ACCT-GB3149 Entertainment Accounting

Warner Music – Revenue Recognition Analysis and Intangible Assets Summary

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Warner Music Group earns revenues from 2 main domains that are Recorded Music and Publishing. As per the Form 10-K there are three main sources of revenue from recorded music; **'Physical and Other'** which involves the revenue earned from the sales of physical CDs and DVDs of the musical content of which the rights are held by Warner Music. This category also includes the revenue from the 360-degree deals that involve revenues via Warner's extended rights with their artists for Live Touring, Merchandise, Sponsorships, Artist and Brand Management etc. The category of **'Digital'** includes the revenue from the sale of Online Song/Album as well as Mobile Song/Album and Ringtone downloads. **'Licensing'** consists of the royalties/fees for rights to use the master in combination with Films, TV Programs/Commercials, and Video Games etc. The Publishing revenue consists of the royalty fees for exploitation of the intellectual property i.e. the song itself through the various mediums and comes through the following five sources such as **Mechanical Royalties, Performance Royalties, Synchronization, Digital and Sheet Music Royalties.**

With respect to the Revenue Recognition Policy, the revenues for the physical CDs / DVDs are recorded when the shipment has occurred and the title and the risk of loss has been transferred. If the physical products are sold with a right to return; gross revenue less provision for future returns is recorded. Revenues from Digital are recorded once the songs/albums are downloaded and related sale documents are available from the providers. Publishing revenues are earned via receipt of royalties from copyrighted material being publicly performed, mechanically reproduced including digital and using in synch with visuals. All music-publishing royalties except for synch are recognized as revenue once cash is received. This difference occurs as; with respect to synch the visuals such as TV Commercials/Films etc. are aired at a later date than the contract has been entered into. Thus the synch revenue is recognized on an accrual basis in accordance with the ASC 605.

Overall the recorded and licensing revenues are shrinking due to the factors such as general economic pressures and the transition from physical sales to new forms of digital sales in the recorded music industry, adversely impacting the physical revenues. On the other hand there was an increase in the

Digital sales due to the above-mentioned transition along with an increase in the European Concert Promotion revenues. A similar pattern can be seen with respect to the decrease and increase in the Publishing revenue.

Goodwill reported as of Sept. 2009 is of 1.4 billion, which included foreign currency translation adjustments, and adjustments to the tax basis of acquired assets and liabilities, which were recorded as a decrease to deferred taxes. The acquired goodwill in 2008 included acquisition of Fran Sinatra Enterprises along with several tour, production, booking and artist management companies. Annual goodwill impairment test in accordance with ASC 350 is performed during the fourth quarter of each fiscal year and no impairment occurred in 2009 according to the tests.

Other Intangible Assets include Recorded Music Catalog, Publishing Copyrights, Artist Contracts, and Trademarks etc., the life of which is established via the expected future cash flows. The estimated useful lives for the company's identifiable-finite lived-intangible assets considered for amortization are 10 years for Recorded Music Catalog, 15 years for Publishing Copyrights as well as Trademarks. Artist Contracts have variable estimated useful life but not exceeding 10 years.

In my opinion OIBDA is not an optimum measure for the company's performance, as it does not portray the periodic costs of certain capitalized tangible and intangible assets used in generating revenues. Thus I agree with the disclosure by Warner that OIBDA should be considered an addition to and not a substitute for measuring the financial performance. They also explicitly mention that their definition of OIBDA may be different as compared to other companies. The increase in the digital media such as Spotify, Pandora etc. will negatively impact the company's revenues as the share of the Digital in the revenues though growing is relatively very small and the percentage share going to the record label from individual streams is miniscule as compared to their share in Physical CDs. Also the growth of the digital content is not an independent phenomenon but at the cost of cannibalization of the physical which is the main source of revenue for Warner Music.