of those changes – usually 10% of the total typesetting costs. An author who makes changes that cost more than this will be charged, once again by having sums owed deducted from royalties due.

Shares of subsidiary income

Most licensing agreements between publishers and authors allow the publisher to develop other works based on the original typescript, or to exploit the value of the asset in other ways. These can take the form of adaptations (such as a translation into another language), the re-publishing of an extract in a magazine or periodical (a so-called serial right), or an exploitation in another medium – dramatisation, a film or TV option, or the creation of a software product derived from or based on the original work.

The contract will specify the shares of income from these other rights that are to be paid to the author. The split is often 50:50, although in the case of exploitation by way of a broadcast on radio or television, or an option to make a film, a higher proportion – sometimes as much as 90% – is paid to the author. Money received in the form of subsidiary rights income, is remitted at the next accounting period, in addition to royalties owed to the author, and is set against any remaining advance or any expenses the author may have incurred.

Model workings

Here are two examples of a 4-year sequence showing an author's royalty payment and shares of other income. Publication takes place at the beginning of Year 2. The book is published at a price of $20 and initially 3000 copies are printed. In the first example the author is paid a royalty of 10% based on the net sums received by the publisher. The book sells at an average discount of 25%. In the second example. The royalty is based on the recommended retail price.

1 *Royalty based on net receipts*

	Year 1	Year 2	Year 3	Year 4 (reprint 1500)
Sales unit	-	2000	1000	600
value	-	30000	15000	9000
Royalty	(10% receipts)	3000	1500	900
Advance	($2000)	Earned out	-	-
Author costs (permissions)	($1500)	($500) still owed	-	-
Share of other income	-	750 (serial rights)	500 (translation)	-
Net payment	($3500)	250	2000	900

2 *Royalty based on selling price*

	Year 1	Year 2	Year 3	Year 4 (reprint 1500)
Sales (units)	-	2000	1000	600
(value)	-	30000	15000	9000
Royalty (10% of selling price)	-	4000	2000	1200
Advance	($2000)	(earned out)	-	-
Author costs (permissions)	($1500)	(covered)	-	-
Share of other Income	-	750 (serial rights)	500 (translation)	-
Net payment	($3500)	1250	2500	1200

PERMISSIONS

Permissions need to be sought and cleared, and any fees paid, before publication. These costs can be borne entirely by the author, or absorbed into the production cost of the publisher, or shared in some way by author and publisher. Permissions (and fees) may apply to text extracts (prose or poetry); artwork, diagrams and drawings reproduced from an existing source (not necessarily published); photographs (whether commissioned or licensed from a picture library); and web material (whether textual, consisting of images, or a composite mixture).

In the following narrative sequence, the author and publisher are working together to produce an illustrated anthology of literature and non-fiction from a particular region.

Text material
20 Third-party owned prose extracts of 500-1000 words
10 Third-party owned poems or poetry extracts of 50-100 lines

For the prose extracts, permission is granted for five of them with no charge. Of the remaining 15, the breakdown is as follows:

8 @ $100 each		800.00
5 @ $200 each		1000.00
1 @ $500		500.00
1 @ $750		750.00
	Total	$3050.00

For the poems and poetry extracts, two are cleared with no fees being charged. Of the remaining eight, the breakdown is as follows:

5 @ $100 each		500.00
2 @ $200 each		400.00
1 @ $800		800.00
	Total	$1700.00
	Total extracts	$4750.00

A budget of $3000 for all the text extracts has been set by the publisher. However, the author is unwilling to fund the full additional $1750, so the $750 prose extract is replaced by another piece costing $150 and the $800 poem is replaced by another also costing $150.

The prose budget now stands at	3050 – 750 + 150 = 2450
The poetry budget now stands at	1700 – 800 + 150 = 1050
	$3500

The author agrees to pay the extra $500 over the budget by having the sum deducted from his first royalty statement.

Artwork
Publishers normally pay for specially drawn artwork, and in this book only two third-party pieces are to be included, one in the back cover. The back cover illustration is charged at $1000 and the other piece at $250. The publisher agrees to pay both these.

Photographs
The author supplies 100 photographs of his own, but they are of variable quality. The book is designed with space allocations for 50 photographs, and after some disagreements only 15 of the author's are decreed to be of sufficient quality. A professional photographer is commissioned to produce 30 pictures to a specific brief, and is paid $300 for a day's shoot. This cost is borne by the publisher as part of the start-up costs.

The remaining five photographs must come from a picture library, and the rates for these are very high, a fee of $500per photograph being initially quoted. After a lot of haggling, the library agrees to provide all five for a one-off fee of $1500. When the picture library discovers that one of the photographs is planned to be used on the cover, they revise the figure back to $2000. More negotiation follows, and a compromise is reached whereby the author and publisher agree to go halves on the photograph library cost, each side paying $1000 of the total bill.

So the author has agreed to pay $500 towards text extracts and $1000 towards the cost of the photographs, a total of $1500. He has been paid $1000 of a $2000 advance, so when the second half of the advance is due to be paid on publication, no more money is paid. Indeed, he still 'owes' $500, which will be set against the first year's sales and royalties.

SUBSIDIARY RIGHTS

We think of income from publishing deriving mainly from sales of copies of a published book. This primary revenue may be the only source of income for an author, often paid in the form of royalties based on a percentage of sales. However, there are many other secondary ways of exploiting the assets represented by a book, and substantial revenue can be generated by these other sources.

There are broadly three ways of defining the way publishers and authors can exploit what are usually known as subsidiary rights.

- other editions or versions of the complete work
- selling rights to parts of the work (textual or illustrative) reproduced in facsimile ways
- adapting or exploiting the original material and producing it in different media

'Complete work'
A hardback can be published as a paperback, either by the original or by another publisher. A work of literature can be produced in an educational edition, with background or explanatory notes to help students studying it for an exam. Visually impaired readers may need an edition of a book manufactured with large print.

Perhaps the most common way in which an entire book is published in a different edition is when it is translated into another language and sold in other countries. If the original publisher itself produces another edition or version of an author's work, then royalties are the most common way of paying that author. The rates may be different if the discounts offered to retailers are different.

If another publisher buys the rights to produce an edition of the original work, then this buyer will usually pay a royalty on sales of the local edition. It depends then who manufactures the local edition: the original publisher can manufacture and supply finished copies (bound or in sheets) of the buying publisher's edition.

This finished copy is often printed at the same time as the original publisher's reprint, so that both parties can benefit from the longer print run. Alternatively, the selling publisher can provide film or digital files of the original work so that the buying publisher (or publishers) can print their own edition.

The first method is especially useful when books are in full colour, as the example below shows. This is because short print runs of books in full colour are still very expensive, even with print on demand technology.

A Publisher prints…

Look how the savings work to the benefit of everyone.

Seller A wants to reprint 1000 copies
Buyer B wants 800 copies for his market in his language
Buyer C wants 700 copies for his market in his language Total: 2,500

Buyers B and C provide files of the text in their languages. The bulk of the book consists of illustrations in full colour. The text files are known as the fifth black working (the other four being the magenta, yellow, cyan [blue] and black of the illustrations). It is much more economical to print all 2,500 copies of the illustrations together, and then drop in each of the different text printings separately.

Cost for 800	Make ready	500
	Printing 800 @ **$1.50**	1200
	Royalty of 50c	400
	Freight @ 50c	400
	Total	2500 (unit cost $3.13)
Cost for 2500	Make ready	500
	Printing 2500 @ **80c**	2000
	Royalty of 50c	1250
	Freight @ 50c	1250
	Total	5000 (unit cost $2)

With a unit cost of $2 to the publisher, he would try to sell on the special editions to buyers B and C at about twice the printing unit cost (including make ready), plus royalty and freight.

For Buyer C (700 copies)

Total Printing cost for 2500 (make ready and PPB)	2500
Unit printing cost	$1
Charge to Buyer C	$2
+ royalty and freight *(50c + 50c)*	$1
Total charge to Buyer C	$3
700 copies (royalty and freight inclusive)	$2100

The selling publisher has to share the royalty element of this income with the author, according to the contract.

700 x 50c = $350. 75% of this goes to the author ($263) so the publisher is left with $87.

B Publisher supplies film or files…

A Nigerian publisher reaches agreement with a South African publisher in Johannesburg to sell the Xhosa language rights of one of his illustrated titles, printed in four colours. The original book sold for $20.

The Nigerian publisher agrees to provide duplicate film at cost plus 10% so that the South African publisher can make use of the four-colour film of the illustrations unchanged. He translates, sets and makes film of the black text in Xhosa. "Cost plus 10%" means the actual price paid for the duplicate film or digital files, plus a 10% handling charge – the cost of production staff ordering it and sending it. This mark up is not shared with the author. Six months later the South African publisher produces and publishes his edition. He prints 2000 copies. The local selling price is 195 Rand (a dollar is worth about R6.80). An 8% royalty on the South African published price is agreed with the local publisher. When he sells out his edition the expected earnings will be:

8% of R195 x 2000
= R31,200 ($4588)

When the deal was concluded, an advance of R15,000 was agreed, about half the expected income. The South African publisher paid this advance as soon as the contract was signed, and the money was paid over in November. It converted to $2200.

In December the following year, the South African publisher prepared accounts. To that point, he found he had sold 1200 copies of the book. At 8% royalty, R18,720 was due. But an advance had already been paid of R15,000. So, when the account was settled the following March, the balance of R3,720 (about $547) was received by the original publisher.

At the end of that year, 500 more copies had sold. The price of the book in South Africa had been increased to R225 from 1 January, so royalty earnings for the year were 8% of R225 x 500 = R9000 (about $1325). The money was paid the March after that.

The original publisher's contract with the author states that the share of income from translation rights shall be 75:25 (75% going to the author, 25% being kept by the publisher). This table shows how it works:

Date	**Event**	**Income R**	**$ Equiv.**	**Author's (75%)**	**(Publisher's (25%)**
Oct. 05	Xhosa Language rights sold	--	--	--	--
Nov. 05	Advance received	15,000	$2200		
Mar. 06	Author's accounts for second half 05	--	--	$1650	$550
Dec. 06	South African accounts prepared for 06 1,200 sold	(18,720 less advance)	--	--	--
Mar. 07	Account paid	3,720	$547	--	--
Sept. 07	Author's accounts for first half 07 paid	--	--	$410	$137
Dec. 07	South African accounts 07 prepared 500 sold	(9,000)	--	--	--
Mar. 08	Account paid	9,000	$1325	--	--
Sept. 08	Author's accounts for first half 08 paid	--	--	$995	$330
	Total income to end 2008			**$3055**	**$1017**

It’s a lot of work for quite small sums of money – but most of the work is done by the publisher to whom you have sold the rights.

‘Parts of works’

Publishers can derive income from selling parts of the publications to which they hold rights. However, it can be a lot of work to achieve sales of many different small parts of dozens of work, so it is not normally a very profitable side of the overall business. Additionally, the publisher (even acting on the author’s behalf and with her authority) will not always own all the rights in the parts of the work that other publishers may wish to acquire.

Text extracts

If you publish the works of a famous fiction writer or a poet; then there will be a steady demand from other publishers wanting to include extracts, stories or single poems in anthologies, or collections of genres of work. Examination boards may want permission to include part of a work in literature papers. The big question – and one that’s impossible to answer – is ‘how much should I charge’? Looked at purely from a commercial point of view, you might say ‘as much as you can get away with’, but there are other factors to consider.

The issues under which you should reach a decision are *ethical, cultural, moral* – and, of course *commercial*.

The balance that has to be struck is one that gets a reasonable return for both the author and the publisher, but does not prevent legitimate third-party users from re-publishing a work (or part of it) by the application of prohibitive or greedy prices. Besides, there can be a benefit in promoting and publicising your author’s work in other publications. A judgement also has to be made on how much of the whole work is being requested for re-use, how prominent the use is (will part of it be used on the cover of the book?), and how extensively the new work will be distributed.

The greater the use (and prominence) and the wider its dissemination, the higher the fee that may be appropriate. Bear in mind too that under the terms of fair dealing (or fair use), publishers may use an insubstantial part of a work without seeking permission or the need to pay a fee. Note too that the publisher and author will normally require the extract or the work to be reproduced exactly as in the original.

In 2002, the following guideline rates were suggested by the UK’s Society of Authors and Publishers Association for prose and poetry.

Prose	$200 - $250 per 1000 words
Poetry	$150 - $200 for the first 10 lines $3.50 - $4 per line from 11-30 lines $2.20 - $2.50 per line for 31 lines and over

These were for world rights, so lower fees would be in order for more limited use, or if the work was to be used in a low circulation specialist journal.

Illustrations
Art work is normally commissioned, as are some photographs. Acquiring artwork that has already been published or using photographs from a picture library requires a licence and usually the payment of a fee. The cost will depend on two things: the size of the reproduced illustration on the page, and the extent to which the new work will be published and disseminated.

Recent guidelines have been devised to give a broad range of appropriate prices.

Page size	**UK rights**	**Commonwealth Rights**	**World English language**	**World all languages**
25%	$120	$145	$190	$225
50%	$135	$175	$225	$275
75%	$170	$200	$275	$305
100%	$225	$275	£355	$390

The rule of thumb, again, is that lower fees may be appropriate for publications with limited circulation, and higher fees for a prominent re-use, such as on the cover rather than in the main text.

Rights owners of photographs, for example will almost always have given you limited rights in the form of a non-exclusive licence. So you cannot sell on rights to a work in one of your publications to a third-party if you have only been granted limited rights. For example, a page of a textbook may contain text, artwork, photographs, diagrams and even maps. You can only sell the rights to reproduce that page if you hold rights in *all* those components – which would be unlikely.

Adaptations and exploitations
Some works lend themselves to substantial further exploitation, in different forms and new media. A novel can be dramatised and performed. The same novel could be read on the radio, either in a complete form or abridged or condensed. Or it could form the basis of a screenplay for a film or television programme to be made. Sections of the novel might be published in a newspaper or magazine. Before publication (first serial rights) such extracts can help publicise the book. After publication (second serial rights) it can extend the appeal or sale of the work to new or wider audiences.

For many educational and academic publications, such glamorous possibilities are very limited. However, a publisher might want to adapt a section of a textbook for a different audience (at a lower ability level, or in simplified language). This would come under the heading of adaptation or abridgement rights.

So, often it is the *medium* in which the exploitation takes place that defines and limits the rights – audio, visual (still and moving images), audio-visual, digital/electronic, and so on.

For some popular children's works, the characters will become so familiar that merchandising rights can be sold, and the image of the famous character used on all sorts of goods and merchandise – from T-shirts to mouse mats, from yoghurt to beans. Licences to use these characters can be very lucrative, if the publisher has retained a share in the rights. However, most of the money in these examples goes to the author or creator.

Whatever the form or medium of the exploitation, the author's share has to be agreed. It will normally not be less than 50% of the income received from the rights sale and can be as high as 90% for consumer books. A 75% author 25% publisher split is a reasonable midway point, while in education and academic publishing, a 50:50 split is much more common.

To show how rights income can be generated and distributed the example below shows a high profile mass-market work, which has commanded a large advance for the famous author. An income and royalty statement after the first year of publication has been prepared for Jackie Jones' novel 'One Night of Romance'. The book is priced at $15.

Royalty advance	$200,000
25,000 copies at 10% of selling price	$37,500
Less returns reserve (20%)	($7500) = $30,000
25,000 copies at 10% of average receipt of $8	$20,000
First Serial rights sold to Sunday newspaper for $100,000 (90% to Jackie)	$90,000
Option for TV serial $50,000 (90% to Jackie)	$45,000
Advance on French and Spanish translation rights $10000 each (Total $20,000) (75% to Jackie)	$15000
Total royalty income generated	$200,000
less advance already paid	$200,000
New royalty income due to Jackie	$0.00

Conclusion

Subsidiary rights come in all shapes and sizes, and many publications will offer no opportunities for exploitation, except perhaps translation. Generally rights income can be expensive and hard work, though much of the revenue is free of overhead, as the work of generating the income has largely been undertaken by the buying publisher.

From a business point of view, this revenue is often a welcome (and sometimes unexpected extra). Agreeing how that income is to be split with the author is the key

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