

DISTRIBUTING YESTERDAYS MEDIA, TOMORROW: HOW MEDIA COMPANIES MASK ANTIQUATED OPERATING MODELS WITH THE VEIL OF COPYRIGHT

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I. INTRODUCTION

Our demanding society seeks efficiency, advancement, and change from companies and their respective industries in order to provide greater value to the customer. Technological advancement represents the prime example of this evolutionary trend. While technology integration was at one time considered a large capital investment, upgrades and obsolescence have given rise to life cycles so short that it is simply rolled into the ordinary cost of doing business.¹ For the consumer, the rapid turnover in technology has driven down costs and made cutting-edge access to the digital world a reality for the masses.² Technological advancements such as the commoditization of home computers and the proliferation of the Internet, coupled with cheaper and faster hardware, have not only led to broad accessibility, but also to improvements in content delivery mechanisms. The ability to provide on-demand media has permitted distributors to place a premium on the freedom of choice; however, this potential windfall has not been adequately embraced by traditional media, including music, movie, and television distribution companies. Nonetheless, this phenomenon has not curbed the demand for such advancements.

A burdensome set of new social norms has developed as a product of new technology, norms incompatible with traditional media. The advent of large-scale file sharing, and the resultant publicity surrounding peer-to-peer ("P2P") networks³, has created the impression that computer piracy is

1. PC LIFE CYCLES: GUIDELINES FOR ESTABLISHING LIFE CYCLES FOR PERSONAL COMPUTERS, TEXAS DEPARTMENT OF INFORMATION RESOURCES 5-6, Jan. 2003, <http://www.dir.state.tx.us/eod/pc/pc-cycle.pdf> (Within slow computing organizations such as government agencies, the expected life cycle of desktops is 4-5 years and laptops 2-3 years with a 20% failure rate.).

2. *Web Access at 75 Percent*, Wired News, March 18, 2004, http://www.wired.com/news/culture/0,1284,62712,00.html?tw=newsletter_topstories_html.

3. In a P2P system, "the participants share a part of their own hardware resources (processing power, storage capacity, network link capacity, printers...). These shared resources are necessary to provide the service and content offered by the network (e.g. file sharing or shared workspaces for collaboration). They are accessible by other peers directly, without passing intermediary entities." Rüdiger Schollmeier, *A Definition of Peer-to-Peer Networking for the Classification of Peer-to-Peer Architectures and Applications*, Technische University Institute of Communication Networks, Page 1, at <http://csdl.computer.org/comp/proceedings/p2p/2001/1503/00/15030101.pdf> (last visited May 14, 2006).

a victimless crime. However, copyright holders maintain that they are victims of theft. In response, media representative groups such as the Recording Industry Association of America (“RIAA”) and the Motion Picture Association of America (“MPAA”) have pursued offensive maneuvers through a series of threats, lobbies, and lawsuits. Despite the significant amount of money being filtered through the legal and political systems, social norms have not shifted to accommodate copyright holders. Further, the media industry arguably overlooked the long-term consequences of failing to optimize their competitive advantages to adequately represent artists and serve their customers.

When dealing with large industries like film and music, the onus must be placed on the distribution companies and their representative groups to harness technology. This must occur not only to protect, but also to effectively disseminate artists’ works; the phenomenon is exemplified by programs such as Napster and Apple’s iTunes. The media companies have adopted a strategy of legal and governmental action with the goal of influencing social norms, but the effect of alienating consumers and driving them from the “legal” marketplace.

Media companies and their representative trade groups must consider both the immediate results and byproducts of their current tactics in calculating new strategies for the future. Technological advances must be employed to manage the content supply chain and preserve industry growth. This process must occur in a dynamic fashion in order to ensure flexibility within the industries well into the future.

Part I of this article will provide an overview of how technology advancements and industry deregulation have affected different media environments and their respective content delivery methods. Part II will discuss the background of media piracy and examine how one industry has managed not merely to deal with it, but ultimately to integrate it into their operations. Part III will examine business operating models, and how these models not only balance creator’s rights for protection, but also contend with evolving social norms. Part IV of this article discusses how traditional media have unsuccessfully employed regulatory and legal methods to influence social norms. Part V goes on to describe how embedded social norms, although apparently adverse to an industry’s preference, can be harnessed not only to elevate the

media product, but to capture a premium for this product. Finally, Part VI offers recommendations on how traditional media companies can change their business practices not only to better serve their customers as logistics companies.

II. THE DIGITAL DISTRIBUTION EVOLUTION

Technological advancements and relaxed federal regulation have always had a profound impact on the media and content delivery industries.⁴ The cable industry, for example, experienced rapid growth, beginning in the 1980s, as a result of both deregulation and the introduction of new technology, namely satellite-delivered cable systems.⁵ Cable experienced 80% growth between 1992 and 2003,⁶ and has emerged as a \$51 billion a year industry with nearly 74 million users in the United States.⁷

The film industry has historically benefited from similar developments. Despite a recent drop in revenue, the movie industry has experienced remarkable growth with the introduction of new technology. As of 2001, “over 70% of the population rents or goes to movies regularly, thus accounting for over 1.5 billion movie attendances each year in the U.S.”⁸ Home movie sales in VHS and DVD format have also significantly increased revenue for the movie studios. In 2004, home video purchases were up 15% from 2003 and were estimated to close out the year at approximately \$16.5 billion in sales.⁹ DVD sales alone have experienced a 30% increase between 1998 and 2003.¹⁰ While this may appear at first blush attributable to the industry’s ability to capitalize on

4. Reference to the “media industries” and “content delivery industries,” in general, includes the film, music, television and cable industries.

5. Roni Mueller & Gretchen Wattig, *The “New” Series Co-Production Deal in Network Series Television*, 31 SW. U. L. REV. 627, 655 (2002).

6. Jim Trautman, *Cable’s Economic Influence Grows*, National Cable and Telecommunications Association, August 11, 2003, <http://www.ncta.com/Docs/PageContent.cfm?pageID=325>.

7. Industry Overview: Statistics & Resources, National Cable and Telecommunications Association, <http://www.ncta.com/Docs/PageContent.cfm?pageID=86> (last visited Nov. 6, 2005).

8. James Jaeger, *The Movie Industry*, Matrixx Entertainment Corporations <http://www.mecfilms.com/moviepubs/memos/moviein.htm> (last visited Nov. 3, 2004).

9. Thomas K. Arnold, *DVD Update*, THE HOLLYWOOD REPORTER, Oct. 14, 2004, http://www.hollywoodreporter.com/thr/television/feature_display.jsp?vnu_content_id=1000672279.

10. See *infra* app. A.

consumer and technology demands, access to these revenue streams would not have been possible had the prediction of Jack Valenti, then president of the MPAA, been embraced.¹¹ Mr. Valenti, speaking before the U.S. Senate in 1984, stated, “the VCR is to the American film producer and the American public as the Boston strangler is to the woman home alone.”¹² This prophecy was not accepted by the Supreme Court,¹³ and the once-feared advances in technology have helped feed the growth of the very industries they were supposed to destroy.

III. THE PIRACY BATTLE PLAN: LESSONS FROM THE SOFTWARE INDUSTRY

While advancements in technology have generally created growth for the media companies, one notable advancement has given fits to content distributors: widespread accessibility to cyberspace.

The Internet, or more generally, computers sharing processes via communication channels, has been in existence for many years. Between 1977 and 1978, the first Bulletin Board Service (“BBS”) was introduced, which allowed anyone with a computer and a modem to connect to another computer and download or share files.¹⁴ Since that time, the general premise behind the architecture has not changed, but the scale of the distribution system has exploded. Users no longer depend on direct connections from one computer to another, and they use their computers to explore countless files and other information existing in a world built not on brick and mortar, but rather, electron transfer. One-to-one BBS connections have been replaced by a global network of servers, routers, hubs, and PCs.¹⁵ Ease of use, along with

11. *20th Anniversary of Betamax: the Court Case that Brought You the VCR*, Public Knowledge, <http://www.publicknowledge.org/content/cases/betamax%20case/> (last visited Nov. 3, 2004).

12. Valenti's comments were made in reference to Sony's new Betamax Machine. *Id.*

13. *See generally*, Sony Corp. of America v. Universal City Studios, Inc., 464 U.S. 417 (1984).

14. *See generally*, Henry Edward Hardy, *The History of the Net*, Sept. 28, 1993, (unpublished Master's thesis, Grand Valley State University), available at http://www.eff.org/Net_culture/net.history.txt.

15. Andrew Somers, *Peer to Peer Networking - Background of Copyright Issues*, Guide to Civil Liberty, <http://civilliberty.about.com/library/content/blP2Prights.htm> (last visited Dec. 11, 2005).

complex marketing trends, has brought what was once an underground system very much into the mainstream. Unfortunately, the problems that existed in the digital underground days of the BBS still exist in the age of the mainstream Internet. Users are sharing copyrighted material with complete disregard for the copyright owner's rights.¹⁶ This was not an acute issue for the film and music industries during the BBS era. The software industry, however, has long been a target for file sharing; and its ability to cope with the issue should serve as a model for the entertainment industries.

The software industry has had to deal with piracy via underground sharing for years. In 1996, the software industry estimated a \$2.3 billion loss in the U.S. and \$11.3 billion globally as a result of piracy.¹⁷ As of 2002 the numbers decreased to an estimated \$2 billion in lost revenue in the U.S., but rose to \$13 billion globally.¹⁸ These numbers represent a piracy rate over three times larger than that recently estimated by the music or movie industry.¹⁹ Unlike the music and movie industries, the software industry's product format has always been electronic, making it very easy to copy; and furthermore, the second copy is exactly the same as the original.²⁰ As new technology, copying methods, and communication methods have emerged, however, the software industry has generally not focused its energy on the losing battle of fighting to subdue these advances. Further, the software industry has not led a campaign to stop all potential home pirates, as the music and movie industries have done. Instead, they use the inevitable march of technology to operate more efficiently and to decrease their operating costs.

Striking a balance between consumer demand for ease of distribution and copyright protection, the software industry

16. *Id.*

17. Michael Coblenz, *Intellectual Property Crimes*, 9 ALB. L.J. SCI. & TECH. 235, 240 n.12 (1999).

18. *Software Piracy Fact Sheet*, Business Software Alliance, <http://www.bsa.org/resources/loader.cfm?url=/commonspot/security/getfile.cfm&pageid=1292&hitboxdone=yes> (last visited Nov. 3, 2004).

19. *Anti-Piracy*, Recording Industry Association of America, <http://www.riaa.com/issues/piracy/default.asp> (visited Nov. 4, 2004).

20. Tanya Poth, *The Computer Piracy Superhighway*, 28 DENV. J. INT'L L. & POL'Y 469, 472 (2000).

has taken a multi-tiered approach to curbing piracy.²¹ First, they have created international trade organizations to raise awareness of relevant intellectual property issues.²² Second, they utilized security features relative to the use and distribution of software.²³ Third, the software industry has created specific trade groups focused on education, amnesty, and litigation of piracy related issues.²⁴ This multi-tiered approach, in conjunction with the revision of business models to reflect modern consumer demands, has had a definitive impact on curbing software piracy.²⁵ The Business Software Alliance (BSA) is the primary trade group within the software industry that deals with piracy, and cites among the reasons for declining piracy rates, 1) greater affordability of commercial software, and 2) greater protection of intellectual property rates on the international stage.²⁶

The software industry's multi-tiered approach to piracy, with its inclusion of trade groups and regulation, may sound similar to the method pursued by the movie and music industries. Why then, has the result been different? Why have piracy rates continued to soar in the visual and audio media markets, while falling in the software industry?

IV. POWER STRUCTURES DRIVE REGULATION AND NORMS

A number of factors distinguish the software industry's effort to combat piracy from that of the film and music industries. The disparity is rooted in social norms, as well as the manner in which these superficially similar strategies have been executed thus far. However, the fundamental disparity lies in the basic structure within which these industries operate.

21. *Id.* at 483.

22. *Id.* at 484-85.

23. *Id.* at 486-87.

24. The software trade groups include the Business Software Alliance and the Software Information Industry Association, which are funded through membership dues. Their responsibilities include educating consumers on relevant issues related to the industry, promoting the legal use of software, and prosecuting cases of copyright infringement. Poth, *supra* note 20, at 487-90.

25. *Id.* at 491.

26. *Id.*

A. Identifying Industry Power Structures

Crucially, the industries are distinguishable in the number of competitors within their respective market places. The software industry is able to adjust its operating model based on a competitive, free market economy approach. The market is defined by:

dynamic, vigorous competition. . . [where] the early entrants into a new software category quickly capture a lion's share of the sales, while other products in the category are either driven out altogether or relegated to niche positions. What eventually displaces the leader is often not competition from another product within the same software category, but rather a technological advance that renders the boundaries defining the category obsolete.²⁷

Since the software industry operates on a free market economic model, prices are set by auction.²⁸ In an auction-style market place, pricing is set by what the consumers are willing to pay for one product as compared to the competition.²⁹ As new companies move into the market, prices are determined by product supply, consumer demand, marketing and advertising, competitive positioning, and product differentiation. In the software industry, through the harnessing of technology, the experience curve³⁰ has shifted and firms have become more effective and efficient. Furthermore, in the software industry, the overall barriers to, or factors necessary for entry into the marketplace are minimal.³¹

In the entertainment industries' model, the free market economy approach cannot function as it does in the software

27. Joshua A. Newberg, *Antitrust for the Economy of Ideas: The Logic of Technology Markets*, 14 HARV. J. L. & TECH. 83, 132 (2000) (citing *United States v. Microsoft*, 65 F. Supp 2d 1, 16 (D.D.C. 1999)).

28. Interview with William Spaulding, Lecturer of Mgmt., Wayne State Univ. Sch. of Bus. Admin., in Detroit, Mich. (May 24, 2004).

29. MICHAEL HITT ET AL., STRATEGIC MANAGEMENT 57 (6th ed. 2004).

30. The marginal decrease in product cost as a company advances its knowledge of how to produce the product over time. George S. Day & David B. Montgomery, *Diagnosing the Experience Curve*, Stanford University Graduate School of Business, <https://gsbapps.stanford.edu/researchpapers/library/RP641.pdf> (April 1982).

31. Juho Lindman, *Effects of Open Source Software on the Business Patterns of Software Industry 25*, (unpublished Master's thesis, Helsinki School of Economics), Fall 2004, available at <http://www.greywolves.org/~deltax/gradu.rtf>. This conclusion is a function based on substitute products, seller power, buyer power, and the sheer number of new entrants in the marketplace.

industry because the barriers to entry are significantly greater. Many theorize that the entertainment industries operate under a monopolistic model, with one or two primary industry players who use their power to exert influence over government and social choice.³² In his book, *Free Culture*, Lawrence Lessig advances this monopoly theory.³³ Despite some compelling arguments, however, Mr. Lessig's theory is flawed: the entertainment industries do not resemble the standard monopoly. Instead, they operate as an *oligopoly*. This distinction is not mere rhetoric, and must be understood because, somewhat counter-intuitively, an oligopoly may in fact possess *greater* power than a monopoly.

In a monopoly in the U.S., there are not one, but rather *two* primary players: the monopolistic company in question, and the government. In a true monopolistic market, the government has the right to regulate changes in pricing.³⁴ In fact, a monopoly that seeks to exclude firms from the market, or impair their ability to compete, cannot exist unless the government regulates it.³⁵ Therefore, it is ultimately the government which has the final word on pricing in regulated monopolies.³⁶ On the other hand, an oligopoly consists of relatively few competitors where pricing and strategic decisions by one firm directly affect the output of other firms;³⁷ there are profit incentives for firms that cooperate in the decision-making process.³⁸ This tends to lead to collusion.³⁹ Since there are more firms involved in competition, there is more freedom from government intrusion, and thus more freedom to set prices.⁴⁰ For example, the price for a CD distributed by Sony tends to be similar to a

32. LAWRENCE LESSIG, *FREE CULTURE* 88-94 (Penguin Books 2004).

33. *Id.*

34. WILLIAM A. MCEACHERN, *MICROECONOMICS* 197-98 (5th ed. 2000).

35. *Federal Trade Commission: Maintaining or Creating a Monopoly*, Free Advice, http://law.freeadvice.com/resources/gov_material/ftc_guide_to_antitrust_laws_monopoly.htm (last visited Nov. 3, 2004).

36. *Chapter 11*, Oswego State University of New York, Department of Economics, <http://www.oswego.edu/~economic/eco101/chap11/chap11.htm> (last visited Nov. 3, 2004). A common example of a regulated monopoly is the utility industry. *Id.*

37. Ted Bergstrom, Slide Presentation on Oligopoly, University of California, Santa Barbara Department of Economics, <http://econ.ucsb.edu/~tedb/Courses/Ec100AF01/PPSlides/Ch27.ppt> (last visited Nov. 1, 2004).

38. *Id.*

39. *Id.*

40. MCEACHERN, *supra* note 34, at 230-34.

CD released by Warner Music. Particularly in the music industry, five firms control 80% of all titles produced in the U.S.⁴¹ As a result, there is a risk for anti-competitive measures as a result of collusion among the dominant companies. This includes predatory pricing, temporarily dropping product prices in order to end a competitive threat.⁴² While it may be difficult to identify collusion, which is inherently covert, the unified lobbying effort by the music industry for stiffer copyright protection seems to provide a plausible example.⁴³ Arguably, the oligopoly's revenue streams are being threatened by technology that allows simplified methods of artist cultivation, promotion, and finished product distribution.⁴⁴ This permits new entrants to come into the marketplace and challenge the industry's oligopoly as more and more of the major entry barriers are being removed.⁴⁵

B. The New Social Norms

The "Dot-Com Era" created a societal and cultural shift in the treatment of Internet-based goods. As companies went live with electronic businesses and moved away from traditional brick-and-mortar enterprises, corporate valuation was no longer based on debt, revenue, and sales, but rather clicks⁴⁶ and unique visits.⁴⁷ The more visitors, and the more they accomplished in the course of their visits, the higher a company's stock rose.⁴⁸ In an effort to garner these unique

41. *Industry Brief: Music Recording 1*, Oligopoly Watch, June 28, 2003, <http://www.oligopolywatch.com/2003/06/28.html>.

42. Predatory Pricing Defined, The Economist.com, <http://economist.com/research/Economics/alphabetic.cfm?TERM=PREDATORY%20PRICING> (last visited Dec. 11, 2005).

43. LESSIG, *supra* note 32, at 248-68.

44. *Music to Whose Ears?*, University of California-Berkeley Boalt Hall School of Law Conference on the Debate over Digital Music 11, April 6, 2000, <http://www.law.berkeley.edu/institutes/bclt/events/roundtable99/background.pdf>.

45. *Id.* at 12.

46. Jerry Useem, *Dot-coms: What Have We Learned?*, FORTUNE, Oct. 30, 2000, at 82.

47. "Clicks" or "unique visitors" are website metrics used when tracking the amount of traffic a website experiences based on the number of different visitors visiting a site within a specified period of time.

Unique Visitor, Internet.com Webopedia, June 13, 2002, at http://www.webopedia.com/TERM/U/unique_visitor.html.

48. Jack Wilson, *eBusiness: The Hope, the Hype, the Power, the Pain*, Univ. of

visits or click-through users, the online enterprises adopted a unique pricing scheme designed to drive users to their electronic stores.⁴⁹ The bottom-line price was often free, and when one company attempted to charge for a particular service, its competitors undercut the pricing and gave away a comparable service.⁵⁰ Dot-Com era pricing structures were the first step in shifting social norms to so-called “access pricing”⁵¹ on the Internet. This shift is exemplified by the pricing structure used by P2P file sharing systems, which still persist today.⁵² In a P2P system, parties are permitted to share their computer files with any person anywhere without data passing through intermediary entities.⁵³ These systems have largely been used to share illegal files, such as copyrighted music and movies. Their presence can still be seen in illegal file sharing programs like KaZaA, which continues to undercut pay services like Napster and iTunes by giving away media for free.

The media industries have used litigation to suppress this norm and attempt to return order to media content distribution.⁵⁴ However, they have largely overlooked the fact that this social norm can be embraced to furnish new revenue streams.

Some philosophers opine that, “so many people. . . knowingly violating the law is culturally unhealthy.”⁵⁵ This author contends, however, that the prevailing attitude is not a sign of a society gone awry, but is merely a reflection of the desire for a market shift and a realignment of social norms.⁵⁶ File sharing, or more broadly, stealing of digital content,

Massachusetts, <http://www.jackmwilson.com/eBusiness/eBusinessBook/Finances.htm> (last visited Nov. 3, 2004).

49. Ronan McGovern, *It's the Cash Flow, Stupid!*, Stanford Business Magazine, Aug. 2002, <http://www.gsb.stanford.edu/news/bmag/sbsm0208/cashflow.shtml>.

50. Useem, *supra* note 46, at 82.

51. “Access pricing” is defined such that the bottleneck in the system sets the price for the whole system. When the customer is the bottleneck as a result of needing click-through views, the customers ultimate demand for prices to hit at, or close to, zero dollars was the target for Internet based businesses. Julian Wright, *Access Pricing under Competition: An Application to Cellular Networks*, University of Auckland Department of Economics, 1-2, <http://profile.nus.edu.sg/fass/ecs/jkw/mobileWright.pdf> (April 12, 2002).

52. LESSIG, *supra* note 32, at 125-26.

53. Schollmeier, *supra* note 3.

54. WILLIAM W. FISHER III, *PROMISES TO KEEP* 243 (Stanford Press 2004).

55. *Id.*

56. *Id.*

should not be classified as a “gateway” crime. That someone downloads this week’s hit single does not translate into bank robbery next week. The social norms we are experiencing now are really no more than a permutation of a harmless principle that has existed for quite some time; a business metric indicating the consumers want an alternative to the physical delivery of media via CD, tape, VHS or DVD.

Some people will always steal, but this is the cost of doing business. Even the corner market is going to lose some product to theft, spoilage and overruns; it is inherent in operations, just as it is in content delivery. However, this does not mean that everyone will steal, or that the corner store or online media distributor should remain permanently closed. In the case of online music programs, the aggregate industry can benefit from allowing users to sample music before purchasing, in fact, this is an option now integrated into iTunes and similar programs to allow you to try before you buy.⁵⁷ Further, the threat of being caught is not the only reason why people do not steal; people have a conscience, which leads to feelings of guilt when stealing⁵⁸ Therefore, given a plausible alternative, they will largely migrate to a pay system. During a time when Internet-based companies established that “free” is the normal and honest way of doing business, consumers followed lock step to those entities like KaZaA and Napster that simply applied this model to the media industry. The media industries apparently misinterpreted this as a transition to a heathen mindset.

V. BARRIERS TO CHANGE ARE BEING ERECTED ON ALL FRONTS

Companies in the media and content delivery industries should be realigning their models to those of a true distribution company. Instead, barriers to constructive change are being erected by lobby groups and Congress alike, including more restrictive copyright laws and continuing lawsuits against offenders.⁵⁹ Traditional media is attempting to preserve the oligopoly, litigate social norms, and perpetuate

57. Russell Roberts, *Napsternomics: What's the Most Effective Way to Protect Intellectual Property?*, The Library of Economics and Liberty, June 3, 2002, <http://www.econlib.org/LIBRARY/Columns/Robertsnapster.html>.

58. *Id.*

59. Michael Grebb, *Senate May Ram Copyright Bill*, Wired News, Nov. 16, 2004, http://www.wired.com/news/politics/0,1283,65704,00.html?tw=wn_tophead_2.

their “old guard” operations.

A. Preserve and Protect

Congress has realigned the laws governing copyright regulation and media distribution with guidance from major industry players.⁶⁰ This guidance has resulted in a regulatory scheme reflecting the needs of the oligopoly, and not necessarily the consumers or creators.⁶¹ In most cases, the individual creators do not market or distribute their creation directly to the public, but rather through an intermediary, the media distributors.⁶² In order to maintain the archaic distribution model, these companies have consolidated and rallied around lobbying actions like the Digital Millennium Copyright Act (“DMCA”), the No Electronic Theft (“NET”) Act, the Protecting Intellectual Rights Against Theft and Expropriation Act of 2004 (“PIRATE Act”) and the Inducing Infringement of Copyrights (“INDUCE”) Act.⁶³ The overriding theme of each of these statutes and proposals rests on stopping end-users from taking copyrighted material from the distributor, not from the creator; and those like the NET that do purport to specifically protect the creator are rarely enforced.⁶⁴ For example, the DMCA makes it criminal to circumvent any technological measures controlling access to copyrighted works;⁶⁵ and the PIRATE Act empowers the Justice Department to file a civil suit against P2P users allegedly violating copyright laws, but in implementation, has been utilized by the RIAA against individual file-sharers.⁶⁶

Lessig proffers that based on a net present value (NPV) analysis of a company’s existing copyright, lobbying efforts are worth the money.⁶⁷ However, this conclusion is premised on the assumption that every company owning a copyright will be able to lobby for, and succeed in, gaining a copyright

60. *Id.*

61. LESSIG, *supra* note 32, at 217-18.

62. Harry Hillman Chartrand, *Myth of the Creator*, Compiler Press, Sept. 1996, <http://www.culturaleconomics.atfreeweb.com/Myth.htm>.

63. *Copyright and Digital Media in a Post-Napster World*, GartnerG2 and The Berkman Center for Internet & Society at Harvard Law School, Jan. 2005, pp. 7-8 and 38-40, cyber.law.harvard.edu/media/files/wp2005.pdf.

64. *Id.* at 8.

65. *Id.* at 8, citing Pub. L. No. 105-304, 112 Stat. 2863, Section 1201(a)(1) (1998).

66. *Id.* at 40.

67. LESSIG, *supra* note 32, at 216-17.

extension based on their marginal contribution. Many perceive that the media companies have unlimited power to engage Congress to manipulate copyright law; but a given company itself does not necessarily possess that power. In an oligopoly, non-associated companies work together collusively to form a cartel.⁶⁸ When firms in a marketplace work together in collusive behavior to set prices, set quantities, and divide up the market, they have established an *illegal* cartel.⁶⁹ Based on the media industries' collective work, via their respective trade groups (the RIAA and MPAA), the industries have ostensibly created a cartel.⁷⁰ However, these trade groups are not classified or prosecuted as a cartel because of the distinction between tacit and explicit collusion.⁷¹ Tacit collusion occurs when companies cooperate without a specific agreement, but with an obvious eye to conformity.⁷² Explicit collusion, where companies do operate under an agreement to set prices,⁷³ is punishable by law. As Maul notes, this appears to be a distinction without a difference:

[T]he act of communication is of central importance. For economists, however, this distinction has no meaning. In game theory models of collusion, the term "agreement" does not imply a formal communication - all that is needed is for the cartel members to have an "understanding" of how others will react to their behavior. Such shared beliefs - whether acquired tacitly or not - can support a self-enforcing, collusive equilibrium⁷⁴

This distinction, though irrelevant for an economic analysis, most likely explains the dearth of antitrust actions

68. DUNCAN K. FOLEY, *ECONOMIC REASONING* 179, 2004, available at <http://homepage.newschool.edu/~foleyd/GECO6190/>.

69. *Id.*

70. Dan Krimm, *Creating a Merit-Based Music Economy: Compulsory or Blanket Licensing for Interactive Subscription Services* 19, June 2003 (unpublished manuscript, on file with the Hastings Law Journal).

71. Anthony Maul, *Are the Major Labels Sandbagging Online Music? An Antitrust Analysis of Strategic Licensing Practices*, 7 N.Y.U. J. LEGIS. & PUB. POL'Y 365, 390 (2003).

72. Subhra Bhattacharjee, *The Concept of Imperfect Competition*, Iowa State University Department of Economics, Slide 32, www.econ.iastate.edu/classes/econ101/Bhattacharjee/documents/Markets3.ppt (visited Dec. 11, 2005).

73. *Id.* at Slide 31.

74. Maul, *supra* note 71, at 390.

against the media companies.⁷⁵ Further, the specter of illegality has not stopped media distributors from overtly exerting their collective power to influence Congressional and market decisions. One of the most recent examples of this influence has come from the cable industry.

Technology accessibility has given rise to consumer demand in what is aptly known as “a-la-carte pricing” in the cable and satellite industry.⁷⁶ In an a-la-carte pricing scheme, cable subscribers are able to purchase only the channels in which they are interested, and are not required to purchase an entire cable package of channels.⁷⁷ Cable prices have climbed at three times the rate of inflation since market deregulation in 1996.⁷⁸ The cable companies claim that an astronomical leap in hardware and technology upgrades would be necessary to implement a-la-carte pricing, and the scheme would thus crush small and niche channels.⁷⁹ They claim that a-la-carte pricing “would ultimately raise subscriber costs and harm diversity on the airwaves,” since popular channels subsidize less popular channels in the package pricing scheme, contributing to programming diversity.⁸⁰ As is the case in the music and film industries, the cable companies may be misrepresenting, or at least misunderstanding, their primary purpose: effective and efficient distribution.

It is not Comcast or Cox Communication’s responsibility to support fledgling networks. Rather, their duty is to act as a means of delivery to end viewers. A-la-carte pricing would not create an all or nothing situation where the package pricing option would be eliminated; rather, it would provide an additional option whereby consumers would be permitted to choose higher priced, single-channel options. Further, cable industry’s argument that it is acting in the interest of small networks and diversity is undercut by the fact that

75. *Id.*

76. Frank Ahrens, *FCC Asked To Examine a la Carte Cable TV*, WASH. POST, May 20, 2004, at E04.

77. *Id.*

78. The cable industry experienced deregulation with the passing of the Cable Television Policy Act of 1984. Frank Ahrens, *Sorry -- No a la Carte Cable*, WASH. POST, March 26, 2004, at E01.

79. Michael Grebb, *Cable a la Carte Still Half-Baked*, Wired News, Jul. 14, 2004, <http://www.wired.com/news/politics/0,1283,64203,00.html>.

80. *Id.*

many of the small niche networks are actually in favor of a-la-carte pricing, but lack the collective power and resources to push their agenda with Congress or the FCC.⁸¹ Further, the Consumers Union and Consumer Federation of America estimates place the additional cost for a-la-carte pricing at an additional one to three dollars per month per subscriber, hardly the impracticable price increase postulated by the cable companies.⁸² The truth is, a-la-carte pricing would substantially open the market to competition, and the cable companies do not want to see that happen. This protective stance, similar to the music industry's position on packaging music rather than selling individual songs, is flawed from a strategic prospective. For consumers, it eliminates choice, and for the industry, whether it is cable television or music, it eliminates a ripe opportunity for additional revenue.

B. Damage Done

The media industry lawsuits and lobbying initially seemed to be met with some success at holding back the tide of societal norms. However, the lawsuits have now reached the point of diminishing marginal returns. The media industry has spent countless dollars on lobbying actions such as introduction of the Induce Act, which purported to target illegal actions of P2P services such that the only purpose of such systems is to make money by tricking, luring, and generally "inducing" children to commit copyright crimes.⁸³ Further, large scale lawsuits over a two year period by the RIAA against over 15,000 children, elderly individuals, single parents, and college students who may or may not have used P2P networks only led to the pinnacle of P2P networks popularity.⁸⁴ The media industry as a whole, including

81. *Id.*

82. Gene Kimmelman & Dr. Mark Cooper, *Reply Comments of Consumers Union and the Consumer Federation of America before the Federal Communication Commission*, at 2, Aug. 13, 2004, (No. 04-027), available at <http://www.consumersunion.org/pub/0813%20CUCFA%20A%20la%20Carte%20FCC%20Reply.pdf>; see also *infra* app. B (A-La-Carte Pricing computations performed by Consumers Union and the Consumer Federation of America).

83. Richard Koman, *Ernest Miller on What's Wrong with the Induce Act*, O'Reilly Policy DevCenter, Aug. 20, 2004, <http://www.oreillynet.com/pub/a/policy/2004/08/20/ErnestMiller.html>.

84. In addition, the RIAA continues to announce approximately 700 new lawsuits per month against a random assortment of P2P users. *RIAA v. The People: Two Years*

television, music, and movies, made over \$29.6 million in lobbying expenditures in 1998 and contributed an additional \$16.4 million to political campaigns.⁸⁵ The RIAA alone spent \$820,000 and \$244,260 in lobbying expenditures and donations to political campaigns, respectively.⁸⁶ Furthermore, the RIAA has spent over \$16.7 million on legal fees related to the prosecution of piracy.⁸⁷ As a result of these efforts, the RIAA has recovered only \$9.5 million in lost profits.⁸⁸ There are still 10.4 million households illegally downloading music, and for instance, “the average number of files downloaded per household grew between April and June [of 2003], from 59 to 63.”⁸⁹ Instead of working to utilize the P2P structure already in place, the music industry adopted an offensive stance against the systems and users. In hindsight, from a cost-benefit point of view, the music industry has spent nearly as much waging this battle as it would have to acquire or technologically improve the industry.⁹⁰

While the music industry points almost exclusively to illegal downloads as the source of its well-documented financial woes,⁹¹ another major economic factor is given short shrift. The U.S. was in a recession for several years, touched off by the burst of the Dot-Com bubble.⁹² As is typical in a recession, when people are insecure about their source of income, they decrease retail spending first.⁹³ The media

Later, Electronic Frontier Foundation, at 1, Nov. 3, 2005, http://www.eff.org/IP/P2P/RIAAatTWO_FINAL.pdf.

85. Alfred C. Yen, *A Preliminary Economic Analysis of Napster: Internet Technology, Copyright Liability, and the Possibility of Coasean Bargaining*, 26 U. DAYTON L. REV. 247, 272 n.81 (2001).

86. *Id.*

87. Jon Newton, *Record Labels - More Powerful than the Police*, Industry News, Aug. 4, 2003, <http://news.dmusic.com/article/7345>.

88. *Id.*

89. Roy Mark, *College File Swapping: Making the Illegal, Legal?*, Sept. 1, 2003, <http://www.internetnews.com/ec-news/article.php/3071331>.

90. If the RIAA or a related music consortium bought Napster, they would have had to contend with potential antitrust related issues. Patricia Jacobus, *Studios Look to Sidestep Antitrust Issues*, CNET News.com, Jan. 16, 2001, http://news.com.com/Studios+look+to+sidestep+antitrust+issues/2100-1023_3-250963.html.

91. *Music Biz Blames Pirates*, CDRinfo, Aug. 28, 2002, <http://www.cdrinfo.com/Sections/News/Details.aspx?NewsId=6757>.

92. Larry Dignan, *Hooray, it's an Official Recession*, Nov. 28, 2001, http://news.com.com/Hooray,+it's+an+official+recession/2010-1071_3-281613.html.

93. Mark Gongloff, *When Will We Spend Again?*, CNN Money, Oct. 26, 2001, http://money.cnn.com/2001/10/26/economy/economy_consumer/.

companies' sales, dependent upon retail goods, were bound to suffer during the recession.⁹⁴ Between 1999 and 2001, collective non-auto retail sales decreased almost 5% per year,⁹⁵ which equates to a 14.3% drop in consumer retail spending over the three-year period. The music industry reported an estimated 16% drop in consumer CD purchases during the same time period;⁹⁶ the decline appears commensurate with the aggregate effects of the recession. The estimated 1.7% difference is considered a *de minimis* deviation for purposes of economic analysis. The numbers suggest that piracy is wrongfully targeted as the primary cause of financial woes in the music industry.⁹⁷

C. Using Copyright Laws to Tighten the Stranglehold

Somewhat counter-intuitively, artists, musicians and all those who add to the creative energy in our society are the ones who suffer most due to big media's actions to protect their antiquated business models and expand copyright protection. One of the foundations of artistic creation is the ability to compose new works based on the work of other artists, a concept known as derivative use.⁹⁸ Some critics prophesize the death of derivative use through amplified statutory protection of copyright, particularly the increasing of copyright duration.⁹⁹ These reforms are being accomplished, at least partially, through intense lobbying efforts, which have resulted in the DMCA,¹⁰⁰ the NET Act,¹⁰¹ and the Sonny Bono Copyright Term Extension Act ("CTEA"), most notably.¹⁰² As stated above, this legislation purports to support creators, but, in practice, has simply been wielded as

94. See generally, *Retail Industry: Top 10 Issues 2004-2005*, Deloitte Consulting (2004), http://www.deloitte.com/dtt/cda/doc/content/US_CB_RetailTop10.pdf.

95. *Id.* at 3.

96. Rafael Rob & Joel Waldfogel, *Piracy on the High C's: Music Downloading, Sales Displacement, and Social Welfare in a Sample of College Students* 1 (Nat'l Bureau of Econ. Research, Working Paper No. w10874, 2004), available at <http://www.nber.org/papers/w10874>.

97. See Dignan, *supra* note 92.

98. Molly Wood, *Web Innovation and Fair Use Bite the Dust*, Aug. 16, 2002, http://reviews.cnet.com/4520-3513_7-5021236-1.html.

99. LESSIG, *supra* note 32, at 136.

100. *Id.* at 157.

101. *Id.* at 215.

102. *Id.*

a weapon by the media industries in a random manner with weak checks and balances for creation versus stealing.¹⁰³ Most of this legislation is very recent, and its effects are therefore still only a matter of prognostication. Many media outsiders see this legislation as upsetting the delicate balance between the free flow of ideas on one hand, and the protection of rights associated with the expression of these ideas on the other, tipping the scales far too much toward the latter. They view the legislation as offensive to the Constitutional framers' vision of copyright.¹⁰⁴

V. SOCIAL NORMS AND PRICING SCHEMES

If social norms cannot be readily changed, they can in fact be harnessed. First, however, the manner in which consumers pay for product differentiation must be understood. Second, the industries' business models and exploitable assets must be considered before change can be implemented.

A. We Will Pay for Our Freedoms

At one time, consumers spent hard earned dollars for a product called a Pet Rock, which was no more than a stone in a box.¹⁰⁵ Despite plenty of free rocks outside, consumers were drawn to this product by clever marketing and packaging.¹⁰⁶ The success of the Pet Rock indicates that people will pay a premium for a product with unique attributes and delivery; a consumer could have a dirty, unfriendly rock for free from the side of the road, or a pleasant, well-trained rock in a box for a premium. The lesson is that when a free market coexists with a pay market there must be sufficient differentiation to motivate consumers to pay for a product as opposed to taking

103. See, *supra*, note 63.

104. Graeme W. Austin, *Does the Copyright Clause Mandate Isolationism?*, 26 COLUM. J.L. & ARTS 17, 37 (2002).

105. *Pet Rock*, http://www.super70s.com/Super70s/Culture/Fads/Pet_Rocks.asp (last visited Nov. 3, 2004).

106. There were countless unclaimed rocks in nature, when dealing with digital copies of copyrighted songs, there are countless copies available as well, however the copyright holder lays claim to those as too. Daniel A. Tysver, *Rights Granted Under Copyright Law*, Beck & Tysver, P.L.L.C., 2005, <http://www.bitlaw.com/copyright/scope.html>.

it for free.¹⁰⁷

The entertainment media industries have overlooked a very major point as they have constructed their strategy: consumers will pay more for the freedom of choice. Both Apple iTunes and the new, entirely revamped, Napster online music service are prime examples of paying a premium for access, delivery method, and format choice. On Napster, it costs users \$9.95 a month for a subscription to essentially *rent* music tracks.¹⁰⁸ If users wish to burn music to a CD to listen to it in a conventional CD player, they incur an additional \$0.99 fee per song.¹⁰⁹ In comparison, the average price of a CD was \$15.06 in 2003;¹¹⁰ the average number of tracks on a rock CD was 13 in that year.¹¹¹ Thus, the average cost per song on a rock CD was \$1.16.¹¹² While this price may at a glance appear to itself justify a \$0.99 price per song on Napster, consider the following information: with over three million paying users on Napster, a user would have to download 62 songs per month to justify the monthly fee, a figure the average user would not reach. Consumer willingness to pay a greater fee per song derives from the premium placed on the freedom to choose single tracks.¹¹³

B. *Missing the Boat*

Misclassification of company, or for that matter, industry-wide directives, will lead to a loss of revenue and failure to progress and survive unless the ship is righted.¹¹⁴ The case of Eastman Kodak presents a strong example of this from

107. *Id.*

108. Napster Website, http://www.napster.com/more_about_napster.html (last visited Nov. 5, 2004).

109. *Id.*

110. Recording Industry Association of America 2003 Yearend Statistics, <http://www.riaa.com/news/newsletter/pdf/2003yearEnd.pdf> (last visited Nov. 9, 2005).

111. *Average Number of Tracks by CD for each Genre*, IT Innovations and Concepts, <http://www.itic.ca/DIC/music/2003/09/avg-content-cd-tracks.jpg> (last visited Nov. 5, 2004).

112. Computed as [\$15.06 per CD] divided by [13 songs per CD].

113. Computed as [\$9.95 monthly fee] divided by [\$1.16 – \$0.99 as the difference between CD and Napster per song fees]. Napster does “not disclose any information regarding the purchasing habits of [its] members,” therefore an exact estimate of the number of songs downloaded per user, per month cannot be obtained. E-mail response from Dana Harris, Director of Napster Corporate Communications, Los Angeles, CA (Nov. 16, 2004, 12:37 P.M.) (on file with author).

114. MICHAEL HITT ET AL., *supra* note 29, at 83.

outside of the entertainment industries. Focusing on its ability to produce high-end prints from photographic film, Kodak, for years, regarded itself as a picture company.¹¹⁵ However, Kodak's revenue stream absorbed a crushing blow with the advent of digital imaging.¹¹⁶ As the price of digital cameras dropped, more people were introduced to digital technology and fewer people paid to expose traditional prints.¹¹⁷ Instead, consumers began storing images digitally on their computers, and printing them sparingly at home. Kodak did not begin to recover its market share until it reverted to an *imaging company* model.¹¹⁸ By viewing themselves as an imaging company and focusing on the images associated with any camera, digital or film, Kodak appropriately moved to a structure focused on customer demand and an evolving marketplace.¹¹⁹

A Strengths, Weaknesses, Opportunities and Threats ("SWOT") analysis as applied to the music industry, reveals that it, like Eastman Kodak, suffers from an improper focus. A SWOT analysis is a method of conducting an external assessment, the process by which a company observes the interaction between itself and the environment in order to understand the implications of changes taking place outside of the company.¹²⁰ Hence, a firm or industry dynamically examines the strengths, weaknesses, opportunities and threats inherent in a given proposed action.¹²¹ A firm's strengths are those resources and capabilities that are valuable, rare, costly to imitate, and sustainable.¹²² In the case of the music industry, the copyrights themselves are not a sustainable competitive advantage, at least not in the long run. While the copyrights are valuable and theoretically sustainable based on current federal regulation, technology has as a practical matter made them inexpensive to imitate. Hence, the music industry must identify and exploit a

115. Laura Rich, *Case Study: Eastman Kodak Co.*, CIO Insight, June 1, 2004, <http://www.cioinsight.com/article2/0,1397,1610188,00.asp>.

116. *Id.*

117. *Id.*

118. *Id.*

119. Rich, *supra* at 115.

120. Peter M. Ginter, Linda E. Swayne & W. Jack Duncan, STRATEGIC MANAGEMENT OF HEALTH CARE ORGANIZATIONS 31 (4th ed. 2002).

121. HITT ET AL., *supra* note 29, at 52-59.

122. *Id.* at 84-88.

different strength.

The ability to control social norms is a strategic weakness in the industry as is. While the industry is convinced it can do so, as discussed above, the legal approach is showing marginal returns at best.¹²³ Further, opportunities and threats come from an environmental analysis of how a course of action interacts with the corresponding environments; namely the socio-cultural, economic, technological, and political/legal environments.¹²⁴ When the entertainment media industries chose to embark on a course of lobbying and lawsuits, attacking those “stealing” from the industry appeared to be a logical maneuver. However, the industries failed to conduct a dynamic analysis of the corresponding environments, and arguably failed to consider the backlash and villainization that would occur in response to a regime of backroom dealing and lawsuits against teenagers. Society’s values and attitudes (social norms) were already in a state of transition, and the media industries overestimated their ability to stem the tide. Furthermore, technology had advanced far beyond what the industries could control.¹²⁵

Failure to properly forecast the repercussions of a business plan or an action can also result in an unwanted regulatory scheme.¹²⁶ An example of this occurred when the Federal Communication Commission’s (FCC) crusade against pop-culture radio icon Howard Stern drove him from the free airwaves to satellite broadcasting.¹²⁷

Radio companies like Clear Channel have a stranglehold on the radio market.¹²⁸ When there was no alternative to the free airwaves, companies like Clear Channel had little incentive to influence the government’s regulatory regime over the content in their broadcast medium. However, the success of advancements like satellite radio has, in effect, blindsided Clear Channel. Consumers once again have opted

123. See discussion *infra* Part IV.B

124. HITT ET AL., *supra* note 29, at 44-52.

125. See discussion *infra* Part IV.B

126. Interview with William Spaulding, Lecturer of Mgmt., Wayne State Univ. Sch. of Bus.Admin., in Detroit, MI (May 31, 2004).

127. *Shockjock Stern to Go Satellite*, CBS News, Oct. 6, 2004, <http://www.cbsnews.com/stories/2004/04/16/entertainment/main612355.shtml>.

128. Randy Dotiga, *Murky Water for Clear Channel*, Wired News, Aug. 07, 2002, <http://www.wired.com/news/business/0,1367,54038,00.html>.

to pay for their freedom of choice.¹²⁹ Overregulation of traditional radio has motivated traditional radio advocates to leave the free airwaves and enter the pay marketplace.¹³⁰ The result has been a loss of market share for traditional radio broadcasters who have not used their influence to slow the torrent of over-reaching federal regulations.¹³¹

VI. ADAPT AND SURVIVE

In clinging to their antiquated business models, traditional television, film and music companies must consistently work harder to even maintain their present market position.¹³² The media companies evince the two primary indicators of a dying industry: rampant consolidation or excessive industry mergers, as well as extensive lobbying in Washington.¹³³ They must consider a new approach in order to survive.¹³⁴ The new model must strike a balance between fair use for innovation and protection of copyrights. Copyright law must be the protectorate of the public interest, not just individual creators;¹³⁵ this view will permit the copyright framework to focus less on monetary interests and more on fostering creativity.¹³⁶

A. Basic Framework: The Logistics Company

The media companies need to look at themselves as logistics companies. Based on a SWOT environmental analysis, as discussed above, their copyrights are no longer a strategic advantage. However, the marketing and distribution network the media companies have at their disposal is very much an advantage. The media industries' strength is no

129. Associated Press, *Shock Jocks Boost Satellite Radio Profile*, Oct. 19, 2004, <http://www.wvec.com/sharedcontent/features/printwire/100904ccjrcwentshockjocks.16fd9a09.html>.

130. *Id.*

131. Seth Seutel, *Viacom Posts Loss on Blockbuster Charge*, Oct. 28, 2004, <http://music.yahoo.com/read/news/12174551>.

132. Interview with Bruce Lynskey, Clinical Professor of Mgmt., Vanderbilt Univ., Owen Graduate Sch. of Mgmt., in Nashville, Tenn. (Nov. 16, 2004).

133. *Id.*

134. *Id.*

135. Jeremy Paul Sirota, *Analog to Digital: Harnessing Peer Computing*, 55 HASTINGS L.J. 759, 780-81 (2004).

136. *Id.*

longer the product; technology has lowered production costs to make production a reality for all artists and small media companies alike. Rather, the key strength lies in their ability to bring that product to the marketplace, because getting the product to the public is still difficult.¹³⁷ While anyone can develop an idea, song, movie concept or television show, the big media companies possess the marketing and distribution capabilities that elude the independents. They are the gatekeepers between the artist and the masses, and this competitive advantage must be fully exploited to survive.

A logistics company, which the media companies must be, serves numerous and diverse constituents. There are artists who need their product distributed and marketed, and there are end users (consumers) who will receive the product in multiple formats. Neither can be ignored because both are necessary for the model to operate properly. With this model, the traditional media format can coexist with the new methods, but the primary focus shifts to a more profitable method of operation.

B. Technology Strategies

The value society places on a creative work should not be determinative of the amount of protection it is afforded. However, the media industries have taken a myopic approach to protection, using the power of their lobby to extend copyright protection. Instead, the focus for protecting the artist needs to be on technology, security protocols¹³⁸ and systems integration.¹³⁹ As evidenced in the software industry, companies need to work *within* the bounds of the technology available, not *against* it.¹⁴⁰

Some industry advocates argue that there is no reason to invest in new technologies and digital distribution methods because they will simply become outdated, and cheaper to

137. Recording Industry Association of America, <http://www.riaa.com/news/marketingdata/cost.asp> (last visited Dec. 15, 2004).

138. Security protocols such as protecting how the ability to digitally copy media can be restricted if the artist or distributor chooses to do so.

139. System integration includes putting the system components for recruiting, security and distribution and integrating them into a complete network such that all the components work together in a fluid, non-piecemeal manner.

140. See discussion, *supra* Part II.

implement, in the future.¹⁴¹ While this contention has some theoretical merit, it fails to account for the multiple timing strategies involved in technology integration, each with relative advantages and disadvantages.¹⁴² Specifically, there are three approaches a media company might take: the first mover, second mover, and late adopter strategies.

With a first mover strategy, a company brings a product to market when there is no comparable product available. The first mover strategy usually requires a large investment in research and development, but provides the opportunity to firmly associate the company name with the product.¹⁴³ With a second mover strategy, a company follows the first mover, but reaches the market before there is much competition. The second mover strategy often requires less research and development, because a company can utilize information from the first mover, the second mover, however, often obtains this benefit at the price of conceding the first movers established market share.¹⁴⁴ Finally, with a late adopter strategy, a company goes to market with a product that has already been tested and adopted by consumers.¹⁴⁵ In this scenario, research and development cost is very low if it exists at all; but this strategy usually results in competing on price as opposed to innovation.¹⁴⁶

Consequently, one cannot argue that declining to adopt, or taking a “wait-and-see” approach to new technology, is *always* smart simply because technology will inevitably decrease in cost over time.¹⁴⁷ While copying the competition expends fewer resources, other competitive advantages will be lost.¹⁴⁸ Certain companies, such as Sony Corporation, have made their mark with a first mover advantage, introducing and perfecting technological advances before the competition.¹⁴⁹

141. LESSIG, *supra* note 32, at 166.

142. HITT ET AL., *supra* note 29, at 149-50.

143. *Id.*

144. *Id.*

145. *Id.*

146. HITT ET AL., *supra* note 29, at 149-50

147. Han T.J. Smit & Lenos Trigeorgis, Quantifying the Strategic Option Value of Technology Investments (unpublished manuscript), at <http://www.realoptions.org/papers2004/SmitTrigeorgisAMR.pdf> (last visited Nov. 2, 2005).

148. *20th Anniversary of Betamax: the Court Case that Brought You the VCR*, *supra* note 8.

149. Charla Griffy-Brown, *Small Firms Keep R&D Vibrant*, GRAZIADIO BUS.

Others, such as Hitachi, have exercised a follower strategy in order to optimize the late adopters market.¹⁵⁰ Each has a niche that fits their individual business model, and empirical data shows that different competitors may benefit from either the first or second mover strategies.¹⁵¹ However, this same data also favors a first mover strategy, or a hybrid strategy, when technological advancements are necessary in order to maximize returns.¹⁵² The technology employment strategy for content distribution by the media industries must be premised on these ideas. Theirs cannot be a static strategy, but must be one continually providing more differentiation for consumer and creator alike.

C. Structural and Supply Chain Integration

Media companies need to depart from their current vertically integrated structure, whereby they own and control virtually the entire supply chain, upstream and downstream.¹⁵³ This variety of integration has resulted in multiple inefficiencies, primarily due to a lack of competition from suppliers and greater overall operating costs.¹⁵⁴ By way of example, if there are three downstream suppliers all competing for business, incentive to keep costs down exists, but when a buyer ostensibly acts as its own supplier, the benefits from competition are lost. These costs have of course been passed on to the consumer.

Within the media industries, the prime example of the problems with a vertical integration scheme is the merger of AOL and Time-Warner in 2000.¹⁵⁵ This merger was supposed to increase efficiency and lower costs, but instead, over \$160 billion in market value was lost based on an inability to optimize supply chain synergies.¹⁵⁶ The media industries must consider a process of decentralizing operations to

REPORT, 2000, available at http://gbr.pepperdine.edu/021/print_r&d.html.

150. *Id.*

151. Smit & Trigeorgis, *supra* note 147, at 3-7.

152. *Id.*

153. Strategic Management, Quick MBA, <http://www.quickmba.com/strategy/vertical-integration/> (last visited Nov. 12, 2004).

154. Kevin Maney, *The Strategy: Pack Distribution and Content into Powerhouse Combo*, USA TODAY, Feb. 16, 2004, available at http://www.usatoday.com/money/media/2004-02-16-comcast_x.htm.

155. MCEACHERN, *supra* note 34, at 56-63.

156. *Id.*

maximize competitive efficiencies. This change will of course be met with resistance because it threatens the oligopoly, but it is necessary to lower costs, meet consumer demand, and revitalize the entertainment industries.

D. Disputes Will Arise

As in the software industry, when digital media distribution is involved, piracy is inevitable, whether willful or "innocent." This alone is not a reason to avoid entering a market or upgrading a distribution network. It is, however, reason enough to ponder how such claims will be handled. The past and present strategy has been a wide-scale legal assault on distributors and users in the courtroom, with marginal results at best.¹⁵⁷ Forcing a party to settle because they are unaware of their legal rights or unable to afford adequate counsel¹⁵⁸ does not adequately or efficiently accomplish the underlying objective of protecting the copyright holders while educating the public.¹⁵⁹ The media industries must consider forms of alternative dispute resolution (ADR) in order to streamline the process for all parties.

An ADR model will provide a number of yet unrealized benefits. In general, the mediation process has been embraced in general because it reduces many of the risks associated with litigation in terms of both tangible and intangible costs.¹⁶⁰ Tangible costs include the dollar value placed on litigation in court fees and legal fees; intangible costs include those related to lost productivity and emotional strain on the parties themselves.¹⁶¹ Undoubtedly there are negatives related to ADR as well, including lower average settlements;¹⁶² but currently, the average consumer case settles for only approximately \$3,000.¹⁶³ If the media

157. See discussion, *supra* Part IV.B.

158. LESSIG, *supra* note 32, at 200.

159. Recording Industry Association of America, April 15, 2004, <http://www.riaa.com/news/newsletter/041504.asp>.

160. Kevin M. Lemley, *I'll Make Him an Offer He Can't Refuse: A Proposed Model for Alternative Dispute Resolution in Intellectual Property Disputes*, 37 AKRON L. REV. 287, 312-13 (2004).

161. *Id.* at 313-14.

162. *Id.*

163. Paul Roberts, *RIAA Sues 532 'John Does'*, PC World, Jan. 21, 2004, <http://www.pcworld.com/news/article/0,aid,114387,00.asp>.

industries wish to honor their mantra that legal action is necessary in order to protect the artists,¹⁶⁴ then ADR is the answer.¹⁶⁵ Claims are settled in a timely manner, costs are lower for all parties, and judicial economy is maximized.

VII. CONCLUSION

The relevant question must not be, "can this new model make money," but rather, "how long can the old guard last before the entire industry implodes?" The writing is on the wall, and traditional media companies are in a perilous situation. New competitors are setting up distribution channels that will allow copyrighted artists to reach the masses with their work in a manner that will not require current distribution channels.¹⁶⁶ The media companies have allowed their size and bureaucracy to place them in a position other oligopoly industries have found themselves in before: fighting for ever diminishing pieces of market share while relatively small competitors begin to dominate the marketplace.¹⁶⁷ As observed in the U.S. automotive industry, long thought to be one of the strongest oligopolies, failure to adapt allowed foreign companies to capitalize on system efficiencies and changes in governmental regulation¹⁶⁸ to bring down the oligopoly.¹⁶⁹

The media industries must understand that neither technology nor the pirates associated with technology

164. Steve Marks, *General Counsel, Recording Industry Association of America, Florida Atlantic University*, Recording Industry Association of America, April 15, 2004, <http://www.riaa.com/news/newsletter/041504.asp>.

165. Lemley, *supra* note 160, at 326.

166. These services include programs such as Digidesign Pro Tools, Adobe Audition, Apple GarageBand, and Live365.com. Services such as these allow users to record, remix, publish, post and gain airplay free of any traditional medial company. Eric Butterfield, *Record and Promote Your Own Music*, PC WORLD, Sept. 28, 2004, <http://www.peworld.com/news/article/0,aid,117926,00.asp>.

167. See Lemley, *supra* note 160.

168. Kerry A. Chase, *Economies of Scale, Domestic Politics, and Trade Conflict at 26-27* (1999) (unpublished manuscript), available at <http://ase.tufts.edu/polsci/faculty/chase/economies.pdf> (last visited Nov. 3, 2005).

169. Toyota, a Japanese manufacturer, is targeting a global market share of 15 % by the end of the decade, which would put it ahead of the current U.S. auto leader, General Motors, and further establish its dominance over the U.S. automotive oligopoly known as The Big Three (Ford, GM, and Daimler-Chrysler). MICHELINE MAYNARD, *THE END OF DETROIT 15* (Doubleday 2004).

advances are the source of all evil. In this day and age, they are factors that simply must be dealt with. Technological advancements and the accessibility of information have greatly reduced the cost to consumers and digital media content providers. However, along with these advancements, a number of roadblocks have arisen. These factors include the need for enhanced security, a reevaluation of the current operating environment, and a reassessment of consumer demand for media in multiple formats. An industry cannot ignore these external environmental factors when designing its strategy, and a failure to recognize this will result in a failure to sustain growth.

Technology has not been the only change to which the industries have responded poorly. Social norms have evolved since the Dot-Com era. For better or worse, consumers care less about the legal implications of their actions and more about the quality of the product they buy.¹⁷⁰ A failure to recognize the benefit of consumers' desire to pay for their freedom of choice is a failure to recognize a market niche that can easily be exploited, and in fact has been exploited by companies such as Napster and Apple, through iTunes.

The media companies' approach has been thus far misguided. They push for stiffer copyright laws, longer periods of enforcement, and additional statutory coverage; but this strategy is not helping to expand the aggregate creative content in society. The artists, the parties who truly deserve the copyrights, are being left out of the equation. The media industries are not achieving the results the artists deserve through their legal assault on piracy alone. Furthermore, the media industries are failing to look at the long-term implications of their increased regulation. It will drive consumers to new media, a scenario best exemplified by the FCC's recent overregulation, driving radio personalities and consumers to pay for satellite radio.

The media industries must make a dynamic, strategic reevaluation of their respective industries and focus on their true strengths, namely their distribution and marketing machines. Further, they need to reassess their supply chain management and vertical integration plans to create as much efficiency in the system as possible. This will reduce product price and decrease time to market while capitalizing on social

170. Tysver, *supra* note 106.

norms. Finally, the media industries need to reconsider their legal approach. Piracy will always exist and while lawsuits may be optimal for large-scale distributors, they do little to equitably resolve individual disputes. They also do not fulfill the media industries desire to "educate" the public that piracy is bad. An alternative dispute resolution process will not only streamline claims, they have the potential to maximize the return on investment into an ADR system.

The music, film, and television industries can look to the software industry as a model. There is no question that a select number of competitors dominate the software industry. Companies like Microsoft, Oracle, Dell, and IBM¹⁷¹ command their respective market in the same manner companies like MGM, Sony, and Viacom dominate their industry.¹⁷² However, new entrants and technologies provide a constant threat to the software giants' respective market share. The attack by open-source operating system Linux on Microsoft Windows is a notable example.¹⁷³ However, even with the assault from pirates and competitors alike, the software giants are able to prevail through a multi-tiered approach including legal, legislative, and competitive reassessment. None of these factors alone are enough to retain a lead in the industry; however, in the aggregate, they allow these companies to survive, grow, and thrive.

By reevaluating their operating structure and consumer demand, the media distributors can come out on top and continue to thrive; it has been done before. Continuing to head in the current direction will not lead to any form of Fountain of Youth for preservation, but rather will result in the same fate as the Fountain's other seekers, nothing more than an untimely demise.

171. Wylie Wong, *Software Giants Unite for Web Services*, CNET News, Feb. 5, 2002, http://news.zdnet.com/2100-1009_22-830090.html.

172. *Industry Brief: Music Recording 1*, *supra* note 41.

173. "Linux garnered a 27% share of operating-system software for computer servers sold last year, up from 24% in 1999 and 17% in 1998, according to market-researcher International Data Corp." *Linux Gains Market Share, Respectability*, Librenix, June 27, 2003, <http://librenix.com/?inode=784>.

APPENDIX A – DVD GROWTH 1998-2003 ¹⁷⁴

Year	Sell-Through DVDs (In Millions of Units)	Percent Change from Prior Year
1998	32.7	---
1999	91.3	35.82%
2000	174.4	52.35%
2001	350.0	49.83%
2002	650.6	53.80%
2003	985.3	66.03%

174. U.S. Entertainment Industry: 2003 MPA Market Statistics, Motion Picture Association of America, <http://mpaa.org/useconomicreview/content.htm> (last visited November 5, 2005).

APPENDIX B – A-LA-CARTE PRICING IN A MIXED BUNDLE ENVIRONMENT ¹⁷⁵

Network Type	Subscribers		Bundled	
	Bundled	Mixed bundled	Revenue per month	Ad revenue per month
	(000,000)	(000,000)		
General	87	70	\$0.67	\$0.48
News	86	60	\$0.20	\$0.20
Older	80	52	\$0.18	\$0.12
Younger	84	63	\$0.25	\$0.24
E. Niche	34	20	\$0.09	\$0.06
E. Mass	64	38	\$0.08	\$0.09

Network Type	Monthly A-La-Carte fee needed to replace lost network revenue				Subscriber price (with cable mark-up)
	Subscriber	Ad	Marketing	Total	
General	\$1.12	\$0.11	\$0.38	\$1.61	\$2.72
News	\$0.50	\$0.10	\$0.16	\$0.76	\$1.28
Older	\$0.60	\$0.09	\$0.20	\$0.89	\$1.50
Younger	\$0.50	\$0.08	\$0.20	\$0.78	\$1.32
E. Niche	\$0.45	\$0.07	\$0.15	\$0.67	\$1.13
E. Mass	\$0.40	\$0.12	\$0.17	\$0.69	\$1.16

Definitions:

- General** – mainstream networks such as ESPN, Lifetime, USA and Nickelodeon
- News** – news networks such as ABC, CNN, and Fox News
- Older** – older trending networks such as A&E and Bravo
- Younger** – younger trending networks such as Disney, Comedy Central and MTV
- E. Niche** – emerging niche networks such as Oxygen, BET Jazz, and Soapnet
- E. Mass** – emerging mass market networks such as The Family Channel, SciFi and Court TV

175. Gene Kimmelman & Dr. Mark Cooper, Reply Comments of Consumers Union and the Consumer Federation of America before the Federal Communication Commission, No. 04-027 at 53, Aug. 13, 2004, <http://www.consumersunion.org/pub/0813%20CUCFA%20A%20la%20Carte%20FCC%20Reply.pdf>.