

DEPARTMENT FOR BUSINESS ENTERPRISE & REGULATORY REFORM

CONSULTATION ON LEGISLATIVE OPTIONS TO ADDRESS ILLICIT PEER-TO-PEER (P2P) FILE-SHARING

Submission by Ingenious Media

Introduction and summary

1. Ingenious Media is the UK's leading media investment and advisory company. Founded in 1998, the company now employs over 150 people across five businesses. The company has raised a total of more than £5 billion to invest in film, TV, games, music, live events and other media and entertainment assets. It is the largest independent investor in the UK media market with over 5,000 clients.
2. Our submission is in two parts. The first part offers a commentary on copyright issues generally as they apply to the future prospects of the UK creative economy. It addresses the key features of the consumer, economic and investment context in which peer-to-peer (P2P) file-sharing takes place. It underscores the importance of the wider economic issues raised by the consultation document from the perspective of experienced private investors and advisers to creative businesses. It distinguishes in particular between two different elements of the problem: illicit downloading as a legal and technical enforcement issue; and the commercial challenge to creative content businesses posed by the ideology of "free".
3. We submit that strong creative industries are incompatible with poor defensibility of intangible assets and a weak copyright and enforcement regime. We argue that the government's preferred option as set out in the consultation document is unlikely to be effective. We propose for wider consideration an idea for speeding up the development of these markets by reference to the analogy of the take-up of plastic cards in the 1970s.
4. The second part of the submission provides direct answers to some of the questions raised in the consultation document. We have not attempted to respond to all of the questions posed at the end of the document, many of which are better addressed by other stakeholders, including the trade bodies most directly involved.

Investment in creative content: the wider context

5. The scale of the problem of illicit P2P file-sharing is acknowledged in the consultation document, as are the difficulties presented by the legal context. UK copyright law is no longer “fit for purpose” in the digital age in two quite different senses. First, as Gowers noted in his *Review of Intellectual Property*:

“copyright in the UK presently suffers from a marked lack of public legitimacy. It is perceived to be overly restrictive, with little guilt or sanction associated with infringement.”¹

Secondly, the remedies available to aggrieved parties are either unenforceable or only enforceable with great difficulty and at disproportionate cost.
6. Given the immense complexities of copyright issues, and the international dimension to such problems, it is right that the government should seek, by proposing a range of options, to address the immediate threat to the interests of content-based creative businesses and the artists on whose work these businesses depend. It would be better to find effective but incomplete solutions, even provisional or time-limited ones, than to defer consideration of what are genuinely complex matters until a more comprehensive rewriting of copyright can be enacted. We note that almost two years has passed since Gowers reported and that progress in implementing his recommendations is painfully slow. We are particularly concerned that Gowers’ recommendation (number 36 in his report) on the need to equalise penalties for copyright infringement in physical and online environments has still not been implemented.²
7. From an investor perspective it is necessary to grasp what is at stake as regards the “old media” world of declining advertising revenues and disintegrating business models, and the “new media” world of minimal revenues and largely untested analytics, to understand the wider cultural and economic context to which the P2P debate relates. In particular it is essential to understand the profound changes in consumer attitudes and behaviour that have been driven by the impact of digital technologies. These changes are well documented. Expressed as consumer “demands”, as they frequently are, they may be summarized as “*what I want*”; “*when I want it*”; “*how I want it*”; and “*paid for in the way I want*”, (or, one might add, “*not paid for, if I so prefer*”). The impact of these profound attitudinal shifts on artists, other creators, creative businesses and investors is less well documented or understood.
8. In considering the complex financial relationships between artists, investors, producers, distributors and consumers, and the critical importance of copyright in the creative value chain, the key issues are, firstly, **fair payment for the consumption of creative outputs**; and, secondly, **the legitimate prerogatives of rights-holders** (to licence or withhold distribution of content, and to enforce or forego payment for the consumption of content). The consultation document notes in its analysis of the legal position that existing copyright law seeks to strike:

¹ *The Gowers Review of Intellectual Property*, HM Treasury, 2006, p.39.

² *Ibid.*, p.98

“an appropriate balance between the interests of the creators of protected works and consumers – ensuring that creators are suitably rewarded to encourage them to create while also allowing for legitimate use by users – through exceptions and by providing that after an appropriate period works fall into the public domain and may be used freely.”

In practice, this “appropriate balance” is being progressively undermined – partly as a consequence of the technology-enabled and consumer-driven changes in public attitudes already referred to; partly because some of the key principles of intellectual property are under sustained attack from a variety of vested interests – both commercial and non-commercial; and partly because the issues raised have not yet been debated with sufficient rigour in the court of public opinion.

9. Some cultural critics have suggested, in effect, that the precepts of copyright are inappropriate to the digital age – that all content should be regarded as falling within the “creative commons” by virtue of its being universally accessible on the internet. Such views do not provide an acceptable basis for advancing general propositions about copyright in a digital environment – an environment in which the marginal cost of distributing a song (or movie or game) is close to zero, if not actually zero, but the sunk costs of production can still be huge. They are singularly inappropriate to serious analysis of the economics of creative content businesses, a sector in which, typically, the experience of producing “hits” is greatly outweighed by the experience of producing “misses” and in which, consequently, the “misses” have to be paid for by “the hits”. This *commercial* dimension to the issues is not sufficiently acknowledged in the consultation document.
10. As the document notes, P2P technology is characterised by “network externalities” that increase exponentially – potentially ever larger numbers of people paying nothing for perfect, copyright infringing, digital copies of films, sound recordings, TV programmes and books. This modal shift, which because of the network externalities property should clearly be distinguished from earlier forms of private copying (one-to-one sharing amongst friends and family), for example through the use of blank audio tapes, is regarded as unstoppable and even desirable by some apologists for the “*it’s free on the internet, so fill your boots*” approach to copyright issues³. This mindset, one that implicitly indulges the proposition that “illegal” down-loaders should contribute nothing to the process of creating, or recovering the costs of creating content, should be challenged more rigorously and vigorously in official commentary.
11. The freeloading “fill your boots” stance is neither justified nor, in our view, economically sustainable – certainly as regards high value creative content. In the case of the music industry it is sometimes argued that the record companies were the authors of their own misfortunes because they were too slow to offer legal digital downloads, and/or that their digital downloads are too

³ See for example the proposed “new system” for the music industry known as System-V, “Future of the Recorded Music Industry (Part 3): Out of the darkness, into the Light”, marketed by a company called Generator. All music would apparently be “free” under this system. Advertising-funded models would take over the world.

expensive. The second argument is ethically curious, given that consumers in the pre-digital age were not indulged if, finding CDs too expensive, they simply took them from record stores without paying for them. The first argument has some merit, but is no longer applicable or relevant. Legal downloads of vast amounts of music are increasingly available throughout much of the world at a range of price points. Where this is not the case, and there are still unmet *wants*, the market may confidently be expected to fill the gaps. There is plentiful evidence that it is doing so with new business models, mostly embryonic and frequently untested, appearing regularly. The *Financial Times* and the trade press report such commercial initiatives almost every week.

12. Politicians and others who blithely call for “more new business models” are perhaps missing the point. The consumer research quoted in the consultation document (at paragraph 3.14) gives the lie to much of the market-failure rationalisation used to justify illicit downloading:

“The attraction for music file-sharing appears straightforward. 18% of respondents to the EMR survey indicated they thought themselves more likely to download in 2008. Of these, 91% said this was *because ‘it was free’.....*” (emphasis added)

This finding, if accurate, is a revealing measure both of the truth of Gowers’ observation about the lack of public legitimacy enjoyed by copyright rules, and equally of the extent of public ignorance of the real cost of producing recorded music (and by extension, creative content generally). It should also ring alarm bells with everyone involved in thinking about the future of the intangibles-based “knowledge economy”, and especially “the creative industries”. Content-based creative businesses are unlikely to grow, and the wider creative economy is unlikely to prosper, unless this ignorance is forcefully addressed on several levels. This is now beginning to be done in schools by the music industry, but such initiatives are unlikely to bear fruit on their own.

13. Perhaps this view is too gloomy given the findings of other researchers commissioned by the music industry⁴ to the effect that some consumers are prepared to pay for “added value” content in the form of additional tracks, background notes, better packaging and so on. In the classical music field such business models have worked for some time. In the audiovisual sector, where consumers are generally only interested in seeing a film once, quite different from patterns of music consumption where repeat listening is the norm, some market research suggests that low-priced VOD services will gain commercial traction.
14. However the 91% finding (“because it’s free”) reported by the EMR survey is hard to disregard. Of course, some content creators and rights-holders will always be happy to give their work away for free – either because this is a calculated part of their marketing strategies, or because they wish to endorse the norms of cyberculture. This is easy to justify if you already have a dominant position in the market (the Radiohead phenomenon). It is likely to be commercially disastrous for new acts just setting out and having no brand recognition. Established acts are entitled to give away as much of their own work as they

⁴ For example in the research commissioned by British Music Rights from the University of Hertfordshire in Spring 2008.

choose for any reason at all. No-one, however, is entitled either to give away work created by others, or, we submit, to frame a general argument for “free” on the basis of their own ideological preferences or economic ignorance.

15. In the unregulated and competitive private sector creative economy there is no equivalent pricing model to the kind found in regulated energy markets in which long-run marginal cost pricing methodologies are deployed to ensure that today’s consumers are not cross-subsidised by tomorrow’s consumers. The only model that exists that is theoretically capable of mitigating this “inter-generational” impoverishment effect is the universal levy model deployed in France and elsewhere. It is apparently unpopular with most stakeholders in the UK, and requires hard choices to be made in respect of the distribution of monies raised. It is not examined in the consultation document, no doubt because it lies strictly outside the document’s scope, but is an indispensable point of reference for anyone interested in the economics of the creative content sector.
16. One conclusion seems clear to us. If large numbers of consumers of content continue not to pay *anything* for what they consume, and no compensatory measures are put in place, then those who follow will find themselves short of choice at the quality end of the market (not of course at the “cheap” end where the supply will be almost infinitesimally large), because - in enough cases to make a difference - creators will not be incentivised to create and investors will not be incentivised to invest.
17. On the basis of our experience as investors we assert both parts of this proposition forcefully. Whilst song-writers will always write songs, dramatists write plays and artists paint, the wider creative community of producers, directors, designers, illustrators, technicians, photographers, publicists, gallery-owners, agents and so on does not generally work on the “art for art’s sake” principle. Nor do rights-holders. Building creative business capacity depends on incentivising a wide range of people no less than in other business sectors. This is hard to do if value is being appropriated. Similarly, it is always easy for an investor to find a less risky home for her money than an IP-based creative business.
18. The government is therefore correct to note in its “strategy document” for the creative industries, *Creative Britain*, that

“since most of the value of the creative sector derives from intangible assets, creative businesses must be able to value them accurately and have confidence that they will be vigorously defended under the law.”⁵

We endorse this statement; defensibility and enforcement are vital to investors. However as is often observed, the other side of the illicit P2P “coin” is the need to develop legal download markets as quickly as possible thereby enabling the fair payment principle. It is therefore appropriate to ask whether any form of market-enhancing public intervention could be devised which would have the effect of radically transforming these markets in a positive direction.

⁵ Department for Culture, Media and Sport, *Creative Britain: New Talents for the New Economy*, London, 2008, p. 50.

An alternative proposal for consideration

19. Perhaps we can learn something from the early days of the market for plastic cards. In the first half of the 1970s one policy objective of the then Conservative government was to encourage the use of credit cards (like Access and Barclaycard) in the face of widespread concern amongst shoppers about the consequences of using plastic, especially in relation to the impact on consumer rights. A new doctrine of *connected lender liability* provided that credit card issuers would be equally liable, with retailers, where a card had been used to purchase goods which turned out to be “not fit for purpose or of merchantable quality”, or services which were inadequately delivered⁶. It was a stratagem to reassure consumers and thereby speed up the development of the new market. The credit card companies initially objected, but the stratagem worked and the card companies were major beneficiaries of the credit card boom. Indeed proposals to repeal S.75 of the Consumer Credit Act have been repeatedly dropped because it remains central to maintaining consumer confidence in the use of plastic cards.
20. This regulatory intervention had the effect both of protecting consumers and of benefiting new service providers: it was a good example of the proposition that the self-interest of all parties can be enhanced by imaginative and bold policy-making. The interesting point is that in this case the service providers (essentially the banks) did not initially recognise their own self-interest.
21. By an approximate analogy for the digital age, we propose that the notion of what might be called *connected provider liability* for ISPs be explored using similar logic. The policy objective would be to speed up the development of “legitimate” download markets in the face of (a) consumer resistance/scepticism/freeloading practices and (b) the teething troubles of the new business models available to facilitate this activity.
22. We recognize that the role of ISPs is pivotal to the development of legal download markets, and that the current situation brings them much opprobrium and little commercial benefit. Our analysis is that the *status quo* no longer serves any interest satisfactorily. Better therefore to turn the *status quo* upside down by providing ISPs with the prospect of developing revenue generating opportunities in return for the assumption of certain critical liabilities.
23. This proposal would therefore require ISPs to accept new legal responsibilities in the interests of developing digital content markets – markets in which they *could* be major beneficiaries themselves where they seek to be providers or aggregators of content. In other words, there should be a contrived convergence of public and private interest delivered through re-regulation. In the absence of voluntary agreement (and recent history suggests they probably won’t agree in sufficient numbers unless required to do so by regulation) the ISPs would be obliged under our proposal to act in their own longer-term best interests by assuming shared liability for illicit P2P activity in law.

⁶ Consumer Credit Act 1974, section 75.

24. To go down this road would clearly not be consistent with a broadly self-regulatory approach to the problem. It would also pose policy challenges in respect of the provisions of the E Commerce Directive and, possibly, data protection law. It would pose a fundamental challenge to the “mere conduit” defence currently used by ISPs.
25. We have not attempted to define what precise liabilities would be imposed on ISPs, an issue which would require extensive discussion, not least with the relevant authorities in Brussels. At this stage the important thing is to establish the principle as the basis for adopting a more muscular approach to policy-making. In our view the circumstances demand that a more imaginative and radical approach to the challenge of developing new legal download markets be fully investigated along the lines proposed above, in tandem with other measures, including those outlined as options A3 and A4 of the consultative document.

Answers to selected questions

1. Do you agree that a voluntary solution based on the principles set out in the draft MOU at Annex D, if effective and fair to consumers, would be the best approach to this problem but is unlikely to be achieved?

No. There is no reason to suppose that all ISPs would sign up to or enforce the provisions of a voluntary set of arrangements. The temptation for irresponsible providers to “free ride” on the work and resource commitment of responsible providers in an industry where entry costs are relatively low, is always likely to be too great to resist. Self-regulation will not work.

2 Do you consider this list (of issues) is complete? Are there any other important factors that should be added?

The practical difficulties raised in section seven of the document – as regards issues of data protection, filtering, infringer identification and consumer protection amongst others – all raise legitimate concerns about the shape, scope and detailed provisions of any proposed regulatory structure. We would make two observations. First, it is apparent that technology has provided consumers with the tools to over-ride the interests of all other stakeholders in the processes of creative production and distribution unless checked by technological and/or regulatory means. Secondly, some of the most serious problems raised here – the duties of ISPs under data protection legislation is an example – are rooted in the provisions of statute law. We conclude from the analysis set out in the consultation document, and from our own observations, that a “light touch” approach to regulation in this area is therefore unlikely to be effective.

3 Are any of these criteria (or any omitted criteria) more important (or less important) than the others and therefore should attract a weighting?

The most important criteria are clarity, consent (of rights-holders), enforceability and effectiveness. The status of different categories of content should be clearly distinguishable in the minds of consumers. Some content is in the public domain; other content is not. Whilst these matters can and are being addressed in media literacy campaigns, education and exhortation are not enough. Serial infringers should be penalized.

4 Do you agree that the preferred approach set out in section 8 is capable of dealing effectively with all of these constraints? If not, which are problematic and how?

Please give reasons.

No. This approach is theoretically elegant but commercially naïve. We are sceptical about the likely effectiveness of codes of practice in these markets, unless they are invested with statutory force.

See our outline alternative proposal in paragraphs 19-25 above.

5. Do you agree that a self-regulatory only approach may not be sufficient to resolve this problem? Please give reasons.

Yes. Please see text above.

6. Do you support the described co-regulatory approach? Please set out clearly what aspects of this approach you support and which you do not support. Please provide reasons and, where appropriate, evidence.

“Co-regulation” is easy to support in principle. In the broadest terms it is likely to be the best way forward, but only if there is some form of appropriate statutory underpinning, credible sanctions and high-profile enforcement.

The discussion of “commercial models” on page 30 of the document is naïve in the context of an analysis which shows a clear preference for a “light touch” approach to regulation. Rights-holders are at great risk in online environments even where their content is protected by encryption.

This is a chicken and egg problem however: it seems unlikely to us that some rights-holders will have the confidence to bring more of their higher value content online until there is evidence that any new regime is working effectively to protect their interests. However it is dangerous to generalize: audiovisual and music markets are quite different.

7. Do you agree that Ofcom is the right regulator to oversee the self-regulatory body?

No, not necessarily. Ofcom is the obvious choice given the existing regulatory landscape, but it is already widely stretched. There is a case for considering the creation of a dedicated Office of Content Rights Management, with its own leadership, repositories of expertise and public profile.

8. Do you agree that the regulatory oversight should include approval of Codes of Practice?

See answer to question 4 above.

9. What do you think the coverage of the self-regulatory approach should be? The proposal above suggests rights holders and ISPs. Is this right? Should any other stakeholders such as consumer organisations have a place in the self-regulatory approach? If so, which?

We would be sceptical about the effectiveness of any regulatory solution based on a “representative” approach to governance. The stakeholder approach to consultation is clearly right, but given the diversity of views and interests within the content industries it would be folly to attempt to replicate it in constituting any new regulatory arrangements – whether “self-regulatory” or not. Such arrangements should be seen to transcend sectional interest.

10. What do you think the scope of the legal obligation should be? Do you agree that as described its effect would be limited to P2P networks? If not, how could such a limitation be achieved?

See paragraphs 19-25 above on legal obligations. We have no view on the other parts of this question.

11. The costs of the self-regulatory approach would have to be met by industry. How do you think this should be split between the stakeholders, including between the different content industries?

These questions are more appropriately answered by the trade bodies.

12. The costs of the activities envisaged under the codes of practice could be met either by those responsible for carrying them out, or by some form of cost sharing between parties. It is envisaged that this should be agreed by industry as a part of relevant codes of practice. Do you agree with this process?

These questions are more appropriately answered by the trade bodies.

13. The [draft] MOU at Annex D provides the principles within which the self-regulatory approach could work. Do you think these are the right principles?

This question is more appropriately answered by the trade bodies.

Questions on Alternative Options

14. Do any of these alternative options seem more likely to achieve the objective of significantly reducing illicit P2P use? If so, which? Please give reasons.

Option A2 comes closest to our view, but options A3 and A4 also have merit. These options should not be regarded as mutually exclusive.

15. In relation to any Alternative Option that you would prefer over the co-regulatory option outlined in section 6 please answer the following questions:

- a) who should take action?
- b) who should decide whether to take action and the nature of the action?
- c) what costs would this Option entail?
- d) who should bear these costs?
- e) what safeguards would this Option require? In particular
 - i) How would the rights of the consumer be protected?
 - ii) Should there be an appeal mechanism? If so, who would handle any appeals?

These questions are more appropriately answered by the trade bodies.

16. If you consider option A3 to be an appropriate model then:–

- a) Is there an existing official body which could take on this role? If not, should such a body be created?
- b) What status should the body have ?
- c) How should the body (or the additional work an existing body would have to take on) be funded?
- d) Who should the body be accountable to?
- e) Who should carry the cost of carrying out action against the alleged file-sharer, given the lack of legal action means there is no prospect of costs being awarded?
- f) Should the body have a legal enforcement role (ie) the power to take legal action:
 - i) to force ISPs to take action?
 - ii) against alleged unlawful file-sharers?

g) What level of cases (ie how many) would such a body need to consider in order to be effective and credible? Could this be automated without an unacceptable loss of control over quality of evidence and proportionality of action?

Please give reasons

These questions are more appropriately answered by the trade bodies.

17. If you consider option A4 to be an appropriate model then:

- a) Do you consider that filters are able to offer a sufficiently high level of reliability in identifying correctly copyright material to justify an obligation to utilise them (or allow their use)?**
- b) Do you consider filters are able to check accurately the status of copyright material and to distinguish between legal and unlawful transactions?**
- c) Who should operate the filters and bear the cost of their installation and operation?**
- d) What redress should consumers have if legitimate material is mistakenly blocked?**
- e) Assuming no technological solution is 100% reliable, there will inevitably be a number of “false positives” generated (ie legal material is wrongly identified and blocked as unlawful). What level of false positives would you deem acceptable, bearing in mind the potential for damage to legitimate business and to the individual?**

Please give reasons.

These questions are more appropriately answered by the trade bodies.

18. Do you agree that a joint rights holder/ISP industry working group to look at filtering options would be a useful initiative? Is there a role for Government in convening and/or facilitating such a group? Should any other stakeholders be involved? Would you be willing to participate in such a working group if it was established?

Please give reasons.

These questions are more appropriately answered by the trade bodies.

19. We are committed to producing an impact assessment in order to quantify as far as possible the implications for business, the consumer and the wider socio-economic environment of any regulatory proposal. This is an integral part of our decision-making process. Can you provide further information to better inform that process?

The first part of this submission stands as our answer to this question!