CHAPTER 13: ROYALTIES
Royalties are the amount of money that authors get from the sales of their books, usually expressed as a percentage. You need to pay attention to how exactly your royalties are defined and calculated. Suppose that your contract specifies that you’ll receive “10% of retail book sales.” Great, you might say, but what does “retail book sales” mean, and how is it calculated? These are the key questions to ask as you’re negotiating your royalty terms as there are a few different ways to define and calculate sales for royalty purposes.

There are three main types of royalties:

1. royalties based on the book’s published price (also called the “list price,” the “cover price,” or the “manufacturer’s suggested retail price”);
2. royalties based on the publisher’s net income from sales of the book (also called “price received” or “sales proceeds”); and
3. royalties based on the publisher’s net profit.

To calculate your royalties under any of these systems, you’ll need to know both the percentage you will be receiving and the price from which that percentage is taken. While this may seem overly technical, it can make a huge difference in your future bank statements. This chapter discusses each type in detail.

**PUBLISHED PRICE ROYALTIES**

*Published price royalties* are based on the list price (the price printed on the book). Your royalty in this situation would be a percentage of the retail price multiplied by the number of copies sold.

\[
\text{Published Price Royalty} = \text{List Price of Book} \times \text{Number of Books Sold} \times \text{Royalty Percentage}
\]

For example, if your book has a list price of $16, you sell 1,000 copies, and you receive a 10% published price
royalty rate, then your royalty check will be $1,600: $16 per copy x 1,000 copies × 10% royalty.

Here’s an example of a published price royalty clause:

The Publisher shall pay the Author a royalty of ten percent (10%) of the retail price thereof on the Work.

**NET INCOME ROYALTIES**

*Net income royalties*, also called *price received* or *sales proceeds* royalties, are like published price royalties, but with a twist. These royalties are based not on the list price of the book but on the amount the publisher receives when the book is sold to retailers or distributors.

\[
\text{Net Income Royalty} = \text{Net Income per Book} \times \text{Number of Books Sold} \times \text{Royalty Percentage}
\]

Because the net income the publisher received from each copy of a book is usually less than the list price, the royalty percentage rate for net income royalties is
generally higher than for published price royalties. For example, your book may have a list price of $16 but it is sold to retailers for $10, which means that a royalty percentage based on net income needs to be higher for you to make the same amount of money:

- $16 list price × 1,000 books sold × 10% published price royalty = $1,600
- $10 net income received × 1,000 books sold × 10% net income royalty = $1,000
- $10 net income received × 1,000 books sold × 16% net income royalty = $1,600

This example shows why “percentage of what?” is an important question to ask: Here, 10% of list price results in a much bigger royalty payment ($1,600) than 10% of net income ($1,000).

A net income royalty clause might look like this:

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The Publisher shall pay the Author a royalty of twenty percent (20%) of the revenue received by the Publisher attributable to the Work.
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Remember that under the net income royalty model, the list price of your book does not change your royalty,
but the actual price at which it is sold to retailers does. Therefore, it’s important that you understand how your book is being distributed by your publisher and under what circumstances the price might change. For example, it’s common for retailers to negotiate significant discounts to the list price, which means that your per-book royalty will be lower when sold through these retailers. (For more on this, see Deep Discounts below.)

Because of volume discounting, published price royalties are generally thought to be better for authors than net income royalties, as an author’s per-book earnings don’t change. This makes it easier for authors to keep track of and anticipate the amount of royalties they’re owed.

**Literary Lesson**

Sara Scary negotiates a 20% net income royalty for her new thriller, *The Emeryville Horrors*. Sara expects her book to be sold to retailers for the volume price of $10 per copy. However, Nile Books, a major online bookseller, strikes a deal with her publisher to buy copies for $5 each. Therefore, Sara receives $2 for each book sold to other retailers, but only $1 from...
books sold to Nile. Had Sara known about her publisher’s deal with Nile, she might have negotiated for a higher royalty percentage.

When your publisher sells books directly to consumers (say, through its own website), you may actually end up getting a percentage of the list price, even under a net income royalty model. This is because the publisher is likely selling your book directly to a consumer at full cover price, rather than to retailers at a discount.

**NET PROFIT ROYALTIES**

*Net profit royalties* are based on the amount of profit that is left after the publisher deducts costs associated with producing the book, such as editing, printing, publicity, warehousing, and shipping. Net profit royalty arrangements are rare. Since the basis for a net profit royalty is far lower than in the two other types (because there is always less profit than there is gross revenue), the royalty percentage is usually significantly higher. Some net profit royalty percentages can be 50% or more.

The key to understanding this royalty structure is understanding how “net profit” will be defined by your
publisher and making sure this definition is written into your contract. Because net profits will determine your royalties, you’ll want to make sure you clearly understand what expenses are factored into your publisher’s net profit calculation.

Be on the lookout for vague terms like “associated costs.” You’ll want to clarify these terms to avoid extra costs that are unrelated to your book, such as administrative overhead. For example, an author-friendly clause would clarify that only costs which are directly and solely related to an author’s book may be deducted; this way there’s less ambiguity when it’s time to calculate net profits. Also, because net profit accounting can be complex, it is a good idea to include an audit clause that allows you to inspect your publisher’s accounts and finances to make sure profit is calculated properly. This helps ensure that unauthorized expenses are not deducted. (For more information, see Chapter 14: Accounting.)

PUTTING IT ALL TOGETHER
This side-by-side comparison of royalty models demonstrates how the royalty basis can affect an author’s bottom line:
On the other hand, it’s possible to earn the same amount per book under each accounting method, even if the percentage rates are wildly different.

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<th>PUBLISHED PRICE</th>
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<tr>
<td>Alfredo Author’s book sells for $20 list price at bookstores. His contract specifies a <strong>12% published price royalty</strong>, meaning he will earn $2.40 per book sold.</td>
<td>Bookstores buy Alfredo Author’s book wholesale for $16 each. His contract specifies a <strong>12% net income royalty</strong>. Therefore, he earns $1.92 for every book the stores buy.</td>
<td>Alfredo Author’s book sells for $20, but the publisher incurs $15.20 in costs, netting $4.80 per book. His contract specifies a <strong>12% net profits royalty rate</strong>. He earns $0.58 for each book sold.</td>
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<td>Alfredo Author’s book sells for $20, but the publisher incurs $15.20 in costs, netting $4.80 per book. His contract specifies a <strong>50% net profits royalty rate</strong>. He earns $2.40 for each book sold.</td>
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In sum, there are two essential questions to ask when you’re negotiating your royalty provisions:

1. What am I being offered a percentage of (e.g., list price, net income, net profits)?
2. How is this royalty calculated?

For some royalty structures, the math is relatively simple. Other times, the accounting is complex, requiring a detailed analysis of all the costs associated with manufacturing and selling your book. Either way, it is important that your contract be clear on how royalties will be calculated and for you to understand how your publisher’s business model will influence your royalty earnings.

**Success Story**

Sergio Troncoso, an author of short stories, essays, and novels, as well as a savvy negotiator, pushed for his royalties to be a percentage of the list price, reasoning that this would likely be the more lucrative option. His publisher was initially resistant, but after a few rounds of back and forth, Sergio’s patience and perseverance paid off. His publisher agreed to a compromise: Rather than getting the published price...
Understanding and Negotiating Book Publication Contracts

(list) royalty he had asked for, he would receive a higher percentage of the net profit royalty than was originally offered.

OTHER FACTORS THAT MAY INFLUENCE YOUR ROYALTIES

**Escalations**

Sometimes, a contract will specify that the royalty rate increases as more copies of a book are sold. These are called *escalations* or *ladders* and are common in trade book contracts. For example, you may start off at a 7.5% published price royalty rate, but after 2,000 copies sold your royalty percentage increases to 10%; then, after another 3,000 copies sold it increases again to 12.5%; and finally, after an additional 5,000 copies sold it increases again to 15%. A clause based on this structure would look something like:

The Publisher agrees to pay royalties to the Author as follows ... 7.5 percent on the first 2,000 copies sold; 10 percent on the next 3,000 copies sold, 12.5 percent
on the next 5,000 copies sold; 15 percent on all copies sold thereafter.

Escalations may also be tied to non-numeric measures of success, such as appearance on a bestseller list.

**Small Reprintings**

Some publishers include a provision that reduces your royalties in cases where a *small reprinting* is made, often of 1,000 copies or less. The reduction in your royalties will either be by a fixed percentage (often two-thirds or three-quarters of your regular rate) or be calculated based on net income rather than list price.

This type of provision is not friendly to authors, and you may want to try to get it removed. It is a relic of the days before print-on-demand technologies, when it cost more for a publisher to do a small print run.

**Reserves on Returns**

By industry custom, book retailers can return unsold books to publishers for a refund. Returns are quite common in publishing, which is why the *reserve on returns* clause is important. This clause allows the
publisher to withhold a portion of an author’s royalties as a “reserve” against future returns.

**Literary Lesson**

National chain Tons-o-Tomes has ordered 10,000 copies of your book, and, after all the math is done, you’re getting $1 per book in royalties. However, when you get your check it’s only for $8,000. Why? Because your publisher has withheld the remaining $2,000 (20%) against the possibility of returns.

A reserve on returns clause might look something like:

> In reporting sales the Publisher may withhold a reasonable reserve for future returns.

Some publishers roll reserves over every accounting period without limit. This means that if the book remains in print, the publisher can hold back a reserve indefinitely. You can try to eliminate this by including a time limit on how long the reserve can last. You could also try to specify a reserve cap, say 15% – 25% of revenues. Or you could do both. For example:
The Publisher may retain a 20% reserve for future returns for two consecutive royalty periods, provided the royalty statements indicate the amount of the reserve and how it has been applied.

You might also want to discuss with your publisher what to do with returned copies. For example, you could try to get your publisher to agree to donate returned copies to libraries, or you could ask for the option to buy unsold copies yourself at cost so that you can sell them or give them away. Keep in mind that some of the copies will come back damaged and need to be pulped.

**Deep Discounts**

Many publication contracts will also include provisions that address reductions to an author’s royalty rate for certain heavily discounted sales. Often, these provisions will define a *deep discount* or *quantity discount* as any sale that has either a “greater than 50% discount of list price” or is more than the publisher’s “normal wholesale discount.” Deep discount provisions are most commonly found in contracts where the normal royalty structure is based on the published price. This is because publishers don’t want to be obligated to pay
authors the same amount for each copy of the book sold if some of these copies bring in far less revenue.

A deep discount clause might look like this:

From sales of the Work at discounts of 50% or more from list price ... 50% of the applicable royalty rate specified in Clause X.

If your contract contains a deep discount provision, you may want to request a copy of the publisher’s current discount schedule before locking in your royalties. For instance, the deep discount provision might not be important if your publisher sells only 5% of its books at a deep discount. But if it discounts 85% of the books it sells, you’ll want to take that into consideration as you’re negotiating. Mind you, selling at a deep discount isn’t necessarily a bad thing—bulk orders at a discount mean lots of books are being sold, after all—but it’s still something you should consider as you work through the financial terms of your contract.

Sometimes, contracts will restrict the deep discount provision to “special” sales, such as non-re-turnable bulk sales. Limiting the reduced royalty rate to “sales not within the scope of normal wholesale and
retail trade bookselling channels” is a common author-friendly approach.

Another variation is to reduce the royalty in proportion to the size of the discount the publisher gives its customer—e.g., if the buyer gets a 20% discount, your royalties go down by 20% as well. This way, the reduction in earnings is shared equally between you and your publisher.

**Remaindered Books**

If publishers have more copies of a book than they can reasonably hope to sell through normal channels, they may *remainder* these copies. This means they sell their overstock to retailers at discounts as steep as 90% off the original list price, which is often at or below the manufacturing cost. Publishers may also find a different way to dispose of remaindered books, such as donating them to libraries or destroying the books for pulp. However, as printing efficiency and technology allow for shorter print runs, remaindering is becoming less common.

Typically, the remainder clause sets out that an author’s royalties on such sales will be 10% of the net amount received for the book. These amounts are
usually minuscule. As an alternative, you may want to try for the right to buy the remaindered books so someone else can sell them, or so you can sell or give them away yourself. Here’s how that might look:

Remainder sales will not be eligible for royalties, but prior to sale to a remainder dealer, the Publisher will make reasonable efforts to notify the Author and accord the Author the opportunity to purchase all or part of such overstock at the remainder price.

This example contains a compromise between the publisher and author. Although the author agrees to forgo her royalties on the remaindered books, she is given the option to buy the remaindered copies. Ideally, you’ll want to ask for the option and the standard 10%, but be ready to compromise.

Here’s an even more author-friendly version:

Should the Publisher decide to remainder the balance of its inventory of the Work, such remaindering not to occur during the first twelve months after Publisher’s initial publication, it shall first offer copies to the Author at the manufacturing cost of the last
printing, and the Author shall have ten business days to respond to this offer.

This example prohibits the publisher from remaining the book in its first year of life, greatly reducing the chance that it will appear on discount shelves only months after publication. If your publisher has a packed release schedule, such a clause may be worth asking for and it can give your book a fair chance to gain traction before it’s pushed aside by newer titles. Note that this clause gives the author a limited period of time in which to respond to the offer, which is a common feature of these clauses.