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FEDERAL TRADE COMMISSION

PUBLIC WORKSHOP

PEER-TO-PEER FILE-SHARING TECHNOLOGY:

CONSUMER PROTECTION AND COMPETITION ISSUES

Thursday, December 16, 2004
9:00 a.m.

Federal Trade Commission
Sixth and Pennsylvania Avenue, N.W.
Washington, D.C.

For The Record, Inc.
Waldorf, Maryland
(301)870-8025

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FEDERAL TRADE COMMISSION

I N D E X

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 Commissioner, FTC 5

PANEL SIX: PEER-TO-PEER FILE-SHARING AND ITS IMPACT ON
 COPYRIGHT HOLDERS

Moderator: John Delacourt, Chief Anti-trust
 Counsel, FTC 11

Panelists:

David Carson, General Counsel, U.S.
 Copyright Office 13

Stanley Besen, Vice President, Charles River
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Mark Bohannon, Senior Vice President,
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 Association 33

Andrew Moss, Director of Worldwide
 Technical Policy, Microsoft Corp. 42

Dean Garfield, Vice President, Motion
 Picture Association of America 51

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 and writer 57

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COMMISSIONER HARBOUR: Thank you, Tom. Good morning, and welcome to day two of our Peer-to-Peer workshop. I am delighted to see the returnees and so many of you here this morning.

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Thanks to our superb panelists, yesterday's very active discussion addressed many cutting edge issues relating to the development of peer-to-peer technology.

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Peer-to-peer file-sharing may substantially improve the Internet experience by increasing speed and access to content, while decreasing the need for storage space.

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However, as we have heard, among other things yesterday, peer-to-peer may at times increase vulnerability to unwanted content; spyware and viruses. It is essential consumers be informed about these potential risks.

1 Think back, if you will, to the time when the
2 automobile was first introduced. Some horse owners and
3 sellers urged that cars might hurt horses and their
4 riders, and that new vehicles therefore should be banned
5 entirely.

6 Of course, other solutions emerged to promote
7 safety while allowing consumers to benefit from that
8 promising new technology. And as with the automobile, it
9 is my hope that faith and responsible solutions, too,
10 will emerge in the peer-to-peer context. So that the
11 future of this promising new technology also will
12 flourish.

13 As Chairman Majoras noted yesterday, a
14 discussion of P-to-P issues is both important and timely.
15 She also explained that the Federal Trade Commission is
16 particularly well-positioned to host this workshop
17 because peer-to-peer file-sharing technology implements
18 and implicates both the consumer protection and the
19 competition matters, and new issues certainly will emerge
20 as the technology continues to develop.

21 As part of our consumer protection mission, the
22 FTC must remain vigilant in protecting consumers against
23 unfair trade practices, deception, and anti-competitive
24 conduct.

25 But in order to remain true to our mission, we

1 also must take care not to pursue, create, or condone
2 policies that inadvertently impede the evolution and
3 adoption of useful new technologies to the long run
4 detriment of consumers and businesses.

5 Our goal in sponsoring this workshop is to
6 bring together individuals and groups who develop and use
7 peer-to-peer technology, as well as those whose existing
8 business models are affected by it, to ensure that
9 policy-makers and the public are as well-informed as
10 possible.

11 Yesterday's panel set a very high bar, and we
12 expect an equally high level of discussion from this
13 morning's panelists, who will focus on some of the
14 intellectual property questions that arise in the
15 peer-to-peer context.

16 Today's panels will look at the impact of
17 P-to-P file-sharing technology on several groups: on
18 industries that rely heavily on copyright protection; on
19 consumers who use the technology; on businesses that
20 redistribute the copyrighted material; and on artists
21 whose work is copyrighted.

22 The first panel will examine the impact of
23 peer-to-peer file-sharing technologies on the copyright
24 holders. Representatives from the legal, economic, and
25 engineering communities will explore a key question, and

1 that is, how to protect the property rights of creative
2 individuals without stifling technological evolution that
3 could benefit consumers and enhance business efficiency.

4 Balancing these competing interests is likely
5 to require some new thinking about the law. For example,
6e the panel will address whether copyright laws might be

1 Christmas Carol, and a movie is made from it, both the
2 motion picture industry and consumers may benefit.

3 Overall, this session today should be very
4 informative and highly thought provoking.

1 create, promote, and sell their work."

2 The study also found, however, that artists are
3 divided about the impact and importance of free file-
4 sharing and other copyright issues. Take, for example,
5 one of the public comments the Commission received in
6 anticipation of this workshop.

7 It came from an artist who, in order to
8 generate interest in his work, offered all of the music
9 of his first album for free to anyone who wished to remix
10 his music.

11 According to his comments, remixers used his
12 tracks around the globe. As this example demonstrates,
13 peer-to-peer technology may offer great rewards for
14 artists, for copyright holders, and for music lovers
15 alike.

16 However, it will achieve its greatest promise
17 only if all parties can agree on a system that fairly
18 compensates artists and copyright holders for the value
19 of their creative work.

20 Hopefully, our panelists will consider whether
21 the motion picture and recording industries are equally
22 likely to be able to work collaboratively with proponents
23 of peer-to-peer technology to achieve maximum benefits
24 for consumers and artists alike.

25 So let me close by saying once again how very

1 pleased I am by your interest and by your participation
2 in this peer-to-peer workshop. On behalf of the
3 Commission, I offer my sincere thanks to all of the
4 panelists, and I hope you enjoy today's program. Thank
5 you.

6 (Applause.)

7 MR. PAHL: Thank you, Commissioner Harbour. I
8 would like to begin now with our first panel, which is
9 peer-to-peer file-sharing and its impact on copyright
10 holders. The moderator of this panel is John Delacourt,
11 who is chief anti-trust counsel in the FTC's Office of
12 Policy Planning.

13 If John and the panelists could come forward,
14 that would be great.

15 MR. DELACOURT: Good morning, everyone, and it
16 looks like we have a good crowd again today. And I would
17 like to take this opportunity to thank all of you for
18 joining us this morning.

19 Our first panel this morning, as Commissioner
20 Harbour indicated, is on P-to-P file-sharing and its
21 impact on copyright holders. This issue, perhaps more
22 than any other, has generated interest in P-to-P networks
23 and inflamed strong passions on all sides.

24 Content providers are, not surprisingly,
25 concerned about the sheer scope of P-to-P piracy of

1 copyrighted music and videos. This activity not only
2 results in substantial revenue losses, which some
3 estimates place in the millions of dollars, but
4 potentially reduces the incentives of the creative
5 community to generate more and better original works.

6 Users of P-to-P networks, in contrast, contend
7 that the impact on copyright holders has been
8 exaggerated. Many of them are deeply offended by what
9 they regard as heavy-handed enforcement efforts, which
10 seem to pit major record labels and movie studios against
11 individual college students. They argue that the content
12 providers should spend more time thinking about how to
13 better use this emerging channel of distribution and less
14 time thinking about how to shut it down.

15 Technology companies have also raised concerns.
16 While generally supportive of strong copyright
17 protection, they argue that enforcement efforts should be
18 focused on bad actors, not the technology itself. In
19 other words, technological solutions to the copyright
20 infringement problem can and should be explored, but
21 content providers should not be given a seat at the

1 lot of thinking on this issue and should have some light
2 to shed. Hopefully, they will be able to bring some
3 insights to the file-swapping controversy, and perhaps in
4 the process also provide some guidance to the U.S.
5 Supreme Court, which, as Commissioner Harbour mentioned,
6 will shortly be taking up this issue, as well.

7 As many of you know, this week the Court
8 granted cert in MGM studios v. Grockster, and I suspect
9 that at least a couple of our panelists will have a few
10 words to say about that.

11 So just a few words about format before I
12 begin. Each of the panelists will give a short prepared
13 statement, and then, subsequent to that, we will be
14 opening the floor to questions.

15 So let me start with our first panelist, David
16 Carson. David is the general counsel of the United
17 States Copyright Office. Prior to joining the Copyright
18 Office, he was in private practice, where he represented
19 a wide variety of copyright holders ranging from authors
20 and recording artists to computer software publishers.

21 David will describe the legal framework in
22 which P-to-P file-sharing takes place. David.

1 All right. Well, my assignment this morning is
2 in six to eight minutes to give you an overview of the
3 state of copyright law with respect to peer-to-peer file
4 transmission.

5 Those of you who know anything about it at the
6 end of this six to eight minutes will complain that it's
7 been a very superficial and selective account, and I will
8 plead guilty, but in the time frame I have, there is not
9 much one can do about that.

10 So let's get right into it. First of all,
11 let's briefly address the question of whether there is
12 copyright infringement with respect to peer-to-peer
13 services. And if you look at it in terms of individual
14 transactions taking place on peer-to-peer services, I
15 don't think there's any question but that copyright
16 infringement does take place on peer-to-peer services.
17 And that when an individual, without permission from the
18 copyright owner, causes the copyrighted work to be
19 transmitted on a peer-to-peer network, and whether as a
20 recipient or as the person who is making it available for
21 transmission, that person has infringed.

22 There have been at least two of the exclusive
23 rights of the copyright owner that have been infringed:
24 the reproduction right -- an unauthorized copy is being
25 made on the recipient's computer -- as well as the

1 distribution right, because a copy is being distributed
2 from one point to another.

3 There may also be an infringement of the public
4 performance right, depending upon the particular way in
5 which that peer-to-peer system is operating. If you're
6 hearing a performance simultaneous with the transmission,
7 then there would be an infringement of the public
8 performance right as well.

9 That's pretty much incontestable, I believe.
10 We'll see, I suppose, in the next 90 minutes.

11 The more interesting question than the one
12 that's occupying all of our minds at the moment in recent
13 events and caused us to focus on that question, is
14 whether a peer-to-peer service or a provider of
15 peer-to-peer software can be held liable for providing
16 that software, or that service, if you will. Not because
17 that service itself is infringing copyright, but because
18 it is enabling the infringement of copyright.

19 Well, copyright law has long had doctrines of
20 secondary liability, and in particular there are two
21 doctrines of secondary liability that have been called
22 into play in this context.

23 The first is that of contributory infringement.
24 To be a contributory infringer two things must be true.
25 One is that you must know that infringing activity is

1 taking place. And the second is that you must make a
2 material contribution to the infringing conduct of the
3 person who is actually doing the infringement.

4 When the 1976 Copyright Act was enacted, the
5 House of Representatives report gave an example: if you
6 rent a movie to somebody knowing that that person is
7 going to make an unauthorized public performance of the
8 movie, then you are liable as a contributory infringer.

9 The second theory is the theory of vicarious
10 liability. It is essentially similar to and based upon
11 the notion of respondeat superior. If you have someone
12 do something for you that is unlawful, then you are
13 responsible for what they have done as though you had
14 done it yourself.

15 There are two elements to that. The first is
16 that you have the right and ability to supervise or
17 control the infringing activity. And the second is that
18 you had a direct financial benefit from that activity.

19 A couple of examples that the case law makes
20 pretty clear is if you're a dance hall operator and you
21 hire a band to play, and that band plays musical
22 compositions without authorization of the copyright
23 owner, you will be liable for their infringements.

24 Another one, if you're an operator of a swap
25 meet and the people who are selling goods at your swap

1 meet are selling infringing goods, you will be held
2 liable for their acts of infringement, at least if it's
3 circumstances where you are getting a direct financial
4 benefit from their sale, and where you could have stopped
5 them.

6 So that's sort of the overview. Why do we have
7 doctrines of secondary liability? Well, a couple of
8 cases have given us some notions of why. The first is
9 one of efficiency and practicality.

10 We heard about the many lawsuits filed by the
11 recording industry, and more recently the motion picture
12 industry, against individual infringers in peer-to-peer
13 networks. And there are hundreds, maybe thousands, of
14 those suits now, but I don't think anyone pretends that
15 it's begun to stop the problem.

16 And one might imagine that no matter how many
17 of these lawsuits you file against the individual
18 infringers, most people aren't going to feel deterred,
19 because the odds are that you, the individual infringer,
20 simply are never going to be sued. It's much more
21 efficient, it's much more practical, to sue the person
22 who is enabling the infringement by all these other folks
23 who may be difficult to track down, who may be judgement-
24 proof. And if you can stop it at the source,
25 essentially, that is a much easier and more efficient way

1 to stop the problem.

2 The second is simply a notion of fairness. If
3 you are in fact engaging in an enterprise which you set
4 up so that you, yourself, aren't engaging in
5 infringement, but you are profiting from the infringement
6 of others, then fairness and equity actually suggest that
7 perhaps you ought to be held responsible for what you've
8 unleashed, essentially -- for that which you are
9 profiting from.

10 So those are theories behind these doctrines of
11 secondary liability.

12 The major case in this area, of course, and the
13 one that we're all grappling with this year, is Sony v.
14 Universal City Studios, the Betamax case, which addressed
15 the video cassette recorder 20 years ago.

16 Now, I can't begin to describe to you what the
17 Court held, because that would take more time than I
18 have. But the very, very brief and selective overview
19 is, first of all, the Betamax was a recording machine,
20 a machine that allows individuals in the privacy of their
21 homes to record over that which is being broadcast to
22 them free and over the air and make personal copies,
23 which the Court found was predominantly for purposes of
24 time-shifting. You miss the evening news because you got
25 home too late tonight, your VCR recorded it so that when

1 you got home, you could watch the evening news, and you
2 would never watch that particular thing again.

3 The Court, in fact, expressly did not say
4 whether or not making a personal archive of television
5 programs that you might want to go back to again and
6 again was fair use. What it did find was that the
7 predominant use of the Betamax was time-shifting, and
8 that that was fair use.

9 The Court found there was no liability for
10 copyright infringement on the part of the manufacturer of
11 the Betamax machine, because even though the manufacturer
12 knew that some of his consumers might infringe, that
13 wasn't sufficient.

14 And the Court imported into copyright law a
15 patent law doctrine, the stable article of commerce
16 doctrine, which says that the sale of copy equipment does
17 not constitute contributory infringement if that product
18 is widely used for legitimate, unobjectionable purposes.

19 And then in the passage that has everyone
20 wondering, all right, what do they really mean, and
21 perhaps this year they will tell us what they really
22 meant, the Court said, indeed, it may merely be capable
23 of substantial non-infringing uses.

24 The question is, thus, whether the Betamax is
25 capable of commercially significant non-infringing uses.

1 Well, let's shift to peer-to-peer services 20
2 years later. A number of questions arise. Is
3 peer-to-peer software a staple article of commerce? If
4 you're an operator of a peer-to-peer network, are you
5 liable if you don't have actual knowledge of specific
6 acts of infringement at the time those acts are taking
7 place, and at a time when you might be in a position to
8 stop them? Does a peer-to-peer service have substantial
9 non-infringing uses, and, if it does, what are the
10 consequences?

11 Well, we've got three cases from the courts of
12 appeals that have spoken on this issue. Different
13 factual contexts, but even putting aside those different
14 factual contexts, the court took very different
15 approaches in each case.

16 The Napster case was, of course, a centralized
17 peer-to-peer service. You heard about that yesterday.
18 Napster did have actual knowledge of infringing activity,
19 because it controlled the index which listed all of the
20 files that were available. And the court found that that
21 was key in terms of determining that there was liability.

22 Napster had the knowledge and its software
23 materially contributed to the infringement.

24 The court also found that Napster was
25 vicariously liable. First of all, it enjoyed a financial

1 benefit from people who used its service, and secondly,
2 it had the right and ability to supervise its users' use.
3 It could have blocked their access to the service when it
4 found out that they were engaging in infringement.

5 2003, the Seventh Circuit took a very different
6 approach in the Aimster case. In that case, the operator
7 of the system encrypted the transmission, so it couldn't
8 know what was going on. It couldn't know what particular
9 files were being exchanged. But the court found,

1 uses.

2 And my time is about up, so I'm going to skip
3 past the next slide and just mention the most recent
4 case, which is the Grockster case, where the Ninth
5 Circuit came up with a different approach.

6 Grockster, as you heard yesterday, again, is
7 decentralized. The people who sell and make the software
8 don't know specifically what files are being exchanged.
9 They don't have a centralized index.

10 The Ninth Circuit, following Sony, said that if
11 substantial non-infringing use was shown, the copyright
12 owner would have to show that the defendant had
13 reasonable knowledge of specific infringement files --
14 infringing files -- something that the plaintiffs

1 that case meant at the time you actually provided the
2 software to the user.

3 I'll just mention then, very quickly, to get to
4 the end, obviously we know the court granted cert last
5 Friday.

6 The one other issue that has arisen in the past
7 year, the Inducing Infringement of Copyrights Act
8 introduced in the Senate by Senators Frist, Daschle,
9 Hatch, and Leahy. The original text of the legislation
10 would have made one liable for copyright infringement if
11 one intentionally induced copyright infringement.

12 You see the definition in front of you from the
13 original bill -- intention, the aiding, abetting,
14 inducing, or procuring infringement, intent to be shown
15 by acts from which a reasonable person would find intent
16 to induce infringement based on all the relevant
17 information reasonably available to that person,
18 including whether the activity relied on infringement for
19 its commercial viability.

20 There was a lot of criticism of the bill as
21 introduced, particularly from folks in the technology
22 industries. The Senators who introduced it asked the
23 Register of Copyright to take a look at the situation,
24 to talk with parties and see if she could come up with
25 another approach.

1 We did come up with an approach in September,
2 which looked at it more from a business model approach,
3 suggesting that what you ought to look at is ultimately
4 how this product is used. Don't focus on the technology.
5 Don't even focus on the state of mind. Just look at what
6 the facts are, in fact, with respect to how a product or
7 service is used. And if you offer a product or service
8 that in fact is a cause of people engaging in infringing
9 public dissemination, not just personal copying in the
10 home, but actual transmission to other people, then if
11 you rely on that infringing public dissemination for your
12 commercial viability, or if you derive a predominant
13 portion of your revenues from infringing public
14 dissemination, or if you principally rely on infringing
15 public dissemination to attract individuals to your
16 product or service, then you ought to be held liable.

17 Well, a lot of folks didn't like that, either.
18 As you probably all know, after considerable discussion
19 thereafter, the clock ran out on this legislation and it
20 simply wasn't possible for all the parties who needed to
21 come to some kind of consensus to come to that consensus.

22 It's questionable whether they ever could, but
23 perhaps the grant of cert might focus people's minds on
24 whether there might be some way to agree on this before
25 the court tells everyone what the answer is going to be.

1 We'll find out.

2 (Applause.)

3 MR. DELACOURT: Well, thank you for that,
4 David. Our next panelist is Stan Besen. Stan is a Ph.D.
5 economist and a vice president with Charles River
6 Associates. He is a nationally recognized expert in the
7 economics of intellectual property rights,
8 telecommunications policy, and computer standards.

9 Stan will endeavor to supplement the legal
10 framework that David has just described by giving us some
11 background on the economic framework in which P-to-P file
12 swapping systems operate. Stan?

13 MR. BESEN: Thank you. My talk is actually
14 replete with caveats and qualifications, starting with
15 the very first slide. So this is only the simple
16 economics of P-to-P networks, and, also, only some of
17 them. But I will endeavor to make the most use as I can
18 of the next eight minutes.

19 I am an economist, so I thought I would start
20 with a theorem, which I think helps to organize people's
21 thinking about the subject.

22 Consider the following case. Suppose that
23 copies and originals are perfect substitutes for all
24 users. That is, no one would pay anymore -- in choosing
25 between them, the only thing that counts is the price.

1 And if the cost of the copy is lower than the cost of an
2 original, you copy.

3 Second, assume that the marginal cost of a
4 copying, importantly, including the cost of finding an

1 I am going to assume that the entire decline
2 was due to illegal downloading. Now, it's possible, of
3 course, some downloading -- that that's an overstatement.
4 And conceivably, in principle, could be an understatement
5 if in fact CD sales would have grown even further above
6 the 2000 level by 2003.

7 Let's just take that as a number. Assume that
8 800 million tracks are downloaded in the U.S. each week.
9 That's a number that I -- I'm really not sure where I got
10 it. I've seen bigger numbers. Numbers as big as 1.6
11 million -- billion. I have seen number -- I think Fred
12 von Lohmann on his paper had 2.5 billion.

13 Let's take 800 million. This implies that
14 there is about a .005 reduction in unit sales for every
15 downloaded track -- i.e., it takes about 200 downloaded
16 tracks to reduce CD sales by one unit.

17 Again, this is not a behavioral analysis. This
18 is just a calculation to get some idea of the
19 relationship between the amount of downloading that
20 occurs and the change in sales that's occurred. No
21 attempt to draw any sort of stronger inferences than
22 that.

23 Why hasn't the effect been larger? Well, you
24 probably all have your own list. I sort of came up with
25 a list, but feel free to think about other things that

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1 liability, and some people are not very good at copying.
2 I think of it as the phobia.

3 The one question -- I think the question that
4 you ought to think about is, how are these things likely
5 to change over time? Will the numbers that I have in the
6 previous chart change, and in what way might you expect
7 they would change?

8 You might think of two things -- and I can't go
9 through all of these in the time that's available -- but
10 think of two things that were actually described at the
11 first session yesterday. It was suggested that system
12 operators could in fact increasingly be able to detect
13 corrupted files. So to the extent that they can do that,
14 the fact that spoofing has raised the cost of copying,
15 that could in fact become less important.

16 On the other hand, we were told that cease and
17 desist orders are pretty effective in discouraging people
18 from copying. And if so, in fact, if that's really true,
19 that in fact the situation might get better for copyright
20 owners.

21 But I think we haven't yet seen the full effect
22 of the technology. There are a variety of factors that
23 affect its impact on sales by copyright owners, and
24 nobody really knows for certain how the trends in these
25 factors as they change over time are likely to affect

1 copyright owners in the future.

2 A final observation -- I think I am going to
3 finish within my time. It's the advantage of growing up
4 in New York and learning to speak really fast.

5 Even if we had good estimates of the effects of
6 downloading on unit sales, we may understate its effect
7 on copyright owners. This is separate and apart from the
8 fact that I'm sure in the next session one of the
9 questions will be whether we're actually observing the
10 endgame.

11 So it may well be that one of the reasons -- we
12 may not be able to get very good estimates of the
13 ultimate effect on unit sales using contemporary data.
14 But quite apart from that, there at least seems to be two
15 reasons why you might expect that even with good
16 estimates of the impact on unit sales, that in fact you
17 may understate the effect on copyright owners.

18 The first, of course, is that downloading may
19 affect the price of originals. And the first, if you go
20 back to the first theorem, the copyright owners
21 conceivably could just lower their price just below the
22 marginal cost of making a new copy. They could maintain
23 all their sales. They might even increase sales. Unit
24 sales might even decline, or might even increase, but the
25 price would go down.

1 So looking at unit sales alone is not
2 sufficient to determine the effect on copyright owners.

3 The second is the fact that the principal
4 effect of illegal downloading may be on legitimate
5 downloading services rather than on the sales of the
6 physical product. I suggested earlier that conceivably,
7 probably likely, many of the downloaded tracks, music
8 tracks, do not represent displaced sales of originals.
9 Sales of CDs.

10 They could, however, represent displaced sales
11 of legal downloads, iTunes and the like. If that is the
12 case, then looking at unit sales, again, will be -- will
13 give you an incomplete picture of the effect of
14 downloading on copyright owners.

15 I'm going to stop here. Thank you.

16 (Applause.)

17 MR. DELACOURT: All right. Stan, thank you for
18 those remarks.

19 Our next panelist is Mark Bohannon. Mark is
20 the general counsel and senior vice president of public
21 policy for the Software and Information Industry
22 Association.

23 Prior to joining SIIA, he was a senior official
24 at the U.S. Department of Commerce, where he served as
25 Chief Counsel for Technology, and also as counselor to

1 the Under Secretary.

2 Mark will describe some of the problems that
3 have arisen with the current legal framework for
4 addressing copyright in the P-to-P context.

5 MR. BOHANNON: And John, if it's okay, since I
6 am Power Point handicapped, I'll just speak from my seat
7 if that's okay.

8 MR. DELACOURT: That would be great.

9 MR. BOHANNON: Good. First of all, it's always
10 a pleasure to be here at the Federal Trade Commission.
11 We once again appreciate the opportunity to share our
12 views. I always enjoy being in the FTC workshops because
13 unlike so many other fora, which tend to be very rigid
14 and formal, I have found that every FTC workshop I have
15 ever participated in is never a dull moment. And I think
16 this workshop has proved itself -- though I have to say
17 that we have yet to reach the heights of the canned Spam
18 workshop, where there were virtual fisticuffs between
19 Commissioner Swindle and members of the audience, but
20 it's only 9:38, the morning is still young. So stay
21 tuned.

22 I am pleased to be here to provide the
23 perspective of the Software and Information Industry
24 Association on the issue of file dissemination and
25 peer-to-peer networks.

1 Just by way of background, and hopefully it
2 will help inform the perspective I am bringing, we are
3 the principal and largest trade association of software
4 code and content companies that produce for a variety of
5 markets ranging from business, education, consumers and
6 the Internet.

7 Our membership includes software companies,
8 eBusinesses, information service companies, as well as
9 electronic commerce companies.

10 Our membership consists of some of what I like
11 to call the largest and oldest technology enterprises in
12 the world, and some of the smallest and newer companies.
13 They are united in their need to make sure that their
14 content and software is protected from theft, and they
15 are also at the leading edge of developing new products
16 and services and business model for distribution through
17 innovative channels that reach their customers and users
18 in ways that they need.

19 We also bring to this perspective the fact that
20 we have been, and remain a pioneer in combatting theft of
21 intellectual property over the Internet. And we were
22 actually the first trade association that began focusing,
23 many years ago, on the challenge of combatting digital
24 piracy over the Internet.

25 And let me just say that since we began that

1 effort, we have seen nothing but growing challenges in
2 trying to deal with that enormous problem.

3 The focus of this panel, of course, is on file
4 dissemination via peer-to-peer networks. And like David,
5 I avoid trying to use the word file-sharing. I think
6 language is important.

7 I think sharing suggests a too benign, a too
8 passive, a too friendly approach here. I think we really
9 are talking in terms of legitimate and non-legitimate
10 activities. About means of distribution and
11 transmission. I think it's very important to keep that
12 in mind.

13 So while I may from time-to-time say file-
14 sharing, I think it's important to talk about what it is,
15 which is about how we disseminate content and software
16 across the Internet to a variety of users.

17 There are two things to keep in mind. That in
18 our industry the issue of file dissemination is neither
19 new to our industry, nor is it unique to peer-to-peer
20 networks. And for those of you who are even older than I
21 am, you will know that dissemination in our industry
22 started with FTP sites, and continued to message board
chat rooms in a variety of means.

1 no longer disseminate software through optical disks, and
2 they are entirely relying on the Internet and other kinds
3 of means.

4 So it's important to understand that file
5 dissemination is essential issue in our industry, even
6 outside the context of peer-to-peer.

7 Likewise, we see peer-to-peer networks and
8 peer-to-peer services as enabling a variety of
9 activities. Many of which we believe are legitimate.
10 And it's important that policy makers not lose sight of
11 this, and I appreciate Commissioner Harbour's comments
12 this morning in that regard.

13 We are seeing, even as we deal with the problem
14 of theft through peer-to-peer networks, that peer-to-peer
15 is becoming an increasingly accepted tool for business
16 enterprises. We are seeing in some sectors efforts like
17 financial services to use peer-to-peer in very creative
18 ways to get their job done.

19 And we are also legitimate content
20 distribution, legitimate content management occurring.
21 It's occurring in a variety of ways. I think it's

22

23
24 Association, legitimate curr-2 TDhcreative

1 consumers want.

2 Those range from everything from interactive
3 games, where there are some very good examples in the
4 press and some companies who are trying to make that
5 work. To areas such as security and anti-virus.

6 We have some member companies in the education
7 market who are actually doing some very innovative things
8 about distributing, for example, model curricula.

9 Again, all of these efforts to try to take
10 advantage of the opportunity and the mechanism and the
11 means. And having said that, what we are finding are
12 issues of scalability, security and trust, and even some
13 standardization issues, particularly for digital content,
14 that are starting to arise in terms of making that viable
15 peer-to-peer approach more viable.

16 But the issue of file dissemination through
17 peer-to-peer, I think, is something that is significant
18 and differs from both the old style of file
19 dissemination, and the broader issues of peer-to-peer.
20 And it impacts our industry I think in three very
21 specific ways.

22 First, while certainly the focus of press and
23 most attention is on file dissemination of recording and
24 audio visual. We are seeing the level of pirated
25 software in digital that occurs through peer-to-peer

1 growing tremendously.

2 In terms of the volume, we have a variety of
3 numbers, but let me just draw on a presentation yesterday
4 in the opening session by Mark Ishikawa with ATSP, who we
5 have found to be a reliable and consistent measurer of
6 what is going on here.

7 He indicated that their study showed that on
8 any given day there are three to 5 million infringements
9 that are occurring. Our working with Mark, we believe
10 that about -- while certainly most of that is recording

1 dissemination from peer-to-peer products. Which are not
2 legitimate copies, and in many cases do pose risks to
3 consumers.

4 We also are seeing an impact on our industry by
5 the fact that peer-to-peer file dissemination services
6 are closely aligned, and in many cases draw their revenue
7 from adware and other kinds of things that affect
8 consumers as they browse the Internet.

9 And those relationships do affect, in fact, our
10 industry. They put great demands on the technical
11 services of our industry, and I call to your attention I
12 think the tremendous of the Center For Democracy and
13 Technology in outlining some of those problems.

14 The third specific impact is, as David pointed
15 out, that as this environment is growing, we are, and
16 have seen, court decision that have left a very concrete
17 hole in the application of copyright law.

18 That leaves copyright holders without effective
19 legal resources to stopping infringements for
20 peer-to-peer file dissemination of pirated software and
21 content is occurring particularly in a decentralized
22 manner.

23 The result is that there are some real risks,
24 and the cost to software and digital content publishers
25 is real and we believe hampers the development of

1 legitimate business that enable distribution over
2 peer-to-peer networks.

3 The economics here -- and I think it's
4 important to keep in mind, and, Stan, I think gave a
5 useful outline. It's important to understand the
6 economics of the motion picture, recording, and software
7 are very different.

8 And let me give you one example about why this
9 is true. The average software company -- and, here, I
10 say average, because in fact we do see quite a few
11 companies that, you know, dominate the space. Involves a
12 company that has three products, one of which accounts
13 for 60 percent of their revenue.

14 The impact of a company's one major product
15 being pirated, particularly through peer-to-peer, can
16 have a tremendous impact. Not just on, as Stan said, the
17 actual price of an end product, but on the overall
18 economics.

19 Others on the panel here are going to have some
20 specific legislative proposals. Let me just I think
21 highlight -- and I'm not quite sure how much time I have
22 left. Thank you. That will give me enough time.

23 To highlight I think a couple of things that
24 the FTC can and should focus on appropriate with their
25 mission, and I think with their background. The first is

1 be willing to recognize, as we have done before, the
2 importance of the FTC's initiatives to educate consumers
3 in spyware. And we want to commend them for having
4 brought the case against Seismic Entertainment.

5 I thought they were very thoughtful in bringing
6 that case. They recognized there need to be an analysis
7 of what potential benefits of the technology there are to
8 consumers, but we think that that is an important role
9 given what is the close association between adware,
10 spyware and some of the peer-to-peer networks that is
11 occurring.

12 Secondly, we talked about the privacy issues,
13 and we think that there are -- there needs to be more
14 information gathered by the FTC in this area. I think it
15 was a useful discussion yesterday to talk about the
16 developments, but I think the FTC does have a role in
17 gathering more data about what are in fact the privacy
18 implications for peer-to-peer networks.

19 And finally, education. I know that's an easy
20 thing to say, but I think the FTC is trusted as a source
21 of information not only by state and local consumer
22 authorities about these impacts, but also by consumers.
23 And we believe that the FTC needs to be very explicit
24 about raising consumer awareness about the implications
25 of illicit dissemination. About the effects on the user

1 downloaded spyware, and that, finally, that it's not the
2 real thing that you're often getting from peer-to-peer
3 networks.

4 But we also urge that the FTC recognize that
5 this is a very dynamic technological business environment
6 in which peer-to-peer applications are emerging and
7 business models are evolving. And just as is done in
8 other areas, I think the FTC needs to make sure it is
9 aware of the pitfalls and the opportunities that are
10 present as it proceeds with any of these initiatives.

11 Thank you, again, for the time, and I
12 appreciate any questions you may have.

13 (Applause.)

14 MR. DELACOURT: Thanks, Mark. Our next
15 panelist is Andy Moss. Andy is the Director of Worldwide
16 Technical Policy at Microsoft. In that capacity, he is
17 responsible for shaping the company's strategy with
18 respect to such issues as intellectual property and
19 content protection, digital broadcasting and broad band.

20 Andy will describe an element by element
21 approach to the P-to-P file swapping issue as one
22 potential approach to possible solutions.

23 MR. MOSS: I guess I wouldn't be Microsoft if I
24 didn't do a Power Point. I don't want to disappoint.

25 Unlike most of the other panelists, I am an

1 engineer and not a lawyer or a trade association. And
2 what I would like to do is step back a little bit from
3 some of the legal discussion and provide some context
4 around the technology that is being discussed, and
5 perhaps put out some basic principles to help understand
6 how, at least we, regard some of decision making around
7 how we view the impact on consumers, the impact on the
8 market, and how we have tried to evolve some of our
9 technology.

10 You know, there is good news and bad news in
11 this. One is that, you know, the convergence that we in
12 the tech industries are talking about for 10 years or
13 more, you know, the good news is it's actually finally
14 happening.

15 You have a lot of merging of interests,
16 consumer technologies and industries. So you have the IT
17 sector merging with the CD sector. You have broadcasting
18 and cable and content communities all wrestling with how
19 to deal with the fact that dissemination of information
20 is changing.

21 The value propositions are changing from
22 economies of scale and high value focused efforts, to out
23 to the consumer and out to the edge and giving people
24 more of an opportunity to control their own destiny with
25 technologies like peer-to-peer.

1 The technology itself is actually not new.
2 While it's been popular now for the last three or four or
3 five years, the reality is that it's just a form of
4 distributive computing that's been around for 20 or 25
5 years. And there's nothing new about it.

6 What's new is the convergence that took place.
7 There was the rapid adoption of Internet. There was the
8 rapid increase in storage capacity. There is the rapid
9 increase of processing power. There is the compression
10 algorithms for video and audio that happened in a
11 relatively short period of time.

12 It all came together that allowed this thing
13 called peer-to-peer to somehow become very popular. And
14 what happened was, consumers got hold of the technology
15 that had largely been in the hands of IT departments that
16 allowed computers to talk to each other for a long period
17 of time.

18 So if you think about it, distributive
19 computing is actually used for everything from AIDS
20 research, to the search for extraterrestrial life in very
21 interesting and creative ways.

22 And so peer-to-peer is just one form of that.
23 The technology is not new, and it's also not going away.
24 And so all of the discussions that we have around future
25 policy or potential laws and changes need to be guided

1 We are all struggling with the convergence that
2 I talked about. We wrestle with it, how we deliver new
3 products. Other industries are wrestling with the human
4 nature of change. I mean everyone grapples with change.

5 What happened when the automobile was
6 introduced; what happened to the buggy manufacturers?
7 Did they become parts manufacturers to the automobile
8 companies, or did they go out of business?

9 Transformation and technological change causes
10 people to adapt. If you adapt successfully, you go on.
11 If you don't adapt successfully, you find something else
12 to do.

13 And that's really what's happening now, is you
14 have lots of people who are trying to figure out how to
15 adapt and what to do with the technology and what the
16 future holds for them. And change is going to happen.

17 And so the way that we think about how to guide
18 our actions and what we have been trying to talk to, lots
19 of communities, whether they're the consumers or the
20 media industry, or distribution outlets and content, are
21 -- there are basically four pillars. None of which is
22 more prominent than the other. They all have to be
23 addressed equally to advance the benefits that we all
24 want, and to curtail the misuses that have been taking
25 place.

1 Technology is one of those pillars. Like I
2 said, like all technology, it's just a tool. You can use
3 it for whatever purpose you want. It's a piece of
4 distributed computing. It's not just file-sharing. It
5 is a broad range of technologies that have common
6 elements that enable multiple good things to happen.

7 Lots of people use Instant Messaging. It's a
8 set of protocols that underline that that also are used
9 in common peer-to-peer systems.

10 Voiceover IP is an up-and-coming technology, or
11 set of technologies. It's not an application. It's
12 actually a set of protocols. Many of which are common to
13 building peer-to-peer applications.

14 And so we have to think about how all of these
15 things are reacting. And I'm getting the high sign, so
16 I'll speak a little faster, as well. I'm also from New
17 York.

18 The other thing that's important, is in
19 addition to the technology, we have to make the content
20 available. Today, the majority of content that's
21 available has been done for illicit purposes.

22 What we would like to see is the creators of
23 content taking more advantage of the availability of
24 making their content available in the ways that they
25 choose, as a way to offset the volume of piracy.

1 So if the volume of legitimate content grows to
2 the point where it's greater than the volume of
3 illegitimate content, then we can have a legitimate
4 conversation with consumers about alternatives.

5 Last slide. Law and enforcement certainly
6 plays a part. We're all -- any commercial, capital
7 society has to have laws that govern it, and it's not
8 just copyright law. It's all forms of law for
9 enforcement around respecting property, but also, you
10 know, all of the issues around consumer awareness and
7 consumer protection.sumer awareness andDrn4i

1 even their own intellectual property.

2 Digital photos and home videos are people's
3 personal intellectual property that they might want to
4 think about how to use. How to control the use of. They
5 may not want those photos to get into hands of strangers
6 and people they don't know.

7 Content and service providers must promote when
8 they make their contents legally and legitimately
9 available. Consumers need to understand the bargain that
10 they're undertaking. What are the rights that they are
11 acquiring. Is it free for one use, is it free forever;
12 am I buying it for \$5 for a month, for a day, for a year.

13 You know, there has to be information conveyed
14 to the consumer so that they know what they're getting,
15 when they're getting, and they understand how to use it
16 and respect it. If they don't know what the rights are,
17 they don't know how to respect it appropriately. And so
18 there is an obligation on all of us to participate in
19 making sure that education of consumers is advanced.

20 And so those are the four basic principles that

1 next panelist is Dean Garfield. Dean is the vice
2 president and director of legal affairs, worldwide anti-
3 piracy, for the Motion Picture Association of America.

4 Prior to joining the MPAA, he was vice
5 president of legal affairs at the Recording Industry
6 Association of America, where he managed a number of
7 intellectual property cases, including litigation against
8 Grockster and Kaza.

9 Dean will discuss the MPAA's position on P-to-P
10 issues, as well as the development of lawful file
11 swapping alternatives.

12 MR. GARFIELD: Thanks, Don. Good morning. Let
13 me begin by dealing with two preliminary issues. First,
14 I would like to thank the FTC for putting together this
15 great conference. I would also like to thank the FTC for
16 inviting the Motion Picture Association of America to
17 participate in this conference.

18 I promise not to call anyone a polluter, or
19 associate anyone with the devil.

20 (Laughter.)

21 MR. GARFIELD: I have heard yesterday's
22 discussion described as CNN meets Jerry Springer. For
23 those who are hold overs from yesterday who are offended
24 by what they claim to be loose use of language, please
25 get in line at the mike now, because I intend to use all

1 of the key terms. Thievery, pirates, and even Microsoft.

2 I plan to quickly cover three issues; where we
3 are, where I see us going, and how we get there. My
4 friend Stan Besen started with a theorem, since he's an
5 economist. I am now part of the movie industry, so I'll
6 start by asking you to use your imagination.

7 Imagine, if you will, a world in which an
8 innovative and potentially transformative technology is
9 introduced into society. Society is immediately improved
10 in small, but noticeable ways.

11 A group of business people choose to take that
12 technology and monetize it. Those same business people
13 hail innovation and technology, but oppose technology and
14 innovation that would cure the ills occurring on their
15 system and services.

16 Those businesses seek praise for their
17 willingness to filter pornography, and employ
18 sophisticated systems to filter viruses. But claim that
19 filtering copyrighted content is just not technically
20 feasible.

21 Those businesses send their users terabytes of
22 data on a daily basis, but claim that it's impossible to
23 communicate with their users about copyright
24 infringement.

25 Those businesses integrate within their

1 networks and systems. Software that monitors detailed
2 information on their users. But claim that it's
3 impossible to tell what their users are doing as it
4 relates to copyright theft.

5 Those businesses regularly update their
6 software. Sometimes multiple times in a month, but claim
7 that their software is not malleable, and to suggest any
8 change to deal with copyright infringement is down right
9 offensive.

10 Where is this brave new world; is it some
11 Orwellian world where right is wrong, up is down, night
12 is day? It is not. It is the world of P-to-P today. It
13 is a world where transformative technology has been
14 high-jacked, not by innovators, but by business people
15 who are motivated by profit and are so blinded by the
16 chase for money that they fail to see the irony, the
17 illogic, and incongruity of claiming to be technologists,
18 while asserting that their hands are tied by
19 technological limitations.

20 It is a world where innovation is being
21 retarded by those who leech on those who choose to
22 create. Technology is simply the platform for their
23 business gains. Their business is different and distinct
24 from technology, the technology itself.

25 P-to-P is, P-to-P is, it has been, and will be.

1 It is not new, but it certainly is innovative. The sale
2 of IBM's PC business is significant in many respects. In
3 my view, it reflects a move from individualized
4 collection of data, to network storage where the concept
5 of the same client will become real, and where
6 distributive computing and transferring data across vast
7 networks using peer-to-peer and the concept of
8 distributive computing will soon be real.

9 To be clear, the Motion Picture Association
10 fully supports this innovation. Our industry -- for our
11 industry, where large files rule, distributing computing
12 will open up new distribution platforms. In fact, the
13 motion picture studios are already working with
14 distributed computing concepts.

15 IFilm, which distributes movie trailers and
16 short films, has been licensed by all of the motion
17 picture studios, and it is built on a distributed
18 computing platform from the company RedSlous.

19 Additionally, the motion picture companies are
20 digitally distributing films through IBeam, CFlicks,
21 MovieLink, and others. In short, we are working to usher
22 in a brave new world.

23 The second issue that I would like to address
24 is the world of tomorrow, which I think is rapidly
25 approaching, where content is ubiquitously available, but

1 respect innovation. It's important to remember that
2 technological innovation is just one aspect of
3 innovation.

4 Working to develop creative works, whether it's
5 music, film, or software is also an important aspect of
6 innovation. And that aspect of innovation should not be
7 lost in the balance.

8 Finally, supporting legal rules that give more
9 than merely symbolic protection to copyright, but also
10 protecting innovation in unrelated areas of commerce is
11 the balance that needs to be struck. And in my view the
12 Supreme Court will do that.

13 In closing, I would like to simply quote
14 Senator Gordon Smith from yesterday. If P-to-P file-
15 trading companies can filter pornography, they can, and
16 should, filter copyrighted works. Thank you.

17 (Applause.)

18 MR. DELACOURT: Thank you, Dean. Our next
19 panelist is Bennett Lincoff. Bennett is an attorney,
20 consultant, and writer living in New York. He previously
21 served as the director of legal affairs for New Media at
22 the American Society of Composers, Authors and
23 Publishers.

24 Bennett will discuss the possibility of
25 addressing P-to-P file swapping through targeted reforms

1 to copyright law.

2 MR. LINCOFF: Thank you, John. I would like
3 to also thank the Commission and Commissioner Harbour, in
4 particular, for organizing this workshop and allowing me
5 to participate.

6 The Internet is fundamentally incompatible with
7 the sales based revenue model for works of popular
8 culture, especially music.

1 measures, pursued legislation to limit the business
2 opportunities of technology firms, consumer electronics
3 makers, and web casters; and sued consumers, seeking
4 ruinous damages for conduct occurring in the privacy of
5 people's homes.

6 Despite these efforts, the unauthorized
7 downloading of recorded music continues unabated, and
8 P-to-P networks proliferate.

9 The industry is now supporting services that
10 provide partial restricted DRM encumbered P-to-P. But
11 any licensing scheme that falls short of allowing full,
12 unfettered DRM free file-sharing, leaves the sales based
13 revenue model vulnerable to widespread infringement by
14 consumers who refuse to comply.

15 And even if the industry were to license the
16 full range of P-to-P capabilities that consumers demand,
17 so long as its fortunes are tied to the sales based
18 revenue model, it will have to continue its aggressive
19 infringement litigation campaign, and its interference in
20 the free markets for technology, consumer electronics,
21 and digital audio services.

22 In the meantime, the industry's effort to
23 salvage its legacy, the business model, has had
24 collateral consequences. It has slowed the deployment of
25 high speed broad band connections for the consumer

1 market. Blocked consumer electronics makers from
2 offering new devices with next generation capabilities.
3 Limited the growth of web casting and other digital audio
4 services. Chilled free speech, and interfered with
5 academic freedom on college campuses. Caused distortions
6 in music licensing marketplace. Exposed consumers to
7 liability for enjoying music when, where and how they
8 want. And by ignoring consumer demand and refusing to
9 sanction lawful access to full, unfettered DRM free file-
10 sharing, the industry has relegated consumers to black
11 market services where adware, spyware, pornography and
12 privacy violations abound.

13 And for it all, there have been fewer licensed
14 transmissions of fewer works and fewer royalties than
15 otherwise may have been earned.

16 I believe that public policy should strongly
17 support the opportunity of music industry rights holders
18 to earn ample rewards from their contributions to culture
19 and commerce.

20 By the same token, however, the industry has no
21 right to demand that public policy support its desire to
22 do business in a particular way.

23 An alternative to the sales based revenue model
24 is needed, and I suggest this. Congress should aggregate
25 the separate rights of song writers, music publishers,

1 recording artists and record labels in their respective
2 works and create a single, unified digital transmission
3 right.

4 This new right would replace the reproduction,
5 distribution and public performance rights for purposes
6 of digital transmissions. The right would extend to all
7 acts that may be implicated in the digital transmission
8 of music to end users, including, with respect to P-to-P,
9 downloading works from the networks, as well as offering
10 them others.

11 The right should be enforceable against all
12 those involved in the digital transmission of music,
13 including service providers who offer streaming, those
14 who offer downloads, P-to-P network operators, and all
15 P-to-P participants.

16 Under the right, all that would need to be
17 known was whether or not a work had been transmitted.
18 Thus, it would no longer matter whether end users only
19 listened to transmissions, or also downloaded them. How
20 many copies, if any, were made in the course of the
21 transmission. Whether transmitted copies were stored on
22 a temporary or on a permanent basis. Or whether works
23 are used on one audio playback device, or another.

24 Moreover, the new right would not depend on
25 access restrictions and anti-copying measures for its

1 success. Nor would it require continued suppression of
2 the free markets for digital audio services, technology
3 products and consumer electronics.

4 Rather than limiting access to music, rights
5 holders would have the incentive to encourage the widest
6 uses possible. This would free the industry from pursuit
7 of unhackable technology, allowing it to focus instead on
8 development of monitoring techniques to support royalty
9 distribution.

10 And with respect to royalties, they should be
11 paid on a census of all licensed transmissions, which of
12 course a digital network would allow. Only through a
13 census can it be assured that royalties go only to those
14 rights holders whose works are actually transmitted, and
15 that all rights holders, large and small, receive that
16 share of royalty that is precisely proportionate to the
17 license fees paid for transmissions of their works.

18 The digital transmission right would be bullet
19 proof against copyright infringement. Unlike the
20 reproduction and distribution rights as underlie the
21 sales based revenue model, but like the public
22 performance right, the digital transmission right cannot
23 be subverted by one, or even several unlicensed services,
24 networks, or end users.

25 Whether or not particular transmissions are

1 only comply with music use reporting requirements, and
2 pay the license fees in a timely manner.

3 And while the statutory license is warranted, a
4 parallel free market could also operate with rights
5 holders and anyone needing a license could enter into
6 voluntary non-exclusive agreements on whatever terms they
7 find agreeable.

8 A statutory license would enable transmissions
9 to be made available from the largest number and widest
10 possible array of competitive licensed services,
11 including through P-to-P, anytime, anywhere, to anyone
12 with Internet access.

13 Obviously a fully free market is to be
14 preferred, but statutory licensing or its equivalent is
15 already standard practice in the music business. Indeed,
16 the record business itself is built on the backs of song
17 writers and music publishers through the compulsory
18 mechanical license.

19 Given the experience to date, experimentation
20 with a free market for the digital transmission right
21 would likely result in continued market failure.

22 Finally, if one looks beyond the interest of
23 the music industry alone, and considers also those of
24 technology firms, consumer electronics makers, audio
25 service providers and consumers, it is clear that a

1 digital transmission right subject to a statutory license
2 would enhance the free market overall.

3 Change is needed. Congress should induce it.
4 Thank you.

5 (Applause.)

6 MR. DELACOURT: Thanks for those remarks,
7 Bennett. Our next presenter is Fred von Lohmann. Fred
8 is senior staff attorney for Fair Use and Intellectual
9 Property with the Electronic Frontier Foundation.

10 In that capacity, he has represented numerous
11 software developers and users against major movie
12 studios, record labels, and television networks,
13 including most recently representing streamcast networks
14 in the MGM v. Grockster case.

15 Fred will discuss the seemingly conflicting
16 accounts of the impact of P-to-P file swapping on content
17 providers, and he will also discuss strategies for
18 addressing file swapping through existing law.

19 MR. LOHMANN: I am a bit tempted to simply say
20 what Bennett said.

21 (Laughter.)

22 MR. LOHMANN: But you know, perhaps I'll go
23 ahead and present what I was going to say anyway.

24 I wanted to say a few words about whether or
25 not in fact the sky is falling, as perhaps many copyright

1 industries would have you believe.

2 And perhaps the more important question of
3 whether or not the propping up of the sky, should it in
4 fact start falling, is something that ought to be done by
5 more laws, more government intervention and more
6 regulation. Or whether, instead, perhaps there are more
7 market based solutions.

8 So I think it's good to begin this discussion
9 with a brief lesson from history. I think history has
10 quite a bit to tell us about this.

11 And when major copyright industries say that
12 new technologies to cause their skies to fall, the place
13 I always begin is with Jack Valenti's famous quote in
14 response to the VCR, that I say to you that the VCR is to
15 the American film producer and the American public as the
16 Boston Strangler is to the woman home alone.

17 A statement that Mr. Valenti, head of the MPAA
18 at that time, made to Congress in 1982.

19 Of course, as those who pay attention to media
20 markets, well, no, the VCR turned out to usher in the
21 single largest new revenue stream the motion picture
22 industry had ever known.

23 So in fact, history is replete with examples
24 that echo this lesson. The player piano, broadcast
25 radio, color television, cable television, the VCR, the

1 copyright were in the long run made better off by the
2 technologies.

3 Of course, history continues to teach us the
4 same lesson even today. New digital technologies have
5 been met with exactly the same hostility by incumbent
6 copyright industries.

7 The MP3 player, the first commercially
8 available portable MP3 player, was greeted with
9 litigation by the recording industry.

10 Peer-to-peer file-sharing applications have
11 also been attacked, as everyone well knows. The personal
12 video recorders, perhaps epitomized by TVO, have also
13 found themselves subject to litigation.

14 Replay TV, one of the leading companies, was
15 forced into bankruptcy by litigation from the motion
16 picture studios and other entertainment industries.

17 And most recently, just last week, an
18 innovative company called Kaleidescape, that had the
19 nerve to try to provide the consumer the same kind of
20 juke box feature that Apple, with their iTunes had
21 provided for music, this company intends to provide that
22 for DVDs, allowing you to put all of the DVDs that you
23 own onto hard drives that will allow you to do
24 interesting things, to watch it all over your house, to
25 access it without having to shuffle optical disks about;

1 they were just sued by the DVD CCA on the theory that no
2 one should ever be entitled to copy a DVD for any reason,
3 without permission of course.

4 So in looking at whether the sky is falling,
5 let's move from history to what we know today. I will
6 begin by saying that there is no clear complete picture
7 at this point. The data is yet very new, but the data
8 that we have suggests at least some trends.

9 So let me start, as this is all information
10 that you have already seen yesterday. Main stream
11 peer-to-peer is now five years old. Napster having sort
12 of launched that revolution. There are at least 20
13 million users of peer-to-peer file-sharing applications
14 today. Probably quite a bit more, 20 million is the
15 lowest I have seen. The other numbers range as high as
16 60 million, a number that exceeds the number of Americans
17 that voted for President Bush just last month.

18 There are more than 2 billion downloads every
19 month. On that number, I guess I agree with the earlier
20 800 million a week, for roughly the same range. That, of
21 course, dwarfs the so-called authorized music service
22 downloads that we have seen thus far.

23 And yet despite the proliferation and continued
24 success of peer-to-peer file-sharing networks and the
25 obvious consumer demand for them, you see that this year,

1 CD sales are in fact up.

2 The first three quarters of this year, Sony
3 music declared to European anti-trust regulators last
4 year in trying to clear their merger with BMG, that they
5 were profitable this year.

6 BMG, in fact, declared in that same proceeding
7 that they had their most profitable quarters in corporate
8 history in the end of 2003 and beginning of 2004.

9 Investment analysts looking at these trends
10 have said, in fact, the music industry is more healthy
11 today, at least in part because they have finally done
12 the kind of belt tightening and downsizing that has been
13 long over due for their industry.

14 The economists, just a few weeks ago, published
15 a story in which the following quote appeared. According
16 to an internal study done by one of the majors, referring
17 to the major record labels, between 2/3 and 3/4 of the
18 reports of the drop in sales in America had nothing to do
19 with Internet piracy. This, again, a study commissioned
20 by the major label itself.

21 So what is going on? Well, I think the music
22 industry is facing a lot of pressures from a lot of
23 quarter. So you have today obviously there was a
24 recession, an economic down turn.

25 The music industry is quick to point out that

1 in prior down turns, they did not suffer. And so this
2 somehow must indicate that they are recession proof
3 business.

4 Of course, if you look historically, at the
5 times when there were recessions in the past, the music
6 industry was fortunate to have had a new format on path
7 that got consumers to buy all of the same music one more
8 time. Whether it be the audio cassettes, or the CD.

9 Unfortunately for them, perhaps a sign of their
10 flagging innovation skills, they don't have that benefit
11 this time. And so that perhaps they are not entirely
12 recession proof. Something that has very little to do
13 with peer-to-peer file-sharing.

14 The Internet, DVDs, and video games are
15 competing for consumer time and money. The Wal-
16 Martification, as I put it, of music retailing is a big
17 problem. They are finding themselves with fewer retail
18 options and more price pressure. Radio consolidation is
19 exacerbating that trend. At the same time, the music
20 industry is reducing the number of new releases they put
21 out every year by as much as 20 percent, and, in fact,
22 during the early part of the peer-to-peer revolution, the
23 music industry responded by raising CD prices. A 10
24 percent increase between '99 and 2003. Perhaps exactly
25 the wrong response.

1

Now, other interesting facts. In Canada, as

1 So I just want to very quickly sum up here,
2 well, what should the FTC be looking at. Well, I don't
3 think the answer is more laws, more lawyers, more
4 lawsuits. This is not a more law problem. Instead, we
5 have a situation where the copyright industries have to
6 adapt, come up with new business models. Early
7 indications are that they are, and they may well be
8 succeeding.

9 You have new authorized music service offerings
10 that are beginning to offer consumers at least a mild
11 facsimile of what they have been demanding for years. I
12 am hoping that maybe additional development there will be
13 helpful.

14 But if that doesn't work, I actually would like
15 to end where Mr. Lincoff ended, by saying what we should
16 be looking for is perhaps some collective licensing
17 solutions. I am in some ways more optimistic than he is.
18 I don't think copyright law needs to be changed. I think
19 the laws will accommodate the creation of new collecting
20 societies that can offer the kind of blanket licenses
21 that Mr. Lincoff mentioned without the need for any
22 copyright law reform.

23 And if the FTC would like to do something
24 productive, I think it should look into what barriers may
25 exist in the current music industry marketplace that are

1 interfering with the creation of those collecting society
2 approaches. Approaches that most industry insiders and
3 economists agree would probably be more efficient, better
4 for innovation, and, in the end, actually generate higher
5 revenues for the very industries that are today most
6 concerned about peer-to-peer file-sharing. Thank you.

7 (Applause.)

8 MR. DELACOURT: Okay. Thanks for those
9 remarks, Fred. Our last panelist will be Peter Menell.
10 Peter is a professor of law at the University of
11 California/Berkeley School of Law, and executive director
12 of the Berkeley Center for Law and Technology.

13 He has written extensively in the area of
14 intellectual property law, with particular focus on legal
15 protections for computer software.

16 So Peter is going to give us -- take a more
17 global approach, and help us make sense of what we have
18 heard so far this morning by describing a framework for
19 understanding and analyzing the various policy proposals
20 that have been set forth so far.

21 MR. MENELL: Good morning, everyone. It's a
22 real honor to be part of this distinguished panel, and I
23 can see -- well, I guess there is some static on the
24 panel that I was picking up.

25 (Laughter.)

1 MR. MENELL: Well, my presentation today tries
2 to provide a framework for moving from rhetoric and
3 advocacy towards at least a somewhat neutral -- I realize
4 neutral is a hard word to use in Washington. But my goal
5 is to really try to provide a systematic framework so
6 that we can compare and contrast different approaches.

7 I do think that we are at a critical stage in
8 the evolution of two of the most important industries in
9 our history. It's really a historic period when you
10 think about the history of copyright law.

11 Copyright law has always been implicitly about
12 platforms, technology platforms. Copyright didn't exist
13 until there was technology for distributing works of
14 authorship. And we are now at, I think, probably the
15 most important transition in the history of this law.

16 So let me try to put this into the broader
17 historical perspective, and I'll go back to 1440, which
18 is roughly the time that the Gutenberg printing press
19 came about. And I think that there is a very important -
20 - and I think along the lines that Fred suggested,
21 symbiotic relationship that has existed between the
22 contents and technology sectors.

23 I realize that there has been tension, but by
24 and large things have worked out in a way that has been
25 generally productive for both sets of industries.

1 Notwithstanding the loss of some jobs in particular
2 sectors. Player piano performers lost business when the
3 talkies came about.

4 And you can find examples like that, but by and
5 large it's a very strong systematic I think symbiotic
6 relationship.

7 Why? Well, almost all of the technologies over
8 this period discouraged unauthorized distribution. One
9 of the greatest forms of encryption ever invented was
10 called vinyl. Vinyl did not allow for others to make low
11 cost, high quality copies of works of authorship.

12 The film industry had a great form of
13 encryption. They didn't release their products to the
14 market. They rented them to theaters for distribution.
15 It was a very good market. It was a secure market.

16 Those entities in our society that distributed
17 works of authorship were highly regulated. Regulated by
18 the FCC. And so anyone who was distributing works
19 without permission on an FCC regulated outlet, was easily
20 detected and easily brought to justice.

21 And so I think one can sum up this very long
22 period of history with the conclusion that unauthorized
23 distribution could be detected at reasonable cost, and it
24 produced a win-win situation as new formats developed.

25 Okay. Let's look at the last decade or so.

1 The digital revolution. I realize the digital revolution
2 goes back to the 1940s, but for our purposes it really is
3 the world wide web. The ability to distribute works
4 across this vast Internet.

5 And so how has that changed these assumptions
6 on which the relationship between content and
7 technologies companies has formed? Well, technology no
8 longer discourages unauthorized distribution.

9 Once the cat got out of the bag. Once the
10 recording industry distributed their content in
11 unencrypted format, basically once the computers became
12 available for copying, the content was copyable and
13 distributable at low cost.

14 And we no longer have control over the
15 distribution outlets. We're no longer talking about FCC
16 regulated entities, we're talking about ISPs and wireless
17 on the world wide web.

18 And so we can no longer, and I think it's one
19 of the clear facts to come out of the last day and a
20 half, that we no longer can prevent unauthorized
21 distribution at reasonable cost. It is a costly
22 enterprise, and we're seeing a lot of resources brought.
23 And that has created an increasingly conflictual
24 relationship.

25 So let me just be a little more specific,

1 because it didn't happen all at once, and as Fred has
2 suggested, alarm bells have gone off periodically.

3 But I do think that there is something to be
4 said about the Peter and the Wolf allegory here. I think
5 -- and I am Peter, so --

6 (Laughter.)

7 MR. MENELL: -- it was brought to my mind early
8 in life. I think Peter eventually gets eaten.

9 (Laughter.)

10 MR. MENELL: So you know, but I realized that
11 you lose credibility if you keep setting off alarm bells.
12 I don't like the Jack Valenti quote because I think it
13 was wrong at the time, and it's clearly wrong
14 historically. But we can look, I think, at technology
15 and see some patterns.

16 So let's look at what I will call the three
17 versions of the Internet, at least for our purposes.

18 So there was the client server model, where
19 basically ISPs were the way by which everyone gained
20 access to this great resource.

21 And in this world, users clients could post
22 works onto web sites. So they would move music files or
23 other files, and the copyright industry said, as Fred has
24 reminded us. You know, this is going to destroy our
25 industry. We cannot survive where people can post files

1 very different views of the role of government.

2 And we are in Washington, and that's what this
3 is about. I would say that the copyright industries and
4 the technology industries have co-existed for most of the
5 last century on a platform which can be called private
6 enforcement, or perhaps more appropriately, anarchy.
7 Now, anarchy didn't unfold because private enforcement
8 tended to work. And as we saw, it was very difficult to
9 engage in unauthorized distribution.

10 One of the choices that is before Congress is
11 whether we should ramp up a regulatory role to view this
12 problem as one to which government, public enforcement,
13 different forms of regulation should apply.

14 And then a third approach, which was talked
15 about by Bennett and Fred, is let's just have the
16 government set the prices. And perhaps the market can
17 play some role in that.

18 But let's just be clear about what we're
19 talking about between these three models. In the
20 regulated market model, we're talking about the notion
21 that content industries will invest on the basis of what
22 they think the willingness to pay consumers will be.
23 That's a traditional structure on which most of our
24 economy is built.

25 In the anarchy model, we're talking about

1 content industries investing based on their ability to
2 constrain access to their work. Where they have to
3 compete with some dark net.

4 And the dark net will always be there, but it's
5 a question of how many people are going to the dark net
6 to get their works.

7 And then the third model is content investment
8 is a function of how much the government is willing to
9 regulate.

10 So let me try to provide a matrix for thinking

1 software. And these are very expensive products to
2 develop. The Lord of the Rings trilogy is not something
3 that my kids would want to see discouraged. And so we
4 have to think seriously about very substantial up front
5 costs in these industries.

6 Okay. We also care about competition. We want
7 competition among content developers. I would like to
8 see the price of music go down, but I would like to see
9 it go down because there is lots of entry. There are
10 lots of indies that want to come in and provide music
11 cheaper.

12 I also care about competition in innovation for
13 systems for delivering content. The IPOD was a great
14 innovation in my household because I didn't let my kids
15 do what their friends do.

16 But because of the IPOD, they're now cool. But
17 there was that three-month period where I was not cool.

18 (Laughter.)

19 MR. MENELL: Then I think we have to look --
20 and I think Fred has been very articulate in a lot of
forums about this, about external effahht W do.1213and I tthis, aahh

1 content industries. The chilling effects on all sorts of
2 consumer products.

3 And then there are the sort of generalized
4 implementation costs that we deal with in any government
5 policy making exercise. Some models of government will
6 bring a lot of lobbyists to Washington. Many of them are
7 here today.

8 I consider this, as an economist, not
9 necessarily a good thing. We won't take a vote on it.

10 Another big cost of this system is private
11 enforcement. It's not a good thing for the record
12 industry and the film industry have to go to court.
13 Those are dead weight losses. They're going to have them
14 in certain policy approaches.

15 And then, last, and I think in some ways the
16 most important issue, is the dynamic qualities of the
17 regime you pick. Whatever system you pick needs to last
18 a long time. We don't want to be back here every five
19 years.

20 So here are the three models. Now, I don't
21 think anyone is going to throw tomatoes yet, because, you
22 know, this is pretty neutral.

23 One of the things that I'll take away from this
24 panel is that no one agrees as to one sort of fix to all
25 of this that will satisfy all of the concerns that I have

1 listed. And if we try to just sort of quickly map it
2 out, and I realize I threw this together late and I don't
3 want to spend a lot of time discussing it, I just want to
4 show that no regime is perfect.

5 So I think the anarchy regime works great if
6 you're trying to promote Internet functionality. But
7 it's not going to be so good in terms of minimizing
8 enforcement costs, and it's not going to be too good on
9 creative expression, at least in some of the industries
10 where there is high up front costs.

11 If you go to the regulated market, it probably
12 would help Dean -- and I thought I saw -- there he is.
13 You know, they would probably like the idea of some
14 regulated market, a little more control. But let's face
15 it, that is going to constrain some of our New Yorkers
16 for fair use, and they're not going to like that.

17 And if we go to compulsory licenses, it's
18 probably going to provide some money in the pockets of
19 artists. It's going to substantially reduce enforcement
20 costs, but it is going to have effects on innovation and
21 new products, because no one is going to be able to make
22 profits in some of these markets.

23 So rather than focus on the details, what I
24 just want to conclude with is there is a heterogeneity of
25 taste, and technological possibilities that at least in

1 one sense favors using markets. Markets are good when
2 things are diverse and complicated.

3 The enforcement issues though would seem to
4 favor some kind of compulsory scheme, because we just cut
5 that off at the pass. But that's going to impede
6 innovation.

7 And if we care mostly about the Internet, we're
8 going to want some kind of non-regulatory approach, but
9 that's going to lead industry to try to lock up their
10 products as much as possible.

11 I do want to say as we turn in the next panel
12 to looking at studies, that there are some dogs that
13 aren't going to bark here that are very important.

14 And what I will say is that the roll-out of
content is no3.3063ooN7-3'7 thrtent is no3.3063ortant

1 So you know, I do think you do have to be
2 careful about how these studies are put together.

3 Now, perhaps Don Henley didn't want to talk to
4 these people, but he's still important and his coalition
5 is one that should be heard from.

6 As I said, I think the dynamic attributes are
7 going to be very important. Right now we are forming the
8 expectations for the next generation of consumers. And I
9 can tell you from looking at my kids and their cohorts,
10 we're not doing a very good job of training them to be
11 good consumers. And that is something that is going to
12 be very important because it's hard to untrain some of
13 those values.

14 And the last thing I'll say, which is pretty
15 self-evident, is that we're not going to get perfection.
16 We're never going to get consensus in this room about
17 what to do, and so we have to look at what the economists
18 would call second best. Thank you.

19 (Applause.)

20 MR. DELACOURT: All right. Well, thank you
21 very much to all of our presenters. And I see that we
22 already have a number of folks lining up at the
23 microphone. So now I would like to take the opportunity
24 to offer these folks a chance to ask questions.

25 I would ask that each of them try to keep your

1 questions brief. I ask the panelists as well to try and
2 keep responses brief given that we only have about 15, 20
3 minutes here.

4 A PARTICIPANT: Mr. Garfield, your statement
5 was extremely eloquent, although parts of it were highly
6 inaccurate. Having said that, I want to focus in on
7 filtering.

8 MR. GARFIELD: Don't let the facts get in the
9 way of rhetoric.

10 A PARTICIPANT: We understand the facts
11 differently, but let me ask about filtering. We're now
12 hearing from the entertainment industry in general this
13 simplistic moniker, well, if you can filter this or that,
14 then certainly it's simple to filter out copyrighted
15 works.

16 But in fact, the legal policy and technical
17 issues raised by filtering out the vast world wide body
18 of copyrighted work really deserve a whole day of
19 hearings or workshop on their own. Also, the industry's
20 demand for filtering is very selective. For example, the
21 record industry, I'm mystified, they never call their
22 friends in Silicon Valley, like Carley Ferarina or Steve
23 Johnson and say, Carley, you know that software you
24 bundle on every computer, that software that burns an
25 unlimited number of our full audio copies and copyrighted

1 works and surely is displacing sales of software that
2 creates the MP3 files, which are the basis of our piracy
3 problem.

4 That software which knows it's facilitating
5 infringement because it immediately goes after the
6 compact disk data base, and knows these are our copyright
7 works. Could you make the trivial, trivial change to
8 block or at least limit that infringement. That
9 filtering demand is never made.

10 But here's my question, and it's the same
11 question I asked --

12 MR. GARFIELD: Knew there was one in there
13 somewhere.

14 A PARTICIPANT: There is a point. That your
15 industry is pleased to sue small start-up companies, but
16 doesn't want to take on big players.

17 My question is, and I asked this of the RIAA
18 yesterday, and I hope to get a more satisfying answer.
19 Any effective filtering system I know for copyrighted
20 works is imperfect and requires centralization because of
21 the vast data base and the identifying technologies that
22 must be employed. They can't be bundled with a small
23 distributed software application. This creates knowledge
24 and control, knowledge and control is what brought down
25 Napster I, and Aimster.

1 Is the MPAA -- would the MPAA support the
2 concept -- but would they support the concept that
3 peer-to-peer software distributors who implement
4 imperfect centralized filtering, and that's -- basically
5 if the law required this would ban decentralized P-to-P,
6 get a legal safe harbor because it's going to create
7 knowledge and control, and because it's not going to be a
8 hundred percent effective?

9 Otherwise, you're asking people to implement a
10 step which is going to put them out of business because
11 they're going to be back in prohibited territory based on
12 U.S. case law?

13 MR. GARFIELD: I think it's a fair question. I
14 disagree with the underlying assumption, though. I don't
15 think that filtering requires centralization. And so I
16 don't think it's necessary.

17 But my view is that --

18 A PARTICIPANT: Can you cite an effective
19 filtering out for copyrighted works process which doesn't
20 require a central server? I don't know of one. I'd be
21 glad to hear of one.

22 MR. GARFIELD: Well, the problem is that most
23 of the P-to-P services that are out there are filtering
24 for other purposes using the same methodologies that
25 would require -- that would apply to filter copyrighted

1 content. But in fact you're not filtering copyrighted
2 content.

3 For example, Kaza has built into it the
4 BullGuard virus filtering, which uses the same hash
5 algorithm that would be required for filtering
6 copyrighted content. It's just not being implemented.

7 MR. DELACOURT: Okay. Does anybody else on the
8 panel have a quick comment on this? Otherwise --

9 MR. LOHMANN: Yes.

10 MR. DELACOURT: Fred, go ahead.

11 MR. LOHMANN: No, I just want to -- I think
12 this entire debate about filtering is an enormous red
13 herring in this debate. I mean, this is a debate
14 between, quite frankly, the current MPAA and RIAA
15 companies and Charmin and other P-to-P companies that
16 really, in my view, are not really the issue anymore.

17 Right? P-to-P companies is, you know, to some
18 extent -- you know, it's an interesting point for debate,
19 but today the leading peer-to-peer application, one of
20 the leading applications, BitTorrent, there is no
21 company. It was designed by one person as a hobbyist, an
22 open source piece of software. He has no company. He
23 doesn't develop any revenues from it. Anyone can improve
24 it.

25 In fact, just yesterday, Professor Edward

1 Felton at Princeton's computer science department put out
2 as a demonstration that you could write a peer-to-peer
3 file-sharing application in 15 lines of code.

4 And within 24 hours, someone had responded by
5 improving it such that he wrote the same application in
6 nine lines of code. All right?

7 This debate about filtering only works in a
8 world where you have centralized intermediary parties who
9 you can enforce against. It is, as Peter mentioned, in a
10 peer-to-peer world, there will no longer be a few
11 companies that you can enforce against.

12 There will be everyone who knows how to program
13 a computer will be able to introduce an application which
14 will not include filtering if consumers don't want it to
15 include filtering.

16 MR. DELACOURT: Okay.

17 MR. LOHMANN: So that's a problem.

18 MR. DELACOURT: We'll get one more. I know
19 there's more that you can say on this.

20 MR. GARFIELD: It's on the point. It's on the
21 point of BitTorrent. I mean --

22 MR. DELACOURT: Okay.

23 MR. GARFIELD: The point is that it's not the
24 technology. I think the example that Fred gave gives the
25 answer. There are a number of BitTorrent services that

1 in fact filter out copyrighted content.

2 There are services that are dedicated to
3 political speech. It's very easy to do if you have the
4 will to do it.

5 MR. DELACOURT: Okay.

6 MR. GARFIELD: It just so happens that most of
7 these companies make their money through the lure of
8 copyrighted content and refuse to do so.

9 MR. MENELL: Okay.

10 MR. GARFIELD: It's that simple.

11 MR. DELACOURT: We'll move on to the next
12 questioner, and if you please could identify yourself
13 before asking your question.

14 MR. FISK: My name is Adam Fisk. I used to
15 work at Limewire for many years, and my question is also
16 for you, Dean.

17 MR. GARFIELD: Surprise, surprise.

18 MR. FISK: Yes. Yes, I basically just take
19 issue with the idea that P-to-P companies are all
20 business and no technology. Or that they are businessmen
21 and not technologists. And I come from a world where you
22 have thousands of open source programmers all over the
23 planet devoting their -- devoting 40 hours a week, in
24 some cases, to this technology.

25 And many of these people I know personally, and

1 beyond that, you have people like Rom Cohen, who
2 distribute BitTorrent, that constitutes 35 percent of all
3 Internet traffic, and he goes about it on his free time.
4 He -- that's a donated project.

5 So I think that's just a misconception.

6 MR. GARFIELD: I agree with you.

7 MR. FISK: You know --

8 MR. GARFIELD: Let's start with where we agree.
9 I agree with you.

10 MR. FISK: Okay. And I guess another sort of a
11 part of that community is the research worlds, where you
12 have top institutions, like the Stanford Data Bases
13 group, MIT, Harvard, Carnegie Mellon, all these computer
14 science departments are investing tremendous resources
15 into distributed search algorithms, distributed
16 downloading algorithms that are incorporated by the
17 P-to-P companies, and where the P-to-P companies are the
18 primary advancers of that technology.

19 So I think it's just wrong to paint the world
20 in that light.

21 And I guess my question to you would be even
22 people like Andrew's colleagues at Microsoft research are
23 investing a great deal of energy into that area, into
24 those kinds of algorithms, and, again, those algorithms
25 are getting incorporated from Microsoft into P-to-P

1 technology and P-to-P companies.

2 So my question to you would be what do you say
3 to Andrew's colleagues at Microsoft about their work?
4 Are they wasting their time, are they --

5 MR. GARFIELD: No, absolutely not. I mean, I
6 think I started by saying imagine -- my little thing
7 about imagine, if you will.

8 I think the one thing to be clear about is that
9 P-to-P and distributed computing generally holds powerful
10 potential for all of us. Particularly for our industry,
11 where you're distributing large files on a large scale.
12 It makes a lot of sense to not have a central server
13 through which all those files are distributed. So I
14 don't think those people are wasting their time.

15 I think it's important that those who are
16 building a business plan around the technological
17 platform come up with rules, business rules, that will
18 allow innovation to flourish while continuing to preserve
19 and protect copyright.

20 MR. DELACOURT: Okay. Andy, do you have a
21 quick comment on that?

22 MR. MOSS: I think I would have to agree. I
23 mean, you know, the technology will continue to advance,
24 and I think that there are a number of technologies.
25 It's not just, you know, the peer-to-peer application

1 level, but it's transport protocols and discovery
2 protocols and compression algorithms; and all those
3 things are going to advance.

4 It's a business model issue. People need to
5 build businesses that support creators' opportunity to --
6 you know, sell their work. It's all about choice, right?
7 You create something, you should have the choice of how
8 it gets distributed.

9 MR. DELACOURT: Okay.

10 MR. MOSS: If you want to give it away, you
11 should give it away. If you want to sell it, you should
12 have that opportunity, as well.

13 MR. DELACOURT: All right. Can we move on to
14 the next questioner, then?

15 MR. MITCHELL: Thank you. John Mitchell, and I
16 would like to thank the panelists for the quality of the
17 presentations.

18 I have basically a fundamental disagreement
19 with the whole approach, however. There has been a lot
20 of discussion of filtering, but we have only been looking
21 at one side of the coin. And I think I'll take issue
22 with -- just not to break the pattern, I'll take issue
23 with something Dean Garfield said.

24 (Laughter.)

25 MR. MITCHELL: But in a way that I think he

1 will agree.

2 MR. GARFIELD: I didn't think I was being so
3 controversial, but apparently I was.

4 MR. MITCHELL: I think you will agree that the
5 statement that peer-to-peer systems can and should filter
6 out copyrighted works is fundamentally wrong in the sense
7 that you will agree that if the government mandated that
8 all peer-to-peer systems had to filter out all
9 copyrighted works, that law would be challenged and
10 stricken on First Amendment grounds immediately.
11 Why? Because there are millions of Americans with
12 billions of works out there who don't want their works
13 filtered.

14 And the problem I think we have is not a
15 filtering out problem, it's a filtering in problem. If
16 I, today, wanted to set up a peer-to-peer system in which
17 I only allowed in works for which the copyright owner --
18 we're talking about copyrighted works -- the copyrighted
19 owners said, "take my works, please, and reproduce them,
20 download them, upload them, please," I have no easy way
21 of doing that.

22 The copyright office system right now is way
23 behind on technology. There is no data base there where
24 I can simply go and find out what works are out there
25 that the copyright owner has already authorized, or, five

1 years into it, decided to authorize to dedicate to the
2 public domain, or license particular rights, or let me
3 use it if it's non-commercial.

4 All those kinds of things, we're suppressing,
5 fundamentally, the freedom of speech of the copyright
6 owners who do not belong to the Motion Picture
7 Association or Recording Association's stable of works.

8 And I think the last comment about someone's

1 copyright office and saying "take my work, please."

2 MR. DELACOURT: David, do you have any comment
3 on that?

4 MR. CARSON: Well, we don't have any position
5 on filtering as such, but I think whenever I hear people
6 like Dean talk about filtering, I don't think they're
7 really saying filter out all copyrighted works.

8 I mean, if you go back to the Napster case and
9 look at the remedy in that case, the copy owners had an
10 obligation to let Napster know what works they didn't
11 want Napster to permit exchange of.

12 And I assume when I hear people talking about
13 filtering, they're talking about something along that
14 model. Copyright owners would in some -- one way or
15 another, let peer-to-peer services know, look, these are
16 the works of art that you are not authorized to permit
17 exchange of. And you would have a list, perhaps -- how
18 you would identify it, I don't know. I'm not a
19 technologist.

20 But I think it's simplistic, and I think we're
21 probably talking in shorthand when people like Dean are
22 saying filter out copyrighted works. I think it's filter
23 out the works for which copyright owners have decided
24 they are withholding authorization.

25 But Dean could probably speak more

For The Record, Inc.
Waldorf, Maryland

1 complain about not being able to distribute work. So
2 that's sort of a new issue, but -- not being able --

3 MR. DELACOURT: Peter had a comment, I believe.
4 Go ahead.

5 MR. MENELL: Just briefly. One of the reasons
6 that I am inclined towards market solutions, is because
7 markets are very good at getting works out. And there
8 are reasons why the major content industries formed in
9 the way they did.

10 There were a lot more barriers to developing
11 the kinds of markets that have supported these
12 industries. But now we're moving to another platform.
13 And I think that their clients, their principle clients,
14 are going to have to sweat a lot more to compete.

15 And we haven't seen sort of the major break-
16 through artist, but we're starting to see the independent
17 record business come back to life. The independent film
18 industry is taking off, and eventually we're going to
19 move away, in the same way we've moved away from travel
20 agents for getting airplane tickets. We're going to move
21 away from brick and mortar distribution models.

22 And the other thing is, I realize this is about
peer-to-peersrpkt

1 without even getting into these issues. And for a
2 musician, the size of the work is going to be small
3 enough that you can do that.

4 For a film producer, probably not yet, but
5 computers are going to make that possible, too.

6 I realize that there are some bigger benefits
from a peer-to-peer network, but there's no question that

1 rapidly became this mesh of interconnected things.

2 We need to keep pace with that, and, you know,
3 we're working really hard to catch up to a lot of the
4 techniques that will help make our operating system a
5 little bit more secure.

6 That's one aspect of it, and we just have a lot
7 of work to do, and we're doing it.

8 The other aspect is, PC is an open platform,
9 and one of the things that has always made it valuable is
10 that people can put anything they want onto it, and
developers can write any software they want for it.

1 also have a comment on that?

2 MR. BESEN: I think somebody should say
3 something in response to the collective licensing --
4 compulsory license proposal here.

5 I can't remember the number of conferences like
6 this in which somebody has proposed how is compulsory
7 licensing as a solution to a problem like this one.

8 I think before when moves in that direction
9 went off to look at the variety of compulsory licensing
10 systems -- they're all quite clumsy, as Peter has
11 suggested. They require someone to set the prices. They
12 require to distribute the boodle among the rights
13 holders. They don't work all that well.

14 And so, like Peter, I think maybe it's just a
15 hope at this point, but I, too, hope that the solution

1 ASCAP. ASCAP is an entity that does not administer a
2 compulsory license. ASCAP was not created by government
3 action. ASCAP's prices are not set by the government.

4 MR. LOHMANN: Actually, that's not quite right.

5 A PARTICIPANT: It is -- it is exactly right.

6 MR. LOHMANN: No --

7 A PARTICIPANT: They are subject to an anti-
8 trust consent decree.

9 MR. LOHMANN: And they have a rate court.

10 A PARTICIPANT: That is correct, but they --
11 but the rate court does not set the initial prices.
12 There is some anti-trust oversight. Something which the
13 FTC, I think, is somewhat familiar with, but that's a
14 different matter than a compulsory license where the
15 government, a priori, sets the prices and handles all of
16 that from a statutory point of view.

17 There is no need for that. We can have a
18 collective approach that doesn't require compulsory
19 licensing and foisting the entire job on the copyright
20 office, which I know from prior conversations with David,
21 the copyright office is not eager to be forced into that
22 position, either.

23 So I think there are intermediate solutions.
24 Solutions that economists like Professor Mergis, and
25 others, have said, you know, this may give us the best of

1 both worlds. I agree with Peter, it's still not perfect,
2 but I do think there is much better here to be
3 accomplished than the old style compulsory licenses of
4 yore.

5 MR. DELACOURT: Peter. Oh, go ahead.

6 MR. LOHMANN: I believe that's a factually
7 inaccurate description of the way that ASCAP rate court
8 operates, but that would --

9 A PARTICIPANT: Then Peter can tell us.

10 MR. DELACOURT: Okay. Peter, your name has
11 been taken -- oh, well, if you can do a quick response,
12 yes.

13 MR. LOHMANN: I'll certainly try to. Actually,
14 I'm not going to respond specifically to the ASCAP rate
15 court.

16 MR. DELACOURT: Okay. Sure.

17 MR. LOHMANN: I won't do that. Compulsory
18 licensing, there is the question of whether the copyright
19 owner is compelled to license the work, and that's what
20 compulsory licensing is. The question of how the fee is
21 going to be set for that compulsory license is really a
22 separate question. Whether it's done through something
23 like an ASCAP rate court, or through the new CARP-type
24 proceeding, or however, both of those processes for
25 setting rates, both of them, begin with the opportunity

1 MR. MENELL: Well, I do want to say one thing
2 on this issue, which is we seem to be experiencing a time
3 warp here. There is no way in which you can solve the
4 music problem and not address the film problem.
5 And there is no compulsory licensing system that anyone
6 has proposed that deals with the highly heterogenous cost
7 structure associated with film. And then you've got
8 software, and when the book reader technology improves,
9 you're going to have books.

10 And so I do think that we're heading into a can
11 of worms if we think we can have the government decide
12 these issues. I think we're going to wind up with the
13 farm support system that we have for agriculture.

14 (Laughter.)

15 MR. MENELL: I'm serious. I'm serious. That
16 would be the ultimate result of this, because every year
17 people would come to Washington, and say, well, how much
18 should the copyright owners get this year.

19 And it would become so far disconnected from
what consumers in the mhe tw thvaluthe ulrms3063 -22yTD far disc dno

MRPAHELL:Mr. Delacourt,ms iIhe y?om13

MRDELACOURT:s. I think we'roult o

1 on us. And the order of presentations will be from my
2 left, continuing on down, as it is in the agenda.

3 I would like to introduce the panelists. The
4 first speaker will be Mr. Cary Sherman, the president of
5 Recording Industry Association of America.

6 Our next speaker, who is accompanied by his
7 co-author, will be Dr. Koleman Strumpf of the Economics
8 Department at the University North Carolina, Chapel Hill.
9 His co-author, Dr. Felix Oberholzer-Gee, is also present,
10 from the Harvard Business School.

11 We'll then have a presentation from Dr. Stan
12 Liebowitz, Director for the Center for the Analysis of
13 Property Rights and Innovation, and Professor of
14 Managerial Economics at the University of Texas at
15 Dallas.

16 John Potter will be speaking. He is the
executive director of the Digital Media Association,

1 he'll be singing.

2 (Laughter.)

3 MR. HADEISHI: And Mr. Newton's well-known
4 songs are Bobby Sue, performed by the Oak Ridge Boys;
5 Riding With Private Malone, performed by David Ball;
6 Twenty Years Ago, performed by Kenny Rogers; and What I
7 Didn't Do, by Steve Warner and also recorded by George
8 Jones.

9 As a plug, his new album, Bubba is in Baghdad,
10 is going to mainstream radio this week. So we look
11 forward to hearing it. And as my wife makes me listen to
12 WMZQ, I'm sure I'll be hearing it soon.

13 And then the last to speak will be Michael
14 Bracy, co-founder and policy director of the Future of
15 Music Coalition.

16 Thank you. Mr. Sherman.

17 MR. SHERMAN: Thanks very much, Haj. Good
18 morning. I certainly would like to thank the FTC for
19 organizing this workshop and inviting us to speak.

20 I just want to give you a quick perspective of
21 the recording industry on everything you've been hearing
22 about today.

23 We've got to differentiate P-to-P as a
24 technology from P-to-P when it's an opportunistic
25 business model. As to the technology, we're all for it.

1 It's an important technology.

2 It holds great promise for everybody, including
3 our industry, but that promise has been diminished by
4 those P-to-P operators who have built business based on
5 the systematic and wholesale theft of others' copyrighted
6 works. That is simply wrong, and the consequences have
7 been devastating, I guess.

8 You have all heard the data by now. Since the
9 end of 1999, when file-sharing first came onto the scene,
10 to the end of 2003, which is the last year of complete
11 data, total units shipped fell 31 percent, while the
12 total value of those shipments fell 18 percent.

13 We don't have figures for 2004 yet, but
14 preliminary indications would suggest a modest
15 improvement.

16 From 1999, to today, the industry's all
17 important top 10 albums shipped over 40 percent less.
18 And the importance of that, of course, is because that's
19 where the industry makes most of its money, from the
20 major sellers. That's what enables them to offset the
21 losses.

22 But let's not forget the personal toll when you
23 just look at these numbers, and I know we're going to
24 hear a lot about numbers from the other panelists.

25 The fact is, that while illicit file-sharing

1 services seek to offer their users a veil of anonymity,
2 and you have to wonder why they emphasize that so much.
3 The effects are hardly a secret.

4 The impact of illegal file-sharing has been
5 felt by tens of thousands of artists, songwriters, retail
6 clerks, plant workers, and other music industry employees

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But the workers aren't the only victims. It's

1 resources, both financial and human, to nurture the
2 talent and try to create the demand in the marketplace
3 that permits those artists and their music to thrive.

4 We don't do that knowing full well that nine
5 out of ten times, we're not going to make it. That nine
6 out of ten of those artists will never return the
7 investment that was made in them.

8 So it's an extremely risky venture, and our
9 reward for the effort is sharing the financial success
10 when the tenth artist does thrive. And that system has
11 helped to create and sustain the most vibrant music
12 community in the world.

13 Rampant on-line piracy has thrown a monkey
14 wrench into that system. Consumers who used to be able
15 to vote for the favorite music with their pocketbooks now
16 don't have to vote with money at all. They can get the
17 same music for free. So as a result, illegal file-
18 sharing has undermined the very foundation of the music
19 marketplace.

20 Using Peter Menell's analogy about anarchy, it
21 really has created a riot, and there has been mass
22 looting. A look at the most illicit P-to-P systems shows
23 that the works most requested are the most popular albums
24 from the most popular artists. These are the very
25 artists, the one out of ten, who support the rest of the

1 industry and allow investment to take place.

2 So the result is inevitable; lower returns
3 means less ability to invest in the market. Fewer new
4 artists, fewer new products, fewer choices for consumers.

5 Fortunately, the industry has not simply
6 allowed that unhappy turn of events to slow down the
7 transition to new technologies. It's clear that
8 consumers are very interested in getting their music
9 digitally. The common mantra that we always hear, that
10 the music industry has to embrace technology in the
11 future by adopting a new business model, well, the fact
12 is that the industry has been doing just that.

13 The recent and rapid increase of legitimate
14 on-line distribution services has been made possible by
15 very aggressive licensing efforts by record companies and
16 other copyright holders. And by the way, this is a very
17 complicated industry in terms of rights structures. So
18 it isn't just record companies who have to license.
19 There are music publishers and songwriters. There are
20 the artists, who often have contractual rights to control
21 electronic distribution on-line.

22 So it is difficult to get everybody to agree on
23 a common business model and move forward, but I think we
24 have finally seen a lot of success on that.

25 One of the industry's most ambitious

1 initiatives has been to work with the higher education
2 community. We filed a report with Congress in October,
3 from the Joint Committee of the Higher Education and
4 Entertainment Communities, in which we demonstrated that
5 the groups have been working together to reach out to
6 colleges and universities across the country to engage
7 students in discussions on P-to-P and copyright, and to
8 find new ways to bring content to those consumers.

9 The good news is that we now have about 36
10 different schools that have signed up to provide a means
11 for students to get a wide range of entertainment content
12 legally and easily, and we hope that number will grow as
13 students continue to embrace these legal services.

14 There are now, in fact, a plethora of sites on
15 the Internet where consumers can get quality, legitimate
16 product. Services such as iTunes, MusicMatch, and the
17 now legitimate Napster offer clearly legal product free
18 of viruses, spyware, adware, corrupt content, as well as
19 good connections. No free riding on users' band width or
20 processing power.

21 You also have notices and labeling that remain
22 intact. So consumers and parents can make informed
23 decisions about whether the content is appropriate for
24 them. And legitimate services provide an infrastructure
25 to ensure that creators, producers, providers, and the

1 thousands of individuals who work hard to bring consumers
2 the products they enjoy, get paid.

3 Illicit P-to-P services offer none of those
4 benefits.

5 The growing avenues for distribution of
6 legitimate content, or for a broad range of ways to enjoy
7 that content, includes subscription and on demand
8 services, as well as services that offer the download of
9 files, both by individual song and by album as the
10 consumer prefers.

11 The different methods and qualities of
12 distribution are made possible by the availability of
13 different price points. Streaming services cost less
14 than tethered or limited time downloads, which cost less
15 than permanent downloads that are transferable to CDs.

16 The problem is that free trumps everything.
17 And those services that offer copyrighted material for
18 free are directly jeopardizing continued development and

1 even suggest what that number is, because I don't think
2 anybody really knows.

3 So even though those services are gaining
4 ground, the continued progress is directly impeded by the
5 unauthorized offering of identical products for free by
6 P-to-P services.

7 The companies that offer P-to-P services derive
8 their revenue primarily from advertising. That revenue
9 stream is dependent upon a significant and consistent
10 number of visitors to the file-sharing network. Those
11 visits are ensured by a wealth of free files made up
12 predominantly of unauthorized copyrighted material.

13 So the incentive for these services to remain
14 illicit is clear. Under their current business model
15 their very viability depends on it, and that was sort of
16 confirmed by Michael Weiss, chief of StreamCast Networks
17 who distributes Morpheus, who said in an interview, users

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1 doom P-to-P technology for the future to a dismal future.
2 Our industry has been trying to work with responsible
3 technology companies to find ways to legitimize P-to-P
4 and succeed where the illicit services have failed.

5 We have partnerships with companies like
6 SnowCap and World Media that are looking now for ways to
7 harness the power of the technology without relying on
8 injury to the rest of the industry to turn a profit.

9 And you know, we've already talked a lot about
10 filtering and how it can be used for porn and everything
11 else, and viruses, we certainly think it can be used for
12 copyrighted works as well.

13 The problem is that there are lot of
14 short-sighted players on the P-to-P side. In the words
15 of Wayne Roso, the problem is that even though the
16 opportunities are starting to arise now and the record

~~companies are starting to arise now and the record~~

1 watch. It's a case against Charmin Networks by the major
2 record companies down there, and the evidence that's
3 coming out in that has been very interesting. It has
4 become clear that services like Kaza not only have the
5 ability to monitor the network activity of users, but
6 also to implement filtering technology.

7 The CTO of Charmin acknowledged the existence
8 of a secret Judas version of the Kaza software that
9 gathered user statistics and sent them to a central
10 server. Such revelations are pretty eye-opening,
11 especially in light of the claims that they simply don't
12 know what their users are doing and have no control over
13 the content they share. The truth is coming out now in
14 court.

15 The clear message, P-to-P is an exciting and
16 promising technology. It's been savaged by bad actors so
17 far. The focus belongs not on the technology itself, but
18 on the unscrupulous services that abuse it to the
19 ultimate detriment of consumers and others. The question
20 is whether we'll embrace this technology in such a way as
21 to benefit everyone or let it be permanently high-jacked
22 for the short-sighted gain of a few.

23 We are ready and willing to work with the --
24 anybody who distributes music in any form, including
25 P-to-P, as long as it recognizes, respects, and enforces

1 the rights of copyright holders and the value of their
2 works. We want consumers to have confidence in a robust,
3 safe, and legitimate on-line experience. Record
4 companies are now doing that. We expect nothing less of
5 the companies that provide P-to-P technology and the
6 exciting possibilities it offers.

7 Thanks very much.

8 (Applause.)

9 MR. HADEISHI: Our next speaker will be Koleman
10 Strumpf, who is presenting a rather remarkable result.

11 MR. STRUMPF: Okay. Thanks, Haj. I,
12 hopefully, will try to convince you by the end of this
13 talk that the results are not quite so remarkable.

14 This is going to be largely framed around some
15 research that I have conducted with my co-author, Felix
16 Oberholzer, who is sitting also on the panel. So the big
17 picture about what I'll be talking about is what's file-
18 sharing do. Well, one thing we've heard quite a bit
19 about over the last two days is that file-sharing seems
20 to reduce some of the controls the copyright owners have
21 over their property. And there has been a lot of policy
22 discussion both here, and particularly in Congress, that
23 we might need to reform laws, provide new powers to
24 copyright owners to offset some of this.

25 And I think what's the sort of fundamental

1 question in answering whether this is an appropriate
2 policy, is what is the actual economic damage from file-
3 sharing. And the sort of smoking gun that Cary just
4 talked about, and I'm sure you read quite a bit about in
5 the newspaper, is the following. Okay?

6 Since 1998, album shipments, according to the
7 record industry, have fallen by 20 percent. In 1999 --
8 that's when the free file-sharing service, Napster, first
9 became popular, so most people say, well, this is
10 obviously a smoking gun -- in fact, I am going to try to
11 give you two intuitive arguments, or two sort of broad
12 arguments first about why I don't think that's actually
13 true, and then I'll sort of drill down and give you some

1 attracted to people who are not likely to have been
2 purchasing albums anyway. In particular, people who have
3 a lot of time on their hands, and not a lot of money.

4 But let me -- you know, even though I'll talk
5 later on about why I'm not such a big fan of looking at
6 aggregate data; let me give you three pieces of
7 information that are not at all consistent with this
8 notion that file-sharing hurts record sales. Okay.

9 The first piece of information is that while
10 Napster, as I pointed out, was created in 1999, record
11 sales actually continued to go up according to Sound
e first since the 2000s, and is far higher than what they'

1 we should expect that sales of albums during the summer
2 shouldn't go down quite as much as they go down
3 throughout the rest of the year because file-sharing goes
4 down.

5 In fact, BigChampagne, for example, documents
6 that file-sharing does decrease by about 15 percent
7 during the summer.

8 Well, in fact, what happens to sales during the
9 summer months? In fact, sales during the summer months
10 haven't changed almost at all since file-sharing was
11 created.

12 So just I'll try to -- bear with me with this
13 graph for two seconds. This graph shows you weekly sales
14 for 1998, and 2003. So the blue line shows sales in
15 1998, the red line shows you sales in 2003.

16 The blue shaded area is the summer. In fact,
17 you can see, according to this graph, that sales during
18 the summer are actually lower in the period when file-
19 sharing had been in creation. The exact opposite of what
20 you'd think.

21 Now, I don't really want to talk a lot about
22 what other people have done in terms of evidence on file-
23 sharing, except for just one sort of broad point. Again,
24 this comes back to what I just talked about. It
25 basically frames a lot, for example, what the record

1 industry has said. And that's looking at time series
2 correlations.

3 So much of the evidence about file-sharing and
4 record sales explicitly says, well, we see that file-
5 sharing goes up and sales go down. There must be a link
6 between the two.

7 But in fact, time series evidence really can
8 only be useful in terms of ruling out factors. In other
9 words, it's very difficult when we look at, for example,
10 two trends that go together to say that one is causing
11 the other.

12 And the main reason is there are lots -- you
13 have to consider every other factor that possibly could
14 be out there.

15 In other words, I can't think of any way, using
16 time series analysis, that I couldn't argue against the
17 fact that the reason the record industry is in trouble is
18 that Brittany Spears is no longer a teenager.

19 So again, there's lots of other evidence, which
20 I'll be glad to talk about with folks later, but because
21 of time constraints, I won't dwell on so much.

22 So let me tell you more specifically about what
23 the research that Felix and I have undertaken. Now, I
24 think the only way, if you want to understand an
25 activity, to really learn or understand about it, is to

1 actually focus on what's going on.

2 And so we are the -- we, Felix and I, in our
3 research, were the first to look at what people were
4 actually downloading on file-sharing networks. In
5 particular, we have access to a very large data base of
6 downloads. Almost 2 million downloads during the end of
7 2002.

8 And so we take the -- the basic idea is we
9 tried to take the argument on face value that file-
10 sharing hurts record sales. And so in particular, the
11 claim would be that albums that are downloaded more
12 intensively should see a greater reduction in sales.

13 Now, there is a very important kind of
14 conceptual issue that I don't want to dwell a lot on.
15 And again, I'll be glad to talk to anybody about this
16 afterwards. But it's important to at least briefly
17 mention here. And that's if you want to do this kind of
18 analysis, it's important to take note of the fact that
19 there is a common factor that drives both sales and
20 downloads -- namely, the popularity of an artist.

21 In other words, somebody like Eminem, who sells
22 a lot of albums, is also very popular in file-sharing
23 networks. That doesn't mean there's necessarily a causal
24 relation between one and the other.

25 And so what Felix and I do is a very standard

1 approach in economics, and it dates back 30 or 40 years.
2 Is to look at factors that shift downloads, but don't
3 necessarily have a direct effect on sales to try to get,
4 tease out, this kind of causal relationship between
5 downloads and sales.

6 So let me just give you one example of the kind
7 of thing that we looked at. It turns out there's quite a
8 bit of variation in the spelling of song titles on
9 albums. In particular, one very common thing is not to
10 use standard English in titling songs.

11 Now this might seem pretty innocuous to most of
12 you, but think about how file-sharing works. Somebody
13 supplies a file, which they name in some fashion, and
14 somebody searches out the file using some kind of search
15 engine.

16 If either the searcher or the sharer of the
17 file changes the spelling, or spells things in a
18 different way, they're not going to find a match.

19 So it turns out empirically in the real world
20 that songs that have misspellings in them tend to be
21 downloaded less frequently. This is exactly the sort of
22 thing that we need. Something that's going to shift
23 around downloads, but, of course, as you probably might
24 surmise, there is very little effect of whether song
25 titles are spelled using standard English on record

1 sales.

2 So what is it that -- what are some of the
3 results that we found in our analysis? Well, there's
4 sort of two main sets of results.

5 The first main sets of results are, well, what
6 is it that people actually download, or what's being
7 downloaded on file-sharing networks? It turns out what's
8 basically being downloaded is stuff that you hear on the
9 radio. In particular, stuff that's on the top 40.

10 But probably just as interesting, people don't
11 download whole albums. They really only download one or
12 two songs per album.

13 Well, why is this important? Well, this is
14 important because it suggests in and of itself that we
15 might not expect to see a lot of crowd out between file-
16 sharing and record sales.

17 Well, why is that? If you're a file -- if
18 file-sharing users are the sorts of people who are only
19 interested in two songs on an album, those are not likely
20 to be the people who are going to pony up \$18 to buy the
21 CD.

22 In fact, somewhat, you know, additionally
23 consistent kind of evidence with this is if you look at
24 paid services, paid download services like iTunes seem to
25 have a different kind of individual where people download

1 whole albums.

2 So what's the big picture about what we found?

3 Well, I'll state it two different ways. The main
4 conclusion is that there really isn't much of an effect
5 of file-sharing on record sales. In fact, in the worst
6 case scenario that we could find, file-sharing only
7 displaced less than 3 million sales, which is less than 1
8 percent of the total.

laring ocyT58 Tn d frn fact, we also show that file-sharing

1 of possible candidates. I'll just mention two. Again, I
2 can give you lots of others later if you want.

3 One example is, of course, the macro economy.
4 The fact that the economy hasn't done all that well.
5 A second one -- and I'm jumping down to kind of the third
6 bullet point on this slide -- is the growth of other
7 entertainment alternatives.

8 Kids, particularly, have lots of different
9 things that they can spend money on. Things like cell
10 phones and video games. In fact, while record sales have
11 gone down by about two-and-a-half billion dollars since
12 filing sharing went on, video game sales are up over \$3
13 billion.

14 It's not hard to argue that what's going on is
15 not something that is due to file-sharing, but simply
16 displacement from one kind of entertainment spending to
17 another. Thanks.

18 (Applause.)

19 MR. HADEISHI: Thank you, Koleman. That was
20 very interesting.

21 Our next speaker is Stan Liebowitz,
22 representing a different economic analysis.

23 MR. LIEBOWITZ: Yes. You may wonder what the
24 time series was that Koleman kept talking about that you
25 shouldn't be paying any attention to. And that's going

1 to be, to some extent, what I'm talking about.

2 (Laughter.)

3 MR. LIEBOWITZ: Now, this is -- let me tell you
4 that there is a paper outside if you want to learn more
5 about this, and, also, that paper contains a discussion
6 of problems with the data in measuring lots of Internet
7 activity that I don't have time to really go into.

8 So that's the first thing. The other thing is
9 sort of a more general point. There are some activities
10 that you really don't need to do much in the way of
11 econometric work to sort of know that there is a cause
12 and an effect.

13 All right. So if one person walks up to
14 someone else and punches them in the nose, and the nose
15 starts bleeding, generally we can say we don't need to
16 call an economist to find out what the cause was of the
17 effect.

18 Now, what I'm going to suggest is that in fact
19 we have essentially a punch that is pretty obvious, and
20 then some bleeding that occurs right after.

21 But I will say that you can in fact go into
22 things in more details, and I'll talk about those. And
23 then I'll say that other people who have -- the last
24 slide I have will be a listing of seven or eight studies
25 by economists who look at this.

1 All of them come to a conclusion that is
2 different than Koleman's. So it's not just time series,
3 which Koleman has in fact complained about.

4 Now, the next slide gives you a bit of the
5 history of record sales. Now, these are sales per
6 capita, and they're using RIAA data, and I should mention
7 that other people have mentioned Sound Scan data, which
8 is fairly common. Sound Scan data comes from resale
9 sales, and it turns out that that -- and this is about 25
10 percent of the market.

11 It also turns out that if you look at the
12 numbers that the non-retail data have had a considerably
13 larger decline in sales than the retail data. So that
14 there is a possibility you can get a miss measurement
15 using Sound Scan data.

16 All right. What it shows is a fairly general
17 increase with little upticks and downticks. Then, in
18 1999, Napster starts, and you can see on the slide where
19 it begins. That's the punch in the nose.

20 Then, you can see afterwards this decline that
21 occurs, which is larger than any other decline that you
22 can find over this period of time, and this is not a
23 period of time that I just randomly chose. This is the
24 longest period of time for which we have consistent data.

25 Prior to 1973, the RIAA did not put out

1 published numbers like this.

2 So what we have is a very large decline, no
3 matter how you measure it, whether it's percentage terms,
4 absolute terms, number of years it would take to get
5 back. So if you take a look, we're at about four -- in
6 2003, it's about four albums per capita. You would have
7 to go back to either 1991, or, in reality to get a lower
8 number, 1987.

9 So it's quite a large decline no matter how you
10 measure it. And one of the things we would want to know

1 sharing might be the cause of this, besides the fact that
2 it occurred right when the sales started to decline, and
3 that it started essentially -- the thing about file-
4 sharing that is so unusual is it didn't sort of grow from
5 something small and over a long time become large.
6 Napster was up to its full size within a year, and it's
7 not clear that there has been that much of an increase in
8 terms of the number of files that have been downloaded
9 since then.

10 The Pugh Survey numbers indicate something like
11 50 percent. There are other numbers floating around, but
12 this is one of the measurements that is off by at least a
13 factor of 10, according to different people who measure
14 how many files get downloaded. So it's not clear whether
15 it's 200 million files a month that get downloaded, or 2
16 billion. We don't seem to really know.

17 Right now, common sense, which we otherwise
18 might say is economic theory to some extent, but some
19 people -- not everybody, but some people -- are going to
20 replace the purchase of a record with a downloaded
21 product that they can get for free.

22 No one that I know says that every downloaded
14 file is going to be a replacement of a sale. It's

1 technologies, which turned out not to be true.

2 But in this case, it seems -- it's very
3 reasonable to think that some people are going to replace
4 -- they have a perfect copy, and now that they have CD
5 burners, which is why it took a few years to get -- to
6 keep dropping as CD burners kept increasing. They have a
7 perfect substitute for the purchase of a CD.

8 So we expect some substitution. It's hard to
9 come up with any good reasons to expect there to be
10 something to countervail the substitution effect, which
11 is only negative.

12 Koleman previously had talked about sampling,
13 and other people have talked about sampling, and Napster
14 used sampling in its defense. That apparently is not
15 anymore an important position for Koleman, but the fact
16 is it's not clear that sampling is expected to lead an
17 increase that would countervail the decline.

18 And so something else is presumably going on if
19 you believe that it's not file-sharing.

20 Now, in fact, you can look at other
21 alternatives independently. One of them is GDP, as I
22 mentioned. The other one would be the price of CDs.
23 That has been basically constant for 10 years. It has
24 declined somewhat this year.

25 The quality of the music has been mentioned.

1 numbers on the axis are 1983 dollars. So they may not
2 look totally realistic to you.

3 And note that there are two scales. And so
4 there is a different scale for each line. So don't
5 confuse the fact that the lines up here intersect each
6 other.

7 The blue line represents units -- I'm sorry.
8 DVD revenues sold. And looking at that, which is what
9 basically people had -- that's what most in the
10 newspapers and the media. You might think, gee,
11 something really did happen in 2000. DVD sales took off.
12 Maybe that would be an explanation, and that would look
13 pretty good.

14 Now, what I pointed out in the past was there's
15 also an increase in the late '80s, and it turns out that
16 that period in the late '80s was when CD sales were doing
17 very well.

18 But it turns out you don't have to do that at
19 all, because if you look at video rentals, it turns out
20 they were declining in the last few years, and they were
21 declining by an amount so that when you take a look at
22 total expenditures on whether you're renting or
23 purchasing DVDs and VHS tapes, yes, they've been going
24 up, but they've going up since 1994, 1995.

25 Nothing is happening in particular in 1999 or

1 have the numbers before 2000 and the numbers after 2000,
2 and what they find is that the K rate is considerably
3 greater now than it used to be.

4 Which is consistent with the substitution
5 story, which is the first week it comes out for the
6 albums that don't get on the on-line services before
7 they're officially out, people still have to buy them
8 because they're not available in great quantities on the
9 services.

10 But in that second, and third, and four, and
11 fifth week, they start decaying more rapidly because
12 people can get them from the services and they don't have
13 to go buy them anymore.

14 So that, again, is consistent with the story
15 that says file-sharing is harmful.

16 So that's the conclusion. That there is no
17 reason to believe that there is any other evidence,
18 except file-sharing, for the decline that's occurred.

19 I should mention that there are -- I remember I
20 started to interview with a woman 110 years old, or
21 something like that, on television a few weeks ago. And
22 I asked her why she lived so long. She said I drink a
23 lot and smoke.

24 And I think, you know, if you see her, it's a
25 cute little story, but I don't think it would be

1 considered as evidence that in fact smoking is good for
2 you because she lived to 110.

3 So the fact that England or Australia may not
4 have had a decline in the last few years in file-sharing,
5 is not evidence that it doesn't in general cause a
6 decline. I try to stick with countries I know best,
7 which happens to be the U.S.

8 Now, it turns out you can do regression
9 results, and I'm not saying we shouldn't do it. I'm not
10 exactly a flat earther. I don't really believe you need
11 to, but if you were to do regression results, here are
12 the studies that have done regression results.

13 As I have said, you can go look at them, my
14 paper outside references them. There are three
15 dissertations here. One of them is at Harvard, from the
16 economics department. There are other papers as well
17 that use different techniques.

18 Interestingly enough, the one at Harvard uses a
19 technique fairly similar to what Koleman does, and finds
20 the exact opposite results that Koleman find. That the
21 most popular albums do better. At least the version of
22 the paper I saw, the top 25 percent of the albums are
23 helped by file-sharing.

24 And in the Harvard study, the Blackburn guy, he
25 finds the exact opposite. That a -- may not have much in

1 fact on the average record, but it has a very strong
2 negative impact on the most successful records.

3 So quite interesting that it's so different.
4 But all the others find some degree of harm. Three of
5 them, including one that I have done, say that the harm
6 is large enough to basically explain the entire fall, and
7 others find that it's not actually capable of explaining
8 the entire decline.

9 But the only saying that it's positive, or zero
10 -- and it's actually positive in the numbers, unless
11 you've changed your results since the April paper; barely
12 significant, that's true, or maybe not -- you know, 90,
13 88 percent confidence level.

14 But they're the only ones saying it's not
15 negative. You can go and look for yourself. Thank you.

16 (Applause.)

17 MR. HADEISHI: I am going to allow Koleman and
18 Felix to do a very, very brief response to that, if you
19 don't mind.

20 MR. OBERHOLZER-GEE: Okay. Let me just say two
21 things. The first one is the cute little story about
22 someone punching someone else in the nose. Yes, it's
23 true, we see that the music industry is bleeding. The
24 key question is was it the short stocky guy, or was it
25 the tall guy that punched the music industry in the nose.

1 And in fact, we have a videotape. Koleman's
2 and my position is let's look at the data. Let's look at
3 the video tape. Professor Liebowitz' position seems to
4 be let's try to guess who the guy was who punch the other
5 guy in the nose.

6 So that's the first part. The second thing
7 that I want to say about all the other studies that are
8 out there, our study, for reasons that I don't quite
9 understand, is the only one that has bothered to look at
10 actual downloads.

11 Every --

12 MR. LIEBOWITZ: The Blackhorn study uses data
13 from Big Champagne on downloads.

14 MR. OBERHOLZER-GEE: Right. So what
15 BigChampagne measures is how many files are sitting on

1 -- at the number of files on people's hard drives
2 increases over time, sales drop off. That, of course,
3 has nothing to do with the effect of P-to-P on sales.
4 That's just a statistical artifact that comes directly
5 from not using the right data.

6 So Professor Liebowitz obviously is a very
7 smart person. He's made up lots of numbers here in a
8 very creative way. What I would ask you to do, is do the
9 second study, but actually look for downloads. Don't
10 look at what's on people's hard drives. Look at what is
11 being downloaded as we speak.

12 And then I'll be very interested to see what
13 you find. I mean, the effect of P-to-P on sales is a
14 moving target. Technologies change all the time.
15 Consumer behavior might change over time.

16 It's interesting to study this, and I think
17 economists are sort of in a unique position to do this
18 because we have the methodological tool. But unless
19 you --

20 A PARTICIPANT: Will you yield that time to
21 those of us who have to actually speak, still?

22 MR. OBERHOLZER-GEE: Unless you look at the
23 videotape, you're not going to find out who punched the
24 guy in the nose.

25 MR. HADEISHI: Okay. And the rest of the

1 speech, let's try not to turn this into a personal --

2 MR. LIEBOWITZ: Let me just say that the
3 videotape is a time series, and they're not doing a time
4 series.

5 MR. HADEISHI: Okay. We're going to have more
6 questions about the economic studies, since that's my
7 inherent bias, but next up is Jonathan Potter, to speak
8 about a large number of his members, if I'm not mistaken,
9 are central server legitimate music downloading sites,
10 and he's going to speak a little bit about what his
11 experience has been.

12 MR. POTTER: Thanks. This is something new for
13 me, watching economists squabble.

14 (Laughter.)

15 MR. POTTER: It's different than the way we
16 lobbyists do it, and, you know, there's no respected
17 colleague, like on the floor of the House.

18 I'm going to talk about three things quickly.
19 I'm going to try to do it quickly. Quicker. I'm going
20 to give you a quick overview of DMA, and who we are, and
21 who our members are, and what they do, and how they fit.

22 I'm going to talk about impact on the market of
23 what I call the black market networks. Other people have
24 used file dissemination and things like that. I think
25 black market network is a pretty apt term.

1 And I'm going to talk about solutions.

2 So DMA was formed in 1998, by folks like
3 RealNetworks and LiquidAudio, our members today are
4 Yahoo, RealNetworks, Amazon.com, as well as much smaller
5 companies.

6 Our vision of the world is that the digital
7 world, digital distribution, web casting versus
8 broadcast, this is all just new media, new technology,
9 new business opportunities.

10 Essentially our companies are in-betweeners.
11 We are in-between the creator and the consumer. Which
12 leads to our view of the Copyright Act, and the copyright
13 provisions in the Constitution, which were all about
14 creators and consumers.

15 Anybody who is in between the creator and the
16 consumer, needs to be adding value to one end of that
17 chain or the other. Or they should get out of the way,
18 or they will soon be pushed out of the way if the
19 marketplace works.

20 Now, we happen to think, selfishly, perhaps,
21 that digital innovation, digital downloads, web casting,
22 consumer influenced web casting; those sorts of services
23 that we offer, create efficiency. Create compelling
24 products and services. Consumers embrace them. Creators
25 embrace them, and, so arguably in the long term future

1 there is a role for our company to play.

2 We think there are also companies out there
3 that don't seem to be adding value to the creators. That
4 don't seem to be adding value to the consumers, or they
5 cloak their value in low prices or free, but arguably,
6 you know, there is things that undermine the value of
7 free that other folks have talked about, and I think was
8 talked about a lot yesterday when I wasn't here. Things
9 like spyware and adware.

10 So sometimes free isn't so good as we all learn
11 in the marketplace. But that's generally who our members
12 are, what our philosophy is of how we look at it. And
13 it's not just a copyright set of values, it's a
14 marketplace set of values.

15 You're not creating opportunities to either
16 benefit the creators with royalties, or with promotion,
17 or with something that is really tangible to them and
18 that they value, or you're not creating true value to the
19 consumer, you know, you just really don't have a
20 legitimate role.

21 Putting aside law. Law has nothing to do with
22 whether you're playing a constructive role in the
23 ecosystem here, in the creative ecosystem, and in the
24 cultural dynamic.

25 Let's talk about the impact on the marketplace.

1 We've heard a lot about -- you know, from brilliant
2 economists who dig deep and come up with all sorts of
3 factoids that they, you know, are able to use for
4 different arguments.

5 I would say as a casual observer and a reader,
6 that there is a lot of statistics that go both ways on
7 what has been the impact of black market networks on
8 creators.

9 Part of it is how do you define the creator.
10 If the creator is a record company who makes money
11 selling plastic disks, or has traditionally made money
12 selling plastic disks. It's pretty hard to say it hasn't
13 harmed them. Probably in great significance. They have
14 a single revenue stream, selling recorded music.

15 Now, if you're a creator, that is a band,
16 perhaps it hasn't hurt your revenue, because, you know,
17 the networks, the dissemination, the distribution of your
18 music has created new fans who come to your concert, or
19 who buy your t-shirts.

20 And so you have created new revenue streams
21 that have offset other revenue streams. That would be
22 the royalties off these CDs that perhaps are not selling
23 so well.

24 Let me just note that in response to something
25 Koleman said, I sat on many panels years ago that the

1 record industry had a broken business model, and it was
2 broken because they were trying to sell two songs I liked
3 with 12 songs I don't for \$18. And that was the physical
4 model.

5 So I would actually say to Koleman the fact
6 that a consumer has only two of the files from a CD,
7 absolutely undermines the issue of whether he is going to
8 buy that CD. He's not. He never wanted the other 12
9 songs in the first instance.

10 So I -- you know, in terms of undermined sales
11 of CDs just because the consumer only had two of the
12 songs of a 12 track doesn't mean that he would have

1 business model, is the RealNetworks Music Store, and
2 that's something that -- you know, so we feel fairly
3 strongly about offering value and figuring out ways to
4 make this market work. It makes it harder for our market
5 to work.

6 For consumers, as I reference easier, one could
7 make the case that the impact on the consumer has been
8 positive. They get stuff for free. This is a good
9 thing. I think the arguments were discussed aggressively
10 yesterday.

11 I have had -- actually not through this sort of
12 service, but I have had the unfortunate circumstance of
13 having my browser high-jacked about six weeks ago. It
14 was brutal.

15 So you know, adware, spyware, call it what you
16 want, at the end of the day the big winners are the IT
17 companies, or the IT consultants that come help you clean
18 up your hard drive. Or you actually end up going out and
19 buying a new PC because you really can't get it off your
20 hard drive.

21 But I think consumers, all it takes is one bit
22 of spyware, one bit of adware, and sooner or later they
23 will give up and go back to legitimate services.

24 What's the solution; the solution is a
25 comprehensive program that includes education,

1 enforcement, and a compelling legal alternative.

2 Consumer education, you know, we can educate consumers a
3 lot about law.

4 Cable theft went down significantly when your
5 neighbor was walked down the street in an orange jump
6 suit with silver handcuffs. You know, it works. General
7 deterrent works. When somebody down the street, somebody
8 in your dorm gets busted, it works.

9 Having said that, it's perhaps not the only way
10 to go. We can educate consumers about doing the right
11 thing. My seven year old came home and told me that
12 every time somebody smokes a cigarette, it knocks five
13 minutes off their life.

14 Twenty-five years ago, we started an
15 environmental education with that littering commercial,
16 anti-littering commercial with the -- now we call the
17 Native American, standing there with the tear dripping
18 down his face because somebody littered, you know, on the
19 road.

20 We teach people how to behave in society. We
21 do it specifically in our homes. We do it in our
22 schools, we do it broadly through the media. We can
23 teach people that creativity has value. That creators
24 deserve to be compensated, and that if we want more
25 creativity, we have to figure out a way to encourage it.

1 We can also, of course, teach people about the
2 price of freedom.

3 Let's talk about enforcement and law. We can't
4 prohibit technology. We can't enforce out of existence
5 any peer-to-peer technology or anything else. We can
6 prohibit abuses of technology, as Andy Moss referenced.

7 We can prohibit or impose liability on
8 parasitical businesses that make a living leeching the
9 value out of one set of creators, and creating
10 interesting, you know, business models, if you want to
11 call it that; by imposing, you know, all sorts of
12 collateral products and harms on consumers.

13 So if that's what the evidence demonstrates, if
14 that's what people believe, we, as a society, can find
15 out who is doing that and go after them.

16 We should also not give any credence to people
17 who play chicken with the law. Hank Berry is an old
18 friend. Hank Berry made an investment in Napster, and to
19 some degree he played chicken with the law and he played
20 chicken with the record industry. And he said "I think
21 file-sharing is going to be so big, so big, that the
22 record industry will have to come to their knees and
23 license everything we want, because it's going to be the
24 only thing left."

25 He rolled the dice; he lost. You know, the

1 litigation that's still going on. I've had a view about
2 it. He rolled the dice and he lost. There's not a lot
3 of pity out there for those who invested knowing of the
4 uncertainty in the law.

5 The availability of the legal alternative, the
6 marketplace, is really how we're going to win. We have
7 to win by making content available. We're not going to
8 win by not making it available.

9 So for the artists who sit there and say piracy
10 is bad, but then don't license their content to Apple, or
11 don't license it to Microsoft's MSN Music Store; they
12 might as well escort their fans, their fans, right over
13 to the black market networks. Because their fans are not
14 necessarily buying their CDs, but they sure do want their
15 music. And they'd sure rather have, you'd assume, virus-
16 free high quality. Is it worth a buck? Yeah, it's worth
17 a buck.

18 So we have to make the content available.
19 Preferably by choice. Preferably not by a mandatory
20 compulsory license, but if the marketplace truly doesn't
21 work, that mat should be the way to protect artists and
22 protect creators.

23 We have to make the system work at a fair
24 price. We don't have to make the price lower than the
25 marginal cost of the duplicate. We sell bottled water.

1 MR. OTTOLENGHI: I want to thank the FTC for
2 the invitation to speak before you this morning. I think
3 I was brought up here because I am neither an economist,
4 nor am I a lobbyist, an attorney, I am not a member of
5 the RIAA, the MPAA, or any other association other than
6 the DCIA.

7 And actually, I have a happy presentation.

8 So --

9 (Laughter and applause.)

10 MR. OTTOLENGHI: -- I've got something good to
11 say about what's going on, and by way of backdrop for
12 that, let me play a little movie for you. This is what
13 our company does. So this is a more interactive
14 presentation for you.

15 A PARTICIPANT: Do you have the legal right to
16 play this movie in public?

17 MR. OTTOLENGHI: You know, I actually made this
18 movie myself. So I am authorized through my own
19 licensing of this particular presentation.

20 (Laughter.)

21 MR. OTTOLENGHI: Now, some of it's cut off here
22 at the bottom, which -- just for the reason of the
23 presentation screen and the resolution.

24 But what our company does is we distribute
25 content -- music, videos, eBooks, software, and games --

1 vis-a-vis various distribution methods. So digital
2 distribution platforms. Specifically, peer-to-peer web
3 sites where we syndicate content. Various web sites for
4 download. Satellite radio, television, and now, we do
5 integration with PC to TV. So from the PC to the TVO, or
6 the personal video recorder, et cetera.

7 And if you want to know more about this, and I
8 won't bore you with the rest of the details of it, you
9 can go to our web site and just take a tour around the
10 web site and see what we do.

11 We have several major artists in the music
12 industry who are part of our portfolio, and we're really
13 a new business model. We're a platform, if you will, for
14 innovation and distribution through peer-to-peer.

15 By way of a little bit of a backdrop, there was
16 a mention by Peter earlier today about travel agencies.
17 We are part of a seven-year-old company that actually
18 started out by creating software which would aggregate
19 reservations from various web sites around the Internet
20 and put it in one screen at one time.

21 So if you've used Orbitz or Travelocity, you've
22 used our technology. Where you find content from several
23 sources in one place, very similar to peer-to-peer. So
24 legitimate use of technology, meta search technology.

25 We've done the same thing in the job placement

1 and job hunting industry. And finally, we turned our
2 sites on to music and media distribution industry because
3 we believed there was a better model, and one of the ways
4 to effect that better model was to use the peer-to-peer
5 networks.

6 So what do we do, we talk to the content rights
7 holder, the artist, publisher, whoever it may be. And we
8 secure rights to distribute their content legitimately in
9 an authorized fashion through the peer-to-peer systems.

10 In fact, we do this so effectively that we're
11 working even with the FBI to find people who don't do it
12 in an authorized way. And we work with the DIA in an
13 effective way to bring content legitimately to the
14 peer-to-peer networks.

15 We combine all of this with an effective viral
16 marketing technique. Meaning we put additional content
17 and information around the media, the actual music, or
18 the song. And we provide additional information for the
19 consumer, so they're more interested in our files, rather
20 than the free and illegitimate files. So we add value.

21 And we also add value by connecting those files
22 to the web so that if someone finds an artist that they
23 like, they can learn more about that artist by clicking
24 on the actual song, or the splash page that comes with
25 the song and go directly to the artists' web site and

1 interact and engage in further commerce.

2 We provide content, as I mentioned, across many
3 channels, and in the interest of time, I won't go back
4 over this. And we do it in a way which enables both paid
5 and free content.

6 So let me stop on that point. We enable an
7 artist or a copyright holder, or a content rights holder,
8 to actually sell their content through peer-to-peer, or
9 to work with one of our advertisers who will support
10 their content, pay them for the content, and make the
11 content available for free over peer-to-peer.

12 We have now also signed up with every paid
13 search provider, except for Google, and we provide paid
14 search ads which underwrite the cost of those files, or
15 the compensation back to the rights holder.

16 So that the file is now offered, or the music
17 is offered, at a lower price point. We've actually
18 effected this in the peer-to-peer environment.

19 We then use, as I mentioned before, advanced
20 technology. Some of the multi-media technologies.
21 Technologies which enable samplers, equalizers, eBooks,
22 portfolios; all in multi-media form which accompany the
23 music file, when we talk about music distribution over
24 peer-to-peer. And incent people to want to listen more
25 to that content and go buy more content, or subscribe to

1 marketing programs where they can get that content for
2 free.

3 Unlike most of the debate in the last two days,
4 this is for real. This happens today. It's not
5 theoretical, it's not based on time snapshots and time
6 frames, or whatever else it may be. But frankly, it's
7 quite open to debate as to whether that information is
8 absolutely legitimate or real.

9 I think Professor Michael Smith yesterday
10 actually had the most legitimate statements about this,
11 which was that you have to look at the real numbers. You
12 have to look at the models, and you have to incent new

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1 thing. We are putting legal and authorized content onto
2 those networks.

3 And I would like very much for any of the
4 members of the RIAA, or MPAA to come and work with us,
5 because we can take your content out there legitimately.
6 We can distinguish it from free, and we can make it
7 interesting and incentive for consumers.

8 It's also a bridge in the model between what
9 you're doing and what the peer-to-peer companies are
10 doing. We work with P-to-P revenue engine, which is the
11 DCIA initiative, and this very simple slide here, which
12 is easy to understand --

13 (Laughter.)

14 MR. OTTOLENGHI: -- was a creation of mine.
15 Unfortunately. Such is life.

16 It is part of an initiative which we can
17 provide secure distribution through the peer-to-peer
18 systems through this technology. The combination of 10
19 companies working together. Some of whom are represented
20 here, some of whom are not, but who can legitimately put
21 content, since we have tested and integrated this
22 technology ourselves.

23 We have detailed information every time we
24 distribute a file on the behavior and actual use of
25 content. I see I have two minutes left.

1 And with that, we are able to ensure marketing
2 programs with content rights holders, and a relationship,
3 which is the most important thing.

4 There was a statement just a moment ago about
5 dragging your customer off in handcuffs in an orange jump
6 suit. I am pretty sure, and I am not an academician or a
7 lobbyist, that is not a good way to keep customers.
8 Okay. That doesn't incent them to want to work with you.

9 So if you do have a legitimate way to work with
10 them, a real business model -- and I really think it's
11 important for the Federal Trade Commission to understand
12 that if there is a legitimate business model out there
13 that's being developed, that they should encourage the
14 various parties to participate in working on such a
15 model. If not ours, something like it, because this does
16 work, and it works today.

17 If you want to know any more, please do go to
18 our web site, or take a look over the peer-to-peer
19 systems. I have some examples here with hyper links. I
20 know that this presentation will be made available

1 she was a model, and now she is a music composer and a
2 musician, and she averages about 2 million impressions
3 ever week on-line just for her music.

4 And approximately 200,000 downloads a month,
5 and she has gone from having to work as a part-time
6 waitress and hostess and so on, to now a full-time
7 musician as a result of distribution through P-to-P.

8 I would say that there are several other
9 Jillian Anns out there. Her case study is here in the
10 MIT Magazine of Innovation, the technology review
11 magazine. But we have several other case studies in that
12 we have 5,000 musicians. We have over 10,000 films,
13 independent films from student film festivals, the
14 winners of the last five years; and these things are
15 doing very well over peer-to-peer.

16 I would encourage this entire group to look at,
17 the FTC in particular, positive business models. If
18 legislation and fighting in the courts is the thought on
19 how this is going to be resolved, that's a complete
20 mistake because the public is ultimately what drives this
21 content commercial use. Thank you.

22 (Applause.)

23 MR. HADEISHI: Thank you, Les. That was very
24 interesting.

25 Our next speaker is Sam Yagan, president and

1 CEO of EDonkey, if I'm not mistaken. And I actually
2 don't know what Sam is going to tell us about. So this
3 should be interesting.

4 MR. YAGAN: I hope you all are not too
5 disappointed that although I have been called a pirate, I
6 don't dress like one.

7 (Laughter.)

8 A PARTICIPANT: Where's the bird?

9 MR. YAGAN: Or the eye patch. I left mine at
10 home.

11 First, I want to thank the FTC for hosting what
12 I believe is the first panel of its kind and having such
13 an open forum of all sides of this issue. Again, I am
14 neither a lobbyist nor an attorney, so my role here, as
15 Haj said, it's not clear, but hopefully my perspective
16 will be at least a little bit unique and interesting to
17 those of you who may not know what it's like to be on the
18 inside of one of these companies.

19 I am the president of EDonkey, also a founding
20 member of P-to-P United, who you heard from yesterday.
21 EDonkey right now is by most accounts the most popular
22 file-sharing software in the world.

23 We are a New York company, we're actually
24 incorporated in the United States. So like the recording
25 companies, we do employ Americans, and we pay taxes.

1 (Applause.)

2 MR. YAGAN: And I don't think any more
3 peer-to-peer companies will incorporate in the United
4 States as long there is this ambiguity in the legal
5 process. So we are driving innovation offshore.

6 I had some remarks prepared, but so much has
7 transpired in the morning I have been here that I felt it
8 was important to at least comment on some of what I have
9 heard so far.

Where to start? First, in response to Mr.

1 Also, Mr. Garfield, you talked about the profit
2 motive as though this were this terrible thing. That we
3 were motivated by profit. And so I have been thinking
4 about that a little bit. I think that is actually in the
5 rights holder's interest that software companies are
6 motivated by profit, because what that means is we
7 actually want to make money selling music. That's where
8 all the big revenue is coming from.

9 What would be more fearful to me would be these
10 rogue anarchists, who might not be profit motivated.
11 Someone talked about BitTorrent and Graham Cohen. That
12 is more frightening. He is not motivated by profit.
13 He's motivated by just developing peer technology.

14 So in some ways I think the profit motive is
15 not a bad thing for the recording industry. In fact, you
16 might want to embrace that and say, well, how can we help
17 you, the software companies, make more money.

18 Another issue that has come up is whether this
19 filtering technology is viable. Can it be done
20 centrally, decentrally; and it occurred to me that this
21 seems to be something that has a factual answer, but that
22 the sites seem to disagree on.

23 So Mr. Sherman and Mr. Garfield, I hope you
24 will join me in calling for an impartial study sponsored
25 by any group of people, the FTC, or other; to actually

1 investigate from a scientific perspective, throw the
2 lobbyists and lawyers out of the room, and let's see if
3 this is actually possible. I hope you'll agree to do
4 that later on when you respond.

5 I'll reiterate what Mr. Moss said earlier, that
6 the technology is just a tool. I won't hit on that too
7 much, since that's been repeated by lots of people. But
8 what's important is that the use of technology is very
9 dynamic. It changes over time.

10 So when you look right now how is the
11 technology being used, it would be a real danger to
12 extrapolate and say that is how the technology will
13 always be used. And the case in point is imagine if when
14 the VCR came out, none of the motion picture companies
15 released their theatrical hits on VHS.

16 Well, of course, the VCR would not be used for
17 legitimate purpose of renting those movies, because they
18 would not have been made available.

19 So I would ask that if you want to increase
20 legitimate use of these networks, let us sell your music.

21 I think everyone has already hit on the fact
22 that peer-to-peer is here to stay. It's important also
23 to recognize that, you know, the technology of these
24 peer-to-peer applications goes well beyond our companies.
25 Just like if Microsoft goes out of business, your

1 Internet Explorer will still work. All of our networks -
2 - all of our software will continue to work regardless of
3 whether the companies actually exist.

4 Fourth point, peer-to-peer is evolving very
5 rapidly. Napster went away, so Kaza and Morpheus and
6 EDonkey came up very quickly. The next generation of
7 this software will be fully encrypted and fully
8 anonymous, and you won't be able to tell who is using the
9 software and what's being shared on that software.

10 So it's just important that we do look forward
11 in looking at what are the possible opportunities with
12 the software, instead of just saying what is the current
13 state of the art, and what is the past state of the art.

14 The technologists and entrepreneurs who are in
15 the P-to-P software development space, ourselves, are
16 struggling to keep track of the technology and stay on
17 top of what's going on.

18 So when we think about what are the rights, you
19 know, should there be government regulation or government
20 intervention, litigation, legislation, I think that you
21 have to think that who is really well positioned to
22 predict the future in this technology. And I would argue
23 it's probably no one.

24 And so when we resort to these -- when we
25 resort to these kind of regulatory solutions, there is a

1 real risk that we're going to get it wrong anyway. So
2 this is not going to be a cure all.

3 I have a quick digression. I want to tell you
4 all a quick story about my first experience with file-
5 sharing. This is a cassette tape that was given to me by
6 my best friend in high school, and that contained on it a
7 mix of U-2s greatest hits up to that time.

8 I had never heard of the band. I was kind of a
9 nerd in high school. Apparently they were a big band.

10 (Laughter.)

11 MR. YAGAN: I didn't really know that at the
12 time. And so he gave me this, and I kind of didn't like
13 U-2 the first time I heard it, and I couldn't really
14 understand what was going on. But I listened to it
15 pretty much every week for the course of my sophomore
16 year in high school, and by the end of the year, I
17 totally fell in love with U-2. I just loved it.

18 And so I was preparing for my talk today, and I
19 thought how much money have I spent on U-2-related
20 paraphernalia? So this includes CDs, bands, you know,
21 tickets, concert tickets, posters, whatever; I've spent
22 over \$2,000 on U-2 paraphernalia, including albums. I
23 have every one of their albums.

24 And so it occurs to me that this is file-
25 sharing, and one customer on one band spent \$2,000.

1 That, to me, seems like a good thing for the artist and
2 for the recording industry.

3 One undeniably positive effect of peer-to-peer
4 on the consumer, is, in a word, iTunes. With all due
5 respect to Mr. Jobs, I would argue that it is the
6 peer-to-peer software that really reinvented the single.
7 Would iTunes be there selling singles had not singles
8 become so pervasively available on peer-to-peer software
9 applications?

10 So you know, again, that's a way you -- you
11 might not have predicted when you first saw peer-to-peer
12 application that what this is going to do is, this is
13 going to deconstruct the album -- the idea of having to
14 buy two songs to get the 14 songs you don't want. That
15 is no longer a constraint to consumers that I would not
16 have predicted, but it clearly was an effect.

17 So one of the questions I was asked to talk
18 about is, is P-to-P just like Walmart.com, or iTunes?
19 And there are too many reasons why it's not. The first
20 is comprehensiveness. A good on-line store I think has a
21 million tracks, tops, and a good -- you know, on the
22 P-to-P world, there's probably about a hundred million
23 unique files.

24 And so I was actually trying to find U-2's 2001
25 Chicago performance on their Elevation Tour, and it turns

1 out I really can't buy that anywhere.

2 So did I go to EDonkey, as you might expect,
3 and download it. No, I didn't, but I went to EBay, and I
4 was able to buy a version. And I'm afraid that nobody --
5 none of the rights holders actually got the payment for
6 that. It was probably some guy who just taped it on a
7 bootleg.

8 So that exists. And then there is this issue
9 of community. People are tied together by music, and
10 that's great news for the music industry. People
11 congregate around your product.

12 And so I think that's something that the P-to-P
13 applications offers, is that community sense. And this
14 is only the tip of the iceberg. As voice over IP and
15 social networking becomes more embedded into these
16 applications, it's only going to become more sticky.

17 Okay. Real quick, since I'm running out of
18 time. There is all this debate about the artist, in
19 particular the poor artist versus the rich artist, let's
20 say.

21 In my other pocket, I have a CD from a band
22 called Bishop Alan. I suspect no one has heard of them.
23 And that's because there was no record label that would
24 sign them. So they have -- we've been promoting them on
25 the EDonkey software for the better part of the last

1 year, and we are helping them to do their own really hard
2 work. They just completed a profitable, very profitable,
3 nationwide tour, and they reached number two best-selling
4 album on Amazon.com.

5 Now, figure that. If they don't have record
6 label support, all they have is their hard work, and
7 distribution on a P-to-P application. Number two on
8 Amazon.

9 I have been hearing a lot about you can't
10 compete with free. These guys would tell you otherwise.

11 The last point, and I will actually stop there,
12 does P-to-P threaten the music industry? I think that's
13 kind of a central question we're all here to talk about.
14 And the answer is, it doesn't, because we're not in the
15 music business. We're in the software business. The
16 real threat to the music industry -- and, here, I'm out
17 of my league, because I'm not in the music industry.
18 But I would suspect the risk to the music industry is
19 someone like me, an enterprising entrepreneur, says, you
20 know what, what if I leveraged the possibilities of
21 P-to-P and created a music company that basically did a
22 lot of what this band, Bishop Alan did, leverage P-to-P
23 to make money.

24 Cutting -- so, Mr. Sherman, I believe you said
25 so many people worked behind the scenes in the music

1 industry; well, that's part of the problem, I think. I
2 think the efficiency of P-to-P is that you don't need as
3 many people working in the industry.

4 And you said your -- where 90 percent of your
5 investments fail; again, that's a problem with the model
6 I think we can think we can improve on that, and we can get

1 it is to be back in Washington, D.C. My wife is a visual
2 artist, and we're in high cotton when we're up here.
3 This is -- we spent yesterday going through the new
4 American Indian Museum, and if you haven't been to that,
5 you need to put it on your list.

6 I'm representing the National Songwriters
7 Association. This is my fifth trip to D.C. for the
8 purpose of fighting for our rights. And it's been quite
9 an education.

10 Before we get into that, though, I should tell
11 you that our motto in Nashville for the Songwriter's
12 Association is "It All Begins With A Song." So I'll
13 start with this song, and you can -- we are the only
14 organization or profession that I know of, or one of the
15 few, that is so big-hearted that we have training
16 sessions in all states. Anybody that wants to start a
17 chapter in your little town can do it, and we will help
18 train you to replace us.

19 So I mean, I don't know how smart that is, but
20 we are -- we are pretty unique. I also should tell you
21 that there used to be an organization similar to that in
22 Los Angeles, but I don't think they could get together.

23 So I'm going to give you a little songwriting
24 lesson. And has anybody ever tried to write their own
25 song? All right. Content providers, there are content

1 creators and owners. It's really pretty easy. You
2 should try it. It's really easy to write a bad song.

3 (Laughter.)

4 MR. NEWTON: And this one may fall into that
5 category, but this song was inspired from my first trip
6 up. I asked somebody on the way up on the plane, I said,
7 well, what does the Constitution say in that gave us this
8 copyright? And one of our writers just happened to have
9 the pocket Constitution in his pocket, and he showed me.

10 And it's right there on the same page where the
11 government is able to have an army, to build roads, to
12 have post offices. And just in a few short words, they
13 mention this thing about copyright, and I tried to
14 memorize it. It's not easy when you're -- it's not easy
15 to do. But I found that songs are much easier to
16 remember than just speeches.

17 So I wrote this little song. It's called -- it
18 has two titles. One is called Article I, Section A.

19 (Laughter.)

20 MR. NEWTON: But it also could be called
21 Promote To Progress.

22 (Plays guitar and sings.)

23 (Applause.)

24 MR. NEWTON: Wow, thank you. You know, I
25 really -- I haven't even recorded that one yet. I never

1 thought about it, although I played it in front of a
2 bunch of lawyers down in Nashville. They were there to
3 learn about the music industry, and they liked it, too.
4 They had a Power Point demonstration up where it showed
5 the -- that was there to kind of teach some of the
6 lawyers who were not in the music business about it.

7 And they had this illustration up there where
8 it says, the RS and the publisher, and the record
9 company, and the managers, and on, and on. Just a whole
10 network of people who derived their benefits and their
11 income from our industry.

12 And of course, the artist had a star around it,
13 but somewhere down there was songwriter, in small print.
14 They changed it when I brought that up. They made it
15 biggest of all, and really -- and really, that's the way
16 it should be.

17 But the experience of songwriting from that
18 point of view, Nashville is a mecca for songwriters.
19 It's not just country music. We have artists from all
20 genres there, and we have brought them together because
21 of our love for our craft and art. And it's quite a
22 community.

23 And I'm here because we want to be in the room
24 on every issue that comes up before the government. We
25 were not here in 1909 when they wrote the first copyright

1 law. We were not in the room. What happened? The
2 original draft of that copyright law had nothing for the
3 songwriter. But some staff person asked about it, and
4 they said, well, okay, we'll give them a penny.

5 So that in 1909, we started out with a penny.
6 Now, here it is -- who knows what the compulsory license
7 and dollar amounts are, who knows how much that
8 compulsory license is right now for a songwriter?

9 Eight-and-a-half cents. Did anybody -- was
10 everybody aware of that? Because when we started
11 educating the Congressmen and the Senators -- and, by the
12 way, we come up once a year, we bring about 30 of us --
13 and since we started doing this about four years ago, we

1 collaborations. So if I'm a co-writer and I have a
2 publisher, then that only leaves me with a quarter, 25
3 percent of that. That's two cents.

4 So if I'm on a big hit album that sells a
5 million records, do the math. You know what that comes
6 out to? \$20,000. Those cuts are really hard to come by.

7 What that comes down to, if I'm signed to a
8 publisher, on an advance, if I'm lucky, and with \$20,000
9 I could sign you a room full of songwriters by the end of
10 next week. I can promise you that, \$20,000 a year.

11 My first deal was for \$75 a week, and I was
12 really happy to have it. But that \$20,000 that goes to
13 pay back their advance, and if you do that very long, you
14 get into the red ink, you won't have a deal anymore.

15 And I can tell you, in our community there are
16 some of the greatest songwriters who have written songs
17 you have -- that you fell in love to, or that you've
18 partied by, or that you may have played at your funeral
19 or the funeral of one of your loved ones; these songs,
20 some of these writers, are struggling. They may have
21 made a lot of money, but it's that income stream can go
22 up and down.

23 To illustrate that, one of the metaphors I use
24 is that it's kind of like being a family farmer without
25 any subsidies. And if you're with a publisher, really

1 what that makes you is a sharecropper.

2 I want to mention real -- I want to plug

1 now. I want to cut out as many people on that chart as I
2 can.

3 (Laughter.)

4 MR. NEWTON: Because that two cents has just
5 not been getting it. So I can happily say that if we can
6 -- when we learn how to protect our rights, and I know
7 the technology allows all this to happen can also monitor
8 these songs without invading anybody's privacy. The
9 songs that are played on the radio are monitored by a
10 company has a digital finger print of our music, and
11 every time one of them gets played, it's like a little
12 odometer that goes over and a few cents go into our
13 pocket from that.

14 So I'm all excited about that technology and
15 using it to help the creativity, but I want to point one
16 other thing. Because this gets down to if we're talking
17 about surveys and what effect it's having.

18 One of our real powerful tools on our last
19 trip, we brought a little poster. And there were all
20 little postage stamp pictures of real estate on Music Row
21 that is for sale. It's unbelievable. Music Row is
22 pretty concentrated in about 10 blocks near Nashville,
23 and it is unbelievable what is happening.

24 It is all about the perceived notion of what's
25 going to happen in the business, and people putting their

1 money behind it.

2 And so that is one very strong effect. And we
3 don't call it file-sharing down there, we call it file
4 stealing, because that's what is if it's not paid for.

5 So thank you very much, and I'm glad to be
6 here.

7 (Applause.)

8 MR. HADEISHI: Thank you, Mr. Newton. We trust
9 you'll send us a wave file, and give us the rights to
10 distribute this on our web page.

11 Michael has the unfortunate position of
12 following that. Michael is the co-founder and policy
13 director of the Future of Music Coalition.

14 MR. BRACY: Yes, I kind of have the Triple
15 Crown today because I'm the last speaker in a two-day
16 forum. I don't have a song, and I don't even have a
17 slide show, but I've got a heck of a statement.

18 So we're just going to rip through this, and
19 we'll be out of here. So I appreciate you all making
20 time.

21 My name is Michael Bracy. I'm a founder, and I
22 am the policy director, of the Future of Music Coalition.
23 The Future of Music Coalition is a non-profit that
24 identifies, examines, interprets, and translates the
25 challenging issues that are at the intersection of music,

1 law, and technology, and policy.

2 Today, we're going to do two things in my
3 remarks. We're going to try to take the discussion we've
4 had for two days about peer-to-peer and put it into a
5 broader context about what's happening with the
6 technology, and what's happening with the music
7 community.

8 And I'm also going to talk a little bit about a
9 study that we worked on with the Pugh Internet and
10 American Life Project. I encourage you all to go to
11 FutureMusic.org to learn more about the work we're doing,
12 but also to read the complete Pugh Study. There's a lot
13 of interesting information in that.

14 The music community is in the midst of a
15 necessary and a welcome transition to new digital
16 business models. Now, historically, the musicians have
17 aligned with major labels for three core reasons; for
18 access to resources like budgets, staff, money, core
19 support, access to distribution, to retail, to promotion,
20 to basic infrastructure, and access to radio, TV, you
21 know, basic promotional opportunities.

22 And for many this has been a good model. It's
23 worked. But for many others, it hasn't been particularly
24 good. And there have been a lot of challenges in this
25 model, including concerns about contracts, accounting,

1 business strategies, priorities, and FMC is one of many,
2 many organizations that have been working in the
3 Coalition to try to look at these issues and try to
4 address them.

5 Now, two very significant developments have
6 really forever altered the music landscape, and this
7 really happened in the late '90s; market consolidation
8 and digital music.

9 Again, we have spoken a lot, and partners in
10 the music community have spoken a lot about our concerns
11 about the impact of concentrated control on the radio,
12 among the major labels about what has happened retail,
13 what's happening in the concert industry, and so I'm not
14 going to talk about that today.

15 But this -- you know, we need to understand
16 this is taking place in a broader discussion about
17 consolidation. I think particularly with radio and
18 concert venues.

19 Now, at the same time that the music landscape
20 was seeing this consolidation, there has been a
21 remarkable technological innovation as we're shaping the
22 way the music is recorded and manufactured, promoted, and
23 distributed.

24 Digital studios and software dramatically have
25 reduced production costs. The Internet vastly increased

1 promotional and sales opportunities. The marketplace for
2 independent music exploded, and new labels proliferated
3 the service community.

4 Now, a lot of this music was not intended to,
5 or simply didn't make sense for the kind of mass
6 audiences that really was of most interest to the major
7 labels and to radio. But there was a market for this
8 music. A big market for this music. And so alternate
9 and Internet based economies began to take shape.

10 Now, as these models took flight, some
11 companies and labels offered more equitable business
12 relationships for artists. Some allowed artists to keep
13 their copyright. Some offered creative control. Others
14 provided higher royalty rates.

15 Many musicians have embraced these, these
16 models that allow greater independence, direct contact
17 with fans, more control over their careers; just one
18 example, CD Baby is an on-line retailer, similar to
19 Amazon.com.

20 As of yesterday, nearly 80,000 independent
21 artists were offering their CDs for sale via CD Baby. CD
22 Baby has paid out over \$11 million directly to musicians.

1 musicians the tools to easily and inexpensively connect
2 directly with fans.

3 And so in this context, the results of the Pugh
4 Study that was released on December 5 really should not
5 be viewed as particularly surprising or controversial.
6 The report found that artists have a broad range of
7 opinion when asked their views about digital music
8 technologies. The report indicated that musicians use
9 the Internet to promote and to sell their work -- 87
10 percent of the 27,000 musicians who participated in the
11 survey said they promote, advertise or display their
12 music on-line. Eighty-three percent provide free samples
13 or previews of their music on the Internet; 69 percent of
14 the respondent say they sell their music on-line, either
15 on their own web site or via stores like Amazon or CD
16 Baby.

75 Now, musicians are also 4 -E-o9-csds abouh

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1 payment. And then 35 percent of the artists who
2 participated agreed with both statements.

3 Now, when you break it down, by musicians
4 income and time, emerging artists are more likely to
5 agree that file-sharing services are not bad, because
6 they allow them to promote and distribute their works.

7 On the other hand, artists who make the
8 majority of their income from being a musician or
9 songwriter, were more likely to agree that file-sharing
10 services are bad. Thirty-five percent opposed to 23
11 percent.

12 So given these various factors, an emerging
13 broadband marketplace, extensive consumer demand for
14 digital distribution models, and an explosion of the
15 amount of music release, the fundamental opportunity and
16 challenges to facilitate the development of a legitimate
17 digital music marketplace. And this marketplace is
18 emerging.

19 As Sound Scan reported the first four months of
20 2004, consumers purchased 35.3 million music downloads,
21 and it's projected at least a hundred million will be
22 sold in 2004. That's only about 1 percent of the
23 recorded music market by the way.

24 So the question is, how do we manage this
25 transition to a legitimate digital marketplace in a way

1 that benefits musicians and music fans.

2 Now, from our stand point there has been
3 significant progress. In '95, Congress passed the
4 Digital Performance Right and Sound Recordings Act, which
5 granted performance rights for digital transmission of
6 sound recordings, and led to the creation of
7 SoundExchange.

8 SoundExchange has emerged as a respected,
9 functioning collection and distribution agency that
10 serves as a compliment to ASCAP and BMI. They paid out
11 6.5 million dollars in royalties earlier this year, I
12 believe. And since 2001, they've paid over \$22 million
13 in royalties.

14 Now, we also must recognize music fans'
15 excitement over new technology and models, including new
16 satellite radio, distribution subscription services, like
17 Rhapsody, EMusic and Napster; MusicBlogs, Ezines, the
18 growth of Internet and web casting and digital download
19 stores like iTunes.

20 This trend is a critical precursor. It
21 demonstrates the consumers' willingness to use legitimate
22 digital services. If we build it, they will come.

23 Now, the point is not that this industry is now
24 perfect, or that we even see a solution. Rather we need
25 to acknowledge the digital transition is complicated. It

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1 One, whenever possible, artists must maintain
2 control over copyright and career decisions. Two,
3 artists must be able to compete fairly in the
4 marketplace. They must be able to receive compensation
5 for the work, and have access to consumers. And third,
6 artists must be viewed by the policy making community as
7 valued stake holders in these debates.

8 Now, as I mentioned before, there are many,
9 many organizations with well reasoned, articulate
10 positions on both the macro concerns and on specific
11 micro issues, and I think you've heard from one or two of
12 them over the last two days.

13 And our hope is that policy-makers across the
14 board will grant at least as much weight to the view
15 points of artists, songwriters, and the music community
16 to those of the affected industries.

17 In the summer of 2000, The Future of Music
18 Coalition said that the only antidote to an illegal
19 Napster was a legal Napster. We meant it then, and we
20 mean it today. In a world of breath-taking innovation,
21 the focus cannot be on restricting technology, but
22 rather, on building new consumer business models.

23 We also said that these technology debates are
24 not black and white. They really rest mostly in the
25 gray. The role of the music community is not to pick

1 sides, or even perceive that there are sides to pick.
2 Rather, this is an opportunity for the music community to
3 identify what is right with the historical models and
4 attempt to place it in a digital context, where artists
5 can control their work and receive fair compensation for
6 their efforts, and music fans can have unprecedented
7 access to music at a variety of price points, using a
8 variety of products.

9 According to the Pugh Internet report, there
10 are 32 million Americans who consider themselves artists,
10

1 this panel, the 1:00 deadline is actually firm. I'm
2 going to allow each panelist to briefly, and I'm talking
3 briefly, clear up the record if they have anything to
4 say.

5 Starting from my left, to the right.

6 MR. SHERMAN: Just one thing, to clarify
7 something that Stan Liebowitz said. We don't claim that
8 every download is a lost sale, and I don't think we have
9 ever claimed that any of the copying technologies,
10 because clearly it's not.

11 I guess most of my response would be to what
12 Sam Yagan had to say. You know, he's talking about it's
13 good that they're profit making and that the decision is
14 ultimately the consumer's.

15 Unfortunately, you can make the same argument
16 if you're an old-fashioned pirate and manufacturing
17 counterfeit CDs and selling them on the street. So that
18 argument really doesn't go that far.

19 I think ultimately this is about the artist,
20 the creator having the choice about how they're going to
21 promote their work. That decision shouldn't be made by
22 some third party without their decision. They shouldn't
23 be telling them, we know what's best for you; we're going
24 to promote your work for you whether you want it or not.

25 And if P-to-P really does offer a sense of

1 community, and it may, it really may, then, Sam, and all
2 the other P-to-Ps, you ought to be signing up with
3 Snowcap or World, or one of the other organizations that
4 offer a legitimate mechanism for taking advantage of the
5 community aspect of P-to-P without the infringement.

6 MR. STRUMPF: I just wanted to thank the FTC
7 for putting together this conference. I think it's
8 exactly this kind of dialog based on facts, based on
9 studies, that is necessary to decide where we take P-to-P
10 from here, and I think this was -- I learned a lot.

11 This was a great conference and it's this type
12 of information dissemination that's more important than
13 the hype that we usually get through the media.

14 MR. LIEBOWITZ: And I don't have much to say.
15 On the point Cary just brought up. I wasn't trying to
16 say that it's something that I've heard recently.

17 My memory, which may be wrong on this, was that
18 Alan Greenspan, when he testified about audio taping in
19 the mid '80s, actually said that for each blank video --
20 audio tape represented a lost sale of a --

21 MR. SHERMAN: No, he didn't. He didn't. It
22 was actually based on a survey. There was a percentage
23 of it

24 MR. LIEBOWITZ: Okay. And I take it back.

25 MR. POTTER: I never had Alan Greenspan on my

1 MR. OTTOLENGHI: Okay. Well, I'll hope that
2 you will encourage your members to work with us directly,
3 and, again, Sam, thank you for your work with us.

4 Woodie, if you have a chance, we would like to
5 talk with you and Michael as well.

6 (Laughter.)

7 MR. YAGAN: Thanks, again, to the FTC for
8 hosting this panel. I guess, Mr. Sherman, I was hoping
9 you would comment on my invitation to join me in calling
10 for an impartial analysis of whether this filtering
11 technology actually works by a bunch of impartial
12 scientists, not funded by lobbyists from either side.

13 MR. SHERMAN: You know, maybe it's just that
14 I'm from Washington, but the oldest thing in the book,
15 when you want to delay something, you say "we'll do a
16 study." We have filtering, actually, in the marketplace
17 right now. Why don't you just try one of those? I'm
18 sure that any of those filtering companies would be happy
19 to put the filter into your client, and test it out with
20 you in any way that you want.

21 MR. YAGAN: And you can understand the concern
22 by technology providers who want to know whether this is
23 actually scalable and functional before we put that into
24 our software.

25 MR. SHERMAN: I'm sure we could agree on a way

1 to test it.

2 MR. YAGAN: We should talk about that, then.

1 individual peer-to-peer application, software
2 application, to say, yes, I want to take this risk for
3 the reward.

4 And the question is what is the reward that the
5 market is going to offer for taking that risk?

6 MR. POTTER: For some people, it might be jail.

7 MR. NEWTON: One other quick note, to plug
8 Stephen Foster again.

9 (Laughter.)

10 MR. NEWTON: And I'm serious now, the album --
11 we were all invited to -- I was fortunate to be the
12 producer on one of the songs, the old Way Down Upon the
13 Swanee River song. Old Folks at Home. And David Ball
14 was the singer, and I got to sing background on it.

15 They asked us to be involved with a group of
16 people. We did this all at our own expense. I called up
17 my favorite musicians. They played for free. All the
18 proceeds from this record go to Roots Music in the
19 schools, and what a great way to teach that.

20 But the great news is, it's nominated for album
21 of the year, contemporary folk category for a Grammy. So
22 you might see us on stage. Who knows.

23 And it prompted me to read a book by the guy
24 that wrote the liner notes; Ken Emmerson wrote a book
25 called DooDa, and I'm in the middle of the book, and it's

1 fascinating. I highly recommend it. It talks about the
2 melding of black and white and folk music, and it's
3 really amazing. And again, thanks for inviting me here,
4 and I enjoyed it.

5 MR. BESEN: I'll just say a couple of notes. I
6 mean, first, thank you so much to the FTC for holding
7 this forum, and thanks for inviting us. I want to, you
8 know, basically mention again not only is Wood's
9 association an organization of great resource, but there
10 are many, many others out there, AFM, Recording Artists
11 Coalition, The Recording Academy, just plain folks, you
12 know, half a dozen others, who all are very interested
13 and engaged and have a lot to say on this issue. So I
14 hope that as these conversations continue, that they're
15 brought into the discussion.

16 And I just also want to say I have -- maybe
17 it's the holidays, but I did get the sense that there is
18 progress being made on all these issues over the years,
19 and I think everybody certainly at this table has got a
20 lot to do with it, and I appreciate -- I think we
21 appreciate that there really is a lot of positive
22 progress.

23 So you know, good work, everybody.

24 MR. HADEISHI: Okay. Thank you all, to the
25 panelists. We need to move on to closing remarks. If

1 the panelists could stay seated, this probably would be
2 easiest.

3 I apologize to those of you who had questions.
4 We just, unfortunately, don't have the time for them.
5 What we're going to do now, is move to closing remarks
6 from Susan Creighton, who is the Director of the FTC's
7 Bureau of Competition.

8 For those of you who waited in line, I'm very
9 sorry, because I know you've been standing there a long
10 time. I would encourage you to submit, you know,
11 something in writing to us so that we can consider the
12 thoughts.

13 A PARTICIPANT: It seems rather fruitless to
14 have brought together a panel of this caliber to address
15 the effects on competition, the compensation system, and
16 not to allow a few questions from the audience.

17 MR. HADEISHI: I'm sorry, we simply do not have
18 time, because we have to turn the room over to another
19 group. And so we will move on to final remarks from
20 Director Susan Creighton.

21 MS. CREIGHTON: We've now reached the end of
22 this important, productive, and very timely workshop. I
23 would like to thank all the panelists who volunteered
24 their time and expertise to discuss the varied and
25 complex issues related to P-to-P file-sharing.

1 I would also like to thank those are not
2 panelists, but provided public comments, or posed
3 questions to direct our discussions and build a rich and
4 detailed record.

5 The record will remain open for public comments
6 until January 18, 2005; and so I would encourage all
7 those who didn't have a chance to ask questions or to
8 pose comments here during the course of the hearing to
9 please submit your comments in response to what you have
10 heard the past two days.

1 intellectual property rights.

2 Discussions this morning have helped us better
3 to understand the importance of reaching the proper
4 balance between the legitimate intellectual property
5 interests of creative people, and the interest that
6 others, particularly consumers, have in maximizing the
7 benefits that the tools of expanding technology provide.

8 Among other things, we have learned that
9 business models that worked successfully in the past may
10 have to be changed -- not merely to accommodate P-to-P
11 file-sharing technology, but also to incorporate that
12 technology.

13 The potential benefits and drawbacks of
14 filtering, digital rights management, and collective
15 licensing schemes, among other technological and legal
16 tools, have been fiercely and energetically debated by
17 leading experts here over the last two days.

18 One thing that is already clear, however, as we
19 learned yesterday and today, this technology clearly
20 holds immense promise significantly to increase
21 efficiency and to expand into ever-widening new
22 applications.

23 Therefore, although there are some legislative
24 efforts currently under way to address the issues and
25 concerns created by the emergence and expanding use of

1 P-to-P file-sharing software, it will be very important
2 for policy makers and legislatures to proceed with
3 caution, less we inadvertently put roadblocks in the way
4 of P-to-P's potential.

5 We must take care so as not to attempt to solve
6 the problems of the present by sacrificing potentially
7 dramatic future longer term gains to consumers and our
8 economy.

9 This final note, let me thank you again all for
10 coming to the workshop. For sticking here to the very
11 end. Please keep an eye on our web site for any
12 additional public comments that will be posted, and for
13 information about when the workshop record will be made
14 available to the public.

Thank you all, and have a good afternoon.13excluded.)on.

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CERTIFICATION OF REPORTER

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3 (2) ~~TJ CASE 01312~~ CASE TITLE: PEER-TO-PEER FILE-SHARING TECHNOLOGY